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 *Feb. 16
 June 26

INDUSTRIAL INCOMES LIMITED }
 (Defendant) } APPELLANT;

AND

MARALTA OIL CO. LTD. (Plaintiff) RESPONDENT.

ON APPEAL FROM THE SUPREME COURT OF ALBERTA,
 APPELLATE DIVISION

Trusts and trustees—Agreements to assign debtor's interest in proceeds of oil well production—Proceeds to be held in separate account until drilling account and creditors' claims paid—Assignee entitled to all further amounts as might be received—Whether trust created.

The plaintiff M had a 30 per cent interest in a farm-out agreement acquired from X. A well was completed and production obtained but M was heavily in debt both to the drilling contractor and many other creditors. The drilling contractor filed a mechanics' lien with the result that M's interest in the operation was in danger of forfeiture. To avoid this forfeiture and to protect its assets and creditors M entered into an agreement with X to assign its 30 per cent interest in the net proceeds of production. X then assigned the same 30 per cent to R. M and the creditor drilling company joined in this agreement. The drilling company's account was settled at \$39,596.22, which R agreed to pay.

From the proceeds of production, R was (a) to reimburse itself for the \$39,596.22; (b) after such payment, to distribute the proceeds among the creditors of M up to the sum of \$52,000; and (c) to retain the balance after those two sums had been paid. R agreed to deposit the proceeds in a separate account in a named bank and the same were to be distributed monthly as set out above.

*PRESENT: Judson, Ritchie, Hall, Spence and Pigeon JJ.

These agreements were all executed at the same time and dated May 1, 1953. There was a further assignment of the 30 per cent interest on April 1, 1954, from R to the defendant I. The latter entered into the same agreement that R had made, the only difference being that when I took the assignment, \$12,811.95 had been paid on the drilling account thus leaving unpaid and subject to retainer under (a) above, the sum of \$26,774.27. This sum had been received and retained by the end of February 1956. The drilling account had then been fully satisfied. From February 1956 to September 1962, I received a further \$50,000. It never kept a separate account of the moneys received. It paid some creditors, made compromises with others and left some claims unpaid.

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An action brought by M against I to recover moneys alleged to be held in trust and misappropriated by the defendant was dismissed by the trial judge on the ground that no trust was established. This judgment was reversed by the Appellate Division of the Supreme Court of Alberta. The defendant then appealed to this Court claiming a restoration of the judgment at trial. A cross-appeal relating to the allowance of set-offs by the Court of Appeal and claiming a return of M's interest in the oil well was also made.

Held: The appeal and cross-appeal should be dismissed.

The Court agreed with the Appellate Division that there was a trust for payment and that the matter did not simply rest in contract as found by the trial judge. *Seller v. Industrial Incomes Ltd.* (1963), 44 W.W.R. 485, 41 D.L.R. (2d) 329, referred to.

APPEAL and CROSS-APPEAL from a judgment of the Supreme Court of Alberta, Appellate Division¹, allowing an appeal from a judgment of Milvain J. Appeal and cross-appeal dismissed.

J. C. Major, for the defendant, appellant.

M. Millard, Q.C., for the plaintiff, respondent.

The judgment of the Court was delivered by

JUDSON J.:—This action was brought by Maralta Oil Co. Ltd., against Industrial Incomes Limited to recover certain moneys alleged to be held in trust and misappropriated by the defendant. The learned trial judge dismissed the action on the ground that there was no trust established. This judgment was reversed by the Appellate Division of the Supreme Court of Alberta. The defendant now appeals to this Court claiming a restoration of the judgment at trial.

The facts are set out in detail in the reasons for judgment of the Appellate Division¹. Maralta had a 30 per cent interest in a farm-out agreement acquired from

¹ (1964), 49 W.W.R. 175, 46 D.L.R. (2d) 511.

