File No. 40166

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

B E T W E E N :

JOHN AQUINO, 2304288 ONTARIO INC., MARCO CARUSO,
GIUSEPPE ANASTASIO a.k.a. Joe Ana AND LUCIA COCCIA a.k.a. Lucia Canderle

Appellants (Appellants)

- and -

ERNST & YOUNG INC., in its capacity as Court-Appointed Monitor
of Bondfield 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
ERNST & YOUNG INC., IN ITS CAPACITY AS COURT APPOINTED MONITOR OF BONDFIELD CONSTRUCTION COMPANY LIMITED ON APPEAL
(Rule 44 of the *Rules of Supreme Court of Canada*)

VOLUME II

CASSELS BROCK & BLACKWELL LLP
Suite 2100, Scotia Plaza
40 King Street West
Toronto, ON   M5H 3C2

Alan Merskey
Tel: 416.860.2948
amerskey@cassels.com

NORTON ROSE FULBRIGHT CANADA LLP
Barristers and Solicitors
222 Bay Street, Suite 3000
Toronto ON M5K 1E7

Evan Cobb
Tel: 416.216.1929
evan.cobb@nortonrosefulbright.com

Stephen Taylor
Tel: 416.216.2436
stephen.taylor@nortonrosefulbright.com

Counsel for the Respondent, Ernst & Young Inc., in its capacity as Court-Appointed Monitor of Bondfield Construction Company Limited

LAW OFFICE OF TERRY CORSIANOS
1595 16th Avenue, Suite 301
Richmond Hill, ON L4B 3N9

Terry Corsianos
Tel: 905.709.7463
tcorsianos@corsianoslaw.com

CORSIANOS LEE
Barristers & Solicitors
3800 Steeles Avenue east, Suite 203W
Vaughan, ON   L4L 4G9

George Corsianos
Tel: 905.370.1095
gcorsianos@cl-law.ca

Counsel for the Appellants

SUPREME LAW GROUP
1800 - 275 Slater Street
Ottawa, ON K1P 5H9

Moira Dillon
Tel: 613.691.1224
mdillon@supremelawgroup.ca

Agent for Counsel for the Appellants

TORYS LLP
79 Wellington St. W., 30th Floor
Box 270, TD South Tower
Toronto, ON M5K 1N2

Jeremy Opolsky
Tel: 416.865.8117
jopolsky@torys.com

Craig Gilchrist
Tel: 416.865.7629
cgilchrist@torys.com

Alex Bogach
Tel: 416.865.7379
abogach@torys.com

Lawyers for the Respondent, KSV Restructuring Inc., in its capacity as Trustee-in-Bankruptcy of 1033803 Ontario Inc. and 1087507 Ontario Limited

NORTON ROSE FULBRIGHT CANADA LLP
45 O'Connor Street, Suite 1500
Ottawa, ON K1P 1A4

Jean-Simon Schoenholz
Tel: 613.780.1537
jean-simon.schoenholz@nortonrosefulbright.com

Agent for Counsel for the Respondent, KSV Restructuring Inc., in its capacity as Trustee-in-Bankruptcy of 1033803 Ontario Inc. and 1087507 Ontario Limited

MINISTRY OF THE ATTORNEY GENERAL
Crown Law Office - Civil
720 Bay Street, 8th Floor
Toronto, ON M7A 2S9

Dona Salmon
Tel: 647.213.0021

Email: dona.salmon@ontario.ca

Jennifer Boyczuk
Tel: 416.909.6673
Email: jennifer.boyczuk2@ontario.ca

Counsel for the Intervener,
The Attorney General for Ontario

JURISTES POWER LAW
50 O'Connor Street, Suite 1313
Ottawa, ON K1P 6L2

Maxine Vincelette
Tel: 613.702.5573
Email: mvincelette@juristespower.ca

Agent for Counsel for the Intervener,
The Attorney General for Ontario

DAVIES WARD PHILLIPS & VINEBERG LLP
155 Wellington Street West
Toronto, ON M5V 3J7

Natasha MacParland
Tel: 416.863.5567
nmacparland@dwpv.com
Chanakya A. Sethi
Tel: 416.863.5516
csethi@dwpv.com
Rui Gao
Tel: 416.367.7613
rgao@dwpv.com

Counsel for the Intervener,
Insolvency Institute of Canada

MICHAEL J. SOBKIN
331 Somerset Street West
Ottawa, ON K2P 0J8

Michael J. Sobkin
Tel: 613.282.1712
msobkin@sympatico.ca

Agent for Counsel for the Intervener,
Insolvency Institute of Canada

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Bill C-55, Statute c.47 and Beyond

edited by

Stephanie Ben-Ishai

and

Anthony Duggan

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Chapter 1

INTRODUCTION

Anthony Duggan and Stephanie Ben-Ishai*

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I. THE RECENT HISTORY OF CANADIAN BANKRUPTCY LAW REFORM[1]

The BIA[2] and CCAA[3] are the two main bankruptcy and insolvency statutes in Canada and they are the focus of this book.[4] Canada's first insolvency statute was the *Insolvent Act* of 1869,[5] which provided for voluntary and compulsory bankruptcies and compositions, but was limited to traders.[6] The 1869 statute was

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* The authors wish to thank Tom Telfer for his helpful comments.

1 The discussion under this heading draws heavily on Jacob S. Ziegel, Anthony J. Duggan & Thomas G.W. Telfer, *Canadian Bankruptcy and Insolvency Law: Cases, Text and Materials* (Toronto: Emond Montgomery Publications Limited, 2003) at 17-20 (written by Jacob Ziegel) and Jacob Ziegel *et al., Submission on Bill C-55 2005: The Wage Earner Protection Program Act and Amendments to the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act presented to the House of Commons Standing Committee on Industry, Natural Resources, Development and Technology* (November 2005), Part III A 1. See also the Senate Report, c. 1 (see Abbreviations, p. xxxvii above). For an historical overview up to 1970, see Consumer and Corporate Affairs, *Bankruptcy and Insolvency: Report of the Study Committee on Bankruptcy and Insolvency Legislation* (Ottawa: Information Canada, 1970), ss. 1.1-1.3. [Tassé Committee Report].

2 See Abbreviations, p. xxxvii above.

3 See Abbreviations, p. xxxvii above.

4 Other relevant federal statutes include the *Winding-up and Restructuring Act*, R.S.C. 1985, c. W-11, and the *Farm Debt Mediation Act*, S.C. 1997, c. 21. Relevant provincial legislation includes the assignments and preferences Acts and, in some provinces, the fraudulent conveyance statutes.

5 32-33 Vic., Can. S. 1869, c. 16.

6 Senate Report, *supra* note 1 at 1. The *Insolvent Act* of 1869 was enacted as a temporary measure with the aim of providing for its own expiry after four years: s. 155. However, the 1869 Act was extended twice by 36 Vic., Can. S. 1873, c. 42 and 37 Vic., Can. S. 1874, c. 46. The 1875 Act had the effect of continuing the 1869 Act to 1 September 1875 when it was repealed and replaced by the *Insolvent Act* of 1875: s. 149.

succeeded by the *Insolvent Act* of 1875,[7] which was also limited to traders and, furthermore, provided only for compulsory bankruptcies. However, the *Insolvent Act* of 1875 was repealed in 1880[8] and was not replaced until the enactment of the *Bankruptcy Act* in 1919.[9] The 1919 statute was re-enacted, with some amendments, in the *Bankruptcy Act 1949*.[10] The current BIA comprises the text of the 1949 statute, as amended, the most important amendments occurring in 1992 and 1997. The CCAA was enacted in 1933 as a depression measure.[11] Thereafter it fell into disuse until the 1980s when, augmented by a process of creative judicial interpretation, it became the vehicle of choice for large-scale commercial reorganizations. The CCAA has been amended several times, most significantly in 1997.

The Tassé Committee, reporting in 1970, recommended a complete overhaul of the then *Bankruptcy Act*. Between 1975 and 1984, six attempts were made to enact the committee's recommendations, all unsuccessful. Thereafter, the government discarded its ambitions for wholesale reform and opted instead for a program of incremental changes. With this aim in mind, the Colter Committee was established to identify the most urgently needed reforms. The Colter Committee reported in 1986[12] and amendments were enacted in 1992 giving effect to most of the committee's recommendations.[13] The most significant changes were as follows:[14]

- a complete overhaul of the commercial proposal provisions in Part III, Division 1, and the enactment of a new Division 2 governing consumer proposals;
- the enactment of a new Part XI governing secured creditors and receivers, requiring secured creditors in certain circumstances to give

7 38 Vic., Can. S. 1875, c. 16.

8 *An Act to repeal the Acts respecting Insolvency* (now in force in Canada), 43 Vic., Can. S. 1880, c. 1.

9 9-10 Geo. V, Can. S. 1919, c. 36. Provincial assignments and preferences statutes, based on the property and civil rights power, were enacted as stop-gap measures. In Quebec, the governing provisions were in articles 763-780 of the *Code of Civil Procedure*. For a history of the 1919 Act, see Thomas G.W. Telfer, "The Canadian Bankruptcy Act of 1919: Public Legislation or Private Interest?" (1995) 24 C.B.L.J. 357.

10 13 Geo. VI, Can. S. 1949 (2nd Session), c. 7.

11 23-24 Geo. V, Can. S. 1932-33, c. 36.

12 Advisory Committee on Bankruptcy and Insolvency, *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency* by G.F. Colter (Hull, PQ: Supply and Services Canada, 1986).

13 S.C. 1992, c. 27. One recommendation not adopted was the committee's proposal for a wage-earner protection program. The amending bill, when first introduced, provided for the enactment of a Wage Claim Payment Act in line with the committee's recommendations, but this turned out to be too controversial and it was dropped before the bill's enactment: Ziegel, Duggan & Telfer, *supra* note 1 at 17. Statute c.47 revisits the issue: see Chapter 4, below.

14 Ziegel, Duggan & Telfer, *ibid.* at 17-18.

notice to the debtor before enforcing a security interest and subjecting privately appointed as well as judicially appointed receivers to judicial supervision;[15]

- substantial changes to the provisions governing priority of claims in section 136, including the elimination of preferred creditor status for Crown claims;
- the enactment, in section 67(3), of special priority rules for certain statutory deemed trusts in the Crown's favour;
- the introduction, in sections 86 and 87, of registration requirements for Crown lien claims as a condition of their recognition in bankruptcy;
- the establishment of a super-priority claim for unpaid sellers in respect of goods supplied within a specified period before the debtor's bankruptcy (sections 81.1 and 81.2);[16]
- new provisions for the automatic discharge of individual first-time bankrupts at the end of nine months (sections 168.1-172);[17] and
- the introduction of mandatory credit counselling for individual bankrupts (section 157).

The 1992 amending statute also provided for a parliamentary review of the legislation in three years' time.[18] In preparation for this review, the Department of Consumer and Corporate Affairs (now Industry Canada) established a Bankruptcy and Insolvency Act Advisory Committee in 1993 to identify further necessary amendments. Legislation was enacted in 1997 giving effect to most of the committee's recommendations.[19] The most important changes to the BIA were as follows:[20]

- extension of protection against liability for environmental damage to receivers, interim receivers, and trustees under proposals;
- refinement of the provisions governing landlords' claims for leases repudiated by the debtor in commercial proposal proceedings;[21]
- the enactment of provisions allowing a debtor in commercial proposal proceedings to compromise claims against directors;

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15 For further discussion of receivers in the context of corporate governance, see Chapter 10, below.

16 In relation to points 3 to 6, see further Chapter 5, below.

17 See further Chapter 14, below.

18 S.C. 1992, c. 27, s. 92.

19 S.C. 1997, c. 12.

20 Ziegel, Duggan & Telfer, *supra* note 1 at 18-19. See also R.G. Marantz & R.H. Chartrand, "Bankruptcy and Insolvency Law Reform Continues: The 1996-1997 Amendments" (1997-1998) 13 B.F.L.R. 107 and Jacob S. Ziegel, "Canadian Bankruptcy Reform, Bill C-109 and Troubling Asymmetries" (1996) 27 C.B.L.J. 108.

21 See further Chapter 2, below.

- the enactment, in Part XII, of new provisions governing the insolvency of securities firms;
- the enactment, in Part XIII, of new provisions governing cross-border insolvencies;[22] and
- reform of the provisions governing an individual debtor's obligations to make contributions to the estate from surplus income earned during bankruptcy.[23]

The 1997 statute also amended the CCAA, the most important changes being as follows:[24]

- replacement of the former provision governing the debtor's eligibility to seek protection under the Act with a new requirement that the debtor and its affiliates must have a minimum indebtedness of $5 million;[25]
- enactment of new provisions limiting the court's initial *ex parte* order to 30 days and requiring a new hearing thereafter;
- introduction of a requirement for a court-appointed monitor to protect creditors' interests in particular by supervising the debtor's management during the reorganization process;[26]
- enactment of provisions allowing a debtor in CCAA proceedings to compromise claims against directors; and
- enactment, in section 18.6, of new cross-border insolvency provisions.[27]

In addition, the 1997 statute provided for a further parliamentary review of the legislation in five years' time.[28] In anticipation of this review, Industry Canada held consultative meetings with stakeholders and commissioned in-depth studies of particular issues, including Crown claims, preferences and gifts and transfers at undervalue, and priorities. The process culminated in a report, published in 2002, which summarized the main issues and the arguments for and against particular reforms, but stopped short of making actual recommendations.[29] Industry Canada's focus was on commercial bankruptcy and insolvency issues. However, in 2000 the Superintendent of Bankruptcy established a Personal Insolvency

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22 See further Chapter 11, below.
23 See further Chapter 13, below.
24 Ziegel, Duggan & Telfer, *supra* note 1.
25 The former requirement was that the debtor must have an outstanding issue of debentures or bonds under a trust deed.
26 See further Chapter 10, below.
27 See further Chapter 11, below.
28 See BIA, *supra* note 2, s. 216 and CCAA, *supra* note 3, s. 22.
29 Industry Canada, Market Framework Policy Branch, Policy Sector, *Report on the Operation and Administration of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (Ottawa: September 2002).

Task Force (PITF) to advise him on the need for reforms on the personal bankruptcy and insolvency front. The PITF Report appeared in late 2002.[30] It contained a large number of recommendations, some more important than others and some of its more radical recommendations provoked dissent within the task force.[31] Meanwhile, the Insolvency Institute of Canada (IIC) and the Canadian Association of Insolvency and Restructuring Professionals (CAIRP) formed a Joint Task Force to prepare a report to government on business insolvency law reform. The JTF Report[32] was completed in March 2002, and it contained a large number of recommendations relating to commercial bankruptcy, the BIA commercial proposal provisions, and the CCAA.

The Standing Senate Committee on Banking, Trade and Commerce (Senate Committee) was charged with carrying out the parliamentary review mandated by the 1997 BIA and CCAA amendments. The committee held hearings during 2003 and released its report (the "Senate Report") in November of that year.[33] The Senate Report contained 19 recommendations relating to personal insolvency law and a further 34 recommendations relating to commercial insolvency. The personal insolvency recommendations relied heavily on the PITF Report, while the commercial insolvency recommendations drew heavily on the JTF Report. At the end of June 2005, the joint task force produced a supplemental set of recommendations in response to the Senate Report.[34] However, by then the government had already introduced Bill C-55.[35] Bill C-55 was aimed for the most part at implementing the Senate Committee's recommendations and its first reading was on 3 June 2005. The bill showed many signs of hurried drafting, and it attracted widespread criticism from industry and other stakeholders.[36] It was referred for review to the House of Commons Standing Committee on Industry, Natural Resources, Development and Technology. However, the committee's proceedings were terminated not long after it had started its hearings and the bill was rushed through Parliament without debate in the dying days of the Martin Liberal government, receiving royal assent on 25 November 2005.

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30 See Abbreviations, p. xxxvii above.

31 Ziegel, Duggan and Telfer, *supra* note 1 at 19.

32 See Abbreviations, p. xxxvii above.

33 See Abbreviations, p. xxxvii above.

34 IIC and CAIRP Joint Task Force on Business Insolvency Law Reform, *Supplemental Report* (30 June 2005), online: <http://www.insolvency.ca/papers/Supplemental%20Report_JTF_Sept-05.pdf>.

35 See Abbreviations, p. xxxvii above.

36 See *e.g.*, Insolvency Institute of Canada (IIC), News Release, "Insolvency Experts Say Proposed Legislation is Flawed" (17 November 2005), online: <http://www.insolvency.ca/papers/Bill%20C-55%20Press%20Release%20for%20IIC_final-Nov17.pdf>. See also IIC, *Position Paper on Bill C-55* (12 October 2005), online: <http://www.insolvency.ca/papers/IIC%20Position%20Paper%20re%20Bill%20C-55_Oct%2012.pdf >; and Legislative Review Task Force (Commercial) of the IIC and CAIRP, *Report on the Commercial Provisions of Bill C-55* (13 October 2005) online: <http://www.insolvency.ca/papers/LRTF%20Report_final_Oct-14-05.pdf>.

Simultaneously, the Senate Committee issued a brief report, the key part of which reads as follows:[37]

> The Committee wishes to indicate our disappointment with the process by which the Bill arrived in the Senate. We recognize the extraordinary circumstances that exist with the impending dissolution of Parliament, but believe we had an inadequate opportunity to review comprehensively such an important piece of framework legislation.
>
> Notwithstanding the foregoing, the Committee has decided to report Bill C-55 without amendment and without having conducted the customary comprehensive study and review. We do so not because we approve of the legislation in its entirety, as drafted, but rather because of three key factors.
>
> First, the Committee unanimously supports and approves of the long-overdue wage earner protection provisions of the Bill and does not wish to delay, or in any way deny—or appear to deny—access to enhanced legislated protection for this vulnerable group of creditors.
>
> Second, the witnesses heard by the Committee, including the Minister of Labour and Housing and the Parliamentary Secretary to the Minister of Industry, gave unqualified assurance to the Committee, to be confirmed in writing forthwith, that Bill C-55 would not be proclaimed into force prior to 30 June 2006 at the earliest.
>
> Third, the Committee expects that between now and the proclamation of Bill C-55, we will receive a timely Order of Reference that will enable us to undertake the thorough review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act that would have occurred with respect to Bill C-55 had it been referred to us on a more timely basis.[38]

The Senate was confronted with what has variously been described as a "Solomon's choice" and a "Hobson's choice": either to oppose the legislation, and in doing so to defeat measures the Senate supported, or to pass it, warts and all.[39] As the above-quoted passages indicate, the Senate agreed to let Bill C-55 through unchanged, in return for the government's commitment to delay proclamation so that the shortcomings in the legislation could be identified and fixed before it came into force. Following its enactment, Bill C-55 became Chapter 47 of the Statutes of Canada ("Statute c.47").

A federal election in early 2006 led to a change of government and 30 June 2006 came and went without referral of the new legislation to the Senate Committee and with no indication of how the new Harper government planned to proceed. Finally, on 8 December 2006, the Minister of Labour introduced a ways and means motion seeking parliamentary authority to fund the wage earner

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37 The report is reproduced in Parliament of Canada, *Debates of the Senate: Wager Earner Protection Program Bill Third Reading* (Speech by Senator Grafstein, 25 November 2005) at 2207.

38 *Ibid.*

39 *Ibid.*

protection program provided for by Statute c.47.[40] Appended to the motion was a bill incorporating substantial amendments to the BIA, the CCAA and Statute c.47.[41] On 12 December 2006, the government house leader requested unanimous all-party approval for the ways and means motion, but, given the lack of time for consultation, the request was refused.[42] The government then decided to leave the ways and means motion on the Parliamentary order paper over the holiday break and to resume negotiations for all-party approval in January 2007.[43] Another 6 months passed before matters were finally resolved. On June 13, 2007, the Minister introduced Bill C-62 into the House of Commons. Bill C-62 is entitled "An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005" and, subject to one substantive change, it replicates the bill that was attached to the December 2006 ways and means motion.[44]

Bill C-62 was passed by the House of Commons on June 14 and this is where matters presently stand. The Bill will now be referred to the Senate for consideration, in fulfillment of the previous government's commitment to consult with the Senate on the reforms. At the time of writing (June 2007), it was not clear how or when the Senate would deal with the Bill. There is one further development that deserves mention. On March 29, 2007, the government introduced, as part of the federal budget package, a number of provisions relating to the treatment of eligible financial contracts in insolvency proceedings.[45] These provisions anticipate and improve on the measures relating to eligible financial contracts contained in Statute c.47 as modified by Bill C-62. At the time of writing, Bill C-52 was at the Third Reading stage and it was not certain whether it would come into force before or after Bill C-62. To deal with this contingency, clause 112 of Bill C-62 contains an elaborate set of provisions aimed at coordinating the two sets of amendments: see further Chapter 3, below.

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40 The following account draws on a memorandum from Paul J. Brown of Campbell Strategies to the IIC, dated 13 December 2006 entitled "Update on Insolvency Legislation: Bill C-55", online: <http://www.insolvency.ca/papers/Request%20for%20Unanimous%20Consent%20-%20Status%20Report%20of%20C-55%20Dec%2013-06.pdf>.

41 Bill appended to "Notice of Ways and Means Motion to introduce an Act to Amend the *Bankruptcy and Insolvency Act*", the *Companies' Creditors Arrangement Act*, the *Wage Earner Protection Program Act* and Chapter 47 of the *Statutes of Canada*, 2005 (Parliament of Canada, House of Commons, Sessional Paper, 8 December 2006).

42 Brown, *op.cit.*, n. 40. at para. 3. If all-party approval had been obtained, the Bill could have been sent directly to the Senate on a fast-track process without first going to the House of Commons: *ibid.* at para. 2.

43 *Ibid.* at para. 3.

44 The substantive change is in s. 32(1), amending BIA, s. 67(1) (property of a bankrupt divisible among creditors): see further Chapter 7, below, n. 74.

45 Bill C-52: An Act to Implement certain provisions of the budget tabled in Parliament on March 19, 2007 (the "Budget Implementation Act").

II. ABOUT THIS BOOK

The main focus of this book is on the need for reform of Canadian bankruptcy and insolvency law, rather than on the specific provisions of Statute c.47. The objectives are to explain current law and policy, compare Canadian law with developments in other countries including the United States, the United Kingdom, and Australia, and to identify and critically analyze proposals for reform of the law in Canada. Statute c.47 has always been in our sights, but only as representing a particular response to the set of issues that concerns us. There would have been a place for this book even if Statute c.47 had never been enacted. Likewise, there is a place for this book notwithstanding the uncertainties that continue to surround Statute c.47's fate at the time of this writing.

Nevertheless, we did have hopes at the outset of the project of being able to write definitively about the proposed reforms. We began work on the book early in 2006. By that time, Statute c.47 had been enacted and it seemed likely that the Senate Committee would have completed its deliberations in time for us to take account of any further amendments before the book went to press. For the reasons discussed above, these projections were not realized and we have been left shooting at a moving target. In fact, given the current politics, a more appropriate metaphor might be that the whole shooting range is in an earthquake zone. It became clear to us in the later part of 2006 that Statute c.47 was unlikely to be settled by our planned publication date. At that point, one of our options would have been to delay publication until the reform process had run its course. However, this would have meant delaying the book indefinitely and, as we have already suggested, this book has a place regardless of what form, if any, the amendments finally take.

The solution we eventually decided on was to proceed with the book as planned, but to produce a supplement once the amendments have been settled, enacted, and proclaimed. Consistent with this agenda and with what we have said above, the book takes a predominantly issues-oriented approach, though with quite extensive references to Statute c.47 and summary references to Bill C-62. The supplement will provide a closer textual analysis of the amendments in their final form. The two volumes in combination will give the reader a comprehensive account of the reasons for the amendments, their implications, and how they measure up both in policy terms and as a matter of practice.

We are privileged to edit a book that brings together an exceptional group of bankruptcy and insolvency law scholars and practitioners, offering wide-ranging contributions that reflect their diverse interests. We think it is fair to say that in addition to contributions from leading members of the bankruptcy bar, and a leading American bankruptcy law scholar, the majority of Canadian academics researching and writing in bankruptcy law today are included in this collection.

III. OVERVIEW OF CONTRIBUTIONS

The book comprises 15 chapters, including this one, covering key aspects of Canadian bankruptcy and reorganization law. A number of themes run through the chapters, including the following:

(1) the extent to which Canada should harmonize bankruptcy and reorganization legislation with the United States, look to other common law jurisdictions as models for reform, or adopt a distinctly "made in Canada" approach;

(2) the need for greater consistency in the treatment of issues that are common to BIA and CCAA proceedings; and

(3) the scope for judicial discretion in BIA and CCAA proceedings.

The contributions to this book offer different perspectives on these themes as they relate to particular aspects of Canadian bankruptcy and reorganization law and, in doing so, they reflect the range of positions to which the various stakeholders subscribe.

Chapters 2 to 4 relate wholly or in part to the issue of executory contracts (or "partly performed contracts", as we prefer to call them). In Chapter 2, "Partly Performed Contracts", Anthony Duggan discusses the disclaimer, affirmation, and assignment of partly performed contracts in bankruptcy and reorganization proceedings, comparing the law as it currently stands in Canada with the executory contracts provisions in section 365 of the United States Bankruptcy Code[46] and the proposed Canadian amendments in Statute c.47. Professor Duggan argues that, while the proposed reforms bring Canadian law closer to the U.S. position, they fall short in terms of both comprehensiveness and consistency. In important respects, different rules continue to apply depending on the nature of the contract in issue and the nature of the proceedings.

In Chapter 3, "Derivatives and the CCAA", Stephanie Ben-Ishai and Peter Kolla consider a particular type of partly performed contract—derivatives, or "eligible financial contracts"—in the Canadian bankruptcy and reorganization regime. Two main considerations have traditionally informed the treatment of eligible financial contracts in the context of financial restructurings: ensuring that companies that use derivatives to manage their risk can continue this risk management if the counterparties to their derivatives contracts become insolvent, and maintaining a favourable regulatory environment vis-à-vis the United States to foster a domestic derivatives industry. Observing that Statute c.47 generally overlooks the important issue of the treatment of eligible financial contracts in bankruptcy proceedings, the authors argue that the proposed reforms do not reflect a principled understanding of the operation of the derivatives industry in the North American context. However, the authors

[46] See Abbreviations, p. xxxvii above.

note that Bills C-52 and C-62 do address a number of the deficiencies orginally found in Statute c.47, while introducing additional concerns due in part to the piecemeal reform process.

In Chapter 4, "Labour Issues", David Baird and Ronald Davis consider the treatment of key labour issues in reorganization proceedings, including the status of collective agreements. Collective agreements comprise an aspect of the partly performed contracts issue. As the authors explain, Statute c.47 excludes collective agreements from the provisions governing disclaimer of contracts and enacts a special set of rules aimed at bringing the parties to the bargaining table. The chapter also considers employee claims for unpaid wages and pension contributions, the proposed wage earner protection program, and employer successor claims against receivers and trustees in bankruptcy.

Baird and Davis deal with, among other things, a particular priorities issue, namely the priority for unpaid wages and pension contributions. In Chapter 5, "Priorities", Tamara Buckwold and Roderick Wood discuss the priorities question at large. They survey the priority rules that operate in bankruptcy, receivership, and reorganization, and consider the priority implications of the changes introduced by Statute c.47. Through their survey, the authors demonstrate a lack of consistency in the priority rules across Canadian insolvency regimes. This lack of consistency, they point out, encourages parties to engage in strategic behaviour to invoke the insolvency regime that affords the highest ranking of their claim. The authors argue that comprehensive insolvency law reform must ensure consistent priority rules, and they suggest a set of principles to produce a more rational, coherent, and predictable priority structure across the major insolvency regimes.

In Chapter 6, "Voidable Preferences", Anthony Duggan and Thomas Telfer outline the history of the BIA preference provisions and discuss the proposed amendments contained in Statute c.47. They argue that the current Canadian preference provisions are deficient because they lack a clear policy foundation; the provisions represent an incomplete statement of the law due to judicial glosses on the statutory text; and the amount of discretion the provisions give to the courts results in inconsistent and unpredictable outcomes. Professors Duggan and Telfer argue that meaningful reform will not be achieved without a clear policy objective, and they urge lawmakers to address the key policy issues before settling the proposed reforms.

In Chapter 7, "Gifts and Transfers at Undervalue", Professors Duggan and Telfer analyze the BIA settlement and reviewable transactions provisions, which allow the trustee to attack pre-bankruptcy transactions in certain circumstances, and consider the provincial fraudulent conveyance laws that operate in conjunction with the BIA provisions. Outlining the policies behind fraudulent conveyance law and the BIA provisions, the authors critically analyze the current law and the recent reform initiatives contained in Statute c.47. They argue that the current provisions are overlapping, inconsistent, and incomplete. Professors Duggan and Telfer conclude that although the Statute

c.47 reforms are a step in the right direction, they fall short because the proposed new transfer at undervalue provision is not comprehensive and does not displace provincial fraudulent conveyance laws.

Chapters 8 through 10 share a common theme, namely judicial discretion under the BIA and the CCAA and the potential impact of Statute c.47 on its use. In Chapter 8, "Judicial Discretion", Janis Sarra examines the role and nature of judicial discretion in bankruptcy and reorganization matters with a focus on the CCAA. She identifies the principles courts have articulated to govern the exercise of discretionary powers under statute and at common law. Professor Sarra analyzes six areas in which Statute c.47 codifies the exercise of judicial discretion: balancing bankruptcy and reorganization legislation with other statutory schemes, interim financing, authority to remove directors, treatment of contracts, sale of assets, and BIA and CCAA cross-border provisions. The author suggests that, for the most part, the reforms codify the courts' current exercise of discretion under the BIA and CCAA and affirm developments in the jurisprudence over the past two decades. She argues that, in codifying certain aspects of judicial discretion, Statute c.47 furthers the objectives of uniformity, predictability, and transparency in bankruptcy and reorganization proceedings. It is possible that the reforms will trigger a new wave of litigation because they could be read as implying that the courts have no discretion except where the legislation expressly says so. However, Professor Sarra does not believe the courts will accept this line of argument.

In Chapter 9, "Debtor-in-Possession Financing", Michael Rotsztain and Alexandra Dostal discuss the development of DIP financing in Canada, review proposals for law reform, and assess the DIP financing provisions in Statute c.47. The new provisions give the courts discretion to determine the amount a debtor may borrow, secured by a court-created charge on the debtor's assets in favour of the lender. The authors conclude that the Statute c.47 reforms are reasonably successful in balancing the advantages of specific rules while preserving flexibility to address particular situations, but they outline areas for further improvement.

In Chapter 10, "Corporate Governance", Steven Golick and Edward Sellers outline how Statute c.47 seeks, in part, to increasingly codify the functions of the courts, boards of directors, and court-supervised officers involved in bankruptcy and reorganization proceedings. After reviewing the new provisions and their impact on directors, monitors, receivers, equity interests, and priority of charges, Golick and Sellers conclude that the amendments fall short of achieving the comprehensive reform needed to fully address governance aspects in Canada's bankruptcy and reorganization regime.

In Chapter 11, "Cross-Border Insolvencies", Jacob Ziegel discusses the Statute c.47 provisions relating to cross-border insolvencies. Although the new provisions are based on the UNCITRAL Model Law on Cross-Border Insolvency, they omit a substantial number of the Model Law provisions and add other provisions that have no counterpart in the Model Law. Professor Ziegel

compares and contrasts the common law and current statutory provisions relating to cross-border insolvencies, the key Model Law provisions, and the Statute c.47 provisions. He concludes that the legislature was right to adopt the Model Law, but wrong to deviate from the model without, at a minimum, engaging in extensive outside consultations. Professor Ziegel makes various arguments for adopting the Model Law, including the fact that the United States has done so almost verbatim and the difficulty in achieving the objectives of the Model Law if enacting states fail to adopt the entire package.

In Chapter 12, "The BIA and CCAA Interface", Professor Ziegel examines the relationship between the CCAA and the commercial proposal provisions in BIA, Part III, Division 1. He points out that Canada is unique in having two separate statutory regimes for commercial reorganizations, and argues that this position is indefensible. Supporters of the status quo, he argues, mistake the need for special procedures to govern large-scale reorganizations with the need for separate statutes. In his view, the CCAA should be repealed and its key provisions re-enacted as part of the BIA. Among other things, this reform would simplify the law by removing the need for duplication of provisions on matters that are common to all forms of proceedings such as partly performed contracts, priorities, and cross-border insolvencies.

Chapters 13 to 15 shift the focus to consumer bankruptcy issues. In Chapter 13, "Means-Testing", Stephanie Ben-Ishai looks at the recently enacted means-testing provisions of the United States Bankruptcy Code. Means-testing requires all debtors to calculate their estimated ability to pay creditors and file these calculations with their chapter 7 petitions; failure to do so will result in an automatic dismissal of the debtor's petition. The author contrasts the U.S. approach with that in Canada, means-measurement, which does not result in the dismissal of a petition, but requires the bankruptcy trustee to establish debtors' payments during the bankruptcy period, if any, based on government regulations. The reforms enacted by Statute c.47 will increase the period of repayment before a debtor may obtain a discharge. The author draws on American literature pertaining to means-testing to argue that Canada's resistance to the United States means-testing model is a laudable feature of the proposed reforms. Some aspects of the means-measuring model, Professor Ben-Ishai cautions, may be functionally equivalent to means-testing for some debtors and the author questions whether the reforms adequately deal with these issues.

In Chapter 14, "Discharge", Professor Ben-Ishai notes that a key component of consumer bankruptcy in Canada, since 1919, has been the non-waivable or mandatory consumer bankruptcy discharge. The 1997 BIA amendments, however, spurred a paradigm shift from rehabilitation of the debtor to debtors rehabilitating their debts by making payments from surplus income. The author documents how the Statute c.47 reforms continue this shift and depart from the contemporary understanding of the bankruptcy discharge—protecting individuals from themselves and restoring them to productivity. By focusing on the exceptions to discharge provided for in the legislation and demonstrating how the

reforms expand opportunities and incentives for creditors to prevent bankrupts from receiving an automatic discharge after a nine-month period, Professor Ben-Ishai concludes that the shift is significant for both debtors and creditors as it threatens to limit both the benefits and function of the bankruptcy process.

In Chapter 15, "A United States Perspective", John Pottow compares Statute c.47 to its United States counterpart, the recently enacted *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* (BAPCPA),[47] looking at various actors in the political process of bankruptcy reform, the coalescing of interests, and the "contextual terrain" in which the public debates took place. The author attempts to explain why the new U.S. law is more anti-debtor than the Canadian reforms. Because the banking industry is more highly concentrated in Canada, one might expect banks to be in a stronger position to lobby for more creditor-friendly legislation. Professor Pottow theorizes that the BAPCPA and Statute c.47 diverged along the lines of political sensitivity: the consumer credit industry lobby in the United States succeeded in raising the stakes by focusing on the issue of debtor fraud. This gave the debate a moral overtone and it effectively silenced the pro-consumer academics. By contrast, in Canada, the process was seen by and large as a technical law reform exercise and it lacked the politically charged dimension of the American experience.

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47 *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, Pub. L. No. 109-8, 119 Stat. 23 (2005).

TAB 17

BENNETT

on

CREDITORS' AND DEBTORS' RIGHTS AND REMEDIES

Fifth Edition

by

Frank Bennett
L.S.M., LL.M.
Toronto, Canada

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Bankruptcy – Assignment or Bankruptcy Order

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1. INTRODUCTION AND HISTORY

Parliament enacted the first Canadian *Bankruptcy Act* in 1919. Until then, Parliament enacted *Insolvency Acts* in 1869 and in 1875, but these were repealed in 1880. In addition, the provinces had enacted insolvency legislation to control fraudulent conveyances and assignments to creditors following confederation in 1867. In 1919, Parliament enacted *The Bankruptcy Act* substantially following the English model.

This Act was amended from time to time until 1949, at which time there were suhstantial changes. With the exception of certain amendments made in 1966 dealing with fraudulent transactions, there had been no substantial changes until 1992, at which time the then *Bankruptcy Act*[1] was amended in several different areas,[2] including a name change to the *Bankruptcy and Insolvency Act* to reflect some provisions dealing with receiverships. The amending Act also

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1 R.S.C. 1985, c. B-3.
2 S.C. 1992, c. 27.

introduced major changes to the areas of consumer and commercial proposals, consumer bankruptcies, rights of unpaid suppliers, Crown priority, receiverships, and several technical amendments.

One of the provisions of the amendments called for a review of the legislation three years after its enactment. In preparation, the Department of Industry, formerly the Department of Consumer and Corporate Affairs, organized a Bankruptcy and Insolvency Advisory Committee in 1993. The Committee comprised of numerous interest and non-partisan groups that met on a regular basis to discuss reform to the whole bankruptcy process. As a result, there were additional amendments to the Act in 1997[3] relating to consumer and commercial bankruptcies, trustees' potential liability under environmental laws, commercial proposals, bankruptcies of securities firms, international insolvencies, amendments to the *Companies' Creditors Arrangement Act,* and amendments to directors' liability while a company is reorganizing. As in previous legislation, Parliament required a report on the efficiency of bankruptcy and insolvency legislation after five years. Reviews and hearings were conducted across Canada throughout 2002, and in November, 2003, the Senate released its report making 53 recommendations.

2. PURPOSE OF BANKRUPTCY LEGISLATION

(a) Definition of Bankruptcy

Bankruptcy legislation has several objectives. The *Bankruptcy and Insolvency Act* is designed "to protect creditors of insolvent debtors and to ensure that there is an orderly and fair administration of their assets."[4] In other words, bankruptcy legislation is designed:

1. to distribute the proceeds of the bankrupt's assets equitably and in accordance with a scheme of distribution;
2. to punish fraudulent debtors where there are breaches of certain standards of conduct. In some instances, principals of corporate bankrupts may be liable for certain of the corporation's debts. There are also criminal sanctions;
3. to reform debtors whereby individual bankrupts can relieve themselves from financial obligations and become rehabilitated;
4. to promote confidence in the credit system such that credit grantors can believe that the system operates fairly with the means of seeking redress for wrongdoing and treating all persons of a like class in the same manner;
5. to permit debtors an opportunity to make proposals where individuals, or restructurings where corporations, of their debts without going into bankruptcy; and
6. to permit the trustee to investigate into the affairs of the bankrupt.

Section 91, item 21, of the *Constitution Act* assigns the exclusive jurisdiction over bankruptcy and insolvency to the Parliament of Canada. In particular, the

3 S.C. 1997, c. 12.

4 *Langille v. Toronto Dominion Bank* (1981), 37 C.B.R. (N.S.) 35 (N.S. C.A.), affirmed (1982), 40 C.B.R. (N.S.) 113 (S.C.C.).

Bankruptcy and Insolvency Act is a statute of Canada, and together with the General Rules and Regulations under the Act, they govern the rights and remedies of the creditors and insolvent debtors. To supplement federal law, there is also provincial statutory and case law that deal with bankruptcy. Under the Act, a bankrupt is defined as being a person who has made an assignment, or against whom a bankruptcy order has been made, or the legal status of such person.

The *Bankruptcy and Insolvency Act* covers several different areas of law governing insolvent and bankrupt debtors. The Act applies to any person, whether an individual or a corporation, who (i) voluntarily makes an assignment in bankruptcy; (ii) becomes subject to a bankruptcy order; or (iii) voluntarily files a proposal. The Act also regulates, to some extent, the rights of creditors and debtors where a receivership is invoked.

A debtor must be insolvent before resorting to an assignment or a proposal. Insolvency is not necessarily bankruptcy, and although all bankrupts are insolvent, not all insolvent persons become bankrupt. Section 2 of the Act defines an insolvent person. In essence, an insolvent person is a person who owes $1,000 to creditors and:

(1) who is unable to meet his or her obligations as they generally become due; or
(2) has ceased paying his or her current obligations in the ordinary course of business as they generally become due; or
(3) the aggregate of whose property is not, at a fair valuation, sufficient or if disposed of under legal process, would not be sufficient to enable payment of all his or her obligations due and accruing due.

The definition is in the alternative and only one of the three criteria need be established.

In order to invoke the Act, there are three procedures available:

(i) *Assignment*

If the debtor "wants to go bankrupt", the debtor can file an assignment. An assignment is the voluntary act by an insolvent person who assigns bis or her property to a licensed trustee in bankruptcy for the general benefit of creditors.[5] The assignment is a one-paged prescribed form accompanied by a sworn statement of the property of the debtor and a list of creditors showing their addresses, the amounts of their claims and the nature of their claim whether secured, preferred or unsecured. The assignment is filed with the official receiver in the locality where the debtor resides or carries on business. Once bankrupt, the person becomes bankrupt for all purposes under the Act and other legislation. There are special rules that apply to consumer debtors including two mandatory counselling sessions and an automatic discharge after nine months if no one opposes.[6]

5 Subsection 49(1). This is covered below in more detail.
6 For example, section 157.1 – mandatory counseling, and section 168.1 – automatic discharge.

(ii) *Bankruptcy Order*

On the other hand, in the case where the creditor "wants to put the debtor into bankruptcy", the creditor, formerly called the petitioning creditor, can issue an application for a bankruptcy order from the bankruptcy court office against the debtor.[7] If the debtor does not defend or defends unsuccessfully, the application creditor obtains a bankruptcy order, formerly called a receiving order. The applicant creditor must allege, among other things, a debt of $1,000 or more owing to the creditor and that the debtor has committed an "act of bankruptcy", usually that the debtor has ceased to meet his or her liabilities generally as they fall due. The application is, in effect, an originating process that is served on the debtor. Once served, the debtor has an opportunity to appear on the return of the application and dispute the creditor's claim. If a dispute is made, the court directs a trial of an issue which is generally placed on a high priority on the trial list. If the application is successful, a bankruptcy order is made against the debtor, at which time the debtor becomes bankrupt.

(iii) *Proposal*

If the debtor "wants to make a deal with his or her creditors", the debtor can file a proposal. A proposal is a contract with the debtor and the creditors governed under Part III of the Act. A debtor or insolvent person may file a proposal with a licensed trustee providing for a composition, extension or re-arrangement of his or her debts to the creditors. The proposal is subject to the ratification by the creditors and the approval of the court. While the proposal is operative, all creditors are prevented from commencing or continuing legal proceedings against the debtor pending the debtor's performance, except in the case of secured creditors who enforced their security before the debtor took protection or those who obtained leave of the court. A bankrupt can also lodge a proposal after bankruptcy, but the inspectors must first approve it. Lastly, the trustee in bankruptcy, and even the debtor's receiver or liquidator can make a proposal.

The *Bankruptcy and Insolvency Act* applies to all business debtors, whether individual or corporate. The Act was originally intended to apply to business debtors. However, as a result of extensive consumer credit by financial institutions and retailers since the 1960s, consumers have taken advantage of the provisions of the Act relating to the release of most of their debts. An individual may make a consumer proposal if his or her debts, excluding real estate, do not exceed $75,000. The procedure for consumer proposals is streamlined to give the debtor, the trustee and the creditors a speedy and less expensive way of dealing with insolvent consumers.

The Act does not apply to banks, insurance and trust companies and railways.[8] Although creditors cannot force farmers and fisherpersons into bankruptcy,[9] these

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7 Subsection 43(1). This is also covered below.

8 Section 1 of the Act defines "corporation" as specifically excluding these entities from the operation of the Act.

9 Section 48.

individuals may make assignments into bankruptcy. Proposals are covered in more detail in the next chapter.

(b) Alternative Remedies for Insolvent Persons

In addition to a bankruptcy or proposal under the Act, there are a number of other schemes that are available to deal with the affairs of an insolvent. Until recent years, they were seldom employed in the province of Ontario. In view of the weakness of the present *Bankruptcy and Insolvency Act* in dealing with larger insolvencies, practitioners looked elsewhere for solutions.

(i) *Companies' Creditors Arrangement Act*[10]

This Act came into force during the Great Depression of the 1930s to protect corporate debtors against holders of debentures issued in series and trust deeds. In effect, the Act provides that a debtor can formulate a compromise or arrangement with *all* of its creditors, including secured creditors. Until the 1992 amendments to the *Bankruptcy Act*, the filing of a proposal did not stay the rights of secured creditors, and therefore, larger corporate debtors employed the *Companies' Creditors Arrangement Act* rather than resort to the then *Bankruptcy Act*.

The debtor can apply to the court and obtain an order staying the rights of the secured creditors and others pending the implementation of the plan. This provision makes the Act more popular today than it used to be as secured creditors are held at bay while the debtor is given an opportunity to restructure.

In an attempt to co-ordinate different insolvency regimes, Parliament amended the *Companies' Creditors Arrangement Act* in 1997 to make that Act more parallel in language to the *Bankruptcy and Insolvency Act* than it was before. A company has a choice of taking protection under Part III of the *Bankruptcy and Insolvency Act* or applying for an order under the *Companies' Creditors Arrangement Act* in order to avoid bankruptcy. However, prior to the amendments, the two Acts overlapped. The *Companies' Creditors Arrangement Act* is far more flexible, but is more expensive to operate.

Access to the *Companies' Creditors Arrangement Act* is restricted to companies having at least $5 million in debts.[11] Companies have a choice between both regimes: either a the more structured process under the *Bankruptcy and Insolvency Act*, or a more flexible process under the *Companies' Creditors Arrangement Act*. However, under the *Companies' Creditors Arrangement Act*, there is less certainty and predictability of the outcome, along with much higher professional costs.

Until the amendments in 1997, the debtor company must have issued secured bonds, debentures, trust deeds or other similar instruments made in favour of a trustee in order for the *Companies' Creditors Arrangement Act* to apply. The Act did not apply to simple bank debentures as there was no trustee interposed between

10 R.S.C. 1985, c. C-36. See Goldman, D. and others "Arrangements under the Companies' Creditors Arrangement Act" (1991), 1 C.B.R. (3d) 135 for a review of the problems under this Act.

11 Subsection 3(1).

the debtor and the investors participating in the debenture stock. In the years prior to the amendments, insolvent debtors intentionally created debentures in series to take advantage of the Act[12] and gain a stay of proceedings against secured creditors. These restrictions were removed in 1997.

The *Companies' Creditors Arrangement Act* gives very little guidance as to the procedure to be followed in formulating a plan of arrangement. It is a short Act containing only 22 sections. Therefore, both the debtor and the creditors are left to the techniques of corporate and commercial laws to create a plan or a compromise that will be acceptable to all creditors and to the court.

To invoke the Act, the debtor applies to a judge in the jurisdiction where the debtor has its head office, or where most of its assets are located, for an order staying the secured creditors pending approval of the plan, directing the calling of a meeting of creditors to consider the plan, classifying the creditors affected by the plan and calling a vote. Usually, the debtor company applies for such an order without notice to its creditors, or sometimes on short notice. The court may grant that such an order stay the rights of creditors for a period of time up to 30 days, and on the return of the motion, the creditors may argue that the Act does not apply or that a particular creditor should be granted leave to proceed on its enforcement. If the order continues, the debtor obtains time to formulate a plan for presentation to the creditors.

As set out in more detail in Chapter 21, the debtor ultimately applies to the court for an order preventing creditors from exercising their remedies. Despite the stay, if the secured creditors are not on side in accepting the plan, or if there is one major secured creditor who opposes the application, the debtor is doomed to fail either on the return of the motion,[13] or on a vote, or on court approval.

In addition to the amendments to the *Companies' Creditors Arrangement Act*, there were also amendments to the *Bankruptcy and Insolvency Act* concerning the stay of proceedings against secured creditors. The *Bankruptcy and Insolvency Act* provides that if a corporation takes protection, the stay provisions apply to restrain the enforcement of the rights of secured creditors up to a maximum of six months.[14] With this particular amendment, the debtor has two alternative remedies under which secured creditors are prevented from proceeding until the proposal or arrangement has been rejected by the creditors or the court.

(ii) *Winding-Up and Restructuring Act*[15]

The *Winding-Up and Restructuring Act* applies to federal incorporated companies, banks, insurance companies and to certain insolvent provincial companies whose affairs are subject to the laws of Canada. The corporation may apply to

12 *Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), (sub nom. *Elan Corp. v. Comiskey*) 1 O.R. (3d) 289 (C.A.).

13 *First Treasury Financial Inc. v. Cango Petroleums Inc.* (1991), 3 C.B.R. (3d) 232 (Ont. Gen. Div.).

14 Section 69.1. There are a number of exceptions, including the rights of a secured creditor who has taken possession of the collateral to continue in its enforcement if the debtor has not filed for protection. See also the next chapter.

15 R.S.C. 1985, c. W-11.

the court for an order winding up its affairs. The Act sets out the procedure to be followed by the liquidator. If proceedings under this Act have commenced and an application for a bankruptcy order has been filed or the debtor has filed an assignment in bankruptcy, the *Bankruptcy and Insolvency Act* takes precedence over the *Winding-Up and Restructuring Act*.[16] Therefore, except in the case of banks and insurance companies, the *Winding-Up and Restructuring Act* is not commonly used. In recent years, the Act has been used in connection with two bank insolvencies.[17]

(iii) *Winding-Up under the Ontario Business Corporations Act*[18]

An Ontario corporation may commence proceedings for winding-up either voluntarily with or without a liquidator, or involuntarily by an order of the court at the request of a shareholder, creditor or other interested person.[19] The corporation must, however, be *solvent* in order for the Act to apply.

The *Business Corporations Act* does not give the liquidator rights to recover property conveyed or given away shortly before winding-up, whereas under the *Bankruptcy and Insolvency Act*, the trustee is able to recover property improperly transferred. However, as the company is solvent, there does not appear to be any need to recover property.

Once a corporation voluntarily commences proceedings for winding-up, no action or other proceeding can be commenced against the corporation without leave of the court.[20] Similarly, if the winding-up proceedings were commenced by a court order, there is also a stay of proceedings. On the other hand, if a creditor invokes the *Bankruptcy and Insolvency Act* and issues an application for a bankruptcy order, the stay of proceedings under the provincial legislation does not apply to the federal legislation dealing with insolvency. The bankruptcy court has the power to make a bankruptcy order against an insolvent corporation even though there are winding-up proceedings in process.[21] Therefore, if a corporation is being wound up and the creditors or liquidator find out that the corporation is insolvent, the creditors should issue an application to place the corporation into bankruptcy. It would appear that the court is unable to give the liquidator the power to assign the corporation into bankruptcy.[22]

(iv) *Farm Debt Mediation Act*

This Act, enacted in 1998 to replace the *Farm Debt Review Act,* is designed to protect insolvent farmers from foreclosures and a mortgagee's exercise of the

16 Section 213 of the *Bankruptcy and Insolvency Act.*

17 The Canadian Commercial Bank and the Northland Bank.

18 R.S.O. 1990, c. B.16.

19 Section 206.

20 Section 198.

21 Section 213 of the *Bankruptcy and Insolvency Act.* See also *Cadwells Ltd., Re* (1932), 14 C.B.R. 72 (Ont. S.C.); *Western Hemlock Products Ltd., Re* (1961), 35 W.W.R. 184 (B.C. S.C.); *Brandon Packers Ltd., Re* (1962), 3 C.B.R. (N.S.) 326 (Man. C.A.).

22 *Western Hemlock Products Ltd., Re,* above.

power of sale. A mortgagee is required to give the farmer 15 day's notice of its intention to enforce its security. A farmer can then apply for a stay of proceedings for a 30-day period that could be increased up to a total of 120 days. During this period, the farmer and the creditors mediate an overall settlement, failure of which the mortgagee can then proceed to realize on its security.

(v) *Informal Arrangements*

More often than not, a debtor may wish to avoid formal bankruptcy proceedings and attempt to settle or compromise his or her debts without the benefit of legislation. In practice, such arrangements are difficult to implement as it takes only one irate creditor to invoke bankruptcy proceedings. Where there are few creditors, informal arrangements can work favourably, thus saving substantial professional costs and avoiding the uncertainty of the process. Where there are several creditors, such arrangements are most difficult to implement and the proposal provisions of the *Bankruptcy and Insolvency Act* should ordinarily be used.

(c) Classes of Creditors

There are two basic classes of creditors under the Act. First, there are secured creditors. Second, there are unsecured creditors. In addition, there are trust claimants who are technically not creditors, but trust claims arise in most bankruptcies nonetheless. The secured creditor is a person holding a mortgage, pledge, charge, lien or privilege on or against the property of the debtor as security for a debt due from the debtor. Secured creditors are generally free to deal with their security and realize upon it in the ordinary course of business, unless prevented from doing so while the debtor is working under a proposal or by court order. Unless the security is invalid or unenforceable, the secured creditor is relatively free from the provisions of the Act. Once in bankruptcy, subsection 69(2) of the *Bankruptcy and Insolvency Act* provides for a stay of proceedings of all creditors with provable claims against the bankrupt. However, the rights of secured creditors are exempt from the stay of proceedings under this subsection.

The class of unsecured creditors comprises sub-classes of preferred, deferred and ordinary creditors. Section 136 of the Act provides a scheme for the distribution of proceeds of realization to the preferred creditors. There are several categories of preferred creditors. The usual claims comprise costs and expenses of the administration, claims of wage earners up to $2,000, business taxes, arrears of rent and accelerated rent to landlords.[23] These categories of creditors are entitled to payment in priority to all other unsecured creditors and, as among those creditors who are entitled to priority under section 136, the priority is fixed by the order. Each category is entitled to full payment before payment to the next category.

Certain creditors whose conduct is contrary to the provisions of the Act may be prohibited from participating in a dividend in some circumstances until all

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23 Prior to the 1992 amendments, the Crown had a preferred claim.

TAB 18

CREDITOR - DEBTOR LAW IN CANADA

Second Edition

by

C. R. B. Dunlop
M.A., LL.M.
Professor of Law, University of Alberta

With Chapter 19 by P. J. M. Lown, LL.M.
and Chapter 20 by E. R. Edinger, B.A., LL.B. (U.B.C.),
B.C.L. (Oxon.)

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FRAUDULENT CONVEYANCES AND PREFERENCES

1. Introduction
2. History of Fraudulent Conveyance and Preference Law
3. Fraudulent Conveyances
4. Fraudulent Preferences

1. Introduction

Our earlier discussion of the rights of unsecured creditors has proceeded on the assumption that debtors take no defensive action to prevent their tormenters from asserting their legal remedies. The assumption is unrealistic. Many debtors, foreseeing impending financial collapse, take steps to assign their property to a relative or friend, who is to retain it until the storm clouds (and the creditors) clear away. The strategy has dangers, not the least of which is the disloyal transferee who converts the debtor's assets to his or her own use.[1] Our concern here is not with the advantages and disadvantages to the debtor of this kind of conveyance, but with its potentially disastrous effect on the practical utility of the creditors' remedies, which are likely to realize nothing unless the conveyance can be set aside.

The debtor may not want to shelter wealth from his or her creditors as a whole but may instead seek to benefit some creditors at the expense of others. This selective generosity is sometimes explained by the characteristics of the various creditors; the average person in financial trouble will want to pay off loans from relatives before satisfying the claims of the bank or the business claimant. In other cases, the debtor will pay first the creditor who is most aggressive or who is vital to the survival of the debtor's business, such as the wholesale supplier of stock in trade. In all these cases, however, the result of this preferential treatment is that some claims will be satisfied in part or in whole while other creditors will get nothing, even if they resort to their legal remedies.

1 See, *e.g.*, *Goodfriend v. Goodfriend*, [1972] S.C.R. 640.

The law has had considerable difficulty in deciding how to deal with the inappropriate[2] conveyance or preference. It is clearly desirable that an insolvent person should not be able to shelter assets from the legitimate claims of creditors by assigning them to a convenient friend. On the other hand, the law is prepared to permit a person embarking on a risky business to protect personal wealth from subsequent claims by incorporating the enterprise as a separate legal entity. To what extent should a debtor have to retain assets so that subsequent creditors will have something to seize? Can and should a distinction be drawn between fraudulent and innocent transfers and, if so, whose intention is significant? The law cannot go to any lengths to protect creditors; the *bona fide* purchaser of assets from a debtor has some claim to be saved harmless from unforeseeable risks. Where should the law draw the line between freedom of commerce and the security of the purchaser's title on the one hand and the legitimate claims of creditors on the other?

When we turn from the fraudulent conveyance designed to defeat creditors generally to the transfer intended to prefer some creditors over others, the policy conflict becomes more acute. At common law, creditors had no responsibility to share the fruits of execution equally with other creditors, and we would expect that the debtor's voluntary payment of some but not others should be equally acceptable. However the first come first served policy of the common law has been rejected in favour of *pari passu* sharing in bankruptcy statutes and, in this country, in creditors' relief legislation. As a corollary, Canadian legislatures have passed Fraudulent Preference Acts, the purpose of which is to prohibit at least some preferential transfers, no matter how valid or meritorious the claim of the preferred creditor. The courts have however been more hesitant to strike down the preference of a legitimate creditor than they have a conveyance designed to defeat all creditors alike.

In this chapter, after looking at the historical background, we will examine two kinds of statutes which prohibit certain types of fraudulent conveyances or preferences.[3] The transfer designed to hinder or delay all creditors in the collec-

2 These transactions are traditionally described as fraudulent conveyances or preferences, and this practice will be followed in this chapter. However, several writers have pointed out that fraud is too narrow a term to encompass the range of transactions caught by this legislation. See, *e.g.*, Williams and Muir Hunter, *The Law and Practice in Bankruptcy* (19th ed. 1979), p. 347.

3 There is a large Canadian literature on fraudulent conveyances and preferences. Particularly useful are Canadian Bar Association — Ontario, *Fraudulent Conveyances, Unjust Preferences and Other Transactions Subject to Attack by Creditors* (1993); Edgson, "Fraudulent Conveyances & Preferences" in Continuing Legal Education Society of B.C., *Realization and Insolvency* (1986), p. 5.1; Gertner, Springman, McGuinness, Morrison, Stewart & Laskin, *Debtor and Creditor: Cases and Commentary* (3rd ed. 1987), pp. 535-629 (hereafter "Gertner Casebook"); Hansford, "Fraudulent Conveyances and Preferences" (1987), 2 Nat. Creditor/Debtor Rev. 108, 124; Howcroft, "Scope of Fraudulent Conveyances and Fraudulent Preferences Legislation in Alberta" (1986), 24 Alta. L. Rev. 496; Kerr, "Fraudulent Conveyances and Unjust Preferences", in Springman and Gertner, eds., *Debtor-Creditor Law: Practice and Doctrine* (1985), p. 191; Legal Education Society of Alberta, *Fraud, Fraudulent Conveyances and Fraudulent Preferences* (1985); Prowse, "Fraudulent and Voidable Conveyances" in Canadian Institute, *Debtors and Creditors: Protection to Collection in an Uncertain Economy* (1987), p.

tion of their claims has been the subject of a long line of English Acts, the most famous of which is the Statute of Elizabeth.[4] We will look first at that legislation and the Canadian statutes which have followed it. We will then examine the Canadian Fraudulent Preference Acts, the primary purpose of which is to restrict the debtor's right to prefer some creditors over others.[5]

2. History of Fraudulent Conveyance and Preference Law

(a) English Legislation

Long before the passage in 1570 of the "act against fraudulent deeds, alienations, etc." (better known as the Statute of Elizabeth),[6] the English judges and legislatures had struggled with the problem of conveyances intended to hinder or defeat creditors. It is sometimes said that the 1570 Act was simply a declaration of the common law; if so, it was not the first such attempt by the legislature to prevent this type of fraud. Statutes can be found as far back as 1376[7] which declare such conveyances to be void, particularly where the debtors, after making the transfer, then "withdraw themselves, and flee into places of holy church privileged, and there hold them a long time, and take the profit of their said lands and goods so given by fraud and collusion".[8]

The Statute of Elizabeth[9] may however have been the first attempt at a comprehensive prohibition of fraudulent conveyances, whether or not the debtor thereafter sought sanctuary. The preamble of the Act announced its purpose:

> For the avoiding and abolishing of feigned, covinous and fraudulent feoffments, gifts, grants, alienations, conveyances, bonds, suits, judgments and executions, as well of lands and tenements as of goods and chattels [which feoffments etc.] have been and are devised and contrived of malice, fraud, covin, collusion or guile, to the end, purpose and intent, to delay, hinder or defraud creditors and others of their just and

C-1; Robinson, *British Columbia Debtor-Creditor Law and Precedents* (1993), cc. 10 and 11; Springman, "Fraudulent Conveyances, Fraudulent Preferences, and Other Voidable Transactions" in Law Society of Upper Canada, *Special Lectures: 1988: Rights and Remedies in the Law of Creditor and Debtor*, p. 59. On reform, see Alberta Law Reform Institute, *Financial Assistance by a Corporation: Section 42, The Business Corporations Act (Alberta): Report No. 54* (1989); Law Reform Commission of B.C., *Report on Fraudulent Conveyances and Preferences* (1988: LRC 94); Ontario Law Reform Commission, *Report on the Enforcement of Judgment Debts and Related Matters* (1983), vol. 4, pp. 125-245. There is also a large literature, not cited here, on creditor-proofing a potential insolvent and the related ethical dilemmas.

4 Fraudulent Conveyances Act, 1571 (13 Eliz. 1), c. 5, made perpetual by the Continuance, etc., of Acts, 1586-87 (29 Eliz. 1), c. 5. See also Fraudulent Conveyances Act, 1584-85 (27 Eliz. 1), c. 4.

5 Some reference by way of comparison will be made to the reviewable transactions sections in the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 91-101.2. See generally Houlden and Morawetz, *Bankruptcy and Insolvency Law of Canada* (3rd ed. 1989).

6 *Supra*, note 4.

7 1376 (50 Edw. 3), c. 6. See also 1379 (2 Rich. 2), c. 3; and 1487 (3 Henry 7), c. 4.

8 1379 (2 Rich. 2), c. 3.

9 *Supra*, note 4.

> lawful actions, suits, debts, accounts, damages . . . not only to the let or hindrance of the due course and execution of law and justice, but also to the overthrow of all true and plain dealing, bargaining and chevisance between man and man, without the which no commonwealth or civil society can be maintained or continued.

Section 2 provided that all such conveyances should be "clearly and utterly void, frustrate and of no effect" as against those "creditors and others" whose actions, suits, debts, etc. "are, shall or might be in any wise disturbed, hindered, delayed or defrauded" by the conveyance. Section 3 established two penalties for the parties to the fraudulent conveyance. Besides imprisonment, the parties were to forfeit one year's value of the lands and the whole value of the goods, to be divided equally between the Crown and the aggrieved parties. Section 6 contained the important proviso that the Act did not extend to a conveyance

> . . . upon good consideration and bona fide lawfully conveyed or assured to any person or persons . . . not having at the time of such conveyance or assurance to them made, any manner of notice or knowledge of such covin, fraud or collusion.

A literal reading of the Statute of Elizabeth suggests that its intention was simply to create a criminal penalty for prohibited conveyances, but in the next year *Mannocke's Case*[10] decided that the Act permitted a court to treat such a transfer as voidable for the purpose of an execution against the property.[11] The later and better known decision in *Twyne's Case*[12] further extended the usefulness of the statute by applying a liberal construction and by permitting the Crown (and therefore a plaintiff creditor) to prove the fraudulent intent of the parties by reference to the surrounding and suspicious circumstances.[13] The effect of these and other cases was to make the Statute of Elizabeth a useful weapon in the hands of the creditor faced by a fraudulent conveyance.

Since 1570, the courts have built up a large body of law discussing the elements which must be established to bring a transaction within the Act. Although the cases are technically constructions of the statute, it has been argued that

> . . . actually a whole body of common law relating to fraudulent transfer sprang up upon the premise that the statutes were only declaratory of the common law and 'that the common law would have attained every end proposed by the statutes 13 El. c. 5, and 27 El. c. 4' (Lord Mansfield, in *Cadogan v. Kennett* (1776), 2 Cowp. 433 at 434 (K.B.).[14]

In this century, the Statute of Elizabeth was repealed and replaced by the similar s. 172 of the Law of Property Act, 1925.[15]

The fraudulent conveyance legislation discussed above had the weakness that it did not prohibit a debtor from preferring one creditor over the others, unless

10 (1571), 73 E.R. 661.

11 Glenn, *Fraudulent Conveyances and Preferences* (revised ed. 1940), pp. 79-96.

12 (1601), 76 E.R. 809.

13 See Holdsworth, *A History of English Law* (3rd ed. 1945), vol. 4, p. 481; Epstein, Landers and Nickles, *Debtors and Creditors: Cases and Materials* (3rd ed. 1987), pp. 86-88.

14 Riesenfeld, *Cases and Materials on Creditors' Remedies and Debtors' Protection (2nd ed. 1975), p. 355.*

15 1925 (15 Geo. 5), c. 20.

the alienation could be described as "a mere cloak to secure a benefit to the grantor".[16] This permissive attitude towards preferential treatment might well be proper in a legal system in which individual creditors ranked in order of delivery of their writs to the sheriff, but it was less acceptable under the Bankruptcy Acts where pari passu sharing was the governing principle. As a result, the courts from the time of Lord Mansfield held that

> . . . a fraudulent preference by a debtor, if made on the eve of, and followed by, the bankruptcy of the debtor, has been void against his creditors; because it aims at preventing that equal distribution of assets among the creditors, which has always been the object of those laws.[17]

Before 1869, the rule had no specific statutory basis, but the Bankruptcy Act of that year included a fraudulent preference section[18] not unlike s. 73(1) of the present Canadian Bankruptcy and Insolvency Act[19] with the addition of a proviso protecting purchasers in good faith and for valuable consideration. A similar section can be found in the current English Bankruptcy Act.[20]

(b) Canadian Legislation on Fraudulent Conveyances and Preferences

It was decided early by American[21] and Canadian[22] courts that the Statute of Elizabeth and the large body of judge-made rules that had grown up around it had become part of local law, at least as a civil remedy for creditors. Whether or not the penalty and criminal sanctions in the statute are also part of Canadian law is more doubtful.[23] Most American jurisdictions soon passed legislation intended to

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16 17 Hals. (3d) "Fraudulent and Voidable Conveyances", para. 1267.

17 Kerr on the Law of Fraud and Mistake (7th ed. 1952), p. 394; *Re Wilcoxon, Ex parte Griffith* (1883), 23 Ch. D. 69 at 74 (C.A.).

18 Bankruptcy Act, 1869 (32 & 33 Vict.), c. 71, s. 92.

19 R.S.C. 1985, c. B-3.

20 Bankruptcy Act, 1914 (4 & 5 Geo. 5), c. 59, s. 44.

21 Countryman, *Cases and Materials on Debtor and Creditor* (2nd ed. 1974), p. 129.

22 Numerous cases assume that the statute is part of Canadian law: see especially *Millar v. McTaggart* (1891), 20 O.R. 617 (C.A.); *Bank of Montreal v. Reis*, [1925] 3 D.L.R. 125 (Sask. K.B.); *Petryshyn v. Kochan*, [1940] 2 W.W.R. 353 (Sask. K.B.); *Goyan v. Kinash*, [1945] 2 D.L.R. 749 (Alta. T.D.); *McGillan v. McGillan*, [1947] 4 D.L.R. 456 (N.B.C.A.); *Meeker Cedar Products Ltd. v. Edge* (1968), 12 C.B.R. (N.S.) 49, affirmed without written reasons 12 C.B.R. (N.S.) 60 (S.C.C.); *Bank of Montreal v. Crowell* (1980), 67 A.P.R. 292 (N.S.T.D.); *Sembaliuk v. Sembaliuk* (1983), 27 Alta. L.R. (2d) 223, 229-30, reversed on other grounds (1984), 35 Alta. L.R. (2d) 193 (C.A.), leave to appeal to S.C.C. refused (1985), 35 Alta. L.R. (2d) x1; *Wright (Trustee of) v. Wright* (1986), 3 R.F.L. (3d) 193 (N.S.S.C.); Bouck, "Introducing English Statute Law into the Provinces: Time for a Change?" (1979), 57 Can. Bar Rev. 74; Côté, "The Introduction of English Law Into Alberta" (1964), 3 Alta. Law Rev. 262 at 281; Law Reform Commission of Saskatchewan, *The Status of English Statute Law in Saskatchewan* (1990), pp. 146-51, 158, 301; Parker, *Frauds on Creditors and Assignments for the Benefit of Creditors* (1903), p. 1. The repeal of the Statute of Elizabeth in England in 1925 does not affect its continued validity in Canada: see *Bank of Montreal v. Crowell, supra*.

23 *Cf. Millar v. McTaggart, supra*, note 22; *Connors v. Egli*, [1924] 1 W.W.R. 1050 (Alta. C.A.).

replace the English law. These statutes caused problems with the result that a Uniform Fraudulent Conveyance Act and later a Uniform Fraudulent Transfer Act have been drafted and widely adopted.[24]

The history of analogous Canadian legislation is more complicated. As early as 1859, Ontario enacted sections prohibiting fraudulent conveyances and preferences.[25] Ten years later, the federal government, which has constitutional jurisdiction over bankruptcy and insolvency,[26] asserted that power by passing the Insolvent Acts of 1869 and 1875,[27] but these Acts were repealed in 1880.[28] From that date to the passage of the Bankruptcy Act of 1919, there was no federal bankruptcy or insolvency legislation in existence. As a result, several provincial governments passed Assignments Acts, which permitted an insolvent debtor to make an assignment of property to an authorized trustee licensed by the province. These statutes invariably contained a group of sections directed against fraudulent conveyances and preferences.[29]

When the federal government re-entered the bankruptcy field in 1919,[30] some provinces retained their assignments statutes intact while others repealed all but the fraudulent preference and conveyance sections.[31] If the latter course of action was adopted, the results were usually called Fraudulent Preference Acts despite the fact that they and the predecessor Assignments Acts usually legislated against conveyances designed to hinder creditors generally as well as preferences to individual creditors.[32] All Canadian jurisdictions today except three[33] have either an Assignments Act, dating from the period between 1880 and 1919, or a Fraudulent Preference Act.

In addition to this legislation, some Canadian provinces passed Fraudulent Conveyance Acts based more or less closely on the Statute of Elizabeth. Indeed, British Columbia's Act was, until the 1979 revision, a word-for-word reproduc-

24 On American law, see Epstein, Landers and Nickles, *supra*, note 13, pp. 86-108; Nickles and Epstein, *Creditors' Rights and Bankruptcy* (1989), pp. 181-212; Riesenfeld, *Cases and Materials on Creditors' Remedies and Debtors' Protection* (4th ed. 1987), pp. 347-89.

25 Relief of Insolvent Debtors Act, C.S.U.C. 1859, c. 26, ss. 17-20.

26 Constitution Act, 1867, s. 91.

27 Insolvency Act, 1869 (Can.), c. 16; Act Respecting Insolvency, 1875 (Can.), c. 16.

28 Insolvency Acts Repeal Act, 1880 (Can.), c. 1.

29 The earliest Assignment Act was passed by Ontario in 1885: see An Act Respecting Assignments for the Benefit of Creditors, 1885 (Ont.), c. 26. The Act incorporated in somewhat modified form the older fraudulent preference sections referred to *supra*, note 25. See also *Bankruptcy and Insolvency: Report of the Study Committee on Bankruptcy and Insolvency Legislation* (1970), pp. 13-16.

30 Bankruptcy Act, 1919 (Can.), c. 36.

31 For an account of this process in Alberta, see *Connors v. Egli*, *supra*, note 23, pp. 1055-67.

32 *E.g.*, *cf.* s. 4(1) with s. 4(2)-(5) in the Ontario Assignments and Preferences Act, R.S.O. 1990, c. A.33. Most Canadian Fraudulent Preference or Assignments Acts have similar sections.

33 Manitoba repealed its Assignments Act in 1984. See Statute Law Amendment Act (1984), (Man.), c. 17, s. 2. Newfoundland has a Fraudulent Conveyances Act, R.S.N. 1990, c. F-24, modelled roughly on the Statute of Elizabeth but no Assignments or Fraudulent Preferences Act. The Northwest Territories has no legislation on fraudulent conveyances or preferences.

tion of part of its Elizabethan model.[34] At present, four[35] provinces have Fraudulent Conveyances Acts in addition to their fraudulent preference legislation. Unlike the United States, there is no uniform legislation on the subject, the only consistency flowing from the favourite Canadian practice of copying Ontario or, in some cases, English statutes.

One might have thought that the passage in a Canadian jurisdiction of legislation along the lines of the Statute of Elizabeth would have the implied effect of repealing the English Act. The case law which concerns the Assignments or Fraudulent Preference Acts of several provinces is divided in result, but most judges have held the Statute of Elizabeth not to be repealed by the Canadian legislation.[36] The result should be different in the four jurisdictions which have passed pure fraudulent conveyance legislation.[37]

In the next section, it is intended to consider the law which has grown up around the Statute of Elizabeth and the Canadian fraudulent conveyance legislation. The Fraudulent Preference Acts, including their fraudulent conveyance provisions, will be left until section 4.

One final comment should be made about the constitutionality of the provincial legislation. Since the *Voluntary Assignments* case in 1894,[38] there has been much judicial consideration of and disagreement about the respective federal and provincial spheres of jurisdiction in the field of fraudulent preferences and conveyances. It is not intended to review the discussion here, but it is essential to note the recent decision of the Supreme Court of Canada in *Robinson v. Countrywide Factors Ltd.*,[39] which upheld the constitutionality of the Saskatch-

34 Fraudulent Conveyances Act, R.S.B.C. 1960, c. 155 [now the Fraudulent Conveyance Act, R.S.B.C. 1979, c. 142].

35 Fraudulent Conveyance Act, R.S.B.C. 1979, c. 142; Fraudulent Conveyances Act, C.C.S.M., c. F160; Fraudulent Conveyances Act, R.S.N. 1990, c. F-24; Fraudulent Conveyances Act, R.S.O. 1990, c. F.29. I do not include for this purpose those jurisdictions which have fraudulent conveyance sections in fraudulent preference or assignments legislation: see *supra*, note 32. I will also not consider rules of court which contain similar provisions (which may, however, differ significantly from the legislation): see, *e.g.*, Alberta Rules of Court, R. 383 (1); *Faulhaber v. Ulseth* (1976), 66 D.L.R. (3d) 488 (Alta. T.D.); *Sauer v. Sauer* (1981), 33 A.R. 164 (Q.B.); *Saec Real Estate and Financial Corp. v. Paramount Motor Inns Ltd.* (1982), 20 Alta. L.R. (2d) 286 (Q.B.); *Woodmann Interiors Ltd. v. Zeh* (1989), 75 C.B.R. (N.S.) 100 (Alta. Q.B.).

36 *Bank of Montreal v. Reis*, *supra*, note 22; *Petryshyn v. Kochan*, *supra*, note 22; *Goyan v. Kinash*, *supra*, note 22; *Bank of Montreal v. Crowell*, *supra*, note 22; *Re Associated Fisheries of Canada Ltd.* (1987), 64 C.B.R. (N.S.) 242 (N.B.C.A.); Bouck, *supra*, note 22; Côté, *supra*, note 22; Kerr, *supra*, note 3, pp. 195-96; *contra Arnold v. Fleming*, [1923] 1 W.W.R. 706 (Alta. T.D.); *Huss v. Lakin*, [1925] 1 D.L.R. 38 (Sask. K.B.). After *Arnold v. Fleming*, the Alberta legislature amended the Fraudulent Preferences Act, R.S.A. 1922, c. 149, to provide expressly that the Statute of Elizabeth was still in force: see Statute Law Amendment Act, 1923 (Alta.), c. 5, s. 46. For the effect of that amendment and its omission from subsequent revised statutes, see *Connors v. Egli*, *supra*, note 23; *Goyan v. Kinash*, *supra*, note 22.

