1959

Feb. 24, 25
*Jun. 9

WILLIAM TREMBLAY (*Defendant*) ....APPELLANT;

AND

J. P. VERMETTE (*Plaintiff*) .....RESPONDENT;

AND

THOMAS H. ONSLOW .....MIS-EN-CAUSE;

AND

BEST WOOD MANUFACTURING LIMITED ..... } BANKRUPT.

APPEAL FROM THE COURT OF QUEEN'S BENCH, APPEAL SIDE, PROVINCE OF QUEBEC

Bankruptcy—Company—Liability of former shareholder as contributory—The Bankruptcy Act, R.S.C. 1927, c. 11, s. 70(1), (3).

*PRESENT: Taschereau, Locke, Fauteux, Abbott and Judson JJ.

[1] (1920), 35 C.C.C. 93, 56 D.L.R. 117.
[2] (1920), 33 C.C.C. 70, 52 D.L.R. 342.
[3] (1920), 61 S.C.R. 413, 57 D.L.R. 648.
[4] (1932), 2 W.W.R. 289 at 293.

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By a written contract, the defendant T and his partner O sold to Best Wood Manufacturing Limited all the assets of a woodworking business which they had been operating. Payment was made in the form of fully paid-up shares. The contract was approved by the shareholders but, by inadvertence, was not filed with the provincial Secretary as required by s. 42 of the *Quebec Companies Act*. From time to time thereafter, T assisted the company in its financial difficulties, but resigned as a director in September 1946 and took no part in its affairs from that date. In July 1947, T sold all claims he might have against the company and his shares in it to A. This transfer of the shares was registered in the books of the company on July 21, 1947. The company was declared bankrupt on March 11, 1948. The trustees in bankruptcy applied to the Court to have T and O declared contributories of the company for the full par value of the shares issued to them. The trial judge dismissed the application, but this judgment was reversed by the Court of Appeal. T alone appealed to this Court.

Held: The appeal should be allowed and the application dismissed.

Per Taschereau, Fauteux, Abbott and Judson JJ.: Even if the failure to register the contract with the provincial Secretary rendered T liable as a contributory, he ceased to be so liable by reason of the transfer of his shares long before the bankruptcy. When a shareholder transfers his shares he transfers all his future rights and obligations as a shareholder from that date. The trustees' claim was based on s. 70 of the *Bankruptcy Act*, R.S.C. 1927, c. 11, but cases decided under a similar section in the *Winding-Up Act*, R.S.C. 1886, c. 129, settled that nothing created any liability on the part of a past shareholder where such liability was not provided by the Act under which the company was created or some related Act. In the circumstances of this case, s. 70(3) of the *Bankruptcy Act* had no application.

Per Locke J.: The appellant was entitled to succeed on the ground that he had ceased to be a shareholder several months prior to the bankruptcy and that the evidence did not support a claim on the part of the trustees under s. 70(3) of the *Bankruptcy Act*. Where a shareholder has validly transferred his shares before a call is made by the company, it is a good defence to an action by the company in respect of the call, provided the transfer has been registered in its books. Apart from any liability that might arise by reason of s. 70(3), after the transfer had been recorded the appellant ceased to be liable to be made contributory in a winding-up or bankruptcy. Section 70(3) had no application in the circumstances of this case.

APPEAL from a judgment of the Court of Queen's Bench, Appeal Side, Province of Quebec[1], reversing a judgment of Cousineau J. in a bankruptcy matter. Appeal allowed.

G. Monette, Q.C., and *Miss L. Tremblay*, for the defendant, appellant.

J. Prieur, for the plaintiff, respondent.

[1] [1957] Que. Q.B. 209.

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The judgment of Taschereau, Fauteux, Abbott and Judson JJ. was delivered by

ABBOTT J.:—Respondent, acting in his quality as trustee of Best Wood Manufacturing Limited in bankruptcy, applied to the Superior Court, sitting in bankruptcy, to have the appellant Tremblay and the mis-en-cause Onslow, declared contributories of the said company for the full par value of the shares issued to them. That application was contested and was dismissed by the trial judge. On appeal[1] the judgment was reversed and both the appellant and Onslow held liable as contributories, Tremblay to the extent of $5,400 on the 2,500 shares having a par value of $25,000, originally issued to him. Onslow did not appeal to this Court.

The record is a most unsatisfactory one. The evidence tendered by the respondent trustee to establish the liability of appellant as a contributory consisted principally of the minute book and some, but not all, of the books of account and bank books of the company. The relevant facts, however, would appear to be as follows.

