CASES

DETERMINED BY THE

SUPREME COURT OF CANADA ON APPEAL

FROM

DOMINION AND PROVINCIAL COURTS

D. K. ELLIOTT (PLAINTIFF) ..... APPELLANT;

AND

CANADIAN CREDIT MEN'S TRUST ASSOCIATION, LIMITED (DEFENDANT) ..... RESPONDENT.

1934

*Oct. 15
*Dec. 12

ON APPEAL FROM THE COURT OF APPEAL FOR MANITOBA

Bankruptcy—Trusts and trustees—Real Property—Person becoming registered owner of land, and making mortgage thereon (with covenant for payment), for benefit of company—Transfer from him to company made but not registered—Authorized assignment by company under Dominion Bankruptcy Act—Indemnity claimed by registered owner (as trustee) against company's trustee in bankruptcy (as cestui que trust) against liabilities in connection with land and mortgage.

W. Co. purchased lands in Winnipeg in the province of Manitoba, and title was taken in appellant's name. Appellant made a mortgage, for W. Co.'s benefit, on part of the lands, with the usual covenant for payment. Appellant delivered to W. Co. transfers of the lands. These were not registered. In 1931 W. Co. made an authorized assignment under the Dominion *Bankruptcy Act*, and respondent was appointed trustee, and became possessed of the said transfers and of certain documents of title. The assignment was duly registered against the lands in the land titles office. On instructions from respondent's clerk (not authorized by the inspectors of the estate) to get title in respondent's name, respondent's solicitor (who did not then know that part of these lands was mortgaged) prepared a transfer direct (to save expense) from appellant to respondent, which was executed but was found objectionable in certain respects in the land titles office and was not registered, and respondent did not pursue this further. It offered to return the transfer. Respondent took over the management of the lands, collected rents, and paid thereout certain interest, taxes and insurance premiums. Appellant claimed that respondent had assumed the relation to appellant of *cestui que trust* and was bound to indemnify him against liabilities in connection with the trust property, including liability under appellant's mortgage covenant.

Held: The claim for indemnity failed. In view of respondent's position under the *Bankruptcy Act* (provisions of which were considered and

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*PRESENT:—Duff C.J. and Cannon, Crocket, Hughes and Maclean (*ad hoc*) JJ.

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discussed in this regard), the equitable rule as to a trustee's right to indemnity from a beneficial owner was not applicable to the case. *Graham* v. *Edge*, 20 Q.B.D. 683, cited. *Hardoon* v. *Belilios*, [1901] A.C. 118, and *Castellan* v. *Hobson*, L.R. 10 Eq. 47, distinguished.

Judgment of the Court of Appeal for Manitoba, 42 Man. R. 69, affirmed.

APPEAL by the plaintiff from the judgment of the Court of Appeal for Manitoba (1) dismissing (Robson J.A. dissenting) his appeal from the judgment of Donovan J. (2) dismissing his action; in which action he claimed that he, as trustee, was entitled to be indemnified by the defendant, as *cestui que trust*, against liabilities to which the plaintiff was or might be subject in connection with certain lands, and particularly against his liability under a covenant in a certain mortgage which he had made on part of the said lands. The material facts of the case are sufficiently stated in the judgment of Hughes J. now reported, and are indicated in the above headnote. The appeal was dismissed with costs.

J. B. Coyne K.C. for the appellant.

W. A. T. Sweatman K.C. for the respondent.

DUFF C.J.—The general principle of equity is well known that a trustee is entitled to indemnity in respect of all expenses properly incurred in the execution of his trust. This right may always be enforced against the trust estate in respect of which he has incurred a debt or liability and in certain circumstances against the *cestui que trust* personally. It is only with this last mentioned right that we are concerned in this appeal.

The right to be indemnified by the creator of the trust, or by a third person, may arise either by the operation of the general equitable principle or from contract express or implied. The general principle is that when a trustee holds property in trust for an absolute beneficial owner, who is *sui juris*, the *cestui que trust* is bound to indemnify the trustee personally in respect of liabilities which arise from the mere fact of legal ownership. It is not material that the beneficiary did not create the trust or did not request the trustee to incur the liability.

(1) 42 Man. R. 69; [1934] 1 W.W.R. 801; [1934] 3 D.L.R. 129; 15 C.B.R. 392.

(2) 41 Man. R. 398; [1933] 2 W.W.R. 11; 14 C.B.R. 350.

The question before us is whether these principles are applicable when the *cestui que trust* becomes bankrupt and his property passes by force of the statute to the trustee in bankruptcy.

