SCC File Number: 40166

IN THE SUPREME COURT OF CANADA
(ON APPEAL FROM THE COURT OF APPEAL OF ONTARIO)

B E T W E E N:

JOHN AQUINO, 2304288 ONTARIO INC., MARCO CARUSO, GIUSEPPE ANASTASIO and LUCIA COCCIA-CANDERLE

Applicants
(Appellants)

and

ERNST & YOUNG INC., in its capacity as Court-Appointed Monitor of Bonfield Construction Company Limited and KSV KOFMAN INC., in its capacity as Trustee-in-Bankruptcy of 1033803 Ontario Inc. and 1087507 Ontario Limited)

Respondents
(Respondents)

and

THE ATTORNEY GENERAL FOR ONTARIO and INSOLVENCY INSTITUTE OF CANADA

Interveners

BOOK OF AUTHORITIES OF THE RESPONDENT, KSV KOFMAN INC., IN ITS CAPACITY AS TRUSTEE-IN-BANKRUPTCY OF 1033803 ONTARIO INC. AND 1087507 ONTARIO LIMITED)
(Rule 44 of the *Rules of the Supreme Court of Canada*)

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Divisional Court gave its decision, that is as much as I need to say about irrationality in the context of this case.

(6) Reasons

Finally, Mr Gordon attacked the tribunal's reasons. They were not, as I have said, well expressed, largely because question 8 on the form failed to reflect the statutory wording and so asked the wrong question, and if the factual situation was still as it was at the time when the matter before the Divisional Court I would order that the matter be remitted to a differently constituted tribunal so that clear findings could be made in relation to s 72(1)(b) and, if appropriate, in relation to s 72(2) in the light of the judgments of this court. To that extent I would have considered it appropriate to vary the order of the Divisional Court, but in the circumstances which prevail at the present time it seems to me inappropriate for any specific order to be made.

NOURSE LJ. I have had the advantage of reading in draft the judgments of Kennedy and Roch LJJ. On the true construction of s 72(1)(b) of the Mental Health Act 1983, the only point on which they differ, I prefer the view of Kennedy LJ to that taken by Roch LJ and the Divisional Court. There is nothing I can usefully add to the reasoning of Kennedy LJ on that question. On all other questions I agree with both the judgments in this court.

I too would allow the tribunal's appeal.

Appeal allowed.

27 April. The Appeal Committee of the House of Lords (Lord Jauncey of Tullitchettle, Lord Browne-Wilkinson and Lord Nolan) refused leave to appeal.

Frances Rustin Barrister.

El Ajou v Dollar Land Holdings plc and another

COURT OF APPEAL, CIVIL DIVISION
NOURSE, ROSE AND HOFFMANN LJJ
13, 14, 15 OCTOBER, 2 DECEMBER 1993

Company – Director – Company receiving improperly obtained money – Whether knowing receipt – Whether director having knowledge – Knowledge to be attributed to company – Directing mind and will of the company – Whether knowledge of agent could be imputed to company – Basis on which company liable to owner of money.

The plaintiff owned substantial funds and securities which were under the control of an investment manager in Geneva who was bribed to invest the plaintiff's money, without the plaintiff's authority, in fraudulent share selling schemes operated by three Canadians through the medium of two Dutch companies. The proceeds of the fraudulent share selling schemes were channelled through Geneva, Gibraltar, Panama and back through Geneva from where some of it was invested in a London property development project in conjunction with the first defendant ('DLH'), a property company which

was controlled by persons unconnected with the Canadians' fraud and which had required financial backers for a speculative building project which it proposed to enter into. DLH had been acquired by those persons on the advice of S, who had been introduced to them by F, a Swiss fiduciary agent who also acted for the Canadians. DLH's affairs were conducted by its controlling shareholders and S, who was managing director of a subsidiary. F was the chairman of DLH but played no active part in its management. S had approached F for assistance in obtaining finance for the development project and F had introduced S to the Canadians, who provided £270,000 as a deposit for the purchase of a site by a DLH subsidiary, DLH London. The Canadians through various companies controlled by them provided further funding of £1,030,000 to DLH to develop the project. The Canadians had also deposited money with a company controlled by F which F had misappropriated and was unable to return. To resolve matters a meeting took place at DLH's headquarters in London at which DLH agreed to guarantee F's indebtedness to the Canadians subject to a specified limit. F later resigned as a director of DLH in June 1987 for health reasons. The Canadians subsequently indicated that they wished to withdraw from the property development project and S was able to negotiate very favourable terms for the purchase by DLH of the Canadians' interest in March 1988. The plaintiff when he discovered the fraud perpetrated by the Canadians and his agent brought proceedings against DLH to recover the money received by it from the Canadians on the grounds that DLH had received the money with knowledge that it represented the proceeds of fraud or, alternatively, sought to recover the value of the Canadians' investment on the grounds that DLH had knowledge of the fraud before it bought the Canadians out. The judge dismissed the plaintiff's claim, holding that although the plaintiff was entitled in equity to trace his money to the DLH venture, he could not succeed in his claim for knowing receipt because he had failed to establish that DLH possessed the requisite degree of knowledge through either F or S that the funds received by DHL from the Canadians were the proceeds of fraud, because F had played only a minor role in the management of DLH and his knowledge could not be attributed to the company since he could not be considered the directing mind and will of the company and the information he had acquired as to the Canadians' fraud had been acquired by him in his capacity as an officer of another company and in the case of S there was no evidence that he knew that the Canadians were using money which they had obtained improperly. The plaintiff appealed, contending that F's knowledge should be treated as the knowledge of DLH on the ground that F was, in relation to DLH's receipt of the fraudulently acquired assets, its directing mind and will and/or he was its agent in the transaction.

Held – The appeal would be allowed for the following reasons—

(1) The directing mind and will of a company was not necessarily that of the person or persons who had general management and control of the company since the directing mind and will could be found in different persons in respect of different activities. It was therefore necessary to identify the person who had management and control in relation to the act or omission in point. The judge had been wrong to hold that a non-executive director such as F who was responsible for formal paperwork but not for the business and who had played no part in business decisions could not be for certain purposes the directing mind and will of the company. On the facts, the transactions to be considered were those by which DLH received assets representing the moneys

fraudulently misapplied and the crucial considerations were that F made all the arrangements for the receipt and disbursement of the £270,000 and the £1,030,000 and significantly, on 6 May 1986 signed the funding agreement whereby DLH obtained the £1,030,000 since it was those steps that caused DLH to become involved in the project and enabled it later to acquire the assets representing the moneys fraudulently misapplied. Each of those steps was taken without the authority of a resolution of the board of DLH, which showed that F had the de facto management and control of the transactions. The directing mind and will of DLH in relation to the relevant transactions was thus the mind and will of F and no one else, so that F's knowledge that the moneys were the proceeds of fraud could be attributed to DLH and therefore the claim to enforce a constructive trust on the basis of knowing receipt succeeded. That conclusion was not affected by the fact that F ceased to be a director of DLH in June 1987 or that DLH did not receive the asset representing the £1,030,000 until March 1988, since the steps that caused DLH to become involved in the project and enabled it later to acquire the asset were all taken when F and consequently DLH had the requisite knowledge. The subsequent acquisition was sufficiently connected with the original investment to be affected by the same knowledge (see p 696 *b j* to p 697 *f*, p 698 *a* to *d*, p 699 *j* to p 700 *e* and p 706 *f* to p 707 *b*, post).

(2) However, F's knowledge could not as a matter of law be imputed to DLH on the basis that he had acted as the agent of DLH in the transaction because DLH was under no duty to inquire as to the source of the offered money. Further, even if F, in his capacity both as broker and as chairman of DLH, was under a duty to inform DLH that the moneys in question were the proceeds of fraud, that duty alone was not a ground for imputing such knowledge to DLH. Moreover, as F had acquired the information about the fraud while acting for the Canadians and not in his capacity as agent for DLH, the principle that communication to an agent was deemed to be communication to the principal did not apply. Accordingly, F's knowledge could not be imputed to DLH on the ground of agency (see p 698 *f* to *j*, p 700 *f g* and p 703 *e* to p 704 *b*, post).

Decision of Millett J [1993] 3 All ER 717 reversed.

Notes

For following trust property, see 16 *Halsbury's Laws* (4th edn) paras 1460–1464 and 48 *Halsbury's Laws* (4th edn) para 941, and for cases on the subject, see 20 *Digest* (1982 reissue) 900, *6706* and 48 *Digest* (1986 reissue) 728–738, *6687–6751*.

Cases referred to in judgments

Baldwin v Casella (1872) LR 7 Exch 325.
Blackburn Lowe & Co v Vigors (1887) 12 App Cas 531, HL.
Blackley v National Mutual Life Assurance [1972] NZLR 1038, NZ CA.
Carew's Estate Act, Re (No 2) (1862) 31 Beav 39, 54 ER 1054.
Dresser v Norwood (1864) 17 CBNS 466, 144 ER 188.
Fenwick Stobart & Co Ltd, Re, Deep Sea Fishery Co's Claim [1902] 1 Ch 507.
Gladstone v King (1813) 1 M & S 35, 105 ER 13.
Hampshire Land Co, Re [1896] 2 Ch 743.
Kelly v Cooper [1992] 3 WLR 936, PC.
Lennards Carrying Co Ltd v Asiatic Petroleum Co Ltd [1915] AC 705, [1914–15] All ER Rep 280, HL.

Montagu's Settlement Trusts, Re, Duke of Manchester v National Westminster Bank Ltd (1985) [1992] 4 All ER 308, [1987] Ch 264, [1987] 2 WLR 1192.
Payne (David) & Co Ltd, Re, Young v David Payne & Co Ltd [1904] 2 Ch 608, CA.
Powles v Page (1846) 3 CB 15, 136 ER 7.
R v Andrews Weatherfoil Ltd [1972] 1 All ER 65, [1972] 1 WLR 118, CA.
Regina Fur Co Ltd v Bossom [1957] 2 Lloyd's Rep 466.
Tesco Supermarkets Ltd v Nattrass [1971] 2 All ER 127, [1972] AC 153, [1971] 2 WLR 1166, HL.
Turton v London and North Western Rly Co (1850) 15 LTOS 92.

Appeal

The plaintiff, Abdul Ghani El Ajou, appealed from the judgment of Millett J ([1993] 3 All ER 717) delivered on 12 June 1992 whereby he dismissed the action brought by the plaintiff against the defendants, Dollar Land Holdings plc (DLH) and Factotum NV (Factotum), in which the plaintiff had claimed, inter alia, (i) damages from DLH, seeking to recover the sum of £1,300,000 being the property of the plaintiff or otherwise money traceable as money of the plaintiff in a development at 22–50 Nine Elms Lane, London SW8 on the ground that DLH received it with knowledge that it represented the proceeds of fraud, or, alternatively, the value of the investment of three Canadians whose interest in the joint venture at Nine Elms was bought out by DLH, the plaintiff alleging that DLH acquired such knowledge before it bought the Canadians out, (ii) a declaration that the said advance was at all times the property of the plaintiff, and/or was at all times held by DLH and Factotum upon trust for the plaintiff absolutely, (iii) a declaration that DLH had received the amount of the advance as a constructive trustee for the plaintiff absolutely and was liable to account to the plaintiff as such trustee, (iv) an order that there an account of all money paid or payable to or received or receivable by DLH (including any profits) in respect of the aforesaid development of the site be taken, (v) an order for the payment of the amount of the advance and all profits earned by DLH by the utilisation thereof and (vi) a declaration that the plaintiff was entitled to payment of all money found due on the taking of the accounts. The facts are set out in the judgment of Nourse LJ.

Michael Beloff QC, Roger Ellis and *Sarah Moore* (instructed by *Bower Cotton & Bower*) for the appellant.
Romie Tager (instructed by *Kaufman Kramer Shebson*) for the respondents.

Cur adv vult

2 December 1993. The following judgments were delivered.

NOURSE LJ.

Introduction

Of the questions that remain in dispute in this case, the most important is whether, for the purposes of establishing a company's liability under the knowing receipt head of constructive trust, the knowledge of one of its directors can be treated as having been the knowledge of the company. That is essentially a question of company law. There are or have been other questions on tracing and constructive trust.

The company is the first defendant, Dollar Land Holdings plc ('DLH'). The director is Mr Sylvain Ferdman, who was the chairman and one of the three directors of DLH between June 1985 and June 1987. The party who seeks to recover against DLH in constructive trust is the plaintiff, Abdul Ghani El Ajou. He has put his claim at £1·3m. On 12 June 1992, after a trial extending over some 11 days, Millett J delivered a reserved judgment dismissing the plaintiff's action (see [1993] 2 All ER 717). He held that the plaintiff had an equitable right to trace the money into the hands of DLH, but that Mr Ferdman's knowledge of their fraudulent misapplication could not be treated as having been the knowledge of DLH, either on the ground of his having been its directing mind and will or on the ground of his having been its agent in the transaction. The judge found that another person closely concerned with the affairs of DLH, Mr William Stern, did not have the requisite knowledge of the misapplication. The plaintiff now appeals to this court. He does not seek to upset the judge's finding in regard to Mr Stern. DLH has put in a respondent's notice whose primary purpose is to impugn the judge's finding as to one part of the tracing exercise.

Because the report sets out in full the judge's clear and necessarily lengthy statement of the facts and because the issues have narrowed in this court, the facts can now be stated relatively briefly. I will state them mainly in the judge's own words.

The facts

The plaintiff is a wealthy Arab businessman resident in Riyadh. He was the largest single victim, though only one of many victims, of a massive share fraud carried out in Amsterdam between 1984 and 1985 by three Canadians, Allan Lindzon (or Levinson), Lloyd Caplan and Harry Roth ('the Canadians'). Some of the proceeds of the fraud were passed from Amsterdam through intermediate resting places in Geneva, Gibraltar, Panama and Geneva (again) to London, where in 1986 they were invested in a joint venture to carry out a property development project at Nine Elms in Battersea in conjunction with DLH. The interest of the Canadians in the joint venture was bought out in 1988 by DLH, which is a public limited company incorporated in England but resident for tax purposes in Switzerland. It is a holding company. Its principal activities, carried on through its subsidiaries, are property dealing and investment. At the material time it was in a substantial way of business. It denies that in 1986 it had any knowledge that the money which the Canadians invested in the project represented the proceeds of fraud. Moreover, in buying out their interest in 1988 it claims to have been a bona fide purchaser for value without notice of the fraud.

Mr Ferdman is a Swiss national, resident in Geneva. He worked for many years for the Bank of International Credit in Geneva. In 1972 he left the bank and set up his own company, Société d'Administration et de Financement SA (SAFI), through which he acted as a fiduciary agent. SAFI was originally owned jointly by Mr Ferdman and an old-established Swiss cantonal bank of good reputation, but in 1982 Mr Ferdman became its sole proprietor. SAFI acted as a fiduciary agent for clients who did not wish their identities to be disclosed. Two of its clients were a Mr Singer and a Mr Goldhar, who were associates of the Canadians. Mr Ferdman was accustomed to accept funds from clients without questioning their origin, and to act for clients who were

anxious to conceal their identity. He regarded the need to preserve his clients' anonymity as paramount—without it he would have had no business—and to this end he was willing on occasion to present himself or SAFI as a beneficial owner and to make false statements to that effect. The judge found that it must have been plain to Mr Ferdman by the end of October 1985 that Singer and Goldhar were implicated in a fraud. Moreover, Mr Ferdman admitted to the judge at the trial that he knew perfectly well that the Canadians were involved with Singer and Goldhar in the fraud and were not just behind them. The Canadians also had a fiduciary agent resident in Geneva who acted for them. He was Mr David D'Albis, an American citizen.

DLH is an English company which was formerly listed on the London Stock Exchange. In June 1985 its entire issued share capital was acquired by Keristal Investments and Trading SA (Keristal), a Panamanian company beneficially owned by a Liechtenstein foundation. In the annual reports of DLH Mr Ferdman described himself as the beneficial owner of Keristal, but that was not the case. He was simply preserving the anonymity of his principals, the founders and beneficiaries of the Liechtenstein foundation, who were two US citizens resident in New York ('the Americans'). The judge recorded that the plaintiff was satisfied that the Americans had no connection of any kind with the Canadians or their associates or any of the other persons involved in the fraud.

DLH was acquired as a vehicle for the Americans' property dealings in the United Kingdom. Its business activities were under the direction of Mr William Stern, described by the judge as a property dealer who suffered a spectacular and well-publicised bankruptcy as a result of the 1974 property crash. He was engaged in the business of identifying opportunities for property investment and introducing them to investors willing to pay him a fee or a share in the eventual profits. Mr Stern had lived in Geneva as a boy and was acquainted with Mr Ferdman. They became friends, though they lost contact with each other for some years. Mr Stern knew that he was a fiduciary agent and had established SAFI, which he believed still to be jointly owned by Mr Ferdman and a reputable cantonal bank. From time to time he suggested deals to Mr Ferdman and inquired of him whether he had any suitable investors among his clients.

