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*Nov. 8.
*Dec. 30.

ISIDORE HOCHBERGER AND OTHERS (PLAINTIFFS) ..... } APPELLANTS;

AND

MOSES RITTENBERG (DEFENDANT). RESPONDENT.

ON APPEAL FROM THE COURT OF KING'S BENCH, APPEAL SIDE, PROVINCE OF QUEBEC.

Debtor and creditor—Agreement for extension of time—Preference—Public order—Advantage to creditor—Security for debt—Conflict of laws—Lex loci.

Where a debtor obtains the assent in writing of his creditors to an extension of time for payment of their respective debts, upon an undertaking the he will not "give a preference" without their consent, a prior secret arrangement by which one of such creditors obtains security and more favourable terms of payment than that provided in the agreement is void as a fraud against the other creditors and as against public order.

The debtor carried on his business in Toronto where the deed granting the extension of time was drawn and executed. H., a New York creditor, obtained security by means of the debtor's promissory notes, drawn up and made payable in Toronto and indorsed by the defendant, residing in Montreal. The action on the notes was brought, in Quebec, against the indorser.

Held, per Idington and Anglin JJ., that the case should be decided according to the law of Ontario if there is any difference between it and the Quebec law on the subject-matter.

Judgment appealed from (Q.R. 25 K.B. 421), affirmed.

APPEAL from a decision of the Court of King's Bench, Appeal Side, for the Province of Quebec(1), affirming the judgment at the trial in favour of the defendant.

In the spring of 1913, one Grossman, a jeweller of the City of Toronto and brother-in-law of respondent, having become financially embarrassed in his business,

*PRESENT:—Sir Charles Fitzpatrick C.J. and Idington, Duff, Anglin and Brodeur JJ.

(1) Q.R. 25 K.B. 421.

called a meeting of his principal creditors, with a view of obtaining from them an extension of time.

After some *pourparlers* with representatives of creditors present they all agreed to an extension of delay and a memorandum of extension of time was drafted and was submitted to the above-mentioned creditors and signed by Grossman, and his creditors, with the exception of appellants whose representative was not authorized to sign.

Shortly afterwards, Julius Hochberger, one of the appellants, came to Toronto, for the purpose of ascertaining the financial standing of their debtor, with special instructions as regards settlement to be made with him. During the course of the discussion, which took place with Grossman alone at Toronto, Julius Hochberger refused to consent to the proposed extension unless appellants' claim was secured and the promissory notes then offered in settlement be made at shorter dates.

The promissory notes sued upon in this case having been prepared by Julius Hochberger, Grossman sent them to respondent, at Montreal, with a request to indorse them. Respondent returned the notes to Grossman refusing to indorse unless he got more particulars about them.

Having been informed by Grossman that plaintiffs, appellants, would not consent to the extension unless their claim was secured, and knowing that Max D. Eisen, the representative of plaintiffs, in Toronto, had previously promised Grossman that Hochberber would supply him with certain goods to carry him along, and replenish his stock, he then and there consented to indorse the notes, not being told that appellants were to sign the memorandum of agreement for extension.

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Defendant, respondent, having returned the promissory notes to Grossman, at Toronto, never heard anything further about them until the following January (1914), when Grossman, being incapable of meeting his payments, had to make an abandonment of his property for the benefit of his creditors. An action was then brought against respondent as indorser.

Lafleur K.C. and *Lamothe K.C.* for the appellants.

R. G. deLorimier K.C. and *Amie Geoffrion K.C.* for the respondent.

THE CHIEF JUSTICE.—This appeal should be dismissed with costs.

The promissory notes sued on were obtained in execution of an agreement between the appellants and their insolvent debtor.

The defendant, indorser of the notes, was a brother-in-law of the maker, Grossman, a jeweller, of the City of Toronto, and the appellants were amongst the latter's creditors. The notes were given to induce the appellants to sign Grossman's deed of composition.

As Best C.J. said in *Knight* v. *Hunt*(1), at page 433, these agreements for composition with creditors require the strictest good faith. The principle to be drawn from all the cases on this subject is

> that a man who enters into an engagement of this kind is not to be deceived.