We are not concerned with any question as to a charge upon the trust property for the amount of the debt or liability incurred or as to the right of the trustee to enforce his claim against the bankrupt estate as a creditor. The contention raised is that the trustee in bankruptcy is personally responsible just as any individual would be who had accepted a transfer of the trust property as purchaser from the *cestui que trust*.

The result of the bankruptcy is that the trustee's personal remedy against the bankrupt is suspended and he may lose it altogether. That involves a hardship, no doubt; but then, bankruptcy and insolvency usually do involve such hardships.

After carefully considering Mr. Coyne's able and elaborate argument, my conclusion is that, the property of the bankrupt, vesting, as it does, by operation of law in the trustee in bankruptcy in his official capacity (who is declared by the statute to be " in the same position as if he were a receiver of the property, appointed by the court," with the duty primarily of applying and distributing the property for the benefit of the bankrupt's creditors (pursuant to the statutory scheme)), effect cannot be given to the principle of equity in the manner contended for unless there is something in the statute expressly or impliedly requiring it. I find nothing having that effect.

I think the reasoning of Lord Esher in *Graham* v. *Edge* (1) is in point.

These considerations apply *mutatis mutandis* to the contention that the trustee in bankruptcy is under a personal obligation to indemnify the appellant as transferee of the mortgaged property.

The appeal should be dismissed with costs.

The judgment of Cannon, Crocket, Hughes and Maclean (*ad hoc*) JJ. was delivered by

HUGHES J.—In the year 1906 R. J. Whitla & Company, Limited, purchased lands in the city of Winnipeg. Title

(1) (1888) 20 Q.B.D. 683.

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was taken in the name of the appellant who was the president and an important shareholder in the company. On April 3, 1907, $25,000 was borrowed to erect a building on part of the lands and a mortgage with the usual covenant for payment was made by the appellant. On September 18, 1912, the appellant delivered to R. J. Whitla & Company, Limited, a transfer of the encumbered property and, on July 15, 1913, a transfer of the unencumbered property; and these transfers and a certified copy of the certificate of title to the encumbered property and a certificate of title to the unencumbered property were in the possession of R. J. Whitla & Company, Limited, at the time of the authorized assignment hereinafter discussed and were turned over to the respondent. No payments of principal were made on the mortgage.

On February 16, 1931, the company made an authorized assignment under the *Bankruptcy Act* and on March 9, 1931, the respondent was appointed trustee. The assignment was duly registered against the real properties in the Land Titles Office. The respondent took over the management of the properties and paid certain interest, taxes and insurance premiums out of the rents as received. Shortly after the assignment a clerk of the respondent wrote the respondent's solicitors enclosing the above transfers, certificate of title and certified copy of certificate of title respectively, with instructions to put the titles in the name of the respondent, or, in the event of objection by the Land Titles Office, in the name of the respondent as trustee for R. J. Whitla & Company, Limited. The inspectors of the estate did not authorize these instructions. Mr. Richards, now the Honourable Mr. Justice Richards of the Court of Appeal of Manitoba, was then head of the firm of solicitors acting for the respondent. He did not notice that the letter of instructions contained a certified copy only of one of the certificates of title and assumed that each property was clear of encumbrance. To save expense, Mr. Richards prepared a transfer covering both properties from the appellant directly to the respondent and did not register the transfers to R. J. Whitla & Company, Limited. The new transfer was then sent to the appellant's solicitor for execution and was returned duly executed. The Land Titles Office rejected the transfer because one parcel was encumbered, and because of some objection about the way in

which the transferee was described. Mr. Richards then first knew that there was a mortgage on one of these properties. The respondent offered to return this transfer to the appellant. The trustee, of course, knew from the time of its appointment as trustee on or about March 9, 1931, that the appellant had executed the transfers to R. J. Whitla & Company, Limited, that the transfers had not been registered and that one parcel comprising the west halves of lots three and four in block K on plan 16 was subject to a mortgage for $25,000 and interest. At the time of the trial the respondent had on hand from these properties $1,390 without deducting its collection charges.

The appellant brought this action against the respondent both in its personal and in its representative capacity for indemnity in full against all liabilities by reason of his alleged trusteeship for the respondent including his liability on the covenants of the mortgage on part of the lands.

The action was tried by the Honourable Mr. Justice Donovan and dismissed. The appellant appealed to the Court of Appeal for Manitoba and the appeal was dismissed, the Honourable Mr. Justice Robson dissenting. From this judgment the appellant now appeals to this Court.