37 Dewar, "Fraudulent Conveyances and Preferences" in Law Society of Manitoba, *Remedies of the Unsecured Creditor* (1987), p. 3; Kerr, *supra*, note 3, p. 197; Springman, *supra*, note 3, p. 62.

38 *Ontario (Attorney General) v. Canada (Attorney General)*, [1894] A.C. 189 (P.C.).

39 [1978] 1 S.C.R. 753. As to the relative spheres of operation of the provincial and federal

ewan Fraudulent Preferences Act. One assumes that the same result should follow as to Fraudulent Conveyances Acts[40] and as to the fraudulent preference sections (at least) in Fraudulent Assignments and Preferences Acts.

3. Fraudulent Conveyances

(a) Generally

The purpose of the Statute of Elizabeth and of the Canadian Acts based on it, as interpreted by the courts, is to strike down all conveyances of property made with the intention of delaying, hindering or defrauding creditors and others except for conveyances made for good consideration and *bona fide* to persons not having notice of such fraud.[41] The legislation is couched in very general terms and should be interpreted liberally. Lord Mansfield concluded that the common law had always been strongly against fraud in every shape and that the Statute of Elizabeth "cannot receive too liberal a construction, or be too much extended in suppression of fraud".[42]

Relying on this policy, the courts have interpreted the statute to include any kind of alienation of property made with the requisite intent, the form of the transaction being immaterial.[43] The conveyance need not be in writ-

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fraudulent preference provisions, see *Henfrey & Co. v. Law Firm* (1983), 149 D.L.R. (3d) 736, 744-45 (B.C.S.C.).

40 *Re Panfab Corp.; Duro Lam Ltd. v. Last* (1970), 15 C.B.R. (N.S.) 20 (Ont. H.C.).

41 *Cf.* Rand, "Historical Basis of Fraud at Common Law" (1964), 3 W. Ont. L.R. 1 at 9:

> The essence of [the Statute of Elizabeth] is the condemnation of attempts to retain property by means of its simulated transfer to another. The fraud lies in that purpose of retention.

See also *Mulcahy v. Archibald* (1898), 28 S.C.R. 523 at 529; *Re Panfab Corp., supra*, note 39; *Anderson Lumber Co. v. Canadian Conifer Ltd.*, [1977] 5 W.W.R. 41 (Alta. C.A.); and *Clarkson Co. Ltd. v. Bank of N.S.* (1979), 32 C.B.R. (N.S.) 124 at 131, affirmed 34 C.B.R. (N.S.) 77 (N.S.C.A.). Can a fraudulent conveyance action be classified as an "action . . . founded on a tort" for the purpose of service ex juris? See *Suncorp Realty Inc. v. PLN Investments Inc.*, [1986] 1 W.W.R. 619 (Man. Q.B.) in which Jewers J. reviews the conflicting authority and concludes that a fraudulent conveyance is not a tort.

42 *Cadogan v. Kennett* (1776), 98 E.R. 1171 at 1172.

43 *Lee v. Glenval Holdings Ltd.* (1988), 85 A.R. 394 (Q.B.); *Chow v. Pearson* (1992), 12 C.B.R. (3d) 226 (B.C.S.C.); *Cadorange Pty. Ltd. (In Liq.) v. Tanga Holdings Pty. Ltd.* (1990), 20 N.S.W.L.R. 26; 18 Hals. (4th) "Family Arrangements, Undue Influence and Voidable Conveyances", para. 360; Parker, *supra*, note 22, c. 4; Robinson, *supra*, note 3, pp. 10-5 to 10-11. Where a debtor with an exigible RRSP collapses the plan and invests the proceeds in an exempt annuity, a series of cases have held such a transaction to be a "settlement" for the purposes of s. 91 of the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, or a conveyance in the context of the Statute of Elizabeth or provincial fraudulent conveyance legislation. See, *e.g.*, *Nicholson v. Milne* (1989), 67 Alta. L.R. (2d) 130 (Q.B.); *Technurbe Building Construction Ltd. v. McKinley* (1989), 70 Alta. L.R. (2d) 222 (Q.B.); *contra*, *Sovereign General Insurance Co. v. Dale* (1988), 32 B.C.L.R. (2d) 226 (S.C.); followed in *Re Sykes* (1993), 18 C.B.R. (3d) 148 (B.C.S.C.). See McKee, "Debtor-Creditor Issues Affecting Annuity Contracts" (1993), 12 Estates and Trusts J. 247, 278-80.

ing[44] nor need it involve a monetary benefit for the debtor.[45] The English and Canadian Acts often expressly invalidate suits, judgments and executions if the fraudulent intent is present.[46]

The Ontario Court of Appeal in *Optical Recording Laboratories Inc. v. Digital Recording Corp.*[47] has recently held that a conveyance to a creditor need not be challenged under fraudulent preference or assignments legislation, but can be attacked under the Fraudulent Conveyances Act. While flexibility is always desirable, the Ontario decision appears to run contrary to the long-established view that the Statute of Elizabeth and its Canadian counterparts do not prohibit a debtor from preferring one creditor over others unless the alienation can be described as "a mere cloak to secure a benefit to the grantor".[48] Indeed, fraudulent preference statutes were enacted to cure this very deficiency. In light of the glacial speed of reform of these creaky statutes, judicial rewriting of the law may be warranted. Whether other Canadian courts will follow *Optical Recording* remains to be seen.

An exception to this expansive view is *Sembaliuk v. Sembaliuk* in which the Alberta Court of Appeal held that a debtor's disclaimer of an interest in an estate is not a conveyance caught by the Statute of Elizabeth.[49] The decision has been the subject of controversy.[50]

Fraudulent conveyance legislation has been held to invalidate a conveyance

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44 *Thomas Flynn & Sons Construction (Toronto) Ltd. v. Laporte* (1990), 78 C.B.R. (N.S.) 158 (Ont. S.C.).

45 *Toronto Dominion Bank v. Miller* (1990), 3 C.B.R. (3d) 285 (Ont. Gen. Div.) — charitable donations.

46 See *Bank of Montreal v. Ewing* (1984), 55 C.B.R. (N.S.) 101, affirmed (1986), 59 C.B.R. (N.S.) 156 (Ont. C.A.); Gertner Casebook, *supra*, note 3, p. 543 (on the *Ewing* case). The effect of these provisions is unclear in jurisdictions with creditors' relief legislation, where an execution creditor, whatever the intent, is compelled to share with those who have writs or certificates in the sheriff's office; see Dore and Kerr, *Third Report of the Consumer Protection Project: Legal Remedies of the Unsecured Creditor after Judgment* (N.B. 1976, pp. 106-07 (unpublished)).

47 (1990), 1 O.R. (3d) 131 (C.A.); followed in *Canadian Imperial Bank of Commerce v. Graat* (1992), 5 B.L.R. (2d) 271, 295-300 (Ont. Gen. Div.). See also *Lee v. Glenval Holdings Ltd.*, *supra*, note 43.

48 *Supra*, note 16 and accompanying text. See also Springman, "Fraudulent Conveyances Under the Fraudulent Conveyances Act and the Assignments and Preferences Act", in Canadian Bar Association — Ontario, *supra*, note 3, pp. 1-5.

49 *Sembaliuk v. Sembaliuk*, *supra*, note 22; followed in *Bank of Nova Scotia v. Chan* (1987), 26 E.T.R. 180 (Man. Q.B.).

50 Law Reform Commission of B.C., *supra*, note 3, pp. 10-16, 94-97; Springman, "The B.C. Law Reform Commission's Report on Fraudulent Conveyances and Preferences" (1989), 15 Can. Bus. L.J. 180, 191-97; Springman, *supra*, note 3, pp. 79-92. The American courts and legislatures have adopted differing answers to the issue. See Gamin, "Renunciation of Testamentary Benefit as Fraudulent Transfer" (1986), 37 Case Western Reserve L. Rev. 148; Parker, "Can Debtors Disclaim Inheritances to the Detriment of their Creditors?" (1993), 25 Loyola Univ. Chicago L.J. 31.

of any kind of exigible or attachable property[51] of the debtor,[52] so long as it is of some real value.[53] Property which would be exempt from execution or attachment,[54] or property which the debtor holds in trust for the transferee[55] cannot be the subject of a fraudulent conveyance action.

The statute and its progeny are less significant today than hitherto, in part because of the enactment of legislation requiring the registration of personal property security agreements on pain of those agreements being void as against creditors. However, the Fraudulent Conveyances Acts still have a useful role to play if creditors or trustees in bankruptcy wish to reach property which has been placed beyond their grasp by the debtor, especially in circumstances where the analogous sections of the Bankruptcy and Insolvency Act cannot be applied.

(b) Voluntary Conveyances

Where the debtor has given property to a donee for nothing or for nominal consideration, the courts have held that, in considering whether the transaction is voidable[56] under the Statute of Elizabeth, it is necessary to consider only the intent of the debtor.

> Assuming his intent to be fraudulent within the meaning of the statute, it does not matter whether or not the donee had knowledge or notice of that intent; for the donee is not within the exception made by the statute in favour of *bone fide* purchasers. A

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51 *Cas's Mechanical Services Inc. v. Topping* (1989), 77 C.B.R. (N.S.) 145 (Sask. Q.B.); *Canadian Imperial Bank of Commerce v. Hallahan* (1990), 48 B.L.R. 113 (Ont. C.A.); *A. & B. Landscaping & Interlocking Ltd. v. Bradsil Ltd.* (1993), The Lawyer's Weekly (March 4, 1994), p. 15 (Ont. Gen. Div.); Hals., *supra*, note 43, para. 361; Hansford, *supra*, note 3, pp. 109-10; Kerr, *supra*, note 3, p. 201; Kerr, *supra*, note 17, pp. 304-07; Robinson, *supra*, note 3, pp. 10-3 to 10-5.

52 *Rosenfeldt v. Olson* (1984), 16 D.L.R. (4th) 103, 118-20, reversed on different grounds (1986), 25 D.L.R. (4th) 472 (B.C.C.A.), leave to appeal to S.C.C. refused 72 N.R. 77 (S.C.C.).

53 Parker, *supra*, note 22, p. 21, citing *Ithaca Gas Light Co. v. Treman* (1883), 93 N.Y. 660.

54 See *supra*, Chapter 13, sections 2(i), 4; *Salter v. WYO-BEN Products Inc.* (1972), 25 D.L.R. (3d) 626 (Alta.); *cf. Toronto Dominion Bank v. Fisher* (1988), 69 C.B.R. (N.S.) 22 (Ont. S.C.). But see Springman, *supra*, note 3, pp. 74-79; Springman, *supra*, note 48, pp. 9-14.

55 Compare *Tempo Building Supplies Ltd. v. Pitura* (1979), 33 C.B.R. (N.S.) 23 (B.C.S.C.); *Bank of Nova Scotia v. Brickell* (1980), 22 B.C.L.R. 222 (S.C.); *Canadian Imperial Bank of Commerce v. Fenner* (1983), 34 R.F.L. (2d) 167 (Ont. H.C.); *Price Waterhouse Ltd. v. Arnoff* (1983), 45 C.B.R. (N.S.) 210 (Ont. C.A.); *Manuliak v. Sapach* (1985), 34 Man. R. (2d) 261 (Q.B.); *Serenity Farms Limited v. Traversa* (1985), 55 C.B.R. (N.S.) 214 (Ont. S.C.); *Re Deamond* (1987), 65 C.B.R. (N.S.) 92 (N.S.S.C.); *Ling v. Chinavision Canada Corp.* (1992), 10 O.R. (3d) 79 (Ont. Gen. Div.).

56 Despite the apparently absolute words of the statute, the courts have held that a fraudulent conveyance is voidable and not void: see Hals., *supra*, note 43, para. 359; 13 C.E.D. (Ont. 3rd) *Fraudulent and Voidable Conveyances*, para. 7. See also *J.W. Bird and Co. v. Downey Bldg. Supplies Ltd.* (1979), 32 N.B.R. (2d) 504 (T.D.). In the situation where the transferee reconveys the property to a *bona fide* purchaser, there has been much discussion about the right of the plaintiff to recover the proceeds of the disposition: see now *Westinghouse Can. Ltd. v. Buchar* (1975), 59 D.L.R. (3d) 641 (Ont. C.A.), and cases cited therein. See also *Re Dyck* (1982), 21 Sask. R. 93 (Q.B.); Ontario Law Reform Commission, *supra*, note 3, pp. 157-60, 221-24, 233-34; *Bernard v. Weiss* (1986), 70 B.C.L.R. 318 (S.C.); *cf. Gooseaire Humidification Ltd. v. Knowles Brothers Ltd.* (1979), 27 N.B.R. (2d) 541 (Q.B.).

> volunteer cannot be said to be injured by the gift to him being defeated; no loss is inflicted on him; he is only deprived of a gain to which others had a better right.[57]

The intent which vitiates a transaction may also be the intent of the debtor's agent.[58]

The crucial problem in any fraudulent conveyance action is to establish the fraudulent intention of the debtor, a task which creates serious problems for counsel and judge alike. In an early comment in the *Law Times*, an anonymous writer speculated on the difficulties associated with the requirement of a judicial finding of fraud in a similar provision in the English Bankruptcy Act:

> The court must therefore proceed to ascertain the state of mind of the debtor. Judicial inquiry into motive is a difficult and delicate matter, and hitherto has not in any branch of jurisprudence been attended with very happy results. It is not disrespectful to say that metaphysical excursions of this sort are responsible for some fine confused pages in our English law reports; the conditions of inquiry are such that it could hardly be otherwise. With regard to the section, it is not merely the object intended to be affected by the deed, which, according to decisions, is to be ascertained. That — as in the case under consideration — would ordinarily present few features of difficulty. It is the dominant motive at the back of the debtor's mind which is to be searched for; an inquiry into the working of human nature affording scope for the display of every eccentricity of speculation.[59]

The Statute of Elizabeth forces the judge into a similarly speculative exercise.

In an oft-quoted passage, Kerr wrote that the cases in which fraudulent conveyances are held to be voidable as against creditors whose claims exist at the time of the conveyance may be divided into two groups, namely:

> (1) those in which the fraudulent intent, though not apparent as a fact in evidence in the case, is established as a presumption of law; and (2) those in which such intent appears as a fact in evidence.[60]

The first class of case obviously involves an attempt by the courts to apply the statute without engaging in the metaphysical excursion into the debtor's state of mind deplored by the writer in the *Law Times*. Even in the second type of case, the courts have been ready to rely on the surrounding circumstances as establishing *prima facie* the intent to defraud or delay. The so-called badges of fraud articulated in *Twyne's Case*[61] are nothing more than typical and suspicious fact situations which may be enough to enable the court to make a finding of fraud unless the debtor leads evidence to rebut the presumption. Again the courts are

57 Kerr, *supra*, note 17, p. 308. The date on which fraudulent intent is to be assessed is the date of execution of the conveyance. See *Bank of Montreal v. Chu* (1994), 24 C.B.R. (3d) 136 (Ont. Gen. Div.).

58 Parker, *supra*, note 22, pp. 44-45, citing *Barwick v. English Joint Stock Bank* (1867), L.R. 2 Exch. 259; *Warner v. Warren* (1871), 46 N.Y. 228.

59 G.A.M. "Fraudulent Conveyances to Creditors" (1898), 105 L.T. 266 at 267.

60 Kerr, *supra*, note 17, p. 308.

61 *Supra*, note 12.

driven to the surrounding circumstances to assist them in making the necessary finding of fact under the statute.

The difficulty in proving the debtor's fraudulent intent is obvious, and the judges' effort to make the decision easier by developing evidentiary rules to assist them is understandable. However, much of this law originated long before the modern analyses of the principles of evidence by Thayer, Wigmore and others with the result that the cases are full of ambiguous and unhelpful terms like irrebuttable (or rebuttable) presumptions of law, presumptions of fact and so on. It is not possible here to reconstruct the law of fraudulent conveyances in the terminology currently approved by evidentiary theorists,[62] but it is essential to be aware of the somewhat dated and unclear notions which underlie many of the standard cases and texts on the subject. My discussion will follow the two-part analysis quoted from Kerr, but it is at least arguable that the presumptions which operate in both types of cases are not basically different in their nature and effect.

Kerr's first class consists of "those [cases] in which the fraudulent intent, though not apparent as a fact in evidence in the case, is established as a presumption of law".[63] The English law on the nature of this "presumption of law" is confusing, the courts having apparently taken different positions on the effect of the presumption. The confusion can be illustrated by discussing the two leading cases.

In *Freeman v. Pope*,[64] the debtor was an elderly clergyman who had some assets, including a life insurance policy. He had as well a number of creditors who were pressing him. On March 3, 1863, the debtor assigned to trustees for Julia Pope the life insurance policy and covenanted to pay the premiums. On the same date, he assigned his other assets or their income to some of his creditors, effectively rendering himself insolvent as of that date. He subsequently paid some debts but acquired more and died, leaving no assets whatever for his creditors. One of them, a tradesman who had supplied goods to the settlor after March 3, 1863, commenced an action to set aside the assignment of the life insurance policy to Pope. The plaintiff succeeded at trial and Pope appealed.

Lord Hatherley L.C. began his judgment with a magnificent, if somewhat sweeping, aphorism:

> The principle on which the statute of 13 Eliz. c. 5 proceeds is this, that persons must be just before they are generous, and that debts must be paid before gifts can be made.[65]

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62 See, *e.g.*, Denning, "Presumptions and Burdens" (1945), 61 L.Q.R. 379; Schiff, *Evidence in the Litigation Process* (4th ed. 1993), c. 16; Sopinka, Lederman and Bryant, *The Law of Evidence in Canada* (1992), c. 4.

63 Kerr, *supra*, note 17, p. 308.

64 (1870), 5 Ch. App. 538.

65 *Supra*, note 64, p. 540. The proverb is not original; versions of it are found in Sheridan, Marryat and Dickens. See Dunlop, "Debtors and Creditors in Dickens' Fiction", in Michael Timko, Fred Kaplan, and Edward Guiliano, eds., *Dickens Studies Annual: Essays on Victorian Fiction*, vol. 19 (New York: AMS Press, 1990), pp. 25, 28.

He went on to note that the trial judge had expressed the view that if he, as a special juryman, had been asked whether the settlor had actually intended to defeat, hinder or delay his creditors, he should have concluded that he had no such intention. The Lord Chancellor commented that this did not put the question exactly on the right ground,

> . . . for it would never be left to a special jury to find, *simpliciter*, whether the settlor intended to defeat, hinder, or delay his creditors, without a direction from the Judge that if the necessary effect of the instrument was to defeat, hinder, or delay the creditors, that necessary effect was to be considered as evidencing an intention to do so. A jury would undoubtedly be so directed, lest they should fall into the error of speculating as to what was actually passing in the mind of the settlor, which can hardly ever be satisfactorily ascertained, instead of judging of his intention by the necessary consequences of his act, which consequences can always be estimated from the facts of the case.[66]

There might well be cases where there was direct and positive evidence of an intention to defraud — Kerr's second class.

> But it is established by the authorities that in the absence of any such direct proof of intention, if a person owing debts makes a settlement which subtracts from the property which is the proper fund for the payment of those debts, an amount without which the debts cannot be paid, then, since it is the necessary consequence of the settlement (supposing it effectual) that some creditors must remain unpaid, it would be the duty of the Judge to direct the jury that they must infer the intent of the settlor to have been to defeat or delay his creditors, and that the case is within the statute.[67]

Giffard L.J. also gave judgment to the same effect.

The second important English case is *Re Wise; Ex parte Mercer*,[68] decided 16 years later. The bankrupt Wise was a master mariner, who in 1881 was engaged to be married to Miss Vyse. However, while in Hong Kong in the course of a voyage, he married another lady. In August of 1881, the slighted Miss Vyse sued the bankrupt for breach of promise and he was served with the writ in Hong Kong. About the same time, Wise was informed that a legacy of £500 had vested in him. He promptly assigned the legacy to a trustee to invest the same and to pay the income during the joint lives of Wise and his wife to his wife and then to the survivor of the two. After the death of the survivor, the trustee was to hold the trust fund for the children of the marriage and in default of children for Wise absolutely. In 1882, Miss Vyse obtained what Lord Esher described as a "vindictive" and "startling"[69] judgment for £500 damages. In 1884, Wise was adjudicated a bankrupt.

Wise's trustee in bankruptcy challenged the settlement of the legacy as fraudulent and void and was successful in the County Court. The decision was reversed by the Divisional Court, whose judgment was upheld by the Court of

66 *Ibid.*
67 *Supra*, note 64, p. 541.
68 (1886), 17 Q.B.D. 290 (C.A.).
69 *Supra*, note 68, p. 300.

Appeal. The reasoning of the judges is complicated and should be examined closely.

Lord Esher M.R. described the argument of the trustee in bankruptcy as follows:

> It is necessary to prove that the bankrupt, at the date of the voluntary settlement, intended to defeat and delay a creditor or his creditors generally; the necessary consequence of what he did was to defeat and delay his creditors; and, therefore, as a proposition of law, the tribunal which had to consider whether he did intend to defeat and delay his creditors was bound to find that he did.[70]

Lord Esher noted that "dicta of great and eminent judges"[71] were cited in support of the argument, but he rejected it firmly.

> I will venture to say as strongly as I can that to my mind that proposition is monstrous. It is said that it is a necessary inference that a man intends the natural and necessary result of his acts. If you want to find out the intention in a man's mind, of course you cannot look into his mind, but, if circumstances are proved from which you believe that he had a particular intention, you infer as a matter of fact that he had that intention. No doubt, in coming to a particular conclusion as to the intention in a man's mind, you should take into account the necessary result of the acts which he has done. I do not use the words 'necessary result' metaphysically, but in their ordinary business sense, and of course, if there was nothing to the contrary, you would come to the conclusion that the man did intend the necessary result of his acts. But, if other circumstances make you believe that the man did not intend to do that which you are asked to find that he did intend, to say that, because that was the necessary result of what he did, you must find, contrary to the other evidence, that he did actually intend to do it, is to ask one to find that to be a fact which one really believes to be untrue in fact.[72]

Lord Esher then added an ambiguous and controversial reservation to the above conclusion.

> Whether the fact that the necessary effect of a voluntary deed is to defeat or delay the creditors of the grantor will make the deed void under the statute of Elizabeth, although there was no such intent in his mind at the time when he executed it, is a question which we are not now called upon to decide. But that is a question wholly independent of the question of intention. That may be the law; the Courts may have put that construction on the statute. But that is a different proposition from that which was put forward in argument, and I will not undertake to decide it now.[73]

Lord Esher went on to hold that at the time of the settlement the bankrupt owed no one any money except Miss Vyse, and the amount of her recovery in the breach of promise action was highly speculative. Wise was not therefore insolvent, it was not the necessary consequence of his settlement to defeat his creditors and he had no intention to do so.

70 *Supra*, note 68, p. 298.
71 *Ibid.*
72 *Supra*, note 68, pp. 298-99.
73 *Supra*, note 68, p. 299.

Lindley L.J. conceded that voluntary settlements were often set aside under the statute in cases where there was no actual intention to defraud but where the circumstances were such that the settlement, if executed, must have that effect.

> But the language which has been used in a great many cases, that a man must in point of law be held to have intended the necessary consequences of his own acts, is apt to mislead, by confusing the boundary between law and fact, and by consequences which can be foreseen with those which cannot.[74]

Lindley L.J. then concluded that no case went so far as to invalidate this settlement.

Lopes L.J. was careful to confine his remarks to the narrow facts before him.

What exactly do these two cases decide? Are the rules or presumptions flowing from the decisions consistent with each other or do they lead in different directions? These issues are much discussed in the literature on fraudulent conveyances but no clear answers have emerged.

Lord Hatherley in *Freeman v. Pope* is clear that the actual intent of the debtor need not be considered if the necessary effect of the conveyance is to defeat, hinder or delay the creditors. Indeed, given proof of this necessary effect, evidence of intent would appear to be irrelevant, at least if the Lord Chancellor's remarks are to be taken literally.

When can it be said that the necessary effect of a transaction is to defeat creditors? Lord Hatherley responds that if a person owing debts makes a settlement which subtracts from the debtor's property an amount without which the debts cannot be paid, the statute has been satisfied and actual evidence of the intent is unnecessary if fraudulent, and irrelevant if the reverse.

This aspect of Lord Hatherley's judgment can best be understood as the conclusion to an earlier dispute.[75] Before *Freeman v. Pope*, there were cases which had suggested that a person was indebted and a transfer therefore invalidated if that person had only one unsatisfied debt and was solvent before and after the transfer. On the other extreme were cases which required insolvency in the sense that the donor's total liabilities exceeded total assets. The solution adopted by Lord Hatherley is a sensible compromise and one which has been much approved since 1870.

What is less clear is the status and limits of the basic presumption developed by the Lord Chancellor. If the necessary effect of the transfer is to defeat creditors, evidence of actual intent is simply irrelevant. But those who support the transfer may seek to defend it by leading evidence, not of intent, but of other surrounding circumstances which will explain or rebut the plaintiff's evidence that the necessary effect of the transaction is to defeat creditors. Such evidence would appear to be admissible and indeed essential if the defendant is to disperse the cloud of suspicion surrounding the conveyance.

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74 *Supra*, note 68, p. 301.

75 See Kerr, *supra*, note 17, pp. 308-09.

When we come to examine *Re Wise; Ex parte Mercer*, we are driven to the conclusion that the *dicta*, if not the decision in that case, tend against the presumption expressed by Lord Hatherley in *Freeman v. Pope*. Lord Esher poses the problem, hypothetical on the facts of the *Ex parte Mercer* case, of a transaction, the necessary result of which is to defeat creditors. The issue is whether those supporting the transaction can lead evidence of circumstances intended to establish that the donor did not intend to defeat any creditors. Lord Esher is clear, not only that such evidence is admissible but that, if convincing, it must decide the case in favour of the defendant. Neither the presumption relied on in *Freeman v. Pope* nor the related presumption that people intend the natural results of their acts prevents this result although either presumption may make it more difficult for the defendant to convince the tribunal.

The above account of Lord Esher's statement is satisfactory if we ignore the ambiguous reservation passage in his judgment, which we quoted above.[76] This writer has difficulty in seeing this passage as anything but directly inconsistent with the thrust of his judgment taken as a whole. The overall effect of *Ex parte Mercer* is therefore less than crystal clear.

It might be interesting and useful to analyze the rules developed in our two leading cases in terms of the distinction between justifiable inferences and compelled-unless determinations discussed by Schiff in his casebook, *Evidence in the Litigation Process*.[77] In the space available, it is intended to take the less ambitious course of reviewing subsequent English and Canadian cases on the requirement to see how the two currents of authority have developed.

The English cases since *Ex parte Mercer* have cited with approval both that case and *Freeman v. Pope* without making a clear choice between them.[78] *Underhill on Trusts* describes the problem as "one of great doubt and difficulty"[79] and goes on to speculate that *Ex parte Mercer* may only have decided that the statute did not apply

> . . . where there was no actual intent to defraud, and *the inevitable result of the settlement was not at its date to defeat or delay then existing creditors*, . . . leaving it still open to argument whether in the latter case a settlement was avoided irrespective of intention.[80]

76 *Supra*, note 68, p. 299.

77 *Supra*, note 62. See also the report of the Ontario Law Reform Commission, *supra*, note 3, p. 133, which argues that most fraudulent conveyance and preference cases are determined objectively, "having regard to the actions of the parties and the debtor's financial position at the time of the transaction". A majority of the Commission goes on to recommend (at p. 211) that "a creditor should be entitled to have a conveyance by a debtor to a third party (not being a creditor) set aside where the effect of the conveyance was to defeat, hinder, delay, or defraud one or more of the debtor's creditors".

78 See *Godrey v. Poole* (1888), 13 App. Cas. 497 (P.C.); *Re Holland; Gregg v. Holland*, [1902] 2 Ch. 360 (C.A.); *Carruthers v. Peake* (1911), 55 Sol. Jo. 291.

79 Underhill's *Law Relating to Trusts and Trustees* (13th ed. 1979), p. 217.

80 *Supra*, note 79, p. 216.

The rewriting of the Statute of Elizabeth in the Law of Property Act, 1925,[81] has created still further interpretation problems which mercifully need not be considered here.[82]

The issue remains unsettled in Canada as in England. There are several cases,[83] including one in the Supreme Court,[84] which quote with approval the presumption in *Freeman v. Pope*. On the other hand, *Ex parte Mercer* also has been followed.[85] Perhaps the most helpful Canadian case is *Mandryk v. Merko*,[86] in which Freedman J.A. (as he then was) wrote a perceptive and convincing decision adopting the *Ex parte Mercer* rule in preference to the more strict presumption adopted in *Freeman v. Pope*. Future courts will hopefully emulate Freedman J.A. in his direct attack on the problem rather than by simply citing *dicta* from one or the other stream of authority as if there was no problem at all.

Our discussion to this point has centered on Kerr's first class of cases in which the fraudulent intent is established by what he calls a "presumption of law". Kerr's second group of situations, namely, "those in which such intent appears as a fact in evidence", need not be discussed here. The problem of proving fraudulent intent is common to cases involving Kerr's second class of voluntary conveyances and to conveyances for consideration, and we should first explain the very different rules which apply to the latter class of transfers.

(c) Conveyances for Consideration

The Statute of Elizabeth and its Canadian counterparts have always created an exception for *bona fide* transfers for consideration. Section 6 of the English

81 *Supra*, note 15.

82 See Langstaff, "The Cheat's Charter?" (1975), 91 L.Q.R. 86.

83 *Killops (Killips) v. Porter* (1916), 9 W.W.R. 949 (Alta. T.D.); *Baxter v. Derkasz*, [1929] 1 W.W.R. 673 (Sask. C.A.); *McGillan v. McGillan*, *supra*, note 22; *China Software Corp. v. Leimbigler* (1990), 49 B.L.R. 173 (B.C.S.C.); *cf. Bank of Montreal v. Crowell*, *supra*, note 22; *Bank of Montreal v. Kelliher* (1980), 36 C.B.R. (N.S.) 205 (B.C.S.C.); *Royal Bank v. First Pioneer Investments Ltd.* (1979), 27 O.R. (2d) 352, affirmed 32 O.R. (2d) 121 (C.A.); *Canadian Imperial Bank of Commerce v. G.E. Cox Limited* (1985), 169 A.P.R. 374 (N.B.C.A.). See also *Coopers & Lybrand Ltd. v. Niton Junction Holdings Ltd.* (1979), 32 C.B.R. (N.S.) 141 (Alta. Q.B.); *Wilson Equipment Ltd. v. Union Construction Ltd.* (1979), 41 N.S.R. (2d) 1 (T.D.); *Re Dyck*, *supra*, note 56. *Cf.* Glenn, *supra*, note 11, pp. 462-67. Scane, "Fraudulent Conveyances" (1964), 3 W. Ont. L.R. 40 at 41-42, goes so far as to say that the presumption is "irrebuttable", a proposition which is not supported by the cases cited.

84 *Sun Life Assurance Co. v. Elliott* (1900), 31 S.C.R. 91; followed in *Bank of Montreal v. Chu*, *supra*, note 57. As Freedman J.A. points out in *Mandryk v. Merko* (1971), 19 D.L.R. (3d) 238 at 243 (Man. C.A.), the statements on the problem in *Sun Life* may fairly be regarded as *obiter*.

85 *Hogg v. Hogg* (1915), 25 Man. R. 226 (C.A.); *Lane v. Lane*, [1938] 2 W.W.R. 577 at 588-91 (Man. C.A.), *per* Trueman J.A., dissenting; *Mandryk v. Merko*, *supra*, note 84; *Newfoundland and Labrador Housing Corp. v. Ennis* (1987), 197 A.P.R. 22 (Nfld. T.D.). See also Jewers, "Fraudulent Conveyance and Preference Legislation in Canada" (1956), 28 Man. Bar News 1 at 5-7.

86 *Supra*, note 84; relied on in *Manuliak v. Sapach*, *supra*, note 55; *Holbrook v. Cedpar Properties Inc.* (1986), 62 C.B.R. (N.S.) 18 (Ont. S.C.); *Toronto Dominion Bank v. Miller*, *supra*, note 45. See also *Bank of Montreal v. Cyr* (1985), 158 A.P.R. 283 (N.B.C.A.).

statute provided that it did not extend to conveyances "upon good consideration and bona fide" made to transferees who did not have "at the time of such conveyance or assurance to them made, any manner of notice or knowledge of such covin, fraud or collusion as is aforesaid".[87] The Canadian Fraudulent Conveyances Acts follow the English pattern with some modifications which will be noted later.

Despite this proviso, it is possible to establish that a transfer for value is voidable under the statute, but the task has been said to be one of great difficulty.[88] The third edition of Halsbury stated the English law as follows:

> For creditors to be in a position to impeach an alienation of property by their debtor they must prove, in addition to fraudulent intent on the part of the grantor, either that the alienation was not made for valuable consideration *or upon good consideration*, or that the grantee was privy to the fraud. Otherwise the grantee will be entitled to the protection given by the provision, even where a creditor is in fact defeated by the grant.[89]

With the deletion of the italicized words, the quotation probably represents accurately the English law before the changes effected by the Law of Property Act, 1925,[90] and therefore the law as it was transmitted to all Canadian jurisdictions.

It is not intended to say much about the requirement of valuable consideration although there is a substantial body of case law on the subject. Before 1925, the English rule was that consideration need not be adequate to support the transfer, although it had to be more than nominal.[91] The English law may be different now because of the Law of Property Act, 1925,[92] but Canadian jurisdictions still adhere to the pre-1925 position.[93]

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87 *Supra*, note 4.

88 *Harman v. Richards* (1852), 68 E.R. 847 at 851. See also *Monteith v. Hayden* (1987), 205 A.P.R. 273 (N.B.C.A.); *Gresham v. Gresham* (1993), 18 C.B.R. (3d) 201 (B.C.C.A.).

89 Hals., *supra*, note 16, para. 1261 [the italics are mine].

90 *Supra, note 15. See Hals., supra, note 16, para. 1261, note (r); Langstaff, supra, note 82, pp. 87-89.*

91 Hals., *supra*, note 16, paras. 1262-64.

92 *Supra*, note 15. See now the 4th edition of Halsbury, *supra*, note 43, paras. 365, 371-72.

93 See *Killops v. Porter, supra*, note 83; *Banque d'Hochelaga v. Potvin*, [1924] 1 W.W.R. 488 (Alta. C.A.); *Re Cohen and Mahlin; Can. Credit Men's Trust Ass'n v. Spivak*, [1927] 1 W.W.R. 162 (Alta. C.A.); *Fuhr v. Fuhr*, [1936] 2 W.W.R. 237 (B.C.S.C.); *Owen Sound General and Marine Hospital v. Mann*, [1953] 3 D.L.R. 417 (Ont. H.C.); *Re Dougmor Realty Holdings Ltd.; Fisher v. Wilgorn Invt. Ltd.* (1966), 59 D.L.R. (2d) 432, reversed on other grounds 65 D.L.R. (2d) 419 (Ont. C.A.); *Meeker Cedar Products Ltd. v. Edge, supra*, note 22; *Commerce Capital Mortgage Corp. v. Jemmett* (1980), 37 C.B.R. (N.S.) 59 (Ont. H.C.); *Lange v. Lange* (1981), 14 Man. R. (2d) 153 (Q.B.); *Re Bishop* (1982), 45 C.B.R. (N.S.) 94 (N.S.T.D.); *Millwork & Building Supplies Limited v. Marchione* (1984), 53 C.B.R. (N.S.) 47 (Ont. S.C.); *India Films Overseas Limited v. Keefer Investments Inc.* (1984), 55 C.B.R. (N.S.) 154 (B.C.S.C.); *Re Laventure* (1985), 44 R.F.L. (2d) 158 (Alta. Q.B.); *Canadian Imperial Bank of Commerce v. Shapiro* (1985), 54 C.B.R. (N.S.) 134 (Ont. S.C.); *Bank of Montreal v. Ngo* (1985), 56 C.B.R. (N.S.) 66 (B.C.S.C.); *Re Nonis* (1984), 52 C.B.R. (N.S.) 297, affirmed (1986), 60 C.B.R. (N.S.) 183 (Ont. C.A.); *633746 Ontario Inc. (Trustee of) v. Salvati* (1990), 79 C.B.R. (N.S.) 72 (Ont. S.C.); Parker, *supra*, note 22, Ch. 10; *cf. China Software Corp. v. Leimbigler, supra*, note 83; *Bank of*

The principal problem in establishing that a transfer for value falls within the statute is to prove that the transferor had the necessary fraudulent intent and that the grantee was privy to the fraud. It may be useful to say something about both of these requirements.

In our discussion of voluntary transactions, we noted Kerr's division of the cases into two groups: (1) those in which the intent of the grantor can be established by a presumption of law and (2) those in which actual fraud is proven. When we turn to transfers for value, it appears that there is no presumption which can establish fraud and therefore no class (1) cases. In *Freeman v. Pope* itself, Giffard L.J. said that where transfers are founded on valuable consideration "an actual and express intent is necessary to be proved"[94] and the same rule has been echoed in several English[95] and Canadian[96] cases. The court may be suspicious that the intent of the grantor was fraudulent, but it is necessary to go further and to establish fraud as a fact.[97]

The courts have frequently dealt with the situation where the transfer has the effect of preferring one creditor at the expense of another. It is clear that, unless fraudulent intent can be brought home to the grantor, the conveyance will not fall within the statute even if its effect is to delay or defeat other creditors.[98] Some courts look at the transaetion to see if the debtor has retained some benefit or has kept control over the property which is alleged to have been sold.[99] Halsbury ex-

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Montreal v. Chu, supra, note 57; *Solar v. Kovacs*, [1994] 2 W.W.R. 534 (B.C.S.C.). The British Columbia, Manitoba and Ontario Fraudulent Conveyances Acts, *supra*, note 35, are modelled on the Statute of Elizabeth and not on the Law of Property Act, 1925, so that the pre-1925 English law should apply in those jurisdictions, a result borne out by the cases cited *supra*.

94 *Supra*, note 64, pp. 544-45.

95 *Holmes v. Penney* (1856), 69 E.R. 1035; *Re Johnson; Golden v. Gillam* (1881), 20 Ch.D. 389, affirmed (*sub nom. Golden v. Gillam*) 51 L.J. Ch. 503 (C.A.); Kerr, *supra*, note 17, pp. 342 and 350; *contra*, Langstaff, *supra*, note 82, p. 98.

96 *Hickerson v. Parrington* (1891), 18 O.A.R. 635; *Manitoba Brewing and Malting Co. v. McDonald* (1909), 11 W.L.R. 313 (Sask. K.B.); *Perkins Electric Co. v. Orpen* (1922), 70 D.L.R. 397 (S.C.C.); *Shephard v. Shephard* (1925), 56 O.L.R. 555 (C.A.); *Ferguson v. Lastewka*, [1946] 4 D.L.R. 531 (Ont. H.C.); *Owen Sound General and Marine Hospital v. Mann, supra*, note 93; *Bank of Montreal v. Vandine* (1952), 33 M.P.R. 368 (N.B.C.A.); *Reutcke v. Reutcke* (1958), 24 W.W.R. 417 (Man. Q.B.); *Royal Bank v. Thiessen* (1981), 12 Man. R. (2d) 260; *Devlin v. Hean* (1982), 41 B.C.L.R. 206 (S.C.); Parker, *supra*, note 22, p. 59.

97 See Scane, *supra*, note 83, p. 46.

98 *Pickstock v. Lyster* (1815), 105 E.R. 650; *Alton v. Harrison; Poyser v. Harrison* (1869), 4 Ch. App. 622 (L.J.); *Middleton v. Pollock; Ex parte Elliott* (1876), 2 Ch.D. 104; *Boldero v. London & Westminster Discount Co.* (1879), 5 Ex.D 47 (D.C.); *Re Johnson, supra*, note 95; *Gurofski v. Harris* (1896), 27 O.R. 201, affirmed 23 O.A.R. 717; *McKinnon v. Gillard* (1907), 9 O.W.R. 77; *Belliveau Co. v. Miller* (1912), 1 W.W.R. 588 (Alta. C.A.); *Union Bank v. Murdock*, [1917] 2 W.W.R. 112, reversed on other grounds [1917] 3 W.W.R. 820 (Man. C.A.); *Penny v. Fulljames*, [1920] 1 W.W.R. 555 (Man. K.B.); *Owen Sound General and Marine Hospital v. Mann, supra*, note 93; *Reutcke v. Reutcke, supra*, note 96; *Monteith v. Hayden, supra*, note 88; *Royal Bank v. Morrison* (1992), 15 C.B.R. (3d) 273 (Ont. Gen. Div.); Kerr, *supra*, note 17, p. 342.

99 Middleton v. Polloek, supra, note 98; *Whitman v. Union Bank* (1889), 16 S.C.R. 410; *McDonald v. Cummings* (1895), 24 S.C.R. 321; *Kirk v. Chisholm* (1896), 26 S.C.R. 111; *Anderson Lumber Co. v. Can. Conifer Ltd., supra*, note 41; *Re Surkan, supra*, note 83; *cf. Re Barnett* (1983), 43 A.R. 215 (Q.B.).

presses the rule as follows:

> Unlike the bankruptcy laws, the statutory provision making voidable voluntary conveyances made with intent to defraud creditors does not prohibit a debtor preferring one creditor to another. A conveyance executed in favour of one or some only of the creditors of the grantor may be in good faith and valid, notwithstanding that the grantor knows at the time that execution is about to be issued against him, or that he is insolvent, and even though the conveyance comprises the whole of the grantor's property. Such a conveyance will, however, be avoided if it is a mere cloak to secure a benefit to the grantor, and the fact that one creditor obtains an advantage will not of itself prevent a transaction from being avoided.[1]

However, if a fraudulent intention on the part of the grantor is proven, along with the privity of the grantee, the transaction will fall within the statute.[2]

The above analysis of the law would appear to be inconsistent with the English case of *Wood v. Dixie*,[3] as interpreted in some Ontario decisions. In *Wood v. Dixie*, it was argued that a conveyance for value was fraudulent as against an execution creditor. The trial judge told the jury that if there really was consideration, "still, if the intention of the transaction was to defeat the execution creditor, the conveyance was void against him".[4] The Court of Queen's Bench held the direction to be wrong. Lord Denman reasoned as follows:

> The jury were given to understand that, although the conveyance was made bona fide, and with a full intention that the property should be parted with, it would yet be fraudulent if made with intent to defeat the execution. Such a motive does not defeat the assignment. We are clearly safe in going so far as to say that a mere intent to defeat a particular creditor does not constitute a fraud. We do not say that many considerations may not exist which would induce a jury to come to the conclusion which they have arrived at: but we hold the direction wrong.[5]

Wood v. Dixie was sharply criticized in a series of Ontario cases[6] but was nevertheless followed[7] until 1887 when the Voluntary and Fraudulent Conveyances Act[8] was amended to dispel the doubts which had arisen. The amendment provided that the Statute of Elizabeth should apply to all instruments executed to the end set forth in the statute "notwithstanding that the same may be executed upon a valuable consideration, and with the intention, as between the parties to

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1 18 Hals. (4th) "Family Arrangements, Undue Influence and Voidable Conveyances", para. 364. See also *Re Associated Fisheries of Can. Ltd.* (1987), 64 C.B.R. (N.S.) 242 (N.B.C.A.).

2 *Supra*, notes 95 and 96.

3 (1845), 115 E.R. 724.

4 *Supra*, note 3, p. 724.

5 *Supra*, note 3, p. 725.

6 The cases are cited in 13 C.E.D. (Ont. 3rd) *Fraudulent and Voidoble Conveyances*, para. 24, note 35, and Parker, *Frauds on Creditors and Assignments for the Benefit of Creditors* (1903), pp. 61-62. See especially *White v. Stevens* (1850), 7 U.C.Q.B. 340 (C.A.).

7 See, *e.g.*, *Smith v. Moffatt* (1869), 28 U.C.Q.B. 486 (C.A.). It would appear that the Ontario cases read *Wood v. Dixie*, *supra*, note 3, far more widely than was warranted by the actual judgments.

8 R.S.O. 1887, c. 96, s. 3.

the same, of actually transferring to and for the benefit of the transferee the interest expressed to be thereby transferred" unless the transaction fell within the protection of the *bona fide* purchaser proviso in the statute itself.

This curious provision was widely regarded as reversing "the dangerous doctrine"[9] of *Wood v. Dixie* and the Ontario cases which had followed it.[10] The present Manitoba,[11] Newfoundland[12] and Ontario[13] Acts contain versions of the 1887 amendments. As to the rest of Canada, it might still be open to argue *Wood v. Dixie* today,[14] but the problem is less likely to arise with the passage in most jurisdictions of fraudulent preference legislation.

The courts have had considerable difficulty in deciding on the intent which the transferee must have to strike down a transfer for value. Section 6 of the Statute of Elizabeth literally requires only notice of the fraudulent intent of the grantor but the courts have tended to require more than simple knowledge. It is clearly not enough to prove knowledge of the grantor's indebtedness or insolvency or even knowledge that the effect of the sale may be to defeat or delay creditors.[15] If the evidence goes further and establishes that the purchaser knew that the seller's intention was to defraud the seller's creditors, the statute literally interpreted would appear to invalidate the transfer, and there are many English[16] and Canadian [17] cases which have taken this view. Despite this authority, mere knowledge of the debtor's intent would appear to be insufficient in Canada as a result of the important decision of the Supreme Court in *Mulcahy v. Archibald*.[18]

In that case, the debtor transferor was assumed to have the necessary fraudulent intent and it was arguable that the transferee, the debtor's sister, must have known his intention. But even if she had this knowledge, Sedgewick J. said that the evidence would still be inadequate to bring the transaction within the statute.

9 *McKinnon v. Gillard* (1907), 9 O.W.R. 77 at 84.

10 *Cameron v. Cusack* (1890), 17 O.A.R. 489 at 492-93.

11 Fraudulent Conveyances Act, C.C.S.M., c. F160, s. 5.

12 Fraudulent Conveyances Act, R.S.N. 1990, c. F-24, s. 5. See *Newfoundland and Labrador Housing Corp. v. Ennis* (1987), 197 A.P.R. 22 (Nfld. T.D.).

13 Fraudulent Conveyances Act, R.S.O. 1990, c. F.29, s. 4.

14 This was Parker's view, *supra*, note 6, pp. 61-62. But see Jewers, "Fraudulent Conveyance and Preference Legislation in Canada" (1956), 28 Man. Bar News 1 at 3-4. *Cf. Ferguson v. Lastewka*, [1946] 4 D.L.R. 531 at 539 (Ont. H.C.).

15 *Middleton v. Pollock; Ex parte Elliott* (1876), 2 Ch. D. 104; *Kvasnedsky v. Birnbaum* (1923), 25 O.W.N. 29; *Prytula v. Prytula* (1980), 30 O.R. (2d) 324 (H.C.); *Toronto Dominion Bank v. Melanson* (1981), 36 N.B.R. (2d) 431 (Q.B.); *Bank of Montreal v. Ewing* (1986), 59 C.B.R. (N.S.) 156 (Ont. C.A.); *Assiniboine Credit Union Ltd. v. Speed* (1989), 74 C.B.R. (N.S.) 158 (Man. Q.B.); *Royal Bank v. Morrison* (1992), 15 C.B.R. (3d) 273 (Ont. Gen. Div.); *Kerr on the Law of Fraud and Mistake* (7th ed. 1952), pp. 335-36.

16 *Glegg v. Bromley*, [1912] 3 K.B. 474 (C.A.); *Denny's Trustee v. Denny & Warr*, [1919] 1 K.B. 583; *cf.* Kerr, *supra*, note 15, pp. 335-36.

17 *Cameron v. Cusack*, *supra*, note 10; *Kvasnedsky v. Birnbaum*, *supra*, note 15; *Toronto Dominion Bank v. Michael*, [1973] 1 W.W.R. 656 (Alta. C.A.); *Solomon v. Solomon* (1977), 79 D.L.R. (3d) 264 (Ont. H.C.); *cf.* Jewers, *supra*, note 14, p. 5. These cases must be regarded as doubtful authority on this issue in the light of *Mulcahy v. Archibald* (1898), 28 S.C.R. 523.

18 *Supra*, note 17.

> The statute of Elizabeth, while making void transfers, the object of which is to defeat or delay creditors, does not make void but expressly protects them in the interest of transferees who have given valuable consideration therefor, and it has been decided over and over again that knowledge on the part of such a transferee of the motive or design of the transferor is not conclusive of bad faith or will not preclude him from obtaining the benefit of his security. So long as there is an existing debt and the transfer to him is made for the purpose of securing that debt and he does not either directly or indirectly make himself an instrument for the purpose of subsequently benefiting the transferor, he is protected and the transaction cannot be held void.[19]

What is unclear from this quotation is what further evidence is necessary to satisfy the statute. Other cases talk about the purchaser being privy or party to the fraudulent intent[20] or concurring in it,[21] but these terms do not tell us much. Perhaps the best analysis of the law after *Mulcahy v. Archibald* is contained in a report of the New Brunswick Consumer Protection Project on unsecured creditors' remedies:

> In setting aside the transaction made by the debtor, the issue is the intent of the transaction. Under the existing jurisprudence, if the third party gives valuable consideration, there must be a concurrence of intent to attack the transaction. Mere knowledge of the debtor's improper intent does not create a concurrence of intent.[22]

Speaking of the common idea that the transferee must be privy to the fraud, the report comments:

> Privity would undoubtedly exist if the third party shared the actual intent to defeat creditors or to give an unjust preference. If the third party's own intent is to gain a good bargain for himself, some form of collusion or assistance with the deliberate object of helping the debtor to carry out his improper intent would probably be necessary.[23]

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19 *Mulcahy v. Archibald, supra*, note 17, p. 529. To the same effect, see *Manitoba Brewing and Malting Co. v. McDonald* (1909), 11 W.L.R. 313 (Sask. K.B.); *Banque d'Hochelaga v. Potvin*, [1924] 1 W.W.R. 488 (Alta. C.A.); *Ferguson v. Laskewka, supra*, note 14; *Bank of Montreal v. Vandine* (1952), 33 M.P.R. 368 (N.B.C.A.); *Woodmann Interiors Ltd. v. Zeh* (1989), 75 C.B.R. (N.S.) 100 (Alta. Q.B.).

20 *Meeker Cedar Products Ltd. v. Edge* (1968), 12 C.B.R. (N.S.) 49, affirmed without written reasons 12 C.B.R. (N.S.) 60 (S.C.C.); *Lange v. Lange* (1981), 14 Man. R. (2d) 153 (Q.B.); *Stathakis v. Sara* (1983), 48 C.B.R. (N.S.) 286 (Ont. S.C.); *Re Associated Fisheries of Canada Ltd.* (1987), *supra*, note 1; *Gresham v. Gresham* (1993), 18 C.B.R. (3d) 201 (B.C.C.A.).

21 *Re Johnson; Golden v. Gillam* (1881), 20 Ch. D. 389, affirmed (*sub nom. Golden v. Gillam*) 51 L.J. Ch. 503 (C.A.); *Monteith v. Hayden* (1987), 205 A.P.R. 273 (N.B.C.A.). Compare *Royal Bank v. Victor* (1986), 7 B.C.L.R. (2d) 151 (S.C.), in which Meredith J. uses the idea of "collusion" between the transferors and transferee.

22 Dore and Kerr, *Third Report of the Consumer Protection Project: Legal Remedies of the Unsecured Creditor after Judgment* (N.B. 1976), p. 115 (unpublished). See also Ontario Law Reform Commission, *Report on the Enforcement of Judgment Debts and Related Matters* (1983), vol. 4, pp. 143-47, 163, 219.

23 Dore and Kerr, *supra*, note 22, p. 116. The writers try to reconcile the Canadian cases with s. 6 of the statute by arguing (p. 115) that the section "would seem to refer, not to the transaction between the debtor and the third party, but to some subsequent transaction by the third party". This seems a strained reading of the section. The better view is that the Canadian cases have

If the New Brunswick writers are correct in their interpretation of *Mulcahy v. Archibald*, our law is now substantially different from the English case law and from what appears to have been the intent of s. 6 of the statute. The case reflects a tenderness for the purchaser which may be justified by the need for freedom and security of commerce but which makes an attack on a transfer for value very difficult indeed.

(d) The Proof of Intent

We noted earlier that the crucial problem in any fraudulent conveyance action is to prove the fraudulent intent of the debtor and, in the case of transfers for value, the concurrence of the transferee. We discussed the presumptions developed by the courts to aid them in finding fraud in certain types of voluntary transactions (Kerr's class (1)). Even where fraud must be proved as a fact, the courts as early as *Twyne's Case*[24] developed evidentiary rules which would enable them to find fraud unless the supporters of the transaction could explain away the suspicious circumstances. These rules have come down to us today as the so-called badges of fraud.

While the legal or persuasive burden to prove the case remains on the plaintiff throughout the trial, the plaintiff may raise an inference of fraud sufficient to shift the evidentiary burden to the defendant if the plaintiff can establish that the transaction has characteristics which are typically associated with fraudulent intent.[25] No doubt proof of one or several badges of fraud will not compel a finding for the plaintiff, but it does raise a *prima facie* case which it would be prudent for the defendant to attempt to rebut.[26]

Lists of the badges of fraud vary from writer to writer, and no comprehensive catalogue is likely to be agreed upon. The judges in *Twyne's Case* listed six "signs and marks of fraud" present in the facts before them:[27]

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effectively rewritten the section in the interest of protecting transfers for value. The history of judicial interpretation of the Statute of Elizabeth is characterized by extensive lawmaking under the guise of interpretation.

24 (1601), 76 E.R. 809.

25 The distinction between legal and evidentiary burdens is based on Thayer, as interpreted in Tapper, *Cross on Evidence* (7th ed. 1990), pp. 110-12. There is the occasional case which supports the rule as set out in the text, *e.g., Koop v. Smith* (1915), 25 D.L.R. 355 at 358-59 (S.C.C.) *per* Duff J.; *Commerce Capital Mortgage Corp. v. Jemmett* (1981), 37 C.B.R. (N.S.) 59 (Ont. H.C.); *Goertz v. Goertz (Trustee of)* (1992), 16 C.B.R. (3d) 42 (Sask. C.A.). However, there are other cases which talk of the burden shifting without making it clear what is meant by that obscure image. *Cf.* Davies J. in *Koop v. Smith, supra*, p. 356. It is submitted that the better view is as expressed in the text. It should be noted that a fraudulent intent deemed to exist by another statute, such as the Bulk Sales Act, may provide the basis for a finding of intent under the Statute of Elizabeth or its provincial equivalent: see *Wiebe v. Holmes*, [1971] 4 W.W.R. 588 (Man. Q.B.), and cases cited therein; Dore and Kerr, *supra*, note 22, pp. 119-20.

26 In Schiff's terms, proof of some badges of fraud raises a justifiable inference of fraud but not a compelled determination of fraud unless the defendant leads evidence: see Schiff, *Evidence in the Litigation Process* (4th ed. 1993), pp. 1651-53.

27 *Supra*, note 24, pp. 812-14.

(1) The gift was general "without exception of his apparel, or any thing of necessity".
(2) The donor continued in possession and used the goods as his or her own, including selling them.
(3) The transaction was secret.
(4) The transfer was made pending the writ.
(5) The transfer amounted to a trust of the goods "and fraud is always apparelled and clad with a trust, and a trust is the cover of fraud".
(6) The deed contained the self-serving and unusual provision "that the gift was made honestly, truly, and bona fide".

Later judges and writers[28] have added other fact situations which raise one's suspicions of fraud:

(7) The deed gives the grantor a general power to revoke the conveyance.
(8) The deed contains false statements as to the consideration.
(9) The consideration is grossly inadequate.
(10) There is unusual haste to make the transfer.
(11) Some benefit is retained under the settlement by the settlor.[29]
(12) Cash is taken in payment instead of a cheque.
(13) A close relationship exists between the parties to the conveyance.

One can think of other candidates for the list.

The judges are very careful to avoid the impression that the badges of fraud doctrine can be used mechanically. The plaintiff is still required to prove fraud

28 See, *e.g.*, *Ferguson v. Lastewka*, *supra*, note 14; *Bank of Montreal v. Vandine*, *supra*, note 19; *Re Dougmore Realty Holdings Ltd.; Fisher v. Wilgorn Invt. Ltd.* (1966), 59 D.L.R. (2d) 432, reversed on other grounds 65 D.L.R. (2d) 419 (Ont. C.A.); *Meeker Cedar Products Ltd. v. Edge*, *supra*, note 20; *Bank of Nova Scotia v. Zgurski* (1970), 72 W.W.R. 464 (Alta. T.D.); *Solomon v. Solomon*, *supra*, note 17; *Holdenreid v. Holdenreid* (1978), 29 C.B.R. (N.S.) 138 (Ont. H.C.); *Westinghouse Canada Ltd. v. Caldwell* (1979), 31 C.B.R. (N.S.) 276 (B.C.S.C.); *Bank of Nova Scotia v. MacDonald* (1982), 39 N.B.R. (2d) 71 (Q.B.); *India Films Overseas Limited v. Keefer Investments Inc.* (1984), 55 C.B.R. (N.S.) 154 (B.C.S.C.); *Sochan v. Sochan* (1984), 31 Sask. R. 13 (U.F.C.); *Bank of Montreal v. Horan* (1986), 54 O.R. (2d) 757 (Ont. H.C.); *Re Associated Fisheries of Canada Ltd.*, *supra*, note 1; *Monteith v. Hayden*, *supra*, note 21; *Nuove Ceramiche Ricchetti S.p.A. v. Mastrogiovanni* (1988), 76 C.B.R. (N.S.) 310 (Ont. H.C.); *633746 Ontario Inc. (Trustee of) v. Salvati* (1990), 79 C.B.R. (N.S.) 72 (Ont. H.C.); *Mannal v. Busch* (1990), 251 A.P.R. 385 (N.S.T.D.); *Chow v. Pearson* (1992), 12 C.B.R. (3d) 226 (B.C.S.C.); *Canadian Imperial Bank of Commerce v. Graat* (1992), 5 B.L.R. (2d) 271 (Ont. Gen. Div.); *Dondee Stock Farms Ltd. (Trustee of) v. Giesbrecht* (1993), 24 C.B.R. (3d) 20 (Sask. Q.B.); Hals., *supra*, note 1, para. 366; Kerr, *supra*, note 15, pp. 350-78; Parker, *supra*, note 6, cc. 5-7.

29 But see *Sun Sudan Oil Co. v. Methanex Corp.* (1992), 5 Alta. L.R. (3d) 292, 318 (Q.B.) where Hunt J. concludes that the Statute of Elizabeth "only comes into play when the assignor reserves some benefit to himself". Taken literally, this would promote a badge of fraud into an absolute requirement, although the judge is able to find some support in dicta by Jessel M.R., quoted in *Mulcahy v. Archibald*, *supra*, note 17, p. 529.

on all the facts of the case, and a court might still dismiss a fraudulent conveyance action because the plaintiff's evidence is explained away by the surrounding circumstances taken as a whole.[30] Some of the above items are obviously more important than others. Still the plaintiff who can identify a number of suspicious circumstances in the transaction is obviously in a better position to escape a non-suit and to force the defendant to give evidence, thus exposing that defendant to cross-examination.

Perhaps the most common type of fraudulent conveyance, and one which is bound to attract suspicion, is the sale or gift of property to a close relative. The existence of this close relationship between the parties is itself a badge of fraud,[31] but the courts have gone further and have developed a secondary evidentiary rule applicable to these kinds of conveyances.

The leading Canadian case is *Koop v. Smith*[32] in which it was sought to set aside a bill of sale executed in favour of the defendant by her brother at a time when the latter was financially embarrassed. Counsel for the plaintiff urged the Supreme Court to accept and apply a rule developed in the Ontario courts to the effect that where the transaction in question occurs between close relatives, the evidence of the relatives as to *bona fide* should be corroborated.

The Supreme Court held that the bill of sale should be declared to be void but their comments on the Ontario corroboration rule do not go quite as far as plaintiff's counsel appears to have argued. Davies J. commented as follows:

> I think the rule laid down by the Courts of Ontario with regard to assignments made between near relations and impeached by the creditors of the assignor as fraudulent is a salutory one, namely, that where it is accessible some corroborative evidence of the *bona fides* of the transaction should be given.[33]

Duff J. considered the proposed rule at greater length. He began by noting that the trial judge appeared to have held that a suspicious transaction between close relatives can only be supported by corroborative evidence. He submitted this proposition to a long but useful analysis:

30 See cases and texts cited *supra*, note 28. See also *Havel v. Galemar Hldg. Ltd.* (1981), 36 O.R. (2d) 348 (H.C.); *Re Ross* (1983), 56 N.S.R. (2d) 264 (T.D.); *Bank of Nova Scotia v. Bass* (1983), 47 C.B.R. (N.S.) 203 (Man. Q.B.); *Austin Marshall Limited v. Bennie* (1985), 56 C.B.R. (N.S.) 71 (Ont. H.C.); *Holbrook v. Cedpar Properties Inc.* (1986), 62 C.B.R. (N.S.) 18 (Ont. H.C.); *Cas's Mechanical Services Inc. v. Topping* (1989), 77 C.B.R. (N.S.) 145 (Sask. Q.B.); *Smeds v. Olney* (1990), 3 C.B.R. (3d) 85 (B.C.S.C.); *Davis v. Thachuk* (1991), 5 C.B.R. (3d) 256 (B.C.S.C.).

31 There are numerous cases. See, *e.g.*, *Re Fancy* (1984), 51 C.B.R. (N.S.) 29 (Ont. H.C.); *Re Whetstone* (1984), 52 C.B.R. (N.S.) 280 (Ont. H.C.); *Carew v. Power* (1984), 50 C.B.R. (N.S.) 275 (Nfld. D.C.); *Courtesy Chevrolet Oldsmobile Ltd. v. Dhaliwal* (1987), 67 C.B.R. (N.S.) 72 (Ont. H.C.).

32 *Supra*, note 25. See also *Re Whetstone*, *supra*, note 31; *Northland Bank v. Smetaniuk* (1986), 62 C.B.R. (N.S.) 113 (B.C.S.C.).

33 *Supra*, note 25, p. 356.

> I do not think the proposition put thus absolutely is part of the English law or of the law of British Columbia; but I think it is a maxim of prudence based upon experience that in such cases a tribunal of fact may properly act upon that when suspicion touching the reality or the *bona fides* of a transaction between near relatives arises from the circumstances in which the transaction took place then the fact of relationship itself is sufficient to put the burden of explanation upon the parties interested and that, in such a case, the testimony of the parties must be scrutinized with care and suspicion; and it is very seldom that such evidence can safely be acted upon as in itself sufficient. . .
>
> I may add that I think it doubtful whether the Ontario decisions when properly read really do lay it down as a rule of law that the fact of relationship is sufficient in itself to shift the burden of establishing the burden of proof in the strict sense. It may be that the proper construction of these cases is that the burden of giving evidence and not the burden of the issue is shifted. (As to this distinction see the admirable chapter IX, in Professor Thayer's 'Law of Evidence'.) In my own view as indicated above, even this would be putting the matter just a little too high; I think the true rule is that suspicious circumstances coupled with relationship make a case of *res ipsa loquitur* which the tribunal of fact may and will generally treat as a sufficient *prima facie* case, but that it is not strictly in law bound to do so; and that the question of the necessity of corroboration is strictly a question of fact.[34]

The other three judgments given in the case add little to the point under discussion.[35]

The passages quoted above have been much referred to in subsequent cases, but the courts' interpretations have not been consistent. A few judges apparently read *Koop v. Smith* as requiring corroboration in all cases of suspicious transactions between close relatives.[36] Most cases and authorities have taken what is submitted to be the better view that in such a situation the uncorroborated evidence will usually not be sufficient but that "the necessity of corroborative evidence under such circumstances is not, however, a hard and fast rule, but a maxim of prudence".[37]

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34 *Supra*, note 25, pp. 358-59. See also *Goertz v. Goertz (Trustee of)*, *supra*, note 25.

35 Anglin and Brodeur JJ. say that the question of fraudulent intent is for the trial judge to decide and his conclusions should not be distributed on appeal. Idington J. agrees but adds, p. 357:

> These cases of alleged fraudulent assignment must generally depend largely upon the view of the facts taken by the trial Judge. It is quite competent for him, if impressed with the veracity of the assignor, to accept and act upon his unsupported statement. The transaction and established surrounding circumstances might be such as to justify his doing so. Or, on the other hand, they might be such as to render his doing so questionable.

See also *E.E. McCoy Co. v. Wiseman* (1987), 200 A.P.R. 1 (N.S.A.D.).

36 *Killops (Killips) v. Porter* (1916), 9 W.W.R. 949 (Alta. T.D.); and *Petryshyn v. Kochan*, [1940] 2 W.W.R. 353 (Sask. K.B.).

37 13 C.E.D. (Ont. 3rd) *Fraudulent and Voidable Conveyances*, para. 128. See also *Union Bank v. Murdock*, [1917] 3 W.W.R. 820 (Man. C.A.); *Imperial Bank v. Esakin*, [1924] 2 W.W.R. 33 (Sask. C.A.); *Re Can. Imperial Bank of Commerce and Ash* (1964), 47 D.L.R. (2d) 620 (B.C.S.C.); *Re Dougmore Realty Holdings Ltd.*, *supra*, note 28; *Bank of Nova Scotia v. Zgurski*, *supra*, note 28; *Toronto-Dom. Bank v. Michael*, *supra*, note 17; *Gallop v. Hamlin* (1973), 39 D.L.R. (3d) 524 (Ont. C.A.); *Traders Group Ltd. v. Mason* (1973) 43 D.L.R. (3d) 76 (N.S.T.D.);

The "close relative" badge of fraud and the *Koop v. Smith* principle have been extended to include transactions between individuals and companies which they control,[38] related corporations,[39] and unmarried persons living together as husband and wife.[40]

(e) Who Can Challenge Conveyance

The Statute of Elizabeth declared conveyances to be void as against "creditors and others"[41] whose claims "are, shall or might be in any wise disturbed, hindered, delayed or defrauded". The term creditor is capable of a fairly clear interpretation[42] but the courts have had more trouble giving content to and placing limits on the potentially all-embracing word "others".[43] Here as elsewhere, much of the law of fraudulent conveyances has been settled in the cases rather than flowing necessarily from the statute itself.

Archibald Farm Products Ltd. v. Shearing (1976), 12 Nfld. & P.E.I.R. 106 (Nfld. T.D.); *Lee v. Lee* (1978), 82 D.L.R. (3d) 429 (Nfld. D.C.); *Tempo Bldg. Supplies Ltd. v. Pitura* (1979), 33 C.B.R. (N.S.) 23 (B.C.S.C.); *Avco Financial Services Ltd. v. West* (1979), 33 C.B.R. (N.S.) 285 (N.S. Co. Ct.); *Bank of Montreal v. Jory* (1981), 39 C.B.R. (N.S.) 30 (B.C.S.C.); *Bank of Nova Scotia v. Sedlacek (Sedlack)* (1982), 40 B.C.L.R. 306 (S.C.); *Davis v. Thachuk, supra*, note 30; *Hirji v. Scavetta* (1993), 15 O.R. (3d) 371 (Ont. Gen. Div.).

38 *Re Martineau and Martineau* (1969), 5 D.L.R. (3d) 165 (B.C.S.C.); *Burton v. R & M Insurance Ltd.* (1977), 5 Alta. L.R. (2d) 14 (T.D.); *Coopers & Lybrand Ltd. v. Niton Junction Hldg. Ltd.* (1979), 32 C.B.R. (N.S.) 141 (Alta. Q.B.); Springman, "Fraudulent Conveyances, Fraudulent Preferences, and Other Voidable Transactions" in Law Society of Upper Canada, *Special Lectures: 1988: Rights and Remedies in the Law of Creditor and Debtor*, p. 55; but see *Reutcke v. Reutcke* (1958), 24 W.W.R. 417 (Man. Q.B.); *Kisluk v. B.L. Armstrong Co.* (1982), 44 C.B.R. (N.S.) 251 (Ont. S.C.).

39 *Batch's Service Ltd. v. McNeill Drilling Ltd.* (1990), 82 Sask. R. 265 (Q.B.); *Canadian Imperial Bank of Commerce v. Graat, supra*, note 28.

40 *Lee v. Lee, supra*, note 37; *Holdenreid v. Holdenreid, supra*, note 28; *Carew v. Power, supra*, note 31.

41 The Manitoba Fraudulent Conveyances Act, *supra*, note 11, s. 2, and the Ontario Fraudulent Conveyances Act, *supra*, note 13, s. 2, speak of "creditors *or* others". One assumes that the substitution of "or" for "and" makes no difference.

42 See Chapter 2.

43 As to maintenance claimants, see *Murdoch v. Murdoch*, [1977] 1 W.W.R. 16 (Alta. T.D.); *Holdenreid v. Holdenreid, supra*, note 28; *Sembaliuk v. Sembaliuk* (1983), 27 Alta. L.R. (2d) 223, 230-31, reversed on other grounds (1984), 35 Alta. L.R. (2d) 193 (C.A.); leave to appeal to S.C.C. refused (1985), 35 Alta. L.R. (2d) x1. As to the beneficiary of a guarantee not yet called upon, see *Bank of Nova Scotia v. Holland* (1979), 32 C.B.R. (N.S.) 153 (Ont. S.C.); *Re Whetstone, supra*, note 31. It has been held (in an application to strike out a writ of summons as disclosing no cause of action) that the creditor challenging a transfer need not be a creditor of the disposing grantor. See *Aspen Planners Ltd. v. Delshar Development Ltd.* (1981), 11 A.C.W.S. (2d) 129 (B.C. Co. Ct.); *cf. J.W. Bird and Co. Ltd. v. Downey Bldg. Supplies Ltd.* (1979), 32 N.B.R. (2d) 504 (T.D.). See also *Gooseaire Humidification Ltd. v. Knowles* (1979), 27 N.B.R. (2d) 541 (Q.B.); *Fraser v. Central United Church* (1982), 38 O.R. (2d) 97 (H.C.). See generally Howcroft, "Scope of Fraudulent Conveyances and Fraudulent Preferences Legislation in Alberta" (1986), 24 Alta. L.R. 496.

Moral claims will not give rise to an action under the statutes.[44] Secured creditors have traditionally been said not to be "creditors and others" unless the security is insufficient to satisfy the debt.[45] The tradition will have to be rethought in British Columbia and perhaps elsewhere in light of the recent decision of the B.C. Court of Appeal in *Canadian Imperial Bank of Commerce v. Boukalis*.[46]

The courts early decided that where a fraudulent settlement was set aside, the property thus recovered was liable to the claims of creditors generally, whether their debts existed at the time of the settlement or arose later.[47] From this starting point, the rule developed that a subsequent creditor could maintain an action to have a conveyance set aside "so long as any debt, due at the date of the settlement, remains unpaid at the time of the commencement of the action".[48] The underlying theory was that, as the prior creditors could have set aside the conveyance and a subsequent creditor would have been entitled to share *pro rata*, therefore the subsequent creditor "has an equity to participate, and may bring his action to enforce that equity".[49] It followed that if the prior creditors were for some reason debarred from impeaching the conveyance because, for example, limitation periods had expired, the subsequent creditor would be equally debarred "for the equity of the latter cannot be higher than that of the former".[50]

44 See *Dower v. Public Trustee* (1962), 35 D.L.R. (2d) 29 (Alta. T.D.).

45 See *Sun Life Assurance Co. v. Elliott* (1900), 31 S.C.R. 91; *Davies v. Dandy*, [1920] 2 W.W.R. 126 (Man. C.A.); *Arnold v. Fleming*, [1923] 1 W.W.R. 706 (Alta. T.D.); *Anderson v. Serge*, [1924] 1 W.W.R. 1260 (Sask. C.A.); *McLean v. Ratekin*, [1926] 4 D.L.R. 174 (Sask. C.A.); *Gauthier v. Woollatt*, [1940] 1 D.L.R. 275 (Ont. H.C.); *Kroman's Electric Ltd. v. Schultes* (1970), 11 D.L.R. (3d) 425 (Ont. H.C.); *Royal Bank v. Dunsmuir* (1978), 85 D.L.R. (3d) 549 (B.C.S.C.); *Delbreuck & Co. v. Muenzenberg* (1984), 54 B.C.L.R. 264 (S.C.); Kerr, *supra*, note 15, pp. 380-81; Parker, *supra*, note 6, pp. 13-15; C.E.D., *supra*, note 37, paras. 62-65; *cf. Bank of Nova Scotia v. Scott* (1985), 67 B.C.L.R. 145 (C.A.).

46 (1987), 65 C.B.R. (N.S.) 66 (B.C.C.A.). On the *Boukalis* case, see Law Reform Commission of B.C., *Report on Fraudulent Conveyances and Preferences* (1988: LRC 94), p. 29; Robinson, *British Columbia Debtor-Creditor Law and Precedents* (1993), pp. 10-24 to 10-27; Springman, "Fraudulent Conveyances, Fraudulent Preferences, and Other Voidable Transactions" in Law Society of Upper Canada, *Special Lectures: 1988: Rights and Remedies in the Law of Creditor and Debtor*, pp. 97-100; Springman, "Fraudulent Conveyances Under the Fraudulent Conveyances Act and the Assignments and Preferences Act" in Canadian Bar Association — Ontario, *Fraudulent Conveyances, Unjust Preferences and Other Transactions Subject to Attack by Creditors* (1993), pp. 34-39.

47 Much of the following account is drawn from Kerr, *supra*, note 15, pp. 317-21. See also *Dancey v. Brown* (1914), 19 D.L.R. 862 (Ont. C.A.); *Ewachowski v. Marchischuk*, [1917] 3 W.W.R. 747 (Man. K.B.); *Arnold v. Fleming*, *supra*, note 45; *Gauthier v. Woollatt*, *supra*, note 45; C.E.D., *supra*, note 6, para. 61; Hals., *supra*, note 1, para. 377; Parker, *supra*, note 6, pp. 71-78.

48 Kerr, *supra*, note 15, p. 318. Of course, the transaction must have been impeachable by the existing creditors: see *Dancey v. Brown*, *supra*, note 47.

49 *Ibid.*

50 Kerr, *supra*, note 15, p. 319; *Dancey v. Brown*, *supra*, note 47; *cf. Wonsch Construction Co. v. National Bank of Canada* (1987), 70 C.B.R. (N.S.) 318 (Ont. H.C.).

If one were to stop at this point, the result would be that a subsequent creditor would have no remedy where there were no existing creditors at the date of the conveyance or where the existing creditors had all been paid off. The courts have been unhappy with this result, particularly in the light of the "creditors and others" formula and have developed a series of exceptions to the rule. For example, it has been said that where the transferor is insolvent at or shortly after the date of the settlement[51] or has paid off the existing debts only to substitute a fresh set,[52] the transfer can be challenged even by a subsequent creditor.[53]

More important than these specific rules is the general exception, advanced in many decisions[54] and texts,[55] that a subsequent creditor can challenge a transfer where he or she can establish an intention to hinder or defraud the challenging creditor specifically or future creditors generally. The judges are by no means unanimous in stating the rule this widely, but it would appear to underlie and tie together the wide variety of cases in which subsequent creditors have successfully challenged fraudulent conveyances.

One common situation which illustrates the principle is the case of the conveyance made at a time when the grantor is or is about to be sued by a claimant who has not yet obtained judgment at the date of the conveyance. Where a person has been sued or knows that a claim may be made, it is not uncommon that he or she will seek to shelter wealth from the claimant by transferring it away, often to a relative. In these circumstances, if the claimant can establish the intent to defeat or delay him or her, the transaction can be successfully challenged under the statute before or after the claimant reaches judgment.[56] If the claimant has not yet

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51 *Crossley v. Elworthy* (1871), L.R. 12 Eq. 158; *Taylor v. Coenen* (1876), 1 Ch. D. 636; *Gauthier v. Woollatt, supra*, note 45; Hals, *supra*, note 1, para. 377; Parker, *supra*, note 6, p. 73.

