ASHLEY COLTER LIMITED (DEFENDANT) ..... } APPELLANT;

AND

W. J. SCOTT (PLAINTIFF) ..... RESPONDENT.

1941
* Oct. 27.
1942
* June 26.

ON APPEAL FROM THE SUPREME COURT OF NEW BRUNSWICK, APPEAL DIVISION

*Promissory notes—Notes endorsed for accommodation of payee, discounted at bank by payee, and, upon non-payment, charged back by bank to endorser—Action by endorser against maker—Partial failure of consideration as between maker and payee—Circumstances alleged as affecting endorser's right of recovery against maker—Bills of Exchange Act, R.S.C., 1927, c. 16, ss. 55, 56 (2), 57, 70, 135.*

Plaintiff sued for $3,673.75 and interest, upon three promissory notes which were made by defendant to S. and, after endorsement by plaintiff, were discounted by S. at a bank, and upon non-payment were charged by the bank to plaintiff. The notes were renewals in respect of drafts accepted by defendant in connection with a contract for sale of lumber by S. to defendant, which provided that S. should ship lumber on receipt of orders, that defendant should pay for lumber 30 days after shipment, and accept drafts up to $5,000, that payments for shipments made should be deducted from the amount of the drafts accepted, that the title to the lumber was to pass to and remain in defendant as soon as any drafts were accepted by it.

The trial Judge found that there was a partial failure in respect of the consideration for the notes; that the lumber shipped fell considerably short of the estimate, and on the basis of actual quantity the amount that would be coming to S. under the contract was only $1,054.48. He further found that plaintiff was not damnified by reason of the notes being charged to his account; that he was a guarantor, as endorser, of S.'s account with the bank to an amount of over $30,000; that he was assisting S. financially in his lumbering operations; that he had full knowledge of said contract, and his endorsements were made for S. with the understanding that the proceeds of the lumber would be applied to reduce S.'s liability at the bank, and, as a result, to reduce plaintiff's liability; that this was done; that the notes when discounted were credited to S.'s account, reducing his as well as plaintiff's liability, and when charged back again plaintiff's liability was the same as before less payments made from proceeds of the lumber; that the consideration for the notes was the providing of lumber by S.; that was the sole purpose for which they were given and the only way by which they were to be paid, and this was understood by plaintiff when he endorsed them and when they were finally transferred to him; that plaintiff was an accommodation endorser; and took the notes after they were overdue, without giving value; and he held that plaintiff was in no

* PRESENT AT THE HEARING:—Duff C.J. and Rinfret, Crocket, Kerwin and Taschereau JJ. By reason of illness, Crocket J. took no part in the judgment.

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better position, as to recovery from defendant, than was S.; and he gave judgment for only the said sum of $1,054.48 (which defendant had tendered and paid into court) less defendant's costs.

The Supreme Court of New Brunswick, Appeal Division, reversed the judgment at trial and gave judgment to plaintiff for the full amount claimed (15 M.P.R. 385). Defendant appealed.

*Held:* The appeal should be dismissed.

The Chief Justice would dismiss the appeal on grounds fully stated in the judgment of Baxter C.J., 15 M.P.R. 385, at 389-399.

*Per* Rinfret, Kerwin and Taschereau JJ.: There was consideration for the drafts (and so, therefore, for the promissory notes which replaced them); the giving of them was part of defendant's obligations under its contract with S.; they were part of the consideration for the contract itself. No restriction was stipulated between the parties to the contract as to S.'s right to negotiate the drafts. Upon their acceptance, the title to the lumber passed to and remained in defendant. The contract merely called for an adjustment after all shipments had been made, should the lumber fall short of the quantity estimated. To all purposes, the acceptance of the drafts was the equivalent of a payment on account of the total purchase. Therefore there was no defect of title affecting the drafts or notes at their maturity; nor were they subject to any inherent equities affecting rights of a holder for value. Partial failure of consideration between the immediate parties to a bill cannot affect the title of remote parties (*Robinson* v. *Reynolds*, 2 Q.B. 196; *Thiedemann* v. *Goldschmidt*, 1 De G. F. & J. 4). The bank gave value, and was a holder in due course. Plaintiff was a holder for value. When the notes were charged back to plaintiff, from all points of view he gave payment for them. He was an accommodation endorser who had received no value therefor. His title to the notes was in no way defective within the meaning of the *Bills of Exchange Act*. Further, assuming that the notes were charged to him after their maturity, he derived his title to them through a holder in due course, and, not being a party to any fraud or illegality affecting them, he had all the rights of that holder in due course as regards defendant. Accordingly, having been compelled as endorser to pay the notes, he could recover their amount from defendant. To escape liability it was necessary for defendant to show that plaintiff was controlled by an equity inherent in the transaction and which was not compatible with the assignment of the notes after they became due; and no such equity here existed. Plaintiff's endorsements were not given pursuant to any agreement in respect of defendant.