The appellant contends that, since the right and obligation of indemnity go with the relationship of trustee and *cestui que trust* and are part of it, when a trustee under the *Bankruptcy Act* succeeds as *cestui que trust,* his position is not different from that of any other *cestui que trust;* and that, if there is a difference, the burden falls on the *cestuis que trustent* of the trustee, namely, the estate. The appellant further contends that the respondent had an option whether it would or would not assume the relationship, but it assumed it by taking over the property and is bound by estoppel personally to indemnify the appellant.

The general principles of such indemnity are discussed in *Hardoon v. Belilios* (1). The question raised on that appeal was whether the plaintiff, who was the registered holder of fifty shares in a banking company which was being wound up, was entitled to be indemnified by the defendant, who was the beneficial owner of the shares,

(1) [1901] A.C. 118.

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against calls made upon the plaintiff in the winding-up of the banking company. The shares in question had been placed in the plaintiff's name by his employers, Benjamin & Kelly, who were share-brokers. The plaintiff never had any beneficial interest in the shares; but he was registered as their holder on April 3, 1891. A provisional certificate of his ownership was made out, and he signed a blank transfer of the shares, and the two documents were held by Benjamin & Kelly. The certificate and transfer afterwards came into the hands of one Coxon, who acted on behalf of a syndicate formed to speculate in the shares of another company. The defendant financed the syndicate and the provisional certificate and blank transfer of the shares were, with other securities, pledged by Coxon with the defendant as security for advances. In October, 1891, the plaintiff's provisional certificate was exchanged for an ordinary certificate which the defendant had in his possession at the commencement of the action. In March, 1892, dividends were paid on the shares. The defendant demanded and received these. The syndicate lost money and, in October, 1892, the defendant became the absolute owner of the shares. The judgment of the Judicial Committee of the Privy Council was delivered by Lord Lindley. Their Lordships point out that the parties stood to one another in the position of trustee and *cestui que trust* and that the fact that the parties never stood in the relation of vendor and purchaser is immaterial. All that is necessary to establish the relation of trustee and *cestui que trust* is to prove that the legal title was in the plaintiff and the equitable title in the defendant. Justice requires that the *cestui que trust,* who gets all the benefit of the property, should bear its burden unless he can shew some good reason why his trustee should bear it himself. The obligation is equitable and not legal, and the legal decisions negativing it, unless there is some contract or custom imposing the obligation, are irrelevant. Where the only *cestui que trust* is a person *sui juris,* the right of the trustee to indemnity against liabilities incurred by him by his retention of the trust property has never been limited to the trust property; it extends further and imposes upon the *cestui que trust* a personal obligation enforceable in equity to indemnify his trustee. In the above case, their Lordships refer with

approval to *Balsh* v. *Hyham* (1). In that case, the trustee sought indemnity in equity, not against a liability incidental to the ownership of the trust property, but against a liability incurred by him by borrowing money at the request of and for the benefit of his *cestui que trust*. The court decided that the plaintiff was entitled to relief on the ground " that a *cestui que trust* ought to save his trustee harmless as to all damages relating to the trust." Lord Lindley points out in the *Hardoon* case (2) that this language, although open to criticism if applied to *cestuis que trustent* who are not *sui juris* and also sole beneficial owners, shews plainly enough that it was taken for granted as well settled that, speaking generally, absolute beneficial owners of property must in equity bear the burden incidental to its ownership. Their Lordships also refer with approval to *In re The German Mining Co.; Ex parte Chippendale* (3), a case where the shareholders of a mining company were held liable personally to indemnify the directors against payments made by the latter in discharge of debts contracted by them but which payments created no legal obligation on the company enforceable at law, and could not be recovered by the directors from the company by an action at common law. The fact that the defendant in *Hardoon* v. *Belilios* (2) *supra,* did not create the trust on which the plaintiff held the shares when they were first placed in his name affords no defence to the defendant. Although the defendant did not create the trust, he accepted a transfer of the beneficial ownership of the shares, first as mortgagee and afterwards as sole beneficial owner, with full knowledge of the fact that they were registered in the plaintiff's name as trustee for the original purchasers. By the acceptance, the defendant became the plaintiff's *cestui que trust*. In the *Hardoon* case (2), the Judicial Committee approve the language of James V.C. in *Castellan* v. *Hobson* (4). In that case H had bought shares on the stock exchange. The name of B, who had consented to hold the shares was given as transferee. C, the original vendor, executed a transfer to B but, owing to the circumstances of the company, B could not be registered. It was held that H was liable to indemnify C for calls. James V.C. states

(1) (1728) 2 P. Wms. 453; 2 Eq Ca. Ab. 741, fol. 8.
(2) [1901] A.C. 118.
(3) (1853) 4 D. M. & G. 19.
(4) [1870] L.R. 10 Eq. 47.