52 *Holmes v. Penney* (1856), 69 E.R. 1035; *Ferguson v. Kenny* (1889), 16 O.A.R. 276; *Gauthier v. Woollatt, supra*, note 45; Parker, *supra*, note 6, p. 73.

53 The term "others" has been stretched to cover people whose status as creditors is doubtful. See cases cited, *supra*, note 43.

54 See cases cited *infra*, notes 56-79. See also *Donohoe v. Hull Brothers & Co.* (1895), 24 S.C.R. 683 at 696; *Bache Halsey Stuart Shields Inc. v. Charles* (1983), 49 B.C.L.R. 396 (S.C.); *Canadian Imperial Bank of Commerce v. Boukalis, supra*, note 46; *cf. Bank of Montreal v. Freed* (1990), 79 C.B.R. (N.S.) 274 (Man. C.A.); *Re Deamond* (1987), 65 C.B.R. (N.S.) 92 (N.S.T.D.).

55 Hals., *supra*, note 1, para. 377; Kerr, *supra*, note 15, pp. 321-34; Parker, *supra*, note 6, pp. 71-72.

56 *Smith v. Orbean* (1916), 10 W.W.R. 368 (Sask. K.B.); *Ewachowski v. Marchischuk, supra*, note 47; *Hopkinson v. Westerman* (1919), 45 O.L.R. 208 (C.A.); *Penny v. Fulljames*, [1920] 1 W.W.R. 555 (Man. K.B.); *McMullen v. Dr. Barnardo's Homes etc. Assn.* (1924), 26 O.W.N. 168; *Shephard v. Shephard* (1925), 56 O.L.R. 555 (C.A.); *Huss v. Lakin*, [1925] 1 D.L.R. 38 (Sask. K.B.); *Bank of Montreal v. Reis*, [1925] 3 D.L.R. 125 (Sask. K.B.); *Gay Co. v. Trick* (1927), 31 O.W.N. 445; *Petryshyn v. Kochan, supra*, note 36; *Bell v. Williamson*, [1945] O.R. 484, affirmed [1945] O.R. 844 (C.A.); *Goyan v. Kinash*, [1945] 2 D.L.R. 749 (Alta. T.D.); *Ferguson v. Lastewka, supra*, note 14; *McGillan v. McGillan*, [1947] 4 D.L.R. 456 (N.B.C.A.); *Murdoch v. Murdoch*, [1977] 1 W.W.R. 16 (Alta. T.D.); *Packer v. Christie* (1980), 30 N.B.R. (2d) 307 (Q.B.); *Holdenreid v. Holdenreid, supra*, note 28; *Sochan v. Sochan, supra*, note 28; *Bank of Nova Scotia v. Simpson* (1984), 52 C.B.R. (N.S.) 183 (N.S.T.D.); *cf. Fuhr v. Fuhr*, [1936] 2 W.W.R. 237 (B.C.S.C.). See also Cave, "Tort Claimants and the Fraudulent Conveyances Act" (1978), 35 The Advocate 427. The result will be otherwise if the action is brought under a rule of court which gives relief to "creditors" only: see *Faulhaber v. Ulseth* (1976), 66 D.L.R. (3d)

obtained judgment by the trial of the fraudulent conveyance action, that claimant will also have to establish that he or she has a valid claim against the debtor.[57] The cases suggest two defences which the debtor may successfully advance to this type of action. The challenge to the conveyance will fail if (1) the claimant's original lawsuit was highly speculative and unlikely to result in judgment for more than a trivial sum,[58] or (2) the conveyance was made to an existing creditor as payment for the debt.[59]

The second major class of case in which subsequent creditors have been able to challenge conveyances is that of the debtor who, on the eve of entering into business, conveys away property to protect it from creditors of the proposed business. The leading case is *Mackay v. Douglas*[60] in which the defendant settled a leasehold property on his wife shortly before becoming a partner in a firm of merchants which engaged in large scale speculations in jute. (The judge found the speculations to be of "a reckless and unjustifiable character".[61]) The partnership later failed and the plaintiffs sued to set aside the settlement.

Sir R. Malins V.C. held for the plaintiffs. He put the issue and his conclusion thereon as follows:

> Can a man who contemplates trade, or who, in point of fact, whether he contemplates it at the time or very shortly afterwards, enters into trade, and thereby incurs liabilities which end in a disastrous state of affairs, make a voluntary settlement which shall be good against the creditors who become so in the course of his trade? . . . But is the Statute of *Elizabeth* so very short in its effect that it will not cover a case where a man on the very eve of entering into trade takes the bulk of his property and puts it into a voluntary settlement and becomes insolvent a few months afterwards? . . . I think not.[62]

Malins V.C. went on to conclude from the evidence that the inducement to Douglas to make the settlement was to protect his property from the risks associated with the new partnership and he relied on the presumption in *Freeman v. Pope*[63] to decide that the court could in the circumstances presume the intent of the debtor, even if it could not be directly proven.

488 (Alta. T.D.).

57 *Bell v. Williamson, supra*, note 56.

58 *Re Wise: Ex parte Mercer* (1886), 17 Q.B.D. 290 (C.A.); *Gurofski v. Harris* (1896), 27 O.R. 201, affirmed 23 O.A.R. 717.

59 *Cameron v. Cusack, supra*, note 10; *Gurofski v. Harris, supra*, note 58; *Montgomery v. Corbit* (1896), 24 O.A.R. 311.

60 (1872), L.R. 14 Eq. 106.

61 *Supra*, note 60, p. 116.

62 *Supra*, note 60, pp. 118-19.

63 (1870), 5 Ch. App. 538.

Malins V.C. wished to make it clear that his decision as to the Douglas settlement should not be extended to invalidate any conveyance in which the grantor subsequently gets into business difficulties:

> The law is perfectly settled that if a man is solvent at the time and after the time of taking away the property which is put into the settlement he remains solvent, and does not at the time contemplate doing anything which could lead to insolvency, that settlement will be good. . . So, in the present case, if Mr. *Douglas* had neither gone into nor contemplated going into trade at the time, but some years afterwards, by a totally new arrangement, made up his mind to do so, I should have had no hesitation in coming to the conclusion that his subsequent insolvency could have had no effect in producing invalidity of the settlement which he made upon his wife and family.[64]

The Vice Chancellor concluded that Douglas had in fact made the settlement with the view that he was going into a partnership in which he might become indebted:

> The conclusion which I arrive at proceeds upon the broad ground that a man who contemplates going into trade cannot on the eve of doing so take the bulk of his property out of the reach of those who may become his creditors in his trading operations.[65]

Subsequent cases have quoted and followed *Mackay v. Douglas* and it is clearly the law of Canada as a result of *McGuire v. Ottawa Wine Vaults Co.*,[66] a decision of the Supreme Court of Canada. Some cases have extended the *Mackay* rule to cover situations in which no new business is established but the debtor has conveyed away property to defraud future creditors of his or her present business.[67] The difficulty which the courts have had is to establish sensible and defensible limits to the principle.

The headnote writer in the Law Reports version of the *Mackay* case sought to narrow its ratio by limiting it to debtors who subsequently engage in "trade of a hazardous character",[68] and this reading of the decision has been adopted by subsequent courts.[69] The hazardous trade limitation seems to be a strained reading of the judgment in *Mackay v. Douglas*, taken as a whole,[70] although there is no doubt that the jute business was in fact a dangerous one.

Another limitation which subsequent cases have sought to place on the *Mackay* rule is suggested by cases like *Re Lane-Fox; Ex parte Gimblett*,[71] in

64 *Supra*, note 60, p. 121.

65 *Supra*, note 60, p. 122.

66 (1913), 48 S.C.R. 44. See also *Newlands Sawmills Ltd. v. Bateman* (1922), 70 D.L.R. 165 (B.C.C.A.); *Clark v. Smith*, [1933] 3 W.W.R. 116 (Man. K.B.); *Re Skinner* (1960), 27 D.L.R. (2d) 74 (B.C.S.C.); *Traders Group Ltd. v. Mason, supra*, note 37; *Commerce Capital Mortgage Corp. v. Jemmett* (1981), 37 C.B.R. (N.S.) 59 (Ont. H.C.).

67 *McGuire v. Ottawa Wine Vaults, supra*, note 66; *Traders Group Ltd. v. Mason, supra*, note 37; *Bank of Nova Scotia v. Holland* (1979), 32 C.B.R. (N.S.) 153 (Ont. S.C.).

68 *Supra*, note 60, p. 106.

69 See *Re Butterworth; Ex parte Russell* (1882), 19 Ch. D. 588 at 598-99 (C.A.).

70 See the sharp criticism of the hazardous business gloss by Martin J.A. in *Newlands Sawmills Ltd. v. Bateman, supra*, note 66, pp. 169-72.

71 [1900] 2 Q.B. 508.

which the debtor became entitled, upon reaching her majority, to about £15,000, whereupon she promptly entered into a voluntary settlement of all her property. During the following years, Miss Lane-Fox incurred debts and then sought to persuade the trustees to consent to her executing partial revocations of the settlement. The trustees at first concurred but later refused to consent to further revocations. The debtor then voluntarily entered bankruptcy, and the trustee (apparently on the urgings of the debtor) moved the court to set the settlement aside.

Wright J. refused to do so on the ground that there were no existing creditors whose claims preceded the settlement, and that subsequent creditors could avoid the settlement only if they could establish an actual intention on the debtor's part to defeat, delay or hinder future creditors. The learned judge concluded that "an honest settlement, affirmatively proved to be honest, ought not to be set aside merely because some years afterwards it is proved to have the effect of defeating and delaying subsequent creditors".[72] There was no reason to foresee future embarrassment, the debtor had no intention of trading and "the income which she would derive under the settlement would be sufficient for all the probable expenses of a young girl of that class, and who might be supposed to be unlikely to wantonly throw away her means".[73]

It seems a sensible limitation to the *Mackay* principle to say that it applies only where the plaintiff can establish a specific intention to defraud future creditors, and this idea has been used to uphold conveyances where the necessary intention could not be established.[74] In *Gauthier v. Woollatt*,[75] Roach J. decided that where it was clear that the debtor had intended to defraud creditors existing at the time of conveyance, this was not enough where there was no evidence of animus directed to future creditors as well.

The difficulty with the requirement of specific intent is that it may be said in most cases of conveyances of property to a relative that the intention is to shelter the property from attacks by future creditors.[76] Why else would Miss Lane-Fox settle her wealth on trustees as soon as she got it? The difference between *Mackay v. Douglas* and *Re Lane-Fox* may be that creditors were more likely to arise in the business of jute speculation than they were in the life of the young Miss Lane-Fox. Douglas' intention in settling the leasehold on his wife was more specific and directed toward defeating the future creditors of the partnership

72 *Supra*, note 71, p. 513.

73 *Supra*, note 71, p. 514.

74 *Denny's Trustee v. Denny & Warr, supra*, note 16; *Fleming v. Edwards* (1896), 23 O.A.R. 718; *Clinton v. Sellars* (1908), 1 Alta. L.R. 135; *Gauthier v. Woollatt, supra*, note 45; *Cromwell v. Comeau* (1957), 8 D.L.R. (2d) 676 (N.S.C.A.); *Lewisporte Wholesalers Ltd. v. Hynes* (1975), 24 Nfld. & P.E.I.R. 252 (Nfld. S.C.); *B & N Flooring Supplies Ltd. v. Williams* (1980), 34 N.B.R. (2d) 582 (Q.B.); *Commerce Capital Mortgage Corp. v. Jemmett, supra*, note 66. Vice-Chancellor Malins had foreseen the necessity for a limitation along these lines: see passage from *Mackay v. Douglas*, quoted *supra*, note 64.

75 *Supra*, note 45.

76 My analysis of this problem owes much to discussions with Professor John Smith.

while Miss Lane-Fox was merely protecting herself against the unlikely (in the judge's view) possibility of creditors arising some time during her life.

These distinctions between the two cases exist and may explain why Sir George Jessel underlined the hazardous character of jute partnerships and the grocery business in his judgment in *Ex parte Russell*.[77] However, one is tempted by these and other decisions to think that what Karl Llewellyn[78] called the "fireside equities" have as much to do with the results as any finding as to the specificity of intent or the likelihood of future creditors. What the courts often appear to be doing is weighing the relative merits of the debtor, the transferee and the future creditors and then deciding the issue of intent so as to produce the desired result. Whatever the reasons or motives of the courts, the cases do not mesh into any clear and coherent pattern, probably because the choice between the debtor's right to plan his or her affairs and the creditors' right to payment is a difficult one.[79]

4. Fraudulent Preferences

(a) Introduction

We earlier noted that the Statute of Elizabeth did not prohibit a transaction which had the effect of preferring one creditor over another.[80] While the policy might be acceptable as far as unsecured creditors' rights were concerned, it did not fit well with the Bankruptcy Acts, the purpose of which was to create a scheme of *pari passu* sharing among creditors entitled to claim. As a result, the English legislation was amended to include sections prohibiting fraudulent preferences occurring within a certain time period before the bankruptcy[81] and the Canadian Bankruptcy Acts have followed suit.[82]

As early as 1859, Ontario had enacted sections prohibiting fraudulent preferences,[83] and these provisions were incorporated into that province's Assignments Act of 1885,[84] enacted to fill the gap left by the repeal by the federal government of the Insolvent Acts of 1869 and 1875.[85]

77 *Supra*, note 69.

78 In *The Common Law Tradition: Deciding Appeals* (1960).

79 For the most thoughtful assessment of the problem, see the judgment of Roach J. in *Gauthier v. Woollatt*, *supra*, note 45. A majority of the Ontario Law Reform Commission, *supra*, note 22, pp. 149-56, 216-19, proposes that (1) the definition of "creditor" be expanded to include persons with a judgment or a cause of action, but that (2) a creditor whose judgment or cause of action arises subsequent to a conveyance should not have a right to impeach that conveyance.

80 *Supra*, Chapter 18, sections 2 and 3(a), although see *Optical Recording Laboratories Inc. v. Digital Recording Corp.* (1990), 1 O.R. (3d) 131 (C.A.).

81 Bankruptcy Act, 1869 (32 & 33 Vict.), c. 71, s. 92. See Farrar, "The Bankruptcy of the Law of Fraudulent Preference", [1983] J. Bus. Law 390.

82 Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3.

83 Relief of Insolvent Debtors Act, C.S.U.C. 1859, c. 26, ss. 17-20.

84 An Act Respecting Assignments for the Benefit of Creditors, 1885 (Ont.), c. 26.

85 1869 (Can.), c. 16; 1875 (Can.), c. 16; 1880 (Can.), c. 1.

We have already discussed the history of assignments and fraudulent preference legislation in Canada. At this point it is enough to say that all jurisdictions today except three[86] have either an Assignments Act more or less based on the Ontario model or a Fraudulent Preference Act which contains only fraudulent preference sections and not the other assignments machinery which still exists in Ontario.[87]

(b) Present Canadian Legislation

While the Ontario assignments legislation was the predecessor of all Canadian fraudulent preference statutes, variations have developed, particularly in western Canada. We will start by looking at the fraudulent preference sections of the Ontario Assignments and Preferences Act[88] and will then examine western and other attempts to improve on the Ontario model.

Section 4(1) of the Assignments and Preferences Act provides that every gift or conveyance[89] of real or personal property[90] made by an insolvent person "with

86 Manitoba repealed its Assignments Act in 1984. See Statute Law Amendment Act (1984) (Man.), c. 17, s. 2. Newfoundland has a Fraudulent Conveyances Act, R.S.N. 1990, c. F-24, modelled roughly on the Statute of Elizabeth but no Assignments or Fraudulent Preferences Act. The Northwest Territories has no legislation on fraudulent conveyances or preferences.

87 There is a large Canadian literature on fraudulent preferences. Particularly useful are Canadian Bar Association — Ontario, *Fraudulent Conveyances, Unjust Preferences and Other Transactions Subject to Attack by Creditors* (1993) — lectures by Springman and Zimmerman; Gertner, Springman, McGuinness, Morrison, Stewart & Laskin, *Debtor and Creditor: Cases and Commentary* (3rd ed. 1987), pp. 601-29 (hereafter "Gertner Casebook"); Hansford, "Fraudulent Conveyances and Preferences" (1987), 2 Nat. Creditor/Debtor Rev. 108, 124; Harris, "Fraudulent Conveyances and Preferences" in Canadian Institute, *Debtors and Creditors: From Protection to Collection* (1986), vol. 2, pp. 6-18 to 6-27; Howcroft, *supra*, note 43; Kerr, "Fraudulent Conveyances and Unjust Preferences", in Springman and Gertner, eds., *Debtor-Creditor Law: Practice and Doctrine* (1985), p. 191; *Legal Education Society of Alberta, Fraud, Fraudulent Conveyances and Fraudulent Preferences* (1985) — lecture by McDonald and Locke; Prowse, "Fraudulent and Voidable Conveyances" in Canadian Institute, *Debtors and Creditors: Protection to Collection in an Uncertain Economy* (1987), p. C-1; Robinson, *British Columbia Debtor-Creditor Law and Precedents* (1993), cc. 10 and 11; Springman, *supra*, note 38. On reform, see Alberta Law Reform Institute, *Financial Assistance by a Corporation: Section 42, The Business Corporations Act (Alberta): Report No. 54* (1989); Law Reform Commission of B.C., *Report on Fraudulent Conveyances and Preferences* (1988: LRC 94) (reviewed by Springman in (1989), 15 Can. Bus. Law J. 180); Ontario Law Reform Commission, *supra*, note 22, pp. 125-245.

88 R.S.O. 1990, c. A.33. I omit reference to s. 3, which avoids fraudulent confessions of judgment. The section goes back to the 1859 legislation, *supra*, note 83, but has lost most of its significance after the enactment of Creditors' Relief Acts: see Dore and Kerr, *supra*, note 22, pp. 106-07.

89 A debtor's disclaimer of an interest in an estate is not a conveyance for this purpose. See *Sembaliuk v. Sembaliuk* (1983), 27 Alta. L.R. (2d) 223, 228-29, reversed on other grounds (1984), 35 Alta. L.R. (2d) 193 (C.A.), leave to appeal to S.C.C. refused (1985), 35 Alta. L.R. (2d) xl.

90 As in the case of fraudulent conveyances, the property must belong to the debtor. See *Rosenfeldt v. Olson* (1984), 16 D.L.R. (4th) 103, 118-20, reversed on other grounds (1986), 25 D.L.R. (4th) 472 (B.C.C.A.), leave to appeal to S.C.C. refused 72 N.R. 77 (S.C.C.).

intent to defeat, hinder, delay or prejudice creditors, or any one or more of them" is void[91] as against the injured creditor or creditors. This provision is nothing more than a limited version of the Statute of Elizabeth and would appear to add little to the English legislation.

Section 4(2) is more interesting. It says that every gift or conveyance made by an insolvent "to or for a creditor with the intent to give such creditor an unjust preference over other creditors or over any one or more of them"[92] is void as against the neglected creditors.[93] The impact of s. 4(2) is expanded by subsections (3) and (4), which provide that "if such a transaction with or for a creditor has the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them", it shall in two situations "be presumed, in the absence of evidence to the contrary, to have been made with the intent mentioned in subsection (2), and to be an unjust preference within the meaning of this Act whether it be made voluntarily or under pressure".[94] The two situations in which the presumption operates are

(1) in respect to any action or proceeding brought within 60 days thereafter to impeach or set aside such transaction, or
(2) if the debtor within 60 days after the transaction makes an assignment for the benefit of his or her creditors.[95]

Section 5 lists a series of transactions to which s. 4 will not apply.[96]

Most provinces have a fairly close equivalent to Ontario s. 4(2) but more variety exists as to the deemed intent provisions. For example, s. 3 of the Alberta statute[97] provides that every gift or conveyance made by an insolvent person to a creditor "and having the effect of giving that creditor a preference" over other creditors is, with respect to any action brought within one year thereafter to impeach the transaction, void as against the injured creditor or creditors.

Seetion 4 adds clarification:

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91 As in the Statute of Elizabeth one assumes that "void" is to be read as "voidable". See *supra*, Chapter 18, section 3(b).

92 Most Canadian Acts omit the word "unjust".

93 Prince Edward Island has a similar section, which goes on to say that the conveyance is void "whether the same be made voluntarily or under pressure": see Frauds on Creditors Act, R.S.P.E.I. 1988, c. F-15, s. 2(2).

94 New Brunswick and Nova Scotia follow the Ontario section but omit the words "in the absence of evidence to the contrary".

95 The Prince Edward Island section allows the presumption to operate in situation (1) only: see *supra*, note 93. The section also provides that the intent referred to is the intent of the assignor or transferor, "and no concurrence therein, or knowledge thereof, or of insolvency, need be shown in the assignee or transferee".

96 See *infra*, section 4(g), "Excluded Transactions".

97 Fraudulent Preferences Act, R.S.A. 1980, c. F-18.

4(1) A transaction shall be deemed to be one that has the effect of giving a creditor a preference over other creditors, within the meaning of section 3, if by the transaction a creditor is given or realizes or is placed in a position to realize payment, satisfaction or security for the debtor's indebtedness to him or a portion of it greater proportionately than could be realized by or for the unsecured creditors generally of the debtor or for the unsecured portion of his liabilities out of the assets of the debtor left available and subject to judgment, execution, attachment or other process.

(2) Independently of the intent with which the transaction was entered into or of whether it was entered into voluntarily or under pressure, the preferential effect or result of the impeached transaction governs, and no pressure by a creditor or want of notice to the creditor alleged to have been so preferred of the debtor's circumstances, inability or knowledge as aforesaid, or of the effect of the transaction, avails to protect the transaction except as provided by sections 6 and 9.

The other western provinces and territories, except for Manitoba and the Northwest Territories, have roughly similar provisions which are discussed below in subsection (f).[98]

(c) Who Can Challenge

The Canadian Fraudulent Preferences Acts prohibit the preferring of creditors as against other creditors, defined to include sureties, endorsers of promissory notes and bills of exchange and, in the western jurisdictions, cestuis que trust or other persons to whom liability is equitable only. However the Canadian statutes have not used the expansive formula "creditors and others" employed in the Statute of Elizabeth. As a result, we would expect the cases to say that subsequent creditors, such as plaintiffs with damage claims which have not yet been reduced to judgment, would not be able to challenge a transaction under the fraudulent preference legislation. Most Canadian cases take this position[99]

98 Fraudulent Preference Act, R.S.B.C. 1979, c. 143, ss. 4 and 5; Fraudulent Preferences Act, R.S.S. 1978, c. F-21, s. 6; Fraudulent Preferences and Conveyances Act, R.S.Y.T. 1986, c. 72, s. 5. The 1979 redrafting of the British Columbia legislation rendered an already difficult statute still more obscure. See the B.C. Law Reform Commission Report and the articles and books by Hansford and Robinson cited *supra*, note 87.

99 *Ashley v. Brown* (1890), 17 O.A.R. 500; *Gurofski v. Harris, supra*, note 58; *Fisher v. Kowslowski* (1913), 13 D.L.R. 785 (Man. K.B.); *Hopkinson v. Westerman, supra*, note 56; *Innes v. Cameron Valley Land Co.*, [1919] 1 W.W.R. 751 (B.C.S.C.); *Huss v. Lakin, supra*, note 56; *Ehattesaht Co-operative Enterprises Assn. v. Vancouver Equipment Corp.* (1977), 3 B.C.L.R. 117 (S.C.); *Devlin v. Hean* (1982), 41 B.C.L.R. 206 (S.C.); *DeGraaf v. Staniszkis Developments Ltd.*, [1988] B.C.D. Civ. 545-01; but *cf. MacDonald v. MacDonald* (1957), 10 D.L.R. (2d) 309 (Ont. H.C.). See also Kerr, *supra*, note 15, pp. 378-87; Ontario Law Reform Commission, *supra*, note 22, pp. 156-57, 162-63, 229-30; Parker, *supra*, note 6, c. 2. Dore and Kerr, *supra*, note 22, argue for a more expansive reading of "creditor". On the right of a court-appointed receiver-manager to sue as agent of the creditor, see *Aries Resources Ltd. v. Zag Invt. Ltd.* (1989), 75 C.B.R. (N.S.) 298 (Alta. Q.B.).

although there is British Columbia authority to the contrary.[1]

As with the Statute of Elizabeth,[2] a secured creditor cannot challenge a transaction under the Fraudulent Preferences Acts unless the security is insufficient to cover the claim.[3]

(d) Requirement of Insolvency

Besides the limitation to creditors, the fraudulent preference legislation is more restrictive than the Statute of Elizabeth in a second aspect, namely, the requirement that the debtor be insolvent. The Ontario Act, in words which have been copied *verbatim* in most other Canadian jurisdictions, provides that the impugned transactions must be "made by a person when insolvent or unable to pay the person's debts in full or when the person knows that he, she or it is on the eve of insolvency".[4] While the statute literally appears to provide three alternatives, the courts have decided that there is no real difference between at least the first two situations.[5]

The cases are less clear on what content to give the notion of insolvency.[6] In an early Ontario decision, Spragge V.C. said that, to determine the solvency or insolvency of a debtor, it is necessary

> . . . to see and examine whether all his property, real and personal, be sufficient if presently realized for the payment of his debts, and in this view we must estimate his land, as well as his chattel property, not at what his neighbours or others may consider to be its value, but at what it will bring in the market at a forced sale; or at a sale when the seller cannot await his opportunities, but must sell.[7]

The quoted passage has been much cited and followed,[8] but judges have shown some unhappiness at the choice of a fictional forced sale as the device to value

1 *Newlands Sawmills Ltd. v. Bateman* (1922), 70 D.L.R. 165 (B.C.C.A.); *Re Skinner* (1960), 27 D.L.R. (2d) 74 (B.C.S.C.); but *cf. Re Ehattesaht Cooperative Enterprises Assn. and Vancouver Equipment Corp., supra*, note 99; *DeGraaf v. Staniszkis Developments Ltd., supra*, note 99.

2 Fraudulent Conveyances Act, 1571 (13 Eliz. 1), c. 5, made perpetual by the Continuance, etc., of Acts, 1586-87 (29 Eliz. 1), c. 5.

3 *Robin Hood Milling Co. v. Maple Leaf Milling Co.* (1916), 9 W.W.R. 1453 (Man. K.B.); *McLean v. Hodge* (1919), 50 D.L.R. 123 (Sask. C.A.); *Barrett v. Baron*, [1925] 1 D.L.R. 474 (Sask. C.A.); *Re Ehattesaht Co-operative Enterprises Assn., supra*, note 99; *Canadian Imperial Bank of Commerce v. Aldergrove Electric Ltd.* (1979), 30 C.B.R. (N.S.) 303 (B.C.S.C.); *Delbreuck & Co. v. Muenzenberg* (1984), 54 B.C.L.R. 264 (S.C.). *Canadian Imperial Bank of Commerce v. Boukalis* (1987), 65 C.B.R. (N.S.) 66 (C.A.) suggests the same result for fraudulent preference (although not fraudulent conveyance) legislation.

4 Assignments and Preferences Act, R.S.O. 1990, c. A.33, s. 4(1). *Cf.* s. 4(2).

5 *Dominion Bank v. Cowan* (1887), 14 O.R. 465; *Bertrand v. Canadian Rubber Co.* (1897), 12 Man. R. 27, affirmed 17 C.L.T. 427 (C.A.); *Jagger v. Turner & Co.* (1909), 12 W.L.R. 588 (Sask. K.B.); *Crestwood Kitchens Ltd. v. Camco Inc.* (1982), 47 C.B.R. (N.S.) 103 (B.C.S.C.); but *cf. Stihl Ltd. v. Motion Engine Services Ltd.* (1990), 106 A.R. 118 (Q.B.).

6 For a useful discussion of the term, see Honsberger, *Debt Restructuring: Principles and Practice* (1990), c. 1.

7 *Davidson v. Douglas* (1868), 15 Gr. 347 at 351.

8 *Warnock & Co. v. Kloepfer* (1887), 14 O.R. 288, affirmed 15 O.A.R. 324, which was affirmed

the debtor's property. In three later cases,[9] Rose J. drew a distinction between legal insolvency, *i.e.*, not having sufficient property to pay one's debts if sold under legal process, and commercial insolvency, namely, not having the means to pay off and discharge one's commercial obligations as they become due in the ordinary course of business. The learned judge concluded that the insolvency referred to in the Assignments Act is legal insolvency, but subject to the caveat that the hypothetical forced sale must be fairly and reasonably conducted. The time at which one pretends the forced sale to take place is not clear.[10] There are cases in western Canada which appear to reject the forced sale formula entirely in favour of something akin to a commercial insolvency test.[11]

Whatever the appropriate definition of insolvency, the legal burden of proving this element of the case clearly rests with the plaintiff who challenges the transaction.[12] Mere suspicion will not be enough[13] nor is it adequate to prove financial embarrassment,[14] much less a simple unwillingness to pay.[15] What must be established is incapacity to pay one's debts. Some cases do say that while the legal burden always rests with the plaintiff, the evidentiary burden will shift to the defendant fairly early in the trial, particularly because the facts necessary to prove insolvency are usually not within the plaintiff's knowledge but are within the knowledge of the defendant.[16]

(1891), 18 S.C.R. 701 (*sub nom. Kloepfer v. Warnock*); *Walter v. Adoph Lumber Co.* (1915), 8 W.W.R. 351 (Alta. T.D.); *Richards & Brown Ltd. v. Leonoff* (1915), 8 W.W.R. 966 (Man. K.B.); *Trotter v. Pedlar*, [1921] 1 W.W.R. 233 (Man. K.B.); and *Knox v. Shaw*, [1927] 2 W.W.R. 494 (Sask. C.A.).

9 *Rae v. McDonald* (1887), 13 O.R. 352 (C.A.); *Clarkson v. Sterling* (1887), 14 O.R. 460, affirmed 15 O.A.R. 234; *Dominion Bank v. Cowan, supra*, note 5. *Cf.* Dore and Kerr, *Third Report of the Consumer Protection Project: Legal Remedies of the Unsecured Creditor after Judgment* (N.B. 1976), pp. 107-11 (unpublished).

10 *Richards & Brown Ltd. v. Leonoff, supra*, note 8.

11 *Bertrand v. Canadian Rubber Co., supra*, note 5; *Richards & Brown Ltd. v. Leonoff, supra*, note 8; *Sun Sudan Oil Co. v. Methanex Corp.* (1992), 5 Alta. L.R. (3d) 292 (Q.B.); *cf. Sutherland v. Nixon* (1862), 21 U.C.Q.B. 629 (C.A.); *Empire Sash & Door Co. v. Maranda* (1911), 19 W.L.R. 78 (Man. K.B.); *Bank of British Columbia v. Parkwood Forest Products* (1985), 65 A.R. 389 (Q.B.).

12 *Walter v. Adolph Lumber Co., supra*, note 8; *Wolfe v. Smith*, [1923] 3 W.W.R. 375 (Sask. C.A.); *McLean v. Ratekin*, [1928] 2 W.W.R. 421 (Sask. C.A.).

13 *Wolfe v. Smith, supra*, note 12; *Caulfield, Burns and Gibson Ltd. v. Kitchen*, [1956] O.W.N. 697.

14 *Caulfield, Burns and Gibson Ltd. v. Kitchen, supra*, note 13.

15 *Clarke v. Sutherland*, [1917] 3 W.W.R. 624 (Alta. C.A.); *Toronto Dominion Bank v. Melanson* (1981), 36 N.B.R. (2d) 431 (Q.B.).

16 *Clarke v. Sutherland, supra*, note 15. See also *Empire Sash & Door Co. v. Maranda, supra*, note 11, p. 86; *Trotter v. Pedlar, supra*, note 8; *Alberta (Attorney General) v. Samuel Doz Professional Corp.* (1993), 9 Alta. L.R. (3d) 201 (Q.B.). But *cf. McLean v. Ratekin, supra*, note 12, where the court draws the distinction between legal and evidentiary burdens but does not permit the evidentiary burden to shift until clear and direct evidence of insolvency is led by the plaintiff.

(e) Transactions Not Attacked Within 60 Days

All Canadian Fraudulent Preference Acts draw a distinction between transactions which occur within 60 days before an attack by the creditor or an assignment by the debtor and transactions which occur outside the 60-day time limit.[17] In order to understand the significance of the distinction, it is necessary to review the history of the Ontario legislation and the judicial reaction to it.[18]

Before 1885, the courts of that province had decided that, in order to invalidate a transaction, it was necessary to prove a concurrent intent to prefer on the part of debtor and creditor. Moreover it had been held that the debtor's intent must be fully voluntary and that pressure by the creditor or by circumstances, if it was of such a nature as to control the debtor's volition, would strip his or her action of its voluntary character and therefore protect the transaction.

In 1885, the Ontario legislature passed An Act Respecting Assignments for the Benefit of Creditors, which amended the preceding legislation to invalidate transactions which had the effect of preferring a creditor.[19] The courts were not prepared to give these words their natural meaning; the decisions of *Johnson v. Hope*[20] and *Molsons Bank v. Halter*[21] effectively brought the law back to its pre-1885 state.

As a result, the Ontario legislature in 1891[22] repealed the controversial section and substituted for it what is now in substance s. 4(2)-(4) of the Act.[23] The distinction between transactions within and without the 60-day time limit has been adopted by all Canadian jurisdictions, although there are significant variations in the Fraudulent Preference Acts of western Canada. In this section, it is intended to look at the transactions which occur outside the 60-day time limit, reserving the special presumptions applicable to 60-day transactions for subsection (f).

There can be no doubt under s. 4(2) of the present Ontario Act and equivalent provisions elsewhere that the dominant intention of the transferor must be to prefer the creditor to whom the impugned assignment is made. Where the debtor makes the conveyance in order to continue in business and meet obligations rather than to prefer the favoured creditor, the transaction will not be struck down.[24] The

17 The time limits are longer in the Alberta and Yukon Territory legislation.

18 See generally Parker, *Frauds on Creditors and Assignments for the Benefit of Creditors* (1903), pp. 169-71.

19 1885 (Ont.), c. 26, s. 2.

20 (1890), 17 O.A.R. 10.

21 (1890), 18 S.C.R. 88.

22 1891 (Ont.), c. 20.

23 On reform of these sections, see Ontario Law Reform Commission, *Report on the Enforcement of Judgment Debts and Related Matters* (1983), vol. 4, p. 160-245.

24 *McCrae v. White (Whyte)* (1883), 9 S.C.R. 22; *Long v. Hancock* (1885), 12 S.C.R. 532; *Canadian Johns Manville Ltd. v. Knight Bros. Co.* (1917), 12 O.W.N. 211; *Re Barnett* (1983), 43 A.R. 215 (Q.B.); *Holbrook v. Cedpar Properties Inc.* (1986), 62 C.B.R. (N.S.) 18 (Ont. H.C.).

intent to prefer is an essential ingredient of the plaintiff's action and mere suspicion of the debtor's motives will not suffice.[25]

Not only must the debtor intend to prefer the assignee, but the intention must be voluntary.

> The actuating or governing or dominant motive must be the debtor's wish to benefit one creditor at the expense of the others. If then the transfer can properly be referred to or is the result of some other motive, it cannot be regarded as a preference.[26]

There are many motives other than the desire to prefer which can remove a transaction from the scope of the fraudulent preference legislation. The most common example is the case in which the debtor simply yields to a more or less urgent request or demand by a creditor to give security. In such a situation, the transfer is said to result from pressure and it will be valid, despite the fact that its effect is clearly to prefer the importunate creditor over the others,[27] unless the court finds that the creditor's demand was a sham intended only to result in a preference to himself or herself.[28]

The early Canadian cases extended the doctrine of pressure so far that it might well have rendered the Fraudulent Preference Acts entirely impotent. The Supreme Court made it clear that "a mere demand by the creditor without even a threat of, much less a resort to, legal proceedings is sufficient pressure to rebut the presumption of a preference".[29] Nor need the pressure flow from the creditor. There are several cases which recognize that pressure of circumstances, such as fear of legal prosecution[30] or a desire to repair a breach of trust,[31] is a motive which can displace the motive to prefer the assignee. The extent to which the early cases could be taken was criticized by Middleton J.A. in *Re Carson*:

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25 *Wolfe v. Smith*, *supra*, note 12; *Kisluk v. B.L. Armstrong Co.* (1982), 44 C.B.R. (N.S.) 251 (Ont. H.C.); *Austin Marshall Limited v. Bennie* (1985), 56 C.B.R. (N.S.) 71 (Ont. H.C.). The test was satisfied in *Re Dyck* (1982), 21 Sask. R. 93 (Q.B.). See Vandor (1983), 61 Can. Bar Rev. 617. On onus, see *Batch's Service Ltd. v. McNeill Drilling Ltd.* (1990), 82 Sask. R. 265 (Q.B.).

26 Parker, *supra*, note 18, p. 178. See also *Holbrook v. Cedpar Properties Inc.*, *supra*, note 24; *Alberta (Director of Employment Standards) v. Sanche* (1992), 5 Alta. L.R. (3d) 243 (Q.B.).

27 *Slater v. Oliver* (1884), 7 O.R. 158 (C.A.); *Molsons Bank v. Halter*, *supra*, note 21; *Stephens v. McArthur* (1891), 19 S.C.R. 446; *Gibbons v. McDonald* (1892), 20 S.C.R. 587; *Roe v. Massey Mfg. Co.* (1892), 8 Man R. 126 (C.A.); *Fisher v. Brock* (1892), 8 Man. R. 137 (C.A.); *Bertrand v. Parkes* (1892), 8 Man. R. 175 (C.A.); *Colquhoun v. Seagram* (1896), 11 Man. R. 339 (C.A.); *Beattie v. Wenger* (1897), 24 O.A.R. 72; *Adams v. Bank of Montreal* (1901), 32 S.C.R. 719; *Brown v. Bank of Montreal* (1916), 23 B.C.R. 68 (C.A.); *Bank of Montreal v. Ngo* (1985), 56 C.B.R. (N.S.) 66 (B.C.S.C.); *cf. Long v. Hancock*, *supra*, note 24. It is necessary to show that the pressure by the creditor actually induced the transfer: see *Munro v. Standard Bank* (1913), 30 O.L.R. 12.

28 *Royal Bank v. Sullivan*, [1957] O.W.N. 68, affirmed [1957] O.W.N. 520 (C.A.).

29 *Stephens v. McArthur*, *supra*, note 27, pp. 453-54.

30 *Bank of Montreal v. Stair* (1918), 44 O.L.R. 79.

31 *Carr v. Corfield* (1890), 20 O.R. 218; *Innes v. Cameron Valley Land Co.*, [1919] 1 W.W.R. 751 (B.C.S.C.); *Re Carson* (1924), 55 O.L.R. 649 (C.A.).

> When the debtor and the creditor both knew the law, it sometimes happened that pressure was, in fact, very gentle before the debtor parted with his property. Demand was made with a farcical simulation of earnestness so that the transaction might be upheld.[32]

The potential dangers of the doctrine of pressure produced a reaction from the courts and the legislature. In *Re Carson*, Orde J.A. suggested that pressure to be effective "must involve the threat or the belief that legal proceedings are about to be taken". It must be "something from without", not simply the pangs of a guilty conscience.[33] The legislatures in all Canadian jurisdictions have limited or abolished the doctrine of pressure in transactions occurring within the 60-day period before an assignment or an action challenging the conveyance. However, as to transactions which fall outside the 60-day period, pressure is still a potent defence to a fraudulent preference action.[34]

To this point, we have been examining the intent of the debtor which must be established, but the assignee's state of mind is also relevant. At least before 1976, the plaintiff was required to prove that (1) the creditor-assignee knew or should have known of the debtor's insolvency at the date of the transfer and that (2) the creditor participated in the fraud in the sense that he or she knowingly and willingly accepted the preference over other creditors.[35] Proof of knowledge of insolvency was made easier by the decision of Lord Hobhouse in *National Bank of Australasia v. Morris*[36] that knowledge will be proven if it is established that the creditor knew facts which ought to have shown that the debtor could not on the date of the assignment meet his or her financial obligations generally. Mere evidence of financial embarrassment would not do;[37] insolvency in the sense

32 *Supra*, note 31, p. 657.

33 *Supra*, note 31, p. 658.

34 Except in Prince Edward Island: see Frauds on Creditors Act, R.S.P.E.I. 1988, c. F-15, s. 2(2), which says that the conveyance is void "whether the same be made voluntarily or under pressure".

35 *Johnson v. Hope*, *supra*, note 20; *Gibbons v. McDonald*, *supra*, note 27; *Benallack v. Bank of B.N.A.* (1905), 36 S.C.R. 120; *Horne v. Galt* (1908), 1 Alta. L.R. 392; *Douglas v. Hourie* (1909), 10 W.L.R. 67 (Sask. K.B.); *Northern Commercial Co. v. Powell* (1911), 17 W.L.R. 297 (Y.T.); *Merchants Bank v. Ken McClary & Co.*, [1921] 1 W.W.R. 940 (Sask. K.B.); *Connerty v. Cross* (1922), 22 O.W.N. 467 (C.A.); *Wolfe v. Smith*, [1923] 3 W.W.R. 375 (Sask. C.A.); *Re Carson*, *supra*, note 31; *Bank of Montreal v. Shean*, [1931] O.R. 489; *Royal Bank v. Sullivan*, *supra*, note 28; *Orpheum Management Ltd. v. Prince Albert Credit Union Ltd.* (1981), 39 C.B.R. (N.S.) 107 (Sask. Q.B.); *Canadian Commercial Bank v. Prudential Steel Ltd.* (1986), 66 C.B.R. (N.S.) 172 (Alta. Q.B.); *Alberta (Director of Employment Standards) v. Sanche*, *supra*, note 26. Concurrent intent is easier to establish where there is a close relationship between the contracting parties: see *Canadian Imperial Bank of Commerce v. Grande Cache Motor Inn Ltd.* (1977), 4 Alta. L.R. (2d) 319 (T.D.); *Burton v. R. & M Insurance Ltd.* (1977), 5 Alta. L.R. (2d) 14 (T.D.).

36 [1892] A.C. 287 (P.C.). See also *Gulf & Fraser Fishermen's Credit Union v. W.R. Menchions & Co.* (1965), 55 W.W.R. 191 (B.C.C.A.); *Moroso v. Monk*, [1984] B.C.D. Civ. 545-03 (B.C.S.C.); *Columbia Bitulithic Ltd. v. M.D. Tuck Lumber Co. Ltd.*, [1985] B.C.D. Civ. 545-04 (B.C.S.C.).

37 *Bank of Montreal v. Shean*, *supra*, note 35.

discussed earlier must be evident to the creditor or to someone standing in the creditor's shoes.

The requirement that the plaintiff prove that the creditor knew of the debtor's insolvency and shared in the intent to prefer was established early in Canadian law, although there were dissenters, particularly in the Manitoba courts.[38] These concurrent intent rules have created obvious problems in challenging fraudulent preferences because the task of establishing the creditor's knowledge and involvement will usually be much more difficult than finding the necessary intent in the debtor alone. A similar problem bedevilled the law of bankruptcy until 1976 when the Supreme Court of Canada held in *Hudson v. Benallack*[39] that, in order to set a transaction aside under s. 73 of the Bankruptcy Act,[40] one need only be concerned with the intent of the debtor. While the Supreme Court is careful to distinguish their previous decisions on fraudulent preference statutes, Dickson J. does describe one of them, *Benallack v. Bank of B.N.A.*,[41] as "unsatisfactory".[42] Bearing in mind the similar history and objectives of fraudulent preference provisions in the Bankruptcy Act and in provincial statutes, it is difficult to see why the reasoning in the later *Benallack* case should not apply to the provincial statutes as well, and this conclusion has already been adopted in one New Brunswick case.[43]

(f) Transactions Attacked Within 60 Days

The purpose of provisions like Ontario s. 4 (3)-(4), as noted earlier, was to lighten the burden of the plaintiff challenging transactions entered into within 60 days of an action or of an assignment by the debtor. The Ontario legislation has not been particularly successful in achieving this end compared to the differently drafted statutes in western Canada.

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38 *Schwartz v. Winkler* (1901), 13 Man. R. 493; *cf. Gunn v. Vinegratsky* (1911), 17 W.L.R. 54 (Man. C.A.); *Robinson v. McCauley* (1913), 4 W.W.R. 930, affirmed 5 W.W.R. 789 (Man. C.A.); *Weidman Bros. v. Simovitch*, [1945] 3 W.W.R. 203 (Man. K.B.); Jewers, "Fraudulent Conveyance and Preference Legislation in Canada" (1956), 28 Man. Bar News 1 at 8-11.

39 [1976] 2 S.C.R. 168.

40 R.S.C. 1970, c. B-3. See now Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, s. 95.

41 *Supra*, note 35.

42 "The case [*Benallack v. Bank of B.N.A., supra*, note 35] is unsatisfactory, if I may, with respect, say so, in that none of the 'long line of decisions' upon which Idington J. relies is identified and no reasons are given for concluding that the intent to which the Ordinance refers must be entertained by the creditor as well as the debtor." (*Supra*, note 39, p. 180).
The criticism is not completely fair. Idington J. no doubt felt it unnecessary to cite previous cases and make policy arguments in light of the then recent decisions on the question in *Gibbons v. McDonald, supra*, note 27 and *Johnson v. Hope, supra*, note 20, not to speak of the discussion by Parker, whose book was published in 1903. The judgment of the Yukon Territorial Court appealed from is not reported but a substantial portion is reproduced in *Northern Commercial Co. v. Powell, supra*, note 35. It appears to have been a more thorough treatment of the issue and, as the Supreme Court affirmed it, they may have felt that extensive reasons were unnecessary.

43 *Federal Business Development Bank v. Van Klaveren* (1979), 51 A.P.R. 79 at 84-85 (N.B.Q.B.). But see *Canadian Commercial Bank v. Prudential Steel Ltd., supra*, note 35.

The Ontario Act originally provided that a transaction occurring within the 60-day period was "presumed" to have been made with the relevant intent and to be an unjust preference. The courts had considerable difficulty in deciding whether the presumption so worded was rebuttable or not.[44] When the sections were amended in 1891 to read "presumed prima facie", the courts, after some initial uncertainty, held that the defence of pressure was gone absolutely but that, as to intent, the presumption was rebuttable. The onus of rebutting the presumption by establishing no fraudulent intent is on those supporting the transaction.[45] The plaintiff must still prove the insolvency of the debtor as a fact before the plaintiff can rely on the presumption sections.[46]

In western Canada, the sections were drafted more widely with the result that it appears clear that the doctrine of pressure is gone absolutely and the presumption of fraudulent intent is irrebuttable.[47] One assumes that, as in Ontario, insolvency must still be proven as a fact.

(g) Excluded Transactions

Most Canadian fraudulent preference statutes contain lists of transactions which are excluded from the operation of the legislation. The reader is referred to the specialist books and essays on reviewable transactions for further assistance. The conveyance of property which is not exigible or attachable at the instance of judgment creditors also cannot be attacked under fraudulent preference or conveyance legislation.[48]

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44 See cases cited in *Lawson v. McGeoch* (1893), 20 O.A.R. 464.

45 *Lawson v. McGeoch, supra*, note 44; *Webster v. Crickmore* (1898), 25 O.A.R. 97; *Dana v. McLean* (1901), 2 O.L.R. 466 (C.A.); *Keenan v. Richardson* (1902), 1 O.W.R. 333 (C.A.); *Brown v. Beamish* (1905), 5 O.W.R. 722; *Crawford v. Magee* (1905), 6 O.W.R. 44; *Craig v. McKay* (1906), 12 O.L.R. 121 (C.A.); *Clifton v. Towers* (1917), 39 O.L.R. 292 (C.A.); and *Pellatt v. McLean* (1929), 63 O.L.R. 522. In *Shediac Boot & Shoe Co. v. Buchanan* (1903), 35 N.S.R. 511 (C.A.), it was held that where the words "*prima facie*" are not included in the statute, the presumption is irrebuttable as to intent. The same results may follow today under the New Brunswick and Nova Scotia statues which omit the words "*prima facie*". *Quaere* as to the Prince Edward Island legislation.

46 *Caulfeld, Burns and Gibson Ltd. v. Kitchen*, [1956] O.W.N. 697.

47 *Empire Sash & Door Co. v. Maranda, supra*, note 11, pp. 87-88; *Hazell v. Cullen* (1914), 20 B.C.R. 603; *Smith v. Sugarman* (1909), 2 Alta. L.R. 442, reversed 3 Alta. L.R. 108, which was reversed 47 S.C.R. 392; *Robinson v. McCauley, supra*, note 38; *Trusts & Guarantee Co. v. R.J. Whitlaw Co.* (1914), 6 W.W.R. 42 (Alta. T.D.); *McLean v. Hodge* (1919), 50 D.L.R. 123 (Sask. C.A.); *cf. Codville v. Fraser* (1902), 14 Man. R. 12 (C.A.); *Weidman Bros. v. Simovitch, supra*, note 38.

48 13 C.E.D. (Ont. 3rd) *Fraudulent and Voidable Conveyances*, para. 106; and see Chapter 13, section 2(i).

TAB 19

DEBTOR AND CREDITOR

Cases and Commentary

Third Edition

E. GERTNER

LL.B. (York), B.C.L. (Oxon),
of the Ontario Bar, and Special Lecturer, Osgoode Hall Law School
and Faculty of Law, University of Toronto

M.A. SPRINGMAN

B.A. (Man.), M.A. (Chicago), M.Sc. (L.S.E.), LL.B. (Tor.)
Senior Legal Research Officer, Ontario Law Reform Commission,
and Special Lecturer, Osgoode Hall Law School and Faculty of
Law, University of Toronto

KEVIN McGUINNESS

LL.B. (Windsor), LL.M.,
S.J.D. (Tor.), of the Ontario Bar

J.J. MORRISON

B.A. (Hon) (York), LL.B. (Windsor), LL.M. (Mich.),
Legal Research Officer, Ontario Law Reform Commission

GEORGE R. STEWART

B.A. (Carleton), LL.B. (Ottawa), LL.M. (L.S.E.),
Professor of Law, University of Windsor

JOHN B. LASKIN

B.A. (York), LL.B. (Tor.), LL.M. (Calif.),
of the Ontario Bar

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TRANSACTIONS IMPEACHABLE BY CREDITORS

1. Introduction

As we have seen, upon obtaining judgment a creditor is entitled to look to his debtor's entire asset pool to satisfy the debt, subject to some notable exceptions and to the statutory exemptions from execution and garnishment. However, in some cases, a debtor, desirous of frustrating his creditors, will convey or give away his property to a third person. Loisseaux, in his *Cases on Creditors Remedies* (Indianapolis: Bobbs-Merill, 1966), stated (at 249):

> [T]he dishonest person in debt, or facing a large prospective debt, has for at least the past four centuries tended to react in the same manner. The debtor will attempt to conceal some or all of his property. If he is a little more sophisticated, he will frequently try to convey it to a relative or a friend who will make an express promise to return the property after the financial trouble has passed. In more desperate straits, such a debtor may simply transfer his assets to friends and relatives for little or no consideration, just to keep the assets from his creditors.

In other cases, a debtor will make a transfer of his property that benefits one or more of his creditors, but prejudices yet other creditors. By means of this type of transfer — or "preference" — the debtor subverts the *pro rata* distribution principle enshrined, for example, in the *Creditors' Relief Act*, R.S.O. 1980, c. 103.

Conceptually, a fraudulent conveyance has been distinguished from a fraudulent or unjust preference. A fraudulent conveyance refers to a transfer by a debtor of his property to a person who is not a creditor, whereas a fraudulent preference is a conveyance to some, but not all, of a debtor's creditors. While the more general Ontario statute, the *Fraudulent Conveyances Act*, R.S.O. 1980, c. 176, would seem to comprehend both fraudulent conveyances and fraudulent preferences, the orthodox (although not quite unanimous) view is that this legislation does not deal with fraudulent preferences.

While, as we shall see, fraudulent conveyances legislation is centuries old, fraudulent preferences were forbidden neither at common law nor under the early statutes: a debtor was entitled to pay his debts in any order he pleased regardless of the prejudicial effect on some of his creditors. It is only under modern statutes — in Ontario, the *Assignments and Preferences Act*, R.S.O. 1980, c. 33 — that these transactions may be set aside.

In the main, there is a fair degree of similarity across Canada in legislation respecting impeachable transactions. All provinces except Newfoundland have fraudulent preference legislation, and British Columbia, Manitoba, Ontario, Quebec, and Newfoundland have adopted separate fraudulent conveyance statutes. In some provinces, pre-*Law of Property Act, 1925* (15 & 16 Geo. 5), c. 20, English fraudulent

conveyance legislation — that is, 13 Eliz. 1, c. 5 — remains in force as part of the general law.

The applicable legislation is as follows: Alberta: *Fraudulent Preferences Act*, R.S.A. 1980, c. F-18 (13 Eliz. 1, c. 5). See *Cdn. Pittsburgh Industries Ltd. v. Roberts & Hall Ltd.*, [1973] 2 W.W.R. 341 (Alta. S.C.); *Goyan v. Kinash*, [1945] 1 W.W.R. 291 (Alta. C.A.); and *Sembaliuk v. Sembaliuk* (1983), 27 Alta. L.R. (2d) 233 (Alta. Q.B.); reversed (1985), 35 Alta. L.R. (2d) 193 (Alta. C.A.). See also generally Cote, "The Reception of English Law" (1977), 15 Alta. L. Rev. 29. British Columbia: *Fraudulent Conveyances Act*, R.S.B.C. 1979, c. 142; *Fraudulent Preferences Act*, R.S.B.C. 1979, c. 143. Manitoba: *Fraudulent Conveyances Act*, R.S.M. 1970, c. F160. New Brunswick: *Assignments and Preferences Act*, R.S.N.B. 1973, c. A-16 (13 Eliz. 1, c. 5). See *Bank of Montreal v. Vandine*, [1953] 1 D.L.R. 456 (N.B.C.A.) and *Cdn. Pittsburgh Industries Ltd. v. Sherman Hardware Ltd.* (1970), 2 N.B.R. (2d) 264 (N.B.S.C.). Newfoundland: *Fraudulent Conveyances Act, 1974*, S.Nfld. 1974, No. 29. Nova Scotia: *Assignments and Preferences Act*, R.S.N.S. 1967, c. 16; (13 Eliz. 1, c. 5). See *Bank of Montreal v. Crowell* (1980), 37 N.S.R. (2d) 292 (N.S.S.C.). Ontario: *Assignments and Preferences Act*, R.S.O. 1980, c. 33; *Fraudulent Conveyances Act*, R.S.O. 1980, c. 176. Prince Edward Island: *Frauds on Creditors Act*, R.S.P.E.I. 1974, c. F-13. Quebec: *Civil Code*, arts. 1032-40. Saskatchewan: *Fraudulent Preferences Act*, R.S.S. 1978, c. F-21.

The B.C. Working Paper noted (at 12) that some cases rely on a close reading of the legislation, while others seem to ignore it. The Paper stated that the law in British Columbia "is more accurately stated without paying too close attention" to the *Fraudulent Conveyances Act*." For a useful survey of voidable transactions law, see Kerr, "Fraudulent Conveyances and Unjust Preferences", in Springman and Gertner, at 191. For Alberta law, see Howcroft, "Scope of Fraudulent Conveyances and Fraudulent Preferences Legislation in Alberta" (1986), 24 Alta. L. Rev. 496 (and (1986), 3 Nat'l Insolv. Rev. 89).

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(at 507–08)

Our earlier discussion of the rights of unsecured creditors has proceeded on the assumption that the debtor takes no defensive action to prevent his tormenters from asserting their legal remedies. The assumption is unrealistic. Many debtors, foreseeing impending financial collapse, take steps to assign their property to a relative or friend, who is to retain it until the storm clouds (and the creditors) clear away. The strategy has dangers, not the least of which is the disloyal transferee who converts the debtor's assets to his own use. Our concern here is not with the advantages and disadvantages to the debtor of this kind of conveyance, but with its potentially disastrous effect on the practical utility of the creditors' remedies, which are likely to realize nothing unless the conveyance can be set aside.

The debtor may not want to shelter his wealth from his creditors as a whole but may instead seek to benefit some creditors at the expense of others. This selective generosity is sometimes explained by the characteristics of the various creditors; the average person in financial trouble will want to pay off loans from his relatives before

satisfying the claims of the bank or the business claimant. In other cases, the debtor will pay first the creditor who is most aggressive or who is vital to the survival of the debtor's business, such as the wholesale supplier of his stock in trade. In all these cases, however, the result of this preferential treatment is that some claims will be satisfied in part or in whole while other creditors will get nothing, even if they resort to their legal remedies.

The law has had considerable difficulty in deciding how to deal with the inappropriate conveyance or preference. It is clearly desirable that an insolvent person should not be able to shelter his assets from the legitimate claims of his creditors by assigning them to a convenient friend. On the other hand, the law is prepared to permit a person embarking on a risky business to protect his personal wealth from subsequent claims by incorporating the enterprise as a separate legal entity. To what extent should a debtor have to retain assets so that subsequent creditors will have something to seize? Can and should a distinction be drawn between fraudulent and innocent transfers and, if so, whose intention is significant? The law cannot go to any lengths to protect creditors; the *bona fide* purchaser of assets from a debtor has some claim to be saved harmless from risks against which he could not have protected himself. Where should the law draw the line between freedom of commerce and the security of the purchaser's title on the one hand and the legitimate claims of creditors on the other?

When we turn from the fraudulent conveyance designed to defeat creditors generally to the transfer intended to prefer some creditors over others, the policy conflict becomes more acute. At common law, creditors had no responsibility to share the fruits of execution equally among their fellows, and we would expect that the debtor's voluntary payment of some creditors but not others should be equally acceptable. However the first come first served policy of the common law has been rejected in favour of *pari passu* sharing in bankruptcy statutes and, in this country, in creditors' relief legislation. As a corollary, Canadian legislatures have passed Fraudulent Preference Acts, the purpose of which is to prohibit at least some preferential transfers, no matter how valid or meritorious the claim of the preferred creditor. The courts have however been more hesitant to strike down the preference of a legitimate creditor than they have a conveyance designed to defeat all creditors alike.

2. Fraudulent Conveyances

(a) INTRODUCTION

The present law of fraudulent conveyances is derived from the *Statute of Elizabeth*, 1570 (13 Eliz. 1, c. 5). The statute imposed criminal penalties on the guilty debtors, with jurisdiction in the Star Chamber, and also declared the transfers to be void.

The precursors of the Ontario *Fraudulent Conveyances Act* are 13 Eliz. 1, c. 5, which generally finds its counterpart in ss. 1-4 of the Ontario Act, and 27 Eliz. 1, c. 4, which dealt with conveyances in fraud of purchasers and which finds its counterpart in ss. 5-8 of the Act. This chapter deals only with transactions in fraud of creditors. With respect to the relationship between 13 Eliz. 1, c. 5, and the common law of England before its enactment, see *Kerr on Fraud and Mistake* (London: Sweet and Maxwell, 7th ed. 1952), at 299:

It has been frequently observed that 13 Eliz. 1, c. 5 was merely declaratory of what was previously the common law of the land. But it may well be doubted whether anything more was intended by these expressions than that "whatever offends against the order and good morals of society is an offence against the law of England, and punishable at common law"; and that "the law abhors covin, and therefore every covinous act shall be void." But be this as it may, the statute expressly laid down, and more clearly defined, the law on the subject; whereas the doctrine of the common law was so general as to be vague and difficult of application.

The most celebrated early application of the statute occurred in *Twyne's Case* (1602), 76 E.R. 809. In 1600, Pierce sold sheep to Twyne, who did not drive them away, as ordinarily he should have done. After some time had elapsed and Pierce had shorn the sheep and marked them as his own, a judgment creditor of Pierce attempted to have the sheep seized in execution. Twyne then appeared to block the seizure, asserting that the sheep were his. The court held that the conveyance had the signs and marks of fraud. The donor continued in possession and used the sheep as his own; he traded with others on these terms, with the result that he defrauded and deceived them. The transfer was made in secret, and it was made pending the writ; there was a trust between the parties, and trust is the cover of fraud. The report of the case concluded, at 814:

[A]nd therefore, reader, when any gift shall be to you in satisfaction of a debt, by one who is indebted to others also; 1st, Let it be made in a public manner, and before the neighbours, and not in private, for secrecy is a mark of fraud. 2nd, Let the goods and chattels be appraised by good people to the very value, and take a gift in particular in satisfaction of your debt. 3rd, Immediately after the gift, take the possession of them; for continuance of the possession in the donor, is a sign of trust.

And by the judgment of the whole Court Twyne was convicted of fraud, and he and all the others of a riot.

There has been no real suggestion that the enactment of the fraudulent conveyance legislation in statutes like the *Assignments and Preferences Act* has repealed, by implication, the *Statute of Elizabeth* or the *Fraudulent Conveyances Act*: see *Bank of Montreal v. Crowell* (1980), 37 N.S.R. (2d) 292 at 301 (N.S.S.C.). In Alberta, see the *Goyan* and *Semabliuk* cases, *supra*, as well as *T.D. Bank v. Michael*, [1973] 1 W.W.R. 656 (Alta. C.A.) and *Murdoch v. Murdoch* (1977), 1 Alta. L.R. (2d) 135 (Alta. T.D.).

A successful fraudulent conveyance action by one creditor will enure to the benefit of all creditors, in the sense that title to the exigible property "reverts" to the debtor and the property may then be seized and sold under a writ. The use of such an action to benefit all creditors is underscored, in part, by the fact that, at least where the plaintiff is not a judgment creditor, he must commence his action as a class action; he must sue on his own behalf, and on behalf of all other creditors, under the Ontario Rules of Civil Procedure, R.12.

See *Kroman's Electric Ltd. v. Schultes*, [1970] 2 O.R. 548 at 553 (Ont. H.C.), citing *Oliver v. McLaughlin* (1893), 24 O.R. 41 (Ont. C.A.); *Mitchell v. Jeffrey*, [1944] O.W.N. 540 at 542 (Ont. H.C.); and *Bell v. Williamson*, [1945] O.R. 484 at 492 (Ont. H.C.); affirmed [1945] O.R. 844 (Ont. C.A.). The *Schultes* case was followed in *Mazzo Bros. Ltd. v. Solomon* (1979), 32 C.B.R. (N.S.) 32On (Ont. H.C.).

Why should a non-judgment creditor (and not a judgment creditor) be required to commence a class action under R.12 if he is to obtain relief?

In its Report, Part IV, at 235-37, the Ontario Law Reform Commission reviewed the manner in which a voidable transaction proceeding must be instituted. (See, also, its

review in *Report on Class Actions* (1982), at 846-47, n. 89, reproduced in the Enforcement Report, at 235). The Commission quoted Mackenzie J. in *St. Gregor Mercantile Co. v. Halbach*, [1927] 1 D.L.R. 761 at 763 (Sask. K.B.), to the effect that the differences in procedure are largely historic, based on the pre-fusion jurisdiction of both law and equity. The Commission rejected the present anomalous rules and stated (at 236–37):

> The Commission has already noted that the existing law governing the institution of a voidable transaction suit in Ontario appears to be premised on jurisdictional matters formerly governing the courts in England that have nothing to do with the prevailing rules in Ontario. Moreover, as a matter of policy, we believe that it is anomalous for all *Assignments and Preferences Act* creditors to be required to bring their actions on behalf of all creditors, whereas *Fraudulent Conveyances Act* judgment creditors are given an option whether to do so or not. It is also anomalous, in our view, that under the *Fraudulent Conveyances Act*, non-judgment creditors must sue on behalf of all creditors, whereas judgment creditors are not so required.
>
> After careful consideration, the Commission has come to the conclusion, and accordingly recommends, that the present rules governing the institution of a fraudulent conveyance and fraudulent preference action should be abolished. Both judgment and non-judgment creditors should be entitled to commence an action to set aside a fraudulent conveyance or fraudulent preference either as individual plaintiffs or on behalf of all creditors. Where the action is commenced on behalf of all creditors, it should be required to be brought under the Commission's Draft *Class Actions Act* or, prior to the implementation of that Act, under Rule 75 of the Rules of Practice [see, now, Ontario Rules of Civil Procedure, R.12].
>
> We see no reason why, unlike other potential plaintiffs, persons intending to impeach an allegedly fraudulent transaction, and who do not purport to act on behalf of others, ought to be forced to invoke the prevailing class action procedure. The result of their individual action will not bind other creditors. As our *Report on Class Actions* makes clear, there are both advantages and disadvantages to proceeding under the [class action procedure]...The option to invoke the governing class action procedure or to proceed in an individual action should be left to the impeaching creditor.

In British Columbia, an "action" need not be instituted to set aside the impugned transaction. See ss. 9-12 of the *Fraudulent Preference Act*, R.S.B.C. 1979, c. 143. Rather, a creditor may apply to the Supreme Court to institute "show cause" proceedings against the debtor and transferee. The "proceedings may be brought either in a summary way or by the trial of an issue, or by inquiry before an officer of the court, or by an action or otherwise, as the court believes necessary or convenient..." (s. 10).

Section 2 of the Ontario *Fraudulent Conveyances Act* and s. 4(1) of the *Assignment and Preferences Act* use the term "void." However, it is clear that a transaction is only voidable as against creditors and is good as between the parties themselves. See *Donohoe v. Hull Brothers & Co.* (1895), 24 S.C.R. 683 (S.C.C.). The traditional view, therefore, is that title validly passes to the debtor's transferee prior to impeachment. However, it has been said that, under some circumstances in the bankruptcy context, fraudulently conveyed property never ceases to be property of the debtor within the meaning of the applicable provincial exemptions provisions: see *Holthuysen (Trustee of) v. Holthuysen* (1986), 49 Alta. L.R. (2d) 25 (Alta. C.A.), discussed *supra*, ch. 4, sec. 14(i)(v) and *infra*, ch. 14, sec. 2(b), commentary 14.16.

As indicated, after a successful action, title reverts to the debtor. In *Taylor v. Cummings* (1897), 27 S.C.R. 589 (S.C.C.), the Supreme Court of Canada stated that all the plaintiff could do was to "set aside the deed in question and thereby render the property covered by it available for execution or garnishment at the instance of judgment creditors" (592). The *Statute of Elizabeth* "avoids the deed, nothing more — it

leaves the creditor defeated or delayed to his ordinary remedies, execution, garnishment" (592). In *McGuire v. Ottawa Wine Vaults Co.* (1913), 48 S.C.R. 44 (S.C.C.), Anglin J. stated (at 56): "In actions such as this, the relief granted is properly confined to setting aside the impeached conveyance, thus removing it as an obstacle to the creditor's recovery under executions against their [*sic*] debtor."

For a different rule in the bankruptcy context, see s. 20 of the *Bankruptcy Act*, R.S.C. 1970, c. B-3, applied in *Re Whetstone* (1984), 12 D.L.R. (4th) 249 (Ont. S.C.), reproduced *infra*, Chapter 14, sec. 3(c).

After a successful voidable transactions proceeding, why should creditors be obliged to invoke ordinary enforcement proceedings against the property where the value of the property does not exceed the creditors' claims? Are not such proceedings a waste of time and money in these circumstances? What other remedy or remedies should be made available?

In British Columbia, s. 9 of the *Fraudulent Preference Act*, R.S.B.C. 1979, c. 143, entitles the creditor to apply to the Supreme Court, calling on the debtor and transferee to "show cause", *inter alia*, why the conveyance should not be set aside "and the property returned or otherwise dealt with as the court may direct." In *Bank of N.S. v. Brickell* (1980), 36 C.B.R. (N.S.) 1 (B.C.S.C.), the court concluded that the debtor-husband was the beneficial owner of a one-quarter share in land conveyed to his wife, and ordered that the wife should transfer back to the husband an undivided one-quarter interest in the land.

In *Bank of Montreal v. Cyr* (1985), 61 N.B.R. (2d) 283 (N.B.C.A.), the issue arose as to whether judgment in the fraudulent preference action should be granted to the creditor against the recipient of the fraudulent preference, or whether the impugned transactions should be declared void. The court decided in favour of the latter.

With respect to remedies generally, see B.C. Working Paper, at 66 *et seq.* It stated that in "British Columbia, the practice of asking the court to rescind the transaction and to order the reconveyance of the property and the rectification of land title office records, appears to be the remedy most often sought, and granted" where the transferee retains the property (at 66). "This practice may be questioned in logic and law," since the transferee's "title is absolute as against the fraudulent grantor" (at 70). Some courts have ordered that the transferee do all things necessary to make the property available to the transferor's creditors. As the Working Paper noted, the form of the order is important, since it affects the right to any surplus after sale of the property (at 72). With respect to enforcement against property in the transferee's hands, see 72-74. While legislation and rules are silent in B.C., it appears that the sheriff has jurisdiction to seize the property as though it were the debtor's. With respect to orders for sale of fraudulently conveyed property, see 74-75. A sale would not be ordered where the plaintiff was not a judgment creditor (at 75). Why not?

With respect to following property into the hands of a third party recipient from the original transferee, see 75-77. The Working Paper appears to deny the right to trace property (at 75). With respect to assets substituted for, or purchased with, the property received by the transferee, see 75. The creditor may recover the proceeds of a sale by the transferee: see s. 7 of the *Fraudulent Preference Act*. In the latter connection, the Working Paper noted that, since s. 7 is restricted to cases where the disposition is invalid as against a "creditor", it is unavailable to a person whose claim is not liqui-

dated. In this connection, note that the word "creditor" alone is also used in s. 12 of the Ontario *Assignments and Preferences Act*. Is the Working Paper's view of s. 7 accurate in light of the principle enunciated in *Westinghouse Can. Ltd. v. Buchar* (1975), 9 O.R. (2d) 137 (Ont. C.A.) reproduced *infra*, sec. 2(h), which held that s. 12 applies to transactions impugned under the *Fraudulent Conveyances Act* as well?

See B.C. Working Paper, at 134-37. A wider range of remedies was proposed, including reconveyance to the debtor, a declaration that the property is exigible in the transferee's hands, a sale of the property, and any other order for disposition of the property or any other direction as to how execution should proceed.

Unlike under the Ontario *Fraudulent Conveyances Act*, under s. 4(1) of the *Assignments and Preferences Act* an impeaching creditor must prove that, at the time of the transaction in question, the debtor was "in insolvent circumstances or [was] unable to pay his debts in full, or [knew] that he [was] on the eve of insolvency." In the Nova Scotia case of *Bank of Montreal v. Crowell* (1980), 37 N.S.R. (2d) 292 (N.S.T.D.), comparing 13 Eliz. 1, c. 5, with the Nova Scotia *Assignments and Preferences Act*, Hallett J. emphasized (at 298) that, under the former statute, "a conveyance made by a solvent person can be impeached..." If the debtor was solvent at the time of the transfer, and if he remained solvent immediately after, could the transfer of his property detrimentally affect his creditors? See *Crowell*, *supra*, at 302 *et seq*.

Concerning the definition of "insolvent circumstances" and "insolvency" in s. 4(1) of the *Assignments and Preferences Act*, see *Rae v. McDonald* (1886), 13 O.R. 35 (Ont. C.A.) *per* Rose J.

Should a future, contingent, or very uncertain liability — for example, an accommodation endorsement of a promissory note made years earlier — be taken into account in determining solvency at the time of the impeached transaction? See the conflicting views in *Union Bank v. Tyson* (1915), 7 W.W.R. 1117 at 1120 (B.C.S.C.); *Bertrand v. Cdn. Rubber Co.* (1897), 12 Man. R. 27 (Man. Q.B.); and *Traders Group Ltd. v. Mason* (1973), 43 D.L.R. (3d) 76 (N.S.T.D.); varied (1974), 53 D.L.R. (3d) 103 (N.S.C.A.). See also *Bank of Montreal v. Crowell* (1980), 37 N.S.R. (2d) 292 (N.S.T.D.). Exempt property is ignored when assessing solvency (see *McGuire v. Ottawa Wine Vaults Co.* (1913), 48 S.C.R. 44 at 54 (S.C.C.)), just as a transfer of exempt property cannot be impeached (*Loder v. Creighton* (1860), 9 U.C.C.P. 295).

The orthodox view that a conveyance of exempt property is not impeachable has been justified on the ground that, if no conveyance had been made, the debtor would have been entitled to claim an exemption for the property. The New Brunswick Report, at 136, stated that, "[s]ince such property is not subject to legal process to satisfy a creditor's claims, setting aside the transaction would serve no useful purpose." As a matter of law, is this view correct? As a matter of policy, should otherwise exempt property be immune when conveyed away? Prior to the conveyance, the property would be exempt only if it met the requirements of the exemption legislation. For example, under s. 2.3 of the Ontario *Execution Act*, R.S.O. 1980, c. 146, in order to qualify for the exemption the chattels must be "ordinarily used by the debtor in his business, profession or calling." What inference should the court draw from the fact that the debtor has conveyed away his tools?

Is it a valid argument to base the unimpeachability of the conveyance on the state of affairs *prior to* the conveyance? Does this immunity further the ostensible purpose

of exemption legislation, that is, to protect certain necessaries, including tools of the trade? With respect to the impeachment of exempt property transfers, see Ontario Law Reform Commission, Part IV at 237, where the Commission reaffirmed existing law and recommended that "the proposed legislation... should not invalidate or affect any transaction involving property exempt from enforcement measures." The New Brunswick Report recommended as follows (at 157):

> It is recommended that an express exemption from the legislation be made for any transaction in so far as it involves property which is exempt from execution, but that, where such a transaction would be voidable if the property were not exempt from execution, and to the extent that the consideration flowing to the debtor does not bear a fair and reasonable relative value to the consideration flowing from the debtor, any property transferred by the debtor be treated as remaining his property for the purpose of determining what property is exempt from execution and the debtor be treated as having selected such property to be exempt in any case where the debtor is entitled to select the property to be exempt.

With respect to the notion that the philosophy of exemptions legislation is to protect, *inter alia*, the tools necessary for a debtor to carry on his business, profession, or calling, see, for example, s. 4 of the Ontario *Execution Act*, which exempts the proceeds of the sale of exempt tools (under s. 3). Does s. 4 represent a movement away from the philosophy described above, so as to cast doubt on the argument that a creditor should be able to impeach a transaction involving otherwise exempt chattels? Or is the s. 4 proceeds exemption simply a necessary or desirable adjunct to the special cases described in s. 3? Note, however, that while the sale of a non-farmer's tools under s. 3(1) is not voluntary, the sale of a farmer's tools under s. 3(2) is, in fact, voluntary. In other words, with respect to the situation described in s. 3(2) and s. 4, the Legislature is clearly willing to countenance a debtor voluntarily giving up ostensibly necessary tools and then receiving an exemption for the proceeds. Is this situation akin to the main scenario to which reference is made in the two previous paragraphs? Note that Part II of the Ontario Law Reform Commission Report endorsed the proceeds exemption but only for a three month period, "so that the debtor may have the opportunity to purchase other exempt assets" (at 87). Note, too, that, with respect to the homestead proceeds exemption in the Western provinces, it has been held that the exemption is lost where the debtor "voluntarily" sells the property. It has been said that, by so doing, the debtor has converted exempt property into non-exempt property, in effect abandoning the exemption. Is the general philosophy behind these decisions germane to the question whether a debtor loses, or should lose, his exemption for tools fraudulently sold to defeat creditors?

For transfers and mortgages of exempt property, see, also, Dunlop, at 341-45. With respect to property that cannot be the subject of a fraudulent conveyance (exempt property and property held by the grantor as trustee), see B.C. Working Paper, at 153–54, *n*. 5.