On December 31, 1945, Tremblay and Onslow acquired a woodworking business theretofore carried on at Pont Viau, for a price of $15,000, plus assumption of the outstanding liabilities of the business, which were stated to be between $12,000 and $14,000.

Tremblay and Onslow continued to carry on this business in partnership as from January 1, 1946, under the name of Best Wood Manufacturing Company, and the evidence indicates that between that date and May 31, 1946, additional assets were acquired to the value of some $7,000 or $8,000.

By contract in writing entered into on May 31, 1946, Tremblay and Onslow sold to Best Wood Manufacturing Limited, now in bankruptcy, for a price of $35,000, all the assets of the business in question. These assets are described in detail in a schedule attached to the contract, with

[1] [1957] Que. Q.B. 209.

a value placed on each item, and a total valuation of $35,065.45. Referring to the assets sold and transferred, the contract contains the following condition:

Tel que le tout se trouvait le 15e jour de mars 1946, et dont ledit acquéreur a pris possession et administration exclusive et ininterrompue depuis cette date.

The company purchaser did not assume payment of any of the liabilities of the said business. The vendors agreed to accept payment of the purchase price in the form of 3,500 fully paid up shares of the capital stock of the company purchaser, of a par value of $10 each. This contract was approved at meetings of directors and shareholders of the said company held on May 31, 1946, and of the 3,500 shares, 2,500 were allotted to Onslow and 1,000 to Tremblay. Apparently by inadvertence, the said contract was not filed with the provincial Secretary under s. 42 of the *Quebec Companies Act,* R.S.Q. 1941, c. 276, which reads as follows:

42. Subscriptions for stock must be paid in cash, unless payment therefor in some other manner has been agreed upon by a contract, a copy of which must be fyled with the Provincial Secretary at or before the issue of such shares or within thirty days thereof.

The amount of paid-up capital from year to year, shall be published annually in a report to the shareholders.

At the said meeting of directors held on May 31, 1946, Tremblay applied for and was allotted an additional 1,500 shares at a price of $10 per share. The minutes of the meeting concerning the issue of these shares read as follows:

Il est résolu:

D'ACCEPTER l'application de monsieur William Tremblay Sr, pour l'achat comptant et immédiat de 1500 actions du capital-actions de Best Wood Manufacturing Limited, au prix de $10.00 l'action à savoir pour un montant global de $15,000.

Le secrétaire expose à l'assemblée que le président de la compagnie, Monsieur William Tremblay Sr a déjà avancé une somme de $15,000 laquelle a été déposée à la Banque Provinciale du Canada au compte de la compagnie.

Tremblay's total shareholding was therefore, 2,500 shares of a total par value of $25,000.

The partnership had maintained a bank account with the Banque Provinciale and the debit balance in that account on May 31, 1946, appeared as $16,082.98. On January 22, February 15 and March 29, 1946, respectively,

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Tremblay had advanced $3,000 to the business and these amounts—totalling $9,000—were deposited in the said account with La Banque Provinciale and applied in reduction of the firm's indebtedness to the bank. On July 13, 1946, Tremblay made two further payments aggregating $19,600 which had the effect of completely extinguishing the indebtedness to the bank, leaving a small credit balance of $23.45.

On July 19, 1946, a new account was opened with the same branch of La Banque Provinciale in the name of the company now in bankruptcy. The small credit balance of $23.45 in the old account in the name of the partnership was transferred to the new account.

As I have stated, the agreement of May 31, 1946, stipulated that the assets of the partnership had been transferred as of March 15, 1946, and it seems clear that the old account at La Banque Provinciale was operated for the benefit of the new company as from that date up to July 24, 1946, when it was closed out.

From July to September 1946, the company continued to keep its account with La Banque Provinciale and during that period a fresh debit balance of approximately $12,000 was built up.

The minutes of a meeting of directors held on September 11, 1946, record that at that time the bank was insisting upon payment of the amount due it, and that at the request of the other directors, Tremblay agreed to pay off the bank. The bank's indebtedness was stated to be approximately $12,500 (the bank account on that date indicated a debit balance of $11,889.02) and it was in fact paid off by Tremblay.

In consideration of the moneys so advanced, the company sold and transfererd to Tremblay all the machinery and equipment in its establishment at Pont Viau, and at the same time Tremblay leased the said machinery and equipment back to the company for a rental of $300 per month up to a total of $12,500. Upon receiving payment of the total sum of $12,500 and interest, Tremblay undertook to reconvey the machinery and equipment to the company.