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that it is not a question of vendor and purchaser but a question of trustee and *cestui que trust,* and that the trustee was entitled to indemnify from the " real equitable owner."

In *Wise* v. *Perpetual Trustee Company* (1), the Judicial Committee considered an appeal from the Supreme Court of New South Wales in which the point involved was whether trustees of a club who had incurred liability under onerous covenants in a lease were entitled to indemnity not only out of the club property to which their lien as trustees extended, but also against the appellant as a member of the club who with the other members, through the committee of management and otherwise, had so far assented to what had been done as to have become *cestuis que trustent* of the lessees. Their Lordships were satisfied that the relation of trustee and *cestui que trust* had been created. They refer, in their judgment, to the *Hardoon* case (2), and again point out that although the right of trustees to indemnity is recognized as well established in the simple case of a trustee and an adult *cestui que trust,* the principle by no means applies to all trusts, and it cannot be applied to cases in which the nature of the transaction excludes it. The appeal was, accordingly, allowed.

It is clear that when on the 9th day of November, 1906, the appellant, at the request of R. J. Whitla & Company, Limited, took title to the lands in question in his name, the relationship of trustee and *cestui que trust* existed between the appellant and R. J. Whitla & Company, Limited, and that, when he executed the mortgage for $25,000, he became entitled to indemnity in respect of the mortgage obligations from R. J. Whitla & Company, Limited. It is also clear that the relationship of trustee and *cestui que trust* existed between the appellant and R. J. Whitla & Company, Limited, at least down to September 18, 1912, in respect to the mortgaged parcel and to July 15, 1913, in respect to the unencumbered parcel, at which dates the appellant delivered transfers respectively to R. J. Whitla & Company, Limited. By these transfers the appellant purported to convey to the company all his estate and interest in the lands in question. After that, his position is not so clear. The appellant maintains that this transfer did not change the relationship and that the

(1) [1903] A.C. 139. (2) [1901] A.C. 118.

appellant still remained a trustee for the company, and refers us to the *Real Property Act,* R.S.M. 1913, ch. 171. Section 88 provides that every transfer, when registered, shall operate as an absolute transfer of all such right and title as the transferor had; but nothing contained in the section shall preclude any transfer from operating by way of estoppel. Section 97 provides that in every instrument transferring an estate or interest in land subject to mortgage under that system, there shall be implied a covenant by the transferee indemnifying the transferor against liability under the mortgage. Section 98 provides that a transfer shall, until registered, be deemed to confer on the person intended to take title a right or claim to registration.

It is now convenient to consider some of the provisions of the *Bankruptcy Act.* Section 9 provides for a voluntary assignment by a debtor. Section 9, subsection 6, provides that upon the appointment of a trustee by the creditors, the Official Receiver shall complete the assignment by inserting as grantee the name of such trustee and that thereupon the assignment shall, subject to the claims of secured creditors, vest in the trustee all the property of the debtor. Section 9, subsection 7, provides that every assignment of property other than an authorized assignment made by an insolvent debtor for the general benefit of his creditors shall be null and void. Section 39 provides that the trustee shall in relation to acquiring and retaining possession of the property of the debtor be in the same position as if he were a receiver of the property appointed by the court. Section 40 provides that the trustee shall, on the making of a receiving order or an authorized assignment, forthwith insure and keep insured in his official name all the insurable property of the debtor. Section 43 provides that the trustee may, with the permission in writing of the inspectors, (*a*) sell, (*aa*) lease, * * * (*k*) elect to retain for the whole or part of its unexpired term, or to assign or disclaim, any lease of or other temporary interest in any property forming part of the estate of the debtor. Section 104 provides that demands in the nature of unliquidated damages arising otherwise than by reason of a contract, promise or breach of trust, shall not be provable in bankruptcy; but, save as aforesaid, all debts and liabilities to which the debtor is subject at the date of the making of the authorized assignment shall be deemed to be debts provable in bankruptcy.

