BURNS & LEWIS (ON BEHALF OF THEMSELVES AND ALL OTHER CREDITORS OF ELIZA BARNET CHEYNE (PLAINTIFFS)..... } APPELLANTS ;

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*Oct. 25, 26, 27.

*Dec. 9

AND

JAMES D. WILSON AND THE W. E. SANFORD MANUFACTURING COMPANY, LIMITED, (DEFENDANTS)..... } RESPONDENTS.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Debtor and creditor—Insolvency—Fraudulent preferences—Chattel mortgage — Advances of money — Solicitor's knowledge of circumstances — R. S. O. (1887.) *c.* 124—54 *V. c.* 20 (*Ont.*)—58 *V. c.* 23 (*Ont.*)

In order to give a preference to a particular creditor, a debtor who was in insolvent circumstances, executed a chattel mortgage upon his stock in trade in favour of a money-lender by whom a loan was advanced. The money, which was in the hands of the mortgagee's solicitor, who also acted for the preferred creditor throughout the transaction, was at once paid over to the creditor who, at the same time, delivered to the solicitor, to be held by him as an escrow and dealt with as circumstances might require, a bond indemnifying the mortgagee against any loss under the chattel mortgage. The mortgagee had previously been consulted by the solicitor as to the loan, but was not informed that the transaction was being made in this manner to avoid the appearance of violating the acts respecting assignments and preferences and to bring the case within the ruling in *Gibbons* v. *Wilson* (17 Ont. App. R. 1).

Held, that all the circumstances, necessarily known to his solicitor in the transaction of the business, must be assumed to have been known to the mortgagee and the whole affair considered as one transaction contrived to evade the consequences of illegally preferring a particular creditor over others and that, under the circumstances, the advance made was not a *bonâ fide* payment of money within the meaning of the statutory exceptions.

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APPEAL from the judgment of the Court of Appeal for Ontario, affirming the judgment of the Honourable the Chancellor, by which the plaintiffs' action was dismissed with costs.

A statement of the case appears in the judgment now reported.

Gibbons Q.C. for the appellants. The person who lent the money to the insolvent was acting as an instrument of a particular creditor, the respondent company, which through him obtained an illegal preference over other creditors. He was not a *bonâ fide* lender, and the transaction does not come within *Gibbons* v. *Wilson* (1); he was a trustee for the company to assist in a scheme to cover up the illegal transaction; *Clarkson* v. *McMaster* (2); *Molson's Bank* v. *Halter* (3). It was a transfer to the company, who got the proceeds and should be made to account for them for distribution amongst creditors.

This is a clear case for setting aside, as a preference, the transfer to the Sanford Company of the proceeds of the chattel mortgage. Wilson gave his cheque to the solicitors of the Sanford company, who had taken an order providing for the handing over of the same to the company. No money passed. If, in relation to the transfer of moneys, the solicitor is to be taken as representing The Sanford Company then there was a delivery to them of the cheque of a third party, Wilson, clearly a security transferred within the sixty days and subject to attack. If he is to be taken as representing Wilson, then the cheque given to the Sanford Company was the cheque of a third party and not cash or money and was the proper subject of attack as a pre-

(1) 17 O. R. 290, 17 Ont. App. R. 1.

(2) 25 Can. S. C. R. 96.

(3) 18 Can. S. C. R. 88.

ference. *Davidson* v. *Fraser* (1). Creditors, whose debts were maturing due, had a right to participate in the assets as they were, and the giving of the chattel mortgage would prevent them enforcing any portion of their claims. It was just as much a transaction with intent to defeat, delay and hinder as an absolute disposal of the stock. *Gottwalls* v. *Mulholland* (2); *Merchants Bank* v. *Clarke* (3); *Mulcahy* v. *Archibald* (4).

Ritchie Q.C. for the respondent, Wilson. Wilson had no knowledge that the money was intended for his co-respondents and did not know that they were creditors of the debtor. He did not know what the money was wanted for and had no right to ask. Had he known of the intention to pay a creditor in full, even if such payment would not leave sufficient to pay the other creditors in full, he had still a perfect right to make the advance and take the security, because the statute expressly favours payments in money. He had no knowledge whatever that the money was wanted to pay creditors, that his co-respondents were creditors, or that the debtor was insolvent, and the learned chanceller has found all these facts in his favour. *Gibbons* v. *Wilson* (5). The debtor did not give the security to get under the cover and protection of the mortgage, and the learned chancellor refused to impute to this respondent knowledge of any understanding between his co-respondents and the debtor by which the latter was to get the support and assistance of the company. This respondent had no knowledge until the trial of this action that his co-respondents had executed and delivered in "escrow" a bond or guaranty, and this respondent had no communication of any kind with the person to whom it was

(1) 23 Ont. App. R. 439.
(2) 3 (U. C.,) E. & A. 194.
(3) 18 Gr. 594.
(4) 33 Can. L. J. 545.
(5) 17 Ont. App. R. 1.