It has been argued that here the debtor is not injured, nor the funds for the other creditors rendered less available, because the indorsation given and sued on was that of a third party who took no interest in the estate, but as the Chief Justice said in *Brigham* v. *Banque Jacques Cartier*(2), at page 436:—

(1) 5 Bing. 432.

(2) 30 Can. S.C.R. 429.

Upon a principle well established by the English courts such a payment by a third person is just as much a fraud on the general body of creditors as a payment or an agreement to pay by the insolvent debtor himself: *Wells* v. *Girling*(1); *Knight* v. *Hunt*(2); *Bradshaw* v. *Bradshaw* (3); *McKewan* v. *Sanderson*(4); *Re Milner*(5).

Pollock on Contracts (7 ed.), 293.

The one question which always remains is whether the judgment of the creditors has been influenced by the supposition "that they are treating on terms of equality as to each and all." This is not a case of a gratuitous gift made after composition. Here there was a previous secret understanding that the appellants should receive security for their debt and a direct advantage over all the others who were contracting on the assumption that all were being treated alike. The notes sued on were given in pursuance of an agreement which was void as made in fraud of the other creditors of Grossman: Art. 990 C.C.; see also *Ex parte Milner*(5).

IDINGTON J.—The appellants sued the respondent as indorser of six or seven promissory notes, remainder of ten or a dozen such, made by one Grossman and indorsed by respondent in order to satisfy the demands of appellants upon said Grossman, who had asked them to join in an agreement he was trying to obtain from a half dozen of his chief creditors for an extension of time. The agreement, as drawn up, had named one Eisen as one of the creditors intended to execute the agreement.

Eisen it turned out had no authority to sign being only an agent of the appellants.

This circumstance tends to confuse matters and the most has been made thereof.

(1) 1 Brod. & Bing. 447.
(2) 5 Bing. 432.
(3) 9 M. & W. 29.
(4) L.R. 20 Eq. 65.
(5) 15 Q.B.D. 605.

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But as appellants signed the agreement and Eisen did not and there can be doubt of what was intended to have been accomplished by the substitution of appellants for Eisen in the way of signing and in fact I think was accomplished, the agreement should be treated as one of the ordinary kind for an extension by creditors of time to a debtor, who otherwise might be forced to make an assignment as an insolvent.

On such basis I agree with the late Mr. Justice Dunlop's construction of the clause in said agreement which reads as follows:—

> The first party agrees that he will not during the currency of this extension and until these liabilities are paid off give any preference or security on any of his assets no matter where situate without the consent of the second parties.

What was done was clearly a preference, and none the less obnoxious because an ingenious method was resorted to of extracting something from the assets without the assent of other creditors.

It was circuitous but partially effective.

The notes given on the basis of the extension were to have been, and I think in fact were, for three, six, nine and twelve months.

The appellants got, in substitution thereof, notes spread over some twelve months, indorsed by respondent, divided into equal sums but payable monthly. Thereby, unless (which is not pretended) the money could be conceivably got elsewhere than out of the debtor's assets mentioned in above clause, the appellants got an improper advantage over others they held themselves out as joining.

Then apart from the interpretation of the agreement the giving these notes was illegal.

It may be worth while to let those people, and others inclined to do the like, know what Vice-Chan-

cellor Malins, an able English judge, thought was the law. He, in the case of *McKewan* v. *Sanderson*(1), at page 234, spoke thus:—

> I give no opinion as to whether this is a proper case for law or equity, and I give no opinion as to the law or the equity. That will have to be considered hereafter; but the ground of this plea is that there was an improper arrangement between the debtor and his creditor to the detriment of the other creditors, and the doctrine of this court is appealed to which was laid down so repeatedly by *Lord Eldon*, and finally in the case always referred to, of *Jackman* v. *Mitchell*(2). It is a doctrine founded on the soundest principles, namely, that whenever there are proceedings in bankruptcy or insolvency, or any arrangement between a debtor and his creditors generally, and one of the creditors stipulates either for the payment of a greater dividend to him than is paid to the other creditors, or for any collateral advantage whatever, even such as giving the right to purchase a horse, or any advantage whatever not common to the creditors, any payment made will be ordered to be repaid, any security given will be ordered to be given up, and this court will treat the whole thing as fraudulent against the other creditors; and anything done in favour of the creditor who obtains this advantage will be set aside by this court. That principle has been frequently acted upon. I refer to *Jackman* v. *Mitchell*(2), because it has been cited, but *Geere* v. *Mare*(3), is a case on the point at law; and finally, it was very much considered by Vice-Chancellor Stuart in *Mare* v. *Sandford*(4), which, as well as some other cases, arose under the same bankruptcy as *Geere* v. *Mare*(3).