Most courts favour an execution, or forced sale evaluation of the debtor's property: see *Re Butterworth* (1882), 19 Ch. D. 588 (C.A.); and *Dom. Bank v. Cowan* (1887), 14 O.R. 465 (Ont. H.C.). However, others have favoured a market value approach: see *Rae v. McDonald* (1887), 13 O.R. 352 (Ont. C.A.) *per* Rose J.

Section 12 of the *Assignments and Preferences Act*, R.S.O. 1980, c. 33, applies to transactions impugned under either that Act or the *Fraudulent Conveyances Act*: see *Westinghouse Canada Ltd. v. Buchar* (1975), 9 O.R. (2d) 137 (Ont. C.A.), reproduced *infra*, this Chapter, sec. 2(h).

With respect to criminal sanctions for fraudulently conveying property, see *Criminal Code*, R.S.C. 1970, c. C-34, s. 350. Section 350 has been interpreted narrowly. See *R. v. Crew* (1926), 46 C.C.C. 123 (Ont. C.A.), where it was held that it did not prohibit a preference. However, a debtor cannot defeat *all* of his creditors. Section 301 deals with fraudulent removal or concealment of assets.

(b) FRAUDULENT JUDGMENTS

In *Bank of Montreal v. Ewing* (1984), 55 C.B.R. (N.S.) 101 (Ont. S.C.) varied (1986), 59 C.B.R. (N.S.) 156 (Ont. C.A.), a father conveyed to his son a farm, the son giving a mortgage as consideration and agreeing to permit the father and mother to remain in the home rent-free. The father subsequently instituted foreclosure proceedings against the now insolvent son. No appearance was entered by the son and, accordingly, the father obtained a final order for foreclosure. The plaintiffs alleged that the son's conduct in failing to redeem was fraudulent, and that the father had knowledge of the son's fraudulent intent.

Fitzpatrick J. characterized the impugned transaction as a fraudulent "judgment" (as opposed to a fraudulent "conveyance", although the latter was not discussed) under s. 2 of the Ontario Act. He then went on to state that "[t]here appears to be no authority on the point and I find that it was [the father] who made the judgment for foreclosure as that word is meant" in s. 2. Fitzpatrick J. held that the father had no fraudulent intent and that the action should be dismissed.

Do you agree with the way in which the judge characterized and considered the transaction? Does the reference in the Act to a "judgment" mean, *inter alia*, that the debtor, in order to defraud his creditors, cannot effectively alienate his property by consenting to a judgment against him? While, in *Ewing*, it was the father who obtained an order for foreclosure, is it accurate to focus on the *father's* intent when determining intent under s. 2, as though he was the party whose creditors were affected? If the father's intent is not central to a consideration of intent under s. 2, is his lack of fraudulent intent relevant under the saving provision (s. 3)? Note that s. 3 appears to deal only with property "conveyed". Under what circumstances, if any, should the court set aside a judgment where the defendant-debtor's purpose in allowing the judgment to be obtained is fraudulent, but where the plaintiff's purpose is legitimate? Should the legislation apply only to judgments obtained in respect of sham debts, where there is collusion between the parties? For an example of the latter case, see *Commercial Bank v. Wilson* (1866), 14 Gr. 473 (U.C.C.A.).

Could the son's failure to redeem, if indeed fraudulent, be characterized as a "conveyance"? In this connection, it bears emphasizing that the courts have given a very broad meaning to that word in voidable transactions law. (Witness, for example, the treatment of the disclaimer in the *Sembaliuk* case, reproduced *infra*). If the transaction had been perceived as a conveyance by the son, would the result of the action have been any different?

See B.C. Working Paper, at 113: "Strictly speaking...no statutory authority is required to permit a collateral attack to be mounted on an order on the ground that it was procured by fraud." See also B.C. Working Paper, at 16.

(c) THE MEANING OF "CONVEYANCE"

SEMBALIUK v. SEMBALIUK

(1983), 27 Alta. L.R. (2d) 223, 35 R.F.L. (2d) 415 (Alta. Q.B.)

MILLER J.:

....

A third more vexing question is whether a disclaimer is covered by the provisions of s. 2 of 13 Eliz., which refers to "all and every Feoffment, Gift, Grant, Alienation, Bargain and Conveyance..."

In looking over the enumerated list of transactions mentioned in s. 2 it must be observed that a disclaimer is not one of those specifically mentioned. The only item which might cover a disclaimer would be the term "conveyance". Nowhere in 13 Eliz. is there a definition of what is encompassed by a "conveyance". However when one follows the history of 13 Eliz. in England, it is noted that it was repealed by the *Law of Property Act, 1925* (15 & 16 Geo. 5), c. 20. Specifically, s. 172 of the 1925 Imperial Act expresses in more modern language the main provisions of 13 Eliz. when it states:

> 172. — (1) Save as provided in this section, every conveyance of property, made whether before or after the commencement of this Act, with intent to defraud creditors, shall be voidable, at the instance of any person thereby prejudiced.
>
> (2) This section does not affect the operation of a disentailing assurance, or the law of bankruptcy for the time being in force.
>
> (3) This section does not extend to any estate or interest in property conveyed for valuable consideration and in good faith or upon good consideration and in good faith to any person not having, at the time of conveyance, notice of the intent to defraud creditors.

A further examination of the 1925 *Imperial Act* indicates that s. 205(1)(ii) specifically defines the term "conveyance" as follows:

> (ii) 'Conveyance' includes a mortgage, charge, lease, assent, vesting declaration, vesting instrument, *disclaimer*, release and every other assurance of property or of an interest therein by any instrument, except a will; 'convey' has a corresponding meaning; and 'disposition' includes a conveyance and also a devise, bequest or an appointment of property contained in a will; and 'dispose of' has a corresponding meaning. (The italics are mine.)

Thus, the 1925 *Imperial Act* would clearly authorize the setting aside of a disclaimer if it was a fraudulent conveyance. *Kerr on the Law of Fraud and Mistake*, 7th ed. (1952), comments on the re-enactment of 13 Eliz., c. 5 by the 1925 Imperial Act and it is stated at p. 304 that there is no reason to suppose that the new section is any narrower or broader than the old statute. To put the matter another way, it is clear that the statute 13 Eliz., c. 5, was received as law in Alberta while the *Law of Property Act, 1925*, was not. While Alberta did not receive a statutory definition of "conveyance" which included a "disclaimer", I hold that the *Law of Property Act, 1925*, did not change or broaden the definition of "conveyance" as that term is used in the statute 13 Eliz., c. 5, but merely made the definition more explicit.

I find that a disclaimer agreement, such as the one involved in this case, is covered by 13 Eliz., c. 5, in the province of Alberta and that it is open to this court to examine the transaction for the purpose of determining whether or not it was designed to defeat valid claims of Mr. Sembaliuk's "creditors or others".

Even if I am in error in arriving at my conclusion by the path already stated, there is another ground upon which I would be prepared to come to the same conclusion. In construing a statute the courts must have the right and, indeed the duty, to try and discern the intent of the legislative body that enacted the legislation. In attempting to understand the intent of 13 Eliz., c. 5, I am greatly assisted by the comments of the learned author May on *The Law of Fraudulent and Voluntary Conveyances* where he states at p. 4:

> ...the chief feature of the statutes of Elizabeth, which are couched in very general terms, so as to include, and allow their application by the Courts to, any fraudulent contrivances to which the fertility of man's imagination might have resorted, as a means of eluding a more precise and inflexible law. The statute 13 Eliz., c. 5, is expressed to be directed against fraudulent feoffments, & c., 'more commonly used and practiced in these days, than hath been seen or heard of heretofore'. So it has been since, and will ever be to the end of time; for fraud is infinite, and will always attempt to evade whatever is done for its suppression; to prune it back on one side is but to give it a stimulus to branch out with fresh vigour in another direction. But the simplicity of the enactment and — if the expression may be allowed — its expansiveness, have enabled the judges to bring within its scope, and extend its operations to, almost every kind of transaction resorted to by debtors to the prejudice of their creditors.
>
> "These statutes," said Lord Mansfield, C.J., "cannot receive too liberal a construction, or be too much extended, in suppression of fraud." [In *Cadogan v. Kennett* (1776), 2 Cowp. 432, 98 E.R. 1171]. So in *Twyne's Case* (1602), 3 Co. Rep. 82a, 76 E.R. 809, it was resolved that "because fraud and deceit abound in these days more than in former times, all statutes made against fraud should be liberally and beneficially expounded to suppress the fraud."

In *Kerr on the Law of Fraud and Mistake*, virtually identical comments are made about the broad scope intended by the statute 13 Eliz., c. 5 (at p. 300). While the provisions of the *Matrimonial Property Act* and the *Fraudulent Preferences Act* may not be broad enough to afford Mrs. Sembaliuk a remedy, it is clear to me that the provisions of the statute 13 Eliz., c. 5, ought to be read broadly enough so as to afford a remedy against all frauds committed against creditors and others, including those frauds executed by the use of disclaimers.

There is yet a third way of approaching the issue. As I understood the heart of Mr. Sembaliuk's legal argument, he contended that a disclaimer always operated to make a bequest void *ab initio* in all circumstances. If he is wrong in this assertion it is possible that his position is built on Alberta muskeg.

In 12 Hals. (4th) 550, para. 1371, it is stated that a person cannot "disclaim any state, interest, or right assured to him without his concurrence *if he is under some legal or equitable obligation to accept it*." (The italics are mine.) This proposition is supported by the decisions in *Re Cary-Elwes' Contract*, [1906] 2 Ch. 143 and *Bence v. Gilpin* (1868), L.R. 3 Exch. 76. In both of these cases, there was an express agreement to accept the property, and thus the parties could not later disclaim the property in breach of their agreements. However, it is submitted that the obligation to accept the property may arise by consent (as in a contract or trust deed), or it may be imposed by law. No matter the source of the obligation, if it exists, a party may not disclaim.

Mr. Sembaliuk cites a large number of cases to show that disclaimers invariably operate to void gifts *ab initio*. The better view is that stated in *Williams on Executors and Administrators*, 14th ed. (1960), vol. 2, at p. 761, where it is said that, "*Prima facie*, the disclaimer operates from the time of the testator's death and makes the gift void for certain purposes *ab initio*." That is, in the absence of any evidence to show that the disclaimer would be wrongful, the disclaimer will void the gift *ab initio*. In

none of these cases cited by Mr. Sembaliuk was there any hint of wrongfulness in the disclaiming of the property: i.e., it did not put the parties in breach of any legal or equitable obligations. For example, *Townson v. Tickell* [(1819), 106 E.R. 575], one of the devisees of a joint ownership of the reversionary interest in some land disclaimed his interest. In an action by the remaining devisee of the reversionary interest against the tenants, the court made a ruling as to the required form of a disclaimer. There was no suggestion that the disclaiming devisee was thereby avoiding his obligations to anyone. In *Wood v. M.N.R.* (1962), 64 D.T.C. 780, the devisee attempted to partially disclaim a gift so as to lessen his tax burden. The disclaimer was ruled invalid as it failed to disclaim the devisee's interest absolutely. But, generally speaking, a disclaimer made to avoid a more onerous tax position is not in any sense wrongful. In *Montreal Trust v. Matthews* [[1979] 3 W.W.R. 621 (B.C.S.C.)], the devisee (a private foundation) disclaimed a gift as the federal *Income Tax Act*, 1970–71–72 (Can.), c. 63, required them to do so. In *Re Paradise Motor Co.*, [1968] 1 W.L.R. 1125, [1968] 2 All E.R. 625 (C.A.), the donee of shares in a company disclaimed the same out of personal dislike of the donor, but the disclaimer did not put the disclaiming party in breach of his legal or equitable obligations. Much the same can be said for the cases *Re McFaden* [[1937] O.W.N. 404 (H.C.)] and *Re Metcalfe* [[1972] 3 O.R. 598 (H.C.)]. The basic point to be made here is that while disclaimers operate *prima facie* to void the gift *ab initio*, if the disclaiming party is under a legal or equitable obligation, either consensual or imposed by law, such that the disclaimer would put them in breach of their obligation, then the disclaimer does *not* void the gift *ab initio*. Rather, it ought to be treated as a conveyance (as that term is used in the statute 13 Eliz., c. 5) and found fraudulent and void.

There is no doubt in my mind that Mr. Sembaliuk has a legal obligation to support the children regardless of his unhappiness with his wife. By disclaiming his interest in his father's estate and relying upon the largesse of his uncle, George Mulek, he is, in [my] view, putting himself in breach of his legal obligations. Surely there could be no clearer case of a person who is under a legal or equitable obligation to accept his bequest and thereby enable himself to better fulfill his legal obligations to his children, not to mention his wife. If necessary, I would hold that the disclaimer agreement executed by Mr. Sembaliuk under these conditions did not void his interest in the estate *ab initio*. That being the case some title to the assets passed through his hands in the legal sense and any subsequent transfer or disposition of these assets by disclaimer would otherwise clearly be subject to the provisions of 13 Eliz., c. 5.

While I have not found any decided cases akin to the fact situation of the case at bar there are some analogous situations which are useful to examine.

In *Freeman v. Pope* (1870), 5 Ch. App. 538, a gift was made of the proceeds of a life insurance policy. This gift so denuded the donor's estate that on his death his assets were found to be insufficient to cover his debts. The court ruled that in the absence of any direct proof of intention, if a person owing debts makes a gift or conveyance without consideration such that the gift or conveyance so depletes the estate that the donor cannot pay his debts the necessary inference is that the gift was made with the intent to defraud creditors. In that decision, Lord Hatherley L.C. stated (at p. 540) that "persons must be just before they are generous, and that debts must be paid before gifts can be made".

In *Mackay v. Douglas* (1872), L.R. 14 Eq. 106, the donor made a voluntary settlement on the eve of entering into a risky business in which the donor would assume large liabilities. The settlement did not make the donor insolvent but the onus shifted to the donor to prove to the court that the settlement was made *bona fide* in the belief that he could still meet his liabilities. In *Murdoch v. Murdoch* [[1977] 1 W.W.R. 378 (Alta. T.D.)], the husband conveyed his property to his son for a price far below the market value. He did this, admittedly, to prevent his wife from making any claim on the land, as the two parties were in the middle of divorce proceedings at the time of the conveyance. Bowen J. found this to be direct evidence of fraudulent intent, and ordered, pursuant to the statute 13 Eliz., c. 5, that the conveyance be set aside and that title to the land be restored in the name of the husband.

In my view, the disclaimer agreement executed by Mr. Sembaliuk falls on the several grounds set out above and it should be declared to be null and void. In the result Mr. Sembaliuk is still at law a beneficiary of a one sixth interest in the estate of Metro Sembaliuk.

....

COMMENTARY

10.01. *Sembaliuk* was reversed on appeal: (1984), 15 D.L.R. (4th) 303 (Alta. C.A.) (leave to appeal to the Supreme Court of Canada refused: February 18, 1985). The court, referring to the lower court's reliance on *Halsbury's Laws of England*, stated that the "exception to the right to disclaim is founded upon the existence of a legal or equitable obligation to accept a conveyance of the property" (307). The "wife cannot point to any legal or equitable obligation of the husband to take the share in the father's estate" (307). Moreover, the court basically refused to import into Alberta the definition of "conveyance" under the *Law of Property Act, 1925*, c. 20 (U.K.). The court then concluded as follows (309-10):

> The gift to the husband was not a specific one. It was not ascertainable or indentifiable. If we return to the meaning of the word "conveyance" in the *Statute of Elizabeth* it can only mean that the debtor has made over property, a situation which does not apply here. There is no donee of a disclaimed gift in a real sense. The bequest lapses. It may go to the creditors or other claimants, it may go to other beneficiaries, or it may go to a residuary beneficiary.
>
> I am satisfied that a disclaimer, being an avoidance of a gift, is not a conveyance of the property comprised in that gift.

With respect to whether a release of an interest is a "conveyance", see, *e.g. C.I.B.C. v. Shapiro* (1985), 44 R.F.L. (2d) 47 at 54 (Ont. S.C.), where this conclusion was assumed, but expressly not decided.

For an argument that a renunciation of a testamentary benefit should not be regarded as a fraudulent conveyance, except "where it is reasonably certain that the debtor has manifested a prior acceptance", see Gamin, "Renunciation of Testamentary Benefit as Fraudulent Transfer" (1986), 37 Case W. Res. L. Rev. 148. The author saw renunciation as the debtor's denial of a benefit to himself, rather than a transfer of property, and endorsed the "ancient maxim against forcing property upon anyone". Gamin made much of the testator's intent to benefit the recipient and not the latter's creditors and appeared to assume that the right to renounce would be rendered nugatory if creditors could impeach the renunciation. Leaving aside the admittedly important question whether the debtor has a property interest to convey, is it at least arguable that the *right* to disclaim as a matter of *estate* law (strongly advocated by Gamin) is not in itself imperilled by legal consequences arising from *fraudulent conveyances* law?

See *e.g.*, Cal. Prob. Code §283 (West 1986) ("A disclaimer is not a fraudulent conveyance by the beneficiary...") and Fla. Stat. Ann. §732.801(6) (a) (West 1976), as am. by Laws 1977, c. 77–87, §15 ("The right to disclaim otherwise conferred by the section shall be barred if the beneficiary is insolvent at the time of the event giving rise to the right to disclaim...").

See B.C. Working Paper, at 111–12, where it was said that, while appointing property to a third party

or disclaiming property resembles a fraudulent conveyance, "refusing a gratuitous benefit is far removed from the evil that fraudulent conveyance legislation is aimed at" (at 112). Moreover, "the settlor or donor of property most frequently intends to benefit the recipient of property and not his creditors," so that deeming such actions to be fraudulent conveyances "will usually frustrate the settlor's [or donor's] intentions" (at 112). The tentative proposal was, therefore, to exclude such actions from the legislation. Why should the settlor's or donor's intentions be relevant?

The B.C. Working Paper, at 12 *et seq.*, stated that a "disposition of property" embraces "virtually any transaction relating to property involving some positive act by the debtor. The Act is less concerned with the nature of the transaction than with whether it was intended to, and does, prejudice creditors and others protected under the Act" (at 13).

(d) PROVING THE DEBTOR'S INTENT

(i) Introduction

While, in Ontario, the provisions of the *Fraudulent Conveyances Act* and s. 4(1) of the *Assignments and Preferences Act* appear straightforward (although sometimes duplicative and occasionally divergent, as between themselves), centuries of case law have introduced considerable complexity and ambiguity into this area of the law. For example, while it would appear that an impeaching creditor must prove, as a subjective matter, the requisite nefarious intent on the part of the fraudulent debtor, in practice this requirement has been watered down by the use of presumptions and inferences of such intent in many circumstances. Moreover, in almost all instances where a creditor has been successful, the actual *effect* of the transaction has been to prejudice creditors; the extent to which the statutory requirement to prove fraudulent intent is, in practice, a real obstacle may well be questioned. See, generally, B.C. Working Paper, at 26 *et seq.* It has been suggested that the debtor's fraudulent intent may be proved by using the deemed fraudulent intent provisions of another statute, for example, the various provincial *Bulk Sales Acts*. See Dunlop, at 525, *n.* 18, citing *Wiebe v. Holmes*, [1971] 4 W.W.R. 588 (Man. Q.B.) (dealing with the *Bulk Sales Act*, R.S.M, 1954, c. 30), and the New Brunswick Report, at 119-20. See also *infra*, sec. 7.

The case law has also introduced other complicating factors, relating, *inter alia*, to whether the transfer by the debtor was voluntary (that is, without consideration) or for "good" or "valuable" consideration. This factor in turn affects the question of whether the transferee's fraudulent intent must be proved.

(ii) Badges of Fraud

The difficulty in proving fraudulent intent has been offset by the existence of presumptions and inferences of fraud arising from the debtor's actions. In this connection, see *McGillan v. McGillan*, [1947] 4 D.L.R. 456 at 460 (N.B.C.A.), where Harrison J. stated that "[t]he Court is not interested in [the debtor's] mental processes, but in his intention as evidenced by his actions." The cases illustrate the problems the courts have had in dealing with the strict language of the legislation, since direct, subjective proof of fraudulent intent is rarely possible.

OWEN SOUND GENERAL AND MARINE HOSPITAL v. MANN

[1953] O.R. 643, [1953] 3 D.L.R. 417 (Ont. H.C.)

ANGER J.:—...Undue haste by the parties to a conveyance to assure a priority over creditors of the vendor, the fact that there is no immediate or early change of possession

following the conveyance, and the relationship between the parties, are all factors relevant to show an intent to defeat or defraud creditors: *Ferguson v. Lastewka, et al.*, [1946] O.R. 577, [1946] 4 D.L.R. 531 [reproduced *infra*, this Chapter, sec. 2(g)(ii)], in which LeBel J. reviewed the authorities.

....

SOLOMON v. SOLOMON

(1977), 16 O.R. (2d) 769, 79 D.L.R. (3d) 264 (Ont. H.C.)

KREVER J:—...The plaintiff and the defendant Solomon had been married to each other until December 14, 1970, when the marriage was dissolved by a decree absolute granted at trial by Mr. Justice Henderson who, at the same time, also ordered that the defendant Solomon pay the plaintiff maintenance for her and the two children of the marriage in the weekly sum of $65, of which $25 was in respect of her own maintenance. The defendant Solomon has failed to make any payments of maintenance since the beginning of April, 1971. During the subsistence of their marriage the plaintiff and the defendant Solomon had become the owners as joint tenants of the matrimonial home at 534 Scofield Ave., in the City of Windsor, the property in question in this action. After the commencement of partition proceedings, the plaintiff, on April 1, 1971, conveyed her interest in the property to the defendant Solomon and received from him upon doing so the sum of $11,310.59. This figure included the value of one-half of the parties' equity in the property. The plaintiff and the defendant Solomon had agreed on a valuation of the property, as of the date of closing, in the amount of $26,500, and there is no suggestion that this amount did not truly reflect the fair market value at that time. In addition to her share of the equity in the property the plaintiff also received upon closing $1,000 as "Part Payment of Arrears of Interim and Permanent Maintenance," as well as the taxed costs of the divorce action and the costs of the partition proceedings. The funds from which the plaintiff received this money were obtained by the defendant Solomon by means of a loan of $11,500 from the defendant Krawec which was secured by a mortgage in that amount from the defendant Solomon to the defendant Krawec and registered on April 5, 1971. The defendant Krawec was aware that the purpose of the proceeds of the mortgage was "to pay her [the plaintiff's] share of the money and whatever else was owed". At the time the proceeds were advanced to the defendant Solomon the defendant Krawec knew he had been divorced and there was an understanding, but no formal agreement, between the defendants that the defendant Krawec would purchase the property from the defendant Solomon.

In June, 1970, the defendant Krawec had submitted to the plaintiff and the defendant Solomon a standard-form written offer to purchase the property for the sum of $26,500 of which $18,500 was to be cash and the balance of approximately $8,000 was to be by way of the assumption of the existing mortgage in that amount. That offer was accepted in writing by the defendant Solomon but, as it was not accepted by the plaintiff, the sale did not take place. On April 21, 1971, the defendant Solomon was in arrears in respect of his obligation to pay maintenance to the plaintiff, an order dated December 14, 1970, possibly the decree absolute of divorce although this is far from clear, was on title, having been registered against the property on April 2, 1971, and a writ of *fieri facias* against the defendant Solomon, in which the plaintiff was the execu-

tion creditor, had been lodged with the Sheriff of the County of Essex. On the same date the defendant Solomon was also indebted to other creditors.

April 21, 1971, was the date on which the defendant Solomon conveyed the subject property to the defendant Krawec. The deed was dated, executed, and registered on that date...[The solicitor] was not instructed to, and did not in fact, search the title or search executions before the deed was registered. Had the title been searched it would have revealed that an order made in a matter between the plaintiff and the defendant Solomon and dated December 14, 1970, had been registered against the property on April 2, 1971. Had a search of executions in the Sheriff's office been made before the registration of the deed on April 21, 1971, it would have revealed the plaintiff's writ of *fieri facias* which had been filed with the Sheriff on January 20, 1971. There was no evidence at trial as to the nature of the order registered on title, dated December 14, 1970, and registered April 2, 1971.

....

In the transaction between the defendants the purchase price of $27,500 was shown in the land transfer tax affidavit as consisting of securities transferred to the value of $11,975 (of which, I find, $11,500 was represented by the previously mentioned mortgage which merged with the deed), balances of existing encumbrances with interest at the date of transfer in the sum of $7,500 and "monies secured by mortgage under this transaction," in the sum of $8,025. A mortgage for $8,025 from the defendant Krawec to the defendant Solomon was dated, executed, and registered on April 21, 1971. That mortgage was discharged within less than two months by a discharge of mortgage from the defendant Solomon to the defendant Krawec dated June 8, 1971, and registered June 10, 1971. The evidence led by the plaintiff in respect of this discharge is that the discharge, filed as ex. 2 at trial, is in the usual form, recites that the defendant Krawec had satisfied all money due on the mortgage and that, although no money passed through the hands of the defendant Krawec's solicitor who prepared the discharge and saw to its execution, the defendant Krawec satisfied the money due under the mortgage by the payment of cash to the defendant Solomon. On the basis of this uncontradicted evidence, I find as a fact that the money due under the mortgage was actually paid. The money secured under the mortgage had been payable in equal monthly instalments of $120, including interest at 6% per annum until the whole of the principle sum was fully paid.

The defendant Solomon suffered a disabling injury in November, 1970, and has been unable to work since that time. In 1971, he owned a car which he had purchased new in 1969 or 1970, and had financed through his bank. In 1970, while he was in the Workmen's Compensation Hospital in Toronto, he became unable to keep up his payment to the bank in respect of the loan obtained to acquire the car. He thereupon sold the car to the defendant Krawec for $300 cash and the assumption by her of the outstanding indebtedness. He also sold to her his damaged aluminum boat and his tools. I infer from the evidence that the tools referred to were not the tools which he had used when he worked as a plumber, but rather the usual tools associated with home ownership. The defendant Krawec therefore became the owner, for value, of the assets of the defendant Solomon who, for all practical purposes, being without assets and employment, is judgment proof.

The defendant Krawec moved into the subject property upon the completion of the transaction between her and the defendant Solomon by which she become the owner. The defendant Solomon, however, did not thereupon vacate the premises, but remained in them as a roomer for as long as the defendant Krawec remained the owner. By a deed dated September 23, 1973, and registered November 14, 1973, the defendant Krawec conveyed the subject property to two *bona fide* purchasers for value, without notice, who are not parties to this action. At the time of the delivery of possession to these purchasers, the defendant Solomon was in hospital but when he was released he moved into the defendant Krawec's new home, again as a roomer. The evidence indicates that, with respect to the subject property and the defendant Krawec's new home, the relationship between the defendant Krawec and the defendant Solomon was that of landlady and roomer respectively... .

Having found that the conveyance from the defendant Solomon to the defendant Krawec was for valuable consideration and was not a voluntary conveyance, I must be concerned with the determination of the question whether the defendant Krawec shared or knew of the defendant Solomon's intent to defeat, hinder, delay or defraud his creditors at the time he conveyed the property. For the purposes of this determination, I am prepared to assume, as against the defendant Krawec, that, despite the minimal weight of the evidence on the point, the defendant Solomon, himself, had that intention. In the circumstances of this case, the burden of proving the necessary state of mind on the part of the defendant Krawec is on the plaintiff. I accept, as a sound starting point, the proposition put by Middleton, J.A., in *Shephard v. Shephard* (1925), 56 O.L.R. 555 at p. 558, [1925] 2 D.L.R. 897 at pp. 899-900:

> The learned trial Judge has, I think, rightly adopted the principle...that where once the Court is convinced of the actuality of the transaction, and that valuable consideration has been given, the plaintiff cannot succeed without actually proving an intention to defraud creditors of the grantor; and this, it appears to me must be based upon something far beyond mere suspicion. Suspicion will not shift the onus in a case of this kind.

....

There is, as I have indicated, no direct evidence that the defendant Krawec was privy to the defendant Solomon's intent to defraud the plaintiff. Any finding to that effect that is to be made must rest, therefore, on circumstantial evidence. Circumstances that are merely suspicious are not sufficient. But all the circumstances surrounding the conveyance of the property must be examined to determine if there are among them some which have been termed "badges of fraud".

In *Bank of Montreal v. Vandine et al.*, [1953] 1 D.L.R. 456, 33 M.P.R. 368, the Appeal Division of the Supreme Court of New Brunswick affirmed the judgment of Harrison, J., who listed the following features of transactions alleged to be made with fraudulent intent as badges of fraud:

(1) Secrecy
(2) Generality of Conveyances, by which is meant the inclusion of all or substantially all of the debtor's assets
(3) Continuance in possession by debtor
(4) Some benefit retained under the settlement to the settlor.

He included as minor badges of fraud:

(5) Gross excess of value of property over price paid and
(6) Cash taken in payment instead of a cheque.

In *Ferguson v. Lastewka et al.*, [1946] O.R. 577, [1946] 4 D.L.R. 531, LeBel, J., looked upon the following circumstances as supporting an inference of fraud on the part of the grantee:
(1) Knowledge of the likelihood of a successful action by the plaintiff against the grantor
(2) Unusual haste in closing
(3) No immediate or early change of possession following the conveyance, adding that "joint possession raised a presumption of fraud,"
(4) The relationship between the parties to the conveyance.

In *Royal Bank of Canda v. Sullivan and Herr*, [1957] O.W.N. 68 at p. 72, 6 D.L.R. (2d) 559 at p. 567 [affirmed [1957] O.W.N. 520, 10 D.L.R. (2d) 494], Thompson, J., held to be badges of fraud secrecy in the transaction and feverish haste to register the mortgage, the conveyance sought to be set aside, on the eve of the plaintiff's judgment. In an earlier case, *Kvasnedsky v. Birnbaum* (1923), 25 O.W.N. 29, Orde, J., held that knowledge on the part of the grantee of the grantor's insolvent circumstances, though by itself insufficient to impute to the grantee knowledge of the grantor's intent to defraud his creditors, was an important circumstance if there were other grounds for suspicion. On the facts of the case before him, he found other grounds in the grantor's remaining in possession, which tended to delay the discovery of the sale, and the absence of any certificate as to title, or as to arrears of taxes or as to executions in the Sheriff's hands.

It is apparent from a survey of the decisions that each case must turn on its own special facts. The special facts of this case, when examined carefully, do not, in my opinion, lead one to the conclusion that the defendant Krawec had knowledge, at the material time, of the defendant Solomon's intent in conveying the property. Neither secrecy nor undue haste has been shown. The speed with which the mortgage given back on closing was discharged has given rise to some suspicion in my mind but I am unable to put it any higher than that. The property was sold at what must, on any reasonable view, be considered its fair market value, and the continued residence of the defendant Solomon in the premises as a *bona fide* roomer has been satisfactorily proved. The transfer by the defendant Solomon of his assets — his damaged boat, his car and his household tools — to the defendant Krawec seems to me to have no significance. On the evidence, the transfer of these items of personal property, and, indeed, the impugned transaction itself, seem to me to be equally consistent with an expectation on the part of the defendant Krawec that the receipt by the defendant Solomon of the proceeds would enable him to discharge his obligations as with any other conclusion. As I have shown, the evidence adduced by the plaintiff was that the defendant Krawec believed that the purpose of the proceeds of the mortgage given before the sale in question was to enable the defendant Solomon to pay the plaintiff "her share of the money and whatever else was owed". There was no evidence that the defendant Krawec knew that the plaintiff had a judgment against the defendant Solomon for maintenance. Even if the defendant Krawec had that knowledge, it would not support a conclusion that she therefore knew of the defendant Solomon's intent. The following language of Orde, J.,

in *Kvasnedsky v. Birnbaum, supra*, seems to me to be apposite [p.30]:

> It does not necessarily follow, however, that knowledge on the part of the intending purchaser of the vendor's insolvency imputes to the purchaser knowledge of the vendor's intent to defraud his creditors, and it is incumbent upon the plaintiff to bring home to the purchaser knowledge of that intent in order to impeach, under the statute of Elizabeth, a conveyance made upon a valuable consideration: *Hickerson v. Parrington* (1891), 18 A.R. 635. There is no law to prevent one who is insolvent from disposing of his property. He may be doing so in good faith and for the purpose of realising the moneys with which to pay his creditors. So that a purchaser for value is not, merely because of his knowledge of the vendor's insolvency, to be presumed to have knowledge of a fraudulent intent which may not in fact exist.

Since knowledge of a grantor's insolvency or indebtedness does not cause a grantee to cease to be an innocent purchaser for value without notice of the grantor's fraudulent intent, I am unable to find significant the defendant Krawec's failure to instruct her solicitor to search the title to the property or to search executions in the Sheriff's office. At most those searches would have revealed, as previously indicated, that an order, the nature of which is not shown by the evidence, in a matter between the plaintiff and the defendant Solomon, dated December 14, 1970, had been registered April 2, 1971, and that a writ of *fieri facias* had been filed with the Sheriff on January 20, 1971, or, more simply, that the plaintiff was an execution creditor of the defendant Solomon. Knowledge of that kind does not invest the defendant Krawec with knowledge of the defendant Solomon's intent.

To sum up, after a consideration of all the circumstances surrounding the transaction between the two defendants, I am unable to conclude that the plaintiff has proved that the defendant Krawec was privy to the defendant Solomon's intent to defeat, hinder, delay or defraud the plaintiff. I am, of course, suspicious, but I am obliged to act on the evidence and, again, suspicion is not enough.

....

COMMENTARY

10.02. See *Kapicki v. Andriuk*, [1975] 2 W.W.R. 332 (Alta. Dist. Ct.). In some circumstances, courts have simply said that suspicious circumstances surrounding a conveyance call for some explanation by the debtor: see *Bank of Montreal v. Crowell* (1980), 37 N.S.R. (2d) 292 (N.S.S.C.).

10.03. See B.C. Working Paper, at 27-29, which lists twenty badges of fraud. With respect to the effect of establishing a badge of fraud, see B.C. Working Paper, at 28-29:

> There are two views on the effect of establishing a badge of fraud. The first is that proof of a badge of fraud is sufficient evidence of fraud to entitle the court to find that the plaintiff has made a case suitable for hearing by a trier of fact. The second view is that once a badge of fraud is established, the onus shifts to the defendant to establish that the transaction was not made with any fraudulent intent. On the first view, the court would not be obliged to avoid a transaction if the evidence is equivocal. Not all badges of fraud are clear and unambiguous, and the weight of the inference to be drawn will vary from case to case. On the second approach, however, the defendant's failure to rebut the inference or adduce positive evidence of a lawful intent will cause judgment to be issued against him. Doubts would be resolved in favour of the plaintiff. Both approaches find support in case law.

The Working Paper doubted whether the notion of a shifting burden of proof serves any useful purpose. "The concept of badges of fraud does little more than acknowledge the value of circumstantial

evidence. We see no reason to forbid reliance upon circumstantial evidence when the intent of the recipient of property is in issue" (at 124).

(iii) Presumptions Arising from the Natural Consequences of the Transaction

As indicated earlier, the nature of the requirement to prove the requisite intent varies, depending upon whether the transfer is made with or without consideration. Where no consideration is present, only the intent of the debtor need be proved: see *Oliver v. McLaughlin* (1893), 24 O.R. 41 (Ont. C.A.). In this situation, however, the cases have been either conflicting or ambiguous concerning precisely what the creditor must show. In some cases, it has been said that where a debtor was insolvent at the time of the transaction or was rendered insolvent as a result of it, and where the transaction involved no, or only nominal, consideration, an irrebuttable presumption of fraudulent intent arises. In *Sun Life Assurance Co. v. Elliot* (1900), 31 S.C.R. 91 at 94 (S.C.C.) Sedgewick J. stated:

> [The trial Judge] appeared to have lost sight of the principle that where at any time a person is solvent and then makes a voluntary conveyance the effect of which is to make him insolvent, the settlement is void and that too, no matter what the intent of the settlor.

The *Sun Life* case was applied in *Atlantic Acceptance Corp. v. Distributors Acceptance Corp.*, [1963] 2 O.R. 18 (Ont. H.C.). See also Scane, "Fraudulent Conveyances" (1964), 3 Western Ont. L. Rev. 40, and *Bank of Montreal v. Pelletier*, [1923] 3 W.W.R. 735 (Alta. C.A.). But see *Royal Bank of Can. v. First Pioneer Investments Ltd.* (1979), 27 O.R. (2d) 352 (Ont. H.C.); appeal dismissed (1981), 32 O.R. (2d) 121 (Ont. C.A.), where, in the lower court, the *Sun Life* case was said to have involved a rebuttable presumption (27 O.R. (2d) at 356 *et seq.*).

Earlier case law, following *Freeman v. Pope* (1870), L.R. 5 Ch. App. 538 (reproduced *infra*) held that, where the effect of the transaction was to prejudice creditors, fraudulent intent would be conclusively presumed. However, more modern authorities (for example, following *Ex parte Mercer* (1886), 17 Q.B.D. 290 (C.A.), reproduced *infra*) have endorsed only a rebuttable presumption under these circumstances.

FREEMAN v. POPE

(1870), L.R. 5 Ch. App. 538

LORD HATHERLEY L.C.:—The principle on which the statute of 13 Eliz., c. 5 proceeds is this, that persons must be just before they are generous, and that debts must be paid before gifts can be made.

The difficulty the Vice-Chancellor seems to have felt in this case was, that if he, as a special juryman, had been asked whether there was actually any intention on the part of the settlor in this case to defeat, hinder, or delay his creditors, he should have come to the conclusion that he had no such intention. With great deference to the view of the Vice-Chancellor, and with all the respect which I most unfeignedly entertain for his judgment, it appears to me that this does not put the question exactly on the right ground; for it would never be left to a special jury to find, *simpliciter*, whether the settlor intended to defeat, hinder, or delay his creditors, without a direction from the Judge that if the necessary effect of the instrument was to defeat, hinder, or delay the

creditors, that necessary effect was to be considered as evidencing an intention to do so. A jury would undoubtedly be so directed, lest they should fall into the error of speculating as to what was actually passing in the mind of the settlor, which can hardly ever be satisfactorily ascertained, instead of judging of his intention by the necessary consequences of his act, which consequences can always be estimated from the facts of the case. Of course there may be cases — of which *Spirett v. Willows* [3 D.J.& S. 293] is an instance — in which there is direct and positive evidence of an intention to defraud, independently of the consequences which may have followed, or which might have been expccted to follow, from the act. In *Spirett v. Willows* the settlor, being solvent at the time, but having contracted a considerable debt, which would fall due in the course of a few weeks, made a voluntary settlement by which he withdrew a large portion of his property from the payment of debts, after which he collected the rest of his assets and (apparently in the most reckless and profligate manner) spent them, thus depriving the expectant creditor of the means of being paid. In that case there was clear and plain evidence of an actual intention to defeat creditors. But it is established by the authorities that in the absence of any such direct proof of intention, if a person owing debts makes a settlement which subtracts from the property which is the proper fund for the payment of those debts, an amount without which the debts cannot be paid, then, since it is the necessary consequence of the settlement (supposing it effectual) that some creditors must remain unpaid, it would be the duty of the Judge to direct the jury that they must infer the intent of the settlor to have been to defeat or delay his creditors, and that the case is within the statute.

The circumstances of the present case are these: The settlor was pressed by his creditors on the 3rd of March, 1863. He was a clergyman with a very good income, but a life income only. He had a life-annuity of between £180 and £190 a year, and besides that he had an income from his benefice — his income from the two sources amounting to about £1000 a year. But at the same time his creditors were pressing him, and he had to borrow from Mrs. *Walpole*, who lived with him as his housekeeper, a sum of £350 wherewith to pay the pressing creditors. That accordingly was done, and he handed over to her as security the only property he had in the world beyond his life income and the policy which is now in question, namely, his furniture, and a copyhold of trifling value. It is said, however, that the value of the furniture exceeded (and I will take it to be so) by about £200 the value of the debt which was secured to Mrs. *Walpole*. That debt may be put out of consideration, not only on that account, but because Mrs. *Walpole*, being herself a trustee of the settlement which is impeached, cannot be heard to complain of that settlement. But he also owed at the time of this pressure a debt of £339 to his bankers at *Norwich*, and he required, for the purpose of clearing the pressing demands upon him, not only the sum which he borrowed from Mrs. *Walpole*, but an additional sum of £150, which sum the bankers agreed to furnish, making their debt altogether, at the date of the execution of this settlement, a debt of £489. They made with him an arrangement (which probably was intended, in a great measure, as a friendly act towards a gentleman who was seventy-three years of age, and the duration of whose life, therefore, could not be expected to be very long), that they would for the present (for it cannot be held to be more than a present arrangement) suspend the proceedings, which, it appears, they were contemplating, upon his allowing his solicitor to receive part of his income, pay £100 a year towards liquidating the £489 (which

was to be carried to what is called a "dead account"), and pay the residue into their branch bank at *Aylsham*, to an account upon which the settlor might draw. That arrangement was made, but there was no bargain on the part of the bankers that they would not sue at any time they thought fit; and, on the other hand, they had nothing in the shape of security for the payment of their debt, for they had not taken out sequestration, and there could be nothing in the shape of a charge upon the living except through the medium of a sequestration. When the settlor had made the voluntary assignment of the policy, he stood in this position, that he had literally nothing wherewithal to pay or to give security for the debt of £489, except the surplus value of the furniture, which must be taken to be worth about £200, and he was clearly and completely insolvent the moment he had executed the settlement, even if we assume that some portion of his tithes and of the annuity was due to him. It appears that a payment of the tithes was made in January, and we cannot suppose that there was more owing to him than the £200 which was paid in May, two months after the date of the deed; and if we add to that £200 as the surplus value of the furniture, and add something for an apportioned part of the annuity, the whole put together would not meet £489. He, in truth, was at that time insolvent; and there I put it more favourably than I ought to put it, because he could not at once put his hands upon that sum, so as to apply it towards satisfying the debt, at any time between March and May. The case, therefore, is one of those where an intention to delay creditors is to be assumed from the act.

....

It seems to me that the difficulty felt by the Vice-Chancellor arose from his thinking that it was necessary to prove an actual intention to delay creditors, where the facts are such as to shew that the necessary consequence of what was done was to delay them. If we had to decide the question of actual intention, probably we might conclude that the settlor, when he made the settlement, was not thinking about his creditors at all, but was only thinking of the lady whom he wished to benefit; and that his whole mind being given up to considerations of generosity and kindness towards her, he forgot that his creditors had higher claims upon him, and he provided for her without providing for them. It makes no difference that Messrs. *Gurney*, the bankers, seem to have been willing to forego the immediate payment of their debt; the question is, whether they could not within a month or less after the execution of the settlement, if they had been so minded, have called in the debt and overturned the settlement? Beyond all doubt they could, on the ground that it did not leave sufficient property to pay their debt; and this being so, we are not to speculate about what was actually passing in his mind. I am quite willing to believe that he had no deliberate intention of depriving his creditors of a fund to which they were entitled, but he did an act which, in point of fact, withdrew that fund from them, and dealt with it by way of bounty. That being so, I come to the conclusion that the decree of the learned Vice-Chancellor is right.

[The concurring judgment of Sir G.M. Giffard L.J. is omitted.]

COMMENTARY

10.04. The proposition that fraudulent intent may be conclusively presumed where the effect of the transaction is to prejudice creditors has also been stated in, *e.g.*, the following cases: *Jeffrey v. Aagaard*,

[1922] 2 W.W.R. 1201 (Man. C.A.); *Bludoff v. Osachoff*, [1928] 3 D.L.R. 179 (Sask. C.A.), citing *Smith v. Cherrill* (1867), L.R. 4 Eq. 390; *Cromwell v. Comeau* (1957), 8 D.L.R. (2d) 676 at 684 (N.B.S.C.) *per* Doull J. dissenting; *Rimco Ltd. v. Leon Devs. Ltd.* (1971), 4 N.S.R. (2d) 592 (N.S.S.C.); *Traders Group Ltd. v. Mason* (1973), 43 D.L.R. (3d) 76 at 87 (N.S.S.C.); varied (1974), 53 D.L.R. (3d) 103 (N.S.C.A.); and *Bank of Montreal v. Crowell* (1980), 37 N.S.R. (2d) 292 (N.S.S.C.). In the *Crowell* case, Hallett J. stated at 305-6:

> As to his intention to defeat his creditors, I am satisfied that on the authority of *Freeman v. Pope*, approved in *Sun Life v. Elliott* and consistently followed by the Courts, that even if there was no direct proof of intention to defeat creditors, that by reason of Arthur E. Crowell's act of having settled property on his wife without valuable consideration (thus denuding himself of the property which was a proper fund for the payment of his indebtedness to the plaintiff so that he cannot pay his debt to the plaintiff), I must infer his intention to defeat or delay the plaintiff. Accordingly, the *Statute of Elizabeth* must apply and the conveyance held void as against creditors as being made with the intention to defeat his creditor, the plaintiff. I find that the effect of the transfer could have been expected by Arthur E. Crowell to defeat the plaintiff's claim and, in fact, has to this point in time defeated and delayed the plaintiff's attempts to collect the account. On these facts, fraudulent intention can be attributed to Arthur E. Crowell (*The Royal Bank of Canada v. Kirkpatrick* (1975), 20 N.S.R. (2d) 458; 27 A.P.R. 458, at p. 468).
>
> In summary, having denuded himself of his property by a conveyance for which he received no valuable consideration, the effect of which was to delay and defeat the claim of the plaintiff creditor, fraudulent intention is imputed... .

10.05. See B.C. Working Paper: "A disposition of property will not qualify as a fraudulent conveyance unless it was made with the intent to, *and has the effect of*," delaying, etc. creditors (at 14; emphasis added). A conveyance will have this effect where the consideration given for it "represents less than the full value of the property," "consists of payments over a period of time," "consists of payments deferred to a particular time," or "is non-exigible or difficult to attach" (at 14). See, also *ibid.*, at 17.

10.06. Parallel to the line of cases following *Freeman v. Pope* has been a line of cases endorsing the less sweeping views expressed in *Ex parte Mercer.*

EX PARTE MERCER

(1886), 17 Q.B.D. 290 (C.A.)

LORD ESHER M.R.:—I think the decision of the Divisional Court was right.

The argument was first put in this way — it is necessary to prove that the bankrupt, at the date of the voluntary settlement, intended to defeat and delay a creditor or his creditors generally; the necessary consequence of what he did was to defeat and delay his creditors; and, therefore, as a proposition of law, the tribunal which had to consider whether he did intend to defeat and delay his creditors was bound to find that he did. In support of that proposition dicta of great and eminent judges were cited. I will venture to say as strongly as I can that to my mind that proposition is monstrous. It is said that it is a necessary inference that a man intends the natural and necessary result of his act. If you want to find out the intention in a man's mind, of course you cannot look into his mind, but, if circumstances are proved from which you believe that he had a particular intention, you infer as a matter of fact that he had that intention. No doubt, in coming to a particular conclusion as to the intention in a man's mind, you should take into account the necessary result of the acts which he has done. I do not use the words "necessary result" metaphysically, but in their ordinary business sense, and of course, if there was nothing to the contrary, you would come to the conclusion that the man did intend the necessary result of his acts. But, if other circumstances make you

believe that the man did not intend to do that which you are asked to find that he did intend, to say that, because that was the necessary result of what he did, you must find, contrary to the other evidence, that he did actually intend to do it, is to ask one to find that to be a fact which one really believes to be untrue in fact. Whether the fact that the necessary effect of a voluntary deed is to defeat or delay the creditors of the grantor will make the deed void under the *Statute of Elizabeth*, although there was no such intent in his mind at the time when he executed it, is a question which we are not now called upon to decide. But that is a question wholly independent of the question of intention. That may be the law; the Courts may have put that construction on the statute. But that is a different proposition from that which was put forward in argument, and I will not undertake to decide it now. It must be recollected that the *Statute of Elizabeth* applies, and may make a deed void, even though the grantor never becomes a bankrupt. But this case was at first argued, not upon that footing, but upon the assumption that, if the natural or necessary effect of what the settlor did was to defeat or delay his creditors, the Court must find that he actually had that intent. That proposition or doctrine I entirely abjure.

We must look at all the facts of this case. The bankrupt was a captain of a merchant ship, and there is no evidence whether his employment ceased at the end of every voyage, or whether it was a constant employment. He had promised to marry Miss Vyse. Then he went to Hong Kong, and there he married another lady, and so laid himself open to an action for breach of promise of marriage by Miss Vyse. That action having been brought, might, so far as any one could foretell, have resulted in a verdict either for 1*s*. or for 500*l*. damages; no one could tell what the result would be. Well, he married the lady in Hong Kong in May, and in October there came out to him, by the same post from England, the information that he had become entitled to a legacy of 500*l*., and also the information that Miss Vyse had brought an action against him for breach of promise of marriage. This was the first time that he had had any intimation of the fact that he had any realized fortune, and he immediately settled the 500*l*. upon his wife and children.

Now, what was his position at that time? According to his evidence, which is not disputed, (for he has not been cross-examined on his affidavit), he did not owe a shilling in the world. There is no evidence that he had not money owing to him for wages, and in all probability he had, because, if his voyage did not terminate at Hong Kong (and there is no evidence that it did), if he had got to take his ship home to England, in all probability his wages were not payable until the end of the voyage. If so, he would have means to that extent, and he did not owe a shilling.

Now with regard to the action, how could any one — how could his legal adviser — have told him what the amount of the verdict was likely to be? If the verdict had been for 50*l*., and he had had 50*l*. coming to him at the end of his voyage, he would have been able to pay it, and on another occasion he would have been able to pay the costs. It was entirely a matter of speculation what the amount of the verdict would be. Therefore he was not insolvent; it was not the necessary consequence of what he did to defeat or delay the plaintiff in the action, for, if the verdict had been for a small amount, she would not necessarily have been delayed for a week.

In order to make this deed void under the *Statute of Elizabeth* (however far that statute may be stretched), we are bound in the present case to find that there was an

actual intent in the bankrupt's mind to defeat or delay his creditors, and there is no evidence of such an intent. He has sworn that he was not thinking of his creditors. The only creditor, that it is suggested he had to think about, was Miss Vyse, and no one could tell what the verdict in her action would be. But what happened afterwards? It is obvious that, when the action came on for trial, evidence must have been given about this 500*l*. legacy to which the defendant was entitled, and the jury took the vindictive view of the plaintiff, and gave her as damages the whole of the defendant's realized property. It was a startling verdict, which I certainly should not have anticipated, and I do not see why he was bound to anticipate it. When you have got those facts, and you are asked to conclude that the bankrupt actually intended to defeat Miss Vyse's claim, it seems to me that the Divisional Court were perfectly justified in declining to find that he had any such intent. Upon the facts, I cannot find that there was such an intent.

The appeal must be dismissed.

[The concurring judgments of Lindley and Lopes L.JJ. are omitted.]

MANDRYK v. MERKO

[1971] 2 W.W.R. 542, 19 D.L.R. (3d) 238 (Man. C.A.)

FREEDMAN J.A.:—The action giving rise to this appeal was one to set aside certain conveyances of land made by the defendant Nicholas Merko on the ground that they were made with intent to defeat, hinder, delay, or defraud his creditors. It is claimed that these conveyances were null and void as against the plaintiff by virtue of the provisions of s. 3 of *The Fraudulent Conveyances Act*, R.S.M. 1954, c. 91, which reads as follows:

> 3. Every conveyance of real property or personal property and every bond, suit, judgment and execution at any time had or made or at any time hereafter to be had or made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures shall be null and void as against such persons and their assigns.

The learned trial Judge, Hunt J., reached the conclusion that there was no fraudulent intent in the conveyances. He expressly found the defendants to be truthful witnesses. Accordingly he accepted their testimony which specifically denied any such fraudulent intent. On the basis of his findings of fact and of credibility he concluded that the plaintiff's action was not maintainable. This is an appeal against its dismissal.

[Freedman J.A. found that there was no fraud involved in the conveyance of the first two parcels. He continued:]

This leaves the third parcel of land, consisting of three lots in Gilbert Plains. These, too, were transferred on 8th July 1965 by Nicholas Merko to his wife. Nicholas asserts that the reason for the transfer was that in the spring of 1965 he became ill, with symptoms of heart trouble. Because of this illness he thought it desirable to transfer the Dauphin farm and the Gilbert Plains lots to his wife. That was the reason for the course of action taken by Nicholas. It was in no way motivated by any intent to defeat, hinder, delay, or defraud the plaintiff. Once again it must be pointed out that on this issue the learned trial Judge expressly found in favour of the defendants. There is substantial evidence in the record to support that finding, and an appellate court should be slow to overrule it. On the facts of this case we do not feel warranted in doing so here.

It may incidentally be pointed out that on the Gilbert Plains lots there was a house

which had originally been on the Dauphin quarter-section above referred to. To the extent that the transfer of the Gilbert Plains lots related to this house the defendants contended that this was merely a reconveyance to the wife of what actually belonged to her. The learned trial Judge's findings support the defendant on this point as well, thereby furnishing another ground on which the judgment may rest. But it is enough to say that the conveyance of the Gilbert Plains lots was not made with any intent to defeat or hinder the plaintiff.

One further factual circumstance needs to be noted. At the time when the transfers were made by the defendant, the plaintiff was not yet a creditor possessed of an existing debt. He was at most a person with a potential debt arising from a claim for damages. These damages were based on an alleged assault committed upon the plaintiff by the defendant, Nicholas Merko. At the time when the transfers in question were made the plaintiff's damage action had been commenced and the statement of claim had been served, but the matter was still a long way from judgment. Indeed the judgment was not obtained until 5th December 1967. The length of time between suit and judgment clearly suggests that the plaintiff's claim was not admitted but was the subject of a dispute that necessitated a trial.

The present appeal accordingly concerns a case in which the plaintiff sought and failed to establish that the impugned conveyances were null and void under s. 3 of the *Fraudulent Conveyances Act*. To the extent that the judgment rests upon issues of fact, it is plain that these were decided against the plaintiff and in favour of the defendants. But Mr. O'Sullivan, counsel for the plaintiff (who was not counsel at the trial before Hunt J.) contends that, regardless of what occurred in the area of fact, the learned trial Judge made an error in law. His position is that the learned trial Judge failed to consider and apply the principle enunciated in the case of *Freeman v. Pope* (1870), 5 Ch. App. 538. In that case Lord Hatherley L.C. stated that the principle on which the *Fraudulent Conveyances Act, 1571* (Imp.), c. 5 (the source of the *Fraudulent Conveyances Act* of Manitoba) is based, in "that persons must be just before they are generous, and that debts must be paid before gifts can be made." Accordingly, if the necessary effect of a conveyance was to defeat, hinder, or delay the creditors, that necessary effect was to be considered as evidencing an intention to do so. In such a case it would be the duty of the judge to direct the jury that they must infer the intent of the settlor to have been to defeat or delay his creditors. If in fact the transfer was not made with that intent, that would make no difference. According to *Freeman v. Pope* the law presumes such an intent, and that absolutely.

There is no doubt that the language of *Freeman v. Pope* appears to be comprehensive enough to warrant such a construction. But the question at once arises whether the general language used in *Freeman v. Pope* was intended to apply to every case, or whether it was to be limited to factual situations similar to the one with which it dealt. There is authority indicating that if a grantor with debts makes a transfer the effect of which is to render him unable to meet his then existing liabilities, that circumstance furnishes very strong evidence of an intent to defraud his creditors, *but such evidence is not conclusive*. Halsbury puts the matter in just that way: *vide* 17 Hals. (3rd), para. 1270, as follows:

> *Indebtedness not conclusive evidence*. The fact that the grantor was at the time of the alienation indebted to a considerable extent, though not amounting to insolvency, especially if by the alienation

he rendered himself unable to meet his then existing liabilities, furnished very strong evidence of an intent to defraud his creditors, but such evidence is not conclusive.

For the statement that such an alienation by a transferor "furnished very strong evidence of an intent to defraud his creditors" Halsbury cites, among other cases, *Freeman v. Pope, supra*. In support of the qualification, "but such evidence is not conclusive", Halsbury cites, among other cases, *Re Wise; Ex parte Mercer* (1886), 17 Q.B.D. 290, to which reference must now be made.

There are certain parallels between the case of *Ex parte Mercer* and the present one. In both, the defendant had made a voluntary transfer of property. In both, the transferor later became bankrupt. In both, the effect of the transfer was to render the defendant unable to pay his debts. In both, the plaintiff, at the time of the transfer, was not yet a creditor for an ascertained debt but rather was no more than a claimant for damages in a matter whose outcome was uncertain. Finally, in both, there was specific evidence that the transfers were made for reasons other than to defeat, delay, or defraud creditors.

Freeman v. Pope was considered by the Court in the *Mercer* case. In the Divisional Court Grantham J., referring to *Freeman v. Pope* and similar cases, made this comment [p. 295]:

> When learned judges have said that, if the necessary result of a settlement is to hinder creditors, it must be taken to have been executed with that intent, this observation must be taken as applied to the character of the particular case in which it was made.

In the Court of Appeal Lord Esher M.R. used the following language [p. 298]:

> But, if other circumstances make you believe that the man did not intend to do that which you are asked to find that he did intend, to say that, because that was the necessary result of what he did, you must find, contrary to the other evidence, that he did actually intend to do it, is to ask one to find that to be a fact which one really believes to be untrue in fact.

In the present case we have actual evidence, accepted by the learned trial Judge, that the transfers were not made with any fraudulent intent. That evidence cannot be ignored and has to be placed in the scale for consideration along with the *Freeman v. Pope* presumption. However strong the presumption may be that if the necessary effect of a voluntary transfer is to delay or defeat creditors an intention to do so should be inferred, it is not conclusive. In an appropriate case the presumption may have to yield in favour of cogent and affirmative evidence establishing an honest purpose in the making of the transfer, a purpose in no way designed to prejudice creditors. The present is such a case.

[The appeal was dismissed.]

COMMENTARY

10.07. With respect to the principle espoused in the *Mercer* case, see, *e.g.*, *Davies v. Dandy*, [1920] 2 W.W.R. 126 (Man. C.A.); *Dunsdon v. Dunsdon*, unreported, April 17, 1980 (Ont. Co. Ct.); *Buckland v. Rose* (1859), 7 Gr. 440 (Ont. Ch.); *Hickerson v. Parrington* (1891), 18 O.A.R. 635 (Ont. C.A.); *Bank of Montreal v. Stair* (1918), 44 O.L.R. 79 (Ont. H.C.); *Ottawa Wine Vaults Co. v. McGuire* (1912), 27 O.L.R. 319 (Ont. C.A.); affirmed (1913), 48 S.C.R. 44 (S.C.C.); *Owen Sound General and Marine Hospital v. Mann*, [1953] O.R. 643 (Ont. H.C.); *Carr v. Corfield* (1890), 20 O.R. 218 (Ont. H.C.); and *Henry Electric Ltd. v. White*, [1976] W.W.D. 10, following *Mandryk v. Merko*, reproduced *supra*.

10.08. An attempt to reconcile *Freeman v. Pope* and *Ex parte Mercer* was made in Langstaff, "The Cheat's Charter?" (1975), 91 L.Q. Rev. 86.

10.09. *Freeman v. Pope*, *Ex parte Mercer*, and *Mandryk v. Merko* were discussed in *G.E. Cox Ltd. v. C.I.B.C.* (1985), 23 D.L.R. (4th) 613 (N.B.C.A.); leave to appeal to S.C.C. refused (1985), 69 N.B.R. (2d) 270 (S.C.C.). Hoyt J.A., relying on *Freeman v. Pope*, stated (at 617) that "to have a voluntary conveyance set aside under the statute it is not necessary to prove the actual intent to defraud or delay creditors when the circumstances are such that the transfer necessarily would have that effect."

After stating that a presumption of fraudulent intent was raised in the present case, he noted (at 618) that "[t]he finality of the presumption has been questioned" in such cases as *Mercer* and *Mandryk*. However, he said (at 618), "[t]hese cases are of no comfort to the appellants because the evidence here falls short of showing a *bona fide* intention on the part of Mr. Cox [the debtor] and, through him, the company [the second debtor]."

It is not entirely clear whether, or the extent to which, Hoyt J.A. subscribed to the more radical interpretation given to *Freeman v. Pope*. While he noted the existence of a *presumption*, he also quoted Harrison J. in *McGillan* that "[i]t is idle for a party who has put through a transaction, the effect of which is to hinder and delay his creditors, to say that he had no intention to defraud." Hoyt J.A. said that this was the view expressed by Lord Hatherley in *Freeman v. Pope*. Yet Hoyt J.A. quoted His Lordship to the effect that the debtor must be presumed to have a fraudulent intent "in the absence of any...direct proof of intention." In other words, "direct proof of intention" would prevail. What of circumstantial evidence of intention? Could it rebut a *prima facie* presumption of fraudulent intent?

10.10. *Freeman*, *Mercer*, and *Mandryk* were discussed in B.C. Working Paper, at 19-20. The Working Paper noted different lines of cases adopting each authority, and stated that "[t]his confusion is in part the result of courts relying on a particular line of authority without considering conflicting authority" (at 20).

(iv) Burden of Proof and Corroboration in Transactions Between Relatives

KOOP v. SMITH

(1915), 51 S.C.R. 554, 25 D.L.R. 355 (S.C.C.)

DUFF J.— I think this appeal should be allowed and the judgment of the learned Chief Justice, who tried the action, restored. The majority of the Court of Appeal appear, if I may say so with respect, to have fallen into the error of treating the relationship of the parties to the impeached transaction as possessing no very material significance. The learned trial judge, on the other hand, treated the relationship as decisive in this sense that it determined the point of view from which the evidence was to be considered and the all important question of the onus of proof. The learned trial judge indeed appears to have laid it down as a proposition of law that a transaction of this kind between two near relatives, carried out in circumstances in themselves sufficient to excite suspicion, can only be supported (in an action brought to impeach it by creditors) if the reality or the *bona fides* of it are established by evidence other than the testimony of the interested parties; and there is a series of authorities in the Ontario courts which has been supposed to decide that, and it may be that it is the settled law of Ontario to-day.

I do not think the proposition put thus absolutely is part of the English law or of the law of British Columbia; but I think it is a maxim of prudence based upon experience that in such cases a tribunal of fact may properly act upon that when suspicion touching the reality or the *bona fides* of a transaction between near relatives arises from the circumstances in which the transaction took place then the fact of relationship itself is sufficient to put the burden of explanation upon the parties interested and that, in such a case, the testimony of the parties must be scrutinized with care and suspicion;

and it is very seldom that such evidence can safely be acted upon as in itself sufficient. In other words, I think the weight of the fact of relationship and the question of necessity of corroboration are primarily questions for the discretion of the trial judge subject, of course, to review; and that any trial judge will in such cases have regard to the course of common experience as indicated by the pronouncements and practice of very able and experienced judges such as Chief Justice Armour and Vice-Chancellor Mowat and will depart from the practice only in very exceptional circumstances.

I may add that I think it doubtful whether the Ontario decisions when properly read reâlly do lay it down as a rule of law that the fact of relationship is sufficient in itself to shift the burden of establishing the burden of proof in the strict sense. It may be that the proper construction of these cases is that the burden of giving evidence and not the burden of the issue is shifted. (As to this distinction see the admirable chapter IX., in Professor Thayer's "Law of Evidence.") In my own view, as indicated above, even this would be putting the matter just a little too high; I think the true rule is that suspicious circumstances coupled with relationship make a case of *res ipsa loquitur* which the tribunal of fact may and will generally treat as a sufficient *prima facie* case, but that it is not strictly in law bound to do so; and that the question of the necessity of corroboration is strictly a question of fact. Having examined the evidence carefully I am satisfied that the learned trial judge was entitled to take the course he did take and not only that the evidence, as I read it in the record, casts the burden of explanation upon the respondent, but that the testimony given by her brother ought not in the circumstances to be accepted as establishing either the actual existence of the debt or of the *bona fides* of the transaction.

[Davies, Idington, Anglin and Brodeur JJ. also gave reasons for allowing the appeal.]

COMMENTARY

10.11. With respect to the issue whether the burden of proof shifts or whether corroboration is required as a matter of law, where the impeached transaction involves relatives, reference should be made to the following cases: *T.D. Bank v. Michael*, [1973] 1 W.W.R. 656 (Alta. C.A.), citing *Greene, Swift & Co. v. Lawrence* (1912), 2 W.W.R. 932 (S.C.C.), and *Koop v. Smith*, reproduced *supra*; *Faulhaber v. Ulseth*, [1976] 4 W.W.R. 48 (Alta. T.D.), citing *T.D. Bank v. Michael*, *supra*; *Kapicki v. Andriuk*, [1975] 2 W.W.R. 332 (Alta. Dist. Ct.); *Bank of N.S. v. Zgurski* (1970), 72 W.W.R. 464 (Alta. S.C.); *Petryshyn v. Kochan*, [1940] 2 W.W.R. 353 (Sask. K.B.); *Bludoff v. Osachoff*, [1928] 2 W.W.R. 150 (Sask. C.A.); *Imperial Bank v. Esakin*, [1924] 2 D.L.R. 675 (Sask. C.A.); *Traders Group Ltd. v. Mason* (1973), 43 D.L.R. (3d) 76 (N.S.S.C.); varied (1974) , 53 D.L.R. (3d) 103 (N.S.C.A.); *Stewart v. Zacharuk*, [1949] 1 W.W.R. 213 (Sask. Q.B.); *Gallop v. Hamlin* (1973), 1 O.R. (2d) 156 (Ont. C.A.); *Tempo Building Supplies Ltd. v. Pitura* (1979), 33 C.B.R. (N.S.) 23 (B.C.S.C.); and *Owen Sound General and Marine Hospital v. Mann*, [1953] O.R. 643 (Ont. H.C.).

In *Re Whetstone* (1984), 12 D.L.R. (4th) 249 at 256 (Ont. S.C.), Sutherland J. adopted the views of Lerner J. in *Commerce Capital Mortgage Corp. v. Jemmett* (1981), 37 C.B.R. (N.S.) 59 at 73 (Ont. H.C.) where Lerner J. stated that, where there is a conveyance to a near relative: (1) the onus of proof does not shift to the defendant; and (2) if there are both "suspicious circumstances" *and* such a conveyance, the trial judge may, but is not strictly bound to, treat the evidence adduced as sufficient to establish a *prima facia* case. In other words, only an "evidentiary burden" may be imposed on the defendants. Sutherland J. emphasized that the "close relationship is not itself the suspicious circumstance".

In *Koop v. Smith*, *supra*, Duff J. stated that "the question of corroboration is strictly a question of fact." In *Re Whetstone*, Sutherland J. concluded that a certain report from a bank manager "constitutes sufficient independent evidence tending to support one material part of Whetstone's testimony as to constitute

sufficient corroboration to make the evidence of Whetstone himself *admissible* on the question of his intent" (at 256–57, emphasis added). Sutherland J. was of the view that the proper rule to follow was that the transferor's "evidence should not be given any effect unless corroborated" (at 257). Is this what Duff J. said or intended in *Koop v. Smith*? Why should uncorroborated evidence from the transferor be inadmissible (presumably as a matter of law)? Or, if admissible, why should it invariably "not be given any effect unless corroborated"?

In *Re Fancy* (1984), 46 O.R. (2d) 153 at 159 (Ont. S.C.), Anderson J. stated that "[w]here the impugned transaction was...between close relatives under suspicious circumstances, it is prudent for the court to require that the debtor's evidence on *bona fides* be corroborated by reliable independent evidence."

10.12. In *Kisluk v. B.L Armstrong Co.* (1982), 40 O.R. (2d) 167 at 182-83 (Ont. S.C.) (reproduced *infra*), Anderson J. dealt with the argument that the relationship between the parties was such as to shift the onus onto the defendant. He stated that such cases as *Koop v. Smith* "are dependent upon an initial finding that the circumstances of the impugned transaction are so suspicious as to reverse the normal onus and require the defendant to support the transaction."

10.13. The principles governing conveyances between close relatives also apply to transfers between individuals and companies that they control (*Burton v. R. & M. Insurance Ltd.* (1977), 81 D.L.R. (3d) 455 (Alta. S.C.); *Re Martineau and Martineau* (1969), 5 D.L.R. (3d) 165 (B.C.S.C.)), to associated companies (*Re Dougmor Realty Holdings Ltd.; Fisher v. Wilgorn Investments Ltd.*, [1967] 1 O.R. 66 (H.C.); reversed on other grounds [1968] 1 O.R. 61 (Ont. C.A.)), and to transfers between unmarried parties living together as husband and wife (*Lee v. Lee* (1978), 82 D.L.R. (3d) 429 (Nfld. Dist. Ct.)), followed in *Van Der Haas v. Van Der Haas*, unreported, May 11, 1984 (Ont. H.C.), at 17.

(e) PROTECTED TRANSACTIONS UNDER THE FRAUDULENT CONVEYANCES ACT

(i) "Bona Fide" Conveyances

To what does the term "*bona fide*" refer in s. 3 of the Ontario *Fraudulent Conveyances Act*? Does it refer to the intent of the debtor? If so, how can the debtor both have "the intent set forth" in s. 2 and be *bona fide*? Does the term refer to the transferee? If so, what is the difference between being *bona fide* and not having "notice or knowledge of the intent set forth" in s. 2? The latter position is reflected in *Halsbury's Laws of England* (4th ed. 1977), Vol. 18, at 176, para. 375, interpreting the phrase "in good faith" in the comparable English provision (*Law of Property Act 1925*, c. 20, s. 172(3)), although the editors also cite the view that the phrase "simply means that the transaction must be a genuine transaction and not a sham." With respect to the latter view, see *Banque d'Hochelaga v. Potvin*, [1924] 1 W.W.R. 488 (Alta. C.A.).

The B.C. Working Paper, at 24-26, was of the view that good faith meant that the transaction was not a sham, a view adopted in the New Brunswick Report, at 125. In *Re Panfab Corp.*, the court linked the term *bona fide* to at least one "badge of fraud" (retention of a benefit by the debtor).

RE PANFAB CORP.; DURO LAM LTD. v. LAST

[1971] 2 O.R. 202, 17 D.L.R. (3d) 382 (Ont. H.C.)

HOULDEN J.:—This is an appeal from the report of the Registrar dated June 12, 1970, made after the trial of an issue. The facts have been carefully detailed by the Registrar in his reasons which accompanied the report. The appeal is only as to the findings of the Registrar that certain debentures dated February 11, 1966, given by the bankrupt company in favour of Elsie Last in the amount of $26,100 and Victor Last in the

amount of $4,000 were fraudulent and void under ss. 64 and 64A [enacted 1966-67, c. 32, s. 11] of the *Bankruptcy Act*, R.S.C. 1952, c. 14.

Victor Last advanced money to the bankrupt on or about August 31, 1965. Elsie Last advanced her funds in October, 1965. At the time the advances were made, there were no arrangements for the parties to receive debentures as security for their loans. In the case of Victor Last, he was to receive a note. With reference to Elsie Last, she had put a mortgage on her home to raise the money, and the debtor company was to make the payments on the mortgage as they fell due.

When the moneys were received in October, the company was in dire need of working capital, and, although the funds gave a temporary respite, by January, 1966, the company urgently needed further financing. This was arranged through Samuel Hogg and Lillian Casselton, two of the directors and officers of the company. To protect these new advances, debentures were given under the *Corporation Securities Registration Act*, R.S.O. 1960, c. 70, and debentures were also issued to Elsie Last and Victor Last in respect of their loans. The effective date of the debentures is February 11, 1966. The petition in bankruptcy was filed on February 9, 1967.

The learned Registrar found, and there has been no attack on these findings, that the company was insolvent at the date the debentures were given and that the receipt of the debentures had the effect of giving Victor Last and Elsie Last a preference over other creditors. He further found that the giving of the securities came within ss. 64 and 64A of the *Bankruptcy Act*, and that Elsie Last and Victor Last were persons related to the bankrupt company within the meaning of s. 2B(2)(*b*) [enacted 1966-67, c. 32, s. 1] of the *Bankruptcy Act*.

....

The last issue is whether or not the debentures fall within the provisions of the *Fraudulent Conveyances Act*. Counsel for the creditors points out the following badges of fraud: (a) the debentures were given for a past-due debt; (b) the debentures were given to relatives of Eugene Last who had *de facto* control of Panfab; (c) the company was insolvent at the time the debentures were given; (d) in effect, the debentures took away all the assets of the company which should have been available to creditors.

Even if all these matters are accepted, it does not make the giving of the debentures void. The problem was dealt with by the Supreme Court of Canada in *Mulcahy et al. v. Archibald* (1898), 28 S.C.R. 523. Sedgewick J., who delivered the judgment of the Court, stated the relevant principles at p. 529:

> The Statute of Elizabeth, while making void transfers, the object of which is to defeat or delay creditors, does not make void but expressly protects them in the interest of transferees who have given valuable consideration therefor, and it has been decided over and over again that knowledge on the part of such a transferee of the motive or design of the transferor is not conclusive of bad faith or will not preclude him from obtaining the benefit of his security. So long as there is an existing debt and the transfer to him is made for the purpose of securing that debt and he does not either directly or indirectly make himself an instrument for the purpose of subsequently benefiting the transferor, he is protected and the transaction cannot be held void.

In the *Mulcahy* case at p. 529, Sedgewick J., quoted the words of Jessel M.R., in *Middleton v. Pollock* (1876), 2 Ch.D. 104 at p. 108:

> It has been decided, if decision were wanted, that a payment is *bona fide* within the meaning of the Statute of Elizabeth, although the man who made the payment was insolvent at the time to his own

> knowledge, and even although the creditors who accepted the money knew it... . The meaning of the statute is that the debtor must not retain a benefit for himself.

See also *P.E.I. Mutual Fire Ins. Co. et al. v. Best* (1933), 7 M.P.R. 107.

On the basis of this authority, *bona fide* in s. 3 of the *Fraudulent Conveyances Act* means that the debtor must not have retained a benefit to himself and in this case no such benefit was retained by Panfab. The transfer was made to give security to Victor Last and Eugene Last for an existing debt, and, even if Panfab knew it was insolvent and Victor Last and Elsie Last knew of the insolvency, this is not sufficient to void the transaction where there was no intention of subsequently directly or indirectly benefiting Panfab.

With reluctance, therefore, the appeal must be allowed.

COMMENTARY

10.14. In the extract from *Mulcahy* in the *Panfab* case, Sedgewick J. stated that "knowledge on the part of such a transferee of the motive or design of the transferor is not conclusive of bad faith and will not preclude him from obtaining the benefit of his security." Is this statement valid, in light of the closing flush of s. 3 of the *Fraudulent Conveyances Act*?

10.15. Commenting on s. 4 of the B.C. *Fraudulent Conveyance Act*, analogous to s. 3 of the Ontario Act, the B.C. Working Paper stated that "[j]udicially glossed, this section carries a meaning quite different from what might be expected. It has been taken to mean that a disposition of exigible property for valuable consideration, which is not a sham transaction, is valid unless the transferee actively participated in the fraud" (at 21).

10.16. If the *Panfab* interpretation of *bona fide* is accepted, could the very purpose of the Act be frustrated by a debtor simply conveying all his assets to another person? See Jewers, "Fraudulent Conveyance and Preference Legislation in Canada" (1956), 28 Man. Bar News 1 at 4, and Langstaff, "The Cheat's Charter?" (1975), 91 L.Q. Rev. 86 at 90.

