1912

*March 28.
*May 7.

THE STECHER LITHOGRAPHIC COMPANY (PLAINTIFFS) ..... } APPELLANTS;

AND

THE ONTARIO SEED COMPANY AND ADAM UFFELMANN (DEFENDANTS) ..... } RESPONDENTS.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO.

Assignments and preferences—Chattel mortgage—Hindering and delaying creditors—Assignment of book debts—Surety.

The Ontario Seed Co. owed a bank some $8,000 for which J. was surety by bond and indorsement of notes for all but $500. The bank also held as further security an assignment of the company's book debts. The company gave to A., a brother of J., a chattel mortgage of all its personal property and agreed to assign to him the book debts. A. then gave to the company an amount sufficient to pay the bank's claim, J. having supplied him with funds for the purpose, and the company gave its own cheque to the bank with a direction to assign the book debts to A., which was done.

Held, that the evidence justified the finding at the trial that the chattel mortgage was given for the benefit of J., who was aware at the time it was given that the company was insolvent, and that it was void under the provisions of the "Assignments and Preferences Act" and should be set aside.

After the assignment of the book debts to A. the company was allowed to go on collecting them.

Held, that such assignment was valid, but that the assignee could not retain the value of what had been collected out of the proceeds of the property covered by the chattel mortgage.

Judgment of the Court of Appeal (24 Ont. L.R. 503) reversed and that of the Divisional Court (22 Ont. L.R. 577) restored.

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*PRESENT:—Sir Charles Fitzpatrick C.J. and Idington, Duff, Anglin and Brodeur JJ.

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

APPEAL from a decision of the Court of Appeal for Ontario(1), reversing the judgment of a Divisional Court(2) in favour of the plaintiffs.

On 12th August, 1909, the Ontario Seed Company, Limited, a company incorporated under the Ontario "Companies Act," executed a chattel mortgage covering all its goods and chattels in favour of the respondent as security for an advance alleged to have been made by the respondent to the company of the amount of $8,300. This chattel mortgage also assigned to the respondent all the book debts of the Ontario Seed Company, a partnership formerly carried on by Christian H. Kustermann and Otto Herold. All the assets of the Ontario Seed Company were taken over and all its liabilities assumed by the Ontario Seed Company, which was its successor. The Ontario Seed Company, Limited, on 13th August, 1909, was indebted to the Merchants Bank of Canada in the sum of $8,254.52, for which the Merchants Bank held as security a bond for $5,000, executed by one Jacob Uffelman, a brother of the respondent, and an assignment of the book debts of the Ontario Seed Company, the partnership concern. On 13th August, 1909, the respondent issued a cheque in favour of the Ontario Seed Company, Limited, for $8,300, representing the amount of the chattel mortgage. This cheque was deposited in the Merchants Bank of Canada to the credit of the Ontario Seed Company, Limited. The Ontario Seed Company, Limited, on 13th August, 1909, issued a cheque in favour of the Merchants Bank of Canada for $8,254.52, thus paying off all its indebtedness to the bank, relieving Jacob Uffelmann from his

(1) 24 Ont. L.R. 503. (2) 22 Ont. L.R. 577.

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

liability on his bond to the bank and releasing the claim of the bank to the book debts that it also held as security for the indebtedness of the company. On the 12th of August, 1909, the Ontario Seed Company and the Ontario Seed Company, Limited, executed a direction to the Merchants Bank of Canada, requesting the bank to assign the book debts held by it to the respondent. This direction states that the transfer of the book debts is to be made to the respondent, on payment by him to the bank of $8,254.52. The transaction as appears by the documentary evidence, shews that the respondent made no payment to the bank; that the bank was paid by cheque of the company. In pursuance of such direction the bank on the 7th day of September, 1909, executed an assignment of the book debts in favour of the respondent.

The appellant is a creditor of the Ontario Seed Company, Limited, and brought this action on behalf of all creditors of the Ontario Seed Company, Limited, for a declaration that the said chattel mortgage is fraudulent and void as against the creditors of the Ontario Seed Company, Limited.