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delivered. He actually made a present *bonâ fide* advance of money and is entitled to hold the security he took.

John J. Scott for the respondents, the W. E. Sanford Manufacturing Company. The chancellor's finding upon the facts are favourable to these respondents and against the appellants and should not be disturbed. The security was for a present actual *bonâ fide* advance of money and within the protection of the third section of the "Act respecting Assignments and Preferences by Insolvent Persons." These respondents were not aware of any fraudulent intention, if any such existed, on the part of the mortgagor, to whom the money was actually paid, and the payment cannot be disturbed. The indemnity bond was left with the solicitor and delivered only as "an escrow."

The judgment of the court was delivered by—

SEDGEWICK J.—In the spring of the year 1895 one Eliza Barnet Cheyne commenced the clothing business in Toronto, and by the first of the month of November in that year had become indebted to the W. E. Sanford Company of Hamilton in the sum of about $4,700, and had also become indebted to the firm of Burns & Lewis, of London, and to other merchants in an amount exceeding $3,000. This indebtedness was to a considerable extent overdue at the time that the mortgage, which is now in controversy, was given. About the end of October the Sanford Company, hearing that Miss Cheyne was about to be proceeded against by some of her creditors, sent an agent to her and suggested that she should make an assignment for the general benefit of her creditors, the object being to have the assets divided ratably among the creditors. She refused to execute such an assignment, but it was agreed that her father, who all through appears

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to have been her business manager, and who alone on her side gave evidence in the case, should go to Hamilton for the purpose of entering into some arrangement looking to the liquidation of the Sanford Company indebtedness. He accordingly came to Hamilton and met there the principal officers of the company. These gentlemen retained the services of a firm of solicitors (Scott, Lees & Hobson) in the matter, which firm were, and had been for years previously, the solicitors of Mr. James D. Wilson, a retired merchant and money lender of Hamilton, who had frequently before advanced money to various parties, and upon such securities as were recommended to him by his solicitors. At the meeting between Cheyne and the company it was apparent that Miss Cheyne could not pay her debts as they become due and that it was an absolute necessity, if her business was to continue, that she must get by some means or other a very considerable extension of time. It was present also to the minds of the parties that she could not give an assignment of her property to the Sanford Company by way of security or by way of preference, because that would be in violation of the statute respecting assignments and preferences; but it was known that under a recent decision of the Ontario Court of Appeal in the case of *Gibbons* v. *Wilson* (1) it was held in effect that it was not contrary to law that a debtor in insolvent circumstances might legally give a mortgage upon the security of his property to a third party and with the proceeds pay a single creditor in full to the detriment of his other creditors, and that too, even although the lender of the money were aware of the fact that such was his purpose and object in obtaining the loan when giving the security. It was then also ascertained that Mr. Wilson would

(1) 17 Ont. App. R. 1.

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be willing to advance whatever money the solicitors wanted upon the securities mentioned by them. It was further understood that in the event of Miss Cheyne giving a chattel mortgage to a third party he would advance her money sufficient to pay the Sanford debt. That security would enable her to hold her other creditors at bay so far as her assets exigible in execution were concerned until the moneys due under the security were paid. It was thereupon agreed that Miss Cheyne should give a chattel mortgage to Mr. Wilson upon her stock in trade, he advancing the amount of the Sanford debt, $4,775, and that the mortgage should be payable with interest at eight per cent per annum by weekly instalments of $100 each, the final instalment to be paid on the 11th of November, 1899 It was agreed further that the money received from Wilson should be handed over to the Sanford Company, thereby wiping out their indebtedness; further, that the Sanford Company should execute an instrument of indemnity guaranteeing to Wilson the amouut of his loan, the solicitor to hold this security and to deal with it as the necessities of the case might require. There was in addition some kind of an indefinite understanding that the Sanford Company should continue to supply Miss Cheyne with goods to enable her to carry on her business (this promise on the part of the company forming to a very considerable extent the inducement under the influence of which Miss Cheyne became a party to the transactions), and that she should at once give to the Sanford Company a second chattel mortgage upon her stock, including subsequently acquired property, in consideration of the sum of $916, the amount of the value of the goods which they were then to advance, the money secured under such instrument to be paid forthwith. Previous to this final