Langstaff, *supra*, after arguing that fraudulent intent could be established either by "direct evidence" or "as a matter of law where the necessary effect of a conveyance is to defeat or delay creditors" (at 99), went on to state that a "grantor" [debtor] may then have an intent to defraud (as a matter of law) yet be in good faith" (also at 99). Langstaff contended that his interpretation gave independent life to the notice provision (which would relate to the transferee and would not be redundant). In reply, see Elkan, "Voluntary Conveyances to Defraud Creditors" (1975), 91 L.Q. Rev. 317.

(ii) The Role of Consideration

Reference should be made to the Ontario *Fraudulent Conveyances Act*, s. 3 ("good consideration") and s. 4 ("valuable consideration"). The analogous English provision is now s. 172(3) of the *Law of Property Act 1925*, c. 20, which reads as follows:

> 172.—(3) This section does not extend to any estate or interest in property conveyed for valuable consideration and in good faith or upon good consideration and in good faith to any person not having, at the time of the conveyance, notice of the intent to defraud creditors.

The *Statute of Elizabeth* simply used the phrase "good consideration," although it appears that "good consideration" and "valuable consideration" were regarded as synonymous. See *Union Bank v. Murdock*, [1917] 2 W.W.R. 112 (Man. Q.B.); reversed on other grounds [1917] 3 W.W.R. 820 (Man. C.A.), *per* Curran J., who used the expression "good (that is, valuable) consideration" (at 2 W.W.R. 114) when

commenting on 13 Eliz. 1, c. 5. See also *Bank of Montreal v. Crowell* (1980), 37 N.S.R. (2d) 292 at 303 (N.S.S.C.) *per* Hallett J.:

> The consideration must be "good consideration"; so-called meritorious consideration, that is, love and affection, is not valuable consideration and therefore not consideration within the meaning of the *Statute of Elizabeth*. (*Cromwell v. Comeau* (1957), 8 D.L.R. (2d) 676, at p. 684.)

With respect to the view that "good consideration" really means "valuable consideration", see B.C. Working Paper, at 21.

Full or adequate consideration is not necessary to uphold a conveyance under the *Fraudulent Conveyances Act*: see *Leighton v. Muir and Windsor Supply Co.* (1962), 34 D.L.R. (2d) 332 (N.S.S.C.); *Reaume v. Guichard* (1856), 6 U.C.C.P. 170; *Carradice v. Currie* (1872), 19 Gr. 108 (Ont. Ch.); *Owen Sound General and Marine Hospital v. Mann*, [1953] O.R. 643 (Ont. H.C.); *Stephens v. Olive* (1786), 2 Bro. C.C. 90; *Nunn v. Wilsmore* (1800), 8 Term. Rep. 521; *Copis v. Middleton* (1818), 2 Madd. 410; and *Thompson v. Webster* (1861), 45 E.R. 233.

However, nominal or grossly inadequate consideration is not sufficient. See *Fleming v. Edwards* (1896), 23 O.A.R. 718 at 722 (Ont. C.A.), where the consideration in question "was a grossly inadequate consideration, and as such was a badge of fraud." In *Hickerson v. Parrington* (1891), 18 O.A.R. 635 at 643 (Ont. C.A.) Osler J.A. stated that "there is no clear and sufficient proof that the consideration was inadequate." Another example of a decision in which a judge seemed to require "adequate" consideration was that of McDermid J.A. in *T.D. Bank v. Michael* (1972), 32 D.L.R. (3d) 498 at 502 (Alta. C.A.). "Very inadequate" consideration can indicate suspicious circumstances: *Bank of Montreal v. Vandine*, [1953] 1 D.L.R. 456 at 461 (N.B.C.A.).

Re Fancy (1984), 46 O.R. (2d) 153 (Ont. S.C.), appears to stand for the proposition that nominal consideration is neither "good" nor "valuable" consideration within ss. 3 and 4 of the Ontario Act. With respect to the effect of nominal consideration (in this case, $1), see *Re Whetstone* (1984), 12 D.L.R. (4th) 249 at 255 (Ont. S.C.): "There being only nominal consideration, the transaction was a voluntary one..."

The B.C. Working Paper, at 17 *et seq.*, noted two classes of conveyances for nominal consideration. "In the first class of conveyances, the transaction renders the grantor insolvent, and his fraudulent intent is presumed" (at 18). See *Freeman v. Pope*, reproduced *supra*. In the second class of conveyances, "fraudulent intent must be proved as a matter of fact"; this necessity "arises in every disposition for inadequate consideration which does not have the effect of making the grantor insolvent" (at 19).

The Working Paper stated that the courts are required "to assess the adequacy of the consideration for the conveyance" (at 21). This "task is often disguised in semantic debates concerning whether consideration is 'good', and whether that term includes 'valuable', 'non-valuable' or 'meritorious' consideration" (at 21).

Concerning whether "good consideration" includes "natural love and affection," see *Cadogan v. Kennett* (1776), 98 E.R. 1171, and *Cromwell v. Comeau* (1957), 39 M.P.R. 347 (N.S.C.A.). Would such an interpretation serve, in practice, to nullify the purpose of the Act? See Langstaff, "The Cheat's Charter?" (1975), 91 L.Q. Rev. 86 at 99-100; and a reply in Elkan, "Voluntary Conveyances to Defraud Creditors" (1975), 91 L.Q. Rev. 317 at 319-20. See also Mowbray (ed.), *Lewin on Trusts* (16th ed. London: Sweet and Maxwell, 1964), at 112. Where a conveyance is voluntary,

only the fraudulent intent of the debtor need be shown. See *Oliver v. McLaughlin* (1893), 24 O.R. 41 (Ont. C.A.); *Gauthier v. Woollatt*, [1940] 1 D.L.R. 275 (Ont. H.C.); *Union Bank v. Murdock*, [1917] 3 W.W.R. 820 (Man. C.A.); *Davies v. Dandy*, [1920] 2 W.W.R. 126 (Man. C.A.); *Banque d'Hochelaga v. Potvin*, [1924] 1 W.W.R. 488 (Alta. C.A.); *Cromwell v. Comeau* (1957), 39 M.P.R. 347 (N.S.C.A.); and *Traders Group Ltd. v. Mason* (1973), 43 D.L.R. (3d) 76 (N.S.S.C.); varied (1974), 53 D.L.R. (3d) 103 (N.S.C.A.).

Where, however, the transferee gives good or valuable consideration, an impeaching creditor must prove an actual intent on the part of the debtor to defraud his creditors, and that the transferee had "notice or knowledge" of that intent. See *Hickerson v. Parrington* (1891), 18 O.A.R. 635 (Ont. C.A.); *Ferguson v. Lastewka*, [1946] O.R. 577 (Ont. H.C.); and the cases cited in the the preceding paragraph. Dunlop apparently concurs, stating that the presumptions cannot be used in such a case (at 521–22). However, Dunlop noted (at 255) that, even where fraud must be proved as a fact, the courts have developed certain "evidentiary rules" such as the "badges of fraud", to enable them to find fraud "unless the supporters of the transaction could explain away the suspicious circumstances." Proof of a badge of fraud "does raise a *prima facie* case which it would be prudent for the defendant to attempt to rebut" (at 525). In practical terms, how much difference do you think it would ordinarily make to use a presumption or to rely on a badge of fraud?

Mere suspicion of fraudulent intent does not appear to be sufficient. See *Shephard v. Shephard*, [1925] 2 D.L.R. 897 (Ont. C.A.), and *Robertson v. Robinson*, [1928] 2 D.L.R. 343 (Ont. C.A.); affirmed [1929] S.C.R. 175 (S.C.C.).

In *Cameron v. Cusack* (1890), 17 O.A.R. 489 at 493 (Ont. C.A.), Osler J.A. stated (emphasis added):

> I take the law to be that if the purchaser knew that the intent of the grantor is to defraud his creditors, the fact that he has paid a valuable consideration, and that the property was intended to pass to him, will not avail him. *There must be bona fides on his part. That is to say, ignorance of the fraudulent intent on the part of the vendor.* Mere intention that the property shall pass, and payment of a valuable consideration, will not save him.

Given the view of Osler J.A., why does the *Fraudulent Conveyances Act* appear to differentiate between *bona fides* and a transferee's want of notice or knowledge?

Respecting whether "notice" includes constructive notice, presumably arising from circumstances surrounding the impugned transaction, see *Lloyds Bank Ltd. v. Marcan*, [1973] 3 All E.R. 754 (C.A.) *per* Pennycuick, V.-C.

Is notice of the debtor's insolvency notice of his fraudulent intent? See *Mulcahy v. Archibald* (1898), 28 S.C.R. 523 (S.C.C.). What if the transferee has notice of the prejudicial effect of the transaction? See *Crawford v. Meldrum* (1866), E. & A. 101 at 107, and, *contra, Cornish v. Clark* (1872), L.R. 14 Eq. 184.

See, also, New Brunswick Report, which did not accept the express language of 13 Eliz., c. 5, at face value:

> Mere knowledge of the debtor's intent on the part of the person who has given consideration will not make the transaction voidable. This appears to apply under both the English statute [13 Eliz., c. 5] and the provincial legislation [akin to the Ontario *Assignments and Preferences Act*], although the actual words of the English statute indicate that notice of the improper intent may be fatal to the rights of a third party. [At 115.]

. . . .

That notice of the debtor's intent is not enough to affect the third party's rights, even under the British statute, is supported by *Mulcahy v. Archibald* (1898), 28 S.C.R. 523, and *Bank of Montreal v. Vandine*, [1953] 1 D.L.R. 456, 33 M.P.R. 368 (N.B.C.A.)... .

On the basis of *Bank of Montreal v. Vandine* and earlier *dicta* in *White v. Hamm* (1904), 2 N.B. Eq. 575, and *Dyer v. McGuire* (1909), 4 N.B.Eq. 203, the position in New Brunswick appears settled that there must be more than notice of the debtor's improper intent if the third party gives valuable consideration.

There need be no conflict between this position and the wording of section 6 of the English statute. In setting aside the transaction made by the debtor, the issue is the intent of the transaction. Under the existing jurisprudence, if the third party gives valuable consideration, there must be a concurrence of intent to attack the transaction. Mere knowledge of the debtor's improper intent does not create concurrence of intent. [At 115, note 139.]

After stating (at 116) that the "test...is whether [the transferee] is privy to the fraud against creditors," the New Brunswick Report stated, with respect to privity (at 116, note 140):

Privity would undoubtedly exist if the third party shared the actual intent to defeat creditors or to give an unjust preference. If the third party's own intent is to gain a good bargain for himself, some form of collusion or assistance with the deliberate object of helping the debtor to carry out his improper intent would probably be necessary.

In *G.E. Cox Ltd. v. C.I.B.C.* (1985), 23 D.L.R. (4th) 613 at 619 (N.B.C.A.); leave to appeal to S.C.C. refused (1985), 70 N.R. 82 (S.C.C.), Hoyt J.A. referred to the need to prove "fraudulent intent". He later referred to the need to prove that the transferee was a "party to this fraudulent intent". While the B.C. Working Paper, at 22-24, noted the different interpretations of the latter doctrine, it said that, "[i]n practice the different formulations appear to have little impact on the result of reported cases. Nothing seems to turn on the precise formula adopted in any particular case" (at 24).

Concentrating on the fraudulent intent of the debtor, and ignoring the actual effect of the transaction, Lord Mansfield stated in *Cadogan v. Kennett* (1776), 2 Cowp. 432 at 434:

But if the transaction be not *bona fide*, the circumstances of its being done for a valuable consideration will not alone take it out of the statute. I have known several cases where persons have given a fair and full price for goods, and where the possession was actually changed; yet being done for the purpose of defeating creditors, the transaction has been held fraudulent, and therefore void.

One case was where there had been a decree in the Court of Chancery, and a sequestration. A person with knowledge of the decree bought the house and goods belonging to the defendant, and gave a full price for them. The Court said the purchase, being with a manifest view to defeat the creditor, was fraudulent, and therefore, notwithstanding a valuable consideration, void... .

The language of Lord Mansfield was quoted by Spragge V.-C. in *Smith v. Moffatt* (1869), 28 U.C.Q.B. 486 at 496. See also *McMullen v. Dr. Barnardo's Homes National Incorporated Assn.* (1924), 26 O.W.N. 168 (Ont. C.A.), where the conveyance was avoided notwithstanding that full consideration was given. Orde J.A. was of the view that the giving of the consideration was itself part of a fraudulent scheme to defeat the creditor.

On the other hand, Hurley has stated that even an insolvent person validly could transfer property "if sufficient consideration were received": Hurley, "Transfers for Insufficient Consideration in Oregon" (1957), 36 Ore. L. Rev. 313 at 317. He said further (*ibid.*): "If there is a corresponding increase in the debtor's assets, the creditors are not prejudiced because they are in no worse position than they were before the conveyance."

See also Mack,"Fraudulent Conveyances — Now and Hereafter" (1980), 32 C.B.R. (N.S.) 82 at 89, where it is stated that s. 2 of the *Fraudulent Conveyances Act* "indeed is not limited solely to voluntary conveyances but will also affect conveyances where full consideration is exchanged if the transaction is entered into with knowledge by both parties of intent to prejudice creditors of one of them."

As a matter of policy, should legislation strike down transactions where no creditor has been prejudiced? Would it make any difference to the determination of whether actual prejudice to creditors has occurred if a debtor sold his house for $200,000 in cash or if he simply exchanged his house for another house worth $200,000?

(f) PROTECTED TRANSACTIONS UNDER THE ASSIGNMENTS AND PREFERENCES ACT

(i) Introduction

Note that s. 4(1), dealing with fraudulent conveyances, begins with the phrase "subject to section 5." However, not all of s. 5 is relevant to such conveyances.

(ii) The Knowledge or Intent of the Transferee

JOHNSON v. HOPE

(1890), 17 O.A.R. 10 (Ont. C.A.)

MACLENNAN J.A.:—

....

The statute, 13 Eliz. ch. 5, sec. 6, saves from its operation, conveyances, & c., made upon good consideration, and *bonâ fide*, to persons not having at the time any *notice* or *knowledge* of the fraud or covin. It is remarkable that there is no similar general provision in our statute, R.S.O. ch. 124 [akin to the present *Assignments and Preferences Act*, R.S.O. 1980, c. 33], saving transactions entered into without notice or knowledge of the intent or other circumstances which make them fraudulent. In one member alone, section 3 (1) [now s. 5(1)], the exception is extended to persons who are described as "innocent purchasers or parties," which of course must mean persons without notice or knowledge.

But then the word *bonâ fide* is used throughout, and it would seem to follow that the Legislature did not intend to involve persons having neither knowledge or notice, in the disabling and penal consequences of the acts thereby forbidden. It would paralyse trade and mercantile business altogether, if transactions entered into in all honesfy and good faith, and for valuable consideration, with persons apparently solvent and prosperous, were liable to be undone upon its being afterwards discovered and proved that such persons were at the time in embarrassed circumstances or unable to pay their debts in full. Such a construction of the Act would make it a trap and a snare instead of an enactment salutary and beneficial to the mercantile community. It has always been the policy of the law to protect, as far as possible, persons acting *bonâ fide*, and without notice of fraud or other wrong doing, and so I think a person who deals *bonâ fide* with an embarrassed debtor, and who at the time of the dealing has no knowledge or notice of his embarrassed condition, is safe from all the consequences enacted by the

statute. It is hard to imagine how a transaction can be otherwise than *bonâ fide*, with reference to what is forbidden in this statute, if it has been entered into without knowledge or notice of the embarrassments of the debtor.

I also think that as our statute is *in pari materiâ* with 13 Eliz. ch. 5, the 6th section of that Act may be held as applicable to the Ontario Act, so as to protect persons not affected with notice, and in that view the point may be regarded as decided by *Burns v. McKay*, 10 O.R. 167, (affirmed in this Court), and the cases there cited by the learned Chancellor.

COMMENTARY

10.17. But see *Schwartz v. Winkler* (1901), 13 Man. R. 493 (Man. K.B.); and *Stephens v. McArthur* (1890), 6 Man. R. 496 (Man. C.A.); reversed (1891), 19 S.C.R. 446 (S.C.C.). Does inadequacy of consideration render irrelevant the knowledge or intention of the transferee?

(iii) "Good" or "Valuable" Consideration and "Fair and Reasonable" Consideration

LEIGHTON v. MUIR AND WINDSOR SUPPLY CO.

(1962), 34 D.L.R. (2d) 332 (N.S.S.C.)

[The plaintiff in this action *pendente lite* conveyed property valued at $8,500 to his sister, who assumed a mortgage of $3,500 on the property. Shortly thereafter, the defendant obtained a judgment against the plaintiff. The defendant applied to have the conveyance set aside, arguing that, under the *Assignments and Preferences Act*, R.S.N.S. 1954, c. 17, and the *Statute of Elizabeth*, 1571 (13 Eliz. 1, c. 5), it constituted a fraudulent preference by an insolvent person.]

COFFIN J.:...A very important point in issue is whether the assumption of the Eastern Canada mortgage by Miss Leighton is adequate consideration for the conveyance of the main property, bearing in mind the fact that the evidence of Mr. Crossley at p. 43 was that the property was worth between $8,500 and $9,000 and the amount due on the mortgage was something over $3,000.

The defendant pleads the *Assignments and Preferences Act*, R.S.N.S. 1954, c. 17 and also the *Statute of Elizabeth*, 13 Eliz., c. 5.

The operative section of the *Assignments and Preferences Act* is s. 3 which makes void every transfer of property by an insolvent person with intent to defeat, hinder, delay or prejudice his creditors, or any one or more of them.

This is modified by s. 4(1) (d):

> 4(1) Nothing in Section 3 shall apply,
>
> ....
>
> (d) to any *bona fide* gift, conveyance, assignment, transfer or delivery over of any property which is made in consideration of any present actual *bona fide* payment in money, or by way of security for any present actual *bona fide* advance of money, or which is made in consideration of any present actual *bona fide* sale or delivery of property; provided that the money paid, or the property sold or delivered, bears a fair and reasonable relative value to the consideration therefor.

The *Statute of Elizabeth*, after making certain transfers void, then provides by s. VI:

> VI. Provided also, and be it enacted by the Authority aforesaid That this Act or any Thing therein contained, shall not extend to any Estate or Interest in Lands, Tenements, Hereditaments, Leases, Rents, Commons, Profits, Goods or Chattels, had, made, conveyed or assured, or hereafter to be had made, conveyed or assured, which Estate or Interest is or shall be upon good Consideration and *bona fide* lawfully conveyed or assured to any Person or Persons, or Bodies Politick or Corporate, not having at the Time of such Conveyance or Assurance to them made, any Manner of Notice or Knowledge of such Covin, Fraud or Collusion as is aforesaid; any Thing before mentioned to the contrary hereof notwithstanding.

It is in the interpretation of these statutes that the question of whether or not there was consideration for the transfer of the main 50 ft. lot from Kenneth Leighton to his sister is extremely vital.

Kerr on Fraud & Mistake, 7th ed., pp. 335-6 states that:

> In cases of voluntary gifts, it matters not whether or not the volunteers had notice of the fraud; but where there has been a conveyance for value, not only must fraud be shown, but, in order to avoid the transaction as against the purchaser it must be shown that he was privy to the fraud against creditors. Unless this position can be established, the purchaser who has paid his money or other consideration has a right paramount to that of creditors. The question, where the conveyance is for value, is, whether there was an intent to defraud creditors in the parties to the transaction. Whatever fraudulent intent there may have been in the mind of the vendor, it would not avoid the conveyance, unless it was shown to have been concurred in by the purchaser. It could not be contended that the mere fraudulent intent of the vendor could avoid the conveyance, if the purchaser were free from that fraud... .
>
> Mere notice of indebtedness or failing circumstances of the vendor, or even that the result of the sale may be to defeat or delay his creditors, or any of them, will not avoid a *bona fide* purchase, if the purchaser does nothing more in furtherance of any intent the vendor may have of defeating, hindering, or defrauding his creditors by means of the sale.

I am satisfied from the evidence of Kenneth Leighton that he was denuding himself of his property at a time when he knew he was seriously indebted to the plaintiff, and if there is no consideration for the transfer to Maxine Elizabeth Leighton, the conveyance must fail.

....

I find that under the terms of the document the plaintiff did assume the mortgage and has made the payments therein stipulated. The problem is whether the consideration was adequate in view of the evidence of Mr. Gordon B. Crossley that in 1957 the property was worth between $8,000 and $8,500 and whether adequacy of consideration is a relevant question in any event.

The American authorities take a very definite and practical attitude to the problem.

Corpus Juris, vol. 27, p. 484, for example, says:

> While there are some decisions apparently to the contrary, it is very generally held that inadequacy of consideration is a fact calling for explanation, and, therefore, a badge of fraud, especially when such inadequacy is gross.

And at p. 534:

> A conveyance in consideration of the assumption of a mortgage or other encumbrance on the property conveyed is based upon a valid consideration, provided the encumbrance equals the value of the

property. If the value of the property conveyed exceeds the amount of encumbrance thereon, an agreement by the grantee to pay off the encumbrance is not a valuable consideration as against the grantor's creditors.

These principles are supported to some extent by such cases as *Crawford v. Meldrum* (1866), 3 Gr. E. & A. (U.C.) 101; *Strong v. Strong* (1854), 18 Beav. 409, 52 E.R. 161, where a property having a surplus income of £178 was purchased for an annuity of £60.

But it should be noted that in one of the cases cited by Corpus Juris, *Carradice v. Currie* (1872), 19 Gr. 108, Mowat, V.-C. said at p. 111:

> Adequacy of consideration is not necessary to maintain a transaction under the 13 Elizabeth (*a*); though in some cases the inadequacy may afford some evidence of guilty knowledge (*b*). But a conveyance by a father to his son in consideration of an annuity of less value than the property conveyed does not suggest guilty knowledge of a fraud by the grantor, in the same way that a conveyance for an inadequate price to a stranger sometimes does.

The same thinking appears in *Black v. Fountain* (1876), 23 Gr. 174, where Spragge, C., said at p. 175:

> Mrs. *Fountain* was dowable inchoately, therefore, of property worth say $1,300 — that she gave up, and what she received was an absolute title to the property, the net value of which was $1,700. It is palpable that what she gave bore a very small proportion to what she received. If her dower had accrued, her right would have been a tenancy for life of one-third of a property worth $1,300, and she receives a property in fee worth $1,700. The two things are out of all proportion. It is something beyond mere inadequacy.

But there have been definite Canadian decisions indicating that consideration, although inadequate, is sufficient to place the burden of proving the fraud on the party endeavouring to set aside the deed.

Owen Sound General & Marine Hospital v. Mann et al., [1953] 3 D.L.R. 417, [1953] O.R. 643, is one of the most generally quoted cases supporting this view, and I quote Anger, J., at p. 420 D.L.R., p. 646 O.R.: "The conveyance in this action was not voluntary but was based upon good and valuable consideration, apart from the monetary consideration of one dollar. The conveyance was made subject to the existing mortgage of $1,000..." After quoting *Falconbridge's Law of Mortgages*, 3rd ed., p. 269, referring to the implied obligation of the transferee to indemnify the transferor, he went on — "In the conveyance before me the grantees have that obligation, so the conveyance was based upon valuable consideration." And, at p. 421 D.L.R., p. 646 O.R.: "Adequacy of consideration is not necessary to uphold a transaction under the *Fraudulent Conveyances Act...*"

Reutcke v. Reutcke et al. (1958), 66 Man. R. 134 appears to support this view, but Monnin, J., at p. 139 pointed out that here the defendant "did not put all of his assets out of reach of plaintiff but only changed the nature of his interests in two parcels of real property into shares".

In *Hickerson v. Parrington* (1891), 18 O.A.R. 635, at p. 637, Burton, J.A., in dealing with consideration by way of assumption of mortgage, went so far as to state "that although a deed, even if made for valuable consideration, may be affected by *mala fides*, those who undertake to impeach such a transaction on that ground, have a task of great difficulty to discharge".

> Inadequacy as between husband and wife or members of a family does not suggest knowledge of a fraud in the same way that a conveyance for inadequate price to a stranger sometimes does:

Parker on Frauds on Creditors & Assignments, 1903, p. 87; *Banque d'Hochelaga v. Potvin*, [1924] 1 D.L.R. 678, 20 A.L.R. 12.

In *Reaume v. Guichard* (1855), 6 U.C.C.P. 170, at p. 172, the trial Judge directed the jury that "as to mere inadequacy of consideration it must be so gross as to startle", and in *Bank of Montreal v. Vandine et al.*, [1953] 1 D.L.R. 456, at p. 468, it was suggested by Harrison, J., that inadequacy must be such that "shocks the conscience".

In *Carradice v. Currie* (1872), 19 Gr. 108, dealing with 13 Elizabeth, Mowat, V.-C., said at p. 111:

> The consideration which *John* contracted to give in lieu of the $1,000, was an annuity of $80 a year as long as either *Duncan* or his wife should live, with firewood and the use of the orchard. Most of the other things agreed to in December, *Duncan* was by the previous agreement entitled to in addition to the $1,000. These new obligations of *John's* were an inadequate consideration for the $1,000; but no authority was cited, and no principle was suggested, which would justify us in holding that the inadequacy of the consideration made the transaction void as against a creditor.

It is true that the authorities support the view that in transactions between near relatives which have the effect of defeating the claims of creditors, the testimony of the parties must be scrutinized with care, and that where corroborative evidence is available it should be given: *Koop v. Smith* (1915), 25 D.L.R. 355, 51 S.C.R. 554; *Lambert v. De Forel*, [1936] 2 D.L.R. 302, 44 Man. R. 110; *Union Bank v. Murdock* (1917), 37 D.L.R. 522, 28 Man. R. 229; *Stewart v. Zacharuk*, [1949] 1 W.W.R. 213.

The question of corroboration of the consideration is no problem here, however, because we have the terms of the document itself. In my opinion the whole problem is the question of adequacy.

The question was considered by the New Brunswick Supreme Court, Appeal Division, in *Bank of Montreal v. Vandine et al.*, [1953] 1 D.L.R. 456. On the trial Harrison, J., at p. 460 summarized the questions to be determined under the *Statute of Elizabeth:*

> (1) Whether the conveyance in question was made by the debtor with the intent "to delay, hinder or defraud" his creditors; and — (2) If there was such intent, whether the party buying such property participated in such fraudulent intent.
>
> The burden of proof as to fraud by the debtor in making the conveyances is upon the party seeking to set aside such conveyances where, as in this case, the conveyances in question were made for valuable consideration. Parker in his *Frauds on Creditors*, 1903, says at p. 43: "But whether a conveyance be fraudulent or not depends upon its being made upon good consideration and *bona fide*. When the transaction is voluntary the fact that creditors are defeated gives rise to a presumption of fraudulent intent, but where there has been a valuable consideration the presumption does not arise."

He then at p. 464 emphasized the principle that in order to succeed in setting aside a conveyance under the *Statute of Elizabeth*, it is necessary to show that the grantee is party to the fraud and he cited — 15 Hals, 2nd ed., p. 252; *Re Johnson* (1881), 20 Ch.D. 389; *Re Reis*, [1904] 2 K.B. 769 at p. 776.

The effect of consideration was considered in *Mulcahy v. Archibald* (1898), 28 S.C.R. 523 and I quote from Sedgewick J., at p. 529:

> At the time of the transaction impeached Wrayton owed the plaintiff upwards of $4,000. The goods which were transferred to her by Wrayton from the proceeds of which the goods levied upon were

bought were transferred to her on account of this indebtedness. No doubt it was the intention on the part of Wrayton to prevent this seizure under the judgment which he expected Blais would very soon recover against him and for the very purpose of securing his sister at the expense of Blais and with intent either to delay him in his remedies or to defeat them altogether. The statute of Elizabeth, while making void transfers, the object of which is to defeat or delay creditors, does not make void but expressly protects them in the interest of transferees who have given valuable consideration therefor, and it has been decided over and over again that knowledge on the part of such a transferee of the motive or design of the transferor is not conclusive of bad faith or will not preclude him from obtaining the benefit of his security. So long as there is an existing debt and the transfer to him is made for the purpose of securing that debt and he does not either directly or indirectly make himself an instrument for the purpose of subsequently benefiting the transferor, he is protected and the transaction cannot be held void.

Defendant's counsel in the present case made reference to the badges of fraud. *Parker's Frauds on Creditors & Assignments* at p. 68 lists the principal badges of fraud:

(1) Generality of conveyance;
(2) Continuance in possession by the debtor;
(3) A voluntary conveyance *pendente lite* to defeat an execution;
(4) Engagement in trade soon after a settlement;
(5) Some benefit retained under the settlement to the settlor;

And at p. 69 he refers to the badge of secrecy.

Badges (1), (2), (4) and (5) do not apply to the Leighton transfer. (3) does not apply if the consideration be considered valuable.

Secrecy was argued because the deed was not recorded for a month after the conveyance. Miss Leighton did give some explanation for this. On cross-examination at p. 24 she answered Mr. Kimball: "Q. Why did you wait three weeks to record the deeds? A. Well, in between that time there were other things I still had to get straightened around. The deeds were here. I had my work to do through the week." And at p. 25: "A. Well, between that time and the time I had them recorded, I know there were one or two week-ends I went up home and I had forgotten to take them."

The badges of fraud against Kenneth Leighton are many, and if this transfer were voluntary I would have no hesitation in setting it aside.

He knew he owed money, which he could not repay without recourse to this property. He left the Province when a writ had just been served on him. Mr. Day, solicitor for the major creditor, had discussed the account in detail with him before the conveyances, and this Kenneth Leighton denied.

None the less, in view of the authorities which I have quoted, I do not think the conveyance of the main property can be set aside under the *Statute of Elizabeth*.

The case, however, does not end there.

The defendants plead the *Assignments and Preferences Act*. If they can bring themselves within that statute, their position will be stronger because s. 4(1)(d) contains the words: "provided that the money paid, or the property sold or delivered, bears a fair and reasonable relative value to the consideration therefor".

Parker's Frauds on Creditors & Assignments at p. 87 points out in his Chapter discussing Consideration that the effect of the provincial enactments in this regard should not be overlooked.

Section 3 of our *Assignments and Preferences Act* deals with transfers of property made by an "insolvent person".

By s. 1 (a): "'insolvent person' means any person who is in insolvent circumstances, or is unable to pay his debts in full, or knows himself to be about to become insolvent"; Parker, *supra*, at p. 107 said:

> Under the Provincial Acts it is necessary in attacking a transaction as a preference to show that it was made when the debtor was in insolvent circumstances or unable to pay his debts in full or knew he was on the eve of insolvency.
>
> This fact of insolvency must in all cases be proved by the attacking creditor, and even in those cases where there is a statutory presumption of invalidity the attacking creditor has none the less to assume the onus of proving insolvency... .
>
> A man may be deemed insolvent in the sense of the Acts if he does not pay his way and is unable to meet the current demands of creditors, and if he has not the means of paying them in full as their claims mature, out of his assets realized upon a sale for cash or its equivalent.

At p. 108: "Equities of redemption are assets realizable under execution, and must be taken into account."

It is quite clear that a voluntary settlement which results in insolvency would be an infraction of the *Statute of Elizabeth*, and clear evidence of the settlor's intent to defeat and delay his creditors: *Sun Life Ass'ce Co. v. Elliott* (1900), 31 S.C.R. 91 at p. 94.

It is quite another thing to say that it is a breach of the *Assignments and Preferences Act*.

The question of insolvency was considered in *Davidson v. Douglas* (1868), 15 Gr. 347 at p. 351, where Spragge, V.-C., said:

> ...but, in considering the question of the solvency or insolvency of a debtor, I do not think that we can properly look upon his position from a more favorable point of view than this, to see and examine whether all his property, real and personal, be sufficient if presently realized for the payment of his debts, and in this view we must estimate his land, as well as his chattel property, not at what his neighbours or others may consider to be its value, but at what it will bring in the market at a forced sale; or at a sale when the seller cannot await his opportunities, but must sell;...

These principles were accepted in *Robinson v. McCauley* (1913), 13 D.L.R. 437, 23 Man. R. 781, and I quote Curran, J., at p. 443: "Although clearly he had not the money in hand to discharge his liabilities owing at this time I could not hold that he had not the adequate means in other species of property at his disposal to do so."

I refer also to *Richards & Brown v. Leonoff* (1915), 24 D.L.R. 180, 25 Man. R. 548.

We are still faced with the practical result that Kenneth Leighton was in fact insolvent after making the conveyances. Of that there can be no doubt. He had nothing after the deeds to the plaintiff. He has on his own admission made no effort to pay his bill.

In *Doucet v. Side Sode et al.* (1916), 27 D.L.R. 732, 49 N.S.R. 485 at p. 487 Harris, J., took this position:

> Holding as I do that the transfer of the real estate was part of a scheme to defraud creditors, the burden is cast upon those supporting the conveyance to prove that he was able to satisfy his creditors after taking into consideration his subsequent illegal and fraudulent transactions. This they have failed to do. That the property subsequently disposed of in a fraudulent way is to be deducted from his remaining assets in deciding upon his solvency is clearly pointed out in *Hunt on Fraudulent Conveyances*. He states a number of cases in which the debtor is to be considered as insolvent and this is his third proposition:
>
> "Where the settlor was, after the execution of the instrument, in perfectly solvent circumstances,

but has since divested himself of so much of the property which was reserved out of the settlement that there is not enough left to pay the debts which he owed at the time the settlement was made."

The *Doucet* case found the conveyance bad both under the *Statute of Elizabeth* and the *Assignments Act*, and the decision was upheld on appeal.

This case then appears to bring the plaintiff Maxine Elizabeth Leighton within the *Assignments and Preferences Act*. The property sold, on the evidence, was worth at least $8,500. The consideration was the mortgage, on which there was due $3,587.47 plus $10.32. I cannot see that the property sold bears "a fair and reasonable relative value to the consideration therefore".

In my view, under this decision, the conveyance fails under the provisions of the *Assignments and Preferences Act*.

The hardship on the plaintiff should not be insurmountable because there should be ample equity in the property to secure a loan sufficient to pay the creditors.

In any event under the authorities I cannot see how the creditors can be deprived of all their rights against the property in question by these conveyances from Kenneth Leighton to his sister, particularly in view of the Nova Scotia decision in *Doucet v. Side Sode et al., supra*.

The conveyances to the plaintiff as described in the statement of claim will therefore be set aside as against the second defendant and other creditors of Kenneth Leighton and the first defendant, J. Grant Muir, High Sheriff for the County of Hants, is authorized to proceed to sell the lots therein described, pursuant to the execution referred to in the counterclaim... .

COMMENTARY

10.18. See New Brunswick Report, at 128-29: "It is unclear whether the proviso in the provincial saving clause [akin to s. 5(1) of the Ontario *Assignments and Preferences Act*] extends to all of the protected transactions, or only to the category of transactions for a present consideration which immediately precedes it. Either interpretation is possible grammatically".

(g) STANDING TO IMPEACH FRAUDULENT CONVEYANCES

(i) Introduction

Note that s. 2 of the *Fraudulent Conveyances Act* speaks of "creditors or others," while s. 4(1) of the *Assignments and Preferences Act* speaks only in terms of "creditors."

(ii) Non-Judgment Creditors

The general position has been referred to by Edwards (ed.), *May on Fraudulent and Voluntary Conveyances*, (3rd ed. London: Stevens, 1908), where it is said (at 102):

> The words "creditors and others" are wide enough to include any person who has a legal or equitable right or claim against the grantor or settlor by virtue of which he is, or may become, entitled to rank as a creditor of the latter.
>
> The claim may arise out of a tort as well as out of a contract express or implied, or other legal obligation.

For example, a conveyance may be made to avoid anticipated civil liability.

FERGUSON v. LASTEWKA

[1946] O.R. 577, [1946] 4 D.L.R. 531 (Ont. H.C.)

LEBEL J.:—The plaintiff is an execution creditor of the defendant Michael Lastewka for $12,075 and costs. She seeks to set aside, as fraudulent and void against her and other creditors, a conveyance dated 3rd July 1944, made by the said defendant to his daughter and her husband, the other defendants. The plaintiff's judgment, on which execution remained wholly unsatisfied at the time of the trial, was recovered in an action instituted on 21st November 1944, for damages sustained in a motor car accident as a result of which the plaintiff was seriously injured and her husband was killed. The motor accident occurred on 3rd April 1944.

The circumstances under which the defendant Lastewka acquired the lands described in the impeached conveyance, and later conveyed them to his co-defendants, are these:

In the early summer of 1943, all the defendants resided in Montreal. With a view to purchasing a farm in the Niagara district, Lastewka sold his home in Montreal. He was then indebted to the defendant Andrew Ewaschuk in the sum of $1,500, but he arranged with Ewaschuk that the latter should accept his promissory note for the amount of the debt, without interest, maturing 1st July 1944. On 14th August 1943, Lastewka purchased fifteen acres in Lincoln County, being part of a fruit farm owned by one James A. Johnson. He paid $2,000 in cash and gave Mr. Johnson a mortgage for $2,200, the balance of the purchase price. In erecting a house and barn on the property, and in commencing his farm operations, he said, he used up all his available cash. In November 1943 he borrowed $500 from a bank, and he swore that he secured loans from a sister amounting in all to $300, and incurred other debts. On 3rd July 1944, the date of the disputed conveyance, besides the mortgage indebtedness and the Ewaschuk note, he said on his examination for discovery, which was read in as part of the plaintiff's case, he owed in the neighbourhood of $1,350 to the bank and the others. Soon after Lastewka's purchase of the fruit farm the Ewaschuks visited him there and they became interested in acquiring property in the vicinity for themselves. That such might be their decision was suggested in a letter the defendant Milly Ewaschuk wrote to her mother as early as 1st August 1943. In another letter, dated 8th February 1944, Milly Ewaschuk told her mother that she and her husband had a prospective buyer for their Montreal house, and that they were interested in the farm adjoining the Lastewkas', *i.e.*, Mr. Johnson's. She also said they would like to obtain payment of the promissory note, or at least $1,000 on account. The Ewaschuks completed the sale of their Montreal house, Milly Ewaschuk swore, a few days before they heard of the motor car accident. On 1st and 2nd May 1944 their furniture was moved from Montreal to the Lastewka farm. The Ewaschuks followed in the same month. Andrew Ewaschuk interviewed Mr. Johnson with a view to buying his farm, but the price was apparently too high. Ewaschuk also looked at some other farms in the vicinity before returning to Montreal to secure a National Selective Service release from his employment in a war plant there. He testified that up to the time that he returned to Montreal for this purpose he had no intention of purchasing his father-in-law's farm. After securing the release

mentioned, Ewaschuk returned to the Lastewkas' farm, but in the meantime, on 21st June 1944, Lastewka had been convicted of an offence related to the operation of his motor vehicle involved in the accident, and he was now serving a three months' sentence in the Ontario Reformatory at Guelph. Ewaschuk swore that his mother-in-law then informed him that her husband had decided to sell the farm and would give him the first chance to buy. On his examination for discovery (Q. 166, also read in as part of the plaintiff's case) Ewaschuk swore that his mother-in-law had said that the price was $5,400. Ewaschuk then sought the advice of Thomas R. BeGora, a solicitor of this court in St. Catharines, and a few days later instructed him to draw a deed from Lastewka to himself and his wife as joint tenants, in consideration of the amount mentioned. Mr. BeGora prepared the deed but did not fill out the land transfer tax affidavit because he did not know all necessary details. The deed as drawn, however, included a covenant for the assumption of the Johnson mortgage. On 3rd July 1944, Mr. BeGora, Andrew Ewaschuk, and a man named Baraniuk, drove to Guelph and interviewed Lastewka in the reformatory. Lastewka testified that at this interview he told Ewaschuk that if he paid him $2,000, the equivalent of the amount he himself had paid down on the purchase of the farm, assumed the balance owing on the Johnson mortgage, *viz.*, $1,900, and returned his promissory note for $1,500, he could have the farm. These amounts total the consideration said to have been mentioned by Mrs. Lastewka. Mr. BeGora then filled in the land transfer tax affidavit and Lastewka executed the deed and handed it back to Mr. BeGora. The document was signed later by the Ewaschuks and by Mrs. Lastewka. Ewaschuk returned the promissory note to Mrs. Lastewka, and, as directed by her husband, gave her his cheque for $2,000 some days later. Out of the proceeds of this cheque, it was said, the bank and all Lastewka's existing creditors were paid off, and Lastewka's wife swore that she afterwards deposited the balance in her own bank account.

The plaintiff alleges that the impeached conveyance was executed and delivered in pursuance of a fraudulent scheme "for the purpose of defeating, defrauding and delaying the Plaintiff and other creditors", and Mr. Lancaster argued that the Court should find that the consideration set up by the defendants in support of the transaction was illusory and inadequate, and in any event that there was an intention on the part of the defendants to defraud the plaintiff and Lastewka's other creditors. Mr. Schreiber contended that the sale to the Ewaschuks was for valuable consideration, and argued that these defendants were as much entitled to take advantage of Lastewka's financial embarrassment, and the predicament he found himself in, as a result of the accident, as a stranger would be entitled to do; in effect that the purchase of the farm by the Ewaschuks was for valuable consideration and was *bona fide*.

I am unable to accede to the plaintiff's contention that the consideration paid by the Ewaschuks was illusory or inadequate. I find as a fact that Lastewka owed Andrew Ewaschuk the sum of $1,500, that Ewaschuk assumed the balance owing on the Johnson mortgage, and that he paid Mrs. Lastewka on her husband's instructions the balance of the purchase price, *viz.*, $2,000. As a result, I find that the impeached conveyance was given for valuable and adequate consideration, and I conclude, as counsel for the plaintiff conceded at the close of his argument, that to succeed the plaintiff must establish an actual and express intent to defruad creditors on the part of Lastewka, and that the Ewaschuks were privy to such intent: see *Hickerson v. Par-*

rington (1891), 18 O.A.R. 635 at 640-41; *May on Fraudulent Conveyances*, 3rd ed. 1908, p. 62; and *Cadogan et al. v. Kennett et al.* (1776), 2 Cowp. 432, 98 E.R. 1171.

....

The circumstances so far related show that it was within the knowledge of all the defendants that while the damage action was not commenced for some seven months following the date of the impeached conveyance — due to the nature of the plaintiff's injuries and her long hospitalization — the accident occurred four months earlier; also, that just prior to the date of the disputed instrument, Lastewka was convicted of an offence in connection with the accident, and was in custody as a result.

The plaintiff's counsel relied upon these factors, as well as on others to be mentioned, as proof of actual fraud, and urged that the conveyance was delivered *pendente lite*, in effect, if not in fact, as a mere scheme or trick to defeat creditors and the plaintiff in particular.

In *Cadogan et al. v. Kennett et al.*, *supra*, Lord Mansfield C.J. said: "So, if a man knows of a judgment and execution, and, with a view to defeat it, purchases the debtor's goods, it is void: because, the purpose is iniquitous. It is assisting one man to cheat another, which the law will never allow."

I am satisfied that the principle enunciated by Lord Mansfield is equally applicable in cases where a creditor has not recovered judgment at the date of the impeached conveyance, but the purchaser, knowing of the creditor's pending or likely action, purchases the debtor's property with a view to defeating the expected execution: see *Gurofski v. Harris et al.* (1896), 27 O.R. 201, affirmed 23 O.A.R. 717; *Hopkinson v. Westerman* (1919), 45 O.L.R. 208, 48 D.L.R. 597; May, *op. cit.*, p. 102; *McMullen v. Dr. Barnardo's Homes National Incorporated Association* [(1924), 26 O.W.N. 168]; *Goyan v. Kinash and Kinash*, [1945] 1 W.W.R. 291, [1945] 2 D.L.R. 749; *Barling v. Bishopp* (1860), 29 Beav. 417, 54 E.R. 689; and *Edmunds v. Edmunds*, [1904] P. 362.

A careful consideration of the evidence and the exhibits, in the light of the principles mentioned, has satisfied me that Lastewka conveyed his farm intending to defraud his creditors, and the plaintiff in particular, and that Andrew Ewaschuk and Milly Ewaschuk, on a lesser scale, were parties to the fraud. I am satisfied that the plaintiff has discharged the onus upon her in this regard.

....

I should not conclude my reasons without adding that I am satisfied that Mr. BeGora was in no way privy to the fraud of the defendants. The advice he gave Ewaschuk was sound, and he was not present during the conversation between Lastewka and Ewaschuk which preceded execution of the conveyance by the former, and which Baraniuk overheard in part at least. The whole incident, however, is illustrative of the fact that solicitors, in circumstances suggestive of possible fraud, must be extremely watchful of their own position in the matter. It should be mentioned, too, that the solicitor for the Ewaschuks waived any question of privilege in so far as Mr. BeGora's evidence was concerned, and none was claimed by Lastewka.

The plaintiff's action succeeds and there will be judgment declaring that the conveyance from the defendant Michael Lastewka to his co-defendants (20535 for the Township of Grantham) is null and void against the plaintiff and other creditors of Michael Lastewka. The plaintiff is entitled to her costs.

COMMENTARY

10.19. Compare with *Ferguson v. Lastewka* the cases of *Ex parte Mercer*, reproduced *supra*, and *Mandryk v. Merko*, reproduced *supra*. Note that spouses seeking maintenance have been held to be "others" within the phrase "creditors or others" in s. 2 of the *Fraudulent Conveyances Act*, and may therefore seek to have conveyances set aside: *Shephard v. Shephard* (1925), 56 O.L.R. 555 (Ont. C.A.); and *Murdoch v. Murdoch* (1976), 1 Alta. L.R. (2d) 135 (Alta. T.D.). The B.C. Working Paper stated that the "phrase 'creditors and others' extends standing to anyone with any type of claim, including unliquidated claims...for the division of matrimonial property" (at 30; see cases cited in note 85).

10.20. In some cases, courts have held that persons with unliquidated claims are not "creditors" and can bring their actions only upon recovering judgment: see *Cameron v. Cusack* (1890), 17 O.A.R. 489 at 493 (Ont. C.A.).

Persons with unliquidated claims are not regarded as "creditors" with standing to impeach a transaction under the *Assignments and Preferences Act*: see *Ashley v. Brown* (1890), 17 O.A.R. 500 (Ont. C.A.); and *Gurofski v. Harris* (1896), 27 O.R. 201 (Ont. H.C.); affirmed (1896), 23 O.A.R. 717 (Ont. C.A.). Only creditors existing at the time of the transaction can impeach it.

10.21. In *Re Ridler* (1882), 22 Ch. D. 74 (C.A.), the defendant was potentially liable on a guarantee. It was held that a creditor of the person whose debts are guaranteed may sue the guarantor to impeach a conveyance by the guarantor. Cotton L.J. stated as follows (at 82):

> Then as to the point that the settlor was not indebted, but only subject to a liability which might never become a debt. A man is not at liberty to take a sanguine view, but is bound to act upon a reasonable view of what is likely to happen. In the circumstances of this case, any reasonable man must have looked upon his guarantee as one which would probably be enforced, and the settlement must be taken as made with intent to delay or hinder creditors.

See also *Re Whetstone* (1984), 12 D.L.R. (4th) 249 (Ont. S.C.).

10.22. In many cases, there is no explicit consideration of the relationship between the debtor's intent and the likelihood of the claim in question being pressed to a successful conclusion. It is reasonable to assume, however, a very close relationship. Where the claim is so remote or frivolous or highly speculative that it virtually has been forgotten by the debtor, it may be inferred that he had no fraudulent intent. On the other hand, where the claim is likely to bear fruit for the claimant, it may be inferred that a conveyance of property was made for a fraudulent purpose. See *Ferguson v. Lastewka*, reproduced *supra*; *Re Ridler, supra*; and *Gurofski v. Harris* (1896), 27 O.R. 201 (Ont. H.C.).

10.23. With respect to standing, see *Van Der Haas v. Van Der Haas*, unreported, May 11, 1984 (Ont. H.C.). In that case, a separation agreement stipulated that the husband was to pay certain specified amounts for support of his wife and children. The husband was in arrears and subsequently conveyed property to a third person. At 15, Mr. Justice Webber stated:

> Although Mrs. Van Der Haas has not obtained a judgment for any of the sums found to be outstanding, there is in my view clearly liability for these sums, pursuant to the separation agreement. In view of these facts and the authorities mentioned, I have no difficulty in determining that Mrs. Van Der Haas does fall withing the words "creditors or others".

SEMBALIUK v. SEMBALIUK

(1983), 27 Alta. L.R. (2d) 223, 35 R.F.L. (2d) 415 (Alta. Q.B.)

MILLER J.:—

....

Effect of the Fraudulent Preferences Act on a disclaimer

Only s. 1 of the Act need be considered. It reads as follows:

> 1. Subject to sections 6 to 9, every gift, conveyance, assignment, transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made
>
> (*a*) by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency, and
>
> (*b*) with intent to defeat, hinder, delay or prejudice his creditors or any one or more of them, is void as against any creditor or creditors injured, delayed or prejudiced.

This section cannot assist Mrs. Sembaliuk, for a disclaimer is not a "gift, conveyance, assignment, transfer, delivery over or payment" as those words are used in s. 1 of this Act.

Nor is it clear in these circumstances that Mrs. Sembaliuk is a "creditor". The definition of "creditor" given in s. 5 of this Act is of no avail to Mrs. Sembaliuk as this definition applies only to ss. 2 through 4 and not to s. 1. In *Murdoch v. Murdoch* , 1 Alta. L.R. (2d) 135, [1977] 1 W.W.R. 378, 26 R.F.L. 1, 1 A.R. 378 (T.D.), a similar situation arose. Bowen J. received the position of Mrs. Murdoch when Mr. Murdoch conveyed some land to his son at a time prior to the *decree nisi*, but after the divorce petition was issued. Bowen J. stated (at p. 5) there was no evidence that Mrs. Murdoch was a creditor of Mr. Murdoch at the time of the transfer. In this case there is no evidence that Mrs. Sembaliuk was a creditor of Mr. Sembaliuk at the time when the disclaimer was made. The reasons for the actions taken in both cases are so similar that it makes it very difficult to call Mrs. Sembaliuk a creditor under the *Fraudulent Preferences Act*.

The *Fraudulent Preferences Act* affords Mrs. Sembaliuk no remedy.

Effect of the Statute of Elizabeth on a disclaimer

The first question to resolve is whether any or all of this ancient English statute is still in force in the province of Alberta?

In a 1945 decision H.J. MacDonald J. of the Supreme Court of Alberta [*Goyan v. Kinash*, [1945] 1 W.W.R. 291, [1945] 2 D.L.R. 749] reviewed the question of whether the enactment of the *Fraudulent Preferences Act*, R.S.A. 1922, c. 149, and subsequent amendments, superseded the Act of 13 Elizabeth which came into force in Alberta in 1905. He stated at p. 295:

> I am holding that secs. 1 and 2 of 13 Eliz., ch. 5, are in force in Alberta irrespective of the fact that the 1942 revision of our statutes may have repealed the 1923 amendment to *The Fraudulent Preferences Act*, R.S.A. 1922, ch. 149.

This decision was followed by our Appellate Division in *T.D. Bank v. Michael*, [1973] 1 W.W.R. 656, 32 D.L.R. (3d) 498, which applied the statute. It was again used by Bowen J. in *Murdoch v. Murdoch*, *supra*.

I am satisfied that, at least ss. 1 and 2 of this statute are still in force in this province.

The next question to determine is whether Mrs. Sembaliuk is of a class of persons who can claim any protection under 13 Eliz., c. 5?

It is interesting here to reproduce the colorful language of s. 1 of the statute which reads as follows:

> For the Avoiding and Abolishing of feigned, covinous and fraudulent Feoffments, Gifts, Grants, Alienations, Conveyances, Bonds, Suits, Judgments and Executions as well of Land and Tenements as

> of Goods and Chattels, more commonly used and practised in these Days than hath been seen or heard of heretofore; which Feoffments, Gifts, Grants, Alienations, Conveyances, Bonds, Suits, Judgments and Executions, have been and are divised and contrived of Malice, Fraud, Covin, Collusion or Guile, to the *End, Purpose and Intent, to delay, hinder, or defraud Creditors and others* of their just and lawful *Actions, Suits,* Debts, Accounts, *Damages,* Penalties, Forfeitures, Heriots, Mortuaries and Reliefs, not only to the Let or Hinderance of the due Course and Execution of Law and Justice, but also to the Overthrow of all true and plain Dealing, Bargaining and Chevisance between Man and Man without which no Commonwealth or civil society can be maintained or continued. [The italics are mine.]

While the *Fraudulent Preferences Act* uses only the term "creditor" in s. 1(*b*) it is noted that 13 Eliz., c. 5, refers to "creditors and others".

May's Law of Fraudulent and Voluntary Conveyances, 3rd ed. (1908), p. 102, comments on this usage in the following passage:

> The statute 13 Eliz. c. 5, is expressed to be to avoid conveyances & c., "to delay, hinder, or defraud creditors and others of their just and lawful actions, suits, debts, accounts, damages, penalties, forfeitures, heriots, mortuaries, and reliefs."
>
> The words 'creditors and others' are wide enough to include any person who has a legal or equitable right or claim against the grantor or settlor, by virtue of which he is, or may become, entitled to rank as a creditor of the latter. The claim may arise out of a tort, as well as out of a contract, express or implied, or other legal obligation.

Bowen J., after noting the above quotation from May went on in *Murdoch v. Murdoch*, *supra*, at pp. 5–6 to make the following comment:

> While there is no evidence that the wife at the time of the transfers was a creditor within the provisions of the section, I am of the view that she can rightly be included in the category of 'others' as set out in the section. Further, at the time of the transfers her counterpetition for divorce and maintenance was extant having been filed on 4th December 1973. This gave her a claim against the husband within the meaning of the section, a claim of which the husband was well aware as shown by his evidence. It is to be noted also that the learned author speaks of a claimant that "may" become entitled to rank as a creditor, thus expressly contemplating a claimant who, while not a creditor at the time of the conveyance, may become one in the future.

I am satisfied that Mrs. Sembaliuk, in the circumstances of this case, is covered by the phrase "creditors and others" and has status to claim whatever protection the statute of 13 Eliz. provides.

....

[See Commentary 10.01.]

(iii) Secured Creditors

Should a creditor who has security by way of pawn, pledge, mortgage or otherwise be entitled to impeach a transaction under the *Fraudulent Conveyances Act*? What if the property secured is not sufficient to satisfy the debt owing to him? In such a case, should the secured creditor be a "creditor" under the Act to the extent of the deficiency? See *Arnold v. Fleming*, [1923] 1 W.W.R. 706 (Alta. S.C.); *McLean v. Ratekin*, [1926] 2 W.W.R. 671 (Sask. C.A.); and *Sun Life Assurance Co. v. Elliott* (1900), 31 S.C.R. 91 (S.C.C.).

In *Crombie v. Young* (1894), 26 O.R. 194 (Ont. C.A.), the debtor made a voluntary settlement subsequent to the mortgage and when he was financially sound. The mortgagee was satisfied that the value of the mortgaged property was considerably in excess of the loan. However, at the date the mortgage matured, the real estate market

had fallen to the extent that the secured creditor no longer was fully secured. The settlement was upheld, and MacMahon J. considered (at 202) the question whether a solvent debtor could make a voluntary settlement where the mortgagee believed the security to be satisfactory:

> If at the time a mortgage is given payable, say in five years, the mortgaged property is regarded by both the mortgagor and mortgagee as ample security for the mortgage debt; then if the mortgagor cannot make a voluntary settlement (although otherwise financially in a position so to do), because he may possibly become a debtor to the mortgagee by reason of the depreciation of the mortgaged property, just before the expiration of the five years, the argument must hold good as to a mortgage having ten years to run, and a like result happening.

The notion that secured creditors are not "creditors" or "others" unless the security is insufficient (see Dunlop, at 528, *n*. 34) has apparently been viewed as too narrow by Kerr ("Fraudulent Conveyances and Unjust Preferences", in Springman and Gertner, 191). At 207, Kerr stated:

> Because of the possibility that the security will become inadequate or that the secured creditor may sue on the covenant to pay, a secured creditor presumably qualifies as a future creditor under the *Statute of Elizabeth* model. A transaction intended to defeat a secured creditor in the event of such contingencies should be voidable under that legislation. Mechanics' lien claims have been held to be protected by the legislation, at least pending enforcement of the lien, because of the uncertainty as to the validity of the lien at this stage. The same reasoning might be applied to most other statutory liens.

In a footnote (*n*. 87, at 207), Kerr further stated:

> The decisions in *Crombie v. Young* (1894), 26 O.R. 194 (H.C.), and *Royal Bank of Canada v. Dunsmuir* (1978), 85 D.L.R. (3d) 549, 5 R.P.R. 74 (B.C.S.C.), are contrary to this position, since both indicate that a creditor's security must be inadequate at the time of the voidable transaction to enable the secured creditor to set it aside. The case of *Crombie v. Young* can be distinguished. The adequacy of the security at the time of the challenged conveyance combined with other circumstances to persuade the Court that there was no improper intent. The time of the conveyance is, of course, the relevant time for assessing the debtor's intent, whether that intent is directed to existing or future creditors. However, this does not dispose of a case where the intent to defeat the secured creditor can be shown at the relevant time.
>
> The Court in *Royal Bank of Canada v. Dunsmuir* proceeds on the basis that the status of a secured creditor under the *Statute of Elizabeth* model is the same as under the assignments [that is, the *A.P.A.*] model. A contemplated future creditor cannot rely on the latter legislation. However, since the *Statute of Elizabeth* model protects future creditors, the Court is in error when it says the position is the same under this legislation.

The B.C. Working Paper said that the "burden lies on the creditor to prove his security inadequate and to rebut the presumption of adequacy which applies" (at 30).

C.I.B.C. v. BOUKALIS

(1987), 11 B.C.L.R. (2d) 190 (B.C.C.A.)

SEATON J.A. (for the Court):—At issue in this appeal is whether one who is not an unsecured creditor at the time of a conveyance has status to challenge the conveyance under the *Fraudulent Conveyance Act*, R.S.B.C. 1979, c. 142.

In the action the Canadian Imperial Bank of Commerce seeks to set aside a second mortgage granted on June 29, 1983 by the defendant Vasilios Boukalis, to his brother,

the defendant John Boukalis, for the sum of $550,000. On June 29, 1983 Vasilios Boukalis was indebted to the Bank but the indebtedness was secured and the Bank has not shown that the security was inadequate at that time. At the time of trial, the security had proved to be inadequate and the bank had several outstanding judgments against Vasilios Boukalis.

In his reasons, the trial judge first posed this issue:

> To succeed in its action to set aside the second mortgage as a fraudulent conveyance the plaintiff must show that it was granted with intent to delay, hinder, or defraud the plaintiff as a creditor of just and lawful remedies.

After carefully reviewing the evidence, the trial judge said:

> Vasilios granted the second mortgage, impugned by these proceedings, at a time when the business of Alpine Carpets Ltd. was failing, when real estate values were falling and when his Granville Street residence, supposed to be built for $125,000, had swallowed up almost $600,000. I am quite satisfied that the mortgage figure of $550,000 was chosen to exhaust the apparent equity. So Vasilios's intent to hinder or delay the plaintiff is shown. I also find that John Boukalis had that intent in accepting the mortgage because I do not accept his evidence that Vasilios owed him that amount of money, but rather something less, and because as brothers their close relationship demands an explanation which, on John Boukalis's part, is unsatisfactory.

The trial judge concluded that that was not enough:

> There is, however, a hurdle of law which the Bank is unable to overcome in this case. It is that a creditor who was fully secured at the time of an impugned transaction is not permitted to take the benefit of the *Fraudulent Conveyance Act*. Much argument, supported by numerous authorities, was devoted to this problem by both counsel.

The trial judge concluded that the Bank had not shown that it was unsecured on June 29, 1983 and, therefore, he dismissed the action.

Counsel for the Bank conceded that there are decisions of the Supreme Court of British Columbia that support the conclusion reached by the trial judge and that there are decisions of this Court that seemed to support that result. He therefore sought and was granted a court composed of five justices of appeal to consider the question.

In the first line of authority that impelled the trial judge to say that the Bank could not succeed unless it was unsecured on June 29, 1983 there is confusion between two statutory provisions; in the second line of authority there is confusion between two steps in one proceeding.

Cases in the first group treat fraudulent conveyance questions the same as fraudulent preference questions. *Royal Bank of Canada v. Dunsmuir* (1978), 85 D.L.R. (3d) 549 (B.C.S.C.), is an example of this (at p. 553):

> The significant date for establishing the status of the secured or unsecured creditor is the date when the transaction took place, *i.e.*, the conveyance from husband to wife. I follow here with respect the judgment of my brother Anderson in *Re Ehatteshat Co-operative Enterprises Ass'n and Vancouver Equipment Corp. Ltd.* (1977), 3 B.C.L.R. 117 at p. 120, where he says:
>
> > In my view a "secured creditor" cannot bring proceedings under the Act unless at the date the preference was given there were moneys owing for which there was no security.
>
> Anderson, J., was there dealing with an application under the *Fraudulent Preferences Act*, but I agree with counsel for the defendant that the principle is the same whether the application be launched under the *Fraudulent Conveyances Act* or the *Fraudulent Preferences Act*.

The language used in the two Acts is different. The *Fraudulent Preference Act*, R.S.B.C. 1979, c. 143, s. 3 provides:

> 3. Subject to section 6, a disposition of property by a person at a time when he is in insolvent circumstances, is unable to pay his debts in full, or knows that he is on the eve of insolvency, is void as against an injured creditor, if made
> (a) with intent to defeat, hinder, delay or prejudice *creditors or some of them*; and
> (b) to or for a creditor with intent to give the creditor preference over *other creditors or some of them*.
>
> (emphasis added)

Section 1 of the *Fraudulent Conveyance Act* is not the same:

> 1. A disposition of property, by writing or otherwise, and a bond, proceeding and order, at any time made, to delay, hinder or defraud *creditors and others* of their just and lawful remedies, shall be void and of no effect as against *a person*, his personal representative and assignee *whose rights* and obligations by collusion, guile, malice or fraudulent devices and practices *are or might be*, in any way, disturbed, hindered, delayed or defrauded, notwithstanding a pretence or other matter to the contrary.
>
> (emphasis added)

The different language indicates that there is a different group to be protected, and that is consistent with the fact that the Acts have different purposes.

This part of the *Fraudulent Preference Act* deals with preferences in favour of certain creditors. A plaintiff cannot be a prejudiced creditor if he was not a creditor at the time the preference was given. The thrust of these sections is to ban the preference of one creditor over another or others. Thus, the Act refers to "creditors or some of them".

The *Fraudulent Conveyance Act* has a different thrust. It is designed to ban the disposing of property to hinder or delay creditors and those who might become creditors. Thus, the Act refers to "creditors and others".

The two Acts have similarities, but they have differences and those differences should be respected. In *Re Skinner* (1960), 27 D.L.R. (2d) 74, Wilson, J. (as he then was) dealt with an application under s. 7 of the *Fraudulent Preferences Act*, R.S.B.C. 1960, c. 156, the predecessor to the present s. 9. He distinguished between a fraudulent preference and a fraudulent conveyance (at p. 78):

> This is not an attempt by one creditor to set aside a preferential transfer to another creditor. It is a bid by a judgment creditor to set aside a conveyance as being, in the words of s. 7 "made to defeat, hinder, delay, prejudice, or defraud creditors".
>
> I can see that in the preference cases it is only logical that if one creditor is to attack a payment to another as preferential when made then he, the attacking creditor, must also have had the status of creditor at that time. If he had not, there could be no preference, because the debt to the attacking creditor did not exist at the time. Therefore it could not be said that another creditor was preferred over him.

I would adopt that reasoning and reject the reasoning in the first line of authority.

The second line of authority adopts language without respect for the context in which it is found.

The trial judge found on the evidence that there was the necessary intention to hinder or delay. In many cases that finding cannot be made except by drawing an inference from the circumstances. The inference of fraud is drawn because of the existence of creditors at the time of the conveyance. If the existing creditors are well secured one is unlikely to infer that the conveyance was made in order to defeat them. Of course, the

time for considering intent is the time of the conveyance. The cases, therefore, which are concerned with whether or not the creditors were secured at that time, are not deciding whether or not the plaintiff has status to bring the proceedings, but are deciding whether or not the impugned conveyance was made with the intent to hinder or delay. Some cases have employed language that appears to support the view that creditors to have standing must be creditors at the time of the conveyance. The context surrounding that language shows, however, that it was used in relation to intent.

Vice-Chancellor Blake detected this problem in *Reid v. Kennedy* (1874), 21 Gr. 86 (at pp. 90–1):

> Looking at the Statute alone, apart from the authorities, I should have thought its effect to be, that where an intention to defraud creditors or other persons was shewn at the time of the execution of the deed, then it mattered not whether the creditor attacking the deed existed at the time of its execution or not. In its inception the deed was fraudulent, it remained so, unless cured by some subsequent act, and was liable to be impeached by a subsequent creditor, whose potential equity has not been lost by some matter *ex post facto*. *Totten v. Douglas* [18 Gr. 341], is an instance of such an equity being lost. There is some inconsistency in the decided cases, but from them I think the opinion I have formed as above expressed is correct.
>
> In many of the cases fraud can only be inferred from the effect of the conveyance; the rule adopted being that a grantor must be taken to have intended the natural result of his act. Where there were no creditors at the time of the impeached conveyance, or all those then in existence have been satisfied, it has been frequently argued that the inference of fraud which might be otherwise drawn has been rebutted by the absence of these debts. If the grantor be insolvent at the time of the impeached conveyance, it is clear it is fraudulent and void. But why is this so? Because as there are creditors, and the effect of the instrument must be to defeat or delay, it is therefore concluded that with this intention the grantor executed it. In other words, direct evidence of the fraudulent intent is wanting; but this may be, and is inferred, and therefore the transaction can be impeached. But here, that, which in the cases referred to is inferred, is proved. The admission made by the parties shew the object they had in view was covinous, collusive, and guileful, and the result that should flow from this must be to find such conveyance "void, frustrate, and of no effect," as against a person whose action is thereby hindered, delayed, or defrauded. The words in the Act are "creditors and others," and, proving that the conveyance was tainted with fraud once, I do not think it loses this stain, but remains a conveyance with this infirmity which prevents it being set up as against a creditor whose debt arises years after the instrument was executed. The words "and others" extend the operation of the Act if the word creditors confined it to those existing when the deed was made.

The Vice-Chancellor reviewed a number of decisions that fully justified the statement he had made.

Those who would revitalize the argument rejected by Vice-Chancellor Blake rely on this sentence from the judgment of Sedgewick, J. in *Sun Life Assurance Company of Canada v. Ellen Elliott* (1900), 31 S.C.R. 91 (at pp. 95–6):

> If, however, he is a *secured* creditor, if he has sufficient of the assets of the debtor in his hands to fully cover the indebtedness, then undoubtedly the statute was not intended for him, but for the general and unsecured creditors.

The language is found in a discussion about whether or not to infer intent. The sentence is preceded by a quotation from *Freeman v. Pope* (1870), 5 Ch. App. 538, dealing with the inference of intention in the absence of direct proof of intention. It is followed by a reference to *Crombie v. Young* (1894), 26 O.R. 194, and this statement (at p. 96):

> In that case it was shewn that at the time of the impeached transaction, a donation from a husband to his wife, the settlor was perfectly solvent after the conveyance, still possessing other lands and a

large interest in the mortgaged property, far in excess of the mortgage. And it was held, whether rightly or wrongly, that under these circumstances, *any intent to hinder or delay could not be imputed to him*. As already shown the facts here are the reverse of those in *Crombie v. Young*. At the time of the impeached conveyances (and all *evidence of intent* except at that particular time is irrelevant), the mortgaged lands were probably wholly insufficient to pay the mortgage debt, and the voluntary convey-
ances themselves forever precluded the settlor from having any means of making up the shortage.
(emphasis added)

Interpreting the language of Sedgewick, J. as barring a creditor who was secured at the date of the conveyance is inconsistent with the remainder of the language used in the judgment and inconsistent with the conclusion reached by the court.

The *Crombie, supra*, judgment referred to by Sedgewick, J. dealt entirely with intent. MacMahon, J. set out why he was considering the adequacy of the security (at p. 200):

> One of the tests to apply in this case in considering whether the settlements though voluntary, are fraudulent and void, is whether *at the time of the settlements* in favour of the wife the property mortgage was insufficient to pay and satisfy the mortgage debt...

He concluded that there was no intention to defraud.

Rose, J. said (at p. 208):

> I do not, on the evidence, find it at all safe to infer that there was any intention to defraud these mortgagees when the impeached transfers were made. My mind turns the other way.

This second line of authority does not support the conclusion of the trial judge.

The conclusion is also inconsistent with the interpretation of the Act found in other cases. The suggestion that a creditor secured at the time of the conveyance is forever barred from claiming under the Act is inconsistent with the cases that say that a subsequent creditor, a person not a creditor at the time of the conveyance, may claim under it. No reason has been offered why an unsecured creditor who was a secured creditor at the time of the transaction has no status, whereas an unsecured creditor who was not a creditor at all at the time of the transaction has status.

A conveyance can be set aside even if there were no creditors when it was made. The judgment of Macdonald, C.J.A. in *Newlands Sawmills Limited v. Bateman and Bateman* (1922), 31 B.C.R. 351, concisely sets out the facts and the decision of this Court (at p. 354):

> This action was brought to set aside a conveyance by James Edward Bateman to his wife, Minnie Bateman, of a farm, being the principal item of the assets of the grantor, on the ground that the same was made to defeat the plaintiff, which subsequently became the creditor of Bateman.
>
> Just previous to the date of the conveyance Bateman had entered into a contract with the plaintiff to cut and boom logs. The contract was rather an extensive one, considering the financial position of the defendant Bateman, and was, in my opinion, a hazardous one within the meaning of that term as used in cases of this kind. It is to be noted that the contract calls for the commencement of logging operations on the 10th of May, 1920, and that the conveyance in question in this action was made on the 22nd of May of the same year.
>
> The submission of counsel for the defendants was that as Bateman had no creditors at the time he entered into the contract he was entitled to make a voluntary conveyance to his wife of the property in question. The authorities to which we were referred do not sustain this contention. It is a question to be decided upon the proper inference to be drawn from the facts and circumstances of the particular case as to whether there was an intention to defeat creditors or not, and if there was the intention to defeat creditors, then it does not matter whether it was to defeat present or future creditors.

I conclude that it was not an essential step in the action for the Bank to prove that it was an unsecured creditor at the time of the conveyance.

The trial judge felt bound by the decision of this Court in *Bank of Nova Scotia v. Scott and Scott* (1985), 67 B.C.L.R. 145. The only issue argued there was whether or not the Bank was a secured creditor. This Court concluded that it was. The issue now before the court was not raised. The *Scott* case is not authority for the proposition that a creditor secured at the time of the conveyance cannot have recourse to the *Fraudulent Conveyance Act*. To the extent that it may imply that that is so, and to the extent that other cases such as *Royal Bank of Canada v. Dunsmuir et al., supra*; and *Delbreuck & Co. v. Muenzenberg et al.* (1984), 54 B.C.L.R. 264 (B.C.S.C.) so hold they should be considered overruled.

....

[Appeal allowed]

(iv) Creditors Arising Subsequent to the Impugned Transaction

See Walden, "Creditors' Rights: Conveyances in Fraud of Subsequent Creditors" (1952), 40 Ky. L.J. 433 at 437:

> The ease of proving fraud, an issue in every fraudulent conveyance case, has brought about a difference in the rights of the two principal types of claimants. It is easy to see why this is true. The task of showing the effect of a debtor's diminution of his present estate upon his ability to meet existing obligations is relatively simple. But once the transaction is completed, it is much more difficult to connect it with some future liability. If the subsequent debt arose a great length of time afterward, the connection is especially difficult to show. Something must be found which justifies the statement that the debtor intended to injure the future creditors.

GAUTHIER v. WOOLLATT

[1940] 1 D.L.R. 275 (Ont. H.C.)

ROACH J.:—In an action in this Court in 1934 the late C. Harold Gauthier obtained judgment against the defendant William R. Woollatt, his father, and two brothers for $25,000 and interest and costs upon a promissory note made by them in his favour dated January 22, 1926, and which became due on January 25, 1929. There remains unpaid on the judgment approximately $23,000. The said note was collaterally secured by,

First — an assignment by way of mortgage from William R. Woollatt to Gauthier of the former's two-fifths interest in certain lands in the City of Windsor referred to during the trial as the Zakoor property.

Second — A first mortgage from Woollatt's father covering the latter's home in the Town of Walkerville.

Third — an assignment of the father's interest in certain lands in the Town of Amherstburg.

In 1927 the defendant William R. Woollatt had purchased or agreed to purchase certain farm lands in the Township of Anderdon in the County of Essex. Those lands consisted of two parcels. The vendor of one was a man named Janisse and the purchase-price was $6,850. The vendor of the other was a man named Scarfe and the purchase-price was $13,000. By December, 1928, the purchase-price of both parcels

had been paid in full and by deed dated December 10, 1928, Janisse, on the instructions of Woollatt, conveyed the one parcel to the latter's wife, the defendant Mabel Alice Woollatt, and by deed dated December 21, 1928, Scarfe on similar instructions conveyed the other parcel to the defendant Mabel Alice Woollatt.

In this action the plaintiff asks a declaration that the defendant Mabel Alice Woollatt held the said lands in trust for her husband on the ground that he caused the title thereof to be placed in her name to defeat, hinder or delay his creditors.

In 1924 the Molsons Bank recovered judgment in an action in this Court against the defendant W.R. Woollatt and others in the sum of $46,193.63. A writ of *fieri facias* was filed with the Sheriff of the County of Essex against all the judgment debtors on January 16, 1924, was withdrawn on December 31, 1925, was refiled on the same day, was subsequently renewed and was finally withdrawn on February 18, 1929.

The defendants deny the allegation of fraud and plead that the said lands were conveyed to the wife as a gift from her husband. The defendant wife had no funds of her own and the full purchase-price of these lands were paid by the husband.

The husband was examined as a judgment debtor on January 13, 1936, and the following are some of the questions and answers from that examination:

> Q. You have given us all the real estate? A. I can't remember anything else at all. The farm out here is Mrs. Woollatt's because it was bought while that judgment was on. Q. Where is that farm? A. Out on the Huron line... Q. How many acres in the farm? A. One hundred. That is the farm I bought in '27. Q. You paid the purchase-price for it did you? A. Yes. Q. How much? A. $20,000. Q. You took it in Mrs. Woollatt's name? A. Yes.

The plaintiff did not call any witness to prove the amount, if any, remaining unpaid on the judgment in favour of the Molsons Bank at the date of the conveyances in question. Counsel for the defendants cited *Dancey v. Brown* (1914), 19 D.L.R. 862, 31 O.L.R. 152. At p. 866 Mulock C.J.Ex. (as he then was) states: "The recovery of judgment, and the evidence of the Clerk of the Division Court that a writ of execution had been placed in the bailiff's hands, does not, as against a person not a party to that action, prove that the debt is still unpaid." That was a case in which the plaintiff was a creditor whose claim arose subsequent to the making of a voluntary conveyance and he was relying upon prior claims alleged still to be in existence and unpaid. I suppose, in so far as proving any balance owing, there is no distinction between the probative value of an execution in the hands of a bailiff and one in the sheriff's hands. It is the amount due on the execution in the sheriff's hands which is a lien on the lands of the execution debtor.

Paraphrased, Woollatt's answer on his examination was: "I put that property in my wife's name to prevent the execution in favour of the Molsons Bank attaching to it." That statement would be evidence against the husband only; but where the conveyance is voluntary it is only necessary to show fraudulent intent on the part of the donor. *Oliver v. McLaughlin* (1893), 24 O.R. 41.