The trial judge declared the chattel mortgage void to the extent of the difference between the actual value of the book debts of the Ontario Seed Company on the 13th of August, 1909, and the sum of $8,300.

The Divisional Court made an order declaring the chattel mortgage to be void in its entirety. The Court of Appeal for Ontario restored the judgment of the trial judge.

The appellant, who is the plaintiff in the action, now appeals and asks to have the chattel mortgage set aside in its entirety.

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

Secord K.C. for the appellants. The chattel mortgage is clearly void under the Statute of Elizabeth and it cannot be void in part and valid in part. *Commercial Bank* v. *Wilson*(1); *Mader* v. *McKinnon*(2); *Totten* v. *Douglas*(3).

The mortgage was *particeps criminis* in procuring the mortgage and cannot obtain relief in equity. Kerr on Frauds, 4 ed., pp. 365 *et seq.; Cameron* v. *Perrin* (4).

Sir George Gibbons K.C. and *Sims* for the respondents. There was a *bonâ fide* advance by the mortgagee which prevents the mortgage being held void under the "Assignments and Preferences Act." *Mulcahy* v. *Archibald*(5); *Middleton* v. *Pollock*(6).

Even if the advance was made with intent to give a preference it was still *bonâ fide. Ex parte Games* (7).

THE CHIEF JUSTICE (oral).—This appeal should be allowed with costs.

IDINGTON J.—I recognize to the full extent that, as has been so often been said, a preferential assignment is not by reason of its preferential character obnoxious to the Statute of Elizabeth, said to be declaratory of the common law, against schemes for defeating, hindering or delaying creditors. I must also recognize as possible that a scheme may be formed

(1) 3 E. & A. 257.
(2) 21 Can. S.C.R. 645, at p. 652.
(3) 18 Gr. 341, at p. 359.
(4) 14 Ont. App. R. 565.
(5) 28 Can. S.C.R. 523.
(6) 2 Ch. D. 104.
(7) 12 Ch. D. 314.

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

Idington J.

having in it the elements which may render it obnoxious to both that law and the provision of R.S.O. 1897, ch. 147 (now ch. 64, Ont. Stat., 1910), aimed at preferential assignments.

In this case I think the chief purpose of the parties to the chattel mortgage in question was clearly to prefer the claim of the surety and relieve him from the situation in which he had as such become involved. There is evidence, however, of its being only part of a wider scheme which involved at least the hindering and delaying of the creditors.

All the courts below have found the chattel mortgage in question was the result of both designs to defeat, hinder or delay, and to prefer one creditor of an insolvent over another. I cannot say they are wrong in taking that view of the facts. But even if I could and I find that the sole purpose of the parties was the alleged preference and nothing else, how would that help the respondent, Adam Uffelmann?

When the immediate object of an agreement is unlawful the agreement is void. Therefore, the object and, if you will, the sole object of the chattel mortgage having been to withdraw certain assets of the insolvent debtor from the reach of other creditors in order to enable the surety to pay the debt he was surety for, and thus prefer one creditor over others, surely the entire object was unlawful.

Primâ facie the whole is tainted with illegality for such is the presumption the statute has declared and created against such transactions when concluded within sixty days prior to attack thereon.

I am, therefore, with all due respect, unable to understand how the learned trial judge and the Court of Appeal have been able to draw a line where the

parties did not, if we have any regard to their language in expressing in this mortgage their intentions, and thereby sever the legal from the illegal.

I concede it was quite possible to have produced whether lawfully or not such an agreement as the learned trial judge finds the parties had intended relative to their purpose. It was not, however, in the minds of the parties to create a security of which the parts and purpose could be severed in the way the judgment appealed from implies; and without doing violence to the language of the instrument and the manifest purpose of the parties thereto, we cannot find anything therein to justify such a severance or drawing of such a line between the legal and illegal as is attempted below.