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Mutual Holdings Limited. A well was completed and production obtained but Maralta was heavily in debt both to the drilling contractor and many other creditors. The drilling contractor filed a mechanics' lien with the result that Maralta's interest in the operation was in danger of forfeiture. To avoid this forfeiture and to protect its assets and creditors Maralta entered into an agreement with Mutual Holdings Limited to assign its 30 per cent interest in the net proceeds of production. Mutual Holdings Limited then assigned the same 30 per cent to Rocky Mountain Supply Company Limited. Maralta and the creditor drilling company joined in this agreement. The drilling company's account was settled at \$39,596.22, which Rocky Mountain agreed to pay.

From the proceeds of production, Rocky Mountain was

- (a) to reimburse itself for this \$39,596.22;
- (b) after such payment, to distribute the proceeds among the creditors of Maralta up to the sum of \$52,000; and
- (c) to retain the balance after those two sums had been paid.

The full terms of the agreement are next set out. Rocky Mountain agreed that:

... it will deposit the share of proceeds of production from the well ... in a separate account in The Royal Bank of Canada, Third Street West Branch, Calgary, Alberta, and will distribute the same on the last business day of each month, commencing with the last business day of May, 1953, as follows:

- (a) To its own account until it has received the sum of Thirty-nine Thousand, Five Hundred and Ninety-six Dollars and Twenty-two Cents (\$39,596.22); then
- (b) rateably among the creditors of Maralta . . . , until such creditors have received an aggregate amount not in excess of Fifty-two Thousand (\$52,000) dollars, or such lesser amount as may be owing to such creditors by Maralta as at the date hereof;

and thereafter the separate account shall be closed and Rocky shall own and be entitled to all further amounts as may be received by it in respect of the said share of proceeds.

These agreements were all executed at the same time and dated May 1, 1953. There was a further assignment of the 30 per cent interest on April 1, 1954, from Rocky Mountain Supply Company Limited to Industrial Incomes Limited, the defendant in this action and the appellant before this Court. Industrial Incomes entered into the

same agreement that Rocky Mountain had made. The only difference is that when Industrial Incomes took the assignment, \$12,811.95 had been paid on the drilling account thus leaving unpaid and subject to retainer under para. (a) of the above agreement, the sum of \$26,774.27. This sum had been received and retained by the end of February 1956. The drilling account had then been fully satisfied. From February 1956 to September 1962 the date when the action was instituted, Industrial Incomes received a further \$50,000. It never kept a separate account of the moneys received. It paid some creditors, made compromises with others but left unpaid creditors' claims which on a reference were ascertained at \$19,781.70, and for that amount judgment was given.

The learned trial judge held that no trust was created by the documents which are outlined above. A unanimous Court in the Appellate Division disagreed with this conclusion. With respect, I agree with the conclusion of the Appellate Division that there was a trust. The Appellate Division emphasized, and rightly so, that these moneys were to be kept in a separate account in a certain bank until the drilling account and the creditors' claims up to \$52,000 had been paid. It was only after this time that the account was to be closed and the assignee entitled to all further amounts that might be received. These assignments did not enable the assignee to refrain from paying certain accounts and retain the money. I agree that there was a trust for payment and that the matter did not simply rest in contract as the learned trial judge found.

One of the difficulties in this case is the judgment of Kirby J. in the Trial Division of the Supreme Court of Alberta given on September 10, 1963. This judgment is *Seller v. Industrial Incomes Limited*². Seller was one of the creditors and he had purchased a number of claims against Maralta and taken assignments of them. In his action he alleged that there was a trust for creditors. The judgment of Kirby J. was that there was no such trust for creditors and he dismissed the action.

He came to this conclusion because there was, in his opinion, no evidence that the creditors had been notified of the transfer or that a trust had been created for particular

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creditors even without communication to or assent by them. This judgment was not appealed. According to ex. 6, which was filed in the present action, there came into existence, at some time, a complete list of some 30 trade creditors with claims totalling \$48,086.64. There were, in addition, on this list, claims of \$3,000 by Maralta's associates in the drilling venture and claims of \$2,000 by two officers of Maralta. There was no proof that this list was a schedule to the documents that are said to have created the trust for creditors but Seller, when he brought his action, was obviously aware of the provision that he thought had been made for creditors. It is difficult for me to understand why this knowledge on the part of creditors, who were not a large body, would not be in existence on May 1, 1953, when the documents were signed.