Mr Ferdman introduced the Americans to Mr Stern, who was able to recommend a successful investment in a United Kingdom property. The Americans were willing to make further investments in the United Kingdom, and Mr Stern suggested that he should look for a suitable English vehicle, if possible a quoted company, which they could acquire and use as a medium for further investment. Mr Stern found DLH and Keristal acquired it as a pure cash shell in June 1985. Mr Ferdman and Mr Favre and Mr Jaton, two fellow directors of SAFI, were appointed to be the directors of DLH and Mr Ferdman its chairman. The judge described the three of them as nominee directors representing the interests of the beneficial owners. They played no part in the conduct of DLH's business which was carried on by Mr Stern in consultation with the Americans. Mr Stern was not a director of DLH, but he was appointed managing director of Dollar Land Management Ltd, one of its subsidiaries. DLH was in a substantial way of business and was able to raise very large sums on the security of its assets. At the end of 1986 it had secured bank loans and

other mortgage creditors of more than £10m. By the end of 1987 that figure had risen to more than £30m.

Mr Stern asked Mr Ferdman if he could find an investor willing to put up equity finance for the Nine Elms project. Mr Ferdman, who was to receive from DLH an introductory commission of 5% of the funds obtained, brought one of the Canadians, Roth, to London in March 1986 and introduced him to Mr Stern, who provided him with a detailed investment proposal which included a profit forecast. All negotiations were conducted between Roth and Mr Stern. Mr Ferdman played no part. By a letter dated 20 March 1986 and addressed to Roth, care of SAFI in Geneva, the terms which had been agreed between him and Mr Stern were set out. Although that letter was signed by Mr Ferdman, it was composed entirely by Mr Stern. I will return to it later in this judgment.

On 25 March Mr Ferdman copied the letter of 20 March (with two variations which the judge inferred were made at the request of the Canadians) by telex to Mr D'Albis, who gave instructions on the same day for £270,000 to be transferred from Geneva to the Royal Bank of Scotland in London for the account of DLH's solicitors, Grangewoods. The judge found that that sum represented proceeds of the fraud and that finding has not been questioned in this court. Subsequently, Mr Ferdman despatched a duplicate of the telex in the form of a letter on DLH's headed paper, and over his own signature, to Yulara Realty Ltd (Yulara) in Panama. That letter was dated 7 April. Again, I will return to it later. Yulara was a Panamanian company owned by the Canadians, which Mr Ferdman knew was a vehicle for their investment in the Nine Elms project. Mr Ferdman retained on his own files a copy of the letter countersigned by a Panamanian lawyer on behalf of Yulara by way of acceptance.

Contracts for the purchase of the Nine Elms site were exchanged on 26 March. The purchaser was a subsidiary of DLH, Dollar Land (London) Ltd ('DLH London'). The £270,000 which Grangewoods had received on the previous day was used to pay the deposit. On 11 June 1986 DHL London assigned the benefit of the contract to DLH for £100,000 and on the same day DLH entered into a contract for the sale of the site to Regalian Properties (Northern) Ltd ('Regalian'). Completion took place on the same day at a price of £2·7m, £1m of which was recorded as being paid by DLH.

The further funding of the project was complex. Reduced to its essentials, the method adopted was as follows. On 6 May 1986 Keristal (expressed to be represented by Mr Ferdman) and Yulara (expressed to be represented by the Panamanian lawyer) entered into a written loan agreement which was signed by them on behalf of Keristal and Yulara respectively. The agreement recited that Keristal was the holding company of DLH and that Yulara and DLH had entered into an agreement as per the letter dated 7 April. Article 1 was in substance a further recital to the effect that Yulara was making available or had given to Keristal (it is not clear which) the amount of up to $US2·5m for as long as the agreement as per the letter of 7 April would be in force. By art 2 Keristal accepted that amount on terms that it undertook to use the funds (a) 'in order to make a joint venture in a certain real estate investment in London' in accordance with the terms contained in the letter dated 7 April and (b) 'in order to [obtain] a bank guarantee of £1,300,000 to be issued in favour of [DLH London] or another company owned by [DLH]'.

On 12 and 16 May respectively two sums of $US1,541,432 and $US1,143,000, making a total of $US2,684,432, were credited to an account of Keristal (the Keristal No 2 account) at Banque Scandinave in Geneva. The account was operated by SAFI and was used exclusively for the purpose of funding the Nine Elms project. The bank statement for the account shows that the first sum came from the Bank of America; the source of the second is not shown. The judge found that both sums were traceable to Panama as proceeds of the fraud. That is the finding which the respondent's notice seeks to impugn. I will return to it shortly.

Pursuant to arrangements made by Mr Ferdman, Scandinavian Bank Group plc in London then agreed to advance £1·3m to Factotum NV ('Factotum'), a shelf company previously incorporated by Mr Ferdman in the Netherland Antilles, which he decided to make use of as a convenient vehicle for channelling the money to DLH. (Factotum is the second defendant in the action, but it has no assets and has never been served.) The advance was supported by a guarantee given by Banque Scandinave secured on the moneys in the Keristal No 2 account. The whole of the loan from Scandinavian Bank in London to Factotum was drawn down and £1,030,000 was paid into Grangewoods' client account on 29 May. Of those moneys £745,598·60 were used to discharge the amount due from DLH on completion of the purchase of the site on 11 June. The balance was used to discharge obligations of DLH and to make various other payments at the direction of DLH, including payment to Mr Ferdman of his introductory commission of £65,000.

It is clear from the foregoing that the £1,030,000 paid to Grangewoods represented moneys that had been credited to the Keristal No 2 account. It is also clear that the moneys so credited belonged to the Canadians. What is in dispute is the judge's finding that they represented moneys which Mr D'Albis had sent to Panama from Gibraltar on 30 March and 1 April 1986, a fact that had to be established in order that they could be treated as proceeds of the fraud. It is convenient to deal with that question now.

Tracing through Panama

The question was dealt with by Millett J (see [1993] 3 All ER 717 at 734–736). He said that the plaintiff was unable, by direct evidence, to identify the moneys in the Keristal No 2 account with the money which Mr D'Albis had sent to Panama only a few weeks before. However, he thought that there was sufficient funds, though only just, to enable him to draw the necessary inference. He continued (at 734–735):

> 'One of the two sums received in the Keristal No 2 account was $1,541,432 received on 12 May 1986 from Bank of America. That corresponds closely with the sum of $1,600,000 transferred to Bank of America, Panama on 1 April 1986. In relation to the later transaction, Bank of America may, of course, merely have been acting as a correspondent bank in New York and not as the paying bank; and the closeness of the figures could be a coincidence. It is not much, but it is something; and there is nothing in the opposite scale. The source of the other money received in the Keristal No 2 account is not known, but from the way in which the Canadians appear to have dealt with their affairs, if one sum came from Panama, then the other probably did so, too.'

After considering other points on each side, the judge said that the fact remained that there was no evidence that the Canadians had any substantial funds available to them which did not represent proceeds of the fraud (see at 735). He concluded (at 736):

> 'In my judgment, there is some evidence to support an inference that the money which reached the Keristal No 2 account represented part of the moneys which had been transmitted to Panama by the second tier Panamanian companies some six weeks previously, and the suggestion that it was derived from any other source is pure speculation.'

Mr Tager, for DLH, submitted that neither of the routes followed by the judge led to the conclusion that he reached. He took us carefully through the bank statement for the Keristal No 2 account. He relied on the fact that there were two separate credits to it of very precise amounts, the second having been made four working days after the first. It had been impossible to identify the source of the second credit. All this suggested that the two credits had come from different sources. There was no necessary connection between the first and the sum of $US1·6m that had been sent from Gibraltar to the Bank of America in Panama on 1 April. Mr Tager argued that there were other very substantial funds available to the Canadians. He disputed the judge's view that there was no evidence that they had any substantial funds available to them that did not represent proceeds of the fraud. He submitted that the plaintiff had not discharged the evidential burden of establishing the necessary link.

Having carefully considered these and other arguments of Mr Tager, I remain unconvinced that the judge drew the wrong inference. I well appreciate both that the question is of critical importance to the plaintiff's case and that, since it depends almost entirely, if not exclusively, on documentary evidence and undisputed events, we in this court are, in theory at any rate, in as good a position to draw an inference as the judge himself. In practice, however, the judge, after an 11-day trial, was in a much better position than we are. From all that I have seen and heard of the case, I would feel no confidence at all in saying that the judge had drawn the wrong inference.

The assets received by DLH

On the footing that the moneys credited to the Keristal No 2 account were proceeds of the fraud, it becomes necessary to identify the assets received by DLH and the dates when it received them. The plaintiff's position is a simple one. He says that DLH received £270,000 on 25 March 1986 and a further £1,030,000 in June 1986 (though logically he ought to say on 29 May 1986, when the latter sum was paid into Grangewoods' client account; see further below). The judge considered these questions. He thought that the position was somewhat more complicated than the plaintiff would have had it.

As to the £270,000, the judge said (at 738):

> 'The sum of £270,000 was never received by DLH. It was paid into Grangewoods' client account, and their client at the time must be taken to have been DLH London. DLH London was not a nominee or agent for DLH. As had previously been agreed between Roth and Mr Stern, it was the intended contractual purchaser of the site, and the money was to be used exclusively for the payment of the deposit on exchange of contracts. In my judgment, DLH did not receive the money at all, and DHL London

did not receive it beneficially but upon trust to apply it for a specific purpose. DLH London used the money, as it was bound to do, to pay the deposit on the site, and thereby acquired for its own benefit a corresponding interest in the site which it subsequently sold and transferred to DLH. The plaintiff can follow his money through these various transactions, but the relevant asset capable of being identified as having been received by DLH is an interest in the site corresponding to the payment of the deposit.'

This question depends on the true construction and effect of the letter of 20 March 1986. Both Mr Beloff QC, for the plaintiff, and Mr Tager for DLH referred to its terms at some length in order to determine whether DLH London had acted as principal or as agent for DLH. Although he was not greatly concerned either way, Mr Beloff submitted that DLH London had acted as agent and that the £270,000 was accordingly received by DLH on 25 March. But in my view the judge was right, as a matter of construction, to conclude that DLH London, and not DLH itself, was the principal, so that it was that company that was Grangewoods' client when the money was received. I therefore agree with the judge that DLH did not receive anything on 25 March, but that on the assignment of the benefit of the contract to it on 11 June it received an interest in the site corresponding to the payment of the deposit.

As to the balance of £1,030,000, the judge said (at 738):

'The sum of £1,030,000 was also paid into Grangewoods' client account, but by then their client had become DLH. The money was disbursed on the instructions and for the benefit of DLH. Only £745,598·60 was used to pay the money due to the vendor on completion, but this was the result of the arrangements which DLH had made with Regalian. So far as Yulara is concerned, the whole £1·3m must be taken to have been disbursed as agreed between them on the acquisition of a 40% interest in the project. Moreover, in my judgment, on a proper analysis of the transaction between Yulara and DLH, Yulara's money should be treated as having been invested in its share of the project, and not in or towards the acquisition of DLH's share. The investment proved highly successful. In itself it was not a breach of trust and caused the plaintiff no loss. Had he been able to intervene before the Canadians were bought out, he could have claimed the whole of Yulara's interest in the project; but whatever the extent of DLH's knowledge of the source of Yulara's funds, his claim would have been confined to Yulara's interest in exoneration of that of DLH. In the events which have happened, the plaintiff is in my judgment bound to treat his money as represented by Yulara's interest in the project, and must rely exclusively on the transaction on 16 March 1988 when Yulara's interest was bought out by DLH.'

For a reason which will become clear when I deal with the question whether Mr Ferdman was the directing mind and will of DLH, Mr Beloff expressed greater concern at the judge's decision of this question. However, subject to one point, I feel unable to differ from his reasoning on it.

I am puzzled by the judge's suggestion that by the time the £1,030,000 was paid into Grangewoods' client account their client had become DLH. He had found that that payment was made on 29 May, before the assignment of the

benefit of the contract by DLH London to DLH on 11 June (see at 730). However, this point (which was not addressed in argument), though it may be of importance in relation to the date at which DLH must be treated as having had knowledge of the fraud (see below), does not affect the judge's view of the asset received by DLH in respect of the £1,030,000 and the date when it received it.

Knowledge

It having been established that DLH received assets representing proceeds of the fraud, I come to the question of knowledge. By the end of the hearing there could have been no doubt that Mr Ferdman himself had the requisite knowledge. The judge said of him (at 740):

> 'He freely admitted that he knew that the persons who were providing the money for the Nine Elms project were the persons who had been behind the fraud in Amsterdam; and that by 7 April 1986, when he signed the letter to Yulara, he knew (or assumed) that the money which he would be receiving into the Keristal No 2 account was part of the proceeds of the fraud.'

Thus arises the most important question remaining in dispute, which is whether Mr Ferdman's knowledge can be treated as having been the knowledge of DLH. The plaintiff contends that it can and ought to be, first, on the ground that Mr Ferdman was, in relation to DLH's receipt of the assets representing the moneys fraudulently misapplied, its directing mind and will; secondly and alternatively, on the ground that he was its agent in the transaction. Because a company's directing mind and will are often the mind and will of one or more of its directors and because a director is for many purposes an agent of the company, there is a danger of confusion between the two grounds on which the plaintiff relies. But they are, as the judge made clear, quite separate. The plaintiff can succeed on either. The convenient course is to deal with the law and the facts in regard to each of them in turn.

Directing mind and will

This doctrine, sometimes known as the alter ego doctrine, has been developed, with no divergence of approach, in both criminal and civil jurisdictions, the authorities in each being cited indifferently in the other. A company having no mind or will of its own, the need for it arises because the criminal law often requires mens rea as a constituent of the crime, and the civil law intention or knowledge as an ingredient of the cause of action or defence. In the oft-quoted words of Viscount Haldane LC in *Lennards Carrying Co Ltd v Asiatic Petroleum Co Ltd* [1915] AC 705 at 713, [1914–15] All ER Rep 280 at 283:

> 'My Lords, a corporation is an abstraction. It has no mind of its own any more than it has a body of its own; its active and directing will must consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the directing mind and will of the corporation, the very ego and centre of the personality of the corporation.'

The doctrine attributes to the company the mind and will of the natural person or persons who manage and control its actions. At that point, in the words of Millett J ([1993] 3 All ER 717 at 740): 'Their minds are its mind; their

intention its intention; their knowledge its knowledge.' It is important to emphasise that management and control is not something to be considered generally or in the round. It is necessary to identify the natural person or persons having management and control in relation to the act or omission in point. This was well put by Eveleigh J in delivering the judgment of the Criminal Division of this court in *R v Andrews Weatherfoil Ltd* [1972] 1 All ER 65 at 70, [1972] 1 WLR 118 at 124:

> 'It is necessary to establish whether the natural person or persons in question have the status and authority which in law makes their acts in the matter under consideration the acts of the company so that the natural person is to be treated as the company itself.'

Decided cases show that, in regard to the requisite status and authority, the formal position, as regulated by the company's articles of association, service contracts and so forth, though highly relevant, may not be decisive. Here Millett J adopted a pragmatic approach. In my view he was right to do so, although it has led me, with diffidence, to a conclusion different from his own.

DLH contends that its directing mind and will in relation to its receipt of the assets representing the moneys fraudulently misapplied were either the mind and will of Mr Stern alone or of Mr Stern and the Americans together. They were not the mind and will of Mr Ferdman. The judge's acceptance of this contention is expressed (at 741):

> 'In 1986 [DHL's] directors were all officers of SAFI, but they were merely nominee directors representing the interests of the Americans. Mr Ferdman was a non-executive director. His only executive responsibilities were to act as a fiduciary agent, represent the interests of the Americans, and ensure that the necessary corporate documentation was in order. The witnesses agreed that, in the early days of DLH, Mr Ferdman played a bigger role than he did [later]; but I do not think that that was due to any change in his role. He was always responsible for the formal paperwork, but not for the business. As the business expanded, so his relative importance diminished. Even in 1986, he played no part in business decisions. These were taken by Mr Stern in consultation with the Americans. In my judgment, Mr Ferdman's position as chairman and non-executive director of DLH was insufficient by itself to constitute his knowledge ipso facto the knowledge of DLH. It has not been alleged, still less established, that the other two officers of SAFI, who with Mr Ferdman constituted the board of DLH in 1986, shared Mr Ferdman's knowledge of the source of the Canadians' money, but in my judgment it would make no difference if they did. Like Mr Ferdman, they were merely nominee directors with non-executive responsibility. They had no authority to take business decisions. In relation to its business affairs in 1986, neither Mr Ferdman alone nor the board as a whole can realistically be regarded as the directing mind and will of DLH.'

In disagreeing with the judge on this question, I start from the position that the transactions to be considered are those by which DLH received assets representing the moneys fraudulently misapplied. The responsibility for the management and control of those transactions is not to be determined by identifying those who were responsible for deciding that DLH would

participate in the Nine Elms project and the nature and extent of that participation, far less by identifying those who were responsible for business decisions generally. Neither Mr Stern nor the Americans made any of the arrangements for the receipt or disbursement of the moneys by Grangewoods. Nor did they commit DLH to the obligations correlative to their receipt. None of them had the authority to do so. That was the responsibility of Mr Ferdman. The crucial considerations are that Mr Ferdman made all the arrangements for the receipt and disbursement of the £270,000 and the £1,030,000; that it was he who signed the letter of 20 March to Roth; that it was he who, on 25 March, copied that letter to Mr D'Albis; that it was he who signed and dispatched the letter of 7 April to Yulara; that it was he who, on 6 May, signed the agreement with Yulara; and that it was those steps that caused DLH to become involved in the project and enabled it later to acquire the assets representing the moneys fraudulently misapplied.