The case is adopted, and cited with many others, by Sir Frederick Pollock at page 238 of his work on contracts, when dealing therein with the subject of fraudulent or illegal contracts of this character.

"Against public policy" is, I think, in this connection but another name for fraud. I agree with the law as laid down in what I quote from Malins V.-C. and hold the promissory notes sued upon herein are of the kind he describes and subject to the legal consequences he suggests.

They furnish no security upon which any one can recover or should as part of public policy be permitted to recover.

(1) L.R. 15 Eq. 229.
(2) 13 Ves. 581.
(3) 2 H. & C. 339.
(4) 1 Giff. 288.

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I cannot distinguish in principle any difference between a deed of composition and anything else of the like nature, jointly agreed upon by creditors, or a number of them, in case of a common debtor.

The Quebec law I imagine is the same despite the nice distinction said to have been made in France. I also think as the debtor gave the notes in Toronto and all else was done there except possibly the mere signing by respondent, and as it is the indorsement of a promissory note delivered there that is in question, the Ontario law is what should govern, if there is any difference.

The appeal should be dismissed with costs.

DUFF J.—The controversy which has led to this appeal arose out of an agreement, the terms of which are embodied in a memorandum dated the 4th April, 1913, between one Grossman and certain creditors of Grossman who included the appellants.

Grossman being in difficulties arranged with these creditors for an extension of time; there were other creditors whose claims were not included in the arrangement, these claims not being considered of sufficient importance to embarrass Grossman after obtaining the extension arranged for. The memorandum embodying the arrangement was executed on its date by all the parties except the appellants and one Ward. The absence of Ward's signature appears to have been accidental, since he carried out the arrangement in accordance with the understanding that he was a party to it. The appellants executed the document in the following month; and the execution of it by them was procured through an arrangement between themselves and Grossman, that Grossman was to obtain the guarantee of his brother-in-law, the respondent Ritten-

berg, that the appellants' claim would be paid. The guarantee was given in the form of an indorsement of each of the promissory notes sued upon; and was given and accepted on the understanding that the existence of the guarantee was not to be disclosed—as in point of fact it was not—to the creditors who were parties to the extension agreement.

The respondent's defence is that the agreement to give this guarantee behind the backs of the other creditors participating in the extension arrangement being a fraud on these creditors—the fraud vitiates the agreement and deprives of all legal effect the indorsements given in execution of it.

The memorandum signed by the creditors contains a recital to the effect that the creditors named as parties have executed it; and there can be no doubt that this recital embodies an essential term of the extension agreement which was made on the understanding that the claims of all the creditors named in the instrument as drawn were to be affected by the extension. It is true that the appellants are not mentioned *eo nomine* as parties but their agent is named and it was no doubt the appellants' claim that the parties had in view. It is clearly made out in point of fact, that Grossman, the appellants and the respondent all understood that the appellants' claim was to be brought within the arrangement for giving time and that involved, as it has been many times held, the assumption that they were to stand on an equal footing with all the other parties to the extension. Any advantage, therefore, obtained by them as the price of their participation, which was not made known to the other parties, must be an advantage which they could not retain without departing from the line of conduct marked out in such circumstances by the dictates of good faith. Yet this,

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in view of the agreement between the respondent and Grossman and the appellants, must be held to have been precisely what it was intended the appellants should do. In *Ex parte Milner*(1), it was decided by the Court of Appeal that the essence of a composition arrangement between a debtor and his creditors is equality among the creditors; and that any departure from the course pointed out by this principle by which one creditor seeks to obtain an unconscionable advantage over the others must fail of its object because any arrangement having that as its object is unenforceable as being a fraud upon the other parties to the composition.