*Bills of Exchange Act*, R.S.C., 1927, c. 16, ss. 55, 56 (2), 57, 70, 135, referred to.

APPEAL by the defendant from the judgment of the Supreme Court of New Brunswick, Appeal Division (1), allowing the plaintiff's appeal from the judgment of Richards J.

(1) 15 M.P.R. 385; [1941] 2 D.L.R. 192.

The plaintiff's claim was for the amount of three promissory notes made by the defendant in favour of one Gordon Scott and endorsed by the plaintiff and discounted by Gordon Scott at the Royal Bank of Canada at Fredericton, N.B., which were not paid by the defendant (except as to a tender, which was rejected, of what the defendant claimed to be the only amount owing, as hereinafter mentioned), and were charged by the bank to the plaintiff.

The notes were renewals in respect of certain drafts accepted by the defendant in connection with the agreement hereinafter mentioned.

By an agreement of June 18, 1930, between the said Gordon Scott and the defendant, the said Gordon Scott agreed to sell and the defendant agreed to purchase all the merchantable white pine lumber owned by Gordon Scott which was then piled at McPherson Siding and which was estimated to be 250,000 feet; Gordon Scott agreed to load the lumber on cars immediately on receipt of orders from defendant to do so; the price to be paid by defendant was $25 per thousand F.B.M.—F.O.B. cars McPerson Siding; defendant was to pay for all lumber shipped 30 days after date of shipment and to accept drafts up to $5,000; any payments for shipments made were to be deducted from the amount of the drafts accepted; if defendant had not given orders for shipment by December 31, 1930, defendant was to pay all interest charges from that date; the title to the said lumber was to pass to and remain in defendant as soon as any drafts were accepted by defendant under the terms of the contract.

Defendant accepted drafts, which were discounted by Gordon Scott at the said bank, after being endorsed by plaintiff. The drafts were renewed from time to time, lumber was shipped and the proceeds applied against the drafts. Later the drafts were changed to promissory notes signed by defendant. The notes sued on were the last renewals.

The plaintiff claimed in all the sum of $3,673.75 and interest thereon. The defendant had tendered to the bank the sum of $1,054.48, as being the amount due under the contract, and paid this sum into court.

The trial Judge, Richards J., gave judgment for the plaintiff for only the said sum of $1,054.48, less defend-

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ant's costs. He found that there was a partial failure in respect of the consideration for the notes; that the quantity of lumber fell considerably short of the estimate; and that, calculated on the basis of the actual quantity, and taking into account the interest overpaid on drafts for an amount greater than that justified by the quantity of lumber, the amount that would be coming to Gordon Scott under the contract would be only the said sum of $1,054.48. The trial Judge further found that the plaintiff was not damnified by reason of the notes being charged to his account; that he was a guarantor, as endorser, of Gordon Scott's account with the bank to an amount of over $30,000; that he was assisting Gordon Scott financially in his lumbering operations; that plaintiff had full knowledge of the contract between Gordon Scott and defendant and the endorsements were made by plaintiff for Gordon Scott with the understanding that the proceeds of the lumber would be applied to reduce the liability of Gordon Scott at the bank, and, as a result, to reduce the liability of the plaintiff; that this was done; that the notes when discounted were credited to Gordon Scott's account, reducing his liability as well as that of the plaintiff, and when charged back again the plaintiff's liability was the same as before less such payments as were made from the proceeds of the lumber; that the consideration for the notes was the providing of lumber by Gordon Scott; that that was the sole purpose for which they were given and the only way by which they were to be paid; that that was fully understood by plaintiff when the notes were endorsed by him and when they were finally transferred to him; that plaintiff was an accommodation endorser; and took the notes after they were overdue, without giving value. He held that the plaintiff was in no better position, as to recovery from defendant, than was Gordon Scott. He referred to s. 70 (1) of the *Bills of Exchange Act*, held that the term therein "defect of title" is equivalent to the former expression "equity attaching to the bill," as used in cases which he referred to; and that partial failure of consideration is an equity attaching to a bill and is a good defence *pro tanto* by the acceptor against the claim of an endorsee without value, of an overdue bill; also that the clearly implied agreement between defendant and Gordon Scott that the original drafts and subsequent renewal notes

(including the notes sued upon) were to be paid only to the extent covered by the value of the lumber, constituted an equity attaching to the notes.