The defendants called one Loveridge as a witness. He and Woollatt owned as tenants in common a real estate sub-division near the City of Windsor. They were selling lots in this sub-division. He says: "The bank (i.e. the Molsons Bank) held us up in giving deeds in our sub-division. In January, 1927, I took over Woollatt's one-third interest in the sub-division and gave the bank my note for approximately $20,000 which I paid off in monthly payments over a two year period. In 1929 Woollatt

redeemed his one-third interest by paying me approximately $20,000." From other evidence it is clear that this money came from the sale in January, 1929, of the assets and undertaking of a company in which Woollatt was a substantial shareholder. This explains the withdrawal of the execution on February 18, 1929.

In my view the proof which was lacking in *Dancey v. Brown, supra*, exists in the case at bar.

Counsel for the defendants next argued that the plaintiff is not a creditor entitled to avail himself of the statute (the *Fraudulent Conveyances Act*, R.S.O. 1937, c. 149) because, at the times of the settlements he held security. In my opinion much depends on the selling value of the security at the date of settlement.

I find as a fact on the evidence that as of the dates of the conveyances in question the then selling value of the securities was greater than the debt. Due to shrinkage in values of real estate this is no longer the case. In fact the debtor subsequently released to the creditor all his interest in one of the securities *viz.* the Zakoor property, on account of the debt, and the selling value of the remaining security is only about one-third of the balance owing on the debt.

....

There is no evidence that as of the date of the institution of this action there remained unpaid any debts which were owing at the date of the last conveyance in question, except the debt owing to Gauthier. That debt was not then due and at that time was amply secured. Because of the sufficiency of his security this plaintiff at that time could not have impeached the conveyances in question because he was not then damnified. In this respect the present case differs from the case of *Sun Life Ass'ce Co. v. Elliott* [(1900), 31 S.C.R. 91], and *Smith v. Robertson* [[1936] 1 D.L.R. 505 (Ont. C.A.)]. The plaintiff was not then such a creditor as the statute was designed to protect. By reason of shrinkage in value of real estate he has since become a creditor within the meaning and purpose of the statute. In this respect he is a subsequent creditor.

As I read the cases a subsequent creditor may in certain circumstances successfully impeach a fraudulent conveyance. Those cases, speaking generally, fall into two classes:

First — Those in which a subsequent creditor impeaches the conveyance while there still remains unpaid a creditor whose claim existed at the date of the conveyance in question.

Second — Those in which the purpose of the settlor was, by such conveyances, to put his assets beyond the chances and uncertainties of the business in which he was then engaged or into which he then contemplated venturing, that is the settlor's purpose was to defraud or hinder creditors generally. In these cases it is not necessary that, at the date of the commencement of the action, there should remain unpaid a debt which was owing at the date of the impeached conveyance.

Cases falling within the second class include *Mackay v. Douglas* (1872), L.R. 14 Eq. 106, and in our own Courts *Ferguson v. Kenny* (1889), 16 O.A.R. 276, and *Ottawa Wine Vaults Co. v. McGuire* (1912), 8 D.L.R. 229, 27 O.L.R. 319 (affd. 13 D.L.R. 81).

The present case does not come within either of the foregoing classes.

May on Fraudulent and Voluntary Conveyances, 3rd ed., p. 43, speaks of a third

class as follows: "If the conveyance has been made with the actual intention of delaying, hindering or defrauding the grantor's existing creditors and although subsequent creditors do not appear to have been in his contemplation at the time it seems that the conveyance will be void as against subsequent creditors who are delayed, hindered or defrauded as a necessary result of the conveyance even though, in the meantime, the claims of existing creditors have been satisfied."

I have not found any reported case the decision in which rested on this proposition.

....

In the absence of decided authority to the contrary, it would seem to me that a settlor who, in embarrassed financial circumstances, makes a settlement admittedly for the purpose of protecting the property thereby settled against the claims of existing creditors, purges his fraud by paying those creditors, provided, of course, that, in paying them, he does not substitute new creditors for the old ones. Even though his earlier generosity had been at the expense of his justice toward his creditors, having paid those creditors and thereby discharged his legal and moral obligation to them and having none others in contemplation, is the conveyance to be forever regarded as contaminated? In my opinion this is not so. By a turn in the wheel of fortune the settlor, instead of wincing under the pinch of financial distress, may become fabulously wealthy. He still desires that the beneficiary of his earlier generosity should enjoy the gift. It it is tainted what could or should the settlor do to purify it? Is he to cause it to be reconveyed to himself and then, simply because he is now in a position to make the gift without any suggestion of fraudulent intent being imputed to him, make a new conveyance thereof to the beneficiary? These would be idle motions and, because they are lacking, is the gift in the hands of the beneficiary to be subject to attack by a subsequent creditor in the event that evil days again overtake the settlor? I do not think that was the purpose or intent of the statute.

In my view of the evidence those are the circumstances in this case. The settlor acquired a large amount of cash shortly after the date of the impeached conveyances and paid off the Molsons Bank debt and there is no suggestion that there were any other debts. From January 10, 1929, to May 10, 1929, Woollatt received over $100,000 in cash out of the realization of other assets.

The note held by Gauthier matured on January 25, 1929. Gauthier did not demand payment. Instead he and Woollatt together on February 13, 1929, embarked on a new venture, the purchase of what was referred to in evidence as the Thompson property, involving a very substantial cash investment by each of them.

I do not attribute any bad faith to Mrs. Woollatt. I think she understood her husband was making a gift of this property to her and she accepted it as such.

For the reasons stated the plaintiff's action fails and is dismissed with costs.

MACKAY v. DOUGLAS

(1872), L.R. 14 Eq. 106, 41 L.J. Ch. 539

SIR R. MALINS, V.C.:—This case raises as important a question, probably, on this branch of the law as has ever been brought before the Court.

The circumstances are very simple. Mr. *Douglas* had been for some years a clerk

in various mercantile houses, and in the autumn of 1863 was a clerk to a firm carrying on business in *London, Liverpool,* and *Calcutta*, under the names of *William Grant & Co., James Smith & Co.*, and *Grant, Smith, & Co.* His salary, which was for some time £200 a year, had latterly been raised to £500.

In the latter part of the year 1863 his employers were engaged on a very large scale in speculations in jute, which is an article subject to very considerable variations in price. These speculations, which I think were of reckless and unjustifiable character, were to some extent carried on by the aid of Mr. *Douglas*, and it is not attempted to be denied that he was to some extent interested in the result of them. The Plaintiffs say that he was interested jointly as a partner, and certainly there is a passage in Mr. *Smith's* evidence which seems to sustain that view.

But, though I do not intend to rest my conclusion on any such grounds, it is not unimportant to observe that for several months before the settlement in question was made he was certainly, either on his own account or on account of the firm whose servant he was, engaged in these reckless speculations in jute. In this state of things the firm was carrying on business in *London* and *Liverpool*, and in connection with some other persons in *India*. Of the English partners it is only necessary to refer to Mr. *Smith* and Mr. *Grant*. Proposals had been made for the retirement of Mr. *Grant*, and this business was to be carried on by Mr. *Smith* alone, or with such persons as he should think proper to take into partnership with him. It is perfectly plain, for it is shewn under the hand of Mr. *Douglas* himself, that he entertained the expectation of going into partnership with Mr. *Smith*, his employer, if Mr. *Grant* retired. That is very distinctly shewn in a letter so early as the 11th of September, 1863, written by Mr. *Douglas* to Mr. *James Smith*. It gives the particulars of some purchases of jute and so forth, and then he says: —

[His Honour then read the passage in the letter above set out, and continued:]

So matters went on, and in October, the very next month, Mr. *Douglas*, who in the course of his clerkship had amassed a sum of money which he says amounted to about £3000 or £4000, but which I cannot make out amounted to so much, entered into this transaction. He was a married man, having at the time no child, but in the progress of this business the first child of the marriage was born, and on the 8th of October, 1863, while it appears that he certainly had it in his mind as a probable event that he would go into partnership with his employer Mr. *Smith*, he entered into a contract to purchase a leasehold house, which is the subject of this suit. The contract was on the 30th of October, and the purchase was completed by an assignment to himself on the 2nd of November. All was right so far, and nobody can complain of that part of the transaction. But while he was carrying on the negotiation for the partnership, on the 19th of January, he saw his solicitor, and talked of making, but did not give him positive instruction to make, a settlement of the leasehold house, which was worth from £1500 to £1800. On the 12th of February, 1864, he gave final instructions to his solicitor to prepare a voluntary settlement of that property, and in pursuance of the instructions the settlement was prepared and duly executed on the 24th of February, 1864.

Now the trusts of that settlement were for Mrs. *Douglas* for her life to her separate use in the usual way, with remainder to himself if he should survive her for life, or until he should become bankrupt or insolvent. Then there were the usual trusts for children, and in default of children, to himself absolutely. On the 8th of April following (forty-

four days, I think, is the precise time, but it may be called six weeks afterwards,) he entered into partnership with Mr. *Smith*. The partnership, in point of profits, was to commence from the 1st of May, that is, Mr. *Grant's* contract was to go out on the 30th of April, and the arrangement between *Smith* and *Douglas* was, that he should succeed on the next day. Accordingly the business begins actively on the 1st of May, 1864, that is, rather more than two months from the time when the voluntary settlement was executed; but it must, for the purpose for which I look at it, be considered as commencing when the articles of partnership were signed.

Mr. *Douglas* went to *India*, and his partner, Mr. *Smith*, remained at home, and whether with the connivance, or approbation, or knowledge of *Douglas*, it seems somewhat uncertain, but it is certain that the business was so conducted that the firm was in difficulties so early as the month of November in the same year. They were borrowing and were embarrassed; the embarrassments so much increased that in the following month of March they failed for the sum of £347,000, and up to this time their dividend has been fourpence in the pound, and I am told that there is a possibility that there may be another penny, so that probably they will not pay sixpence in the pound.

Now to all these proceedings, however innocent Mr. *Douglas* may have been while in *India*, I must regard him as a party, because one partner is liable for the misfeasance of another. One of the most fruitful sources of ruin to men of the world is the recklessness or want of principle of partners, and it is one of the perils to which every man exposes himself who enters into partnership with another.

Now this question seems to me to raise a most important point. Can a man who contemplates trade, or who, in point of fact, whether he contemplates it at the time or very shortly afterwards, enters into trade, and thereby incurs liabilities which end in a disastrous state of affairs, make a voluntary settlement which shall be good against the creditors who become so in the course of his trade? I am not aware of any case upon the exact point, and none was cited, although almost all the cases which have occurred upon the subject were mentioned. But is the *Statute of Elizabeth* so very short in its effect that it will not cover a case where a man on the very eve of entering into trade takes the bulk of his property and puts it into a voluntary settlement and becomes insolvent a few months afterwards? Is it to be said that such a settlement cannot be reached by any principle of law? I think not...Mr. *Douglas*, having become bankrupt or insolvent within seven months after the execution of the settlement, has the burden cast upon him of shewing, not merely that he was solvent, but that he was in a situation which justified him in making a voluntary settlement of the great bulk of his property... . I am satisfied from the evidence that Mr. *Douglas* contemplated a partnership, and that the probability of such a partnership was the inducement to him to make the settlement. He had very likely never heard of the *Statute of Elizabeth*; but taking a common business-like view of the matter, and considering the rather reckless nature of the business into which he was entering, he wished to make a provision out of the leasehold house which he had bought for his wife and any children he might have. I cannot hesitate to come to the conclusion that the inducement to him to make this settlement on the very eve, as I consider it, of his going into business was to protect this property from any risk.

....

The statute speaks of cases where the creditors "are, shall, or might be in any wise disturbed, hindered, delayed, or defrauded," and it is not necessary to shew an intention to do that, because if the settlement must have that effect the Court presumes the intention and will attribute it to the settlor. That is distinctly laid down by the present Lord Chancellor, on appeal from Vice-Chancellor *James*, in *Freeman v. Pope* [L.R. 9 Eq. 206, 5 Ch. 538]… . So I dare say that Mr. *Douglas* had no fraudulent intention, according to his view, in making the settlement, and that he thought it a prudent thing to protect his wife and children. But in doing that he has, within the meaning of this statute, committed a fraudulent act, because, going into trade, he was taking away the only property which would be available for his creditors.

This happens to be a small amount of property with reference to the debts incurred, and with reference to the position of Mr. *Douglas* when the settlement was executed. But if I were now to decide against the Plaintiffs my decision would be applicable to any case. Suppose then the case of a man with a large fortune, and having a fancy (and I have known such cases) for going into trade. He says: "I am going into trade; I believe I may make a great deal of money by it, but nobody knows what may happen. Therefore, I will make this large fortune safe by settling it on my wife and children absolutely." The law is perfectly settled that if a man is solvent at the time and after the time of taking away the property which is put into the settlement he remains solvent, and does not at the time contemplate doing anything which could lead to insolvency, that settlement will be good… . So, in the present case, if Mr. *Douglas* had neither gone into nor contemplated going into trade at the time, but some years afterwards, by a totally new arrangement, made up his mind to do so, I should have had no hesitation in coming to the conclusion that his subsequent insolvency could have had no effect in producing invalidity of the settlement which he had made upon his wife and family.

The only rule I have found laid down on the subject that commends itself to my judgment, as I think it must commend itself to the judgment of all right-thinking men, is laid down in a very few words by Lord *Hardwicke* in *Stileman v. Ashdown* [2 Atk. 477]. "It is not necessary that a man should actually be indebted at the time he enters into a voluntary settlement to make it fraudulent; for if a man does it with a view to his being indebted at a future time it is equally fraudulent." Mr. *Bristowe* pressed upon me that it meant he contemplated getting into debt. But I do not read it so. I read it thus: that if a man does it with a view of being indebted at a future time, that is, with a view to a state of things in which he may become indebted, that makes it fraudulent, just as if he were indebted at the time. In the present case Mr. *Douglas* made the settlement, as I am perfectly satisfied, with the view that he was going into partnership in which he might become bankrupt or insolvent and utterly ruined; and therefore he did it with the view that he might be indebted, and the settlement in my opinion was fraudulent and void against creditors. The conclusion which I arrive at proceeds upon the broad ground that a man who contemplates going into trade cannot on the eve of doing so take the bulk of his property out of the reach of those who may become his creditors in his trading operations.

[His Honour then referred to some of the correspondence as shewing that it was treated in January, 1864, as almost a settled thing that he was to go into the business, and continued:]

I therefore hold that the settlement of the 24th of February, 1864, was absolutely null and void against the creditors within the meaning of the *Statute of Elizabeth*, and consequently that when Mr. *Douglas* executed the deed by which he vested all his property either at law or in equity in the inspectors or trustees, this property vested in them as being his, just as much as if the settlement of the 24th of February had never been executed.

....

MCGUIRE v. OTTAWA WINE VAULTS CO.

(1913), 48 S.C.R. 44, 13 D.L.R. 81 (S.C.C.)

DAVIES J. (dissenting).:—This is an appeal from a judgment of the Court of Appeal for Ontario reversing the judgment of the Divisional Court (Chief Justice Falconbridge dissenting), and restoring the judgment of the trial judge, Chief Justice Mulock, setting aside a conveyance made by the appellant John L. McGuire to his wife of the former's equity in a hotel property in the Village of Madoc, on the ground that such conveyance was fraudulent and void as against the grantor's creditors under the statute 13 Elizabeth.

The debts due the creditors of McGuire at the time of the execution of the impeached conveyance, outside of the mortgage debt secured upon the property conveyed, were contracted some time subsequent to the conveyance. Only two creditors gave evidence respecting the debts due them and it shewed that their debts were contracted long after the impeached settlement was made. There was no evidence that any of McGuire's debts which were due at the date of the settlement remained unpaid at the date of the insolvents' assignment.

The mortgage debt was one secured upon property much more than sufficient to pay it and may, therefore, for the purposes of this action, be disregarded. *Jenkyn v. Vaughan*, in 1856 [3 Drew 419, at p. 426].

It may be conceded as established by the cases that the statute extends to subsequent creditors. They have the same right to set aside an alienation made with intent to delay, hinder or defraud them, as creditors whose debts were due at the date of the alienation, but they have a more difficult task in proving a fraudulent intent on the part of the grantor in the case of a voluntary settlement. In such case they must prove either an express intent to delay, hinder or defraud creditors or that after the settlement the grantor had not sufficient means or reasonable expectation of being able to pay his then existing debts. 15 Halsbury's Laws of England, page 88, par. 180. The cases there cited I think support that proposition.

The courts below have all found that the impeached settlement was a voluntary one and I shall deal with the case on that finding, though I am bound to say I should have some difficulty in reaching it on the evidence.

There is no pretence for saying that any fraudulent intent under the statute was proved and the single question left was whether the grantor after the settlement was left without sufficient means or reasonable expectations of being able to pay his then existing debts and so that a fraudulent intent might be inferred.

As to the financial condition of McGuire at the time he made the settlement, I think the statement embodied by Riddell J. in his judgment is a fair and proper one. It

omits the Madoc property, the settlement of which is in question, and the mortgage upon it, and subject to which the property was conveyed to Mrs. McGuire, and aside from that shews McGuire to have been left with assets of the value of $14,180 and liabilities amounting to $3,947.

Amongst the assets was included $8,500 which he had paid for the Ottawa business and chattels, including the "good will." I agree that looking at McGuire's financial position from a business stand point there is no reason in the world why its value should not be taken into consideration. But when you are considering that financial position with respect to a settlement made by the man upon his wife of part of his property, and determining the "intent" with which it was made, to omit the value of such good will from your consideration would be, to my mind, most unfair.

....

I have already stated why I accept Mr. Justice Riddell's statement of McGuire's financial position at the time he made the settlement as correct. It shewed McGuire to have had a very handsome surplus of assets over debts and quite justified the settlement he made upon his wife. His business in Ottawa had continued prosperous from the time he bought it and remained so for six or eight months afterwards. The firm's obligations seem to have been met with reasonable promptness as they matured and to McGuire the outlook was promising. There was no indication or anticipation by either defendant that the venture was likely to prove a failure. My conclusion is that McGuire was clearly solvent when he made the settlement. He made that settlement in consequence of a promise given by him to his wife when at his solicitation she joined with him in the conveyance of some property he owned in Toronto. He and she both thought she had a dower interest in that property. They may have been wrong in their belief, but from their evidence both husband and wife believed she had. She thought she had a moral claim at any rate to the Madoc property as she had done as much if not more to build it up and make it what it was as her husband had done. He admitted that to be so. She was apparently living in Toronto with her two invalid daughters and the settlement seems to have been made when their home there was broken up and a very short time after she signed away whatever rights she had in the Toronto property. It was made at a time when, if the statement of his financial condition I accept is correct, he was undoubtedly entitled to make it. Even if the onus of proving that is cast upon him on the assumption of the settlement being a voluntary one, I think he has discharged it.

What, then, if this story is true, brought about the insolvency? A perusal of the evidence satisfies me that it was brought about by causes which could not have been foreseen or anticipated when he made the impeached settlement.

In the summer of 1909, McGuire Bros. were compelled by the License Commissioners to move their bar from the corner of Bank and Sparks Streets, a great thoroughfare, to the upper side of Bank Street. This change necessitated extensive alterations being made claimed to have cost about $4,000. This, of course, was not, and could not have been, anticipated in November, 1908. To make these necessary changes good paying tenants of theirs were dispossessed and their rentals lost. In the early part of 1910 the fire took place causing further damage to their business and much loss. McGuire states in his evidence that the direct loss in the receipts of the bar from the change compelled by the License Commissioners was 25%. The rentals of the tenants

they had to dispossess so as to make room for the new bar amounted to $110 per month, and McGuire says they were not able to get a tenant for the corner they vacated. Then the municipality brought into effect a by-law to reduce the number of licenses in the city and that made it impossible for them to sell out. Reverses began about June, 1909. They struggled from that date under the adverse circumstances I have above stated from the evidence, to meet their obligations until December. Then followed the plaintiffs' suit and the assignment followed by the landlord's distress for three months' advance rent and the sale under the distress with its usual pitiful returns.

In all of these facts as stated in evidence, I see nothing to justify the conclusion that the insolvency could have possibly been foreseen in November, 1908. The proper inference is that it was brought about by causes which could not have been reasonably foreseen at that time or for many months afterwards, and so forms an exception to the general rule respecting voluntary conveyances preceding insolvency.

It was said that this case was governed by that of *Mackay v. Douglas* [(1872), L.R. 14 Eq. 106]. I do not think so. The broad ground upon which that case was decided is stated by the Vice-Chancellor at page 122 to be that a man who contemplates going into trade cannot on the eve of doing so take the bulk of his property out of the reach of those who may become his creditors in his trading operations. The facts of the two cases are not analogous. McGuire was not like a man "going into trade" for the first time when or immediately after he made the settlement. He appears to have been for the greater part of his life in the hotel business, and he did not, as I have shewn, take the bulk of his property out of the reach of his creditors. I think it is a case forming an exception to the principle laid down in *Mackay v. Douglas*.

....

The settlement impeached did not embrace "all of his property" or indeed the larger part of it. It embraced practically that part of the property which the wife had herself in great part built up. It was made by a man who was not insolvent at the time he made it, but became so afterwards from accidents and causes which he neither did nor could have anticipated. It does seem to me to be rather the refinement of irony when the two chief creditors, the Wine Vault Company and the Capital Brewing Company, in order to defeat the claim of the wife and children to a portion of the property which the life's labours of the former largely created, unite to proclaim a business a "hazardous" one which they themselves exist upon and supply with the "sinews of war" to keep alive and on a commercial basis.

I am of opinion that the appeal should be allowed and the judgment of the Divisional Court restored.

DUFF J.:—I think there is not sufficient ground for impeaching the finding of the learned trial judge that the conveyance was voluntary; but I do not agree that the circumstances justify the conclusion that the necessary effect of the conveyance was to defeat or delay existing creditors. The burden was consequently upon the plaintiffs at the outset to shew that the conveyance was made by the debtor with a view to protecting himself or his family against the consequences of failure in the business into which he had a short time before entered. I think the fact that a collapse did come within a few months after the execution of the conveyance was sufficient to shift the burden to the

appellants of shewing that such was not the intent of the transaction. I do not think that burden has been discharged.

[Anglin and Idington JJ. wrote separate concurring judgments.]

COMMENTARY

10.24. In *Fleming v. Edwards* (1896), 23 O.A.R. 718 (Ont. C.A.), it was held that the *Mackay v. Douglas* rule does not apply where the debtor is entering a business which does not appear risky, *e.g.*, a business in which he has had experience and success in the past. Is this position sustainable after *McGuire v. Ottawa Wine Vaults Co.*? Should *Mackay v. Douglas* apply in all business situations?

There are many cases that make it clear that the debtor need not have entered into a hazardous undertaking in order for subsequent creditors to invoke the statute. This broader rule has been stated in *Newlands Sawmills Co. v. Bateman*, [1922] 3 W.W.R. 649 (B.C.C.A.) by Martin J.A., who, after discussing the decision of Sir R. Malins V.-C. in *Mackay v. Douglas*, stated at 654:

> It thus becomes apparent that the principle is based upon the contemplated entry into a trading or other venture which "might" lead to indebtedness merely, *and it is not necessary that the business should be of a hazardous nature*, and the use of that expression in the headnote [to *Mackay v. Douglas*] in the Law Reports, and the consequent restriction of the principle to the special class of hazardous undertakings is not justified by anything in the judgment when it is closely examined, though it is true that the firm in which Douglas became a partner had been to his knowledge, and continued to be engaged in speculations in jute, which made the business of a "rather reckless nature" as the Vice-Chancellor said L.R. 14 Eq. at p. 120; nevertheless, the result would have been the same upon the "broad ground" clearly laid down if insolvency had resulted as one of the ordinary risks of the partnership's business operations, quite apart from the jute speculations. The headnotes in the other three reports property [*sic*: properly] omit this restriction and simply state the principle upon the *broad ground of a voluntary settlement executed on the eve of going into trade*. It is desirable to notice this error because the Law Report's headnote was adopted by Garrow J.A. in the Court of Appeal for Ontario in *McGuire's case*, 8 D.L.R. at pp. 230–31, 27 O.L.R. at p. 322, without reference to the other reports which are of equal authority...[Emphasis added.]

The above observations are likely *obiter*, since the court held that the business in fact was "hazardous". What constitutes a "hazardous" business? Is the determination subjective or objective? In *Jeffrey v. Aagaard*, [1922] 2 W.W.R. 1201 at 1206 (Man. C.A.), Dennistoun J.A. stated that the "restaurant business is a hazardous business inasmuch as it depends very largely upon the character of the management." The B.C. Working Paper stated that the law in British Columbia does not require the business to be "hazardous". Rather, "the key element is the contemplation of future creditors who will be defrauded" (at 31).

10.25. Suppose that instead of conveying his property to his wife, McGuire had incorporated a company to carry on the hotel business. Is there any functional difference between the two situations? Can you justify the different legal consequences?

See B.C. Working Paper, at 11: "[T]he conclusion that a person who divests himself of property before entering business commits a fraud on his future creditors does not sit well with modern commerce which approves conducting business through a company with limited liability." The Paper called such views "outdated". Do you agree? Is incorporation *necessarily* inconsistent with fraudulent conveyance legislation?

10.26. See B.C. Working Paper, at 127 *et seq.*, which discussed the Ontario Law Reform Commission Report, Part IV, proposals (abolishing the right of subsequent creditors to sue) and the New Brunswick Report proposals (retaining such right). The conclusion was to abolish the right.

(h) TRACING THE PROCEEDS

Where, subsequent to avoidable transaction from a debtor to his transferee, the transferee sells the property to another party, can the creditors trace the proceeds in the original transferee's hands?

WESTINGHOUSE CANADA LTD. v. BUCHAR

(1975), 9 O.R. (2d) 137, 59 D.L.R. (3d) 641 (Ont. C.A.)

LACOURCIERE J.A.:—This appeal, brought by the plaintiff from the judgment of His Honour Judge G.J. Sullivan, raises the vexed question of the Court's right to follow the proceeds from the sale of property fraudulently conveyed and later resold.

....

There is no difficulty in declaring that the impugned conveyance to the wife is fraudulent and void as against the plaintiff under the provisions of s. 2 of the *Fraudulent Conveyances Act*, R.S.O. 1970, c. 182, as being made "with intent to defeat, hinder, delay or defraud" the said plaintiff in the recovery of its damages. The real problem comes from the conveyance of the lands on June 29, 1973, by the female defendant to an innocent purchaser for value, whose conveyance or title cannot be attacked, defeated or impeached under s. 6.

The learned County Court Judge refused to order an accounting by the female defendant of the moneys and benefits received by her from the resale of the lands. He found that the conveyance from the husband to the wife was in fact fraudulent, but dismissed that action without costs on two grounds: (1) that there was no provision in the *Fraudulent Conveyances Act* to follow realized funds, relying on the judgment of Middleton J. in *Gray v. Quinn* (1922), 22 O.W.N. 325.

....

I am of the opinion that...the tracing provisions [that is, s. 12] of the *Assignments and Preferences Act* should be available where a conveyance is void under the *Fraudulent Conveyances Act*. A remedial statute for the protection of creditors' rights should receive a fair, large and liberal interpretation to ensure the attainment of its object; the plain intention of the statutes, to be read together, is to constitute the fraudulent transferee a trustee of the proceeds replacing the lands, for the benefit of the defrauded creditors.

....

COMMENTARY

10.27. In *J.R. Watkins Medical Co. v. Gray*, [1920] 2 W.W.R. 588 (Alta. S.C.), the debtor transferred personal property to his wife, who in the course of the business sold the property and used the proceeds to purchase further inventory. The court held that the property then in the possession of the wife was not a substitution for the original property and was not earmarked in such a way as to be held in trust for the creditors. It was impossible to say which part of the present stock-in-trade was a direct result of the original sale. See also *Tennant & Company v. Gallow* (1894), 25 O.R. 56 (Ont. H.C.), and Annotation, "Fraudulent conveyances — Right of creditors to follow profits" (1912), 1 D.L.R. 841.

In *Vannerus and Kyme v. Coutts* (Van. Reg. No. C763450, April 1, 1979, B.C. Co. Ct.), a husband conveyed his half interest in the family home to his wife. This transfer was found to be void under the *Fraudulent Conveyance Act*, R.S.B.C. 1979, c. 142. The wife had sold the home and had purchased another. Paris Co.Ct.J. declared that the new home was "proceeds" of the sale of the fraudulently conveyed property and, therefore, was liable to be "seized or recovered" under s. 7 of the *Fraudulent Preference Act*. He also declared the wife to be trustee of the "proceeds" of the sale up to the amount owing the creditor, and awarded personal judgment against the wife for that amount.

10.28. Would creditors be entitled to follow proceeds in the hands of a transferee where the proceeds arise in a manner other than by means of a sale or other similar disposition — *e.g.*, if the proceeds were

insurance proceeds where the property has been destroyed? See *Bellhouse v. Wong*, [1941] 3 W.W.R. 503 (B.C.C.A.); and *Cdn. Credit Men's Trust Assn. v. Chow Lun*, [1931] 1 W.W.R. 211 (Alta. S.C.).

3. Fraudulent or Unjust Preferences

(a) INTRODUCTION

In this portion of the chapter, the term "preference" is confined to a conveyance by a debtor of property, including money, to one of his creditors in payment of an antecedent debt. It has been observed that "originally there was no express statutory enactment in regard to fraudulent preferences" *(Ex parte Griffith* (1883), 23 Ch. D. 69 (C.A.)); without such legislation — see, for example, the Ontario *Assignments and Preferences Act* — preferences were not, and are not, invalid. The rationale relates to the very nature and requirements of ordinary commercial dealings, for "[d]irect payment made by a debtor to a creditor is the normal, and by far the most frequent, method through which the claims of creditors are satisfied" (Law Reform Commission of British Columbia, *The Enforcement of Judgment Debts: The Creditors' Relief Act* (Working Paper No. 21, n.d.), at 52). The B.C. Working Paper noted the need to limit the application of the *Fraudulent Preference Act*, R.S.B.C. 1979, c. 143, on the ground that "[m]odern commerce would grind to a halt if a creditor could never be sure that payment on account, or security taken for an advance of money, was not liable to be set aside at the instance of another creditor" (at 33).

(b) PREFERENCES UNDER THE FRAUDULENT CONVEYANCES ACT

GUROFSKI v. HARRIS

(1896), 27 O.R. 201 (Ont. H.C.)

BOYD C.:—...A distinction is to be marked in the cases between selling to a stranger and handing over property to an existing creditor in satisfaction of his claim. In the latter case no provision of the *Statute of Elizabeth* is invaded, and its policy is not thereby frustrated. The scheme of the Act was to provide that a man's property should go to pay his creditors, or some, or one of them; but it was not intended to provide for rateable or other distribution among the mass of his creditors. Applying to this case the decisions under the *Statute of Elizabeth*, and having regard to the parliamentary exposition of that statute given by the Ontario Legislature in R.S.O. ch. 96, sec. 3, I think the case of *bona fide* satisfaction of the claim of one creditor is not within the mischief which the Act strikes at. [This decision was affirmed by the Ontario Court of Appeal (23 O.A.R. 717).]

COMMENTARY

10.29. But see the reference, in a preference situation, to the *Fraudulent Conveyances Act* in *Royal Bank v. Sullivan*, [1957] O.W.N. 68 (Ont. H.C.); affirmed in part [1957] O.W.N. 520 (Ont. C.A.).

(c) THE CONSTITUTIONAL ISSUE

Because the operation of provincial fraudulent preferences legislation is premised on insolvency, doubts have been raised concerning its constitutionality in the face of

TAB 20

THE PRINCIPLES

OF

MODERN COMPANY LAW

BY

L. C. B. GOWER, LL.M. (Lond)

Solicitor of the Supreme Court
Sir Ernest Cassel Professor of Commercial Law
in the University of London

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CHAPTER 2

HISTORY OF MODERN ENGLISH COMPANY LAW TO 1825

THIS book is concerned with modern company law, but there are some branches of modern English law which cannot be properly understood without reference to their historical background, and company law is certainly one of them; indeed, of all branches of the law it is perhaps the one least readily understood except in relation to its historical development, a somewhat extended account of which is therefore essential.[1] Such an account falls conveniently into three periods: (1) Until 1720 when the Bubble Act was passed; (2) From 1720 until the Bubble Act was repealed in 1825; and (3) From 1825 until the present day. The present chapter deals with the first two of these periods.

1. HISTORY OF ENGLISH COMPANIES UNTIL 1720

Early forms of commercial associations

Various forms of associations were known to medieval law and as regards some of them the concept of incorporation was early recognised. At first, however, incorporation seems to have been used only in connection with ecclesiastical and public bodies, such as chapters, monasteries and boroughs, which had corporate personality conferred upon them by a charter from the Crown or were deemed by prescription to have received such a grant.[2]

[1] For further details see especially Formoy, *The Historical Foundations of Modern Company Law* (Lond. 1923); C. A. Cooke, *Corporation, Trust and Company* (Manchester, 1950); Holdsworth, H.E.L., Vol. 8, pp. 192–222; *Anglo-American Essays in Legal History,* Vol. 3, pp. 161–255 (Boston, Mass. 1909); A. B. Levy, *Private Corporations and their Control,* Vol. 1, Part 1 (Lond. 1950); Lloyd, *Unincorporated Associations,* Part 1; Horrwitz (1946) 62 L.Q.R. pp. 375–386; W. R. Scott, *Joint Stock Companies to* 1720 (Camb. 1909–1912)—especially Vol. 1; C. T. Carr, *Law of Corporations* (Camb. 1905) and *Select Charters of Trading Corporations* (Selden Society, 1913); C. M. Schmitthoff, "The Origin of the Joint Stock Company," (1939) 3 Toronto L.J. 74 to 96; A. B. DuBois, *The English Business Company after the Bubble Act,* 1720–1800 (N.Y. 1938); H. A. Shannon, "The Coming of General Limited Liability," and "The First 5,000 Limited Companies and their Duration" (1931–1932) Econ.Hist., Vol. 11, 267 and 396; and B. C. Hunt, *The Development of the Business Corporation in England,* 1800–1867 (Harvard Economic Studies, 1936). The works of DuBois and Hunt are particularly fascinating accounts of the formative years which largely render obsolete earlier accounts of the periods to which they relate. Much old learning is to be found in J. Grant, *Law of Corporations* (Lond. 1850).

[2] While it is doubtful whether English law has ever unequivocally committed itself to the "fiction" theory of corporation, it seems to have fairly consistently adopted the concession theory—namely that incorporation depends upon a State grant. But

In the commercial sphere the principal medieval associations were the Gilds of Merchants, organisations which had few resemblances to modern companies but correspond roughly to our trade protection associations, with the ceremonial and mutual fellowship of which we can see relics in the modern Freemasons. Many of these gilds in due course obtained charters from the Crown, mainly because this was the only effective method of obtaining for their members a monopoly of any particular commodity or branch of trade. Incorporation as a convenient method of distinguishing the rights and liabilities of the association from those of its members was hardly needed, since each member traded on his own account subject only to obedience to the regulations of the gild.

Trading on joint account, as opposed to individual trading subject to the rules of the gild, was carried on through partnerships, of which two types were known to the medieval law merchant. The first of these, the *commenda*, was in fact a cross between a partnership and a loan whereby a financier advanced a sum of money to the active trader upon terms that he should share in the profits of the enterprise, his position being similar to that of a sleeping partner but with no liability beyond that of the capital originally advanced. In Continental law the *commenda* developed into the *société en commandite*, a form of association which has played, and still plays, an important part in the commercial life of those countries which adopted it. But in England it never took root, possibly because we lagged behind the Continent in book-keeping technique.[3] Had it become an accepted institution of English law the history of our company law might well have been very different, but in fact it only became legalised here in 1907[4] by which time complete limitation of liability could be obtained easily and cheaply by incorporation under the Companies Act.

The other type of partnership was the *societas*, a more permanent form of association which developed into the present-day partnership,

it has recognised the power of foreign States (see Chap. 28), and it may be that until the Reformation a grant of incorporation could be conferred on an English religious body by the Pope. That incorporation might be granted by statute appears never to have been doubted (Holdsworth, H.E.L., Vol. 3, p. 476) but in fact it was not until the latter part of the eighteenth century that it became the practice for Acts of Parliament actually to effect the incorporation. Until then statutes were used only to amplify the royal prerogative by authorising the Crown to confer a charter of incorporation with privileges beyond those which the Crown alone could confer (this was done, for example, in the case of the Bank of England and the South Sea Co.). In a modern case (*Elve* v. *Boyton* [1891] 1 Ch. 501) it has been held that such a company is "incorporated by Act of Parliament" within the meaning of an investment clause. DuBois (*op. cit.*, pp. 87 and 88) quotes examples of incorporation granted by Scottish burghs during the eighteenth century when the question also arose of the extent to which the royal prerogative could be delegated to colonial governors. As Sir Cecil Carr pointed out long ago (*Law of Corporations*, pp. 173 *et seq.*) the concession theory has worn somewhat thin now that incorporation can be obtained by mere registration.

[3] See Cooke, *op. cit.*, p. 46.

[4] Limited Partnerships Act, 1907. It was adopted in Ireland by statute in 1781 and it seemed for a time that it might take root in Scotland: DuBois, *op. cit.*, pp. 224–225.

each partner being an agent of the others and liable to the full extent of his private fortune for partnership debts. The full implications of the partnership relationship were only worked out by courts of equity during the eighteenth and nineteenth centuries, but these two main elements of agency and unlimited liability were already appreciated during this period.

Merchant adventurers

The first type of English organisation to which the name "company" was generally applied was that adopted by merchant adventurers for trading overseas. Royal charters conferring privileges on such companies are found as early as the fourteenth century,[5] but it was not until the expansion of foreign trade and settlement in the sixteenth century that they became common. The earliest types were the so-called "regulated companies" which were virtually extensions of the gild principle into the foreign sphere and which retained much of the ceremonial and freemasonry of the domestic gilds. Each member traded with his own stock and on his own account, subject to obeying the rules of the company, and incorporation was not essential since the trading liability of each member would be entirely separate from that of the company and the other members. Charters were nevertheless obtained largely because of the need to acquire a monopoly of trade for members of the company and governmental power over the territory for the company itself. "Thus, in the first instance, corporate form was valued both by the king and by the merchants, not so much because it created an artificial person distinct from its members, as because it created a body endowed with these governmental powers and trading privileges. It was from the point of view of trade organisation and the foreign policy of the State, rather than from the point of the interests of the persons comprising the company—from the point of view of public rather than commercial law—that the corporate form was valued."[6] And, it may be added, it was only from these points of view that organisation as a regulated company was at all suitable.

At a later stage, however, the partnership principle of trading on joint account invaded the regulated companies which became joint commercial enterprises instead of trade protection associations.[7] At first, in addition to the separate trading by each member with his own stock and later instead of it, they started to operate on a joint account and with a joint stock. This process can be traced in the development of the famous East India Company,[8] which received its first charter in 1600, granting it a monopoly of trade with the Indies. Originally

[5] See C. T. Carr, *Select Charters of Trading Companies* (Selden Society), pp. xi–xiii.
[6] Holdsworth, H.E.L., Vol. 8, 201–202.
[7] For a good account of this development and a comparison with similar developments on the Continent, see Schmitthoff (1939) 3 Toronto L.J., pp. 74 *et seq.*
[8] See Scott, *op. cit.*, Vol. II, pp. 89–206.

held to be realty,[11] and so they remained until the twentieth century.

Rather surprisingly the most important advantage of all those conferred by incorporation—limited liability—seems only to have been realised as an afterthought. The fact that an individual member of a corporation was not liable for its debts had been accepted in the case of non-trading corporations as early as the fifteenth century,[12] and, not without some doubts, it was eventually recognised at the end of this period in the case of trading companies.[13] But although it was recognised, it appears at first to have been valued mainly because it avoided the risk of the company's property being seized in payment of the members' separate debts,[14] rather than as a method of enabling the members to escape liability for the company's debts. This doubtless was because many charters expressly conferred a power on the company to make leviations (or calls) on the members and it was by no means clear that a company did not have this power in the absence of an express provision.[15] This being so limited liability was illusory; the company as a person was, of course, liable to pay its debts and in order to raise money to do so it would make calls on its members. Moreover, the creditors, by a process resembling subrogation, could proceed directly against the members, if the company refrained from taking the necessary action.[16] But legal ingenuity was not long in appreciating the possibilities of expressly excluding or limiting the company's power to make levies by a bargain to that effect between the company and its members. Such agreements seem to have been in use by both incorporated and unincorporated companies, and the fact that they were only effective in the case of the former was probably not clearly grasped by lawyers and certainly not by investors.

Growth of domestic companies

By the middle of the seventeenth century powerful monopolistic companies were already coming to be regarded as anachronisms; it was

(s. 9 (1)) and which vested the water-supply part of the undertaking in the Metropolitan Water Board. In pursuance of a further statute the company registered under the Companies Acts in 1905 and still exists as an investment trust company.

[11] *Townsend* v. *Ash* (1745) 3 Atk. 336. The theory seems to have been that a corporation held its assets on trust for its members; *cf. Child* v. *Hudson's Bay Co.* (1723) 2 P.Wms. 207. This theory avoided the difficulty regarding assignments since these were recognised in equity. Later Equity went a stage further by recognising, both in partnerships and companies, an implied trust for conversion under which the shares became personalty irrespective of the nature of the firm's assets. In many charters and statutes of incorporation this conversion was expressly provided for; *cf.* Companies Clauses Consolidation Act, 1845, s. 7, and Companies Act, 1948, s. 73.

[12] Holdsworth, H.E.L., Vol. 3, 484.

[13] *Edmunds* v. *Brown & Tillard* (1668) 1 Lev. 237; *Salmon* v. *The Hamborough Co.* (1671) 1 Ch.Cas. 204, H.L.

[14] See the common form provision in petitions for charters quoted by Carr, *Select Charters*, xvii, xviii.

[15] See DuBois, *op. cit.*, 98 *et seq.*

[16] *Salmon* v. *The Hamborough Co.*, *supra*.

realised that their governmental powers were properly the functions of the State itself and that their monopolies were an undue restraint on freedom of trade. Most of them atrophied; some survived for a time by converting, as did the Levant and Russia companies, from the joint stock to the regulated form (a strange reversal of the normal trend designed to allow greater freedom to their members); others, like the Royal Africa Company, by completely relinquishing their monopolies.[17] And after the Revolution of 1688[18] it seems to have been tacitly assumed that the Crown's prerogative was limited to the right to grant a charter of incorporation, and that any monopolistic or other special powers should be conferred by statute.[19]

The decline in the foreign-trading companies was however accompanied by an immense growth in those for domestic trade. Some of these were powerful corporations chartered under statutory powers (such as the Bank of England[20]) the objects of which resembled those of the public corporations of the present day, but most were public companies only in the sense that they invited the participation of the investing public. As regards these, the close relation between incorporation and monopoly was still maintained, for most companies were incorporated in order to work a patent of monopoly granted to an inventor.[21] By the end of the seventeenth century some idea had been gleaned of one of the primary functions of the company concept—the possibility of enabling the capitalist to combine with the entrepreneur. Share dealings were common and stock-broking was a recognised profession, the abuses of which the legislature sought to regulate as early as 1696.[22] But it would be entirely misleading to suggest that there was in any sense a company law; at the most there was an embryonic law of partnership which applied to those companies which had not become incorporated and, with modifications required by the terms of the charter and the nature of incorporation, to those which had. Both deeds of partnership (or settlement to use the later term) and charters owed much to the practice of the medieval gilds, particularly as regards the constitution of the governing body which generally consisted of a governor and assistant governors. From the end of the seventeenth

[17] The Hudson's Bay Company did not do so until 1869 and still survives as a chartered company. The East India Co. also survived until the middle of the nineteenth century but as a State organ rather than as a trading concern.

[18] Previously it seems to have been assumed that the *Case of Monopolies* (1602) 11 Co.Rep. 84b, and the Statute of Monopolies, 1624 (21 Jac. 1, c. 3), had left unimpaired the Crown's power to grant a monopoly for the regulation of foreign trade and this power had been upheld by the H.L. in 1684 in *East India Co.* v. *Sandys*, 10 St.Tr. 371. But *cf. Horn* v. *Ivy* (1668) 1 Ventr. 47, showing that the courts were already placing limitations on the extent of its exercise.

[19] Even earlier this had become the practice in the case of domestic companies requiring special powers; for example the New River Co. (see note 10, above).

[20] Incorporated, by charter preceded by statute, in 1694.

[21] See Cooke, *op. cit.*, Chap. 4.

[22] 8 & 9 Wm. 3, c. 32. It is interesting to note that this legislation followed a report of the Commissioners for Trade (the forerunners of the Board of Trade) which seems to be the first instance of this department interesting itself in a branch of company law (see pp. 37–38, *infra*).

century the term " directors " began to supersede " assistant governors." But the terminology varied and still varies.[23] It is interesting to note that although the invention of Preference shares is generally attributed to the railway boom a century later, certain companies had already experimented with different classes of shares or of loan stock [24] (for the distinction between shares and debentures was not appreciated until much later).

The South Sea Bubble

The first and second decades of the eighteenth century were marked by an almost frenetic boom in company flotations which led to the famous South Sea Bubble.[25] Most company promoters were not particularly fussy about whether they obtained charters (an expensive and dilatory process) and those who felt it desirable to give their projects this hallmark of respectability found it simpler and cheaper to acquire charters from moribund companies which were able to do a brisk trade therein.[26] An insurance company acquired the charters of the Mines Royal and Mineral and Battery Works, and a company which proposed to lend money on land in Ireland and a banking partnership [27] in turn acquired the charter of the Sword Blade Company which had been formed to manufacture hollow sword blades.

Impetus was given to this boom by the grandiose scheme of the South Sea Company to acquire virtually the whole of the National Debt [28] (some £31,000,000) by buying out the holders or exchanging their holdings for the company's stock, the theory being that the possession of an interest-bearing loan owed by the State was a basis upon which the company might raise vast sums to extend its trade. This theory was not necessarily unsound—it was indeed a logical extension of the principle upon which the Bank of England, and the South Sea Company itself, had been originally formed—but unfortunately the company had precious little trade to expand. Moreover, it had to pay dearly for its privileges by outbidding and outbribing the Bank of

23 Thus the B.B.C. and most incorporated schools and colleges still employ the term " Governors " while other corporations use the expression " Managers."

24 Scott, *op. cit.*, Vol. I, pp. 364–365.

25 The literature on the Bubble crisis is, of course, immense; the most scholarly treatment is still that of Scott, *op. cit.*, Vol. I, Chaps. XXI and XXII. For popular accounts, see Lewis Melville, *The South Sea Bubble* (Lond. 1921) and Erleigh, *The South Sea Bubble* (Lond. 1933).

26 We cannot afford to scoff at our predecessors, for a trade is still done in registrations of defunct companies. Two centuries hence, a generation which, owing to the incidence of taxation, was prepared to pay for registrations in direct proportion to the amount of the old company's accumulated losses, will probably appear just as ridiculous.

27 Which thereupon issued " sword blade " notes and bonds, and acted as bankers for the South Sea Company.

28 The company was originally formed, by charter preceded by statute in 1711, to incorporate the holders of the floating debt in exchange for a monopoly of trade with South America, a right which the power of Spain rendered something of a *damnosa hereditas.* The extended scheme seems to have been inspired by the financial experiments known as the Mississippi System introduced in France, with equally disastrous results, by John Law.

England.[29] And, of course, it paid too dearly—but that story belongs to our next period.

When the flood of speculative enterprises was at its height, Parliament decided to intervene to check the gambling mania which the Government had itself encouraged by sanctioning the South Sea Company's scheme. Its attempt was, however, somewhat inept. A House of Commons Resolution [30] of April 27, 1720, ignored the causes and merely emphasised the effects of the rash speculation by drawing attention to the numerous undertakings which were purporting to act as corporate bodies without legal authority, practices which "manifestly tend to the prejudices of the public trade and commerce of the kingdom." This was followed by the so-called Bubble Act [31] of the same year, which also made no attempt to put joint stock companies on a proper basis so as to further industry and trade and protect investors. Exactly what it did is, however, somewhat obscure.

The main section, 18, repeated the Resolution of the House of Commons and provided that all such undertakings as were therein described "tending to the common Grievance, Prejudice and Inconvenience of His Majesty's subjects" should be illegal and void. The section then proceeded to give particular examples, *viz.*, the acting as a corporate body and the raising of transferable stock or the transfer of any shares therein without legal authority either by Act of Parliament or Crown charter, or acting or pretending to act under any obsolete charter. By section 21 brokers dealing in securities of illegal companies were to be liable to penalties. The remaining sections, however, exempted companies established before June 24, 1718 (which were therefore left to the common law, whatever that may have been), and also the East India and South Sea Companies and the two assurance companies authorised by the first part of the Act. Finally, in section 25, there was a vague proviso that nothing "shall extend . . . to prohibit or restrain the carrying on of any home or foreign trade in partnership in such manner as hath been hitherto usually and may be lawfully done according to the Laws of this Realm now in force."

This statute was our first attempt at a Companies Act [32] and it

[29] It is interesting to speculate on what might have happened had the Bank of England outbidden the company. Perhaps it would have been the former whose bubble reputation was so soon pricked, and the latter which acquired the mantle of respectability (with the final canon of nationalisation) in fact worn by "the old lady of Threadneedle Street."

[30] H.C.Jour. XIX, 351. This resolution was based upon the Report of a Committee appointed on Feb. 22 to inquire into certain of the projects; for its Report, see *ibid.*, pp. 341 *et seq.*

[31] 6 Geo. 1, c. 18. This prolix and confusing statute, which, as Maitland said, "seems to scream at us from the Statute-book" (*Collected Papers*, Vol. 3, p. 390), is divided into two parts. The first (ss. 1–17) authorised the incorporation of the London and Royal Exchange Assurance Companies with a monopoly of the corporate insurance of marine risks. It is with the later sections only that we are at present concerned.

[32] Or, perhaps, more properly, a Prevention of Fraud (Investments) Act, such as that of 1939.

clearly reflected little credit on anyone concerned with it. As Holdsworth says,[33] "What was needed was an Act which made it easy for joint stock societies to adopt a corporate form and, at the same time, safeguarded both the shareholders in such societies and the public against frauds and negligence in their promotion and management. What was passed was an Act which deliberately made it difficult for joint stock societies to assume a corporate form and contained no rules at all for the conduct of such societies, if, and when, they assumed it." But in fact the authorities were faced with a new phenomenon and had no clear idea of the issues involved. Nor is it altogether fair to blame them; a further 120 years' experience was to be needed before anything on the right lines was to be enacted and even today we find it necessary to amend our company law every twenty years and to precede the amendment by a long and careful inquiry by an expert committee. It was obviously too much to expect the Parliament of 1720 to rush through a Companies Act comparable to that of 1948 or even 1844. Where they seem most blameworthy is not for what they omitted to do, but for the vagueness of what they in fact did, and when the courts were called upon to interpret it they found it vague indeed. But this they were not called upon to do for many years.

2. History of English Companies from 1720 until the Repeal of the Bubble Act in 1825[34]

The Bubble bursts

The passage of the Bubble Act, to which publicity was given by Royal Proclamation, and the events leading up to it must obviously have done much to sap public confidence. But what precipitated the disastrous collapse of 1720 was the institution of proceedings against some of the companies operating under obsolete charters with a view to these being forfeited.[35] This, as might perhaps have been foreseen,[36] led to a widespread panic from which the South Sea Company itself never fully recovered.[37] In June, 1720, its stock had stood

[33] H.E.L., Vol. 8, 219-220.

[34] Fascinating and learned accounts of this period are now available in the pages of DuBois and Hunt. As their researches are not as well known in this country as they deserve, I have dealt with this period rather more fully.

[35] For an account of these proceedings and an attempted refutation of the generally accepted theory that they were instituted by the Souh Sea Company or its directors, see my article in (1952) 68 L.Q.R. 214.

[36] Although the legitimacy of the birth of the South Sea Company was beyond reproach, it was employing as its bankers a company incorporated under the Sword Blade Charter. The failure of these bankers was one of the factors which frustrated the efforts to arrest the panic by an agreement between the South Sea Company and the Bank of England.

[37] The third volume of Scott, *op. cit.*, contains a graph showing the fluctuations in the shares of the South Sea Company, the East India Company and the Bank of England between May-September, 1720.

at over 1,000 per cent. and immediately before the issue of the writs it was still at 850 per cent. A month later it had fallen to 390 and by the end of the year it was quoted at 125. The Government was too much involved to allow the company to crash completely,[38] but the subsequent investigations disclosed fraud and corruption (in which members of the Government and the Royal household were implicated) and it never fully recovered. With it fell many of its contemporaries, which, not being regularly chartered nor so fortunate as to have friends in high places, burst like the bubbles they were. But, although they disappeared, they were not forgotten, for public confidence in joint stock companies and their securities was destroyed so effectively that it was three-quarters of a century before there was a comparable boom. If the legislature had intended the Bubble Act to suppress companies they had succeeded beyond their reasonable expectations; if, as seems more probable, they had intended to protect investors from ruin and to safeguard the South Sea Company, they had failed miserably.

This result was attained almost without prosecutions under the Act, for only one,[39] in 1723, is reported[40] until the beginning of the nineteenth century. Nevertheless it is clear that the Bubble Act was for long a sword of Damocles which exercised a restraining influence as potent as the memory of the great slump. DuBois's researches[41] have shown how existing companies and the promoters of new enterprises took counsel's opinion on the application to them of the Act, and it is to this Act that he attributes the first traces of the dominant part subsequently played by lawyers in the development of company law and practice.

Effect of the Bubble on incorporations

Joint stock companies did not disappear completely. On the contrary, many regularly chartered companies and a few unincorporated ones,[42] had survived the panic and were living examples of the advantages of this type of organisation. Others, too, still succeeded in obtaining charters; but not many, for a lasting effect of the Bubble Act and the crisis of 1720 was to make the law officers of the Crown

[38] In the words of Holdsworth (H.E.L., Vol. 2, p. 210) it "dragged out a struggling existence till 1807; and the faded splendours of its South Sea House survived long enough to secure immortality in the Essays of Elia." Later it became for a time the home of the Baltic Exchange, and a building in the City of London still bears the name having survived the blitz of World War II more successfully than the company survived the financial "blitz" of an earlier century.

[39] *R.* v. *Cawood*, 2 Ld.Raym. 1361. It decided nothing of importance on the interpretation of the Act.

[40] But contemporary news-sheets make it clear that others were instituted.

[41] *Op. cit.*, pp. 3 *et seq.* He refers particularly to the opinions of Sjt. Pengelly who is known to have delivered opinions (which still survive) on no fewer than twenty-seven organisations and whose views foreshadow the judicial interpretation adopted in the succeeding century.

[42] Including the Sun Fire Office, established in 1709.

far more chary of advising the grant of charters,[43] and to insist on restrictive conditions in those that were granted.[44]

Nor at first was Parliament any more complaisant. It was not until towards the end of the century, with the growth of canal building, which necessarily involved an application to Parliament for special powers, that Parliament became less strict in its requirements and that direct statutory incorporation became common.[45] It is to this statutory incorporation that we owe many of the features of modern companies: in particular the method of limiting liability of the members to the nominal value of their shares.

Hence throughout the century (and beyond) the shadow of 1720 retarded the development of incorporated companies. The official view is well represented by the oft-quoted words of Adam Smith,[46] writing as late as 1776, in which he stated that a joint stock company was an appropriate type of organisation only for those trades which could be reduced to a routine, namely, those of banking, fire and marine insurance, making and maintaining canals, and bringing water to cities; others, in his view, were bound to be inefficient as businesses as well as being contrary to the public interest. Smith, therefore, put the seal of his approval on the current legislative and administrative practice, for the authorities, in their wisdom, had incorporated precisely these four types and had (with rare exceptions) refused to incorporate others.

Growth of unincorporated companies

Had the authorities granted incorporation more readily, already in the eighteenth century, incorporated companies might have become the dominant type of commercial enterprise. And had that policy been adopted, the Government, by its control over charters and statutes, would have shaped the development of business practice 200 years earlier than it attempted to do so on any large scale. Instead, as we have seen, the authorities placed almost insuperable difficulties in the way of incorporation and thus abdicated their control to businessmen and their legal advisers who sought an alternative device. This they found in the unincorporated association; paradoxically, the Bubble Act in the end caused a rebirth of the very type of association which it had sought to destroy. The history of the previous period had shown that it was

[43] For an account of the difficulties which company promoters had to surmount, see DuBois, *op. cit.*, pp. 12 *et seq.* "The law officers of the Crown, mindful of [the Act's] provisions, hesitated to approve of applications for charters which contemplated the creation of large stocks of transferable shares. Consequently, not only were the operations of unincorporated joint stock companies restricted by the Act, but the Act was used as an expression of policy to restrain the formation of business corporations": *ibid.*, p. 12.

[44] *Ibid.* To this period can be traced conditions restricting the amount of capital which the company might raise. A further restraint on joint enterprise arose from the habit, introduced after 1720, of inserting in patents of invention prohibitions of assignment to more than five persons: *ibid.*, p. 21–24.

[45] Over a hundred statutory incorporations occurred during the last forty years of the eighteenth century.

[46] *Wealth of Nations*, V, Chap. 1, Part III, Art. 1.

perfectly feasible to trade with a joint stock without incorporation, and although the Bubble Act had struck at unincorporated companies it had expressly exempted partnerships carried on "in such manner as hath been hitherto usually and may be lawfully done."[47] This exemption clearly could not have covered every type of existing unincorporated company, for otherwise the Act became completely meaningless, but exactly how far partnerships could lawfully go was far from clear. The size of the membership could not be the decisive factor for at this time there was and never had been any upward limit on numbers.[48] Professional opinion at the time[49] took the view, in fact adopted by the courts in the nineteenth century, that the basic test of illegality was the existence of freely transferable shares and for a time such unincorporated associations as were formed (and the shock of the crash of 1720 caused there to be few for many years) were careful to place severe restrictions on transfers.[50] But from the middle of the century onwards it is clear that unincorporated joint stock companies often with a large number of proprietors[51] were operating to a gradually increasing extent and that (as the Bubble Act came to be regarded as a dead letter) complete freedom of transfer was often permitted.

The deed of settlement company

Great legal ingenuity[52] was brought to bear to confer on these unincorporated associations nearly all the advantages of incorporation, and for this purpose use was made of the trust. The company would be formed under a deed of settlement (approximating closely to a cross between the modern articles of association and debenture trust deed) under which the subscribers would agree to be associated in an enterprise with a prescribed joint stock divided into a specified number of shares; the provisions of the deed would be variable with the consent of a specified majority of the proprietors; management would be delegated to a committee of directors; and the property would be vested in trustees,[53] who would usually be persons other than the directors. Often

[47] s. 25.
[48] Except in the case of banking, as regards which the Bank of England's monopoly was protected by a prohibition, under a statute of 1708 (7 Anne, c. 7), of banking in England by more than five persons in association. And under the first part of the Bubble Act itself the London and Royal Exchange Assurances had a monopoly of insuring marine risks by companies or societies.
[49] See DuBois, *op. cit.*, pp. 3 *et seq.*
[50] In the light of this it is interesting to note that unincorporated companies were often described as "private" companies, in contradistinction to the incorporated "public" company; restriction on transfer is of course the major feature of the twentieth-century private company. The use of the term "public company" to describe those formally incorporated will be found in a statute of 1767 (7 Geo. 3, c. 48), which struck at the practice of splitting shareholdings to increase voting power, by disqualifying members from voting until they had held their shares for six months.
[51] The true extent of the numbers was sometimes disguised by the device of sub-partnership, *i.e.*, the original few shares would be subsequently subdivided; see DuBois, *op. cit.*, pp. 78–79.
[52] For details, see DuBois, *op. cit.*, Chap. III.
[53] This was by no means unusual even in the case of incorporated companies: *ibid.*, pp. 115–116.

it would be provided that these trustees should sue or be sued on behalf of the company, and although the legal efficacy of such a provision was by no means clear, suit by the trustees in a court of equity seems to have been generally permitted.[54] As for the right to be sued, it will be appreciated that obscurity on this point was by no means an unmixed disadvantage from the point of view of the company.

Long before the end of the century a considerable proportion of certain types of commercial enterprise was organised on this basis, which strangely enough, seems to have been encouraged rather than frowned upon by the Government, for frequent examples are found of refusal by the law officers to recommend charters of incorporation on the ground that "coparcenary" was a more appropriate form of organisation.[55] Unincorporated associations had a virtual monopoly of the growing activity of non-marine[56] insurance, both by companies trading for the profit of their members (where the old Sun had formed the model for the Phoenix, Norwich General, Norwich Union and a host of others) and by mutual and friendly societies.[57] They were also used extensively in the metal industries, they invaded the theatre, and were even used at times in canal building where statutory incorporation was more common. Indeed, the researches of DuBois into the eighteenth-century company records and counsel's opinions have made it clear that the use of joint stock companies was far more widespread than had hitherto been supposed on the basis of the paucity of incorporations and of decided cases on unincorporated companies.

On the other hand we have to wait until the nineteenth century for any outbreak of speculation in shares comparable to that of 1720.

[54] In practice considerable use was made of arbitration: *ibid.*, 221.

[55] Thus on the Equitable Assurance petition in 1761 the Att.-Gen. (Yorke) said: "If the Petitioners are so sure of success there is an easy method of making the experiment by entering into a voluntary partnership of which there are several instances now subsisting in the business of insuring": quoted in DuBois, *op. cit.*, 30. Having regard to the size of these enterprises the Law Officers can hardly have been so naïve as to suppose that the "partnership" would be other than on a joint stock basis. Indeed petitions were often made by existing unincorporated companies and it was not unknown for such companies to take the opinion of the Law Officers on questions relating to their constitutions: *ibid.*, p. 313, note 35.

[56] The first part of the Bubble Act had given the London and Royal Exchange Assurance Companies a monopoly of marine assurance by associations. During this period the value of this monopoly was diminished by individual insurances by underwriters who assembled at Lloyd's Coffee House and grew into the famous "Lloyd's" which was eventually incorporated in 1871, although policies continue to be underwritten not by the corporation but by individual underwriters: see further, Gibb, *Lloyd's of London* (Lond. 1957). For a popular account of the historical development with particular reference to life assurance, see Hartley Withers, *Pioneers of British Life Assurance* (1951).

[57] Friendly Societies became so common that they were authorised by statute in 1793 (33 Geo. 3, c. 54), the first general authorising Act from which sprang not only the modern Friendly Society but also Industrial and Provident Societies, Building Societies, and Trustee Savings Banks. Under the Act the rules had to be approved by the local justices, who probably enjoyed ratifying the rule of the Beneficent Society of Tinwold (1793) that "None shall be admitted into this Society who are suspected of being friendly to the new fangled doctrines of LIBERTY AND EQUALITY AND THE RIGHTS OF MAN as set forth by Thomas Paine and his adherents."

During the remainder of the eighteenth century, although the mechanism of the stock market was well understood and several rather half-hearted attempts were made by the legislature to check its abuses,[58] company shares do not seem to have been generally regarded as suitable investments or gambling counters[59] for the lay public, but rather as means of enabling members of the mercantile community to acquire a permanent stake in enterprises with which they were familiar. But the picture changed at the turn of the century, when first the exigencies of war and then the growth of the railways led to an outbreak of company promotion and of general speculation comparable to that of the Bubble period. It was only then that the inherent disadvantages of the unincorporated type became fully apparent.

Disadvantages of unincorporated companies

As we have seen, one difficulty lay in the power to sue or be sued. In law these unincorporated companies were merely partnerships,[60] and this was before the time when the courts permitted suit in the firm's name. On the contrary, actions at law[61] had to be brought by or against all the partners liable, and the difficulties[62] which this caused, particularly when there had been changes in the shareholdings, can be imagined. The only satisfactory, but expensive, solution was the promotion of a private Act of Parliament permitting the company to sue or be sued in the name of one or more of its officials. Such Acts became common towards the end of this period,[63] and the right was conferred on Friendly Societies by the Act of 1793. As will be appreciated, the proprietors of the company would probably only be concerned with the possibility of suing and would be only too happy to find obstacles in the way of being sued, particularly as they would be personally liable without limitation.

This brings us to the second and most important disadvantage of the absence of incorporation—the members could not limit their personal

58 7 Geo. 1, stat. 2, No. 8 (1721); 7 Geo. 2, c. 8 (1734); and 10 Geo. 2, c. 8. (1737).

59 During the eighteenth century the lotteries met this need. Their abolition in 1826 under the Lottery Act. 1823 (4 Geo. 4, c. 60) may well have encouraged share speculation. For Lotteries, see J. Ashton, *A History of English Lotteries* (Lond. 1893)—a most entertaining book.

60 But even the law could not shut its eyes to all the differences between a large company and a simple partnership. A shareholder in the former could obviously not bind the company, as a partner could the firm; anyone dealing with the company must be deemed to know that powers of management were restricted to the directors. Here we can detect the germ of the later rule in *Royal British Bank* v. *Turquand*, see Chap. 8, *infra*.

61 As we have seen equity was somewhat more lenient and even at common law if the contract was with the trustees they could sue on it for the benefit of the company: *Metcalf* v. *Bruin* (1810) 12 East 400.

62 They are well described in George on *Companies* (1825), pp. 19 *et seq.* quoted by Formoy, *op. cit.*, pp. 33 *et seq.*

63 DuBois, *op. cit.*, p. 142 quotes an example as early as 1730 but this was exceptional.

liability. Until late in the century limited liability still seems to have been regarded as only a secondary consideration. DuBois [64] finds the earliest clear recognition of it as the motive for incorporation in the petition for incorporation by the Warmley Company in 1768, but increasingly from then on it became openly recognised as a factor of prime importance and one which incorporation alone could fully obtain. Unincorporated companies could only strive to approximate to it by expressly contracting in every case that liability should be limited to the funds of the company—a solution only practicable where the contracts were of a formal type such as insurance,[65] for it was generally believed that a statement to this effect in the deed of settlement would be ineffective even if the creditor had notice of it.[66] Or, of course, they could make a virtue of necessity, as did the Phoenix Assurance which, when its rivals, the incorporated Royal Exchange Assurance, boasted of the advantages to their policy-holders of a ready remedy against the corporate stock, retorted by emphasising the advantages to the public of the full responsibility of its members.[67]

In truth, however, unlimited liability, though a danger to the risk-taker, was often a snare and a delusion rather than a protection to the public and no handicap at all to the dishonest promoter. The difficulties of suing a fluctuating body and the even greater difficulties of levying execution [68] made the personal liability of the members largely illusory. Moreover the investor was supposed to become a member by signing the deed of settlement and until he did so his identity would not be known by the creditors. But in fact "stags" would deal in allotment letters or scrip certificates to bearer without signing the deed and often before any formal deed was in existence, and dishonest promoters, who alone might be under any legal liability, might disappear with the subscription moneys.[69] Many promotions were still-born and others perished with the slumps [70] which followed each successive boom. Some intervention by the State was inevitable but the question was what form it should take.

[64] *Op. cit.*, p. 95.

[65] In the nineteenth century these stipulations became common form in the policies of unincorporated offices. Such an express contract was ultimately held to be effective: *Hallett* v. *Dowdall* (1852) 21 L.J.Q.B. 98.

[66] But statements alleging limited liability were common form in both deeds of settlement and prospectuses. See Hunt, *op. cit.*, pp. 33–34, 72 and 99–101. They were eventually held to be ineffective in *Re Sea, Fire & Life Insurance Co.* (1854) 3 De G.M. & G. 459.

[67] Quoted by DuBois, *op. cit.*, p. 96.

[68] These difficulties are well explained in Formoy, *op. cit.*, pp. 35 *et seq.* They did not disappear even if there was a private Act permitting the company to be sued in the name of its officers.

[69] The *modus operandi* is explained in *ibid.*, p. 43. The opportunities for fraud thus provided are immortalised by Charles Dickens's account of the "Anglo-Bengalee Disinterested Loan and Life Assurance Company" in the pages of *Martin Chuzzlewit.*

[70] These occurred particularly in 1808, 1825–1826, and 1844–1845. See Hunt, *op. cit.*, *passim.*

State intervention

The first form was the characteristic English expedient of reviving an old remedy—in this case prosecution under the almost forgotten Bubble Act. In November, 1807, the Attorney-General (at the instance of a private relator) sought a criminal information against two recently formed unincorporated companies,[71] both of which had freely transferable shares and advertised that the liability of the members would be limited. Lord Ellenborough [72] dismissed the applications because of the lapse of eighty-seven years since the Act was previously invoked, but he issued a stern warning that no one in the future could pretend that the statute was obsolete and indicated that a " speculative project founded on joint stock or transferable shares " was prohibited.[73] Shortly afterwards two further associations were held illegal, apparently because their shares were transferable.[74]

These decisions caused alarm among investors and promoters and were probably contributory causes of the slump of 1808. However, despite further prosecutions, confidence was gradually restored and the years 1824–1825 witnessed a boom which was compared with that of 1719–1720 and which was followed by a similar slump. The various court cases [75] did little to clarify the law; the better view seemed to be that a company with freely transferable shares was illegal, but that one where the right to transfer was restricted was only unlawful if it had a mischievous tendency. On the other hand there were many who were opposed to the whole conception of joint stock enterprise both incorporated and unincorporated, and until the middle of the nineteenth century bitter debates continued in which the virtues of healthy private enterprise were contrasted with the dead hand of monopolistic companies.[76] Lord Eldon, in particular, attacked the latter in both his legislative and judicial capacity. In the former he announced his intention of introducing further restrictive legislation but finally dropped this idea on the ground that the law as it stood was sufficiently strict [77]; had his view of it prevailed it certainly would have been strict for he was

[71] The London Paper Manufacturing Co. and the London Distillery Co.

[72] *R.* v. *Dodd* (1808) 9 East 516.

[73] *Ibid.*, pp. 526–528.

[74] *Buck* v. *Buck* and *R.* v. *Stratton* (1808) 1 Camp. 547. As we have seen (*supra*, pp. 30–32) this was Sjt. Pengelley's view in 1721.

[75] They are summarised by Hunt, *op. cit.*, Chaps. II and III, and in Cooke, *op. cit.*, Chap. VII. The most instructive of those reported are: *R.* v. *Webb* (1811) 14 East 406, *Pratt* v. *Hutchinson* (1813) 15 East 511; *Josephs* v. *Pebrer* (1825) 3 B. & C. 639; *Kinder* v. *Taylor* (1825) 3 L.J.Ch. 68. See further Lindley on *Companies*, 6th ed. (1902), pp. 180–184.

[76] Admirable accounts of these will be found in Hunt, *op. cit.*, *passim*. The arguments used by the supporters of " private enterprise " are astonishingly reminiscent of those now used by the opponents of nationalisation. The company chairmen who inveigh against the menace of State enterprise would doubtless be shocked to realise that 100 years earlier very similar arguments were being used to attack their cherished companies. " The idea that a company was synonymous or at least co-extensive with monopoly persisted well into the nineteenth century ": Hunt, *op. cit.*, p. 17.

[77] *Ibid.*, pp. 38 and 39.

apparently prepared to hold that assuming to act as a corporation [78] was an offence at common law as well as under the Act.[79]

Finally, the Government felt compelled to do something to bring the law more into accord with the facts; but just as their predecessors in 1720 could think of nothing more constructive than the Bubble Act, so now they could think of nothing better than its repeal. In 1825, its Indian summer was finally ended. The repealing statute [80] was sponsored by Huskisson, the President of the Board of Trade, and it is then that this Government Department first started to take an active part in the development of company law.

Influence of the Board of Trade

The Board [81] was the successor of the Commissioners for Trade and Plantations, the history of which, as an *ad hoc* or standing Committee of the Privy Council, can be traced back to the beginning of the seventeenth century and whose report on stock-jobbing in 1696 led to the first legislative attempt [82] to regulate brokers. Throughout the eighteenth century examples can be found of references to the Commissioners of petitions for charters of incorporation,[83] especially in cases where the object was colonial trade (for at this time the greater part of the Commissioners' work was concerned with the colonies rather than with domestic trade). But, in general, decisions were taken by the Law Officers [84] (which in practice must often have meant the Attorney-General's devil [85]) and it was not until the Board was re-created by Pitt in 1784 that the emphasis changed and that it gradually came to be recognised that the Board was the appropriate Government Department to advise on incorporations and to guide the development of company law. Since Huskisson repealed the Bubble Act a century and a quarter

[78] But Eldon himself was unable to give any clear account of what this meant. The Inns of Court come close to acting as corporations, even to the extent, or so it is generally said, of using common seals and this seems to have impressed Eldon and acted as a restraining influence: see *Lloyd* v. *Loaring* (1802) 6 Ves. 774 at p. 779. But query if the Inns do, in fact, use common seals: see Lloyd, *Law of Unincorporated Associations*, p. 51, note (*c*).

[79] He did not get a very good press; the *Morning Chronicle* said it confirmed their view that his opinions "as a Politician were seldom worth much": March 30, 1825, quoted by Hunt, *op. cit.*, p. 39.

[80] 6 Geo. 4, c. 91. The marine-insurance monopoly had been repealed a year earlier: 5 Geo. 4, c. 114.

[81] The influence of the Board has been largely ignored by writers on the history of company law. For accounts of the Board's development, which, however, say little about its functions in connection with companies, see Llewellyn Smith, *The Board of Trade* (The Whitehall Series, 1928) and Prouty, *The Transformation of the Board of Trade* 1830–1855 (Lond. 1957).

[82] 8 & 9 Wm. 3, c. 32.

[83] See DuBois, *op. cit.*, pp. 13, 57, 58, 60, 62, 66, 69, 70, 76, 89 and 172. There are also occasional examples of applications to the Commissioners for investigation of the affairs of existing companies: *ibid.*, 126.

[84] DuBois, *op. cit.*, pp. 169–170 (note 135) says, "The usual procedure in the case of an application for incorporation was the presentation of a petition to the Privy Council. The Privy Council would refer the matter to a subcommittee, which, if it were favourably inclined to the plan after consideration, would submit the petition to the Attorney-General or Solicitor-General. On occasion the Commissioners of Trade and Plantations would be consulted."

[85] Napier, *A Century of Law Reform* (Lond. 1901), p. 389.

ago the Board has been responsible for all company legislation and has been entrusted with gradually increasing supervisory powers over joint stock enterprises. It is appropriate that its first major intervention should have been an act of liberation rather than of control, for its policy throughout has been to allow the greatest possible freedom to private enterprise. As its official historian [86] truly says: "Broadly speaking the part played by the Board of Trade in relation to the movement which has revolutionised the structure of industry has been that of a vigilant onlooker rather than of a continuous supervisor." [87]

Chapter 3

HISTORY OF COMPANIES FROM 1825 TO THE PRESENT DAY

Legislative control

The repeal, like the enactment, of the Bubble Act was followed by a disastrous slump further emphasising the need for some constructive measures of control. These, however, were still lacking; the only concrete advance made by the new Act was a provision [1] enabling the Crown to declare the extent of the members' liability on the grant of incorporation, so that a charter was no longer necessarily accompanied by a complete absence of liability on the part of the members for the company's debts. This provision might have been expected to encourage greater freedom in the grant of charters, but in fact the authorities remained as strict as ever. Applications for statutory incorporation, stimulated by the boom in railway promotion, fared better but their expense was prohibitive except in the case of the largest concerns.[2]

Hence when the speculative fever broke out again in 1834 most promoters were thrown back on the unincorporated form, the legality of which was still in doubt, especially as Eldon had secured the inclusion in the repealing Act of an express recital that undertakings should be adjudged and dealt with according to common law. It was not until 1843 that doubts upon their common law legality were finally eradicated,[3] and even then little had been done to remove the disadvantages under which unincorporated associations laboured. But despite these handicaps joint stock banks,[4] insurance companies and a

[1] s. 2.