Nor do we find anything in the language of section 10 (now section 13) of the statute upon which this action is founded to warrant the giving only such conditional relief as given.

That section, sub-section 1, is as follows:—

13. (1) In the case of a gift, conveyance, assignment or transfer of any property, real or personal, which is invalid against creditors, if the person to whom the gift, conveyance, assignment or transfer was made shall have sold or disposed of, realized or collected the property or any part thereof, the money or other proceeds may be seized or recovered in any action by a person who would be entitled to seize and recover the property if it had remained in the possession or control of the debtor or of the person to whom the gift, conveyance, transfer, delivery or payment was made, and such right to seize and recover shall belong, not only to an assignee for the general benefit of the creditors of the debtor, but where there is no such assignment, to all creditors of the debtor.

I quote this just to point out that it does not countenance any such thing as has been done, and next to shew its limitations in relation to another point I am about to refer to in connection with the book debts.

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

Idington J.

I submit that the language, "assignment or transfer of any property * * * which in law is invalid," lends no countenance to what has been done.

Are there, however, two or more agreements or assignments in this chattel mortgage? I think there are, for we have the assignment of the stock in trade and then a distinctly separate assignment by way of additional security of all book debts, etc., due the old company, and we have also another relative to the unpaid capital. It is conceivable in many ways that an instrument might well contain in this way a series of assignments of which some might be legal and others illegal, but in the language used relative to the stock in trade part of the mortgage, there is no room left for any such severance or suggestion as made, of the good from the bad. To do so on the lines laid down is, I respectfully submit, to construct a theory of what the parties might fairly have so designed as to bring them within one or more of the saving clauses of the statute; and constitute thereby a bargain they never dreamed of.

I incline to think the vicious purpose tainted each of the whole of these assignments in this instrument. But as to the collaterals, held by the bank, and called book debts, I think they were on his payment to the bank the property, or at all events the potential property of Jacob Uffelmann, for whom the respondent was acting and on behalf of whom he was entitled to receive said securities by virtue of his (Jacob's) right as a surety paying off the creditor holding same.

The same day as the mortgage was given, the company gave a direction to the bank to transfer these book debts to respondent Adam Uffelmann, but as he clearly was but the substitute of Jacob, no violence is

done to the actual intention or even the language used in attributing what was done to an assertion of Jacob's rights as the surety who had in fact raised money and in a needlessly roundabout way, paid off the bank.

His right need not be rested upon the clauses in the mortgage and cannot be injured by any clause therein referring to the same subject.

When these securities were transferred thus, they formed an asset distinctly severed from the rest of the estate, and if Jacob took no care to collect them, but let the company do so, he lost his security to that extent and has no one but himself to blame.

Indeed, he may truly blame the illegal purpose of hindering and delaying the creditors for the year that was needed to enable them to pay, as evidently was the intention of those who concocted the circular issued four days later over Jacob's own hand as secretary of the company.

If he permitted the collection and appropriation thereof by the company pursuant to such a scheme, how can any equity rest thereon to make good his consequent loss out of other property to which he was not at all entitled as against the other creditors to resort ? If he permitted it through sheer neglect, how again can he resort for indemnity to a mortgage that the statute presumes, under the circumstances, void ?

Again let us look at the above quoted sub-section of section 10, read it closely and we see that the right of appellant is bounded by and is limited to an account of the proceeds of that which would have been exigible had it "remained in the possession or control of the debtor," etc.

On the one hand the respondent has no right to

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

Idington J.

claim any part of that which he has taken possession of by virtue of an instrument presumed to be illegal and void. And on the other, the appellant has no right to claim an account of those securities which clearly, under the circumstances, never could have become exigible to answer the claims of other creditors.

As to the argument rested on sub-section 5 of section 3, relative

> to the substitution in good faith of one security for another security for the same debt so far as the debtor's estate is not thereby lessened in value to the other creditors

where is the evidence of any such substitution in good faith or bad faith ?