Each of the steps taken by Mr Ferdman was taken without the authority of a resolution of the board of DLH. That demonstrates that as between Mr Ferdman on the one hand and Mr Favre and Mr Jaton on the other it was Mr Ferdman who had the de facto management and control of the transactions. It may be that that state of affairs involved some breach of the directors' duties to DLH. But that would not enable DLH to say that Mr Favre and Mr Jaton were parties to its directing mind and will in any relevant respect. Mr Tager sought to show that they did perform duties as directors of DLH. No doubt they did. But there is no real evidence that they had any responsibility for the transactions in question. In my view the directing mind and will of DLH in relation to the relevant transactions between March and June 1986 were the mind and will of Mr Ferdman and none other. That means that DLH had the requisite knowledge at that time.

Next, I must consider whether the plaintiff's right to recover is affected by Mr Ferdman's having ceased to be a director of DLH in June 1987. This question is of significance only in relation to the £1,030,000. It has no bearing on the £270,000. Millett J, having repeated his view that, in regard to the £1,030,000, the relevant transaction was the acquisition by DLH of Yulara's interest in the joint venture on 16 March 1988, continued (at 743):

> 'By then Mr Ferdman had ceased to be a director of DLH for nine months, and he had nothing at all to do with the transaction. Even if, contrary to my judgment, Mr Ferdman's knowledge should be attributed to DLH in 1986, it would be quite wrong to treat DLH as still possessing that knowledge in 1988. As Megarry V-C pointed out in *Re Montagu's Settlement Trusts* [1992] 4 All ER 308 at 329, [1987] Ch 264 at 284, a natural person should not be said to have knowledge of a fact that he once knew if at the time in question he has genuinely forgotten all about it. In my judgment, where the knowledge of a director is attributed to a company, but is not actually imparted to it, the company should not be treated as continuing to possess that knowledge after the director in question has died or left its service. In such circumstances, the company can properly be said to have "lost its memory".'

While I might agree with the judge that the knowledge of a director, who had known of a misapplication of trust moneys at the time of their misapplication but had genuinely forgotten all about it by the time that they

were received by the company, could not be attributed to the company, I am unable to see how that can assist DLH here. The steps that caused DLH to become involved in the project and enabled it later to acquire the asset representing the £1,030,000 were all taken between March and June 1986. Moreover, although the judge held that the plaintiff was bound to treat the £1,030,000 as represented by Yulara's interest in the project, he found that that sum had been paid into Grangewoods' client account on 29 May 1986 and had thereafter been wholly disbursed as directed by DLH, £745,000 approximately in satisfaction of the purchase price (see at 730). In the circumstances, DLH having had the requisite knowledge at the time that it became involved in the project and when the £1,030,000 was disbursed as it directed, it would in my view be unrealistic to hold that it ceased to have that knowledge simply because the mind and will that had been the source of it played no part in the receipt of the asset itself. I am therefore of the opinion that DLH is on this ground liable to the plaintiff in constructive trust.

Agency

Although the views so far expressed are enough to dispose of the appeal in favour of the plaintiff, I turn briefly to the alternative question whether Mr Ferdman's knowledge ought to be imputed to DLH, on the ground that he acted as DLH's agent in the transaction.

Millett J thought that it was not accurate to describe Mr Ferdman as having acted as the agent of DLH in obtaining money from the Canadians. I am not sure that I would agree with him on that question. The real question is whether Mr Ferdman acted as the agent of DLH in the transactions by which it received assets representing the moneys fraudulently misapplied. I find it unnecessary to answer either question. That is because I agree with the judge that, even if Mr Ferdman was DLH's agent, his knowledge could not, as a matter of law, be imputed to it.

It is established on the authorities that the knowledge of a person who acquires it as a director of one company will not be imputed to another company of which he is also a director, unless he owes, not only a duty to the second company to receive it, but also a duty to the first to communicate it: see *Re Hampshire Land Co* [1896] 2 Ch 743 and *Re Fenwick Stobart & Co Ltd, Deep Sea Fishery Co's Claim* [1902] 1 Ch 507.

Mr Ferdman acquired his knowledge of the fraudulent misapplication as a director of SAFI. I do not doubt that he owed a duty to DLH to receive it. But I agree with the judge that he owed no duty to SAFI to communicate it. I also agree with him that the facts of this case are indistinguishable in any material respect from those in *Re David Payne & Co Ltd, Young v David Payne & Co Ltd* [1904] 2 Ch 608.

Conclusion

I would allow the appeal. On that footing, it becomes necessary to consider the relief to which the plaintiff is entitled, a consideration so far made unnecessary by the judge's dismissal of the action. Although it would be possible for this court to deal with that question itself, I think it preferable to remit it for consideration by the judge.

ROSE LJ. I gratefully adopt the recital of facts in the judgment of Nourse LJ. For the reasons which he gives, I agree that the appellant's submissions with regard to the payment of the deposit and the balance of the money fail. Millett J's conclusions, namely that the deposit was paid to Dollar Land Holdings London beneficially and that the balance was received by Dollar Land Holdings plc ('DLH') on trust to invest on behalf of Yulara Realty Ltd ('Yulara') pursuant to a joint venture agreement, were, on the evidence before him, correct. Equally, the judge's finding, which DLH seek to challenge, that the money can be traced to the proceeds of fraud by the Canadians, is, in my view, unimpeachable.

The submissions with regard to the role of Ferdman and whether his knowledge of the fraudulent origin of the invested funds should be attributed to DLH raise considerations of more general importance. In English law the concept of a company's directing mind and will has its origins in the speech of Viscount Haldane LC in *Lennards Carrying Co Ltd v Asiatic Petroleum Co Ltd* [1915] AC 705 at 713, [1914–15] All ER Rep 280 at 283. In *Tesco Supermarkets Ltd v Nattrass* [1971] 2 All ER 127 at 155, [1972] AC 153 at 200 Lord Diplock identified those who are to be treated in law as being the company as—

> 'those natural persons who by the memorandum and articles of association or as a result of action taken by the directors, or by the company in general meeting pursuant to the articles are entrusted with the exercise of the powers of the company.'

Lord Reid said ([1971] 2 All ER 127 at 132, [1972] AC 153 at 171):

> 'Normally the board of directors, the managing director and perhaps other superior officers of a company carry out the functions of management and speak and act as the company ... But the board of directors may delegate some part of their functions of management giving to their delegate full discretion to act independently of instructions from them.'

Lord Pearson said ([1971] 2 All ER 127 at 148, [1972] AC 153 at 190):

> 'There are some officers of a company who may for some purposes be identified with it, as being or having its directing mind and will, its centre and ego, and its brains ... The reference in s 20 of the Trades Descriptions Act 1968 to "any director, manager, secretary or other similar officer of the body corporate" affords a useful indication of the grades of officers who may for some purposes be identifiable with the company ...'

There are, it seems to me, two points implicit, if not explicit, in each of these passages. First, the directors of a company are, prima facie, likely to be regarded as its directing mind and will whereas particular circumstances may confer that status on non-directors. Secondly, a company's directing mind and will may be found in different persons for different activities of the company.

It follows that Millett J's unchallenged conclusion that Stern, although neither a director nor an employee, was the 'moving force' behind the company's activities does not preclude a finding that Ferdman was the company's directing mind and will in relation to some activities.

In the present case, the company's activity to which Ferdman's knowledge was potentially pertinent was the receipt of over £1m for investment.

Ferdman had been appointed by the Americans for two reasons in particular: first, as a Swiss resident operating the formal aspects of the company he was able to confer the tax advantages of non-resident status on DLH on the basis that its 'central management and control' was in Switzerland not England; and secondly because the Americans did not want Stern to be seen to have any official role in the company. Ferdman was a director and chairman of the board and his services were charged for at a higher rate than that for other directors. He instructed accountants and solicitors. He convened meetings. He claimed in the company's accounts to be its ultimate beneficiary. He was a necessary signatory of legal documents and signed the Yulara agreement without needing the authority of a board resolution to do so: by so doing he committed the company to that agreement.

Having regard to these matters, it seems to me to be plain that, for the limited purposes here relevant ie the receipt of money and the execution of the Yulara agreement, he was the directing mind and will of the company. In consequence, his knowledge of the fraud was DLH's knowledge and, in this respect, I differ from Millet J. It is immaterial that by March 1988, when DLH acquired Yulara's interest, Ferdman had ceased to be a director. That cessation did not deprive DLH of its continuing knowledge in relation to the transaction, which embraced both the initial receipt of the money in May 1986 and the ultimate acquisition of Yulara's interest.

If the appellant does not succeed on this point, Mr Beloff's alternative submission based on agency is, in my view, doomed to fail. This court is, in my judgment, bound to hold, on the authority of *Re David Payne & Co Ltd, Young v David Payne & Co Ltd* [1904] 2 Ch 608 that, qua agent, Ferdman was under no obligation to disclose his knowledge to DLH, there being no duty on DLH to inquire as to the source of the offered money. I agree with Hoffmann LJ's analysis of the three categories of agency cases to which he refers and with his conclusion that they have no application in the present circumstances.

To the extent indicated I would allow this appeal.

HOFFMANN LJ. This is a claim to enforce a constructive trust on the basis of knowing receipt. For this purpose the plaintiff must show, first, a disposal of his assets in breach of fiduciary duty; secondly, the beneficial receipt by the defendant of assets which are traceable as representing the assets of the plaintiff; and thirdly, knowledge on the part of the defendant that the assets he received are traceable to a breach of fiduciary duty.

There is no dispute that the first requirement is satisfied. The Canadians bribed the plaintiff's fiduciary agent to give them over $US10m of his money in return for worthless shares. The argument in this appeal has been over, first, which assets were received beneficially by Dollar Land Holdings plc ('DLH'); secondly, whether they are traceable as representing the plaintiff's money; and thirdly, whether the admitted knowledge of the frauds on the part of Mr Ferdman, chairman of DLH, can be imputed to the company.

1. IDENTIFYING THE ASSETS BENEFICIALLY RECEIVED

The judge has found as a fact that certain assets received by DLH, namely the benefit of the deposit paid under the contract for the purchase of the Nine Elms site and Yulara Realty Ltd's ('Yulara') interest in the development, were traceable in equity as proceeds of fraud. Both sides have challenged certain aspects of this finding.

(*a*) The deposit

The plaintiff says that the asset received by DLH was not the benefit of the deposit but the money used to pay it. This had been sent on 25 March 1986 to DLH's subsidiary Dollar Land (London) Ltd ('DLH London'), which entered into the contract to buy the site and afterwards assigned that contract (with the benefit of the deposit) to DLH. The plaintiff says that DLH London received the money as agent for DLH. The only evidence for this claim is that it was paid pursuant to an agreement between Roth and DLH. But that in my judgment is no reason why DLH London should not have received the money beneficially and this would be consistent with its having been the contracting party and subsequently assigning that contract for a substantial consideration to DLH.

(*b*) The main investment

The plaintiff says that the other asset received by DLH was not Yulara's interest in the project, which it acquired on 16 March 1988, but the £1,030,000 invested by Yulara on 29 May 1986. In my judgment the judge was right in holding that money was not received by DLH beneficially but on trust to invest on behalf of Yulara. DLH and Yulara were joint venturers. Yulara was making an equity investment by which it acquired a proprietary interest in half the share of profits due to DLH under its arrangements with Regalian Properties (Northern) Ltd (Regalian) and the benefit of a guarantee by DLH that its capital would be repaid. DLH received no part of this investment beneficially until it bought out Yulara's interest.

2. TRACING

DLH challenges the judge's finding that the money can be traced to the proceeds of fraud which the Canadians had remitted to Panama. In my view, this was a finding which the judge was entitled to make. Mr Tager says that it might have been the proceeds of frauds on other people or even the money realised by the Canadians when they sold the business. It might have been, but as against the plaintiff I do not think that the Canadians would have been entitled to say so. Nor is DLH. The mixed fund was impressed with an equitable charge in favour of the plaintiff which was enforceable against the Canadians and persons claiming under them.

3. KNOWLEDGE

The judge correctly analysed the various capacities in which Mr Ferdman was involved in the transaction between DLH and the Canadians. First, he acted as a broker, introducing the Canadians to DLH in return for a 5% commission. In this capacity he was not acting as agent for DLH but as an independent contractor performing a service for a fee. Secondly, he was authorised agent of DLH to sign the agreement with Yulara. Thirdly, he was at all material times a director and chairman of the board of DLH.

There are two ways in which Mr Ferdman's knowledge can be attributed to DLH. The first is that as agent of DLH his knowledge can be imputed to the company. The second is that for this purpose he *was* DLH and his knowledge was its knowledge. The judge rejected both.

(*a*) The agency theory

The circumstances in which the knowledge of an agent is imputed to the principal can vary a great deal and care is needed in analysing the cases. They fall into a number of categories which are not always sufficiently clearly distinguished. I shall mention three such categories because they each include cases on which Mr Beloff QC placed undifferentiated reliance. In fact, however, they depend upon distinct principles which have no application in this case.

(i) Agent's knowledge affecting performance or terms of authorised contract

First, there are cases in which an agent is authorised to enter into a transaction in which his own knowledge is material. So, for example, an insurance policy may be avoided on account of the broker's failure to disclose material facts within his knowledge, even though he did not obtain that knowledge in his capacity as agent for the insured. As Lord Macnaghten said in *Blackburn Lowe & Co v Vigors* (1887) 12 App Cas 531 at 542–543:

> 'But that is not because the knowledge of the agent is to be imputed to the principal but because the agent of the assured is bound as the principal is bound to communicate to the underwriters all material facts within his knowledge.'

In this category fall two of the cases upon which Mr Beloff relied, namely *Turton v London and North Western Rly Co* (1850) 15 LTOS 92 and *Dresser v Norwood* (1864) 17 CBNS 466, 144 ER 188. In the former case the agent was authorised to conclude a contract of carriage on behalf of the principal. The agent's knowledge of the carrier's standard terms of business was held sufficient to enable those terms to be treated as included in the contract. The agent, said Pollock CB, 'made the same contract in this case as if he had made it for himself'. In the latter case, the agent was authorised to enter into a contract for the purchase of wood. His knowledge that the vendor was a factor dealing for a principal was held sufficient to enable the contract to be treated as made with the principal and so preclude the purchaser from relying on a set-off against the factor. Neither are cases of imputation of knowledge. Rather, the agent's knowledge affects the terms or performance of the contract which he concludes on behalf of his principal.

These principles have no application in this case. We are not concerned with the contractual terms upon which DLH received the traceable assets but whether it had the knowledge which would impose a constructive trust. In other words, real imputation of knowledge is required.

(ii) Principal's duty to investigate or make disclosure

Secondly, there are cases in which the principal has a duty to investigate or to make disclosure. The duty to investigate may arise in many circumstances, ranging from an owner's duty to inquire about the vicious tendencies of his dog (*Baldwin v Casella* (1872) LR 7 Exch 325 at 326–327) to the duty of a purchaser of land to investigate the title. Or there may be something about a transaction by which the principal is 'put on inquiry'. If the principal employs an agent to discharge such a duty, the knowledge of the agent will be imputed to him. (There is an exception, the scope of which it is unnecessary to discuss, in cases in which the agent commits a fraud against the principal.) Likewise in

cases in which the principal is under a duty to make disclosure (for example, to an insurer) he may have to disclose not only facts of which he knows but also material facts of which he could expect to have been told by his agents. So in *Gladstone v King* (1813) 1 M & S 35, 105 ER 13 a marine insurance policy was avoided because the master of the ship knew that it had suffered damage, even though he had not in fact communicated this information to the owner. *Regina Fur Co Ltd v Bossom* [1957] 2 Lloyd's Rep 466 upon which Mr Beloff strongly relied, also concerned the duty to make disclosure under an insurance policy and therefore falls within the same category.

None of these cases are relevant because in receiving the traceable assets, DLH had no duty to investigate or make disclosure. There was nothing to put it on inquiry.

(iii) Agent authorised to receive communications

Thirdly, there are cases in which the agent has actual or ostensible authority to receive communications, whether informative (such as the state of health of an insured: *Blackley v National Mutual Life Assurance* [1972] NZLR 1038) or performative (such as a notice to quit: *Tanham v Nicholson* (1872) LR 5 HL 561) on behalf of the principal. In such cases, communication to the agent is communication to the principal. These cases also have no application here. Mr Ferdman did not receive information about the frauds in his capacity as agent for DLH. He found it out while acting for the Canadians.

(iv) Agent's duty to principal irrelevant

What it therefore comes to is that Mr Ferdman, an agent of DLH, had private knowledge of facts into which DLH had no duty to inquire. Mr Beloff said that Mr Ferdman nevertheless owed DLH a duty to disclose those facts. He then submits that because he had such a duty, DLH must be treated as if he had discharged it.