At meetings of directors and shareholders, held on September 11, 1946, these arrangements with Tremblay were approved, appropriate agreements were executed, and Tremblay resigned as a director and officer of the company although retaining the shares which had been issued to him.

At the same meetings, Tremblay was replaced as a director, new officers were elected, and a resolution adopted authorizing the change of the company's bank account from la Banque Provinciale to the Bank of Montreal.

From September 11, 1946, to July 21, 1947, no directors or shareholders meetings appear to have been held, and there is no indication that after September 11, 1946, Tremblay took any part in the affairs of the company although the company's boks, produced by the trustee, indicate that the company continued to carry on business. No bank books were produced by the trustee covering the period between September 30, 1946, and September 8, 1947 (when an account appears to have been opened with the Banque Canadienne Nationale, as hereinafter mentioned), but the company's books indicate that during that period an account was maintained with the Bank of Montreal.

On July 21, 1947, Tremblay transferred all claims he might have against the company, as well as the shares in the company held by him, to one Ewart C. Atkinson for the price of $3,500. The transfer of 2,500 shares from Tremblay to Atkinson was registered in the books of the company on July 21, 1947, and Tremblay ceased to be a shareholder on that date. The company's books of account indicate that by July 21, 1947, Mr. Atkinson was already a substantial creditor of the company and the minutes of a meeting of directors held on that date state that he was.

A Cash Book of the company, filed as an exhibit by the respondent, contains entries made from September 12, 1946, to November 15, 1947, and the respondent also produced a bank book of Banque Canadienne Nationale in the name of the company, indicating that an account was opened with that bank on September 8, 1947, with a credit of $5,000, and which contains entries made from that date up to November 14, 1947, when the account still showed

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a credit of $220.06. The company's minute book, however, contains no record of any authorization for the opening of such account.

Onslow, who was the Secretary of the company, testified that he was aware that on or about September 8, 1947, a loan had been obtained by the company from the said bank; that this loan had been guaranteed personally by Mr. Atkinson but that no resolution of the Board had been passed authorizing the loan.

The company was declared bankrupt on March 11, 1948. The statement filed by the respondent as trustee indicates ordinary claims filed amounting to $7,145.75 and privileged claims totalling $2,123.78. The largest creditor was the Banque Canadienne Nationale with a claim of $4,717.10. The obvious inference to be drawn from the evidence is that all these claims arose subsequent to July 21, 1947, when Atkinson appears to have taken over the direction and control of the company. Certainly those arose subsequent to September 1946 when Tremblay paid off the company's indebtedness to the Banque Provinciale.

The legal issues involved in this appeal are the following:

1. Whether the failure to register the contract of May 31, 1946, with the provincial Secretary, under the provisions of s. 42 of *The Quebec Companies Act,* rendered the appellant liable as a contributory, for the full issue price of the shares.
2. Even if it did, whether he ceased to be so liable by reason of the transfer of his shares to E. C. Atkinson on July 21, 1947.

The Court of Appeal held against appellant on both issues but declared the liability of $25,000 on his shares to have been compensated to the extent of $19,600, and held him liable as a contributory for the balance of $5,400. There has been no cross-appeal.

Since I have reached the conclusion that appellant is entitled to succeed on the second issue of law to which I have referred, I do not find it necessary to consider whether s. 42 of *The Quebec Companies Act* has any application in the circumstances of this case.

The law as to the effect of a transfer of shares was comprehensively stated by Lindley L. J. in *In re National Bank of Wales; Taylor, Phillips, and Rickards' Cases*[1], where he said:

> The word "share" does not denote rights only—it denotes obligations also; and when a member transfers his share he transfers all his rights and obligations as a shareholder as from the date of the transfer. He does not transfer rights to dividends or bonuses already declared, nor does he transfer liabilities in respect of calls already made; but he transfers his rights to future payments and his liabilities to future calls.

Since appellant had transferred his shares to Atkinson long prior to the bankruptcy, respondent based his claim to have appellant declared a contributory, upon s. 70, subss. 1 and 3, of the *Bankruptcy Act* then in force, R.S.C. 1927, c. 11, which read as follows:

> 70. (1) Every shareholder or member of a corporation or his representative shall be liable to contribute the amount unpaid on his shares of the capital or on his liability to the corporation or to its members or creditors, as the case may be, under the act, charter or instrument of incorporation of the company or otherwise.
>
> (3) If a shareholder has transferred his shares under circumstances which do not, by law, free him from liability in respect thereof, or if he is by law liable to the corporation or to its members or creditors, as the case may be, to an amount beyond the amount unpaid on his shares, he shall be deemed a member of the corporation for the purposes of this Act and shall be liable to contribute as aforesaid to the extent of his liability to the corporation or its members or creditors independently of this Act.