arrangement Mr. Scott, the partner of the solicitor, Mr. Lees, had a personal interview with Mr. Wilson and had in effect informed him that he wanted this money upon the security of a chattel mortgage covering the stock and goods owned by one Miss Cheyne in Toronto. Mr. Scott, who was aware of all the circumstances, had not given Mr. Wilson any further information upon the subject than I have stated, Mr. Wilson having the fullest confidence that so far as he was concerned, Mr. Scott's assurance that he would be fully protected was all that was necessary. He had never known or heard of Miss Cheyne before. In fact he did not know whether she was single or married, but as already stated he knew from his experience that he might place the most implicit reliance upon the advice of his solicitor, Mr. Scott. In pursuance then of this arrangement, Miss Cheyne executed the chattel mortgage in favour of Wilson, and Wilson gave the money to the solicitors; the solicitors gave the money to the company, the company gave the bond of indemnity in favour of Wilson to the solicitors, and within a week the Sanford Company sent goods to the extent of $916 to Miss Cheyne, and on the 5th of November she gave the chattel mortgage above referred to, to the company payable forthwith. Two weeks afterwards the Sanford Company, without Wilson's knowledge, took possession of the whole of the property covered by the mortgages, advertised the same for sale, and realized a sum not quite sufficient to pay off the two mortgages, leaving nothing whatever for the appellants, Messrs. Burns & Lewis, nor for any of her other creditors. An action was commenced on the 15th of November, 1895, a fortnight after the date of the mortgage, to set it aside, the defendants being Miss Cheyne, Mr. Wilson and the company. Upon the trial the learned Chancellor for Ontario de-

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cided, although with very great doubt, that the transaction was valid, and his finding was sustained by the Court of Appeal upon the authority of *Gibbons* v. *Wilson* (1), and it is from that judgment that this appeal is taken.

The law upon the subject is contained in the Act Respecting Assignments and Preferences of Insolvent Persons, (Revised Statutes of Ontario, ch, 124) and the Amending Acts, 54 Vict. ch. 20 and 58 Vict. ch. 23. Section 2 of the principal Act (R. S. O. Chap. 124) was repealed by the Act of 1891, a new section of that Act being substituted therefor, and it enacts, among other things:

First—

That every assignment of property made by a person at a time when he is in insolvent circumstances, or is unable to pay his debts in full, or knows that he is on the eve of insolvency, with intent to defeat, hinder, delay, or prejudice his creditors, or any one or more of them, shall as against his creditor or creditors injured, delayed or prejudiced, be utterly void.

Secondly—

That every such transfer to or *for* a creditor with intent to give such creditor an unjust preference over his other creditors or over any one or more of them, shall, as against the creditor or creditors injured, delayed, prejudiced or postponed, be utterly void.

And further that a transaction of that kind shall be presumed to be made with intent and to be an unjust preference if made within sixty days previous to the time when any action is taken to impeach it. These provisions are, however, subject to section 3 of the principal Act, which enacts, among other things, that nothing in the preceding section, to which I have referred, should apply to any *bonâ fide* assignment of property which is made by way of security for any present actual *bonâ fide* advance of money.

(1) 17 Ont. App. R. 1.

The Act of 1895 above referred to only affects this case in so far as it adds to the existing rights of the attacking creditors. In order to arrive at a conclusion as to whether this case comes within the statute the case must be looked at from three points of view, viz.: First, from the view of the debtor; secondly, from the view of the creditor; and thirdly, from the view of the lender. I do not think there can be any question here, but that Miss Cheyne, as a matter of fact, was a person in insolvent circumstances and unable to pay her debts in full at the time she executed the instrument impeached. There is a question, however, as to the intent with which she did it. Did she do it with the intent to delay her creditors, or with the intent to give a preference to the company, or only with the intent of enabling her to carry on her business? While this latter intent no doubt did exist there can be no question but that such intent was to be carried out by so protecting her property that her other creditors could not by any means avail themselves of it for the payment of their claims. In other words, her desire to carry on her business was to be attained by setting her other creditors at defiance through the medium of this chattel mortgage which for four years at least was to remain in existence against them. There was therefore clearly an intent on her part to hinder, delay, and prejudice her creditors.

Now, from the point of view of the company: It was admitted at the argument, and it is unquestionably correct, that they could not have taken this mortgage in their own names. Had they done so it would at once have come within the statute and been void as an unjust preference.