I am inclined to agree that Mr Ferdman did owe a duty, both as broker employed by DLH to find an investor and as chairman of the Board, to inform DLH that the Yulara money was the proceeds of fraud. I reject Mr Tager's submission, based on *Kelly v Cooper* [1992] 3 WLR 936, that no term can be implied in a contract with a Swiss fiduciary agent which requires him to disclose that the money for which he is being paid a 5% procurement commission has been stolen. There is no evidence that Switzerland will enforce a confidence in iniquity any more than this country.

But Mr Beloff's submission that DLH must be treated as if the duty had been discharged raises an important point of principle. In my judgment the submission is wrong. The fact that an agent owed a duty to his principal to communicate information may permit a court to infer as a fact that he actually did so. But this is a rebuttable inference of fact and in the present case the judge found that Mr Ferdman did not disclose what he knew to anyone else acting on behalf of DLH. In some of the cases in the third of the categories I have mentioned, the fact that an agent with authority to receive a communication had a duty to pass the communication on to his principal is mentioned as a reason why the principal should be treated as having received it. I think, however, that the true basis of these cases is that communication to the agent is treated, by reason of his authority to receive it, as communication to the principal. I know of no authority for the proposition that in the absence of any

duty on the part of the principal to investigate, information which was received by an agent otherwise than as agent can be imputed to the principal simply on the ground that the agent owed to his principal a duty to disclose it.

On the contrary, I agree with the judge that *Re David Payne & Co Ltd, Young v David Payne & Co Ltd* [1904] 2 Ch 608 at 611 is authority against such a proposition. In that case the Exploring Land and Minerals Co Ltd lent £6,000 to David Payne & Co Ltd for 30 days on the security of a debenture. One Kolckmann, a stockbroker who was concerned in an ambitious and somewhat dubious scheme of flotation involving David Payne & Co Ltd, was also a director of the Exploring Land Co. In his capacity as stockbroker he knew that the money would not be applied to any authorised purpose of the company but diverted to the use of its controlling shareholder. He actually signed the cheque by which the money was advanced. David Payne & Co Ltd went into liquidation and the liquidator challenged the validity of the debenture on the ground that Kolckmann's knowledge of the ultra vires purposes for which the money would be used should be imputed to the Exploring Land Co.

Buckley J appears to have assumed that, as a director of the Exploring Land Co, Kolckmann owed a duty to disclose what he knew about the real purposes for which the money would be used. But he regarded this as insufficient to enable that knowledge to be imputed to the company. He said (at 611):

> 'I understand the law to be this: that if a communication be made to an agent *which it would be his duty to hand on to his principals* ... and if the agent has an interest which would lead him not to disclose to his principals the information that he has thus obtained, and in point of fact he does not communicate it, you are not to impute to his principals knowledge by reason of the fact that their agent knew something which it was not in his interest to disclose, and which he did not disclose.' (My emphasis.)

It is true that in the Court of Appeal, both Vaughan-Williams and Romer LJJ said that Kolckmann owed no duty to impart his knowledge to the Exploring Land Co. Thus Romer LJ said (at 619):

> 'I take it that in such a transaction the lending company was not bound to inquire as to the application of the money at all by the borrowing company. That being so, it appears to me that knowledge independently acquired by a director in his personal capacity in respect to a matter which was irrelevant so far as concerned the lending company is knowledge which cannot be imputed to the company, for it was knowledge of something which really did not concern the lending company as a matter of law. Therefore, you cannot imply a duty on the part of the director to have told these facts to the lending company, or a duty on the part of the lending company to have inquired into that question.'

It is however clear from the process of reasoning that what Romer LJ means is that in the absence of a duty to inquire, there was no duty of disclosure on the part of the director on which an outsider could rely for the purpose of imputing his knowledge to the company. I do not think that it would have affected his conclusion if the director had for some other reason (eg some internal company rule) owed a duty of disclosure with which he did not in fact comply. I agree with Buckley J that this would have been irrelevant.

It follows that in my judgment Millett J was right to hold that Mr Ferdman's position as agent or broker does not enable his knowledge to be imputed to DLH.

(*b*) The 'directing mind and will' theory

The phrase 'directing mind and will' comes from a well-known passage in the judgment of Viscount Haldane LC in *Lennards Carrying Co Ltd v Asiatic Petroleum Co Ltd* [1915] AC 705, [1914–15] All ER Rep 280 which distinguishes between someone who is 'merely a servant or agent' and someone whose action (or knowledge) is that of the company itself. Despite their familiarity, it is worth quoting the terms in which Viscount Haldane LC said that the directing mind could be identified ([1915] AC 705 at 713, [1914–15] All ER Rep 280 at 282):

> 'That person may be under the direction of the shareholders in general meeting; that person may be the board of directors itself, or it may be, and in some companies it is so, that that person has an authority co-ordinate with the board of directors given to him under the articles of association, and is appointed by the general meeting of the company, and can only be removed by the general meeting of the company. My Lords, whatever is not known about Mr. Lennard's position, this is known for certain, Mr. Lennard took the active part in the management of this ship on behalf of the owners, and Mr. Lennard, as I have said, was registered as the person designated for this purpose in the ship's register.'

Viscount Haldane LC therefore regarded the identification of the directing mind as primarily a *constitutional* question, depending in the first instance upon the powers entrusted to a person by the articles of association. The last sentence about Mr Lennard's position shows that the position as reflected in the articles may have to be supplemented by looking at the actual exercise of the company's powers. A person held out by the company as having plenary authority or in whose exercise of such authority the company acquiesces, may be treated as its directing mind.

It is well known that Viscount Haldane LC derived the concept of the 'directing mind' from German law (see Gower *Principles of Modern Company Law* (5th edn, 1992) p 194, n 36) which distinguishes between the agents and organs of the company. A German company with limited liability (GmbH) is required by law to appoint one or more directors (Geschäftsführer). They are the company's organs and for legal purposes represent the company. The knowledge of any one director, however obtained, is the knowledge of the company (see Scholz *Commentary on the GmbH Law* (7th edn, 1986), s 35). English law has never taken the view that the knowledge of a director ipso facto imputed to the company: see *Powles v Page* (1846) 3 CB 15, 136 ER 7 and *Re Carew's Estate Act (No 2)* (1862) 31 Beav 39, 54 ER 1054. Unlike the German Geschäftsführer, an English director may, as an individual, have no powers whatever. But English law shares the view of German law that whether a person is an organ or not depends upon the extent of the powers which in law he has express or implied authority to exercise on behalf of the company.

Millett J did not accept that Mr Ferdman was the directing mind and will of DLH because he exercised no independent judgment. As a fiduciary he acted entirely upon the directions of the American beneficial owners and their

consultant Mr Stern. All that he did was to sign the necessary documents and ensure that the company's paper work was in order. This involved seeing that decisions which had really been taken by the Americans and Mr Stern were duly minuted as decisions of the board made in Switzerland.

But neither the Americans nor Mr Stern held any position under the constitution of the company. Nor were they held out as doing so. They signed no documents on behalf of the company and carried on no business in its name. As a holding company, DLH had no independent business of its own. It entered into various transactions and on those occasions the persons who acted on its behalf were the board or one or more of the directors.

It seems to me that if the criterion is whether the candidate for being the 'directing mind and will' was exercising independent judgment, as opposed to acting upon off-stage instructions, not even the board of directors acting collectively would in this case have qualified. It also did what it was told. But Mr Tager was inclined to concede that the board, acting as a board, could properly be regarded as the directing mind and will. It was certainly held out in certain quarters as such. DLH claimed non-resident status from the Inland Revenue on the ground that its 'central management and control' was situated in Switzerland.

The authorities show clearly that different persons may for different purposes satisfy the requirements of being the company's directing mind and will. Therefore the question in my judgment is whether in relation to the Yulara transaction, Mr Ferdman as an individual exercised powers on behalf of the company which so identified him. It seems to me that Mr Ferdman was clearly regarded as being in a different position from the other directors. They were associates of his who came and went. SAFI charged for their services at a substantially lower rate. It was Mr Ferdman who claimed in the published accounts of DLH to be its ultimate beneficial owner. In my view, however, the most significant fact is that Mr Ferdman signed the agreement with Yulara on behalf of DLH. There was no board resolution authorising him to do so. Of course we know that in fact he signed at the request of Mr Stern, whom he knew to be clothed with authority from the Americans. But so far as the constitution of DLH was concerned, he committed the company to the transaction as an autonomous act which the company adopted by performing the agreement. I would therefore hold, respectfully differing from the judge, that this was sufficient to justify Mr Ferdman being treated, in relation to the Yulara transaction, as the company's directing mind and will. Nor do I think it matters that by the time DLH acquired Yulara's interest in the Nine Elms project on 16 March 1988, Mr Ferdman had ceased to be a director. Once his knowledge is treated as being the knowledge of the company in relation to a given transaction, I think that the company continues to be affected with that knowledge for any subsequent stages of the same transaction. So, for example, if (contrary to the judge's finding) the £1,030,000 sent by Yulara on 29 May 1986 had been received beneficially by DLH as a loan, but Mr Ferdman had resigned or died a week earlier, I do not think that DLH could have said that it received the money without imputed knowledge of the fraud. And in my judgment the

subsequent acquisition of Yulara's interest was sufficiently connected with the original investment to be affected by the same knowledge.

I would therefore allow the appeal. I do not regard this as an unsatisfactory outcome. If the persons beneficially interested in a company prefer for tax or other reasons to allow that company to be for all legal purposes run by off-shore fiduciaries, they must accept that it may incur liabilities by reason of the acts or knowledge of those fiduciaries.

Appeal allowed. Case remitted to judge to determine relief to which plaintiff was entitled.

16 May 1994. The Appeal Committee of the House of Lords (Lord Jauncey of Tullichettle, Lord Slynn and Lord Woolf) refused leave to appeal.

Frances Rustin Barrister.

Marchant v Onslow

CHANCERY DIVISION

DAVID NEUBERGER QC SITTING AS A DEPUTY JUDGE OF THE HIGH COURT

14, 17 SEPTEMBER 1993

Education – School – Conveyance under School Sites Act 1841– Reverter – Cesser for use for purposes of Act – Land conveyed for full value – Provision for land to 'revert to and become a portion of ... Estate' – Whether provision capable of applying to freestanding land not part of an estate – Whether reverting to original grantor and successors – School Sites Act 1841, s 2 – Reverter of Sites Act 1987, s 1.

In 1848 the defendant's predecessors in title conveyed a piece of land to the plaintiffs' predecessors in title to be held by them on trust for use as a school pursuant to the School Sites Act 1841, s 2[a] of which provided, inter alia, that any person seised of and having the beneficial interest in any land could grant or convey 'any Quantity [of that land] not exceeding One Acre ... as a Site for a School' provided that 'upon the said Land so granted ... ceasing to be used for the Purposes [of] this Act ... the same shall thereupon immediately revert to and become a portion of the said Estate'. By virtue of s 1[b] of the Reverter of Sites Act 1987, which was passed in order to amend the law with respect to the reverter of sites that had ceased to be used for particular purposes, the proviso to s 2 of the 1841 Act had effect as if the land, instead of reverting, vested in a trust to sell the land with the proceeds being held on trust for the persons otherwise entitled to the reversion. The land conveyed in 1848 ceased to be used for school purposes in 1984 and was sold in 1987, and the question arose whether the proceeds of sale were held on trust by the plaintiffs for the benefit of the successors in title to the grantors of the 1848 conveyance, as the defendant contended, or for the successors in title to the grantor's land of which the site once formed part.

a Section 2, so far as material, is set out at p 709 *e* to *h*, post

b Section 1, so far as material, is set out at p 709 *j* to p 710 *b*, post

TAB2

[HOUSE OF LORDS.]

LENNARD'S CARRYING COMPANY, LIMITED APPELLANTS; AND ASIATIC PETROLEUM COMPANY, LIMITED RESPONDENTS.

H. L. (E.)* 1915 *March* 8.

Ship—Loss of Cargo by Fire—Fire caused by Unseaworthiness—"Actual fault or privity" of Owners—Merchant Shipping Act, 1894 (57 & 58 *Vict.* c. 60), s. 502.

By s. 502 of the Merchant Shipping Act, 1894, the owner of a British sea-going ship shall not be liable to make good to any extent whatever "any loss or damage happening without his actual fault or privity" where any goods or merchandise taken in or put on board his ship are lost or damaged by reason of fire on board the ship.

A cargo of benzine on board ship was lost by a fire caused by the unseaworthiness of the ship in respect of the defective condition of her boilers. The shipowners were a limited company and the managing owners were another limited company. The managing director of the latter company was the registered managing owner and took the active part in the management of the ship on behalf of the owners. He knew or had the means of knowing of the defective condition of the boilers, but he gave no special instructions to the captain or the chief engineer regarding their supervision and took no steps to prevent the ship putting to sea with her boilers in an unseaworthy condition :—

Held, that the owners had failed to discharge the onus which lay upon them of proving that the loss happened without their actual fault or privity.

Decision of the Court of Appeal [1914] 1 K. B. 419 affirmed.

APPEAL from an order of the Court of Appeal affirming a judgment of Bray J. (1)

The appellants were the owners of the steamship *Edward Dawson*. By a charterparty dated February 23, 1911, the ship was let on time charter to the Anglo-Saxon Petroleum Company for nine, twelve, or fifteen months at the option of the charterers. Under this charterparty she loaded a cargo of 2011 tons of benzine at Novorossisk in Russia for carriage to Rotterdam. The respondents were purchasers of this cargo and

* *Present:* VISCOUNT HALDANE L.C., LORD DUNEDIN, LORD ATKINSON, LORD PARKER OF WADDINGTON, and LORD PARMOOR.

(1) [1914] 1 K. B. 419.

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indorsees of the bills of lading. On October 1, 1911, whilst in the course of her voyage from Novorossisk to Rotterdam the ship and her cargo were destroyed by fire. The respondents brought an action against the appellants for damages for loss of the cargo.

By their points of claim the respondents alleged the failure to deliver the cargo. Alternatively they alleged that the ship was unseaworthy at Novorossisk by reason of the defective condition of her boilers and that owing to this unseaworthiness the ship with her cargo was driven ashore and lost.

The appellants by their points of defence admitted the failure to deliver, but relied on s. 502 of the Merchant Shipping Act, 1894 (1), as relieving them from liability, and they denied the allegation of unseaworthiness. The respondents by their points of reply denied that the cargo was lost by fire within the meaning of s. 502 and alleged that it was lost by perils of the sea occasioned by the unseaworthiness. Alternatively they alleged that if the cargo was lost by fire the fire was occasioned by the unseaworthiness. In the further alternative they alleged that by the terms of the contract of carriage the appellants had precluded themselves from relying on the protection of the section; but in the circumstances it became unnecessary for the Court to determine this question.

The *Edward Dawson* was a steel screw oil tank steamer. She had two boilers and each boiler had three furnaces. Her average speed was about seven knots. She was built in 1890 for a French firm and was classed in the first division of the Bureau Veritas. She was supplied with new boilers in 1896. In 1897 she was purchased by the appellants, who then expended 6500*l.* upon her. The managers of the appellant company were another company, John M. Lennard & Sons, Limited, and the managing director of that company was John M. Lennard, who

(1) Merchant Shipping Act, 1894, s. 502: "The owner of a British sea-going ship, or any share therein, shall not be liable to make good to any extent whatever any loss or damage happening without his actual fault or privity in the following cases; namely,—

"(i.) Where any goods, merchandise, or other things whatsoever taken in or put on board his ship are lost or damaged by reason of fire on board the ship; . . . .'

was the registered managing owner of the ship. Lennard did not give evidence at the trial.

In February, 1911, the ship was repaired at Liverpool to the requirements of the Bureau Veritas surveyor, Mr. Viehoff; and her class was extended for twelve months to March 31, 1912, but subject to the pressure of her boilers being reduced from 160 lbs. to 130 lbs. She then proceeded under the time charter to various ports in the Mediterranean and returned to Thames Haven in June, 1911. There had been trouble with her boilers during this voyage. Before the arrival of the ship at Thames Haven the charterers sent a letter to the appellants complaining that there was something greatly wrong with her engines and boilers and urging that they should be put in thorough working order, and in July, 1911, the appellants ordered new boilers and stipulated that they should be ready by the middle of November. On her arrival at Thames Haven the boilers were examined by a foreman boilermaker named Clarke, representing the general marine superintendent of the ship, Mr. Smaling. Clarke reported that the repairs necessary were of a miscellaneous but not very serious character. No instructions were given by Lennard or the appellants either to Smaling or to Clarke, nor was the charterers' complaint communicated to them. The repairs were done by Fletcher & Sons, Limited, a responsible firm, under the directions of Clarke and were limited to repairing existing leaks. The evidence showed that the normal life of a boiler if well cared for was from sixteen to eighteen years and the normal life of a set of tubes about ten years. The ship then proceeded to New York, and from New York to Barcelona and from Barcelona to Novorossisk, and during all this time the trouble with the boilers continued and increased. The master made no communications on this matter either to the appellants or to Lennard. On her arrival at Novorossisk there was a very large accumulation of salt in the boilers owing to leakage, and the crew spent two days cutting out the salt. After loading her cargo of benzine the ship left Novorossisk for Rotterdam, and before she reached the English Channel the two centre furnaces were completely salted up so that they had become useless, and two tubes in the boilers had burst. Shortly after passing Dover on September 30, 1911, the ship

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encountered a strong north-westerly gale with a heavy sea. At 3.30 P.M. the captain brought her head to the wind as he considered it dangerous to approach the Dutch coast. At 11 P.M. a tube in the port boiler burst. The fires of that boiler had to be drawn to allow the tube to be plugged, and the ship was rapidly driven to leeward. About 2 A.M. the fires were relighted, and about 3 A.M. the full pressure of steam which the two boilers and four furnaces could raise was obtained, but the ship still continued to be driven to leeward owing to the want of sufficient steam power to face the gale. At 5.30 A.M. she grounded on the Botkill Bank, and after bumping on the bank several times she got off, but about 7.40 A.M. she finally grounded in the Scheldt near Flushing. The stranding of the ship injured the tanks to such an extent that some of the benzine escaped, and the vapour of the escaping benzine coming into contact with the combustion chambers of the boilers caused an explosion which resulted in the loss of the ship and cargo.