No section similar to s. 70(3) is contained in the present *Bankruptcy Act*, R.S.C. 1952, c. 14.

The effect of a similar section in the *Winding-up Act*, R.S.C. 1886, c. 129, was considered by Meredith C. J. C. P. in *In re Wiarton Beet Sugar Manufacturing Co.; Freeman's Case*[2], an appeal from a report of the official trustee which placed appellant on the list of contributories in respect of certain shares in a company then being wound-up under the *Winding-up Act*. The shares in question were bonus shares and although issued as fully paid, in fact nothing had been paid in respect of them. It was sought to hold Freeman liable not only for shares still registered in his name, but also for shares which he had previously transferred as fully paid up shares to a third party.

[1] [1897] 1 Ch. 298 at 305.
[2] (1906), 12 O.L.R. 149.

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Dealing with the shares transferred prior to the winding-up order, the learned Chief Justice referred to the fact that under the English *Companies Act* past members, within a year after they have ceased to be members, are in the event of the company being wound-up, made liable (under certain conditions and with certain limitations as to the extent of their liability) to contribute to the assets of the company, and that legislation of a similar character was then found in the *Bank Act of Canada,* and went on to point out that the Ontario *Companies Act,* under which the Wiarton Sugar Company was incorporated, contains no provision of a similar character, and that the only persons upon whom calls might be made are the shareholders of the company.

It might be noted here, that in this respect *The Quebec Companies Act,* under which the company in bankruptcy was incorporated, is similar to the Ontario *Companies Act* and contains no such provision.

The learned Chief Justice then went on to deal with the position under the *Winding-up Act,* in the following passage at p. 152:

> I find nothing in the Winding-up Act which creates any liability on the part of a past member of a company where such a member is not subjected to such a liability by the Act under the authority of which the company is created or some Act relating to it.
>
> Section 44 of the Winding-up Act, R.S.C. ch. 129, (now section 53(1) which is in virtually the same terms as s. 70(1) of the Bankruptcy Act), though very general in its terms, notwithstanding the use of the words "or otherwise", has, I think, no application to any liability which is not one of the shareholder or member as such, and sec. 45 (now sec. 54) is designed, I have no doubt, to meet such cases as are dealt with in the provisions of the Bank Act to which I have referred, and to provide for cases in which as under that Act a shareholder is liable beyond the amount unpaid on his shares.
>
> I am unable therefore to come to the conclusion that the appellant is liable *qua* shareholder to contribute to the assets of the company under the Winding-up Act.

The decision in *Freeman's* case was followed by Robson J., as he then was, in *In re Winnipeg Hedge and Wire Fence Company Limited*[1], another case involving s. 45 of the *Winding-up Act.*

[1] (1912), 22 Man. R. 83, 1 D.L.R. 316.

Section 70, subs. 3 of the *Bankruptcy Act* is in virtually the same terms as s. 45 (now s. 54) of the *Winding-up Act*, which was considered in *Freeman's* case and in the *Winnipeg Hedge and Wire* case, the same principles must be applicable under both Acts, and I am in agreement with the views expressed by the two learned judges, in the decisions to which I have just referred.

There is no suggestion of fraud or bad faith on the part of appellant. No attempt was made to show that the assets transferred under the contract of May 31, 1946, were not worth the price agreed upon. Appellant appears to have afforded substantial financial support to the company in bankruptcy. He took no part in the management of its affairs after September 11, 1946, the date on which he resigned as a director and officer of the company. When he transferred his shares to Atkinson on July 21, 1947, he appears to have done so in perfect good faith, believing them to be fully paid up, and the claim against him is based solely upon non-compliance with the statutory requirement of s. 42 of *The Quebec Companies Act*. In my opinion s. 70(3) of the *Bankruptcy Act*, R.S.C. 1927, c. 11, had no application under such circumstances.

For the reasons which I have given, I would allow the appeal with costs here and below, and restore the judgment of the learned trial judge.