There never existed a foundation on the facts for alleging substitution of one or part of one for another.

The mortgage treated in express words the one as being in addition to the other.

And when we depart from it to the other basis of right to the book debts as security, the two subjects as security are entirely independent of each other, and the book debts free from any such pretension.

No one ever thought of any substitution in regard to either or any part thereof.

And as clearly as can be the debtor's estate has been, by what has taken place relative to book debts, lessened in value, if affect be given the judgment appealed from, to the other creditors.

I repeatedly pressed counsel to see if the proceeds could be traced to anything specific which now formed part of the estate, but was told it could not be done.

Now, as I take this saving clause, if the money had been found invested in some specific thing that has remained to answer for the condition I have quoted relative to lessening of the estate "in value to the

other creditors," principles of equity would require, as well as the statute, relief to be given to that extent.

Or if some privileged claim over the whole estate, the payment of which would enhance the value of the whole estate to the creditors, had been paid off thereby, the same should be done in regard thereto.

As it is, there is nothing either in shape of agreement or actual results to lay a foundation on which to apply such principles.

The appeal should be allowed with costs and the Divisional Court judgment be restored.

DUFF J.—I agree that this appeal should be allowed with costs.

ANGLIN J.—A study of the evidence has satisfied me that it fully supports the findings of the learned trial judge that the impeached chattel mortgage, nominally given to Adam Uffelmann, was in fact the security of Jacob Uffelmann; and that it was given and taken with knowledge of the mortgagors' insolvency and with the intent and purpose that it should serve to "hinder" and "delay," though, perhaps, not to "defeat" or "prejudice," the creditors of the mortgagors, other than the bank and Jacob Uffelmann. Unless, therefore, it comes within some one of the saving exceptions of sub-section 1 and sub-section 5 of section 3, of the R.S.O. 1897, ch. 147, I am convinced that, as against such creditors, it is void under sub-section 1 of section 2 of that statute.

Jacob Uffelmann, as surety to the bank for the mortgagors, was already their creditor for all of the $8,300 which the mortgage purports to secure, except about $500. The evidence makes it reasonably clear

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

Anglin J.

that the real object of the parties was not to secure this $500, but to secure Jacob Uffelmann in respect of his existing liability of upwards of $7,700 as surety, which he was by payment converting into a direct claim against the company. The additional $500 he had to assume in order to clear off the bank's claim and to obtain an assignment of the $6,000 worth of book debts held by it as collateral. The last of the exceptions made by sub-section 1 and the last under sub-section 5 of section 3, therefore, do not apply to the transaction.

The other exceptions under sub-section 1 and the first exception of sub-section 5 clearly have no application.

The bank is not a party to this action. The payment to it is not now in question. The second exception under sub-section 5 does not apply to the case as between the plaintiffs and the chattel mortgagee.

I shall presently give my reasons for thinking that the respondent has not brought himself within the only remaining exception made by sub-section 5, namely,

> the substitution in good faith of one security for another security for the same debt.

I am, therefore, of the opinion that the validity of the impeached instrument is not saved by anything in sub-section 1 or sub-section 5 of section 3.

I agree, however, with Meredith, J.A., that, although

> the plaintiffs are entitled to have the transaction in question set aside * * * it does not follow from that that Jacob Uffelman is also to lose the rights which he had against the company at the time of the carrying into effect of the impeached transaction.

I also agree that the plaintiffs have no right "beyond the removal of the fraudulent security out of

their way." In his factum counsel for the appellants expressly disclaims any intention to attack in this action the assignment by the bank to the defendant Adam Uffelmann of the book debts held by it as collateral. As surety for the debtors, Jacob Uffelmann was entitled on paying the guaranteed debt to be subrogated to the rights of the creditor. I agree with the learned trial judge that

> it was part of the transaction that the bank should transfer to Adam Uffelman the book accounts which they held under assignment from the company and which they subsequently assigned to him.