On appeal by the plaintiff to the Supreme Court of New Brunswick, Appeal Division, that Court allowed the appeal and gave judgment to the plaintiff for the full amount claimed, for reasons which are reported (1).

The defendant appealed to this Court.

*P. J. Hughes K.C.* for the appellant.

*C. L. Dougherty* for the respondent.

THE CHIEF JUSTICE—The grounds on which I think this appeal should be dismissed are fully stated in the judgment of the Chief Justice of New Brunswick (2).

The appeal should be dismissed with costs.

The judgment of Rinfret, Kerwin and Taschereau JJ. was delivered by

RINFRET J.—In my opinion, this appeal should be disallowed.

The respondent sued the appellant on three promissory notes, of which he became the holder in the following way:

The appellant had purchased from Gordon G. Scott, of Fredericton, "all the merchantable white pine lumber owned by the [latter] which is now piled at McPherson Siding, on the Canadian National Railway." The lumber was estimated at 250,000 feet, of which 220,000 was of a two-inch thickness and 30,000 of one-inch.

Gordon Scott agreed to load the pine on cars immediately on receipt of orders from appellant to do so.

The price to be paid by the appellant was fixed at $25 per thousand F.B.M.—F.O.B. cars McPherson Siding.

The appellant agreed to pay for all lumber shipped thirty days after date of shipment and to accept drafts up to $5,000. The payments for shipments were to be deducted from the amount of the drafts accepted.

It was also agreed that, if the appellant had not given orders for shipment by December 31st, 1930, appellant would then pay all interest charges from that date.

(1) 15 M.P.R. 385; [1941] 2 D.L.R. 192.
(2) 15 M.P.R. 385, at 389-399 (Baxter C.J.).

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It was "further agreed that the title to the said lumber shall pass to and remain in the said Ashley Colter Limited as soon as any drafts are accepted by the said Ashley Colter Limited under the terms of this contract."

In June, 1930, the appellant accepted a draft from Gordon Scott for $1,000; in February, 1931, one for $725; and, in June of 1931, another for $4,000.

The two drafts for $1,000 and $4,000 obviously covered the full amount for which the appellant had agreed to accept drafts; but it was explained in the evidence that the other draft of $725 was to cover a further amount required by Gordon Scott to provide for compensation or insurance in connection with the lumber.

The drafts were renewed from time to time; lumber was shipped and the proceeds were applied against the drafts. Later, the drafts were changed to promissory notes signed by the appellant. The notes sued on are the last renewals thereof.

The learned trial Judge found that, according to the evidence, the lumber shipped by Gordon Scott fell considerably short of the estimate. Taking into account the interest paid on drafts for an amount greater than the amount justified by the quantity of lumber, and accepting the appellant's calculation, the learned Judge found that the amount due Gordon Scott by the appellant was $1,054.48, after the last of the lumber covered by the contract had been shipped, in June, 1934.

Gordon Scott had died in the preceding month.

The notes were then held by The Royal Bank of Canada, at its Fredericton branch, where they had been discounted.

The appellant delivered a cheque for the amount of $1,054.48; but the bank refused to accept it on the ground that the amount was insufficient (although the manager of the branch also says it was not accepted on instructions of the respondent).

The amount of the notes was then charged to the account of the respondent on October 3rd, 1934, the cheque of $1,054.48 being returned to the appellant.

The action was commenced on October 18th, 1934, and the appellant paid the amount of $1,054.48 into court with the delivery of the defence on January 8th, 1935.

The appellant contended that consideration for the notes failed by reason of the fact that there was insufficient lumber to cover the amount of the drafts.