LOCKE J.:—If it were necessary to determine the standing of the accounts as between the appellant and the bankrupt company as of the date of the receiving order, the proper disposition to be made of this matter, in my opinion, would be to direct a new trial, due to the inadequacy of the evidence. I consider, however, that the appellant is entitled to succeed on the grounds that he had ceased to be a shareholder several months prior to the bankruptcy and that the evidence does not support a claim on the part of the trustees under subs. (3) of s. 70 of the *Bankruptcy Act*, R.S.C. 1927, c. 11, and amendments.

It should be said that there is nothing in the evidence to indicate any inadequacy in the consideration given by the appellant and the mis-en-cause for the shares allotted to them on May 31, 1946, as payment for the assets transferred to the company, and the failure to register the contract with

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the Provincial Secretary, as required by s. 42 of *The Quebec Companies Act*, R.S.Q. 1941, c. 276, was not attributable to either of these parties. As to the subscription for 1,500 other shares by the appellant on that date which, according to the company's records, had been paid for in cash by the appellant depositing the amount of $15,000 in the company's bank account, while the evidence shows that this amount had not been paid prior to the allotment, I would consider that it was a proper inference from the evidence that this amount had been paid by the moneys paid in to the company's credit in the Banque Provinciale by the appellant on July 13, 1946. The evidence is so unsatisfactory and incomplete, however, that if it were necessary to deal with this aspect of the matter it would be my opinion that there should be a new trial.

The evidence is, however, clear that the shares issued to the appellant were so issued as being fully paid up and that on July 21, 1947, nearly eight months prior to the making of the receiving order, the appellant sold and transferred all of these shares to E. C. Atkinson and the transfer was approved at a regularly constituted meeting of the directors and new shares issued as fully paid up to Atkinson. While unnecessary, the proceedings at this meeting of the directors were approved at a meeting of the shareholders held later on the same day.

The bankrupt company was incorporated by letters patent under *The Quebec Companies Act*. Under s. 38 shareholders are liable for any amount unpaid on their shares in the capital stock of the company. Under s. 68 transfers of shares are not valid for any purpose until entry thereof is duly made in the register of transfers and, in the present case, in respect of the shares of the appellant that requirement was duly complied with.

Section 70 of the *Bankruptcy Act*, as it read at the relevant times, under a sub-heading "Contributories to Insolvent Corporations", provided by subs. (1) that every shareholder shall be liable to contribute the amount unpaid on his shares of the capital. The liability of a contributor is *qua* shareholder and the appellant was not declared bankrupt until March 11, 1948, several months after the appellant had ceased to be a shareholder.

For the trustee, however, it is contended that there is liability under subs. (3) of s. 70 which read:

> If a shareholder has transferred his shares under circumstances which do not, by law, free him from liability in respect thereof, or if he is by law liable to the corporation or to its members or creditors, as the case may be, to an amount beyond the amount unpaid on his shares, he shall be deemed a member of the corporation for the purposes of this Act and shall be liable to contribute as aforesaid to the extent of his liability to the corporation or its members or creditors independently of this Act.

This subsection was taken practically *verbatim* from s. 54 of the *Winding-Up Act,* R.S.C. 1927, c. 213.

Where a shareholder has validly transferred his shares before a call is made by the company, it is a good defence to an action by the company in respect of the call, provided the transfer has been registered in its books. Apart from any liability that might arise by reason of subs. (3) of s. 70, after the transfer had been recorded the appellant ceased to be liable to be made a contributory in a winding-up or bankruptcy: Masten & Fraser on Company Law, 4th ed., p. 286; *In Re Hoylake Railway Co.; Ex-parte Littledale*[1]. The property in the shares passes when the directors assent to the transfer and it is registered, and the transferor cannot be liable *qua* shareholder.

Subsection (3), which was not reproduced when the *Bankruptcy Act,* 1927 was repealed and reenacted by the *Bankruptcy Act,* 1949, dealt with cases where the transfer of shares is made under circumstances which do not by law free the shareholder from liability in respect thereof, which presumably refers to transfers which may be impeached for, *inter alia,* fraud or other irregularity, and does not touch the present transaction. The meaning to be assigned to the words "if he is, by law, liable to the corporation or to its members or creditors, as the case may be, to an amount beyond the amount unpaid on his shares" is, I think, not free from doubt but has no application to the present matter.

[1] (1874), L.R. 9 Ch. 257.

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I would accordingly allow the appeal with costs, including the costs of the respondent's motion made on May 25, 1959, and restore the judgment at the trial.

Appeal allowed with costs.

Attorneys for the defendant, appellant: Lafleur & Ste. Marie, Montreal.

Attorney for the plaintiff, respondent: J. Prieur, Montreal.