Bray J. found that the vessel on leaving Novorossisk was unseaworthy by reason of the condition of her boilers, that the fire and consequent loss of the cargo were caused by the unseaworthiness, and that the loss did not happen without the actual fault or privity of the owners. He accordingly gave judgment for the respondents for an amount to be ascertained, which amount was subsequently ascertained at 13,500*l*. In the Court of Appeal the appellants did not contest the finding of Bray J. as to unseaworthiness, but contended that neither the unseaworthiness nor the stranding caused the fire, and that the fire and loss of the cargo occurred without the actual fault or privity of the appellants.

The Court of Appeal by a majority (Buckley and Hamilton L.JJ., Vaughan Williams L.J. dissenting) affirmed the decision of the learned judge.

1915. Feb. 26; March 1, 8. *Adair Roche, K.C.*, and *Raeburn* (with them *I. H. Stranger*, for *J. A. H. Wood*, serving with His Majesty's Forces), for the appellants. The main defence to the action is s. 502 of the Merchant Shipping Act, 1894. Unseaworthiness in respect of the boilers is admitted, but there is

nothing to connect the loss of the cargo with that unseaworthiness. The loss occurred without the actual fault or privity of the appellants. The manager Lennard was not aware of the unseaworthy condition of the boilers, nor had he the means of knowledge. He was entitled to rely on the certificate of the Bureau Veritas and upon the subsequent repairs, which were not found by Bray J. to be insufficient. But assuming that Lennard was to blame, the manager's fault or privity is not the fault or privity of the owner. It must be actual or personal fault or privity: *Virginia Carolina Chemical Co.* v. *Norfolk and North American Steam Shipping Co.* (1); *Ingram & Royle* v. *Services Maritimes du Tréport* (2); *The Fanny* (3); *The Warkworth.* (4)

[LORD ATKINSON referred to *Wilson* v. *Dickson.* (5)]

In the case of a company the persons responsible would be the board of directors. There is a distinction between the board, who have the general management and control of the company, and a person appointed by the board or by the company at general meeting to do a particular class of acts: *Smitton* v. *Orient Steam Navigation Co.* (6) Lennard had the supreme control of the technical management of the ship, but he was nothing more than an agent of the appellant company. He was not the alter ego of the company. He did not represent the company in the sense of making his fault the fault of the company. The case of a company is analogous to the old case of a sixty-fourth owned ship. Sleeping ownership is recognized by law and is in the interest of public policy, and s. 502, which is a reproduction of similar provisions in older Acts, expressly exempts a sleeping owner from responsibility. The object of the section is to restrict the doctrine of respondeat superior within certain defined limits.

Maurice Hill, K.C., and *F. D. MacKinnon, K.C.*, for the respondents, were not called on.

VISCOUNT HALDANE L.C. My Lords, in this case the appellants have, at all events, the satisfaction of knowing that their case has been excellently argued by both the learned counsel who have appeared for them at your Lordships' Bar.

(1) [1912] 1 K. B. 229.
(2) [1913] 1 K. B. 538, at p. 544.
(3) (1912) 28 Times L. R. 217.
(4) (1883) 9 P. D. 20.
(5) (1818) 2 B. & Ald. 2.
(6) (1907) 12 Com. Cas. 270.

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The case, which we have now heard fully and as to which we do not think it necessary to trouble the respondents' counsel, is shortly this. The *Edward Dawson* was a tank steamer designed for the carriage of oil in bulk. She was chartered by her owners, the appellants, on a time charter to a company known as the Anglo-Saxon Petroleum Company, and in the course of her employment she proceeded to Novorossisk in the Black Sea. There she loaded in bulk 2011 tons of benzine, and the bills of lading, six in number, were indorsed by the Anglo-Saxon Petroleum Company to the Asiatic Petroleum Company, who are the respondents in this case. My Lords, the benzine has been lost, and the respondents have brought an action against the appellants to recover damages for the loss of their cargo.

Now the story of the case is in outline this: The *Edward Dawson* was built in 1890, as I have said, for the carriage of oil in bulk, and in 1907 she was bought by the appellants, who spent a good deal of money upon her, and proceeded to use her for certain voyages. In January, 1911, after she had been for a good while at sea, she was overhauled at Birkenhead, and the Bureau Veritas, a well-known agency which issues certificates and keeps a list for the purpose of showing the condition of ships, gave a certificate through Mr. Viehoff, who was their agent at Birkenhead, to the effect that she would have a satisfactory character for another twelve months, but only on condition that her boiler pressure was reduced from 160 to 130 lbs. My Lords, that obviously made a great deal of difference to the energy developing limits of capacity of the ship. Subsequently to that she proceeded on what has been described in the course of the argument as a round voyage. She went to Thames Haven, and at Thames Haven certain repairs were done under the superintendence of a Mr. Clarke to her boilers; she proceeded to New York, and from New York to Barcelona, and after various intermediate voyages she came to Novorossisk in the Black Sea, where she loaded the cargo of benzine of which I have spoken. She left Novorossisk, and the unsatisfactory condition of her boilers soon became manifest. These boilers leaked; they leaked salt water into the central furnaces, the furnaces became silted up with salt, so that their capacity was diminished, and the result

was that when the ship on her way back passed the Straits of Dover and came into the North Sea she was not in a condition to develop such power as was desirable in the event of her encountering heavy head weather. My Lords, she found herself on October 1 off the Dutch coast near the mouth of the Scheldt. There was a gale blowing, and she hove to and set her head against that gale to prevent herself from being driven on to the lee shore, but she was driven. She first of all grounded on the Botkill Bank, and then she grounded again in the mouth of the Scheldt. Her port of destination was Rotterdam, but she was by this time a good way away from Rotterdam at the mouth of another river which lies south of the Maas, on which Rotterdam is situated, namely, the Scheldt, and in the Scheldt, as I have observed, she took the ground again. She does not appear to have been under adequate control. She had, among other things, burst a tube, which was not unlikely, having regard to wear and tear in excess of the length of life of tubes, which was given in the evidence as only ten years, and to the general condition of her boilers. She burst a tube, she took the ground, she was unable to get off the ground, she bumped, and as the result of bumping the benzine got loose from the tanks, the deck bulged, the tanks were probably cracked, anyhow the benzine began to get into the furnaces, and the result was a conflagration. It was suggested that if the flame had been extinguished by the injection of water, this might have been prevented, but I do not think the evidence upon that point at all satisfactorily established that that could have been secured, or, at any rate, that the operation could have been properly carried out.

My Lords, in that state of things the loss of the cargo took place, and the case came before Bray J., who tried it, and Bray J. found a number of facts. He found these facts after hearing the evidence on both sides, and I think that his findings of fact were justified. They were these: The first was that the ship when she left Novorossisk was unseaworthy by reason of defects in her boilers. The second finding of fact was that the stranding on the Botkill Bank, just off the mouth of the Scheldt, was caused by the want of steam, which in its turn was caused by the unseaworthy condition of the boilers; and he found the same causes as

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regards the subsequent stranding in the Scheldt itself. Then in the third place he found that the loss was not caused by any negligence or want of precautions on the part of the engineers, because he does not find it proved that anything they could have done could have altered the consequences. He found that the loss of the cargo was caused by the unseaworthiness of the ship due to the condition of the boilers. Then there are other findings which are findings of mixed fact and law. One of these is that the duty of supervision remained with the managing owners, and that the fault of the managing owners was a fault that affected the company itself.

My Lords, that last question gives rise to the real question of law which occurs in this case. Taking the facts to be as the learned judge has found them, what is the consequence as regards the liability of the appellants? The appellants are a limited company and the ship was managed by another limited company, Messrs. John M. Lennard & Sons, and Mr. J. M. Lennard, who seems to be the active director in J. M. Lennard & Sons, was also a director of the appellant company, Lennard's Carrying Company, Limited. My Lords, in that state of things what is the question of law which arises? I think that it is impossible in the face of the findings of the learned judge, and of the evidence, to contend successfully that Mr. J. M. Lennard has shown that he did not know or can excuse himself for not having known of the defects which manifested themselves in the condition of the ship, amounting to unseaworthiness. Mr. Lennard is the person who is registered in the ship's register and is designated as the person to whom the management of the vessel was entrusted. He appears to have been the active spirit in the joint stock company which managed this ship for the appellants; and under the circumstances the question is whether the company can invoke the protection of s. 502 of the Merchant Shipping Act to relieve it from the liability which the respondents seek to impose on it. That section is in these words: "The owner of a British sea-going ship, or any share therein, shall not be liable to make good to any extent whatever any loss or damage happening without his actual fault or privity in the following cases; namely, —(i.) Where any goods, merchandise, or other things whatsoever

taken in or put on board his ship are lost or damaged by reason of fire on board the ship."

Now, my Lords, did what happened take place without the actual fault or privity of the owners of the ship who were the appellants? My Lords, a corporation is an abstraction. It has no mind of its own any more than it has a body of its own; its active and directing will must consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the directing mind and will of the corporation, the very ego and centre of the personality of the corporation. That person may be under the direction of the shareholders in general meeting; that person may be the board of directors itself, or it may be, and in some companies it is so, that that person has an authority co-ordinate with the board of directors given to him under the articles of association, and is appointed by the general meeting of the company, and can only be removed by the general meeting of the company. My Lords, whatever is not known about Mr. Lennard's position, this is known for certain, Mr. Lennard took the active part in the management of this ship on behalf of the owners, and Mr. Lennard, as I have said, was registered as the person designated for this purpose in the ship's register. Mr. Lennard therefore was the natural person to come on behalf of the owners and give full evidence not only about the events of which I have spoken, and which related to the seaworthiness of the ship, but about his own position and as to whether or not he was the life and soul of the company. For if Mr. Lennard was the directing mind of the company, then his action must, unless a corporation is not to be liable at all, have been an action which was the action of the company itself within the meaning of s. 502. It has not been contended at the Bar, and it could not have been successfully contended, that s. 502 is so worded as to exempt a corporation altogether which happens to be the owner of a ship, merely because it happens to be a corporation. It must be upon the true construction of that section in such a case as the present one that the fault or privity is the fault or privity of somebody who is not merely a servant or agent for whom the company is liable upon the footing respondeat superior, but somebody

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for whom the company is liable because his action is the very action of the company itself. It is not enough that the fault should be the fault of a servant in order to exonerate the owner, the fault must also be one which is not the fault of the owner, or a fault to which the owner is privy; and I take the view that when anybody sets up that section to excuse himself from the normal consequences of the maxim respondeat superior the burden lies upon him to do so.

Well, my Lords, in that state of the law it is obvious to me that Mr. Lennard ought to have gone into the box and relieved the company of the presumption which arises against it that his action was the company's action. But Mr. Lennard did not go into the box to rebut the presumption of liability and we have no satisfactory evidence as to what the constitution of the company was or as to what Mr. Lennard's position was. The memorandum and articles of association were not put in. The only evidence was that of the secretary, Mr. Simpson, who told the Court that he was secretary not only to the company but also to the managing company, and the inference to be drawn is that the officials of the two companies were very much the same and transacted very much the same business. Under the circumstances I think that the company and Mr. Lennard have not discharged the burden of proof which was upon them, and that it must be taken that the unseaworthiness, which I hold to have been established as existing at the commencement of the voyage from Novorossisk, was an unseaworthiness which did not exist without the actual fault or privity of the owning company. My Lords, if that is so, then the judgment of the majority of the Court of Appeal and of Bray J. was right.

My Lords, there is another point which I have not entered upon, because it was not touched upon in the Court below, and that is the question as to whether the terms of the charterparty are such as to exclude the operation of s. 502 altogether. That question remains intact. It is not necessary to deal with it in this case and I therefore pass it by.

My Lords, for the reasons which I have given, I move that this appeal be dismissed, and dismissed with costs.

LORD DUNEDIN. My Lords, I concur, and I have but little to add to what the noble and learned Lord on the woolsack has said. It appears clearly from the facts, and indeed eventually was admitted by the appellants' counsel, that the loss which had its final outcome in the fire was really due to a set of defects in the steam power in the boilers which constituted unseaworthiness. In the Court below at the trial the principal controversy seems to have turned upon whether the fault in allowing the vessel to be unseaworthy was a fault committed by the captain at Novorossisk or was the fault of J. M. Lennard, the registered manager of the ship. I agree with what my noble and learned friend has said that the true view of the facts is that the fault was the fault of Lennard. But before your Lordships' House the chief argument has been, admitting that it was the fault of J. M. Lennard, whether that was actual fault or privity in the sense of s. 502 of the Merchant Shipping Act. The real question therefore turns upon what is to be the application of the words there used to a metaphysical conception like an incorporated company who cannot act directly themselves.

My Lords, I do not know that a case will ever arise in which that will need to be treated as a purely abstract proposition. I do not think it arises in this case, and I certainly incline to the opinion that it will be found always to depend upon the particular facts of the case. If I was bound to decide affirmatively in this case, I should be inclined to think that there was enough known about Lennard to show that, to use the appellants' learned counsel's own phrase, he was the alter ego of the company. He was a director of the company. I can quite conceive that a company may by entrusting its business to one director be as truly represented by that one director, as in ordinary cases it is represented by the whole board. I am quite sure that you cannot at least put as a general proposition in law that it is true that nothing will ever be the actual fault or privity of an incorporated company unless it is the actual fault of the whole board of directors. But, my Lords, I think the true criterion of the case is that which was found and applied by Hamilton L.J., that the parties who plead this 502nd section must bring themselves within its terms; and therefore the question is, have the company

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LENNARD'S CARRYING COMPANY, LIMITED v. ASIATIC PETROLEUM COMPANY, LIMITED.

freed themselves by showing that this arose without their actual fault or privity? I think they have not. Lennard may have been deputed by the company to do all these things, or again there might have been liability upon the ground that Lennard had told the whole body of directors and that they knew and sent him the money, and so on. Anyway they have not discharged the onus which was upon them, and I therefore concur in the motion which has been made by my noble and learned friend on the woolsack.

LORD ATKINSON. My Lords, I concur.

LORD PARKER OF WADDINGTON. My Lords, I concur.

LORD PARMOOR. My Lords, I concur.

Order of the Court of Appeal affirmed and appeal dismissed with costs.

Lords' Journals, March 8, 1915.

Solicitors for appellants: *Downing, Handcock, Middleton & Lewis, for Bolam, Middleton & Co., Sunderland.*

Solicitors for respondents: *Parker, Garrett & Co.*

TAB3

Kappler v. Beaudoin

Ontario Judgments

Ontario Superior Court of Justice

Lalonde J.

Heard: August 30, 2000.

Judgment: September 13, 2000.

Court File No. 99-CV-009854

[2000] O.J. No. 3439 | [2000] O.T.C. 666

Between Susanne Kappler and Erich Kappler, plaintiffs, and Marie France Beaudoin, defendant

(30 paras.)

Counsel

Andrew J. McMurray, for the plaintiffs. Jeffrey Langevin, for the defendant.

LALONDE J.

1 Erich Kappler, the plaintiff, is 78 years of age and his wife, Susanne Kappler, also a plaintiff, is 80 years of age. They are the parents of Robert Kappler who lived in a common-law relationship with the defendant, Marie France Beaudoin, from 1994 to 1998.

2 Robert Kappler, the plaintiffs' son, entered into a relationship with the defendant in 1994, shortly after being laid off from his job in North Bay, Ontario. Robert Kappler decided to finish his secondary education and obtain a university degree over a six-year period of time. Since Robert Kappler could not obtain a loan to finance his education, the plaintiffs decided to advance him $400 per month. After the defendant became pregnant with her first child, both she and Robert Kappler moved in with the plaintiffs and occupied the basement of the plaintiffs' home. The defendant's first child, Ryan, was born in the spring of 1995. After the birth of Ryan, the plaintiffs decided to move into the basement of their home and give the defendant and their son, Robert Kappler, occupation of the first floor. This situation endured until such time as the defendant's second child, Jenna, was born. The plaintiffs then bought and moved into another home. The defendant and her common-law husband, Robert Kappler, had the plaintiffs' house to themselves and were not required to pay any rent. The defendant paid municipal taxes, insurance, and public utilities.