The principal question in controversy is as to Wilson. Was this mortgage, so far as he was concerned, by way of security for a "present actual *bonâ fide* advance of money?"

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Now I admit that an insolvent debtor may sell or mortgage his property for money and then pay that money to one of his creditors, even though in doing so, he should give a preference to that creditor over all of the other creditors, and further that such a transaction cannot be successfully attacked under the statute, even though the lender knows of the debtor's intent to effect such preference, and we have so held in *Campbell* v. *Patterson* (1). The payment of money to a person in exchange for property of that person does not *per se* affect in any way the quantum of his assets available for his creditors generally, and there is no principle of law which compels any man bargaining for or taking security upon goods to make any inquiry either before or afterwards as to what disposition it is intended to make of the money or property transferred. He is none the less debarred from completing the transaction even although aware of its purpose. Is Mr. Wilson in that position here? He endeavours to shield himself by setting up his ignorance. It was at first contended at the argument before us that Mr. Scott was not his solicitor, and even if it were held that he was, the solicitor's knowledge was not his knowledge. The first contention was abandoned, but the other was pressed. So far as this point is concerned we are of opinion that his solicitor's knowledge necessarily acquired in connection with these same transactions was his knowledge, and that he must be held to have known what his solicitor knew. It was in our view the same as if the solicitor had Mr. Wilson's money in his hands for the purpose of investing it in such a way as the solicitor might think expedient, he having a power of attorney to carry on the business in the same way and to the full extent that his principal

(1) 21 Can. S. C. R. 645.; *Sub nomine. Campbell* v. *Roche*, 18 Ont. App. R. 646.

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might have done. Under such circumstances, the defence of ignorance on the part of the principal would be of no avail as against the knowledge of the attorney. Now, in our view all of these transactions must be viewed as one transaction. Each of its constituent facts had relation to every other in connection with it, and all must stand or fall together. The defendant company were rightly desirous of payment or security for their debt. They called in the aid of a solicitor to advise as to how this desire might be accomplished. The solicitor had, in substance, in his possession funds of his principal with full powers of investing them. Both he and the company knew that the debtor could not give a security direct to the company. That would undoubtedly be a violation of the statute, but the solicitor suggests: "In your interest I can get over the statute. I have read *Gibbons* v. *Wilson* (1); I will take my client's money and pay you and get Miss Cheyne to give a chattel mortgage to me, you at the same time giving me a bond of indemnity that I will eventually get back my money." It was a happy suggestion, is immediately adopted, and the transaction was completed upon these lines. I may have drawn too strong inferences from the admitted facts, but it is clear that substantially the transaction was just as I have stated. I do not think that under these circumstances the money, even although it was Wilson's money, was given in good faith to Miss Cheyne. The whole intent and object of the scheme, so far as the company was concerned, and so far as its solicitor (he being Wilson's solicitor as well) was concerned, was to secure the payment in full of the Sanford claim, the necessary consequence of which was, and was known to be, that all the other creditors would be, at all events, hindered and delayed in their remedies, if not, as matters subsequently

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turned out, defeated altogether. The money was not money paid to Miss Cheyne at all. The chattel mortgage was a mere instrument taken by the company to secure the object they had in view. Wilson himself was a like instrument used by them to aid in the same purpose, nothing more than a mere portion of the machine devised by the solicitor to work out his ingenious plan. It was not upon the security of the Toronto goods that the solicitor paid the company, but it was because he knew, whether by verbal promise or by reason of the written indemnity of the company, they would protect him and Wilson from all loss in the matter, and under these circumstances it seems to me an impossible task to show that there was a *bonâ fide* payment of money by Wilson to Miss Cheyne. On the contrary it was a *malâ fide* payment to the company for the purpose of avoiding the statute under the guise of a colourable or fictitious payment to Miss Cheyne.

It is satisfactory to know that all the money due to Wilson has been realized from the sale of the proceeds, the same having been paid over to him since the commencement of this action, by the company.

We are of opinion that this appeal should be allowed. The result will be that the money received by the company from Wilson, instead of being devoted exclusively to the company's benefit, will now be divided *pro ratâ* among themselves and their fellow creditors.

There will be judgment for the appellants, and they will have judgment in the court below as asked in their statement of claim, with costs.

Appeal allowed with costs.

Solicitors for the appellants: *Gibbons, Mulkern & Harper.*

Solicitor for the respondent, Wilson: *T. B. Martin.*

Solicitors for the respondents, The W. E. Sanford Manufacturing Company: *Scott, Lees & Hobson.*