It was not suggested that the principle is any less a principle of law in the Province of Quebec than in places where the common law obtains. But it was argued by Mr. Lafleur that the principle has no application in the case of a mere agreement for extension. That is a view I cannot accept, for the core of the matter is that the inculpated transaction is a fraud upon persons to whom in the circumstances the creditor owes a duty of disclosing any such transaction. I cannot concede that the principle of equality or that this duty of disclosure is any less imperative where the creditors give merely an extension of time, than where they give up a proportionate part of their claims; and such being the case the sterility which affects a bargain for a secret advantage where a composition is in question is equally the consequence of a secret bargain having reference to an arrangement for giving time only.

An argument which at first gave me some concern arising out of the last paragraph of the memorandum requires notice. The paragraph is in the following words:—

(1) 15 Q.B.D. 605.

The First Party agrees that he will not during the currency of this extension and until these liabilities are paid off give any preference or security on any of his assets no matter where situate without the consent of the Second Parties.

It was contended by Mr. Lafleur that the preposition "on" connects "preference" as well as "security" with the succeeding phrase "any of his assets" and that consequently the respondent's guarantee is not within the contemplation of this clause. I do not find it necessary to express any opinion upon the point of construction. Assuming Mr. Lafleur's reading to be the right reading, I think, after reflection, that the respondents' rights are not in any way prejudiced by the presence of this clause. The clause, it should be noted, is not primarily directed to securing the observance of good faith among the persons executing the memorandum; it imposes primarily a duty upon the debtor who is a party to the agreement and the result of it is to disable him from giving any preference or security to any of his creditors including, of course, those who were parties to the extension agreement, but including also those who were not parties to it. The clause itself would no doubt, apart from any general principle of law, involve the persons executing the memorandum in an obligation not to concur with the debtor in any conduct which would be in violation of the letter or spirit of it. But the clause is not aptly framed to displace, and the duties and rights expressly created by, or arising by implication out of the clause, do not necessarily displace, the reciprocal obligations of good faith which the law imposes *ab extra* upon the creditors who are parties to the transaction *inter se;* and it would not be right to infer an intention to displace them for the reason already mentioned, namely, that primarily the clause is framed *alio intuito*, namely, to impose an obligation on

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the debtor; and extends to the claims of all creditors whether parties to the arrangement or not.

I think the appeal should be dismissed with costs.

ANGLIN J.—By executing the agreement made between the debtor Grossman and a number of his principal creditors the appellants represented to the other creditors who were parties to it that they were giving to the debtor an extension upon the terms contained in that agreement, to which the other creditors had bound themselves, and without obtaining any preference or advantage over them. The agreement contained a recital that the creditors named in it had agreed to grant the debtor an extension only on the condition that all of them should join therein. In that agreement the appellants were first represented by their agent Eisen. Eventually they executed it in their own name. But whereas the other parties who executed the agreement accepted from the debtor, without other security, his notes at three, six, nine and twelve months the appellants insisted on their claim being liquidated in monthly instalments and upon payment thereof being secured by the indorsement of the debtor's brother-in-law. When making this arrangement they impressed upon the debtor the necessity of keeping it from the knowledge of the other creditors.

I can see no distinction in principle between an agreement for extension given by his creditors to a debtor and an agreement whereby they forego proportionate parts of their claims. Equality as between themselves and a strict adherence to the terms of the common arrangement with the debtor is an essential element in both cases. On grounds of public policy a secret bargain violating that equality is unlawful

and additional security obtained under it is unenforceable: *Clark* v. *Ritchie*(1); *McKewan* v. *Sanderson*(2). No authority has been cited which upholds a security obtained in distinct violation of the express terms of an agreement made with other creditors such as we have before us. The present case is clearly distinguishable from *Langley* v. *Van Allen*(3), relied on by the appellant. That was a case of seeking to recover for the estate money given by the debtor to a creditor who had insisted on being paid off sooner than the other creditors. This is a case of resisting the enforcement of a security unlawfully taken.

This action was brought in Montreal, no doubt because the defendant resides there. But the notes sued upon were made at Toronto and are payable there. The extension agreement was also made at Toronto where the debtor resided and carried on business. It would therefore seem that the legality of the transaction whereby Rittenberg became an indorser must be tested according to the law of that province, which was duly proved at the trial. It may be observed, however, that a French decision cited by the appellants, reported in D. 69.1.92 and noted in Fuzier-Herman, Rep. Vo. "Atermoiement" No. 106, is there significantly referred to as having been "commandée par l'espèce," and not in conflict with the rule of equality.