3 Susanne Kappler explained in Court that their son, Robert Kappler, was a student and not earning a salary. The defendant, Marie France Beaudoin, was employed as a clerk at the Ottawa General Hospital, (as it was then known), earning $30,000 per year. Susanne Kappler and her husband felt they had to help in every way they could. They contributed $100 per month for each child, over and above the $400 per month they were giving their son, Robert Kappler. The plaintiffs also babysat the children as often as they could.

4 Erich Kappler stated that the defendant had a car on which she was paying a loan with interest at 10%. He offered to pay off the car loan to the finance company and asked the defendant to pay him back whenever she could. As the loan was interest free, the defendant accepted. Erich Kappler opened a ledger card and an entry was made every month upon receipt of a payment on the loan. He testified that he was in the habit of doing that as both his son, Robert, and his daughter, borrowed money from him from time to time. All payments received by the plaintiffs were recorded on a similar ledger sheet. The defendant made her regular monthly payments. At one point in time, there was $3,500 left on the $8,500 loan. To make the defendant feel part of the family, the plaintiffs decided to forgive the last $3,500 owing on the debt.

5 Erich Kappler further testified that the defendant asked him to loan her $20,000 to buy another car. In those days, the defendant travelled back and forth to visit her mother two to three times per week at Mont Ste Marie, in the province of Quebec. As the distance was considerable and the defendant travelled with infant children in a very old car, the plaintiffs decided to advance that sum of money, to the defendant. The purchase of the car was made through the joint efforts of Robert Kappler and the defendant. Once purchased, the vehicle, a Suzuki Sidekick, was placed in the defendant's name. Part of the consideration came from Robert Kappler's credit card, part came from the trade-in of the defendant's GEO Metro car, and the balance of the purchase price came from the plaintiffs' $20,000 loan. The bill of sale for the car was made out to Robert Kappler. This fact was explained at trial and the evidence received satisfies me that it does not help resolve the issues in this case. Erich Kappler stated that the defendant was very happy when she received the loan: "I could see it in her face".

6 The plaintiffs advanced the defendant $20,000 on June 28, 1998 and on August 15, 1998, the defendant announced she was leaving the plaintiffs' son. She moved out of the plaintiffs' home that she had occupied with Robert Kappler, on or about September 15, 1998.

Issues

> Is there a presumption of advancement or a presumption of resulting trust in regard to the $20,000 loan made by the plaintiffs to the defendant?
>
> Has the defendant been unjustly enriched to the detriment of the plaintiffs?

7 The evidence of Erich Kappler was corroborated by Susanne Kappler. She was not present in the courtroom when her husband testified. She stated that Erich Kappler told her the defendant had requested a $20,000 loan to purchase another car. Susanne Kappler confirmed that no money would have been advanced had the defendant not promised to repay the loan. Susanne

Kappler then typed up a document (the promissory note) that was filed as an Exhibit at trial and which is reproduced as follows:

Marie-France Beaudoin
2221 Beaver Ave.
Ottawa, Ont.
K1H 7W3

June 22, 1998

I, Marie-France Beaudoin, received a loan of $20,000. (twenty thousand) from Mrs. Susanne Kappler to purchase a car. I agree to repay this loan in 60 equal payments of $333.00 monthly, payable on the first day of each month. The first payment is due July 1, 1998.

8 According to the evidence of Susanne Kappler, it was the defendant who figured out that the sum of $333 would be the correct amount to amortize this loan. Both plaintiffs testified that Erich Kappler provided $14,000 and Susanne Kappler provided $6,000 to make a total of $20,000. There is no dispute that the amount of money was advanced. Both plaintiffs testified that the defendant took the note from Susanne Kappler and did not sign it. Neither did she refuse to sign it.

9 Even after the separation was announced, the plaintiffs continued to pay to the defendant and their son, Robert Kappler, the $100 for each of their children, they had paid each month since the birth of each child, until the defendant moved out of their house on September 15, 1998. Following the defendant's separation from their son, the plaintiffs made two more payments and then the payments stopped. During the month of September 1998, the plaintiffs were preparing to leave to spend the winter in the State of Florida, in the United States of America. Susanne Kappler testified that she presented the defendant with six deposit slips for the monthly payment on the $20,000 loan, to cover the period of time when the plaintiffs would be abroad. Susanne Kappler maintained that the defendant refused to sign the deposit slips. The defendant is alleged to have told the plaintiffs she would take out a loan in the spring, (meaning the spring of 1999), and pay off the plaintiffs' $20,000 loan. This, of course, never did happen. Susanne Kappler then stated that as they received news from their son, Robert Kappler, in March 1999 that the loan was not going to be repaid and that the defendant had borrowed money from the Bank of Montreal for other purposes, they decided to call in their $20,000 loan.

10 Marie France Beaudoin applied to the Regional Municipality of Ottawa-Carleton for a daycare subsidy for both her children. She submitted for that application two documents also entered in evidence at trial. The first document reads as follows:

Susanne KAPPLER

222 Beaver Ave.

Ottawa, Ont.

K1H 7W3

To whom it may concern

I confirm that Ms. Marie-France Beaudoin, 2221 Beaver Ave., Ottawa, Ont., is living in my house for 3 years. She pays to me monthly $460. plus long distance charges.

signed Susanne Kappler

Ottawa, June 5, 1998

11 The letter confirmed to the daycare officials that the defendant had lived in the plaintiff's house and paid a monthly rent of $460 plus long distance charges. The plaintiff, Susanne Kappler, explained that the sum of money mentioned in this letter, was the equivalent of the money received from the defendant to cover the operating cost of 2221 Beaver Avenue. The plaintiff, Susanne Kappler, admitted that the wording of this letter should have indicated that the $460 monthly payment was made by the defendant on her behalf to third parties such as public utilities and local government.

12 The second document the defendant submitted with her daycare application was the promissory note mentioned in paragraph 7 above that had been left unsigned at the time Susanne Kappler had presented it to the defendant. It is not known when the defendant signed the promissory note. She did not tell the plaintiffs she had signed the promissory note. She filed the promissory note with the Regional Municipality of Ottawa-Carleton showing an indebtedness to the plaintiffs thus qualifying for 100% daycare subsidy for both her children.

13 Marie France Beaudoin, 27 years of age, also testified. She claimed that her relationship with the plaintiffs while living with their son, was a very close one and she described the relationship as "perfect". The plaintiffs paid for everything and the defendant confirmed that after Ryan was born, she received $100 per month for Ryan and later she also received the same monthly payment for Jenna. The defendant confirmed that the plaintiffs had taken over her $8,500 loan for her GEO Metro car, and that she made regular payments to the plaintiffs who forgave her the last $3,500 of indebtedness for one of her birthdays. She quoted the plaintiffs as saying: "we all put our hands in it for Robert". She knew nothing about the ledger sheet filed with the Court by the plaintiff, Erich Kappler. She also confirmed that the amount of money advanced by the plaintiffs, for the GEO Metro car, was a loan. The defendant testified that with the $20,000 advance, she purchased a Suzuki Sidekick vehicle and the title of the vehicle was made in her name. She said this advance was not a loan, as she made no monthly payments to the plaintiffs. Another reason advanced by the defendant to establish a distinction between the advance for the first vehicle and the advance of the second vehicle was that the plaintiffs did not deduct the $200 monthly they gave to the children and apply it to the so-called car loan. She claims she was not asked for payments and that while the loan was advanced, the plaintiffs continued to make payments to her for the children, without deducting the car payment. The fact that the Suzuki Sidekick was placed immediately in her name, according to her, made it a gift by

the plaintiffs. She claimed that the promissory note referred to in paragraph 7 was sent to the officials at the Regional Municipality of Ottawa-Carleton to help her qualify for a 100% subsidy for daycare. The defendant said in Court she did not have any debts and that it was Susanne Kappler's idea to create this debt artificially to enable her to claim the entire daycare subsidy. She testified that this was the only reason she signed the promissory note. Since no request for the payments of the loan was made by the plaintiffs between June 30, 1998 and March 31, 1999, it means the $20,000 advance could be construed as a gift. For July 1st, August 1st, and September 1st, 1998, she received the $200 per month for the children from the plaintiffs without adjustment for the sum of $333 that the plaintiffs argued she owed on the promissory note. In fact she was very surprised to get a demand letter on March 5, 1999, while the plaintiffs were still holidaying in Florida.

14 During cross-examination, the defendant admitted that she had conversations with her estranged common-law husband, Robert Kappler, during the winter months of 1999, about the repayment of the plaintiffs' advance of $20,000. She said that she was willing to say and do anything to get her subsidy from the Regional Municipality of Ottawa-Carleton. She admitted that she was aware that there could have been criminal sanctions for misleading officials at the Regional Municipality of Ottawa-Carleton on the matter of the "loan". She told counsel for the plaintiffs that she did not have any recollection of being presented with deposit slips by Susanne Kappler prior to Susanne Kappler leaving for her six months holiday in Florida. According to the defendant that conversation between herself and Susanne Kappler did not happen.

15 The position taken by the plaintiffs is that the $20,000 advance was made by way of a loan to the defendant and that that loan should now be repaid to them to prevent any unjust enrichment of the defendant at their expense.

16 The position taken by the defendant, Marie France Beaudoin, is that the advance of $20,000 was a gift made to her and ought not now to take any different character simply because of the failure of the marital relationship between her and the plaintiffs' son.

The Law

17 The applicable law can be found in the case of Flatters v. Brown, *[1999] O.J. No. 2608*, where the Honourable Madam Justice Robertson states at paragraph 23, the following:

> Special classes of relationships, such as parent and child, attract special rules. [4] It does not matter that the account was jointly held. The presumption of advancement applies to the Boston bank account and it is taken for granted to be a gift by father to daughter. As Justice McCart said in Smith Estate v. Smith, *[1995] O.J. No. 253* (Quicklaw) (Ont. Gen. Div.) and as applied in the decision of Close v. Close *(1998), 33 R.F.L. (4th) 210* (Ont. Gen. Div.) 233:
>
> > "Where there is a conveyance or transfer of property without consideration from a parent to a child, the law presumes it was intended as a gift. The presumption of advancement is rebuttable if the party adduces evidence of a contrary intention on a balance of probabilities. Furthermore, the evidence required to rebut the presumption is evidence of the donor's intention at the time of the transfer."

> [4] Equity and the Law of Trust, P.H. Petit Butterworths 1989, p. 123: "In addition to rebutting the presumption of resulting trust by evidence as to the true intention, the existence of certain special relationships between the person who provides the purchase money or who transfers the property and the person into whose name the property is conveyed or transferred, either alone or jointly, gives rise to a presumption of advancement, which displaces the presumption of resulting trust."

18 At paragraph 27, Madam Justice Robertson continues as follows:

> No evidence contradicted the intention, to make a gift. The relevant time to consider the terms and conditions of the gift to children is what happened at the time of the making of the gift.

19 Counsel for the defendant advances the proposition that the advance of monies by the plaintiffs to the defendant should be treated in the same fashion as an advance made by parents to a child, stating that the plaintiffs were in loco parentis to the defendant. The counsel for the defendant quotes the decision of Kirpalani v. Hathiramani, *[1992] O.J. No. 1594*, given by the Honourable Mr. Justice McMurtry. At page 14 of the decision, he states:

> (iii) Presumption of advancement in the context of in loco parentis'
>
> The defendant properly submits that the onus of proof on a transferee to establish that the transfer of property does not create a resulting trust can be shifted, if the evidence establishes that the transferee stood in loco parentis' to the transferor. It is submitted on behalf of the defendant that he did stand in loco parentis' to Mr. Ram at the time of the conveyance of the property.

Mr. Justice McMurtry goes on to discuss what happens where property is purchased in the name of another or transferred to another without consideration and states:

> "A resulting trust will be presumed in favour of the person who has paid the purchase price. The presumption is overcome where the property vests in the name of a person towards whom the purchaser stood in loco parentis'. In that event the presumption is reversed and there is a rebuttable presumption that the purchaser intended to confer benefit or an advancement."

20 The Ontario Court of Justice (General Division) had to consider this problem in the case of Reain v. Reain *(1995), 20 R.F.L. (4th) 30*, at p. 43. In that decision, the Honourable Mr. Justice Sills had this to say about the doctrine of resulting trusts at paragraphs 16 and 17:

> The doctrine of resulting trusts based as it is on the unexpressed but presumed intention of the donor, will not arise where the relation existing between the donor and donee is such as to raise a presumption that a gift was intended. This presumption of advancement applies to most cases where the person to whom property is conveyed is the child of the donor. This presumption of advancement is rebuttable in a variety of circumstances such as those discussed by the learned authors of Snell's Principles of Equity at pp. 178 and 179. At p. 178, the authors state,
>
> > Both the presumption of a resulting trust and the presumption of advancement can be rebutted by evidence of the actual intention of the purchaser ... The clearest evidence

> is an express declaration of trust on the face of the conveyance of the legal estate, but even where this is absent the Court puts itself in the position of a jury, and considers all the circumstances of the case, so as to arrive at the purchaser's real intention; it is only where there is no evidence to contradict it that the presumption of a resulting trust, or of advancement, as the case may be, will prevail.

In dealing with determination of the question of debt versus gift in familial situations, the Ontario Court of Appeal in Reynolds v. Reynolds *(1995), 13 R.F.L. (4th) 179* at 182, stated,

> Without an agreement there can be no debt. It would be a dangerous precedent to permit moral family obligations to creep into equalization calculations, no matter how deserving the recipient may be.

The learned judge went on to say, "in the absence of agreement for repayment, there can be no debt".

Decision

21 While the $20,000 advance gives rise to a presumption of advancement in this case, I consider that such a presumption has been rebutted by evidence of a contrary intention. The presumption, as stated in the case of Reain v. Reain (supra), is not rebutted by a broad general expectation that the advance will be repaid in the absence of an agreement by all parties to that effect. In this case there was an agreement in writing for repayment, there were agreed terms of repayment, and the agreement was signed.

22 I have no difficulty in rejecting the defence advanced by Marie France Beaudoin.

23 It was normal for the plaintiffs to carry on paying the sum of $200 per month for the children from July 1, 1998 until the defendant left their home on September 15, 1998. Such payments were for the plaintiffs' grandchildren and this matter was, in their minds, a very separate matter from the $20,000 advance. I also accept their evidence, evidence that was not challenged, that they did not want to make a claim for repayment of the loan in August and September 1998, hoping that in the early months of the defendant's separation, their son, Robert, would reconcile with the defendant. I find this to be a very natural reaction on the part of the plaintiffs.

24 I was not convinced by the defendant's statement that what distinguished her loan for the first car from the loan for the second car was that she did not make any payments on the second loan. This argument does not help the defendant because it is clear from the evidence that the defendant decided to separate from the plaintiffs' son, Robert Kappler, within two months of the advance of $20,000. It was also clear, from both plaintiffs, that they were not going to cause any further acrimony between the defendant and their son by insisting that the July 1st, August 1st, and September 1st, 1998 payments be made on time. It is important to note that the evidence revealed that while the defendant was making payments to the plaintiffs on the first car loan, she had delayed all payments during the winter months of 1996 until such time as the plaintiffs had returned from their winter months in Florida, without any objections from the plaintiffs. Thus there was a precedent set for deferring payments on a loan from the plaintiffs. Considering the

age of both plaintiffs and their sincere desire that their son's relationship to the defendant could be saved, it is understandable that no request for the loan payment was made by the plaintiffs.

25 I accept the evidence of Susanne Kappler over the evidence of the defendant, Marie France Beaudoin, as it was given in a straightforward fashion and without hesitation. The promissory note, which the defendant originally left unsigned, was, as admitted by the defendant, signed at a later date and used by her. It is clear from the quote given earlier in this judgment and found in the case of Reain v. Reain (supra) that without an agreement, there can be no debt. In this case, whether the defendant wishes to acknowledge the agreement or not, she is faced with an agreement that bears her signature. The explanation for her signature on the promissory note cannot be accepted. To decide otherwise, would mean that the defendant could benefit from a fraud perpetuated upon the Regional Municipality of Ottawa-Carleton in order to obtain 100% subsidy for daycare costs. In the case of Jackson v. Jackson and Jackson *(1960), 26 D.L.R. (2d) 686*, it was made clear that the defendant cannot assert an illegal arrangement in order to rest her defence in this action and I quote the Honourable Mr. Justice Verchere at p. 687:

> Counsel for the plaintiff has contended that the defendants cannot successfully oppose this application because in so doing they must assert and establish an illegal purpose behind their acknowledgment, i.e., to deceive the Income Tax Department and avoid payment of gift tax. He relied on Scheuerman v. Scheuerman (1916), 28 D.L.R. 223, *52 S.C.R. 625*, and especially the remarks of the Chief Justice at p. 224 D.L.R., pp. 627-8 S.C.R., namely:
>
> > I am prepared to hold that a plaintiff is not entitled to come into Court and ask to be relieved of the consequences of his actions done with intent to violate the law, and that though they did not and even could not succeed in such purpose.
> >
> > I think the maxim quoted by Lord Eldon applies in this case and the Court should say, "Let the estate lie, where it falls".
> >
> > And those of Idington, J., at p. 629, namely:
> >
> > But from none of them can I extract authority for the proposition of law that when a man has, out of the sheer necessity to prove anything upon which he can hope to rest the alleged claim of trust, to tell of an illegal purpose as the very basis of his claim, that he may yet be entitled to succeed.