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The court shall value all contingent claims and after, but not before, such valuation, every such claim shall be deemed a proved debt to the amount of its valuation. Section 106 provides that if a secured creditor realizes his security, he may prove for the balance due to him after deducting the net amount realized. If he surrenders his security to the trustee, he may prove for his whole debt. Section 107 provides that a secured creditor who does not either realize or surrender his security may value his security and claim a dividend on the balance; and that the trustee may redeem the security at the assessed value. Section 113 provides that, subject to the provisions of section 107, no creditor shall receive more than one hundred cents on the dollar and interest. Section 120 provides that a creditor may prove for a debt not payable at the date of the authorized assignment as if it were payable presently and may receive dividends equally with the other creditors, deducting only an allowance for interest. Section 121 provides for priorities of claims. Section 123 provides that all ordinary debts shall be paid *pari passu*. Section 127 provides for the disallowance of claims by the trustee and for appeals to the court from such disallowances. Section 151 provides that where the debts of the bankrupt are paid in full, the court may annul the adjudication of bankruptcy and that, in such event, all acts of the trustee shall be valid, but the property of the debtor who was adjudged bankrupt shall vest in such person as the court may appoint or, in default of such appointment, revert to the debtor for all his estate or interest therein on such terms and subject to such conditions, if any, as the court may declare by order; and that, for the purposes of the section any debt disputed by a debtor shall be considered as paid in full if the debtor enters into a bond with approved securities to pay any amount recovered with costs. In view of the above provisions, it seems clear that the position of the respondent in the case at bar is somewhat analogous to the position of the official liquidators in *Graham* v. *Edge* (1). In that case, an order having been made for the winding-up of an unregistered company under the *Companies Act*, 1862, the court directed under section 203 of the Act that certain land, vested in trustees for the company subject to a rent

(1) (1888) 20 Q.B.D. 683.

charge, should vest in the official liquidators appointed for the purposes of the winding-up. The plaintiffs were the owners of the rent charge upon the land. They sued the liquidators in their personal capacity to recover arrears of the rent charge from them as terre-tenants. It was held by the Court of Appeal that the action ought to be stayed as being manifestly groundless. In that case the liquidators held possession for five years and it was contended, as in the case at bar, that they had elected and were personally liable. Lord Esher points out that the power to appoint the official liquidators was given by section 92 of the Act which provided that the liquidators were appointed "for the purpose of conducting the proceedings in winding up a company and assisting the Court therein," and that section 203 provided that the court might direct that all property, real and personal, belonging to or vested in the company or to or in any person in trust for the company should vest in the official liquidators by his or their official name or names. Lord Esher then proceeds to say that the meaning is that the property shall vest in the official liquidator, not in his personal capacity, but in his official capacity as official liquidator appointed by the court to assist in the winding-up of the company. The contention of the plaintiff is dealt with that the position of the official liquidators was the same as that of a trustee in bankruptcy under the English statute, who had a power to disclaim onerous property. No such power existed in the official liquidators who, therefore, could not be personally liable on the ground of election. Lord Justice Bowen was of the same opinion. He said that it could not really be suggested that the defendants had done anything but submit to the operation of section 203 by which the property was vested in them in their official name; and that they were not clothed with the property in any capacity other than that of official liquidators, subject to the directions of the court, and that there was no colour for suggesting that they were personally liable.

I have endeavoured to indicate the sections of the *Bankruptcy Act* which may be relevant to this case but, at the risk of repetition, I again point out that the respondent had by section 43 (*k*) a power to disclaim a lease but that nowhere was there power in the trustee to disclaim this property. I am of opinion that this is not a case for the

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application of the equitable rule of indemnity as in the *Hardoon* case (1) where the defendant *cestui que trust* was the beneficial owner of the shares. The respondent in the circumstances of this case does not come within the words "sole beneficial owner" or "absolute beneficial owner," *Hardoon* v. *Belilios* (1), *supra,* or within the words "real equitable owner," as used by James, V.C., in *Castellan* v. *Hobson* (2), *supra;* or within the more common words expressing the same legal concept, namely, "beneficial owner." In this connection, at the risk of another repetition, I refer back to section 151 of the *Bankruptcy Act.* A case similar to the case at bar may very easily be visualized where the debts are paid in full without selling the property held in trust for the debtor at all and where, under that section, the property may revert to the former debtor.

I should also add that if between November 9, 1906, and September 18, 1912, and possibly up to the assignment in bankruptcy, the appellant had paid off the mortgage and had recovered a judgment for indemnity against the company, he would have had to prove his claim as a secured or ordinary creditor. In this action, without payment, he asks for indemnity in full. To this he is not entitled.

The appeal should be dismissed with costs.

Appeal dismissed with costs.

Solicitor for the appellant: *J. B. Coyne.*

Solicitors for the respondent: *Sweatman, Fillmore, Riley & Watson.*

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(1) [1901] A.C. 118.

(2) (1870) L.R. 10 Eq. 47.