The appellant's case, in my opinion, is wholly devoid of merit. The appeal should be dismissed with costs.

BRODEUR J.—Par un acte d'atermoîment daté du 14 avril 1913 entre le débiteur Grossman et certains

(1) 11 Gr. 499. (2) L.R. 20 Eq., 65.
(3) 32 Can. S.C.R. 174.

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de ses créanciers parmi lesquels se trouvaient les appelants il avait été convenu qu'une extension de temps serait accordée au débiteur pour payer ses différents créanciers; et l'une des clauses de ce contrat comportait que le débiteur ne pourrait pas pendant le cours de cette extension

give any preference or security on any of his assets, no matter where situate,

sans le consentement de ses créanciers.

Les appelants malgré cette convention formelle, ont obtenu de leur débiteur des billets endossés par l'intimé. La question est de savoir si cet endossement est légal et ne constitue pas une préférence contraire à l'ordre public.

Les appelants prétendent qu'en vertu de la convention le débiteur ne pouvait pas donner de préférence ou de garantie sur aucun de ses biens mais que le fait pour eux d'avoir obtenu ce consentement ne constituait pas une violation de cette convention.

Cette clause formelle qui se trouve dans l'acte ne pouvait pas permettre aux différents créanciers d'obtenir de leur débiteur des avantages spéciaux. Cette clause, suivant moi, avait pour but d'empêcher le débiteur, pendent l'existence de l'atermoiement, de donner à aucun autre créancier des privilèges ou des garanties sur ses biens. Alors on ne voulait pas que le débiteur qui aurait contracté de nouvelles dettes put donner à ses nouveaux créanciers des faveurs particulières sur les biens qui étaient le gage de ses créanciers antérieurs.

Mais cette disposition particulière du contrat pouvait-elle empêcher les créanciers qui la signaient d'obtenir à leur tour de leur débiteur des avantages particuliers?

Je dis que non.

La loi exige que tous les créanciers dans les concordats ou dans les atermoîments soient tous mis sur le même pied. Elle proscrit tout avantage consenti à l'égard d'un seul créancier. Fuzier-Herman, verbo "Atermoiement" No. 96. Il est d'ordre public, il est dans l'interêt de la bonne foi des contrats, que ces actes soient faits sans qu'aucun créancier soit plus avantagé que l'autre. C'est là un principe bien établi dans notre droit et qui a été reconnu par la jurisprudence dans la cause de *Brigham* v. *La Banque Jacques-Cartier*(1) où il a été décidé qu'un billet promissoire donné pour garantir le montant d'une préférence est absolument nul.

Les appelants ont tenté de démontrer que les règles concernant le concordat et l'atermoiement étaient différentes et ils ont cité à cette fin une cause rapportée dans Fuzier-Herman, Répertoire, vo. atermoiement, No. 106.

La décision qui est invoquée par les appelants doit être considérée comme décision d'espèce, vu que Fuzier-Herman déclare lui-même qu'il ne faudrait pas la considérer comme contraire à la doctrine qui exige que les avantages consentis à l'égard d'un créancier soient prohibés.

En supposant que la prétention des appelants serait bien fondée sous ce rapport, il ne faudrait pas s'appuyer trop fortement sur les autorités françaises, vu que les dispositions de leur code de commerce diffèrent quelque peu d'avec les dispositions de notre droit. En principe général, les concordats comme les atermoiements doivent être faits avec la meilleure foi du monde entre les différents créanciers qui les signent. Le débiteur alors ne doit pas avantager aucun de ces créanciers; mais ils doivent toujours être maintenus

(1) 30 Can. S.C.R. 429.

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sur le même pied. Il ne doit pas donner à l'un des garanties qu'il ne donnerait pas aux autres, à moins que ces derniers ne soient mis au courant de ces avantages particuliers; et alors tout acte ou endossement qui serait fait par le débiteur et qui serait de nature à détruire cette égalité qui doit exister entre tous les créanciers est suivant moi illégal, contraire à l'ordre public et doit être mis de côté.

Les cours inférieures en sont venues à cette conclusion et les jugements qu'elles ont rendus doivent être confirmés avec dépens.

Appeal dismissed with costs.

Solicitors for the appellants: *Lamothe, Gadbois & Nantel.*

Solicitor for the respondent: *R. G. deLorimier.*