26 Finally, I fail to understand how the defendant could interpret the fact that payments on the promissory note were flexible as meaning that the plaintiffs had made her a gift of $20,000. The fact that the defendant received gratuitous payments on behalf of the grandchildren, while the car loan was in default, is not an argument to characterize the loan as a gift. The plaintiffs were devoted and generous to their grandchildren, from their birth. On the contrary, the defendant should have known that the plaintiffs made a distinction between money contributed for the grandchildren and car loans. No promissory notes were produced for the monies advanced for the grandchildren.

27 Finally, I find that the plaintiffs were extremely generous towards the defendant, Marie France Beaudoin, and in her evidence she acknowledges that fact. However, this does not place Susanne Kappler and Erich Kappler in the position of standing in the shoes of Marie France

Beaudoin's parents. I find it difficult to accept the defence argument that the plaintiffs stood in loco parentis to Marie France Beaudoin who at the relevant time was 27 years of age.

28 Both Erich Kappler and Susanne Kappler convinced me that all loans to their own children had to be repaid. When defence counsel asked both plaintiffs if they knew how much money was advanced to their son, Robert, for his education, both answered by giving a figure without hesitation. Susanne Kappler testified that in the case of Robert Kappler, a ledger sheet had been opened and payments had commenced.

29 I find the defendant was unjustly enriched by the advances made by the plaintiffs. The three elements of unjust enrichment have been met:

(1) There was an enrichment of the recipient defendant,

(2) There was a corresponding deprivation of the donor plaintiffs, and

(3) There was no juristic reason for the enrichment as I have found the money proffered was not a gift but an advance.

The presumption of advancement was not rebutted by the plaintiffs.

30 There will be an order for the repayment by the defendant of the sum of $20,000 to the plaintiffs and interest will run at the rate of interest provided for in the Courts of Justice Act from the date of this judgment until payment. I may be addressed within 7 days of the receipt of this judgment by the parties on the matter of costs. Counsel are not to submit more than two typewritten pages of argument. I might add that if I should consider awarding costs in this matter, should I be requested to do so, I would not consider any higher scale than party/party costs.

LALONDE J.

TAB4

ROBERT J. SHARPE

Good Judgment

Making Judicial Decisions

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While judges should consider the capacity of the legislature to make the proposed change, it is an important feature of our democratic tradition that legislatures avoid getting involved in the intricacies of substantive common law. The common law has always evolved as new cases present new problems, and legislatures have tacitly accepted that changing the common law is a function the courts perform. As Professor Mel Eisenberg argues, legislatures cannot satisfy the demand for "the enrichment of the supply of legal rules," and "in many areas the flexible form of a judicial rule is preferable to the canonical form of a legislative rule."[64] Legislatures tend to be preoccupied with more general issues of public policy, matters such as health, welfare, education, public safety, infrastructure, and budget. Law reform commissions with a mandate to study and make recommendations for change in specific areas of law can fill this void, but in most jurisdictions, the resources available to these bodies have been significantly curtailed. The practical reality is that legislatures rarely engage with the intricacies of the common law, so if the courts do not act, the law will remain static.

Law-Making and the Judicial Hierarchy

The place the judge occupies in the hierarchy of courts affects the judge's law-making authority. Lower courts are bound by the pronouncements of higher courts, and there is a tendency when discussing judicial law-making to focus on appellate courts. I think this focus is misguided and underestimates the significant law-making powers of trial judges.

The first reason for this is that trial judges control the facts, and the facts are what drive change in common law. Trial judges become immersed in the facts and the details of each case they hear. They see the parties and hear the witnesses over the days, weeks, and sometimes months it takes for the trial to unfold. Their close involvement with the facts and details of the case provides the perspective needed to decide what justice requires. Trial judges are required to apply the law as laid down by appellate courts, but their authority to find the facts to which the governing legal rules and principles apply carries with it significant law-making powers. If the trial judge finds that the facts of the case are novel and do not fall within the reach of established precedent, the trial judge has the capacity to move the law in a different direction. The common law tradition depends upon this

highly fact-sensitive process. The facts and circumstances of every case are closely scrutinized at the trial level and, as circumstances change and society evolves, the demands of justice influence trial judges to shape the law, slowly but surely, this way or that.[65]

The trial judge's decision will be subject to review on appeal, and that certainly operates as a constraint on the trial judge's law-making power. On the other hand, trial judges enjoy a measure of freedom not available to appellate judges. Their liberty flows not only from the authority to find the facts but also from the reality that as a trial judge's pronouncements will not bind other judges,[66] they can be less concerned about the broader consequences of their decisions. I certainly do not mean to suggest that trial judges should be cavalier or careless about their pronouncements. But they are at greater liberty than appellate judges to preoccupy themselves with the demands of justice in the particular case they are deciding. Appellate judges have additional concerns that arise from the binding nature of their decisions. All judges at the same level and below the appellate judge in the judicial hierarchy will be obligated to follow what the appellate judge has stated as the law. Appellate judges must strive to do justice in the particular case, but they have significantly more reason to worry about the consequences of the precedent they establish.

There is another marked shift as one moves from an intermediate appellate court to the Supreme Court of Canada. Intermediate appellate judges are immersed in the nitty-gritty of deciding a large volume of cases on a wide range of subjects. They have virtually no control over their docket, as most litigants enjoy a right of appeal. As mentioned in chapter 2, most of the cases heard by intermediate appellate courts fall into the "error correction" category and involve no issues of precedential value. The mindset of an intermediate appellate judge is inevitably affected by the experience of deciding many cases, most of which do not involve jurisprudentially significant issues. This encourages a cautious, minimalist, and incremental approach.

Things are quite different at the Supreme Court of Canada. That court controls its own docket. The leave to appeal process allows the Supreme Court to pick and choose the cases it hears on the basis of their national importance. The Supreme Court can defer hearing an issue until it has been dealt with by more than one provincial court of appeal. This allows the issue to ripen on the basis of a variety of facts and a variety of trial and appellate decisions. The Supreme

Court hears very few "error correction" appeals. Its task is to decide sixty-five to eighty important cases each year that raise issues of legal importance that transcend the immediate interests of the litigants. Virtually every case the Supreme Court decides has precedential value.

I suggest that a comparison of intermediate appellate judgments and the judgments of the Supreme Court of Canada reveals that the judge's approach to the challenge of judicial law-making is influenced by day-to-day routine. A judge who decides many cases, most of which are not precedent-setting, will think of judging differently from the judge who, as one of nine, deals only with cases of national importance. Intermediate appellate judgments tend to be more focused on the facts of the case, and the legal pronouncements the judges make tend to be more minimalist in nature, deciding only what is necessary to deal with the case at bar. Reading Supreme Court judgments, one regularly encounters broad general statements of principle that extend beyond the confines of the actual dispute between the parties. The temptation to settle entire areas of the law is often present and sometimes irresistible, but there are perils to be avoided. The more detached the pronouncement is from the facts of the case and the more the court deviates from established common law method, greater is the risk that the pronouncement will fail to anticipate facts or circumstances not before the court and will have unintended effects.

Now of course intermediate appellate courts do decide many precedent-setting appeals, and they do have a significant law-making role. We hear appeals raising issues of broad jurisprudential significance that require us to make pronouncements on important legal issues. Although we do not have the final word, many of our jurisprudentially significant decisions are not appealed, or leave to appeal is denied. In these cases, our role is not unlike that of the Supreme Court.

The question, then, of whether and to what extent judges make law depends on a number of factors, not the least of which is the judge's place in the court hierarchy. As one moves up the hierarchy of trial, intermediate appeal and final appeal, one moves from the specific to the general. The trial courts are the pulse of the entire system. As I have explained, trial courts are preoccupied with the facts and the justice of the specific case. Intermediate appeal courts have a more general perspective. The trial judge's case-specific findings

and perceptions of what justice demands are tested at the intermediate level of appeal for legal integrity and reliability. The task of the intermediate appellate court is to ensure that trial judgments are free from legal error and that the law and the legal process are responding appropriately to the disputes that arise. The apex court has general oversight over the entire system. It is charged with settling the most contentious issues of law, and by limiting its attention to cases of that nature it is bound to have a significant law-making role.

Conclusion

Judicial law-making is a fundamental aspect of the common law tradition. That does not mean that judges can make law as they please. Judges decide cases, and they must respect the role of the legislature as the primary source for legal change. They must also respect the limits imposed by their place in the judicial hierarchy. But judges also have a duty to maintain the integrity of the law. Their decisions should aim to enhance the law's clarity and its consistency with contemporary conditions and needs. The judicial maintenance function of "keeping the law in good shape" sometimes involves changing the law. If the judge is able to support such a change on the basis of a legally manageable and workable principle that emerges from the pattern of past decisions, legislative enactments, or *Charter* values, the judge is making law, not making up law. Changes that make the law a more complete and coherent whole fall within the judicial function.

weakens the force of precedent and significantly diminishes the capacity of appellate courts, including the Supreme Court of Canada, to have the final word on the constitutionality of legislation.

I find the proposition that trial judges effectively have the last say on the constitutionality of legislation troubling and problematic. We could well have different trial judges in different provinces coming to opposite conclusions on the constitutionality of legislation based upon expert opinion evidence. It is quite conceivable that both findings could be reasonable and effectively immune to appellate review. How would the Supreme Court deal with conflicting but reasonable findings by different trial judges in different provinces on the constitutionality of the same legislation?[89]

ARE DECISIONS THE SUPREME COURT IS LIKELY TO OVERRULE BINDING ON LOWER COURTS?

If the Supreme Court is increasingly prepared to depart from its own prior decisions, what does a trial judge or intermediate appellate court do when faced with a Supreme Court decision that it thinks the Supreme Court itself is likely to overrule? Do the lower courts have to obey the prior ruling of the Supreme Court and leave it to the litigants to take the case higher, or is it permissible for the lower court to predict the outcome at the Supreme Court and rule accordingly?

In 2011, the Federal Court of Appeal was confronted with a much criticized 1978 decision of the Supreme Court interpreting a provision of the *Income Tax Act*. Another panel of the Federal Court of Appeal had carefully considered the 1978 Supreme Court decision in 2006, and, in light of the criticism the 1978 decision had attracted as well as the practical difficulties it had caused, the 2006 panel declined to follow it.[90] The 2011 panel decided that it was bound to follow its own decision and not that of the Supreme Court. The Supreme Court of Canada held that the Federal Court was wrong, both in 2006 and in 2011, not to follow the problematic 1978 Supreme Court decision.[91] Writing for the Supreme Court, Rothstein J said that the Federal Court of Appeal should have followed the 1978 decision, providing reasons explaining why the 1978 decision was problematic. It was for the Supreme Court to overrule itself, and that is what the court proceeded to do.

However, as noted above, the decisions in *Bedford*, *Carter*, and *Saskatchewan Federation of Labour* indicate a very different approach in *Charter* cases. The Supreme Court appears to have opened the door

to permit trial judges to refuse to follow earlier Supreme Court *Charter* decisions where there have been significant changes in fact or law. Not only is the Supreme Court prepared to overrule its own rulings, the court places such a high premium on "getting it right" in *Charter* cases that it is prepared to allow, if not encourage, lower courts to depart from the court's earlier *Charter* pronouncements if either or both the factual and legal landscape have changed. The Supreme Court retains the last word, but even that has been attenuated by the holding in *Bedford* and *Carter* that findings on social and legislative facts are entitled to deference on appeal.

Conclusion

Precedent is a foundational principle of the common law. But the weight attached to precedent cannot be reduced to a set of mechanical rules. It is the starting point to legal analysis. For most disputes, precedent will be decisive. But the capacity of the common law to evolve is inconsistent with rigid, unbending adherence to past decisions. We must keep in mind that the ultimate purpose of precedent is to foster certainty, predictability, and coherence in the law. Blind adherence to *stare decisis* may not only perpetuate an unjust rule but may also conflict with the very purpose of the doctrine itself.

The doctrine of precedent is a prime example of the kind of disciplined decision-making I discussed in chapter 6. It is easy to follow precedents with which we agree. The hard part of precedent kicks in when we disagree with the prior ruling or with the result it produces in the case at hand, but we know that we must allow the values of certainty and predictability to prevail.

However, the doctrine of precedent is also a prime example of the principled approach to legal reasoning that I discussed in chapter 5. Those principles recognize that certainty and predictability exact the price of injustice when circumstances unforeseen by past decisions arise. This creates a tension between, on the one hand, the certainty and predictability we need to satisfy the rule of law and achieve systemic justice, and, on the other hand, our perfectly proper concern over achieving justice in the individual cases we decide. And, in the words of Lord Denning, a great English judge notable for his impatience with what he regarded as the dead hand of the past, "The doctrine of precedent does not compel your Lordships to follow the wrong path until you fall over the edge of the cliff."[92]

As we edge towards that cliff, we have various tools at our disposal. We may be able to distinguish the precedent, read it narrowly, or find exceptions or qualifications to restrict its reach. Over time, this may so undermine the precedent that it becomes unstable, and it is better, in the name of certainty and predictability – the very goals precedent is meant to serve – that it be jettisoned. Sometimes we realize that the precedent was simply wrongly decided or that it was the product of another era when very different conditions prevailed. But when we are tempted to jettison a precedent to avoid the injustice side of the cliff, we must remain mindful to avoid falling off the other side into uncertainty and *ad hoc* decision-making.

Neil Duxbury, an English legal scholar argues, "The common law requires not an unassailable but a strong rebuttable presumption that earlier decisions be followed."[93] I suggest that the "strong rebuttable presumption" approach to precedent accurately reflects the way intermediate appellate courts in Canada use precedent. When it comes to apex courts, some scholars argue that the presumption should shift. Decisions now thought to be wrong should be overruled, "unless their retention can be justified in the circumstances by overriding *stare decisis* values."[94] That shift in presumption has not been formally accepted by our Supreme Court, nor, so far as I am aware, by any other common law apex court. However, as the number of instances in which the Supreme Court reverses itself rises, it may be that the shift in presumption accurately reflects the direction that precedent has taken in the modern era.

TAB5

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assumption in this area seems again to be that it should not do so[1295] unless the agent's knowledge can be said to have been "bought", or he is an "agent to know",[1296] as where a shipmaster is engaged who has prior knowledge of the ship. It may however be that too much significance has been attached to this limit on the acquisition of knowledge, which derives largely from the identification theory. In so far as the solicitor cases can be classed here, some certainly have involved the attribution of knowledge acquired outside the agency: for in land law there can be a positive duty to initiate inquiries not unlike that required of proposers for insurance.[1297] However, in this area the matter is in England and Wales now affected by statute.[1298]

8–212 **Duty to communicate.** Hoffmann L.J. finally rejected an argument, for which there are many supporting dicta, that where an agent had a duty to communicate information, knowledge of it might be imputed to his principal.[1299] He admitted that there were situations in which a weak presumption that information had been passed on might be applied, but no more, and treated the reasoning as primarily applicable to notification cases. It is submitted that this is correct, for the "passing on information" argument is in the last resort as weak as, or perhaps weaker than, the identification of principal and agent argument, and is rightly abandoned. And where the agent is subject to a fiduciary duty to another *not* to disclose information, knowledge cannot be imputed.[1300]

8–213 **Rule (4). Fraud of agent.** Rule (4) refers to what is usually called the "fraud exception" and is often attributed to *Re Hampshire Land Co.*[1301] It is clear, on the one hand, that the mere fact that the agent does not communicate his knowledge or information which he has, from fraudulent or other motives, is not sufficient to negative notice to the principal[1302]: at the other extreme it is clear also that where the third party had actual knowledge that the agent would not pass information on (e.g. because he is a party to the fraud together with the agent), the principal will not be treated as having notice.[1303] It seems that the second is the only case where the agent's fraud will prevent a *notification* being effective.[1304] Both *Restatements* also recognise the exception, though not without

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[1295] See the *Permanent Trustee* case, n. 1286 above, at [87].

[1296] See cases cited above, n. 1285.

[1297] e.g. *Rolland v. Hart* (1871) L.R. 6 Ch.App. 678, Illustration 8.

[1298] See below, para. 8–215.

[1299] [1994] 2 All E.R. at 703–704; Watts, n. 1270 above.

[1300] See *Restatement, Third*, § 5.03(b).

[1301] [1896] 2 Ch. 743. See the case discussed by Watts (2001) 117 L.Q.R. 300 at 319–320. See further Watts, in *Unjust Enrichment in Commercial Law* (Degeling and Edelman eds, 2008), Chap. 21 where *Hampshire Land* is argued to be correctly decided for the wrong reasons. The exception first manifested itself in *Kennedy v. Green* (1834) 3 My. & K. 699.

[1302] *Atterbury v. Wallis* (1856) 25 L.J.Ch. 792; and see Illustrations: *Bunbury v. Hibernian Bank* [1908] 1 I.R. 261. See too *Lebon v. Aqua Salt Co. Ltd* [2009] UKPC 2; [2009] 1 B.C.L.C. 549 at [26].