The present action which is now under appeal was instituted on September 20, 1962. The judgment at trial in this action is dated November 14, 1963, two months after the dismissal of the creditors' action, *Seller v. Industrial Incomes Limited*.

Although the Court of Appeal in the present action said that the question whether these documents constituted a trust for the creditors or whether Maralta itself was the beneficiary of the trust, was not argued before them, nevertheless their judgment must be based on the conclusion that Maralta was the beneficiary of this trust and that it was revocable by Maralta for non-compliance with its terms. Industrial Incomes never made any attempt to keep the moneys received from the production of the well in a separate account as required by the agreement and left unpaid claims amounting to the sum for which judgment was given.

The principle is stated in 38 Hals., 3rd ed., p. 840, in the following terms:

Trusts for creditors. If a debtor conveys property in trust for the benefit of his creditors who are not parties to the conveyance, and to whom the fact of its execution is not communicated, the conveyance merely operates as a power to the trustee to apply the property in satisfying their claims; and inasmuch as the debtor himself is in fact the only cestui que trust, it is revocable by him before the property is so applied, and cannot be enforced by the creditors. A trust in favour of creditors is not, however, revocable if the creditors are parties to or assent to the conveyance or if the fact of its execution is communicated to them.

The order of the Court of Appeal was made in the following terms:

Once the amount owing to creditors as at the 1st day of May, 1953 is ascertained, then from such amount or \$52,000, whichever is the lesser, the respondent may deduct the aggregate of amounts paid by it to the creditors either in payment of such claims or in purchase of such claims. The appellant will be entitled to the balance. Where the respondent has purchased a claim at less than the actual amount owing, it may only claim credit for the amount actually paid and not the original amount owing, for a trustee may not benefit by buying up debts. See Lewin on Trusts, 15th ed., p. 202.

As this is an express trust, The Limitation of Actions Act has no application.

There will be judgment for the appellant for the amount so ascertained with costs

If counsel are unable to agree as to the amount of this judgment, the matter shall be referred to the trial judge.

As a result of this order for reference, certain agreements were made between counsel. The Court of Appeal also advised counsel that it intended to allow set-offs as well as payments made and that its judgment was to be read accordingly.

Only two items came before the trial judge on the reference. The first was the cost of defending the law suit, *Seller v. Industrial Incomes Limited*, above referred to. The second was extra payments for auditors' work. Both these items were allowed by the trial judge and credit was given for them under the judgment as entered. The result was that the Court of Appeal directed the entry of judgment in favour of Maralta for \$19,781.70.

We are now faced in this Court with a cross-appeal. First, it is said that there was error in allowing set-offs other than payments made in cash. I agree with the Court of Appeal on this point.

Second, it is said that if set-offs are allowed, then certain allowances were not made for two deliveries of oil well casings. If Maralta had intended to open up this matter, it should have done so on the reference back to the trial judge, who could have taken evidence and made an adjudication. I am unable on this record at this stage to make any finding on the validity of this claim. I am in the same position with the extra allowance for auditors' claims.

The cross-appeal also claims a return of Maralta's interest in the oil well. This must be dismissed. Maralta

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entered into the agreement to save its interest in the oil well from being lost in mechanics' lien proceedings. To do this it had to agree, first, to the payment of the drilling costs, and then to the release of any surplus after the payment of creditors' claims. The trust is only for the payment of these creditors' claims and it is being enforced.

The appeal and the cross-appeal should be dismissed with costs.

Appeal and cross-appeal dismissed with costs.

Solicitors for the defendant, appellant: Chambers, Saucier, Jones, Peacock, Black, Gain & Stratton, Calgary.

Solicitors for the plaintiff, respondent: Millard, Johnson & Maxwell, Calgary.