In taking this assignment, Jacob Uffelmann did nothing fraudulent. He merely exercised a clear equitable right. It is not material to this part of the case that he took it in the name of his brother Adam.

But I am, with respect, unable to concur in the conclusion of the learned trial judge and of the Court of Appeal, as expressed by Meredith, J.A., that, in the result, the defendant Uffelmann is entitled to retain, on account of his claim against the insolvent company, out of the proceeds of the property covered by the chattel mortgage, a sum equal to the value, at the time they were assigned to him, of the book debts formerly held by the bank as collateral. The statute provides that nothing contained in it shall affect

> the substitution in good faith of one security for another security for the same debt so far as the debtor's estate is not thereby lessened in value to the other creditors.

But there is no evidence in the record that a substitution of chattel property for book debts as security was ever agreed upon or intended. Moreover, the finding of intent to hinder and delay creditors in the giving and taking of the chattel mortgage is incompatible with that good faith which would be essential to its

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

Anglin J.

validity had a substitution been contemplated. What the parties had in view was not the substitution of a new security for the same debt; it was rather to obtain security upon the chattel property in addition to the book debts, so that all would be out of the reach of other creditors, and also to secure the whole claim of $8,300 instead of the $6,000 already secured by the book debts. The debtor's estate was lessened in value to the other creditors.

The right of the defendant Uffelmann must, in my opinion, be restricted to such of the book debts transferred to him by the bank as still remain outstanding. His title to these is distinctly severable from the claim which he asserts to the proceeds of the chattel property. It in nowise rests or depends upon the impeached chattel mortgage transaction. But for such of the book debts as he has allowed the debtor to collect, or to discharge by a set-off of contra-accounts, he cannot be allowed to have indemnity out of the proceeds of the chattels, to which his only claim is under an instrument found to be fraudulent. To give him the benefit of security upon this property, without any agreement or understanding that it was to be substituted for the released book debts and notwithstanding the finding of *mala fides,* would be to give efficacy to a transaction which the legislature has declared to be invalid.

I am, for these reasons, of the opinion that this appeal must be allowed and the cross-appeal dismissed, both with costs. The appellant is also entitled to his costs in the Court of Appeal. The judgment of the Divisional Court should be restored.

There may be some hardship in this result. Jacob Uffelmann appears to have been persuaded by Kus-

termann to lend himself to his schemes. He undoubtedly advanced substantial sums of money. He may even have thought that in taking the chattel mortgage in question he was giving the Seed Company a chance to retrieve itself and was thus, while temporarily helping it to stave off its other creditors, taking a step which would ultimately benefit them. He nevertheless contravened the statute when he took as security for his own claim a conveyance of his debtors' property with intent to hinder and delay other creditors; and that he knew he was entering into a transaction of very doubtful legality is manifest from the efforts he made to conceal the fact that the chattel mortgage was really taken for his benefit.

BRODEUR J.—It has been found by the trial judge that the chattel mortgage in question was made with intent to defeat, hinder and delay creditors and that view has been confirmed by the Divisional Court and the Court of Appeal.

It is perhaps unfortunate for Uffelmann that he might lose as a result of this judgment the greater part of the value of the book debts that had been transferred to the bank as a security for the debt for which he was also responsible. But instead of paying purely and simply that debt and becoming thereby possessed of the security he tried through the respondent, his brother, to make a fraudulent transaction and take a chattel mortgage which the company in view of its insolvent situation could not legally grant and have a larger security that would cover the whole indebtedness of the company to him.

I am of opinion that the chattel mortgage to Adam Uffelmann is illegal and should be set aside.

1912

STECHER LITHOGRAPHIC CO. v. ONTARIO SEED CO.

Brodeur J.

As to the book debts I concur in the views expressed by Mr. Justice Idington and Mr. Justice Anglin.

The appeal is allowed and the cross-appeal dismissed.

Appeal allowed with costs.

Solicitor for the appellants: *M. A. Secord.*

Solicitors for the respondents: *Millar & Sims.*