[1303] *Sharpe v. Foy* (1868) L.R. 4 Ch.App. 35; *Re Fitzroy Bessemer Steel Co. Ltd* (1884) 50 L.T. 144.

[1304] See Comment to Article 94.

considerable difficulties of formulation.[1305] In knowledge cases, however, any presumption that information will be passed on is said to be nullified by proof that the agent was defrauding the principal in that transaction, whether or not the third party knew this. It can in such a case be said that there was a moral certainty that the information would not be communicated,[1306] or that communication would require disclosure of the very fraud being practised upon the agent by the principal,[1307] or that the agent was not acting for the principal when he received the information.[1308] The mere suppression of a document is however not sufficient fraud.[1309]

> "It must be made out that distinct fraud was intended in the very transaction, so as to make it necessary for the [agent] to conceal the fact from his [principal] in order to defraud him."[1310]

The exception has been found inapplicable where a company's sole shareholder and controller is responsible for, or aware of, the fraud.[1311]

But the existence of any general fraud exception is open to question.[1312] It can be said first that the deployment of the exception as a defence to property-based or restitutionary claims is not supported by the weight of authority,[1313] nor is it consistent in that context with the principles of vicarious liability.[1314] Secondly,

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[1305] *Restatement, Third*, § 5.04: "Nevertheless, notice is imputed (a) when necessary to protect the rights of a third party who dealt with the principal in good faith; or (b) when the principal has ratified or knowingly retained a benefit from the agent's action"; *Restatement, Second*, § 282. Both of these go beyond fraud to cases where the agent simply acts adversely to the principal.

[1306] *Thompson v. Cartwright* (1863) 33 Beav. 178 at 185 (affd (1863) 2 De G.J. & S. 10).

[1307] *Waldy v. Gray* (1875) L.R. 20 Eq. 238 at 251–252; *Kennedy v. Green* (1834) 3 My. & K. 699; *Re European Bank* (1870) L.R. 5 Ch.App. 358; *Re Hampshire Land Co.* [1891] 2 Ch. 743; *Houghton & Co. v. Nothard, Lowe & Wills* [1928] A.C. 1; *Kwei Tek Chao v. British Traders & Shippers Ltd* [1954] 2 Q.B. 459; *Stoneleigh Finance Ltd v. Phillips* [1965] 2 Q.B. 537; *United Dominions Trust (Ireland) Ltd v. Shannon Caravans Ltd* [1976] I.R. 225; *Belmont Finance Corp. v. Williams Furniture Ltd* [1979] Ch. 250; *Wall v. New Ireland Assurance Co. Ltd* [1965] I.R. 385; *Cricklewood Holdings Ltd v. C.V. Quigley & Sons Nominees Ltd* [1992] 1 N.Z.L.R. 463; *Group Josi Re v. Walbrook Insurance Co. Ltd* [1996] 1 Lloyd's Rep. 345; *P.C.W. Syndicates v. P.C.W. Reinsurers*, n. 1287 above, 241; *Arab Bank Plc v. Zurich Insurance Co.* [1999] 1 Lloyd's Rep. 262. But *cf. Moore Stephens v. Stone & Rolls Ltd* [2008] EWCA Civ 644; [2009] 1 A.C. 1391; [2008] 2 Lloyd's Rep. 319; [2008] 2 B.C.L.C. 461 at [72], doubting *Arab Bank Plc v. Zurich* on this point (upheld [2009] 1 A.C. 1391).

[1308] *Espin v. Pemberton* (1859) 3 De G. & J. 547 at 555; *Cave v. Cave* (1880) 15 Ch.D. 639 at 644; *Beach Petroleum NL v. Johnson* (1993) 115 A.L.R. 411 at [22.34] (directors' acts "totally in fraud of the company").

[1309] *Atterbury v. Wallis* (1856) 25 L.J.Ch. 792.

[1310] *Rolland v. Hart* (1871) L.R. 6 Ch.App. 678 at 682–683, *per* Lord Hatherley L.C.

[1311] *Stone & Rolls Ltd v. Moore Stephens Ltd* [2009] UKHL 39; [2009] 1 A.C. 1391 (noted byWatts (2010) 126 L.Q.R. 14; Halpern (2010) 73 M.L.R. 487).

[1312] See (2001) 117 L.Q.R. 300.

[1313] This point is developed by an examination of all the main cases. See too *Nathan v. Dollars & Sense Ltd* [2008] 2 N.Z.L.R. 557 (noted by Watts (2008) 124 L.Q.R. 529); and *Permanent Trustee Co. Ltd v. O'Donnell* [2009] NSWSC 902 at [369].

[1314] See *Doe d. Willis v. Martin* (1790) 4 T.R. 39 ("without imputing any fraud to Martin, and indeed it is negatived by the verdict, the maxim, that the principal is civilly responsible for the acts of his agent, universally prevails both in Courts of Law and Equity"); *Lloyd v. Grace, Smith & Co.* [1912] A.C. 716.

it is not surprising that the use of such an exception has been deployed to protect claimants against a defendant's arguments (for example, when sued for knowing assistance to the fraud of the claimant's agent) that the claimant is deemed to know of the fraud of its own agents,[1315] and on that account can be assumed to have condoned the wrong (by estoppel or ratification). Such arguments by defendants, though hazarded from time to time, are plainly without merit. However, in such situations imputation has no reason to operate. The rules of imputation do not exist in a state of nature, such that some reason has to be found to disapply them. Whether knowledge is imputed in law turns on the question to be addressed. Hence, a fraud exception is superfluous in these situations. Indeed, the irrelevance of imputation to cases where a principal is pursuing an agent, and implicated third parties, as a result of breach of duty by the agent to the principal is not confined to fraudulent breaches of duty. Were the principal deemed to possess the agent's knowledge of his own breaches of duty, and thereby to have condoned them, the principal could never successfully vindicate his rights.[1316]

Further confusion has been created in this area by the repeated failure to differentiate cases concerned with the scope of contractual obligations, inter partes, from cases in a delictual or restitutionary context. It may well be appropriate in particular contractual contexts not to impute to a party the knowledge (or conduct) of a fraudulent agent,[1317] and indeed in some cases it may be inappropriate to impute knowledge even where the agent's conduct is not fraudulent, or if fraudulent the conduct does not involve a fraud being practised on the principal.[1318] Such cases are always context specific, and are strictly of no application outside the contractual context.[1319]

8–214 **Agents of companies.** These lines of reasoning may obviously cause special difficulty in the case of agents of companies,[1320] for there may be situations where the information required by one agent is available elsewhere in the company; it may perhaps also have been acquired at an earlier time. In some such cases it may, because of a time gap or a gap between departments (for example, as to renewals of insurance and new proposals), not be appropriate to attribute the

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[1315] As in *Houghton v. Nothard, Lowe & Wills* [1928] A.C. 1; and *Belmont Finance Corp. v. Williams Furniture Ltd* [1979] Ch. 250; *Nationwide Building Society v. Dunlop Haywards Ltd* [2007] EWHC 1374 (Comm) at [75]; *Moore Stephens v. Stone & Rolls Ltd* [2008] EWCA Civ 644; [2009] 1 A.C. 1391; [2008] 2 Lloyd's Rep. 319; [2008] 2 B.C.L.C. 461 at [71]–[72] (affd [2009] UKHL 39; [2009] 1 A.C. 1391); *Soods Solicitors v. Dormer* [2010] EWHC 502 (QB).

[1316] See *Stone & Rolls Ltd v. Moore Stephens Ltd* [2009] UKHL 39; [2009] 3 W.L.R. 455 at [198]; and Watts (2001) 117 L.Q.R. 300 at 316–318.

[1317] Cases of this sort include *P.C.W. Syndicates v. P.C.W. Reinsurers* [1996] 1 Lloyd's Rep. 241; *Group Josi Re v. Walbrook Insurance Co. Ltd* [1996] 1 Lloyd's Rep. 345.

[1318] See, e.g. *Arab Bank Plc v. Zurich Insurance Co.* [1999] 1 Lloyd's Rep. 262. But *cf. Moore Stephens v. Stone & Rolls Ltd* [2008] EWCA Civ 644; [2008] 3 W.L.R. 1146; [2008] 2 Lloyd's Rep. 319; [2008] 2 B.C.L.C. 461 at [72] (affd [2009] UKHL 39; [2009] 1 A.C. 1391). See too *S.A. d'Intermediaries Luxembourgeois v. Farex Gie* [1995] L.R.L.R. 116, and the explanation of the case in (2001) 117 L.Q.R. 300 at 329.

[1319] For recognition of this, see *In re Bank of Credit and Commerce International S.A. (No. 15); Morris v. Bank of India* [2005] EWCA Civ 693; [2005] 2 B.C.L.C. 328 at [124].

[1320] For application of the basic rules to companies see Illustrations 9, 12, 13, 14.

TAB6

ESSENTIALS OF
CANADIAN LAW

BANKRUPTCY AND INSOLVENCY LAW

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- a federal exemption that shelters registered retirement savings plans (RRSPs) from the claims of creditors;
- reformulated provisions governing preferences and transactions at undervalue that allow a trustee to impugn pre-bankruptcy transactions;
- changes to the rules that govern discharge of a bankrupt; and
- a new set of cross-border insolvency provisions based on the UNCITRAL Model Law on Cross-Border Insolvency.

This incremental approach to the reform of bankruptcy law has its drawbacks. Although some aspects of the bankruptcy statute are modernized, other features have become progressively obsolete and outdated. At some point a thorough revision of the entire statute will be required.[47]

B. THE OBJECTIVES OF BANKRUPTCY LAW

The Supreme Court of Canada has stated that the purpose and object of bankruptcy law is to (1) distribute equitably the assets of the debtor and (2) permit the rehabilitation of the debtor as a citizen.[48] This provides a very useful starting point for examining the objectives of bankruptcy law. The first objective is to create a collective process through which the assets of the debtor are liquidated, the claims of the creditors are assessed, and the proceeds of the liquidated assets are distributed to the creditors. The second objective is to afford the debtor a fresh start when it is appropriate to do so. The entire history of bankruptcy law reform reveals a third objective: the prevention of fraud and abuse of the bankruptcy system, the promotion of commercial morality, and the protection of the credit system.[49]

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47 R Wood & D Bryan, "Creeping Statutory Obsolescence in Bankruptcy Law" (2014) 3 *Journal of the Insolvency Institute of Canada* 1.

48 *Industrial Acceptance Corp v Lalonde*, [1952] 2 SCR 109; *Vachon v Canada (Employment & Immigration Commission)*, [1985] 2 SCR 417.

49 The three foundational objectives of bankruptcy law have been recognized for over two hundred years. Basil Montagu commented in 1805 that the "laws of bankruptcy are a system of laws constructed by statute for the benefit of trade (a), to secure an equal and speedy distribution of an insolvent or improvident trader's property amongst all his creditors (b), to discharge the unfortunate trader from his debts (c), and to suppress fraud." See B Montagu, *A Digest of the Bankrupt Laws*, vol 1 (London: Butterworth, 1805–7) at 1.

1) Liquidation and Distribution of the Debtor's Assets

The insolvency of a debtor typically means that there will not be sufficient assets to satisfy the claims of all the creditors. Bankruptcy is a legal process that seeks to maximize the recovery of the creditors as a group. In a world of no bankruptcy, some of the creditors — those who are able to grab assets before the other creditors are able to do so — are better off. But the creditors as a whole are worse off. There are two reasons why this is the case. First, in the absence of bankruptcy, each creditor must incur the cost of obtaining judgment and of enforcing it. This produces duplication in adjudication and enforcement costs that might be reduced if there was a collective liquidation proceeding carried out on behalf of all the creditors. Second, under a regime where the ranking among creditors is determined by a principle of first come, first served, each creditor will have a strong incentive to rush in and grab the assets even though a more orderly liquidation of assets would produce a higher return for all the creditors as a group. Bankruptcy law protects the integrity of a collective liquidation proceeding by imposing an automatic stay of proceedings that pre-empts the enforcement remedies of the creditors. In doing so, it provides "a way to override the creditors' pursuit of their own remedies and to make them work together."[50]

A collective liquidation proceeding requires a process for the assessment of creditors' claims and the distribution of assets to creditors. Creditors do not invoke the usual civil process for the adjudication of their claims. Instead, an administrative rather than a judicial process is created under which a trustee in bankruptcy assesses and values their claims. This ensures that the claims can be processed more quickly and cheaply than would otherwise be the case. Bankruptcy law also provides rules for the ranking of the claims of creditors. Historically, bankruptcy law has adopted a *pro rata* sharing principle among creditors. This has sometimes been said to form one of the foundational principles of bankruptcy law. The pre-eminence of this principle, however, is undercut by the recognition of a number of exceptions under which certain creditors, such as preferred creditors, are given a higher ranking. Rather than a fundamental principle, *pro rata* sharing might better be regarded as a sensible rule for ranking among claims of the same

50 T Jackson, *The Logic and Limits of Bankruptcy Law* (Cambridge, MA: Harvard University Press, 1986) at 17.

type where there is no convincing reason for preferring one claim over another.[51]

2) Rehabilitation of the Individual Debtor

The second objective of bankruptcy law looks to the economic rehabilitation of the debtor. This objective is not engaged if the debtor is an artificial entity, such as a corporation. Bankruptcy proceedings in respect of corporations and other artificial entities are mostly concerned with issues of liquidation and distribution. It is in respect of individuals that the second objective of bankruptcy law comes into play. Indeed, in many cases of consumer bankruptcy, the debtor owns very few assets. In these "no asset" cases, debtor rehabilitation is the primary objective that is being pursued.

The rehabilitation of the debtor is accomplished through a number of means, the most important of which is the ability of a debtor to obtain a bankruptcy discharge. Because of illness, loss of employment, or other cause, a debtor may be left in a position where there is no reasonable prospect of repayment of all debts. The bankruptcy discharge gives the honest but unfortunate debtor the ability to be freed from the crushing burden of debt that cannot be met. This gives the debtor a fresh start that will permit his or her reintegration into society. Discharge releases the debtor from the claims of creditors that were in existence at the time of the bankruptcy. The creditors may resort to the debtor's assets, including after-acquired assets, up until the date of the discharge. Assets acquired after that date are not available to the creditors.

The bankruptcy discharge is not the only means through which bankruptcy law seeks to foster the economic rehabilitation of the debtor. Bankruptcy law also pursues this objective by ensuring that the debtor is not stripped of all assets during the course of the bankruptcy but is permitted to retain sufficient assets to provide the debtor and his or her family with food, accommodation, and other necessaries of life. Bankruptcy law does so through its treatment of exempt property and through the surplus income regime that covers the post-bankruptcy, pre-discharge earnings of the debtor. Bankruptcy law also pursues the objective of debtor rehabilitation through mandatory credit counselling that attempts to reduce the occurrence of repeat bankruptcies.

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51 See R Mokal, "Priority as Pathology: The *Pari Passu* Myth" (2001) 60 *Cambridge Law Journal* 581.

3) Enhancing Commercial Morality and Protecting the Credit System

The third objective of bankruptcy law is premised on the idea that bankruptcy is not simply a private matter between creditors and debtors but a subject where there are legitimate matters of public interest at stake.[52] Bankruptcy law seeks to protect commercial morality by preventing fraudulent debtors from abusing the credit system. Equally, creditors and trustees in bankruptcy are prevented from engaging in practices that abuse the bankruptcy system or undermine public trust in the credit economy. The Supreme Court of Canada, in an early decision, stated although one of the objects of bankruptcy law is to secure a speedy and equitable distribution of the bankrupt's assets, it is not confined to this purpose and also has as its goals the prevention of fraud and bad faith.[53] It therefore "acts as a preventative to fraud and collusion on the one hand, and as an encouragement to honest and cautious trading on the other."[54]

Bankruptcy law imposes a set of bankruptcy offences that can be used to discipline persons who transgress the norms of commercial morality. It also provides for a system for the licensing of trustees to force out those who are fraudulent or incompetent. Additionally, bankruptcy law possesses an investigatory apparatus that permits public officials to investigate complaints, and it recognizes the importance of an information-gathering function concerning the causes of insolvencies and the operation of the various insolvency regimes. The ability to compile insolvency statistics is now regarded as a crucial element in effective bankruptcy law reform.

The integrity of the bankruptcy process can be seriously weakened if the debtor's assets are dissipated before the bankruptcy is invoked. This can occur if a debtor transfers assets to a third party and does not receive their fair value in exchange. Such payments and transfers have the effect of undermining the ranking of claims established by the insolvency regime. This is the problem of the fraudulent preference, which is not unique to bankruptcy law and is liable to arise whenever creditors seek recovery from the debtor's assets. Bankruptcy law provides rules that allow the creditors to recover value that has been transferred to third parties to address this problem. In essence, these

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52 See *Tassé Report*, above note 35 at 87–88; *Cork Report*, above note 18 at 62–63. See also *Re Posner* (1960), 3 CBR (NS) 49 (Man QB).

53 *Shields v Peak* (1883), 8 SCR 579.

54 *Ibid* at 588, Ritchie CJ.