The learned trial Judge found as a fact that there was a partial failure in respect of the consideration for the notes. He admitted, however, that such a fact, in itself, would not be sufficient to constitute a defence; but he said it was clear, from the evidence, that the respondent "was not damnified by reason of the notes being charged to his account". He was a guarantor and endorser of Gordon Scott's account to an amount of over $30,000. He was assisting him financially in his lumbering operations; he had full knowledge of the contract between Gordon Scott and the appellant,

> and the endorsements were made by him for Gordon G. Scott with the understanding that the proceeds of the lumber would be applied to reduce the liability of Gordon G. Scott at the Bank, and as a result to reduce the liability of the [respondent] * * * The notes when discounted were credited to Gordon G. Scott's account, reducing his liability as well as that of the [respondent]; and, when charged back again, the [respondent's] liability was the same as before, less such payments as were made from the proceeds of the lumber.

In the opinion of the learned trial Judge, Gordon Scott could not have recovered from the appellant more on the notes than the balance due on the lumber which, as already stated, he found to be $1,054.48; and he did not think the respondent was in any better position because he, as accommodation endorser, took back the notes after they were due without giving value; and he referred to section 70 of the *Bills of Exchange Act*, which is:

> When an overdue bill is negotiated, it can be negotiated only subject to any defect of title affecting it at its maturity, and thenceforward no person who takes it can acquire or give a better title than that which had the person from whom he took it.

Accordingly, and in view of the tender made with the defence, the learned trial Judge dismissed the respondent's action with costs.

In the Appeal Division, the appeal was allowed and the respondent's action was maintained; and, as already indicated, my view is that the judgment of the Appeal Division should be affirmed.

There cannot be any doubt that there was consideration for the drafts given by the appellant, and so, therefore, for the promissory notes which replaced them. The giving

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of the drafts was part of the obligations undertaken by the appellant under the agreement with Gordon Scott. They were part of the consideration for the contract itself. No restriction was stipulated between the immediate parties to the contract as to the right of Gordon Scott to negotiate these drafts or, subsequently, the notes.

Immediately upon accepting the drafts, the title to the lumber passed to and remained in the appellant.

The agreement merely called for an adjustment after all the shipments of lumber had been made, if it should happen that the lumber fell short of the quantity estimated. To all purposes, the acceptance of the drafts was the equivalent of a payment on account of the total purchase.

As a consequence, there was no defect of title affecting the drafts or notes at their maturity, nor were the notes subject to any inherent equities which might have affected the rights of a holder for value.

Assuming there be partial failure of consideration between the immediate parties to a bill, such a failure cannot affect the title of remote parties (See: Lord Denman, C.J., in *Robinson* v. *Reynolds* (1), of which the Lord Chancellor said, in *Thiedemann* v. *Goldschmidt* (2), that the authority had never been questioned; Byles, on Bills, 18th Ed. at p. 137).

The bank gave value for the bills or notes, and it was a holder in due course. The respondent was a holder for value. When the notes were charged back to the account of the respondent, from all points of view, the respondent gave payment for them. He was himself an accommodation endorser who had received no value therefor (*Bills of Exchange Act,* sec. 55 of ch. 16 of R.S.C., 1927). The title of the respondent to the notes was in no way defective within the meaning of the Act. He had not obtained them "by fraud, duress or force and fear, or other unlawful means, or for an illegal consideration * * * or under such circumstances as amount to a fraud" (sec. 56 (2)).

Further, assuming that the notes were charged to the respondent's bank account after their maturity, the respondent derived his title to the notes through a holder in due course; and, under sec. 57 of the Act, not being himself a party to a fraud or illegality affecting the

(1) (1841) 2 Q.B. 196.

(2) (1859) 1 De G. F. & J. 4.

notes, he had all the rights of that holder in due course as regards the appellant which signed the notes. Accordingly, the respondent, having been compelled as endorser to pay the notes, may recover the amount thereof from the appellant, which was the promissor thereof (sec. 135). To escape liability, as was said by the learned Chief Justice of the Appeal Division, it was necessary for the appellant "to show that the [respondent was] controlled by an equity inherent in the transaction and which [was] not compatible with the assignment of the notes after they [had] become due—if they are to be treated as overdue before assignment." No such equity existed in the present case. The respondent's endorsements on the notes were not given pursuant to any agreement in respect of the appellant.

When it is stated that the endorser of an overdue bill takes it back subject to its equities, that means: the equities of the bill, not the equities of the parties. He does not take it subject to a mere right not inherent in a contractual relation represented by the bill. (The *Swan* case (1), Malins, V.C., at p. 359).

For these reasons, the appeal ought to be dismissed with costs.

*Appeal dismissed with costs.*

Solicitor for the appellant: *Peter J. Hughes.*

Solicitors for the respondent: *Hanson, Dougherty & West.*