[2] Hunt, *op. cit.*, p. 82, quotes two railway incorporations which cost £72,868 and £40,588. Even the fees for a charter amounted to at least £402 which was a substantial sum in those days: *ibid.* The Report on Investments for the Savings of the Middle and Working Classes (1850 B.P.P., Vol. XIX, 169) quoted a chartered incorporation costing £1,134 which was alleged (surely erroneously?) to be "greater even than that of obtaining an Act of Parliament."

[3] *Garrard* v. *Hardy* (1843) 5 M. & G. 471, *Harrison v. Heathorn* (1843) 6 M. & G. 81 not following *Duvergier* v. *Fellows* (1828) 5 Bing. 248 and *Blundell* v. *Winsor* (1835) 8 Sim. 601. Brougham L.C. on the Bench took a more liberal view than his predecessor (*Walburn* v. *Ingilby* (1833) 1 Myl. & K. 61) although in the House he was almost equally reactionary on this matter and received an equally unfavourable press. ("The commercial part of the community have little reason to thank God, with Cobbett, that there is a House of Lords, and above all a Lord Brougham": *Morning Chronicle*, August 15, 1838 (cited in Hunt, *op. cit.* 84)—a reference to the prosecution of Cobbett in 1831 for criminal libel when he subpoenaed six members of the House of Lords and secured an acquittal largely because of the evidence of Brougham L.C.)

[4] Guided by the experience of Scotland (where joint stock banks had flourished in contrast with the failures of the English private concerns), the monopoly of the Bank of England was whittled away by Acts of 1826 (7 Geo. 4, c. 46) and 1833

host of other projects flourished as never before and joint stock companies came to play an important role in every part of the country's economy. Clearly some steps had to be taken to remove the legal confusion.

The first step was taken by the Trading Companies Act of 1834,[5] which was intended to extend slightly the availability of corporate advantages. It empowered the Crown to confer by letters patent all or any of the privileges of incorporation (except limited liability) without actually granting a charter, thus in particular obviating the need for special Acts enabling companies to sue and be sued in the names of their officers.[6] The major importance of this highly illogical compromise was that it was the first general Act requiring public registration of members but it expressly preserved their liability except after three years from parting with their shares. Moreover, its practical value was much diminished by the restrictive rules which the Board of Trade laid down for the granting of petitions under it.[7]

In 1837 the Board of Trade instructed a Chancery barrister, H. Bellenden Ker, to prepare a report on the law of partnership with particular reference to the expediency of introducing limited partnerships on the Continental model.[8] His report[9] was pigeon-holed and the only result was the re-enactment of the 1834 Act in the Chartered Companies Act of 1837[10] but with the valuable extension that personal liability of members might be expressly limited by the letters patent to a specified amount per share. In the ensuing seventeen years some fifty companies did in fact form under this Act, but most still preferred to rely on the *de facto* protection from personal liability conferred by the difficulties of suing and levying execution on the members of a fluctuating body. Many of these were from their inception fraudulent shams, particularly the bogus assurance companies such as those pilloried by Dickens in *Martin Chuzzlewit*,[11] and it was primarily the existence of these which led the Board of Trade to secure the appointment in 1841 of a Parliamentary Committee on Joint Stock Companies. In 1843 Gladstone, who had become President of the Board of Trade, assumed the chairmanship of the Committee and widened the scope of

(3 & 4 Wm. 4, c. 98). These Acts provided that banking companies could sue or be sued in the names of their officers and, in anticipation of the Act of 1844, provided for registration of certain essential particulars.

[5] 4 & 5 Wm. 4, c. 94.

[6] The difficulties with which a suitor might otherwise be faced have already been stressed; they are well exemplified in *Van Sandau* v. *Moore* (1825) 1 Russell 441 in which Lord Eldon, at p. 472, gave this as his principal justification for holding unincorporated companies to be illegal.

[7] They are quoted by Hunt, *op. cit.*, at pp. 57–58. The progressive Huskisson had retired from the Board in 1827, and in 1830 had lost his life in an accident at the opening of the Liverpool and Manchester railway—a victim of the railway boom which he had himself done so much to promote.

[8] John Austin was a staunch advocate of this proposal: see 1825 *Parliamentary History and Review*, p. 711.

[9] 1837 B.P.P., Vol. XLIV, 399.

[10] 7 Wm. 4 & 1 Vict. c. 73.

[11] First published 1843.

its inquiries. Its epoch-making Report [12] and the Joint Stock Companies Act, 1844,[13] which followed it, were mainly due to his genius and energy.

Gladstone's legislation of 1844 and 1845

The 1844 Act introduced three main principles which have constituted the basis of our company law from that time. In the first place it drew a clear distinction between private partnerships and joint stock companies by providing for the registration of all new companies with more than twenty-five members,[14] or with shares transferable without the consent of all the members. Secondly, it provided for incorporation by mere registration as opposed to a special Act or charter; but this it did by a system, curious to modern eyes, of provisional registration, which only authorised the company to function for certain strictly limited preliminary purposes, followed by complete registration on filing a deed of settlement containing the prescribed particulars and other documents when for the first time the company became incorporated.[15] Thirdly, it provided for full publicity which ever since has been regarded as the most potent safeguard against fraud. It is to this Act, too, that we owe the registrar of companies [16] with whom particulars of the companies' constitution, changes therein, and annual returns are filed.

Limited liability, however, was still excluded. Although the company became incorporated, the personal liability of the members was preserved,[17] but their liability was to cease three years after they had transferred their shares by registered transfer [18] and creditors had to proceed first against the assets of the company.[19] Existing companies were compelled to register certain particulars, but did not have the privileges conferred by the Act unless they amended their deeds of settlement so as to comply with its provisions.[20] Winding up was dealt with by a separate Act [21] of the same date which made companies subject to the bankruptcy law. Banking companies were also dealt with by a

[12] 1844 B.P.P., Vol. VII.

[13] 7 & 8 Vict. c. 110. It contained eighty sections and nine Schedules and was by far the most elaborate piece of company legislation attempted in England up to that time. It did not apply to Scotland which was left to its common law (Scottish judges were distinctly more liberal than their English colleagues) until the Act of 1856.

[14] Reduced to the present twenty by the Act of 1856. This provision was based on Ker's report of 1837 which suggested a maximum of fifteen. New assurance companies were also required to register irrespective of the number of members or transferability of shares: s. 2.

[15] We may detect resemblances to this "two-tier" arrangement in the modern provisions for a certificate of incorporation followed later, in the case of a public company, by a "trading certificate" (Companies Act, 1948, s. 109) but there is no historical connection between the two sets of provisions.

[16] s. 19.

[17] s. 25.

[18] This provision was, of course, based on the Trading Companies Act, 1834.

[19] s. 66.

[20] ss. 58–59.

[21] 7 & 8 Vict. c. 111.

separate Act,[22] the provisions of which were generally similar, except that the maximum number of members of an unregistered partnership was six [23] (instead of twenty-five) and that there were stringent requirements for a minimum nominal and paid-up capital. It is perhaps surprising that these latter conditions never became established requirements of English company law for they constitute an essential feature of Continental practice [24] and appear to be a fair price to pay for the boon of simple and cheap incorporation by registration.[25]

Finally, Gladstone prepared and introduced the Bill which was passed under his successor as the Companies Clauses Consolidation Act, 1845.[26] This set out the standard provisions normally included in private statutes of incorporation. These provisions were thereafter to be incorporated by reference, thus materially shortening and cheapening the process of statutory incorporation still necessary in the case of public utilities requiring powers of compulsory acquisition.

Gladstone, therefore, during his short tenure of office as President of the Board of Trade, succeeded for the first time in placing joint stock companies on a sound legal footing; he may fairly be regarded as the father of modern company law. His legislation, however, only solved the legal and not the commercial problems. It gave a company the legal status of a corporation but denied its members the most important advantage of it—freedom from personal liability. In the latter respect the only advance was the recognition that the company itself was primarily liable and that its bankruptcy did not necessarily involve bankruptcy of its members.

The winding-up Acts

The legislation of 1844 was passed at the height of the "railway mania" and the wave of speculation led to promotions in other fields, thus bringing the man in the street into contact with companies as never before, and to an expansion of the stock markets both in London and the provinces.[27] Inevitably, however, the boom was followed by a collapse a year later which changed the emphasis from promotions to liquidations. In 1846 was passed a winding-up Act applying to

[22] 7 & 8 Vict. c. 113.

[23] Later it became ten.

[24] Levy, *op. cit.*, *passim.*

[25] *Cf.* O. Kahn-Freund: "Some Reflections on Company Law Reform" (1945) 7 M.L.R. 54 at pp. 57–59. Such provisions were, in fact, included in the Limited Liability Bill of 1855, but were struck out in Committee. They were reintroduced by the H.L. in an emasculated form but deleted in the Act of 1856.

[26] 8 & 9 Vict. c. 16. A separate Act of the same date dealt with Scottish statutory companies (8 & 9 Vict. c. 17). These Acts contained the general corporate powers and duties and Table A of later Acts owed much to them. They were supplemented in the cases of particular types of utilities by other Acts of the same and later years, see Chap. 1, p. 6, note 16. As Cooke points out (*op. cit.*, p. 119), these were illustrations of a wider tendency to bring under general legislation matters which had previously been left to private Bills; other examples will be found in the fields of divorce, naturalisation and municipal corporations.

[27] Hunt, *op. cit.*, pp. 104 *et seq.*

railway companies[28] and this was followed in 1848[29] and 1849[30] by Acts of general application conferring winding-up jurisdiction on the Court of Chancery. Unhappily the resulting conflicts of jurisdiction between the Courts of Bankruptcy and Chancery led to great confusion,[31] a confusion which, less unhappily, proved highly beneficial to the legal and the new-born accountancy professions.

At a later date[32] the confusion was resolved by the total removal of incorporated companies from the bankruptcy jurisdiction. It is to these historical accidents that we owe the distinction drawn in English law (but unknown to most other systems) between bankruptcy and liquidation; with us an insolvent company is not made bankrupt but is, instead, subject to an analogous process administered under different rules by a different branch of the courts. This development was not completed until after the general recognition of limited liability, but these earlier Acts played a part in the movement which led to this recognition since their emphasis on the administration of the company's assets as a separate estate made still more illogical the distinction drawn between incorporation and limited liability.

The struggle for limited liability

Several features of the Act of 1844 were open to criticism. In particular the cumbersome procedure of provisional and final registration was attacked, but was left unaltered until 1856, though frequently disregarded by unscrupulous promoters[33] who dealt in scrip prior to complete registration.[34]

But, of course, the main cause of complaint was the absence of limited liability and the next ten years saw the battle fairly joined on this issue. It is clear that public opinion began to harden in favour of the extension of limited liability, particularly when the slump of 1845–1848 drew poignant attention to the consequences of its absence. But it was less clear how and to what companies it should be extended.

[28] 9 & 10 Vict. c. 28.

[29] 11 & 12 Vict. c. 45.

[30] 12 & 13 Vict. c. 108.

[31] Admirable accounts appear in Formoy, *op. cit.*, pp. 93 *et seq.*, and Cooke, *op. cit.*, Chap. X. They illustrate their accounts principally by the *Royal British Bank* liquidation (1856) 28 L.T.(o.s.) 224. It is, of course, to this company that we are indebted for the famous rule in *Royal British Bank* v. *Turquand* (*infra*, Chap. 8).

[32] The Joint Stock Companies Act, 1856 (19 & 20 Vict. c. 47) and the Companies Winding Up (Amendment) Act, 1857 (20 & 21 Vict. c. 78).

[33] It is estimated that less than half the provisional registrations were ever followed by complete registration. Shannon, (1931-1932) *Econ.Hist.*, Vol. II, p. 397. See also *ibid.*, pp. 281–282. The defects were emphasised in the Report of the Select Committee on Assurance Associations, 1852–1853, B.P.P. Vol. XXI.

[34] A few amendments were made in 1847 (10 & 11 Vict. c. 78), notably the deletion of the need to file prospectuses, a retrograde step which was apparently taken without any reference to the registrar: see his evidence before the Select Committee on Assurance Associations, *supra*, at p. 13, Q. 160. It was not corrected until 1900.

As a result of the 1844 Act there were three principal types [35] of commercial associations:

1. Private partnerships of not more than twenty-five persons, and quasi-partnership of unlimited dimensions formed before 1844 which had not re-formed under the Act of that year. These were unincorporated and the liability of the members was necessarily unlimited.

2. Chartered and statutory companies, which were incorporated and the members of which were normally free from liability or had their liability limited to a prescribed sum per share.

3. Companies formed or registered under the Act of 1844 which were incorporated but with unlimited liability.

The first question therefore was whether limited liability should be extended to private partnerships on the lines of the Continental *sociétés en commandite*, to registered companies, or to both.

Bellenden Ker's report of 1837 had been directed primarily to private partnerships and the desirability of the *société en commandite*. The 1844 Report had given birth to the third type of association but had not extended limited liability to it; the object of the Commission was to control companies and discourage frauds, not to stimulate promotions. The *société en commandite* was outside the terms of reference of the 1844 Commission but was the main subject of consideration by the Select Committee of 1850 on Investments for the Savings of the Middle and Working Classes, which reported [36] that "the difficulties which affected the law of partnership operate with increasing severity in proportion to the smallness of the sums subscribed and the number of persons included in the association . . . Any measures for the removal of these difficulties would be particularly acceptable to the Middle and Working Classes and would tend to satisfy them that they are not excluded from fair competition by laws throwing obstacles in the way of men with small capitals." The result, as Hunt [37] says, was that the argument for limited liability acquired a "tinge of social amelioration." Hunt's remark has a somewhat sardonic note, and it must be admitted that one can detect more than a slight whiff of Victorian humbug when one reads the evidence of Chancery barristers accepting the eager invitation of M.P.s to persuade them that limited liability was desirable in the interests of the poor. In truth, as the evidence of working class

[35] There were also companies granted letters patent under the Trading Companies Act, 1834, and Chartered Companies Act, 1837, which were unincorporated (unless they registered under the 1844 Act) but with most of the advantages of chartered incorporation except limited liability.

[36] 1850 B.P.P., Vol. XIX, 169.

[37] *Op. cit.* 120. As Mr. G. Goyder emphasises (*The Future of Private Enterprise*, Lond. 1951), the hopes that limited liability would improve the relations between capital and labour have been falsified by events; workers, whose whole livelihood is dependent on the success of the undertaking for which they work, cannot be expected to take kindly to a system which enables the proprietors to limit their risks. Joint stock enterprise has also, of course, contributed to the dehumanising of the master-and-servant relationship.

witnesses makes plain, what the working man required was an improvement in the law of friendly societies particularly as regards housing trusts, co-operative societies and building societies—and this in fact soon came about.[38] John Stuart Mill, more realistically, pointed out[39] that "the great value of a limit of responsibility as it relates to the working classes would be not so much to facilitate the investment of their savings, not so much to enable the poor to lend to those who are rich, as to enable the rich to lend to those who are poor."

A year later a similarly constituted Select Committee considered the law of partnership. On the major issue of limited liability their report[40] was non-committal; it recommended that this vexed question should be referred to a Royal Commission "of adequate legal and commercial knowledge." It did, however, make one firm recommendation, namely, that it should be permissible to lend money at a rate of interest varying with the profits of a business without becoming a partner in the business. At this time it was supposed that such a loan automatically made the lender a partner,[41] and the Committee proposed that instead he should be a deferred creditor in the event of bankruptcy and thus placed in a position not dissimilar to that of a limited partner under a *société en commandite*.

In accordance with the recommendations of the Committee the question was referred to a strong Royal Commission[42] containing representatives from England, Scotland and Ireland.[43] They were, however, quite unable to reach unanimity. They had, they said "been much embarrassed by the great contrariety of opinion. . . . Gentlemen of great experience and talent have arrived at conclusions diametrically opposite; and in supporting these conclusions have displayed reasoning power of the highest order. It is difficult to say on which side the weight of authority in this country predominates." In the result a bare majority of five[44] signed a Report, opposing the general extension of limited liability to joint stock companies or the introduction of the *société en commandite*, and stating that they were unable to agree on the 1851 Committee's proposal regarding loans. Bramwell and Hodgson (a merchant banker), on the other hand, were wholeheartedly in favour of all three proposals. They came out uncompromisingly in favour of *laissez-faire*. "If ever," said Bramwell,[45] "there was a rule established

[38] Industrial and Provident Societies Acts, 1853, 1854 and 1856 (15 & 16 Vict. c. 31; 17 & 18 Vict. c. 25; and 19 & 20 Vict. c. 40); Building Societies Act, 1874 (37 & 38 Vict. c. 42).

[39] In his evidence at p. 78.

[40] 1851 B.P.P., Vol. XVIII, 1.

[41] *Grace* v. *Smith* (1775) 2 Wm.Bl. 998, and see Lindley, *Law of Partnership*, 11th ed., pp. 54 *et seq*.

[42] 1854 B.P.P., Vol. XXVII, 445. The same commission was to consider the assimilation of the mercantile laws of the various parts of the U.K.

[43] The English legal representatives were G. W. Bramwell Q.C. (afterwards Baron Bramwell) Cresswell J. and J. Anderson Q.C. (afterwards an official referee).

[44] Including Cresswell J.

[45] At p. 23.

by reason, authority, and experience, it is that the interest of a community is best consulted by leaving to its members, as far as possible, the unrestricted and unfettered exercise of their own talents and industry." In his opinion the restraint on limited liability offended against this golden rule. He therefore recommended [46] that persons should be allowed as of right to form partnerships limiting the liability of all or some by private agreement followed by registration; and that where the liability of all was to be limited the partnership should be incorporated and the word " limited " added after the name. The remaining member, Anderson, was against the introduction of limited liability and *sociétés en commandite*, but in favour of the 1851 Committee's proposal regarding loans.

In effect, therefore, the majority against limited liability was six out of eight, but despite this the House of Commons immediately passed, without a division, a motion in favour of limited partnerships.[47] On this occasion the Government remained non-committal,[48] but in the following session they introduced two Bills, the Partnership Amendment Bill allowing profit-sharing loans without partnership, and the Limited Liability Bill which provided for limited liability in the case of companies securing complete registration under the 1844 Act subject to certain safeguards. Their bold action in introducing the latter is the more surprising since almost all the prior discussion had related to limited partnerships and not to incorporated companies.

Both Bills secured a second reading in the Commons [49] without a division, but thereafter the former fell a victim to time pressure and proceeded no farther. Nevertheless, the Government determined to press on with the Limited Liability Bill, which was rushed through all its stages in the Commons and given a third reading, again without a division.[50] It was then sent to the Lords who were asked to pass it that same session as a matter of urgency. Certain Lords protested vigorously,[51] and certainly it is difficult to see why the Government, which had sat on the fence for so long, should suddenly regard this as a matter of the utmost urgency at the most critical time of the Crimean War. Doubtless it was true that public opinion, at any rate as represented by the Press,[52] had at last come to favour the measure, but this

[46] At p. 29.
[47] (1854) Hansard, 3rd Ser., Vol. 134, at cols. 752 *et seq.*
[48] Commenting on the speech of Cardwell, the President of the Board of Trade, Cobden said (*ibid.*, col. 779) that " all he could learn of the views of the right hon. gentleman was that he told them when he began that he would not offer an opinion, and he contrived very ingeniously to keep his word."
[49] *Ibid.*, Vol. 139, cols. 310 *et seq.*
[50] *Ibid.*, cols. 1709 *et seq.* (for Committee stage, see cols. 1348, 1378, 1445 and 1517).
[51] Fourteen voted against and nine of them minuted a formal protest (*ibid.*, col. 1918).
[52] By this time even *The Times*, formerly an uncompromising opponent, had come round. Lord Stanley of Alderley (P.B.T.) in introducing the measure in the Lords said that a hostile deputation had " candidly admitted that, with the exception of the *Leeds Mercury*, there was no journal in the kingdom which would admit an article against the principle of limited liability " (Hansard 139, col. 1896). This seems to be an exaggeration so far as the legal Press was concerned, for the

hardly explains the almost indecent haste with which it was pushed through,[53] particularly as the official view still seemed to be that it was a question of abstract principle rather than of practical importance.[54] The Committee stage before the Commons deleted a number of the safeguards which had originally been included, but others were inserted by the Lords which finally passed the Bill without a division.[55] The Commons[56] reluctantly accepted the Lords' amendments and the Bill was given the Royal Assent in August, 1855.

The attainment of limited liability

The Act[57] provided for the limited liability of the members of a company on complete registration if (a) the company had at least twenty-five members holding £10 shares paid up to the extent of 20 per cent., (b) not less than three-fourths of the nominal capital was subscribed, (c) "Limited" was added to the company's name, and (d) the Board of Trade approved the auditors. The directors were to be personally liable if they paid a dividend knowing the company to be insolvent or made loans to the members, and the company had to wind up if three-fourths of the capital was lost.[58] Banks and insurance companies were excluded. The method of limitation was that already used for chartered companies under the Act of 1837 and for statutory companies under the Companies Clauses Act of 1845, namely, the restriction of members' liability to the nominal (unpaid) value of their shares.

Law Times was still most hostile—even to the extent of describing the Bill as the "Rogues Charter"; see (1854) 24 L.T. 142; (1855) 25 L.T. 116 and 210; (1856) 26 L.T. 230; and (1858) 31 L.T. 14. Nor was it universally popular in business circles. The Manchester Chamber of Commerce declared it "so subversive of that high moral responsibility which has hitherto distinguished our Partnership Laws (!) as to call for their strongest disapproval": Proceedings, June 13, 1855, cited by Redford, *Manchester Merchants and Foreign Trade*, p. 215, and Cooke, *op. cit.*, p. 157.

53 It may be that the altruism of 1851 had been supplanted by more selfish fears for self-preservation; by this time the fortunes of the governing classes were in commerce rather than land, there had been a number of disturbing liquidations in 1854–1855 and more were to follow; at the height of the War the future could not have looked rosy. On the other hand, John Bright told the Manchester Chamber of Commerce in 1856 (cited Redford, *op. cit.*, and Cooke, *op. cit.*, *ibid.*) that the Bill was rushed through because the Palmerston administration wanted to be able to say that something had been done besides voting money for the War; but Bright was opposed to the War and hostile to the arch-apostle of limited liability, Robert Lowe (afterwards Viscount Sherbrooke) who had become Vice-President of the Board of Trade in July, 1855.

54 Both Pleydell-Bouverie (the Vice-President of the Board of Trade) in the Commons (*ibid.*, *col.* 329), and Lord Stanley of Alderley (the President) in the Lords (*ibid.*, col. 1919) said that they thought it would prove the wisdom of Adam Smith's view (*supra*) "that in ordinary trading undertakings Joint Stock Companies could not compete with private traders" (*ibid.*, 329), but that there ought to be no legal impediments in the way of competition.

55 *Ibid.*, cols. 1895 *et seq.*, 2025 *et seq.* and 2123 *et seq.*

56 *Ibid.*, cols. 2127 *et seq.*

57 18 & 19 Vict. c. 133. It contained only nineteen sections.

58 An existing company could take advantage of the new Act on complete registration under the 1844 Act if it made the necessary alterations to its deed of settlement by a resolution passed by a three-fourths majority of shareholders voting at a special meeting, and obtained a certificate of solvency from the Board of Trade.

The Limited Liability Act only remained in force for a few months, as it was repealed and incorporated in the Joint Stock Companies Act, 1856.[59] This Act, of 116 sections and a Schedule of tables and forms, was the first of the modern Companies Acts. It did away with provisional registration, superseded deeds of settlement by the modern memorandum and articles of association,[60] and incorporated provisions for winding up. Banks and insurance companies were still excluded but, unlike the earlier Acts, it applied to Scotland. Passed as it was in the heyday of *laissez-faire* it allowed incorporation with limited liability to be obtained with a freedom amounting almost to licence; all that was necessary was for seven or more persons to sign and register a memorandum of association. Virtually, all the safeguards prescribed by the 1855 Act were deleted; there was no minimum nominal or paid up capital or share value, only the provision for winding up on the loss of three-fourths of the capital was retained, and this, too, disappeared in 1862. Board of Trade approval of auditors was not required and even their appointment was no longer compulsory.[61] Directors were still to be liable if they paid dividends knowing the company to be insolvent, but the only other requirements were the use of the word "limited" and provisions for registration and publicity. In effect the legislature had adopted Lord Bramwell's [62] recommendations and accepted his view that those who dealt with companies knowing them to be limited had only themselves to blame if they burnt their fingers. The mystic word "Limited" was intended to act as a red flag warning the public of the dangers which they ran if they had dealings with the dangerous new invention. It is because of the arbitrary separation of personal liability from incorporation which had prevailed for eleven years, that English companies still bear the label "Ltd." instead of the more logical "Inc." of the U.S.A.

The battle for incorporation with limited liability by simple registration was now won and the issue has never been seriously reopened,

[59] 19 & 20 Vict. c. 47. The Government had reintroduced the Partnership Amendment Bill at the same time (Hansard 140, cols. 110 *et seq.*) but this ill-fated measure was ultimately withdrawn (*ibid.*, col. 2201).

[60] Model articles were appended in Table B which became the famous Table A of the 1862 and later Acts.

[61] Provisions regarding auditors were moved from the operative parts, where they had been in the Acts of 1844 and 1855, to the optional Table B. In fact these provisions continued to be adopted expressly or impliedly by most companies, so that the salutary practice of a professional audit remained customary although not again compulsory until 1900 (Companies Act, 1900, *infra*). It had been reintroduced as regards banks by the Companies Act, 1879. For an account of the historical development of the accounting and auditing provisions of the Acts, see Littleton & Yamey, (ed.) *Studies in the History of Accounting*, 356–379.

[62] He was justly proud of the honour of having invented "Limited"; see his speech to the Institute of Bankers in 1888, *Journal of Inst.*, Vol. 9, pp. 373 *et seq.*, and especially p. 397. Llewellyn Smith (*op. cit.*, p. 165) says that he even suggested playfully that the word should be inscribed on his tombstone; I have been unable to find the source of this suggestion and therefore cannot say whether he envisaged it as a laudatory epitaph or a warning to posterity.

although the victory has at times been unpopular.[63] Its importance has sometimes been discounted. Certainly it is true that the various devices, already described, for acquiring *de facto* freedom from liability had become perfected, and this led the *Economist* [64] to regard the issue as of no great importance. Maitland [65] seems to have taken much the same view. "If," he said, "the State had not given way we should have had in England joint stock companies, unincorporated, but contracting with limited liability. We know nowadays that men are not deterred from making contracts by the word 'limited.' We have no reason to suppose that they would have been deterred if that word were expanded into four or five lines printed at the head of the company's letter paper." Nevertheless it is clear that without legislative intervention, limited liability could never have been attained in a satisfactory and clear-cut fashion, and that it was this intervention which finally established companies as the major instrument in economic development. Of this the immediate and startling increase in promotions is sufficient proof.[66]

Subsequent developments

The subsequent history of companies belongs to the modern law and can be sketched more briefly.[67] Its main feature has been a movement away from the complete freedom allowed by the 1856 Act and the imposition of greater controls and increased provisions for publicity—the basic policy of Gladstone's Act of 1844 which had suffered partial eclipse in later Acts.

In 1857 the Act of the previous year was slightly amended,[68] banks were brought within its scope by the Joint Stock Banking Companies Act, 1857,[69] but without limited liability which was not conceded until the following year,[70] and legislation was passed dealing with frauds by directors.[71] In 1862 the various enactments were consolidated and amended in an Act which is the first to bear the brief modern title of

[63] The repeated bank failures during the second half of the nineteenth century caused renewed outburst against limited liability, and in the case of the failure of Overend Gurney, Ltd. in 1866 (see Hunt, *op. cit.*, pp. 153 *et seq.*) these amounted almost to a panic. But had liability been unlimited the failures would have occurred just the same and the victims, although different, would probably have been just as numerous.

[64] (1854) Vol. XII. 698

[65] *Trust and Corporation*, Collected Papers, Vol. III, p. 321, at p. 392.

[66] Between 1844 and 1856, 956 companies were completely registered under the 1844 Act; in the six years following the 1856 Act no fewer than 2,479 were registered and their paid-up capital in 1864 was over £31 millions; Shannon, *op. cit.*, p. 290. For further details see the table at *ibid.*, p. 421.

[67] Students of the history of this later period are referred to Dr. J. B. Jefferys' London Ph.D. Thesis: "Trends in Business Organisation in Great Britain Since 1856" which is unfortunately unpublished but is available in the London University Library. It contains an excellent account of the major trends and an invaluable bibliography.

[68] 20 & 21 Vict. c. 14.

[69] 20 & 21 Vict. c. 49.

[70] 21 & 22 Vict. c. 91.

[71] 20 & 21 Vict. c. 54. See also Larceny Act, 1861 (24 & 25 Vict. c. 96), ss. 81-84.

Companies Act,[72] and which, with numerous amendments,[73] remained the principal Act until 1908. It was considerably larger than the 1856 Act, consisting of no fewer than 212 sections and three Schedules. The additions were mainly amendments to the winding-up provisions and improved and more detailed drafting, but it included insurance companies [74] and also introduced the company limited by guarantee which, as already pointed out,[75] affords a particularly suitable type of organisation for clubs and charitable or quasi-charitable associations.

Limited partnerships and private companies

Hence by 1862 two of the three [76] functions of the modern company had been provided for. Capitalists were encouraged to lend their money to industry without having themselves to operate the enterprise, and fluctuating bodies formed for social or philanthropic purposes could conveniently adopt the company rather than the trust as their *modus operandi*. But, or so it was thought, the need for limited liability within the field of the ordinary partnership or one-man business had still not been met. By the Mercantile Law (Amendment) Act, 1865 [77] (commonly known as Bovill's Act) it was ultimately provided that sharing of profits should not be conclusive evidence of partnership but that lenders, or sellers of goodwill, in consideration of a share of profits should be deferred creditors. At the time it was thought that this had effected a substantial advance by legalising something in the nature of limited partnerships. In fact, as the courts soon held,[78] it did no such thing; it only protected the creditor where he was not in truth associated in the running of the business, if he was he became fully liable as a partner notwithstanding that he was described as a contributor "under Bovill's Act." It therefore made no advance on the decision of the House of Lords in *Cox* v. *Hickman* [79] which had already overruled the rule in *Grace* v. *Smith*.[80] Far from protecting creditors the Act merely worsened their position by making them, in the two most common circumstances, deferred creditors in bankruptcy.

When this was realised there was a renewed outbreak of attempts to introduce full-fledged Limited Partnerships on the Continental model,

[72] 25 & 26 Vict. c. 89. The keen eye of Mr. W. H. Auden is able to detect in this Act the symptoms of a modification of the pure liberal doctrine of *laissez-faire*: *Poets of the English Language*, Vol. 5, p. xxiii.

[73] The most important were the Companies Acts of 1867, 1879 and 1880 (30 & 31 Vict. c. 131; 42 & 43 Vict. c. 76; and 43 Vict. c. 19), the Companies Winding Up Act, 1890 (53 & 54 Vict. c. 63), the Directors' Liability Act, 1890 (53 & 54 Vict. c. 64), and the Companies Act, 1900 (63 & 64 Vict. c. 48).

[74] Hitherto governed by the 1844 Act which had been revived for their benefit: 20 & 21 Vict. c. 80.

[75] *Supra*, Chap. 1, p. 12.

[76] *Supra*, Chap. 1, p. 11.

[77] 28 & 29 Vict. c. 86. This was an amended version of the ill-fated Partnership Bill of 1855.

[78] *Syers* v. *Syers* (1876) 1 App.Cas. 174, H.L.; *Pooley* v. *Driver* (1876) 5 Ch.D. 458.

[79] (1860) 8 H.L.C. 268.

[80] (1775) 2 Wm.Bl. 998, *supra*.

and it was from one such abortive attempt [81] that the Partnership Act, 1890,[82] resulted, although this in its final form merely codified the existing law. In fact, however, the Companies Acts enabled all of the advantages of limited partnerships, and more besides, to be obtained, for the requirement of seven members did not mean that so many as seven had to be beneficially interested—some could be bare nominees for the others and all could thus acquire the benefits of limited liability.[83] When this was established, as a result of the House of Lords' decision in the famous case of *Salomon* v. *Salomon*,[84] the need for limited partnerships had ceased, particularly as the legislature far from discouraging "one-man" and other small "private companies" discriminated in their favour by the Companies Acts of 1900 [85] and 1907 [86] by exempting them from certain of the requirements of publicity. Nevertheless, public opinion, in this instance lagging behind the law, caused limited partnerships to be legalised by the Limited Partnerships Act, 1907.[87] In practice this Act has not been much used because the private limited company involves little more trouble and expense to the members, enables the liability of *all* to be limited, and permits them to take part in the management without forfeiting their freedom from liability.

Case law developments

As already pointed out, the Companies Acts are far from being a complete code and it would be entirely misleading to give an impression that the major developments during the nineteenth century were entirely statutory. On the contrary, the courts, building on the foundations of partnership law, the law of corporations and the statutes, had for the first time evolved a coherent and comprehensive body of company law. Many of the most fundamental and salutary principles were worked out by the courts with little or no help from the statutes and their decisions constitute landmarks which later Acts have done little to obliterate. Thus the House of Lords in *Ashbury Carriage Co.* v. *Riche* [88] applied the *ultra vires* doctrine to companies and laid down that companies could

[81] See the account by the original draftsman, Sir F. Pollock, in the preface to the 12th edition of his *Law of Partnership* (reprinted in the current edition).

[82] 53 & 54 Vict. c. 39.

[83] The result, as has been well said (by O. Kahn-Freund in his notes to Renner, *The Institutions of Private Law* (Lond. 1948) at pp. 221 and 222) is that whereas in the eighteenth and early nineteenth centuries the law of partnership had been pressed into the service of joint stock enterprise, now the legal form of joint stock undertakings has come to annex the functions of the law of partnership. A similar reversal has taken place in the law of Trusts into whose service the joint stock company is now pressed as a Trust Corporation: for a brief history of this development, see D. R. Marsh, "The Friendly Corporation," in (1951) IV Cambridge Jo. 451, and for a fuller account, the same author's *Corporate Trustees* (Lond. 1952).

[84] [1897] A.C. 22, H.L. *Infra*, p. 63.

[85] 63 & 64 Vict. c. 48.

[86] 7 Edw. 7, c. 50.

[87] 7 Edw. 7, c. 24.

[88] (1875) L.R. 7 H.L. 653.

only do acts expressly or impliedly authorised by their memoranda of association. Although, as we shall see,[89] their Lordships' intentions have been largely frustrated by the ingenuity of company draftsmen, and the practical effect of their ruling reduced by later action of the legislature, they at least prevented the misuse of corporate powers and the trafficking in incorporations which had been a scandal at the time of the South Sea Bubble. They also afforded some protection to the public against the abuses of limited liability by enunciating, in cases such as *Trevor* v. *Whitworth*[90] and *Ooregum Gold Mining Co.* v. *Roper*[91] the principle of the raising and maintenance of capital.[92] When principles inherited from partnership law proved unduly restrictive the courts had no hesitation in rejecting them; for example, in *Andrews* v. *Gas Meter Co.*[93] they finally removed the idea that there was any implied condition that all shareholders are to be on an equality, and thus freed companies in their efforts to raise further capital by creating new preference shares.[94] And they protected the investor by laying down, in *Erlanger's Case*[95] and *Gluckstein* v. *Barnes*,[96] that company promoters stood in a fiduciary position towards their fledglings[97] with all the duties of disclosure and good faith which that implies.

On the other hand, they were less successful in evolving principles which would afford adequate protection of the minority against oppression by the majority,[98] and common law rules relating to misrepresentation proved totally inadequate to protect investors against misleading statements by directors in prospectuses; the disastrous decision in *Derry* v. *Peek*[99] had to be promptly modified by the legislature[1] so far as its application to companies was concerned. Further, by construing the statutory rules for public registration as implying constructive notice to all the world of the registered data, they introduced an entirely artificial doctrine which has been fraught with complication and which has caused the basically healthy publicity principle to do almost as much harm as good.[2]

[89] *Infra*, Chap. 5.
[90] (1887) 12 App.Cas. 409, H.L.
[91] [1892] A.C. 125, H.L.
[92] *Infra*, Chap. 6.
[93] [1897] 1 Ch. 361, C.A., overruling *Hutton* v. *Scarborough Cliff Hotel Co.* (1865) 2 Dr. & Sm. 521.
[94] Until the 1948 Act, the model articles in Table A provided that, in accordance with partnership principles, new shares should be offered to the existing shareholders in proportion to their existing holdings. In U.S.A. this remained the common law rule; for the difficulties which it caused, see Berle & Means, *op. cit.*, pp. 146 *et seq.*
[95] *Erlanger* v. *New Sombrero Phosphate Co.* (1878) 3 App.Cas. 1218, H.L.
[96] [1900] A.C. 240, H.L.
[97] See *per* Lord Macnaghten in [1900] A.C. at p. 248.
[98] See Chap. 24, *infra*.
[99] (1889) 14 App.Cas. 337, H.L.
[1] By the Directors' Liability Act, 1890.
[2] We shall see examples of this harm in connection with the *ultra vires* rule (Chap. 5) and the rule in *Royal British Bank* v. *Turquand* (Chap. 8).

Twentieth-century reforms

By the end of the nineteenth century the Board of Trade had established the practice, that has since been followed, of securing the appointment of an expert committee to review company law at intervals of about twenty years, and of carrying out the recommended amendments by a statute which is immediately repealed and incorporated in a consolidating Act. Thus the Companies Act, 1907, was based on the recommendations of the Loreburn Committee,[3] and was followed by the Companies (Consolidation) Act, 1908,[4] which consolidated the mass of legislation since 1862.

A trifling amendment was made in 1913 [5] and there were several wartime measures of which only one [6] remained permanently in force. In 1918 the Wrenbury Committee [7] made certain suggestions but these were not followed up until the Greene Committee [8] made far more extensive recommendations in 1926. Most of these were adopted in the Companies Act, 1928,[9] which was repealed and incorporated in the consolidating Companies Act, 1929.[10] In 1936 the Anderson Committee reported [11] on the problems raised by the analogous institution of the Unit Trust [12] and in 1937 the Bodkin Committee [13] considered the problem of share-pushing in a context wider than that of registered companies alone. Effect was given to the recommendations of both Committees in the Prevention of Fraud (Investments) Act, 1939.[14] During the war years the Government imposed restrictions on the raising of capital by the Defence (Finance) Regulations and these have now been placed on a semi-permanent basis by the Borrowing (Control and Guarantees) Act, 1946,[15] and the Regulations made thereunder. This Act, like the Prevention of Fraud Act, is not restricted in its application to registered companies but it is principally in relation to them that it is important. Here again history has to some extent repeated itself, for just as the State, at the birth of companies, granted or withheld charters in what it believed to be the public interest, so now it grants or withholds the right to raise capital in the same interest.

Finally, the Cohen Committee [16] reported in 1945 and their recommendations, with certain modifications, were enacted in the Companies Act, 1947,[17] which, so far as it amended the Companies Act, was

[3] Cd. 3052/06.
[4] 8 Edw. 7, c. 69.
[5] 3 & 4 Geo. 5, c. 25.
[6] Companies (Particulars as to Directors) Act, 1917 (7 & 8 Geo. 5, c. 28).
[7] Cd. 9138/18.
[8] Cmd. 2657/26.
[9] 18 & 19 Geo. 5, c. 45.
[10] 19 & 20 Geo. 5, c. 23.
[11] Cmd. 5259/36.
[12] As to these, see *infra*, Chap. 11.
[13] Cmd. 5539/37.
[14] 2 & 3 Geo. 6, c. 16.
[15] 9 & 10 Geo. 6, c. 58.
[16] Cmd. 6659/45.
[17] 10 & 11 Geo. 6, c. 47. Certain provisions of this Act remain unrepealed, *e.g.*, those amending the Registration of Business Names Act, 1916, and the Prevention of Fraud Act, 1939.

repealed and incorporated in the consolidating Companies Act, 1948.[18] This Act constitutes the existing legislation governing registered companies.

Problems faced

During the present century the issue with which these Committees and the legislature have been concerned is no longer that of simple and cheap incorporation with limited liability, but with the perfection of its machinery, especially, as the Cohen Committee reported,[19] in two respects.[20]

The first of these is, "to ensure that as much information as is reasonably required shall be made available both to the shareholders and creditors of the companies concerned and to the general public." Here the major developments have been in connection with prospectuses and accounts. As regards the former the statutory provisions have owed much to the stringent requirement of the various stock exchanges (London in particular) for permitting dealings in new issues. Such regulations have, of course, no legal force and until recently they received no legal recognition.[21] In practice, however, they have been far more potent instruments of protection than the legal provisions in the Companies Acts, for it is commercially impossible to make a public issue without obtaining a stock exchange quotation necessitating compliance with the regulations and scrutiny from the stock exchange concerned. Very largely the prospectus provisions of the Acts have been copied from those of the London Stock Exchange after the latter has subjected them to a period of trial. Similarly, as regards accounts, the elaborate provisions in the latest Act are an attempt to codify the minimum requirements of the best accountancy practice.[22] After a long struggle the publication of balance-sheets was made compulsory, in the case of public companies, in 1908. This, however, did not destroy the traditional view of management that even the members should be told as little as possible, and balance-sheets continued to be uninformative and often, because of hidden reserves, positively misleading. The provisions of the 1948 Act are the latest, but doubtless not the last, attempt to secure full disclosure. And this Act, for the first time compels publication and prescribes the contents of the profit and loss account, a document as important as the balance-sheet to the potential investor.

Secondly, the recent amendments have been concerned "to find means of making it easier for shareholders to exercise a more effective general control over the management of their companies." This problem has already been touched on and it is generally admitted that it is one which has not yet been solved.

[18] 11 & 12 Geo. 6, c. 38.
[19] Para. 5.
[20] *Cf.* H. B. Samuel, *Shareholders' Money* (Lond. 1933) *passim.*
[21] But see now Companies Act, 1948, ss. 39 and 51.
[22] Cohen Report, para. 97.

Problems to be faced—companies in the Welfare State

Over and above these questions of internal improvement, the present century has brought to light two major problems of policy which impinge on company law although they transcend its boundaries. The first of these is that of monopolies. This is not a new problem; indeed, as we have seen, the fear of monopolies was a major factor in the early development of companies and one which lingered on well into the nineteenth century. No sooner had it been eradicated than it was realised that the vast industrial empires which could be built up with the aid of companies were potentially very real dangers. In America this realisation led to the Anti-Trust [23] legislation making monopolistic combines subject to the criminal law. In England attempts at control have been more recent and more cautious but the first steps have now been taken in the Monopolies and Restrictive Practices (Inquiry and Control) Act, 1948.[24] It is not difficult to foresee that in the future anti-monopoly legislation may once again play an important part in company law and practice as, indeed, it already does in the U.S.A.

The second major problem is whether industry and trade shall remain largely in the hands of companies or whether they shall be taken over by organs of the State. In Britain and elsewhere many branches of enterprise have already been nationalised, the *modus operandi* having been to vest the undertaking in a new form of corporation, subject to some measure of State control, but not being a branch of the government service like the Post Office. A comparison between these new public corporations and companies must be left to a later chapter [25] (when it will be pointed out that the new type of corporation owes much to company law [26]) and with their rival merits the lawyer as such is not directly concerned. As, however, both are legal institutions it may perhaps be suggested that it entirely misrepresents the nature of the problem to describe it as one of choosing between public and private enterprise. If, by private enterprise, is meant an organisation in which the owners of a business display personal initiative for their personal profit, that issue was lost and won in the nineteenth century when the major part of industry passed to public companies in which the initiative is displayed by a small body of managers, who are not the owners or profit-sharers. In this respect there is no difference between public companies and public corporations. The latter may, indeed, be a solution of the problem of subjecting the managers to some real control by the owners, in this case the public as a whole represented by the

[23] In company matters Equity has suffered badly from debasement of its terms. Not only has "equities" come to mean non-preference shares but its precious "trust" has here been applied to a monopolistic combination.

[24] 11 & 12 Geo. 6, c. 66, as amended by the Monopolies and Restrictive Trade Practices Act, 1953 (1 & 2 Eliz. 2, c. 51), and the Restrictive Trade Practices Act, 1956 (4 & 5 Eliz. 2, c. 68). Similar legislation has been passed in other parts of the Commonwealth.

[25] Chap. 11, *infra*.

[26] Companies were produced by Victorian Liberalism out of the trust; public corporations by twentieth-century Socialism out of companies. Conservatives will take the point that the latter union is within the prohibited degrees.

responsible Minister and Advisory Councils—though whether that is a desirable form of control is another matter, for the relationship between the government and the corporation may create equal difficulties. The difference between the unnationalised public company and the nationalised public corporation is, basically, merely one of legal form. The latter is a new type of corporate entity designed to facilitate the assumption of public control which, however, can alternatively be exercised through the older form of company organisation by the acquisition of the company's shares and the appointment of Government nominees to its board.[27] In the iron and steel nationalisation we had a combination of both forms, for a public corporation, the Iron and Steel Corporation, acquired the whole of the shares in the nominated operating companies which continued to operate as companies.[28]

There now seems, however, to be growing recognition that if the major part of industry and commerce is to be left to unnationalised corporate enterprise, substantial modifications will have to be made in the legal framework of companies. The view has been expressed by writers of very different political leanings, that company law is unreal in that it treats the company as owing duties only to its members, whereas in fact its relationships with its workers, the consumers of its products, and the community as a whole, are of equal if not greater importance.[29] Nor does nationalisation of itself solve all the problems arising out of these relationships. It obviates the difficulties arising between management and shareholders by the extreme measure of abolishing the latter altogether, but the mere conversion of a public company into a public corporation does not necessarily improve the relationship between management and labour—indeed it may make it more difficult [30]—nor that between producer and consumer. The Liberal

[27] As in the case of Cable and Wireless, Ltd. (see the Cable and Wireless Act, 1946), and the British Petroleum Co. (formerly the Anglo-Iranian Oil Co.). As Cooke says (*op. cit.*, p. 180): "A Conservative government may perhaps be said to have begun the fashion when, as a matter of policy, Disraeli's Cabinet bought the Khedive's holding of shares in the Suez Canal Company in 1881." As he also points out (*ibid.*, 136), the possibility of the State's acquisition of public utilities was recognised in principle in Gladstone's Railways Regulation Act, 1844 (7 & 8 Vict. c. 85), and the Reports of the Select Committee which preceded it. Lord Beaverbrook (*Men and Power*, 1917-1918, p. 112) has pointed out that the nationalisation of the Bank of England really began when Bonar Law (a Conservative Chancellor of the Exchequer) in 1917 dismissed Lord Cunliffe from his Governorship of the Bank: for an account of this episode, see *op. cit.*, Chap. 3.

[28] This fact facilitated the "unscrambling" as a result of the denationalisation under the Iron and Steel Act, 1953. To facilitate the denationalisation of road transport it was found necessary to form numerous separate companies which could be sold as going concerns and, even in the sector remaining nationalised, increasing use is made of separate companies controlled by the Transport Commission: see Transport Act, 1953, ss. 4 and 5, as amended by Transport (Disposal of Road Haulage Property) Act, 1956.

[29] *Cf.* W. Mackenzie King in *Industry and Humanity* (Boston, Mass., 1918) and the *Four Parties to Industry* (Toronto, 1919), Lord Eustace Percy in his Riddell Memorial Lecture, *The Unknown State* (Lond. 1944), Chap. 3; and, especially George Goyder in *The Future of Private Enterprise* (Lond. 1951).

[30] Hence it was thought necessary to insert in the various nationalisation Acts provisions for the establishment of joint machinery for settlement of conditions of employment and for consultation on questions of safety, welfare, and the like.

Party have long advocated, as a partial solution of these problems, co-partnership schemes, whereby workers acquire shares in the undertaking; a solution which the existing law does not prohibit although it does little to help.[31] Socialists [32] have argued in favour of compulsory dividend limitation and co-option of government directors on to the boards of all major public companies. More recently, however, leading opinion in the Labour Party seems to be tending towards the policy of governmental acquisition of shares without the assumption of managerial control. This type of "nationalisation" would be intended as an instrument for capital redistribution rather than of State planning. But the most sweeping proposals have come from a representative of business itself, Mr. George Goyder,[33] who believes that the company's obligations to workers, consumers, and the community should be specified as fundamental objects in its memorandum of association and protected by special articles, and that a director should be charged with the responsibility of watching the interests of each of these classes. He even goes so far as to advocate compulsory redemption of members' share capital within fifty years, so that thereafter the ownership of the company would be restricted to workers and management.

It is no part of the purpose of this book to take part in these controversies or to make any recommendations for general reform of company law. Recommendations, such as those of Mr. Goyder, may seem Utopian, and certainly little recognition of the need for any fundamental changes will be found in the Cohen Report which like its predecessors concentrated on the improvement of the existing internal mechanism. But company law has developed with exceptional rapidity in the last hundred years and further changes are inevitable, for company law necessarily reflects the contemporary social and economic outlook.[34] The lawyer of the future will have to play a major part in the shaping of any changes that are resolved upon and to advise on their practicability before they are tried. Before he can do so he must understand the present law, not merely as an arid set of abstract rules, but as an essential part of the working machinery of the modern State.[35]

31 The proviso to s. 54 (1) of the Companies Act, 1948, is designed to help, but its effect is severely limited.

32 *e.g.*, Prof. G. D. H. Cole in the *New Statesman* for May 12, 1951, and for Nov. 12, 1955 (*cf.* the shocked comment in the *Investors' Chronicle* of Nov. 19, 1955). And see especially Albu and Hewitt, *The Anatomy of Private Industry* (1951 Fabian Research Series, No. 145), which, irrespective of politics, contains some useful material.

33 *Op. cit.* This brief summary does less than justice to Mr. Goyder's well-written and stimulating arguments which are not so naïve as they may appear from this bald account.

34 And, in turn, helps to mould the social and economic organisation of which it forms part. The British system of company law, which has been the model for the whole of the Commonwealth and Empire and exercised a considerable influence on the U.S.A., has therefore helped to determine the nature of the economy of the greater part of the English-speaking world.

35 *Cf.* the Report of the Indian Company Law Committee (Delhi, 1952) at p. 14: "It follows . . . that, while company law cannot anticipate economic policy, much less be based on any *a priori* view as to the economic organisation of a country, it is very much its province to have the instruments of policy clearly set out. A precise

The excuse for this somewhat lengthy historical introduction is that this machinery cannot properly be understood without an appreciation of how and why it has evolved. The fact that the modern British company has evolved from the unincorporated partnership based on agreement, rather than from a corporation based on a State grant, accounts for many of its distinguishing features. Its equitable origin accounts for many more. Company matters are still assigned to the Chancery Division and thus, with partnership, are divorced from other commercial matters dealt with on the common law side. There is, in England, no special " Companies Court " in the strict sense; the court described by that name is merely a judge of the Chancery Division exercising in certain company matters the jurisdiction specifically conferred upon it by the Companies Act in winding up and the like.[36] Accordingly modern company law bears the distinctive imprint of the Chancery judges and practitioners who have moulded it, and of traditional Equitable principles and ways of thought. Increasingly its shape has also been influenced by Statute. And an understanding of the statutory rules has equally to be sought in the past—in the particular events and crises which led to their enactment.

formulation of the concepts and categories in company law is necessary not only to define the relationships between the parties interested in the promotion, formation and management of a company, but also to subserve the ends of public policy."

[36] See *Re Wool Textile Employers Mutual Insce. Co.* [1955] 1 W.L.R. 862 at p. 867.

TAB 21

BANKRUPTCY IN CANADA

Lloyd W. Houlden

The purpose of this lecture is to give a general introduction to the *Bankruptcy Act*, particular aspects of which will be discussed in detail in the lectures which are to follow. It is proposed, therefore, to deal with a number of miscellaneous subjects, which it is hoped will carry out this purpose and which will sketch a general background for what you are to hear next.

GENERAL APPROACH TO THE ACT

The general approach to the Act by the Courts has been that it is a commercial statute, the administration of which in the first instance is largely in the hands of businessmen, and technical objections should, therefore, not be given effect to beyond what is necessary to interpret properly the Act (*In re McCoubrey*, 5 C.B.R. 248 and *In re J. F. Camirand Limited*, 4 C.B.R. 344). Although this position has been reiterated in numerous cases, it cannot be relied upon to too great an extent. It can be of use though where narrow and technical objections are being raised, especially as regards some action taken by a trustee.

GENERAL PURPOSES OF THE ACT

Next I would like to review with you the purposes of bankruptcy legislation. I felt that by reviewing these purposes, I might give you an over-all picture of our present bankruptcy legislation and how it operates.

(1) One of the purposes is to permit the property of an insolvent person to be fairly distributed amongst his creditors. This aspect of the *Bankruptcy Act* is not in my opinion being adequately carried out under existing bankruptcy legislation. Time and again the Dominion Government is able to obtain a substantial payment on its claims, and the ordinary creditors receive little or no dividend. If government claims were restricted in their preference to a fixed period of say three months preceding

the bankruptcy, then ordinary trade creditors would be in a much fairer position.

(2) To permit an honest debtor to be discharged from his liabilities and make a fresh start. The present Act sometimes achieves this result too quickly. Under the summary administration provisions of the *Bankruptcy Act,* at the time an assignment is made, an appointment is obtained for the hearing of the debtor's discharge and notification of the application for discharge is sent out with the notice calling the first meeting of creditors. It is quite possible for a debtor to go bankrupt and be discharged within a three-month period under these sections, and this creates considerable dissatisfaction in the trading community. Apart from summary administration, the discharge provisions do, however, work reasonably well.

(3) A third purpose is to permit an investigation to be made of the affairs of the bankrupt. Under the present Act there could be improvement in this respect. One trustee told me that he analogized his position to that of an undertaker. An undertaker, of course, buries a man but makes no examination to find out the causes of death. Similarly in many estates the trustee because of a lack of funds winds up the estate but can make no investigation. It has been suggested that where a trustee suspects that something is not right, he should be able to make a report to the Superintendent of Bankruptcy giving his reasons, and if the Superintendent feels that it is justified, he could then appoint a solicitor or accountant, or both, to make an investigation, and if action is justified, see that it is taken. Even if funds are available, bankruptcy investigations are hard work and frequently do not produce results. A debtor can so cleverly conceal his fraud that it is hard to ferret out the facts, and although you may have your suspicions, it is facts that must be presented to a court.

(4) To permit a proper realization to be made of the assets of the bankrupt. Generally this works very well. Trustees receive a fee of 7½ per cent of the realization after payment of secured creditors' claims, and trustees often achieve amazing results in realization of assets which, of course, increases their compensation.

(5) To compel a debtor who is insolvent to turn over his property to a trustee for distribution. Frequently you will find that if a debtor is stopped soon enough, a fair sized dividend can be paid; and the *Bankruptcy Act* by permitting a petition to be presented does allow a creditor to force a debtor to turn over his assets to a trustee.

Now these are generally regarded as the purposes of bankruptcy legislation, and it is sometimes helpful to review with a client, who is pressing you to issue a petition, some of these purposes and to point out to him what he may hope to achieve by his petition. The layman frequently expects a bankruptcy to produce miracles, and when it fails to do so he is disgruntled. For example, if your client is told that the investigation features of bankruptcy are not always successful, and, although you will do your best, it is impossible to guarantee results, then if nothing is achieved your client is prepared for what occurs.

HISTORY OF THE ACT

Before we proceed further, I would like to remind you very briefly of the history of bankruptcy legislation. The lecturers who follow will, of necessity, be referring to such things as the 1919 Act and the 1949 Act, and it is my hope that this very short summary will make it easier for you to understand what is to follow.

The *B.N.A. Act,* as you know, gave to the Parliament of Canada power to enact laws in relation to matters coming within certain classes of subjects, one of which was "bankruptcy and insolvency". In 1869 an Act was passed by the Dominion Parliament dealing with bankruptcy which remained in force until a new Act was passed in 1875; but in 1880 this Act was repealed and there was no federal bankruptcy legislation in Canada, apart from the *Winding Up Act* which was restricted to corporations, until the *Bankruptcy Act* was passed in 1919.

To judge from the comments contained in some of the cases, the legislation existing prior to 1880 left a good deal to be desired. Apparently the fees of solicitors and trustees were extortionate, and the situation was so bad that the Act was repealed, and it took some forty years before Par-

liament got up enough courage to pass another *Bankruptcy Act* (see the comments of Mr. Justice Middleton in *Bartley's Trustee* v. *Hill,* 1 C.B.R. 477).

The Act, which is the basis of our present *Bankruptcy Act,* was passed by the Dominion Parliament in the 1919 session (9-10 Geo. V, c. 36) and became operative by Royal Proclamation on July 1, 1920. This Act was largely patterned after the English *Bankruptcy Act* of 1914. Since 1920 the Act has been amended almost constantly, and the whole Act was revised and given a careful going over prior to the 1949 session, and a new Act was passed (13 Geo. VI, c. 7) which came into force on July 1, 1950. The Act was streamlined and improved by the 1949 revision. Some of the changes were a little drastic, and time has shown weaknesses in some of the sections, but on the whole it has worked quite well. Two of the principal changes made by the 1949 Act were:

(1) The abolition of the office of custodian. Under the former Act, a custodian was appointed in the assignment or receiving order who held office up to the first meeting of creditors, but under the present Act the trustee is now appointed in the assignment or receiving order and is affirmed at the first meeting of creditors.

(2) The composition and arrangement sections were overhauled, and provision was made for proposals being made to creditors without bankruptcy occurring.

CONSTITUTIONALITY

This history of bankruptcy legislation leads naturally to a consideration of constitutional law. You will remember that prior to the enactment of the 1919 *Bankruptcy Act,* a number of the provinces had passed statutes which had an effect similar to bankruptcy legislation such as *The Assignments and Preferences Act* of Ontario (R.S.O. 1950, c. 26). This legislation was held in *The Assignments and Preferences Act* case, [1894] A.C. 189 to be valid in the absence of any Dominion legislation on this subject. In the earlier case of *Cushing* v. *Dupuy,* 5 App. Cas. 409, the Privy Council had upheld the validity of the 1875 *Insolvency Act* and

recognized that it must of necessity interfere with and modify property and civil rights, and that there was power not only to deal with the substantive law of bankruptcy by Dominion legislation but also to provide a code of procedure.

Two very practical problems arise out of the constitutional issue, *firstly,* when does a section of the *Bankruptcy Act* cease to be bankruptcy legislation and become an interference with property and civil rights and hence *ultra vires,* and *secondly,* how far can provincial statutes dealing with subjects analogous to bankruptcy legislation still be resorted to now that we have a federal *Bankruptcy Act.*

In considering the first problem, the general principle is well established that the pith and substance of the enactment must be determined, or putting it on the basis of the ancillary doctrine, if the legislation is ancillary to the powers given the Dominion Government by section 91 and is necessary to make the legislation workable and effective, it is valid, but if it is not ancillary or necessary to the effective working of the Act, it is *ultra vires.* While it is easy to state the general principle, it is difficult in practice to determine when you go beyond the boundary of necessarily incidental or ancillary to and pass into the provincial field of property and civil rights. To illustrate this problem for you, I would like to give you two examples, one of which held that the Dominion legislation was bad, and the other held the legislation to be good. In the 1919 Act, section 52 made substantial encroachments on the rights of landlords, and provision was made by subsection (5) that notwithstanding the provisions of any lease the trustee could elect to retain the unexpired portion of the lease. It was held in the case of *In re Stoper,* 4 C.B.R. 34, that this was not properly ancillary to bankruptcy legislation and was *ultra vires.* On the other hand in the case of *Larue* v. *Royal Bank of Canada,* 7 C.B.R. 285 and 8 C.B.R. 579, the Privy Council held that the *Bankruptcy Act* could validly provide that a receiving order or assignment should have precedence over the rights created prior to bankruptcy by an execution in the Province of Quebec.

Coming to the second problem, as to Provincial Acts which can still be made use of, it has been held that *The Fraudulent Conveyances Act* (R.S.O. 1950, c. 148) can still be used to

attack transactions which cannot be set aside under the provisions of the *Bankruptcy Act* (*In re Davison,* 5 C.B.R. 860; *In re United Exhibitors,* 5 C.B.R. 200 and 779; *In re Cohen and Mahlin,* 7 C.B.R. 655 and 8 C.B.R. 23). It was early decided that the provisions of *The Bulk Sales Act* of Ontario had not been superseded by the *Bankruptcy Act,* and that if the proceeds of a bulk sale were in the hands of a trustee under *The Bulk Sales Act* he could retain them against a trustee in bankruptcy (*In re St. Thomas Cabinets,* 1 C.B.R. 521). A great deal of litigation has taken place with regard to the provisions of *The Assignments and Preferences Act.* A number of cases suggested that a transaction which did not fall within section 64 of the *Bankruptcy Act* because it had occurred more than three months prior to the bankruptcy could be attacked under section 4 of *The Assignments and Preferences Act* (*In re Davison,* 5 C.B.R. 860; *In re Berman,* 4 C.B.R. 233; *In re Cohen and Mahlin,* 7 C.B.R. 655 and 8 C.B.R. 23; *Re Pommier,* 11 C.B.R. 449); however, in the case of *In re Trenwith,* 15 C.B.R. 372, the Ontario Court of Appeal held that the provisions of *The Assignments and Preferences Act* were no longer available to a trustee, and the *Trenwith* case was subsequently approved by the Supreme Court of Canada in the *Bozanich* case, 23 C.B.R. 234, so that our jurisprudence appears to be settled.

OFFICERS AND OFFICIALS WHO ADMINISTER THE BANKRUPTCY ACT

THE SUPERINTENDENT OF BANKRUPTCY

At the present time the Superintendent is Mr. J. S. Larose. He is a man with a considerable background of experience in the Superintendent's Office, and he knows the Act extremely well.

So far as lawyers are concerned, the average lawyer doing bankruptcy work will have little occasion to deal with the Superintendent. Most of the Superintendent's work is with the trustee, and it is only when some unusual problem arises that you will have any dealings with this office.

The Superintendent has a general supervisory function over all estates (section 3(2)). He handles the licensing of trustees (section 3(3)). Under the new Ontario *Corpora-*

tions Act, 1953 (Statutes of Ontario 1953, c. 19) provision is made for granting a charter to a trustee in bankruptcy, and the only occasion that I have ever dealt with Mr. Larose was on a trip to Ottawa to find out what the Superintendent's Office would require before they would grant a licence to such a corporate trustee.

The Superintendent looks after the bonding of trustees, and he has power to bring action to enforce such bonds (section 3(3)(c) and see *In re Savignac*, 21 C.B.R. 214).

The Superintendent keeps records of all bankruptcies throughout Canada, and he checks the trustee's final statements, and he must approve them before the trustee receives his discharge from the court (section 3(3)(d), (g)). He can, if he sees fit, intervene in any matter or proceeding in the bankruptcy court and sometimes he exercises this power (section 3(4)). The Minister of Justice on report from the Superintendent has power to cancel or suspend a trustee's licence and appoint some other trustee to administer his estates (section 6(2)). On the application of the debtor for his discharge the Superintendent has the power to make a report to the court (section 128(3)). When a bankruptcy offence has been committed, the Official Receiver or trustee must make a report to the Superintendent (section 163(1)), and the Superintendent has power to apply to the Bankruptcy Court for leave to initiate criminal proceedings against the debtor (section 163(3), (4)).

One of the most important matters for solicitors in connection with the Superintendent is his levy. Section 106 provides for a levy on all payments made by the trustee apart from the payment of the first execution creditor's preferred costs. The levy is one per cent on all payments under $1,000,000 (Rule 108).

In the case of *In re Kop Beverages*, 32 C.B.R. 221, it was decided that the levy was payable not only on payments to ordinary and preferred creditors, but also on payments made by the trustee to secured creditors. In that case the trustee had sold certain property in which he had only a small equity. The sale was for all cash, and the trustee was required to pay off certain large mortgages and liens, and the levy amounted to $1,100 on one secured claim and $500 on

another. It was held that the Superintendent's levy must be deducted from these payments which meant a substantial loss to the secured creditors. If a sale by a trustee is made with the levy in mind, arrangements can often be worked out to avoid the *Kop* case and save the secured creditors this money.

Not all payments made to secured creditors are, however, subject to the levy. It has been decided that when a trustee collects accounts receivable or realizes security covered by section 88 for a bank, which is frequently done as a matter of convenience in bankruptcy, no levy is payable when the proceeds are turned over to the bank by the trustee (*In re Colonial Manufacturing*, 15 C.B.R. 244).

THE REGISTRAR

The Registrar is appointed by the Chief Justice of the Supreme Court of Ontario (section 141). The present Registrar is, as most of you know, Mr. F. G. Cook, Q.C. He has had a long experience in the administration of the *Bankruptcy Act*, and he is always ready to assist both trustees and lawyers and to share his experience with them. To Mr. Cook and his very capable secretary, Miss Marjory Colloton, must be given credit for the efficient and capable operation of the Bankruptcy Office. It is one of the few legal offices where a practitioner can take his problems and get helpful advice as to the procedure to be followed.

The general powers of the Registrar are conferred by section 149. Under this section:

(1) The Registrar has power to hear unopposed matters such as petitions for receiving order, applications for approval of proposals, etc. In connection with approval of proposals, a proposal is deemed to be opposed if any fact is set out in the trustee's report which would justify the Court in refusing to approve the proposal (Rule 83).

The Act gives power to the Registrar to hear unopposed applications for discharge, but the practice in Ontario is to refer all these applications to the judge.

(2) The Registrar can make interim orders in cases of urgency. For example, the Registrar has power to grant an

interim injunction if the judge is not available and the matter is urgent.

(3) The Registrar conducts examinations of the bankrupt and other persons. As we shall see, it is the obligation of the Official Receiver to conduct the first examination of the bankrupt after the assignment or receiving order. As Mr. Cook is also the Official Receiver for Bankruptcy Division No. 9, which includes the counties of York, Peel and Ontario, he conducts the examinations for these counties, and they are usually heard at ten o'clock in the morning. The Registrar is always happy to have a solicitor attend on these examinations and put questions; and where you wish information before the first meeting of creditors, it is sometimes helpful to attend on the examination and ask the Court for permission to put your questions. Apart from the examination before the Official Receiver, wide powers of examination are given by section 121, and these examinations can be conducted before the Registrar or one of the special examiners. Where it is a routine examination I follow the practice of conducting the examination before a special examiner, but where it is an important matter and there have been serious defalcations I try, if at all possible, to conduct them before the Registrar. The Registrar, in my experience, is able to give much more effective rulings than a special examiner, and the surroundings in which the Registrar conducts the examinations makes a much more serious impression on debtors.

(4) The Registrar hears appeals from disallowance of claims by the trustee. The trustee should not use the method of disallowance for secured claims, and it is only appeals from disallowances of unsecured claims that the Registrar has jurisdiction to try. On secured claims a motion to the judge for determination of the question is the proper procedure (*Re Shapiro*, 29 C.B.R. 203).

(5) The Registrar taxes costs of solicitors and passes the accounts of trustees. Where a matter has been opposed, he usually refers it to the taxing master to tax costs, but the ordinary bill of costs for services rendered to the trustee is taxed before the Registrar.

(6) The Registrar can hear contested matters where all parties consent.

(7) Matters of practice and procedure are determined by the Registrar.

(8) The Registrar settles and signs all orders and judgments of the court.

An appeal lies from a decision of the Registrar to the judge. The Registrar has power to refer any matter ordinarily within his jurisdiction to the judge, and this power is exercised by Mr. Cook where it is a matter of difficulty or of importance (*In re Arthur Flint Co. Ltd.*, 25 C.B.R. 156).

Under the original Act there was considerable doubt whether the Registrar and the judge had co-extensive jurisdiction. The first Registrar, Mr. Holmstead, felt that the whole bankruptcy jurisdiction of the court could be exercised by the Registrar (*In re Shortt*, 2 C.B.R. 449); but a number of cases held that this was not correct, and it is now clearly established that apart from the special provisions in section 149 the Registrar has no power to deal with opposed matters (*In re Dumais*, 5 C.B.R. 540).

The Registrar has power to make interim receiving orders and in practice they are usually made by him. However, an application to fix damages occasioned by an interim receiving order which has been improperly obtained cannot be heard by the Registrar (*In re Stuart & Sutterby*, 11 C.B.R. 279; *In re Bartram*, 11 C.B.R. 345). If an application is improperly heard by the Registrar, and a party attends and argues the motion, he can still argue the lack of jurisdiction of the Registrar on an appeal to the judge even though no objection was taken before the Registrar to the matter of jurisdiction (*In re Stuart & Sutterby* and *In re Bartram*, *supra*).

THE OFFICIAL RECEIVER

The Province of Ontario is constituted under the Act as a Bankruptcy District (section 4), and the Province is subdivided into Bankruptcy Divisions. There are sixteen Bankruptcy Divisions in the Province of Ontario, and for each Division there is an Official Receiver. Usually a Division includes more than one county. Where there is a vacancy

in the office of an Official Receiver, the Registrar performs the duties (section 4(4)). When an assignment is made, the papers in connection with the assignment are filed with the Official Receiver in the locality of the debtor. Similarly, once the receiving order is made, a true copy of the order is filed with the Official Receiver. The Official Receiver on receipt of these papers fixes a time for the first meeting of creditors.

Prior to the first meeting of creditors the Official Receiver conducts the examination of the bankrupt. The procedure on this examination varies greatly. In Toronto, Mr. Cook conducts a formal examination in which he reviews the questionnaire, which has been completed by the debtor, and clears up any points which are in doubt. Out of town, it is more usual for the Official Receiver to be satisfied merely with going over the questionnaire with the debtor (see *R.* v. *Davidson,* 14 C.B.R. 475).

The Official Receiver has the power to have the meeting held at the office of another Official Receiver, or such other place as he sees fit (section 68(1)). It is sometimes handy when the creditors are mainly from Toronto, but the debtor has conducted his business elsewhere, to get an order from the Official Receiver that the meeting be held in Toronto and be presided over by the trustee.

The Official Receiver fixes the amount of the bond to be filed by the trustee, and he has power to increase or decrease it (section 8(1)). If an estate has been a large one, and by virtue of interim dividends most of the assets have been distributed, expense can be saved by getting an order decreasing the amount of the bond.

At the first meeting the Official Receiver, or his nominee, acts as chairman and decides all questions which arise (*In re Maritime Eduction Co. Ltd.,* 11 C.B.R. 333) subject to an appeal to the courts (*In re Louis Webber,* 12 C.B.R. 274 and *In re Brittania Canning Co. Ltd.,* 19 C.B.R. 250). In Toronto the trustee is almost always nominated to act as chairman of the first meeting of creditors, but out-of-town the Official Receiver usually conducts the meeting. Once the first meeting is over the Official Receiver makes his report to the Registrar of what has taken place at the first meeting of creditors and forwards the questionnaire and long state-

ment of affairs and other documents to the Bankruptcy Office at Osgoode Hall.

Apart from the filing of Assignment or Receiving Order, the setting of the date for the first meeting of creditors, and the holding of the first meeting of creditors, the Official Receiver has very little to do with this official. The solicitor's duties usually commence after the first meeting of creditors, and from that time on the proceedings are conducted through the Registrar's office at Osgoode Hall.

JURISDICTION

Section 140 is the general section conferring jurisdiction. It provides that the Supreme Court of Ontario is invested with such jurisdiction at law and in equity as will enable it to exercise original, auxiliary and ancillary jurisdiction in bankruptcy and in other proceedings authorized by the Act. Section 140 (2) confers authority upon the Court of Appeal to hear appeals in bankruptcy matters and section 140 (3) gives authority to the Supreme Court of Canada.

By section 142 the Chief Justice of the Supreme Court of Ontario has power to name a judge to exercise the judicial powers and jurisdiction conferred by the Act. The present bankruptcy judge is the Honourable Mr. Justice Smily. He administers the *Bankruptcy Act* fairly and expeditiously. Discharge of debtors is a very difficult job for the judge, and rather than attempt, as some of the judges have done, to lay down rigid rules, the present judge has followed the practice of deciding each case on its merits, which has worked extremely well.

It should be noted that the Act did not create a new court. It is common to refer to the Bankruptcy Court but this description is not accurate. All that the *Bankruptcy Act* has done is to confer on a pre-existing court a jurisdiction in bankruptcy, and it is well established that all judges of the Supreme Court have jurisdiction in bankruptcy and power to deal with bankruptcy matters. The provisions in the Act which provide for the designation of a particular judge to deal with bankruptcy questions has been inserted in the Act for convenience of administration and in no way deprives any other judge of jurisdiction (*In re Dominion Shipbuilding*, 7 C.B.R. 349).

At the present time, the judge in bankruptcy sits twice a month, and all sittings are in chambers and gowns are not worn. All applications to the court are made by motion (Rule 12) and the procedure is simple and inexpensive.

The court is given power under the Act to review, rescind, or vary any order (section 144(5)). This is a very useful power but, of course, it is not exercised too freely. It has been held that on such an application to the court, evidence must be presented which is not merely corroborative of what was heard previously but some new evidence must be brought forward (*In re Bryant Isard & Co. Kent's Claim*, 3 C.B.R. 534; *In re Barter*, 3 C.B.R. 677; *In re Capital Trust Corporation*, 24 C.B.R. 207).

There is power to transfer proceedings from one bankruptcy court to another if it means that the affairs of the bankrupt can be more economically administered in the other court (section 144(7)). One bankruptcy court can request the aid of another bankruptcy court in a matter arising under the Act (section 145(2)). In the case of *In re Legace*, 3 C.B.R. 124, the bankruptcy occurred in Quebec but a certain party in Manitoba had in his possession papers and documents of the bankrupt company. The Quebec court requested that the Manitoba court assist in obtaining possession of these papers and documents, and in due course pursuant to this request an order was made by the Manitoba court for this purpose (*In re Legace, supra*).

A bankruptcy court has power throughout the Dominion. For example, in one case a bankruptcy occurred in Quebec, and there were certain assets in the United States, and an Ontario creditor conceived the idea of taking proceedings in the United States to seize these assets to satisfy his claim. The Quebec court held that it had authority to restrain this creditor from taking such proceedings (*In re Mount Royal*, 8 C.B.R. 240).

The court has power, if it sees fit, to direct the trial of an issue by a judge or officer of another court of the province, and such decision is subject to an appeal to the judge in bankruptcy unless it is a Supreme Court judge to whom the matter has been referred when it goes to the Court of Appeal

(section 144(8)) (*In re Belleville Milling*, 12 C.B.R. 507; *In re Fulton*, 7 C.B.R. 199).

A very handy section is section 144(9). It provides that no proceeding in bankruptcy shall be invalidated by any formal defect or irregularity unless a substantial injustice has occurred which cannot be remedied by an order of the court. I have made use of this section where a trustee sent out notices by ordinary mail which should have gone by registered mail.

Section 144(10) gives a wide power of extending time even after the time provided for in the Act has elapsed, and this again can be very useful where some error has occurred. Section 144(12) gives the court power to omit certain material required by the Act, or to direct that it be sent by ordinary mail. If you have a large bankruptcy with a vast number of creditors and limited assets, subsection (12) can be of great use in saving the trustee time and expense.

Even if no specific provision exists in the Act for making a certain order or directing that something be done, it has been held that there is an auxiliary jurisdiction conferred by the Act which permits the making of the required order. For example, the Act makes no provision for setting aside an assignment which has been improperly filed, but it has been held that the court under its auxiliary jurisdiction can make such an order (*In re Tlustie*, 3 C.B.R. 654; *In re Sims Packing Co.*, 4 C.B.R. 367; *In re Jacobson*, 8 C.B.R. 258).

The really difficult problem, which arises under the heading of jurisdiction, is the relationship between the so-called Bankruptcy Court and the ordinary jurisdiction of the Supreme Court of Ontario. When should an action be brought in the Bankruptcy Court, and when should it be brought by the ordinary procedure in the Supreme Court of Ontario? The problem in effect is tied in with the constitutional issue. The Bankruptcy Court has no jurisdiction over property and civil rights but only over bankruptcy issues and matters necessarily incidental thereto; and as has been pointed out earlier, it is difficult to say when you pass from one field to another. There have been any number of cases on this question, and certain principles have emerged.

Firstly, where it is sought in the proceedings before the judge in bankruptcy to obtain some remedy which is given by the Act (for example, to declare a transaction to be a fraudulent preference or a settlement), these proceedings are properly brought in the Bankruptcy Court (*In re Levine,* 1 C.B.R. 479). On the other hand, if the question in dispute in no way affects the bankruptcy, it is clear that it cannot be brought before the judge in bankruptcy for decision. For example, in the case of *In re Princeton Tailors Ltd.,* 12 C.B.R. 208, a trustee in bankruptcy admitted that the bank and the landlord had superior claims to certain inventory. The bank brought an application before the bankruptcy judge to have it decided that it had superior rights to the landlord, and it was held that the judge had no jurisdiction to hear this application (see also *Stobie Forlong* v. *Beck,* 13 C.B.R. 392). An action brought by or against a person who is a party to the bankruptcy is properly brought in the Bankruptcy Court. For example, if a trustee disallows a creditor's claim the creditor's appeal is properly brought in the Bankruptcy Court for a determination of this question.

It is frequently stated that where a stranger to the bankruptcy is involved the action should not be brought in the Bankruptcy Court. The neat question is to determine who is a stranger to the bankruptcy.

The leading case on the problem is *In re Morris Lofsky,* 28 C.B.R. 165. In that case a receiving order had been made against Mr. Lofsky on February 11, 1947. On March 31, 1947, Mr. Lofsky transferred to his wife a motor car. Mrs. Lofsky said that the car had been her property since its purchase, but for convenience, and because she had been sick, it had been put in her husband's name. The trustee brought an application before the judge in bankruptcy to have an issue directed to determine the ownership of the car. It was argued for Mrs. Lofsky that the proceedings were in the wrong court, because if her contentions were right, her husband never had any interest in the car, and she was a stranger to the bankruptcy. The Ontario Court of Appeal accepted this argument and said that the bankruptcy judge had no jurisdiction. The question raised here was, according to the court, a question of property and civil rights and not a bankruptcy matter. Since the *Lofsky* case,

a new section has been added to the *Bankruptcy Act* (section 50(5)) which provides that no proceedings shall be instituted to establish a claim to or recover any right or interest in any property in the possession of a bankrupt at the time of his bankruptcy, except as provided in that section. If section 50(5) is *intra vires*, then the question which arose in the *Lofsky* case could now be determined by the judge in bankruptcy. In view of the decision in the *Lofsky* case, and other similar cases, it is doubtful whether section 50(5) would be held to be *intra vires.*

One Quebec judge solved this problem in a unique fashion. On an application to attack a preference given more than three months prior to the bankruptcy, it was argued that the judge in bankruptcy had no jurisdiction. The judge said that there was no separate Bankruptcy Court but merely an additional function had been given to an existing court, and as he had already heard the evidence, he would refer the matter to himself in his dual capacity as a bankruptcy judge and as a judge of the Superior Court and give the proper judgment (*In re Paltiel,* 15 C.B.R. 720).

There have been any number of cases on jurisdiction. The days of strict pleading are a thing of the past, and I submit that it is improper that lawyers should be plagued with this problem. It would seem ludicrous to a layman that a judge who has jurisdiction both in bankruptcy and in ordinary litigation should not be able to give all proper remedies merely because the action was commenced by a motion, instead of by a writ, but unfortunately this is the law.

I am sorry that I cannot give you any simple rule of thumb, but the question is difficult, and I have only been able today to sketch it for you. In the printed lectures I have referred to some eighteen additional cases, which I hope you will find useful when the problem arises in practice.

The following additional cases have been decided on the matter of jurisdiction where there is a conflict between the two courts:

Eastern Trust v. *Lloyd Manufacturing Co.,* 3 C.B.R. 710
In re Canadian Carpet Co., 4 C.B.R. 423 and 5 C.B.R. 54
Viscount Grain Growers v. *Brumwell,* 4 C.B.R. 340

In re Nobert, 4 C.B.R. 586
McLennan v. *Carter*, 8 C.B.R. 56
In re Reynolds, 10 C.B.R. 127
In re Walker, 11 C.B.R. 288
In re Payette, 12 C.B.R. 224
Longue Pointe Development v. *Eastern Trust Co.*, 13 C.B.R. 217
Lemieux v. *McCauley*, 21 C.B.R. 127
In re Maple Leaf Fruit Co., 30 C.B.R. 23
In re Martin, 33 C.B.R. 163
Re M. B. Greer & Co., 33 C.B.R. 69
In re Rousseau, 14 C.B.R. 182
In re Savignac, 21 C.B.R. 214
In re Maritime Mining Co. Ltd., 21 C.B.R. 319
In re Dominion Utilities, 21 C.B.R. 430

OTHER STATUTES DEALING WITH THE WINDING UP OF CORPORATIONS

The Dominion *Winding Up Act*, R.S.C. 1952, c. 296 by section 6 applies to Dominion companies and to insolvent provincial companies. An application is made to court for a winding up order, and the Act then sets out the procedure to be followed by the liquidator. Section 153 of the 1927 *Bankruptcy Act* provided that by leave of the court, a company which was in bankruptcy could be wound up under the *Winding Up Act*, but this section was not carried forward into the 1949 Act, and whether or not a court could make such an order at the present time is uncertain.

The Dominion *Companies Act*, R.S.C. 1952, c. 53, makes provision for surrendering the charter of a company where there are no debts or liabilities, or where an arrangement has been made with creditors, and *The Corporations Act, 1953* of Ontario (Statutes of Ontario 1953, c. 19) makes similar provisions (section 366). The Ontario Act also makes provision for winding up of provincial companies (Part 7) either voluntarily or, if the company is not insolvent, by order of the court.

TAB 22

Bankruptcy and Insolvency Law of Canada, 4th Edition § 2:36

Bankruptcy and Insolvency Law of Canada, 4th Edition
The Honourable Mr. Justice Lloyd W. Houlden, Mr. Justice Geoffrey B. Morawetz, Dr. Janis P. Sarra

Part I. The Bankruptcy and Insolvency Act

Chapter 2. Part I Administrative Officials

VIII. Sections 16 to 29

§ 2:36. Duties and Powers of Trustees—Generally

Although ss. 16–38 deal with the powers and duties of trustees, various other sections of the Act confer powers and impose duties on the trustees. However, in addition to the powers and duties specifically conferred by the Act, the court exercising bankruptcy jurisdiction has, for the purpose of carrying out the provisions of the Act, the necessary power and jurisdiction to authorize and sanction acts required to be done by the trustee in the due administration and protection of the estate, even though there are no specific provisions in the Act expressly conferring such powers and jurisdiction: Re Tlustie (1923), 3 C.B.R. 654, 23 O.W.N. 622 (S.C.). See § 8:4 "Jurisdiction of the Bankruptcy Court".

The Superintendent of Bankruptcy has issued a number of policy statements dealing with the duties and powers of trustees. These are found in vol. 5 under Policy Statements, including Directive No. 4R, issued November 17, 1994, which deals with delegation of tasks. Directive No. 28 provides for the "Non-Resident Office" of a trustee. Such an office must be registered with the Bankruptcy Administrator for the area in which the office is located. Directive No. 29 sets out the guidelines for advertising by trustees.

A trustee must know the provisions of the Act and *Rules* including the duties and powers of the trustee; the trustee cannot plead ignorance of the Act and *Rules* as an excuse for non-compliance with them: Re Bryant Isard & Co. (1923), 4 C.B.R. 41, 24 O.W.N. 597 (Ont. S.C.).

The trustee can make use of valid provincial legislation that is not in conflict with the *Bankruptcy and Insolvency Act*, s. 72(1); Robinson v. Countrywide Factors Ltd. (1977), 23 C.B.R. (N.S.) 97, [1978] 1 S.C.R. 753, [1977] 2 W.W.R. 111, 72 D.L.R. (3d) 500, 14 N.R. 91; Paccar Financial Services Ltd. v. Sinco Trucking Ltd. (Trustee of) (1989), 73 C.B.R. (N.S.) 28, [1989] 3 W.W.R. 481, (*sub nom. Paccar Financial Services Ltd. v. Touche Ross Ltd.*) 74 Sask. R. 181 (C.A.); Passmore (Trustee of) v. Heinrichs Bros. Holding Co. (1990), 79 C.B.R. (N.S.) 306, 1990 CarswellSask 50 (Sask. Q.B.).

It is essential that the trustee have no interest that will conflict with its administration of the bankrupt estate; it must be wholly impartial: Re Martin (1888), 21 Q.B.D. 29, 5 Morr. 129, 57 L.J.Q.B. 384; Re Lamb; Ex parte the Board of Trade, [1894] 2 Q.B. 805, 64 L.J.Q.B. 71, 38 Sol. Jo. 667 (C.A.).

A trustee in bankruptcy is an officer of the court: Re Beetown Honey Products Inc. (2003), [2003] O.J. No. 3853, 2003 CarswellOnt 3755, 46 C.B.R. (4th) 195, 67 O.R. (3d) 511 (Ont. S.C.J.); affirmed (2004), 3 C.B.R. (5th) 204, 2004 CarswellOnt 4316 (Ont. C.A.).

As an officer of the court, the trustee should impartially represent the interests of creditors: Re Roy (1963), 4 C.B.R. (N.S.) 275 (Que. S.C.). The trustee has an obligation to be neutral and evenhanded in its dealings with all classes of creditors and with the bankrupt. The court must ensure that the trustee has been transparent and evenhanded in meeting these obligations: Engels v. Richard Killen & Associates Ltd. (2002), 35 C.B.R. (4th) 77, 2002 CarswellOnt 2435 (Ont. S.C.J.), affirmed (2004),

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48 C.B.R. (4th) 68, 2004 CarswellOnt 62, 181 O.A.C. 94 (Ont. C.A.); Re Reed (1980), 34 C.B.R. (N.S.) 83, reversing 32 C.B.R. (N.S.) 203 (Ont. C.A.).

In bringing proceedings, such as an application to set aside a fraudulent preference, the trustee in giving evidence should not adopt an adversarial or hostile role: Touche Ross Ltd. v. Weldwood of Canada Sales Ltd. (1983), 48 C.B.R. (N.S.) 83, additional reasons at (1984), 49 C.B.R. (N.S.) 284 (Ont. S.C.). Rather, the trustee should present the relevant facts to the court in a dispassionate, non-adversarial manner, and leave the matter to the court for decision. Where a claim of litigation privilege asserted by a trustee would call into question the trustee's impartiality, the court will deny the privilege claim: Re Beetown Honey Products Inc. (2003), [2003] O.J. No. 3853, 2003 CarswellOnt 3755, 46 C.B.R. (4th) 195, 67 O.R. (3d) 511 (Ont. S.C.J.); affirmed (2004), 3 C.B.R. (5th) 204, 2004 CarswellOnt 4316 (Ont. C.A.).

In making business decisions relating to sale of the bankrupt's assets, a trustee, with the authorization of inspectors, must exercise reasonable business judgment, must act with honesty and integrity, and must provide advice to inspectors equivalent to advice one would expect from a reasonably competent trustee in the circumstances: Re Krzysztof Stanislaw Geler (2005), 2005 CarswellOnt 2094, 12 C.B.R. (5th) 15 (Ont. S.C.J.).

In Ontario, an officer of a court of justice is ineligible to serve as a juror, and consequently a trustee in bankruptcy is ineligible to serve as a juror: Re Page (2002), 38 C.B.R. (4th) 241, 2002 CarswellOnt 3892, 27 C.P.C. (5th) 310 (Ont. S.C.J. [Commercial List]).

The trustee is the legal representative of the bankrupt: Grobstein v. Kouri, [1936] 3 D.L.R. 9, [1936] S.C.R. 264, 17 C.B.R. 333, 3 I.L.R. 415; Mercure v. A. Marquette & Fils Inc. (1975), 65 D.L.R. (3d) 136, [1977] 1 S.C.R. 547, 10 N.R. 239; Metal Fabricating & Construction Ltd. (Trustee of) v. Husky Oil Operations Ltd. (1997), 153 D.L.R. (4th) 432, 1997 CarswellSask 628, (*sub nom. Bank of Montreal v. Deloitte & Touche Inc.*) 97 D.T.C. 5538, (*sub nom. Metal Fabricating & Construction Ltd. (Bankrupt), Re*) 158 Sask. R. 302, 153 W.A.C. 302, [1998] 5 W.W.R. 335, 1 C.B.R. (4th) 1, 37 C.L.R. (2d) 159 (Sask. C.A.), leave to appeal refused (1998), 227 N.R. 292 (note), 168 Sask. R. 319 (note), 173 W.A.C. 319 (note) (S.C.C.).

A trustee is the representative of unsecured creditors and as such has the necessary status to maintain proceedings to have security declared invalid by reason of its failure to comply with provincial legislation. The provincial legislation can confer on the trustee a greater interest in property than that possessed by the bankrupt: Re Margaritis (1977), 23 C.B.R. (N.S.) 150, 16 O.R. (2d) 83, 77 D.L.R. (3d) 359, 1 P.P.S.A.C. 1, 1977 CarswellOnt 64 (C.A.); Re Giffen, [1998] 1 S.C.R. 91, 1 C.B.R. (4th) 115, 45 B.C.L.R. (3d) 1, 155 D.L.R. (4th) 332, 222 N.R. 29, 101 B.C.A.C. 161, 164 W.A.C. 161, [1998] 7 W.W.R. 1, 13 P.P.S.A.C. (2d) 255, 1998 CarswellBC 147, 1998 CarswellBC 148, [1998] S.C.J. No. 11 (S.C.C.).

Although a trustee in bankruptcy has all the powers of a receiver appointed by the court, a receiver does not have the powers of a trustee in bankruptcy: China Shoftware Corp. v. Leimbigler (1990), 4 C.B.R. (3d) 185, 1990 CarswellBC 391, 4 C.P.C. (2d) 41 (B.C. Master).

A trustee must conduct itself in such a manner as to avoid a conflict between its interest and duty, and the trustee must not profit from the assets at the expense of the creditors of the bankrupt estate. Thus, it is improper for a trustee to delay the winding-up of the bankrupt estate because of an expected change in the fees allowed to trustees: Re Frustaglio (1985), 56 C.B.R. (N.S.) 158 (Ont. S.C.).

Where the company acted as trustee and receiver manager, and took inconsistent positions regarding security in their two capacities, the court observed that the receiver manager may be exposed to a claim for damages. The case highlights the need for care when the possibility of conflict arises. In this case, the trustee fulfilled its duty to challenge the security, but a conflict arose exposing the receiver manager to damages: Re Orion Truck Centre Ltd. (2003), 47 C.B.R. (4th) 99, 2003 CarswellBC 1857, 17 B.C.L.R. (4th) 337, 6 P.P.S.A.C. (3d) 93, 2003 BCSC 1167 (B.C. S.C. [in Chambers]) (See as well § 12:2).

A trustee is bound by the *Bankruptcy and Insolvency Act* and cannot refuse to enforce its provisions or refuse to carry out its statutory requirements: Re Stefaniuk (2001), 27 C.B.R. (4th) 162, 2001 SKQB 308, 210 Sask. R. 157, 2001 CarswellSask 505 (Sask. Q.B.).

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The trustee's obligation is to act for the benefit of the general body of creditors, not just the benefit of unsecured creditors. The trustee must not, therefore, act in a manner that is prejudicial and unfair to the interests of secured creditors: Bank of Montreal v. Touche Ross Ltd., 60 C.B.R. (N.S.) 244, [1986] 4 W.W.R. 211, 48 Sask. R. 241 (Sask. Q.B.).

A trustee in bankruptcy does not function as an agent of the creditors in the ordinary sense, but as an administrative official required by law to gather in and realize on the assets of the bankrupt, and then to divide the proceeds among those entitled thereto in accordance with the scheme set out in the *Bankrupty and Insolvency Act:* Clarkson Co. v. Muir (1982), 43 C.B.R. (N.S.) 259, 53 N.S.R. (2d) 609, 109 A.P.R. 609 (C.A.).

An officer of the court, the trustee has an absolute duty to make full and frank disclosure of what has occurred in the administration of the bankrupt estate. Where a trustee informed the court that the inspectors had approved the trustee's final statement of receipts and disbursements when, in fact, one inspector had not approved it, the court reduced the trustee's remuneration by one-half: Re Van Straten (1997), 46 C.B.R. (3d) 96, 1997 CarswellAlta 239 (Alta. Q.B.).

A trustee in bankruptcy has a duty to realize as much as possible from the estate for the benefit of the creditors. Where the trustee is aware that unless some account is taken of the bankrupt's future income the creditors would receive nothing, it is incumbent on the trustee to make a realistic assessment of the bankrupt's only asset his future earning potential as a doctor. The trustee must determine whether or not, through the attachment of conditions to a discharge, the asset can reasonably generate a return to the estate, even though it may not be realizable immediately. Where the bankrupt was completing a medical residency at the time of the discharge application and had a limited current ability to pay, the discharge order was crafted to reflect the bankrupt's real future earning potential: Re Coffey (2004), 2004 CarswellNfld 160, 2 C.B.R. (5th) 121, 2004 NLSCTD 22, (*sub nom. Coffey (Bankrupt), Re*) 235 Nfld. & P.E.I.R. 66, 699 A.P.R. 66 (N.L. T.D.).

In considering the conduct of a trustee, the trustee's actions should be judged by the reasonableness of the business approach taken at the time of the action, and not necessarily by whether the actions attain satisfactory results: Re Brown (2003), 2003 CarswellAlta 1637, 2003 ABQB 899, 48 C.B.R. (4th) 38 (Alta. Q.B.).

The Ontario Superior Court of Justice reviewed the basis for solicitor-client privilege and litigation privilege and determined, in this case, that the trustee, as an independent court officer, was required to produce documents and information that it considered to be privileged. Justice Gates noted that three prerequisites must be satisfied before the privilege can be invoked: a communication between the client and his or her lawyer, which entails either the seeking of or the giving of legal advice, and the parties intend the information to be confidential. It is the client's privilege and can only be waived by it. Gates J. held that the party claiming the privilege must show that a substantial purpose of a document was the contemplation of litigation. Secondly, a “competing interest” approach must be applied to determine whether the harm arising from non-disclosure clearly outweighs any benefit arising from it; whether there is more harm done by preventing disclosure than by protecting it. Gates J. also observed that litigation privilege is not a black hole from which evidence of one's misconduct can never be exposed to the light of day. Access may be ordered in favour of a party seeking disclosure of material that might otherwise be subject to litigation privilege where a *prima facie* case of actionable misconduct by the other side can be demonstrated. A trustee is an officer of the court who has an obligation of fairness and impartiality to all creditors. Gates J. was of the view that this obligation does not change because one of the creditors, for its own commercial or business reasons, provides funds to the trustee to bankroll litigation. Gates J. concluded that what was at stake was fairness and consistency flowing from the trustee's statutory obligations relating to the production and protection of the remaining records. These principles trumped the notion of privilege: Impact Tool & Mold Inc. (Receiver of) v. BDO Dunwoody Ltd., 2013 CarswellOnt 9048, 2 C.B.R. (6th) 120, 2013 ONSC 2616 (Ont. S.C.J.), leave to appeal denied 2013 CarswellOnt 15576, 2013 ONCA 697 (Ont. C.A.).

See Frank Bennett, “The Trustee's Role on Discharge Hearings, Taking Responsibility from the Beginning to the End” (2012), 94 C.B.R. (5th) 167.

The Newfoundland and Labrador Supreme Court granted the application of a discharged bankrupt for an order that she was no longer liable for her student loans. Justice Orsborn commented on the role of the trustee, which had urged the court to allow

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the application and not leave the applicant with a lengthy period of indebtedness and uncertainty. Orsborn J. observed that the trustee is an officer of the court and should act equitably and, as far as possible, hold an even hand between competing interests of various classes of creditors. The trustee should present the relevant facts to the court in a dispassionate, non-adversarial manner, and leave the matter to the court to decide. Here, the trustee's participation on behalf of the discharged bankrupt went beyond being objective and informative, and was not an approach to be encouraged: Re Taylor, 2017 CarswellNfld 413, 53 C.B.R. (6th) 177, 2017 NLTD(G) 177 (N.L. T.D.). For a discussion of this judgment, see § 7:207 “Debts not Released by an Order of Discharge—Student Loans”.

In a proposal application, creditor “A” brought an application challenging the trustee's acceptance of the proof of claim of creditor “H”. The application was granted, Justice Fitzpatrick of the British Columbia Supreme Court finding that the trustee had not properly carried out its duty under the *BIA* to perform an independent assessment of H's claims. This failure led to the application by A. The Court allowed the appeal and ruled that H's claim should be reduced to $809,382. Creditor A sought its costs of the application. Justice Fitzpatrick held that s. 197(3) of the *BIA* makes it clear that a trustee will not normally be held personally liable for costs of an application in a proceeding. Here, however, Fitzpatrick J. held that the trustee took an adversarial position by arguing positions for both H and the debtor, and seemed to have abandoned any impartial attitude towards the creditor in favour of the debtor's proposal. The Court held that it had no hesitation in awarding the costs against the trustee personally. Justice Fitzpatrick concluded that the entire appeal could have been avoided if the trustee had properly performed its independent and impartial role in the first place: Re Asian Concepts Franchising Corporation, 2019 CarswellBC 2279, 64 C.B.R. (6th) 117, 2018 BCSC 1464 (B.C. S.C).

The Newfoundland and Labrador Supreme Court held that the bankrupt lacked standing to bring a motion on his own behalf and on behalf of a related corporate entity—which was registered in Newfoundland and Labrador, and owned and operated warehouses where it rented space to cryptocurrency miners for computers, servers and the other hardware—to remove the plaintiff's counsel as solicitor in its claims against the bankrupt and the related entity. The bankrupt's trustee had standing to bring the motions, but Handrigan J. questioned the propriety of the trustee acting as an advocate for the bankrupt: Re Great North Data Ltd., 2020 CarswellNfld 73, 77 C.B.R. (6th) 27, 2020 NLSC 48 (N.L. S.C.).

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Bankruptcy and Insolvency Law of Canada, 4th Edition § 5:460

Bankruptcy and Insolvency Law of Canada, 4th Edition

The Honourable Mr. Justice Lloyd W. Houlden, Mr. Justice Geoffrey B. Morawetz, Dr. Janis P. Sarra

Part I. The Bankruptcy and Insolvency Act

Chapter 5. Part IV Property of the Bankrupt

VI. Section 91

§ 5:460. Fraudulent Conveyances—Generally

The provisions of the *Bankruptcy and Insolvency Act* are not to be deemed to abrogate or supersede the substantive provisions of any other law or statute relating to property and civil rights that are not in conflict with the Act: s. 72(1). The trustee is entitled to avail itself of all rights and remedies provided by such law or statute to supplement the rights and remedies provided by the *Bankruptcy and Insolvency Act:* see s. 72(1). Provincial *Fraudulent Conveyances Acts* do not conflict with the *Bankruptcy and Insolvency Act*, and a trustee in bankruptcy is entitled to make use of such legislation to supplement the rights and remedies provided by the *Bankruptcy and Insolvency Act:* Duro Lam Ltd. v. Last (1970), 15 C.B.R. (N.S.) 20, [1971] 2 O.R. 202 (H.C.); Allison & Burnham Concrete Ltd. v. Mountain View Const. Ltd. (1965), 9 C.B.R. (N.S.) 52, 53 W.W.R. 274, 54 D.L.R. (2d) 67 (B.C. S.C.); Robinson v. Countrywide Factors Ltd. (1977), 23 C.B.R. (N.S.) 97, [1978] 1 S.C.R. 753, [1977] 2 W.W.R. 111, 14 N.R. 91, 72 D.L.R. (3d) 500; Re Optical Recording Laboratories Inc. (1990), 1990 CarswellOnt 143, 2 C.B.R. (3d) 64, 75 D.L.R. (4th) 747, 42 O.A.C. 321, 1 O.R. (3d) 131 (Ont. C.A.); Flightcraft Inc. v. Parsons (Trustee of) (1999), 12 C.B.R. (4th) 35, 68 B.C.L.R. (3d) 197, [2000] 1 W.W.R. 461, 125 B.C.A.C. 228, 204 W.A.C. 228, 175 D.L.R. (4th) 642, 1999 CarswellBC 1373 (C.A.).

Fraudulent conveyances provisions should be read in conjunction with provisions addressing preferences and transfers at undervalue. Sections 95, 96 and 96.1 create a complete framework for challenging transactions that may diminish the value of the insolvent debtor's estate, reducing the amount of money available for distribution to the creditors. Section 95 specifies that a transfer of property made, provision of services made, a charge on property made, a payment made, an obligation incurred or a judicial proceeding taken or suffered by an insolvent person in favour of a creditor who is dealing at arm's length with the insolvent person, or a person in trust for that creditor, with a view to giving that creditor a preference over another creditor is void as against the trustee, or, in Québec, may not be set up against the trustee, if it is made during the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy. For creditors not dealing at arm's length with the insolvent person, or a person in trust for that creditor, that period is twelve months.

Under the amendments, settlements and reviewable transactions were replaced with a single cause of action, “transfer at undervalue”. The court will determine as a question of fact whether the transfer was at undervalue, and whether the parties were at arm's length or at non-arm's length. Persons who are related to each other are deemed not to deal at arm's length unless there is evidence to the contrary. If the court finds that the transaction was a transfer at undervalue and that the other party was at arm's length, the court may grant judgment for the difference between the actual consideration and the fair market value if the transfer took place within one year before the date of the initial bankruptcy event and the debtor was insolvent at the time of the transfer and the debtor intended to defeat the interests of creditors. If the court finds that the transaction was a transfer at undervalue and that the other party was not at arm's length, the court may grant judgment for the difference between the actual consideration and the fair market value if the transfer took place within one year before the date of the initial bankruptcy event or within one to five years before the date of the initial bankruptcy event if the debtor was insolvent at the time of the transfer or intended to defeat the interests of creditors. If the preference was made to a non-arm's-length creditor within one year, no intention test is required; rather, it is an effects-based test.

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By the *Bankruptcy and Insolvency Act*, the trustee is the representative of all the unsecured creditors of the bankrupt: see § 2:36 "Duties and Powers of Trustees— Generally". Under the *Fraudulent Conveyances Acts*, the creditors are given the right to impeach transactions that the bankrupt himself or herself could not impeach. The trustee therefore, in seeking to set aside an alleged fraudulent conveyance, is asserting a higher and better title to property than the bankrupt; for the bankrupt is a party to the alleged fraud: Re Harrison; Ex parte Butters (1880), 14 Ch. Div. 265. If the action is successful, the trustee will recover property of the bankrupt for the benefit of unsecured creditors.

The *Fraudulent Conveyances Acts* are based on the *Statute of Elizabeth:* 1571, 13 Eliz. 1, c. 5. The purpose of the *Statute of Elizabeth* is to put the parties in the position they would have been had the transfer not occurred. Although the language of the statute has been modernized, the basic intent of the legislation is still the same as in the original Act. Nova Scotia has no *Fraudulent Conveyances Act*, but it has been held that the original *Statute of Elizabeth* is still in force in that province, even though it has been repealed in England: Bank of Montreal v. Crowell (1980), 34 C.B.R. (N.S.) 15, 37 N.S.R. (2d) 292, 67 A.P.R. 292 (T.D.). A similar result was reached in Saskatchewan: McCallum (Trustee of) v. McCallum (1998), 5 C.B.R. (4th) 223, 1998 CarswellSask 598 (Sask. Q.B.).

The language of the *Fraudulent Conveyances Act* is broad and all encompassing. The statute should be given a liberal interpretation: Nicholson v. Milne (1989), 74 C.B.R. (N.S.) 263, 67 Alta. L.R. (2d) 130, 96 A.R. 114 (Q.B.); Re Optical Recording Laboratories Inc. (1990), 1990 CarswellOnt 143, 2 C.B.R. (3d) 64, 75 D.L.R. (4th) 747, 42 O.A.C. 321, 1 O.R. (3d) 131 (Ont. C.A.); Ramgotra (Trustee of) v. North American Life Assurance Co., 1996 CarswellSask 212F, 1996 CarswellSask 418, 37 C.B.R. (3d) 141, [1996] S.C.J. No. 17, [1996] 1 S.C.R. 325, [1996] 3 W.W.R. 457, [1996] 1 S.C.R. 325 (S.C.C.); Krumm v. McKay (2003), 47 C.B.R. (4th) 38, 2003 CarswellAlta 961, 17 Alta. L.R. (4th) 103, 342 A.R. 169, 2003 ABQB 437, [2003] 9 W.W.R. 442 (Alta. Q.B.). The aim of the *Fraudulent Conveyances Act* is to catch virtually any transaction made with the intent to delay or defeat creditors: Boudreau v. Marler (2002), 2002 CarswellOnt 5844, 18 R.P.R. (4th) 182, 48 C.B.R. (4th) 178 (Ont. S.C.J.), affirmed (2004), 2004 CarswellOnt 1502, 18 R.P.R. (4th) 165, 48 C.B.R. (4th) 188, 185 O.A.C. 261 (Ont. C.A.).

In Alberta Social Housing Corp. v. Khosla (2003), 2003 CarswellAlta 921, 44 C.B.R. (4th) 172, 19 Alta. L.R. (4th) 318, [2004] 3 W.W.R. 403, 2003 ABQB 556 (Alta. Q.B.), it was held that the court must assess what would have happened had the bankrupt not attempted to delay or hinder creditors by making the fraudulent conveyance. The conveyance before the court had occurred thirteen years prior to the plaintiff obtaining the judgment that resulted in the defendant making her assignment in bankruptcy. Although in most cases, the setting aside of the fraudulent conveyance is all that will be required, in view of the lapse of time from the conveyance to the date of judgment, the court determined that setting aside the conveyance was an inappropriate remedy. The court concluded that the property would have been attached approximately ten days after the plaintiff obtained judgment. The property fraudulently conveyed was therefore valued as of that date for the purposes of distribution to creditors.

The effect of the *Fraudulent Conveyances Act* is that a conveyance that is fraudulent and void against creditors is not absolutely void but only voidable; the conveyance is valid as between the parties to it and remains valid as between the parties even if the conveyance is declared to be a fraudulent coveyance: 384238 Ontario Ltd. v. R., 37 C.B.R. (N.S.) 126, [1981] C.T.C. 129, 81 D.T.C. 5098 (Fed. T.D.); Bank of Montreal v. Bray (1997), 36 O.R. (3d) 99, 50 C.B.R. (3d) 1, 1997 CarswellOnt 3903, 33 R.F.L. (4th) 335, 14 R.P.R. (3d) 139 (C.A.); Re Lawrason's Chemicals Ltd. (1999), 87 C.P.R. (3d) 213, 1999 CarswellOnt 392 (Ont. C.A.).

A trustee is entitled to relief under the *Fraudulent Conveyances Act even though the status quo ante* cannot be restored, e.g., the transferee has conveyed the property to an innocent third party: Bank of Montreal v. Bray (1997), 36 O.R. (3d) 99, 50 C.B.R. (3d) 1, 33 R.F.L. (4th) 335, 14 R.P.R. (3d) 139, 1997 CarswellOnt 3903 (C.A.).

The *Fraudulent Conveyances Act* does not prohibit a debtor from preferring one creditor over another. If the intent of the transferor was only to prefer the creditor or creditors, a conveyance executed in favour of one or only some of the creditors of the transferor will be valid even though the transferor knows that he or she is insolvent and even though the conveyance comprises the whole of the transferor's property: Bank of Montreal v. Ngo (1985), 56 C.B.R. (N.S.) 66, 66 B.C.L.R. 171 (S.C.); Anderson Lumber Co. v. Can. Conifer Ltd., 25 C.B.R. (N.S.) 35, [1977] 5 W.W.R. 41, 4 A.R. 282, 77 D.L.R. (3d) 126 (C.A.);

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Canada Life Insurance Co. v. 494708 Alberta Ltd. (1995), 1995 CarswellAlta 362, 32 Alta. L.R. (3d) 311, 173 A.R. 172, [1996] 1 W.W.R. 21 (Alta. Q.B.). The fact, however, that a conveyance is made to a creditor does not mean that it cannot be attacked as a fraudulent conveyance: Re Optical Recording Laboratories Inc. (1990), 1990 CarswellOnt 143, 2 C.B.R. (3d) 64, 75 D.L.R. (4th) 747, 42 O.A.C. 321, 1 O.R. (3d) 131 (Ont. C.A.). The *Fraudulent Conveyances Act* does not prohibit a preference but prohibits only those conveyances entered into with the intention to harm other creditors: Royal Bank v. Morrison (1992), 15 C.B.R. (3d) 273, 43 R.F.L. (3d) 278, 1992 CarswellOnt 195 (Ont. Gen. Div.).

While the *Statute of Elizabeth* is not directed against the preference of one creditor over another, it will apply if in the course of making the preference the debtor obtains some benefit for itself: Krumm v. McKay (2003), 47 C.B.R. (4th) 38, 2003 CarswellAlta 961, 17 Alta. L.R. (4th) 103, 342 A.R. 169, 2003 ABQB 437, [2003] 9 W.W.R. 442 (Alta. Q.B.).

Unlike proceedings under the *Bankruptcy and Insolvency Act* attacking a fraudulent preference, pressure brought to bear upon a debtor by a creditor is admissible under the *Fraudulent Conveyances Act:* Royal Bank v. Morrison (1992), 15 C.B.R. (3d) 273, 43 R.F.L. (3d) 278, 1992 CarswellOnt 195 (Ont. Gen. Div.).

The definition of “conveyance” in the *Fraudulent Conveyances Act* is not exhaustive; rather it gives examples of what the term will cover. It does not include a voluntary disclaimer of a beneficiary's entitlement under a will, since a disclaimer is not a conveyance of property but a refusal to accept property. If the beneficiary received a payment for the disclaimer, it would come within the definition of “conveyance” as it would constitute an assignment: Bank of N.S. v. Chan (1987), 68 C.B.R. (N.S.) 118, 26 E.T.R. 180 (Man. Q.B.).

“Conveyance” is wide enough to encompass every method of disposing of, or parting with, property or an interest therein, absolutely or conditionally. It is wide enough to cover the transfer of an annuity from a mutual fund into an insurance policy that is exempt from seizure: Nicholson v. Milne (1989), 74 C.B.R. (N.S.) 263, 67 Alta. L.R. (2d) 130, 96 A.R. 114 (Q.B.).

For a “conveyance”, there must be a transfer of property. A milk quota under the Ontario *Milk Act* is not property and hence a transfer of such a licence cannot be attacked as a fraudulent conveyance: Canadian Imperial Bank of Commerce v. Hallahan (1990), 69 D.L.R. (4th) 449, 39 O.A.C. 24, 1990 CarswellOnt 126 (C.A.).

“Conveyance” is not confined to written conveyances and is wide enough to include transfers made without consideration. Charitable donations can constitute “conveyances”: Toronto Dominion Bank v. Miller (1990), 3 C.B.R. (3d) 285, 1 O.R. (3d) 528, 1990 CarswellOnt 153 (Bktcy.).

The designation of a beneficiary under an insurance policy constitutes a “conveyance” or “disposition” of property falling within the *Fraudulent Conveyances Act:* Re Sykes (1998), 156 D.L.R. (4th) 105, 2 C.B.R. (4th) 79, 1998 CarswellBC 120 (B.C. C.A.).

A transfer of shares may constitute a fraudulent conveyance. A sole shareholder in a private company is guilty of a fraudulent conveyance if the shareholder dilutes the value of his or her interest in the company by causing the company to issue treasury shares to his or her spouse: Re Kostiuk (1999), 14 C.B.R. (4th) 101, 1999 CarswellBC 2528 (B.C.S.C.).

In order to successfully attack a transaction as a fraudulent conveyance, there is no need to show that there was some benefit, material or spiritual, to the debtor when he made the conveyance: Toronto Dominion Bank v. Miller (1990), 3 C.B.R. (3d) 285, 1 O.R. (3d) 528, 1990 CarswellOnt 153 (Bktcy.).

The time to determine whether a conveyance is fraudulent is the time of the conveyance: Woodmann Interiors Ltd. v. Zeh (1989), 75 C.B.R. (N.S.) 100, 98 A.R. 68, 1989 CarswellAlta 345 (Q.B.); not the time of the registration of the conveyance: Bank of Montreal v. Chu (1994), 24 C.B.R. (3d) 136, 17 O.R. (3d) 691, 1994 CarswellOnt 260 (Gen. Div.).

There is no necessity under the *Fraudulent Conveyances Act* to prove that the grantor was insolvent at the time of the making of the conveyance: Burton v. R & M Insurance Ltd. (1977), 26 C.B.R. (N.S.) 49, 5 Alta. L.R. (2d) 14, 9 A.R. 589, 81 D.L.R. (3d) 455 (T.D.); Re Barnett (1983), 46 C.B.R. (N.S.) 211 (Alta. Q.B.); Bank of Montreal v. Shore (1983), 46 C.B.R. (N.S.) 294 (N.S. T.D.); Re Hansen (1977), 26 C.B.R. (N.S.) 57 (Ont. H.C.); Bank of Montreal v. Crowell (1980), 34 C.B.R. (N.S.) 15, 37 N.S.R.

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(2d) 292, 67 A.P.R. 292 (T.D.); Bank of N.S. v. Simpson (1984), 52 C.B.R. (N.S.) 183, 64 N.S.R. (2d) 383, 143 A.P.R. 383 (T.D.); Bank of Montreal v. Marleau (1994), 29 C.B.R. (3d) 180, 1994 CarswellSask 30 (Sask. Q.B.); Ocean Construction Supplies Ltd. v. Creative Prosperity Capital Corp. (1995), 34 C.B.R. (3d) 241, 1995 CarswellBC 373 (B.C. S.C.); Krumm v. McKay (2003), 47 C.B.R. (4th) 38, 2003 CarswellAlta 961, 17 Alta. L.R. (4th) 103, 342 A.R. 169, 2003 ABQB 437, [2003] 9 W.W.R. 442 (Alta. Q.B.). In this respect, the Act differs from the *Assignments and Preferences Acts* and *Fraudulent Preferences Acts:* see § 5:469 “Attacking Fraudulent Conveyances under Provincial Assignments and Preferences Acts, Fraudulent Preferences Acts and Similar Statutes”. If a conveyance renders the transferor insolvent, this fact is evidence that the conveyance is fraudulent: Ocean Construction Supplies Ltd. v. Creative Prosperity Capital Corp. (1995), 34 C.B.R. (3d) 241, 1995 CarswellBC 373 (B.C. S.C.).

A fraudulent conveyance is an act of bankruptcy: see *above*, s.42(1)(b) and § 3:50.

In order to attack a transaction as a fraudulent conveyance, the trustee must prove that the bankrupt had a beneficial interest in the property and that he or she conveyed this interest to the grantee: Bank of N.S. v. Leifer (1978), 28 C.B.R. (N.S.) 291 (Ont. H.C.); Serenity Farms Ltd. v. Traversa (1985), 55 C.B.R. (N.S.) 214 (Ont. H.C.). If, at the time of the conveyance, the debtor had no beneficial interest in the property because he was holding it on a resulting trust for his wife, the conveyance cannot be attacked as a fraudulent conveyance: Bank of N.S. v. Leifer (1978), 28 C.B.R. (N.S.) 291 (Ont. H.C.); Bank of N.S. v. Brickell (1980), 36 C.B.R (N.S.) 1, 22 B.C.L.R. 222 (S.C.); Janodee Investments v. Weisz (1996), 38 C.B.R. (3d) 119, 1996 CarswellOnt 177 (Ont. Gen. Div.). Similarly, where property was put in the joint names of husband and wife because the mortgagee insisted, but the husband never had any beneficial interest in the property and never contributed towards its purchase or upkeep, it was held that a conveyance by the husband to the wife of his joint interest could not be attacked as a fraudulent conveyance: C.I.B.C. v. Fenner (1983), 47 C.B.R. (N.S.) 156, 34 R.F.L. (2d) 167 (Ont. H.C.); but see Bank of Montreal v. Kelliher (1980), 36 C.B.R. (N.S.) 205 (B.C. S.C.).

The Nova Scotia Supreme Court held that the transfer of certain assets did not constitute a fraudulent conveyance or a conveyance with the intention to defraud, hinder or delay creditors and was, therefore, not an act of bankruptcy under ss. 42(1)(b) or (g) of the *BIA*. The court held that an appeal of a decision of a registrar is a true appeal and not a hearing *de novo*, and that such a decision should not be overturned unless an appellant can establish that the registrar erred in principle in failing to take into account a proper factor or by taking into account an improper factor that demonstrably led to a wrong conclusion. It is not enough that a court might have reached a different result based on the evidence: Heritage Salmon Ltd. v. Atlantic Ova Pro Ltd. (2006), 2006 CarswellNS 300, 2006 NSSC 224, 23 C.B.R. (5th) 167 (N.S.S.C.).

A conveyance of exempt property, such as a homestead, is not a fraudulent conveyance: Woodmann Interiors Ltd. v. Zeh (1989), 75 C.B.R. (N.S.) 100, 98 A.R. 68, 1989 CarswellAlta 345 (Q.B.). However, if the bankrupt's interest in the conveyed property is greater than the amount of the exemption allowed by law, the excess can be found to be a fraudulent conveyance: Re Sawatsky (2001), 28 C.B.R. (4th) 116, 2001 CarswellAlta 799, 2001 ABQB 504, [2001] 8 W.W.R. 656, 94 Alta L.R. (3d) 378 (Alta. Q.B.). For the use of non-exempt property to purchase exempt property and attacking such transactions as fraudulent conveyances: see § 5:57 “Property Exempt from Execution or Seizure—(4) Fraudulent Transactions and Exempt Property”.

If the Minister of National Revenue has petitioned a debtor into bankruptcy, the trustee, in bringing proceedings for a declaration that certain assets are property of the bankrupt, can make use of evidence obtained by investigators of the Department of Revenue in the course of investigating the affairs of the bankrupt prior to bankruptcy, notwithstanding s. 241 of the *Income Tax Act:* Slattery (Trustee of) v. Slattery (1991), 7 C.B.R. (3d) 157, 84 D.L.R. (4th) 360, 1991 CarswellNB 27 (N.B.C.A.), affirmed (1993), 21 C.B.R. (3d) 161, 1993 CarswellNB 122, 1993 CarswellNB 152 (S.C.C.).

The court held that a structured settlement that is exempt from execution because of ss. 196 and 216 of the *Insurance Act* (Ontario) can be set aside as a fraudulent conveyance pursuant to s. 2 of the *Fraudulent Conveyances Act* (Ontario), being a conveyance of personal property, or a suit or judgment made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits or debts. Fraudulent conveyances involve two classes of cases, the first where the consideration for the conveyance is no consideration or only nominal consideration; and the second where the consideration for the conveyance is valuable and more than nominal. For the first class of case, the plaintiff must prove that the debtor had the intent to defeat, hinder, delay, or defraud creditors. For the second class, the plaintiff must also prove a culpable state of

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mind in the transferee of the property. This case fell within the first class, and here, the evidence was insufficient to establish a fraudulent intent. Apart from establishing a non-exigible asset, there are many benign motivations for structuring a settlement of a personal injury action, including the motivation that a structured settlement may be the fairest way for the defendant to compensate the plaintiff for his or her income losses: Salna v. Hie (2007), 2007 CarswellOnt 7558, 88 O.R. (3d) 202, 38 C.B.R. (5th) 100, 55 C.C.L.I. (4th) 258 (Ont. S.C.J.).

A corporation became general partner in another business, in part to gain the benefit of capital cost allowance, lending in excess of $5 million through an intermediary. A new company was created and the bankrupt transferred 99.9% of its assets to the new company, including profitable real estate interests. Through a series of transactions, the new corporation assumed $4.3 million of the bankrupt's liabilities and issued shares and promissory notes to the bankrupt, shares were redeemed and promissory notes set off against one another with the result that assets were transferred to the new corporation. The Court of Appeal upheld the trial judge's finding that the transactions constituted fraudulent conveyance and that dishonest intent is not necessary to apply the doctrine of fraudulent conveyance as the bankrupt had the intent to defeat creditors. A defence was not available as the transaction had no good consideration; the transaction was not made in good faith with regard to creditors; and the transferee was aware of the fraud: Botham Holdings Ltd. (Trustee of) v. Braydon Investments Ltd. (2009), 2009 CarswellBC 3135, 59 C.B.R. (5th) 1 (B.C. C.A.).

The British Columbia Supreme Court reviewed the provisions of the British Columbia *Fraudulent Conveyance Act* (*FCA*) and held that an important exception set out in s. 2 is that the Act does not apply to a disposition of property for good consideration and in good faith lawfully transferred to a person who, at the time of the transfer, has no notice of collusion or fraud. The only intent now necessary to avoid a transaction under the *FCA* is the intent to "put one's assets out of the reach of one's creditors". No further dishonest or morally blameworthy intent is required. The court held that the presence or absence of consideration is of critical importance with respect to the impeachment of conveyances for fraud. Where there is evidence of a transfer for good consideration, the plaintiff must show that the transferee actively participated in the fraud, beyond mere knowledge or notice. Otherwise, the conveyance will not be disturbed: Sutton v. Oshoway (2010), 2010 CarswellBC 2754, 70 C.B.R. (5th) 261 (B.C.S.C. [In Chambers]), additional reasons at (2011), 2011 CarswellBC 247, 74 C.B.R. (5th) 197 (B.C.S.C.), affirmed (2011), 2011 CarswellBC 1220, 77 C.B.R. (5th) 219 (B.C.C.A.).

The Ontario Superior Court of Justice declared a transfer of property to be a fraudulent conveyance, rejecting the defendant's argument that he was holding the property on a resulting trust for his wife. Pursuant to the terms of the mortgage, the defendant and his wife had certified to the lender that they were the lawful owners of the property and that there were no limitations affecting their title to their interest in the property. The defendant also signed the mortgage commitment and the mortgage and the proceeds from the mortgage were deposited into their joint bank account. Justice Leitch held that the appellant facilitated a transaction by pledging his credit and becoming exposed to the financial risk of the full amount of the mortgage, which was fatal to the existence of a resulting trust in favour of the appellant pursuant to s. 14 of the Ontario *Family Law Act*. Justice Leitch held that the impugned transaction was a fraudulent conveyance; as the evidence of the defendant and his wife revealed that the purpose of the impugned transaction was to prevent the defendant's creditors from having access to the matrimonial home. Even if he did not intend to specifically defeat, hinder or delay the plaintiff's claim, the fact that they intended to prejudice future creditors was enough to act contrary to the Ontario *Fraudulent Conveyances Act* (*FCA*). The court also considered provisions of the Ontario *Assignments and Preferences Act* (*APA*), which permit a creditor to "follow" proceeds of property fraudulently transferred, finding that the requirement that a transaction be "invalid against creditors" in s. 12 includes the consequences of s. 2 of the *FCA*. As a result, the tracing provisions of the *APA* are available where a conveyance is void under the *FCA:* Mitchell Jenner & Associates Inc. v. Saunders (2011), 2011 CarswellOnt 3728, 78 C.B.R. (5th) 169, 2011 ONSC 2930 (Ont. S.C.J.), affirmed on appeal, subject to a variance with respect to the appropriate interest rate in the judgment, varied from the amount set out in the commission agreement to the applicable rate under the *Courts of Justice Act*: Mitchell Jenner & Associates Inc. v. Saunders (2012), 2012 CarswellOnt 5299, 2012 ONCA 290 (Ont. C.A.).

The British Columbia Court of Appeal held that the only intent now required to avoid a transaction under the *Fraudulent Conveyances Act*, R.S.B.C. 1996, c. 163 is the intent to put one's assets out of the reach of one's creditors: Sutton v. Oshoway (2011), 2011 CarswellBC 1220, 77 C.B.R. (5th) 219 (B.C.C.A.).

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The court held that transactions involving certain collapsed RRSP were fraudulent conveyances within the meaning of the Manitoba *Fraudulent Conveyances Act*, RSM 1987, c. F160 and as such were void and of no force and effect. As the transfer had been to the debtor's wife, Master Berthaudin held that there was a substantial evidentiary burden on the debtor to show the transfer was not made with intent to defeat, hinder, delay or defraud creditors. The factual circumstances of the transactions raised several "badges of fraud" that had transferred the onus to the defendant. Here, intent was established. It was not necessary for the debtor to have been insolvent at the time of the transactions. The court granted summary judgment to the bankruptcy trustee: Tsouras Estate v. Tsouras (2011), 2011 CarswellMan 743, 78 C.B.R. (5th) 66 (Man. Master).

The Manitoba Court of Queen's Bench dismissed a motion for summary judgment brought by a bank and granted competing summary judgment motions of the defendants dismissing the bank's action. The court reviewed the applicable law relating to fraudulent conveyances. Justice Oliphant held that a transaction under the *Fraudulent Conveyances Act* cannot be set aside without some valid proof of claim against the person who has transferred her or his interest in the real property, citing Bell v. Williamson (1945), 1945 CarswellOnt 67, [1945] O.R. 844 (Ont. C.A.). The court held that fraudulent intent is essentially a matter of fact to be proved in the circumstance of each particular case. Proof that the transferor intended to defeat or delay its creditors usually involves drawing inferences from the circumstances surrounding the transaction. Justice Oliphant concluded that a close examination of the evidence revealed no direct evidence of a fraudulent intent on the part of any of the defendants when they conveyed their respective interests in the two pieces of real property. Moreover, there were no circumstances surrounding either of the transactions from which he could infer an intent to defraud. Accordingly, Oliphant J. was of the view that the bank had failed to demonstrate a *prima facie* case and its motion for summary judgment was dismissed: Alterinvest Fund L.P. v. Page (2011), 2011 CarswellMan 521, 2011 MBQB 251 (Man. Q.B.).

The Ontario Superior Court of Justice reviewed the factors to be taken into account on an *ex parte* application to obtain a certificate of pending litigation and an order to register the certificate. In this case, the court set aside the order as the trustee had not commenced a proceeding. However, the trustee was provided with a period of time to commence a proceeding, during which time period the order remained in effect: Re Erdman (2012), 2012 CarswellOnt 6945, 91 C.B.R. (5th) 82, 2012 ONSC 3268 (Ont. S.C.J.). For a discussion of this case, see § 16:90 "Issuing a Certificate of Pending Litigation".

The Ontario Superior Court of Justice, in a claim to set aside a fraudulent conveyance as between parent and child, awarded costs as against the parents, who were non-parties to the action. Justice McIsaac held that the following principles should inform the exercise of such authority: 1) although costs orders against non-parties are to be regarded as "exceptional", the ultimate question in any such exceptional case is whether, in all the circumstances, it is just to make the order; 2) where, however, the non-party not merely funds the proceedings but substantially also controls or at any rate is to benefit from them, justice will ordinarily require that if the proceedings fail, he or she will pay the successful party's costs; 3) if a non-party does so for his or her own financial benefit, either to gain the fruits of the litigation or to preserve assets in which the person has an interest, it may, depending on the circumstances, be appropriate to make an order for costs against that person. Given the findings of the debtor's impecuniosity, McIsaac J. concluded that she had no financial wherewithal to fund the litigation and that her parents did so; hence it was fair and just to saddle them with the costs order sought by the plaintiff: Rose v. Pica, 2012 CarswellOnt 8243, 5 C.B.R. (6th) 156, 2012 ONSC 3855 (Ont. S.C.J.).

The Ontario Superior Court of Justice declared certain transactions as being a fraud on creditors. The Court reached this conclusion through a piercing of the corporate veil in the reverse direction, *i.e.* piercing through a corporate debtor and attributing the debt to the person that is the owner of the corporation. The plaintiff law firm moved for default judgment in two actions that it brought in respect of its fees. The personal defendant in the first action retained the plaintiff to represent him and the corporate defendants in respect of a number of environment-related regulatory charges. Morgan J. noted that there was no doubt that the accounts rendered represented fair value for the work performed on the defendants' behalf and for their benefit. Justice Morgan noted that the Supreme Court of Canada has for several decades held the view that the corporate form, while ordinarily respected as a legitimate method of business organization, is not to be abused, citing Kosmopoulos v. Constitution Insurance Co. of Canada, 1987 CarswellOnt 132, 1098 Carswellont 1054, [1987] 1 S.C.R. 2, 63 O.R. (2d) 731 (S.C.C.). Justice Morgan held that piercing the corporate veil is an equitable doctrine whose purpose is to relieve against injustice. Morgan J. held that the personal defendant had used corporate vehicles, and had transferred and encumbered property in favour of his spouse, in

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order to perpetrate a fraud on the plaintiff as his creditor, violating s. 4(1) of the Ontario *Assignments and Preferences Act* and s. 2 of the Ontario *Fraudulent Conveyances Act*. In seeking to unjustly deprive the plaintiff of its rights, the personal defendant acted in a way that prompted the court to pierce the corporate veil of the entities having title to the properties and to treat the two properties as if they were owned by the personal defendant. In the result, Morgan J. granted the plaintiff judgment against the defendants in both actions and set aside as being void the real property transactions as against the plaintiff. He permitted the judgment to be registered against those properties as if their respective titles were in the name of the personal defendant. Further, given the findings of fraudulent conveyances against the defendants, costs were awarded on substantial indemnity basis in the amount requested by the plaintiff: Borden Ladner Gervais LLP v. Sinclair, 2013 CarswellOnt 17323, 14 C.B.R. (6th) 317, 2013 ONSC 7640 (Ont. S.C.J.).

A plaintiff obtained judgment against a defendant with respect to breach of contract. The defendant conveyed property to his defendant wife and her defendant company. The plaintiff's actions against the defendants were allowed in part, with two of four alleged fraudulent conveyances set aside pursuant to the *Fraudulent Conveyances Act*, R.S.O. 1990, c. F-29. Both parties appealed and both appeals were dismissed. The Court of Appeal's analysis hinged primarily on determination of when the defendant knew he was in financial trouble. By the time of the latter transfers, he knew he was in significant financial jeopardy, and circumstances surrounding the transactions pointed to fraudulent intent. The Court held that the trial judge was in the best position to consider and weigh all the documentary and testimonial evidence and to assess the credibility of witnesses. There was no palpable and overriding error: Indcondo Building Corp. v. Sloan, 2015 CarswellOnt 16689, 31 C.B.R. (6th) 110, 2015 ONCA 752 (Ont. C.A.).

The Manitoba Court of Queen's Bench set aside the assignment of the bankrupt former spouse's claim under *The Family Property Act* (Manitoba) to her mother as a fraudulent conveyance. Justice Bond concluded that the evidence from the bankrupt regarding the assignment letter was vague, contradictory and unsatisfactory; and the evidence regarding the consideration for the assignment lacked credibility, and included amounts not supported by any documentation or independent evidence. The Court also held that the former spouse and her mother committed the tort of conspiracy by intentionally defrauding the legitimate claim of the bankrupt's creditors: Garlicki (Trustee of) v. Garlicki, 2015 CarswellMan 392, 2015 MBQB 125 (Man. Q.B.).

The Alberta Court of Queen's Bench held that the *Fraudulent Preferences Act* and the fraudulent conveyance provisions of the *Statute of Elizabeth* are limited to striking down an alleged fraudulent conveyance or ordering the sale of the property wrongfully conveyed. Justice Shelley noted that the clear language in Rule 9.24 provides that a court may order the sale of the property that was fraudulently conveyed to pay the amount owing. It does not say that the court can summarily award judgment against the non-party that received the property. Consequently, the Court could not grant judgment against a non-party and could not order her to pay damages or compensation: 336239 Alberta Ltd. v. Mella, 2016 CarswellAlta 572, 35 C.B.R. (6th) 332, 2016 ABQB 190 (Alta. Q.B.).

The Ontario Superior Court of Justice declared that the conveyance of a one-half interest in a matrimonial home was a fraudulent conveyance. Relief was granted under both the *Bankruptcy and Insolvency Act* and the *Fraudulent Conveyances Act.* Justice Lemay noted that the most important badge of fraud in this case was the timing of the transaction, which strongly suggested that the transaction was taken to prevent the debtor's creditors from obtaining his interest in the home. Based on the evidence, the Court rejected the respondent's argument that the property was the subject of a trust in her favour: Royal Bank of Canada v. Nonis, 2016 CarswellOnt 10227, 37 C.B.R. (6th) 293, 2016 ONSC 3643 (Ont. S.C.J.).

The Court of Appeal for Ontario dismissed an appeal arising from a successful application under the Ontario *Fraudulent Conveyances Act*. The Court reviewed issues relating to the burden of proof. Miller J.A. noted that the appeal was largely an attack on the trial judge's determinations of credibility and factual findings related to the impugned transactions. Miller J.A. noted that these determinations of credibility and factual findings were open to the trial judge, were entitled to deference, and there was no basis on which the Court of Appeal should interfere with them. These findings were dispositive of most of the grounds of appeal. The trial judge had correctly stated the law with respect to burden of proof where there is an allegation of fraudulent conveyance; it is up to the challenger of a transaction to establish on, a balance of probabilities, that a conveyance was made with the intent to “defeat, hinder, delay or defraud creditors or others”, within the meaning of s. 2 of the *FCA*. If a challenger raises evidence of one or more “badges of fraud” that give rise to an inference of intent to defraud, the evidentiary

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burden then falls on the parties defending the transaction to adduce evidence showing the absence of fraudulent intent. The requisite fraudulent intent is to be assessed at the time of the impugned transactions: Purcaru v. Seliverstova, 2016 CarswellOnt 12336, 39 C.B.R. (6th) 15, 2016 ONCA 610 (Ont. C.A.).

The Ontario Superior Court of Justice granted summary judgment against the bankrupt. The plaintiffs had sought an order that a conveyance of RRSP made prior to bankruptcy be set aside pursuant to the *Fraudulent Conveyances Act.* The defendant had been convicted of fraud, a judgment was obtained against her for close to $1 million. Shortly thereafter, the defendant declared bankruptcy. Prior to the fraud being discovered, the defendant conveyed approximately $206,000 into a creditor proof segregated RRSP mutual fund. The Court held that to find a fraudulent conveyance so as to void a transaction, there must be: a "conveyance" of property, an "intent" to defeat, and a "creditor or other" towards whom that intent is directed. Courts have found that, in some circumstances, it is not necessary for there to be any creditors at all at the time of a transaction in order to conclude that it was done with the intent to defeat creditors. It is remedial legislation and must be given as broad an interpretation as its language will reasonably bear. Although there was no direct evidence of intent, the Court inferred from the circumstances that the defendant had intended to defraud the plaintiffs. Maranger J. held that it was inconceivable that the legislation did not apply to a situation where a person embezzled money from another individual, put it into a creditor proof fund, when the fraud was discovered and judgment was obtained declared bankruptcy, and was allowed to retain part of the fruits of the embezzlement. In the result, the motion was granted and an order was granted for summary judgment ordering the transfer back of the RRSP funds from a segregated fund to a general fund so that they could be executed upon by the plaintiffs: Bearsfield Developments Inc. v. McNabb, 2016 CarswellOnt 15843, 41 C.B.R. (6th) 310, 2016 ONSC 6294 (Ont. S.C.J.).

The Court of Appeal for Ontario rejected the appeal of transferees of property that had been found to be the subject of a fraudulent conveyance. The Court of Appeal noted that the motion judge had considered the evidence and had reached the following conclusions: (i) the appellants were not arm's-length parties in relation to the husband; (ii) the appellants had knowledge of the court order prohibiting any sale of the property; and (iii) the husband had transferred the property with the intent to defeat the wife's claims and the appellants had not rebutted the evidentiary presumption that they had been privy to such intent. The Court of Appeal noted that the motion judge had relied on the principles described in Conte Estate v. Alessandro, 2002 CarswellOnt 4507, [2002] O.J. No. 5080 (Ont. S.C.J.), affirmed 2004 CarswellOnt 3218, [2004] O.J. No. 3275 (Ont. C.A.) to analyze intent to defraud for the purposes of ss. 2 and 3 of the *Fraudulent Conveyances Act.* In doing so, the motion judge noted that an inference of fraudulent intent can be made by suspicious circumstances or "badges of fraud" surrounding the conveyance. The presence of such suspicious circumstances raises a presumption of fraud that must be rebutted by the parties to the conveyance. The motion judge found ten badges of fraud and the appellants had not rebutted the presumption of fraud. The Court of Appeal saw no error in the motion judge's analysis or conclusions: Shoukralla v. Dumolong, 2016 CarswellOnt 17387, 41 C.B.R. (6th) 6, 2016 ONCA 128 (Ont. C.A.).

The Alberta Court of Queen's Bench reviewed the required elements of both the *Fraudulent Preferences Act* and the *Statute of Elizabeth*: Westcorp Inc. v. H & H Stucco & Siding Ltd., 2016 CarswellAlta 2233, 42 C.B.R. (6th) 258, 2016 ABQB 650 (Alta. Q.B.); see § 5:469 "Attacking Fraudulent Conveyances under Provincial Assignments and Preferences Act, Fraudulent Preferences Act and Similar Statutes for a discussion of this judgment".

The British Columbia Court of Appeal addressed the question as to what happens when a court sets aside a fraudulent conveyance. The *Fraudulent Conveyance Act* (B.C.) has only two sections: 1. If made to delay, hinder or defraud creditors and others of their just and lawful remedies (a) a disposition of property, by writing or otherwise, (b) a bond, (c) a proceeding, or (d) an order is void and of no effect against a person or the person's assignee or personal representative whose rights and obligations are or might be disturbed, hindered, delayed or defrauded, despite a pretence or other matter to the contrary. 2. This *Act* does not apply to a disposition of property for good consideration and in good faith lawfully transferred to a person who, at the time of the transfer, has no notice or knowledge of collusion or fraud. Newbury J.A. referenced the *Report on Fraudulent Conveyances and Preferences* of the B.C. Law Reform Commission, which observed that both the *Fraudulent Conveyance Act* and the *Fraudulent Preference Act* are silent on the effect, as between the grantor and grantee, of a fraudulent transfer. Both statutes simply provide that the disposition is "void" as against the successful claimant. Justice Newbury held that a fraudulent conveyance is only "voidable". The conveyance continues to be valid, or "absolute", against the grantor. Another consequence of the validity of

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the transfer as between grantor and grantee is that if latter sells the property for valuable consideration to a *bona fide* purchaser, that purchaser takes title. Justice Newbury held that the *Act* does not operate so as to "re-vest" the conveyed property in the grantor, nor to allow the grantor to set up his or her fraudulent act as a basis on which to re-claim it from the grantee. Rather, the relief granted is properly confined to setting aside the impeached conveyance, thus removing it is as an obstacle to the creditor's recovery under executions against the debtor. The chambers judge had erred in holding that the orders made by judge validly restricted remedies under the *Fraudulent Conveyances Act.* Once a conveyance has been found to infringe the *Act*, it remains fraudulent, and is ineffective against all creditors who may be hindered or delayed. Newbury J.A. observed that it would be contrary to logic and existing authority to require that a creditor who wishes to enforce more than one judgment return to court to have the same transaction declared void "time and time again". Similarly, it would offend the purpose of the *Act* to require that creditor after creditor prove in court that the same transfer was intended to avoid the just claims of creditors. In the result, the appeal was allowed, the order of the chambers judge was set aside, the decision of the trustee was set aside, and the trustee was directed to make the remaining sale proceeds of the property available to the extent necessary to enforce the costs order and any other judgment: Guthrie v. Abakhan & Associates Inc., 2017 CarswellBC 530, 2017 BCCA 102 (B.C. C.A.).

The Ontario Superior Court of Justice dismissed the motion of a defendant who had moved to dismiss a fraudulent conveyance claim. The action arose out of an automobile accident where the plaintiffs claimed at least $20 million in damages. After commencement of the action, the defendant transferred his interest in the matrimonial home to his wife for no consideration. On learning of the transfer, the plaintiffs amended the statement of claim to add the wife as a defendant, and to assert a claim under the *Fraudulent Conveyances Act* (*FCA*). They also obtained a Certificate of Pending Litigation and registered it against the property. Justice Gray was not persuaded that the provisions of the statement of claim relating to the fraudulent conveyance should be struck out. Gray J. noted that there was little doubt that the words "or others" in s. 2 of the *FCA* are broad enough to include a person whose claim has not yet been reduced to judgment. The real issue in this case was whether the fraudulent conveyance claim and the claim for punitive damages, should be stayed pending the outcome of the personal injuries claim. Gray J. acknowledged that to require the two sets of claims to be litigated at the same time may result in additional expense and difficulty for the defendants that may prove to be unnecessary. However, if the plaintiffs succeed, and if they achieve a judgment in excess of the insurance policy limits, they would be delayed in attempts to collect. Another set of examinations for discovery and another trial would need to be held. Gray J. held that it would cause considerable delay and additional expense. The trial judge has ample power to conduct the proceedings in a way that would minimize, if not eliminate, any prejudice to the defendants. The trial judge could conduct the trial of the personal injuries claim with a jury first, and hold the fraudulent conveyance claim in abeyance. If it becomes necessary to try the fraudulent conveyance claim, the trial judge could dispense with the jury if appropriate, and hear the claim immediately after the trial of the personal injury claim. On balance, Gray J. held that the claims should proceed at the same time: Ahmed v. Rowe, 2017 CarswellOnt 5509, 47 C.B.R. (6th) 130, 2017 ONSC 2289 (Ont. S.C.J.).

The Ontario Superior Court of Justice dismissed a fraudulent conveyance action that had been assigned to the plaintiff under s. 38 of the *BIA*. Justice Faieta noted that the plaintiffs' claim arose more than eleven years after the impugned transfer. The plaintiffs did not have standing to bring the action as they had no claim against the defendants at the time of the impugned transfer and thus were not "creditors or others" within the meaning of s. 2 of the *FCA* in respect of the transfer. Justice Faieta held that under s. 38 of the *BIA*, there are only two conditions precedent to a creditor's commencement of an action: the trustee's refusal or neglect to initiate it, and the court's order authorizing such action. The trustee's assignment of rights, title, and interest in the subject matter of the proceeding, under s. 38(3), is not a pre-condition to the commencement of an action. Faieta J. also noted that the language of s. 38(1) of the *BIA* requires that court approval be obtained in respect of "any proceeding … for the benefit of the estate of a bankrupt". By failing to obtain court approval to commence the proceeding against all of the named defendants, the plaintiffs had not complied with s. 38(1). A failure to satisfy this condition precedent was an irregularity that may be cured, *nunc pro tunc*, in appropriate circumstances, but the court declined to do so in the circumstances of this case. In the result, Faieta J. dismissed the action: Wilfert v. McCallum, 2017 CarswellOnt 9686, 49 C.B.R. (6th) 272. 2017 ONSC 3853 (Ont. S.C.J.), additional reasons 2017 CarswellOnt 11078, 2017 ONSC 4431 (Ont. S.C.J.).

The British Columbia Supreme Court granted judgment in favour of a plaintiff trustee against a defendant for a fraudulent conveyance arising out of a Ponzi scheme. The defendant had not been a party to, and had had no knowledge of, the bankrupt

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companies' fraudulent scheme. The bankrupt corporate group received approximately $110 million from investors as part of the scheme. Approximately 150 investors suffered losses; however, other investors, including the defendant, received payments from the scheme that exceeded the principal amount of their investment. The Court noted that the U.S. Securities and Exchange Commission has defined a Ponzi scheme as: "A Ponzi scheme is an investment fraud that involves the payment of purported returns to existing investors from funds contributed by new investors. Ponzi scheme organizers often solicit new investors by promising to invest funds in opportunities claimed to generate high returns with little or no risk. In many Ponzi schemes, the fraudsters focus on attracting new money to make promised payments to earlier-stage investors and to use for personal expenses, instead of engaging in any legitimate investment activity." Justice Weatherill found that Canadian courts have described Ponzi schemes similarly, citing Re Titan Investments Ltd. Partnership, 2005 CarswellAlta 1153, 14 C.B.R. (5th) 112, 2005 ABQB 637, [2005] A.J. No. 1041 (Alta. Q.B.) and Millard v. North George Capital Management Ltd., 2006 CarswellOnt 7784, [2006] O.J. No. 4902 (Ont. S.C.J. [Commercial List]). Justice Weatherill held that the *Fraudulent Conveyance Act* (B.C.) (*FCA*) provides that "1. If made to delay, hinder or defraud creditors and others of their just and lawful remedies (a) a disposition of property, by writing or otherwise, (b) a bond, (c) a proceeding, or (d) an order is void and of no effect against a person or the person's assignee or personal representative whose rights and obligations are or might be disturbed, hindered, delayed or defrauded, despite a pretence or other matter to the contrary. 2. This Act does not apply to a disposition of property for good consideration and in good faith lawfully transferred to a person who, at the time of the transfer, has no notice or knowledge of collusion or fraud." Justice Weatherill accepted that a Ponzi scheme is insolvent from its inception, and held that an intention to defraud creditors may be inferred from the fact that a debtor is operating a Ponzi scheme. Payments used to continue the fraud are not good consideration for payments made to investors in excess of their principal investment. The *FCA* must be applied in a manner consistent with modern commerce and common sense, and the defendant had not provided any consideration, let alone good or valuable consideration, for the receipt by him of the amount. The only fraudulent intent required to be shown was that of the principal of the bankrupt companies. The excess was transferred to the defendant as part of the unlawful scheme, and thus not saved by s. 2 of the *FCA*. In the result, Weatherill J. found that the payment of the excess to the defendant was void as a fraudulent conveyance, contrary to the *FCA*. Although this determination was sufficient to dispose of the case, Weatherill J. also found that the excess paid by the bankrupts at a time when they were in insolvent circumstances was with the intent to defeat, hinder, delay or prejudice creditors. The excess had been paid to the defendant in preference over other creditors. As concurrent intent of both the debtor to give and the creditor to receive a preference is required under the s. 3 of the *Fraudulent Preference Act* (B.C.) (*FPA*), the plaintiff's claim under the *FPA* failed. Justice Weatherill then considered restitutionary claims, relying on A. Marquette & fils Inc. v. Mercure, 1975 CarswellQue 51, [1977] 1 S.C.R. 547, in which the Supreme Court of Canada held that when a trustee is appointed following a bankruptcy, it assumes a dual role as the debtor's representative and the representative of all creditors to the extent that it can act on their behalf. A trustee may pursue actions against third parties based on statute, common law, or equitable causes of action; thus, the trustee had standing to bring claims of unjust enrichment and "money had and received" on behalf of the net losers under the Ponzi scheme. The Court found unjust enrichment and ordered the excess returned to the plaintiff as money had and received for distribution to all investors who had suffered losses by the fraud, granting judgment against the defendant in the amount of $384,000: Boale, Wood & Company Ltd. v. Whitmore, 2017 CarswellBC 2962, 54 C.B.R. (6th) 100, 2017 BCSC 1917 (B.C. S.C.). For a discussion of the court's finding of unjust enrichment, see § 5:129 "Unjust Enrichment".

The Alberta Court of Appeal dismissed the appeal from a decision of the chambers judge. The lower court had declared a conveyance of assets to be fraudulent and void as against creditors and had also granted judgment personally against the sole shareholder as transferee: Beltline Real Estate Holdings Ltd. v. Domicile Interiors Ltd., 2017 CarswellAlta 2522, 2017 ABCA 407 (Alta. C.A.). For a discussion of this judgment, § 5:529 "Provincial Legislation Dealing with Preferences".

The Ontario Superior Court of Justice reviewed the circumstances leading up to the debtor providing a secured guarantee and held that it could not infer that the debtor gave the guarantee with the intent to defraud, defeat, or delay a creditor. The monitor moved for an order disallowing the claim filed by a contractor, which claimed $2.3 million against the debtor company pursuant to a secured guarantee. In support of its obligations under the guarantee, the debtor had granted mortgages in favour of the contractor over 13 condominium units. The monitor took the position that when the debtor gave the guarantee and supporting mortgages, it was insolvent, and as such, was a reviewable transaction under s. 96 of the *BIA*, as incorporated into s. 36.1 of the *CCAA*. The monitor asserted that the guarantee was a transaction at undervalue under s. 96 of the *BIA* or a fraudulent

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conveyance under the *Fraudulent Conveyances Act* (*FCA*), or that it was oppressive under the Ontario *Business Corporations Act* (*OBCA*). Justice Myers dismissed the monitor's motion and upheld the validity of the secured claim. Justice Myers held that the debtor and the contractor were operating at arm's-length, they were adverse in interest and were operating under normal economic incentives, and there was no evidence to suggest that they were under common control or acting in concert. Section 96(1) of *BIA* requires that to succeed, the monitor must establish that in granting the guarantee, the debtor intended to defraud, defeat, or delay creditors. Myers J. found that the monitor failed to prove a fraudulent intention at the relevant time and held that the remedies under s. 96 of the *BIA* and the *FCA* could not apply. Myers J. was also of the view that there was no basis on the evidence for an oppression remedy to lie. In the result, the motion of the monitor was dismissed: Re Urbancorp Toronto Management Inc., 2018 CarswellOnt 7672, 60 C.B.R. (6th) 241, 2018 ONSC 2965 (Ont. S.C.J. [Commercial List]).

The Court of Appeal for Ontario quashed an appeal from the Superior Court of Justice. The plaintiff's summary judgment motion, which was directed at fraudulent conveyance claims, had been dismissed on the basis that the plaintiff had failed to follow the correct procedure. In the result, because the order made by the motion judge was interlocutory, and as it did not determine the substantive rights of the parties, an appeal properly lay to the Divisional Court with that court's leave pursuant to s. 19(1)(b) of the *Courts of Justice Act.* The Court of Appeal noted that the claimant could still pursue his fraudulent conveyance claims in the court sitting in bankruptcy or he could seek leave to appeal the summary judgment in the Divisional Court: Esfahani v. Samimi, 2018 CarswellOnt 8804, 61 C.B.R. (6th) 24, 2018 ONCA 516 (Ont. C.A.).

A plaintiff was a creditor and assignee of the trustee. The bankrupt had transferred six properties to the defendant recipient less than three months prior to the date that it filed a notice of intention to make a proposal. The Ontario Superior Court of Justice held that the matter was appropriate for determination on a motion for summary judgment. The Court held that the debtor was insolvent at the time the transfers were made, and a creditor was given a preference over other creditors in violation of s. 95(1)(b) of the *BIA*. The transfers were made at undervalue in violation of s. 96 and the Court ordered that they be set aside. The Court also declared that the transfers at undervalue were void as against the trustee in bankruptcy. The Court further held that the debtor had made a fraudulent conveyance within the meaning of the Ontario *Fraudulent Conveyance Act*, R.S.O. 1990, c. F.29, and there was grossly inadequate consideration and a close relationship between the debtor transferring the property and the recipient. The Court also made orders in respect of tracing any property that had been disposed of by the recipient: Truestar Investments Ltd. v. Baer, 2018 CarswellOnt 8093, 60 C.B.R. (6th) 70, 2018 ONSC 3158 (Ont. S.C.J.).

The Ontario Superior Court of Justice dismissed the request of a party who sought equitable relief to set aside the discharge of a mortgage. Justice Corthorn noted that the jurisdiction of the court to grant equitable relief pursuant to s. 183(1) of the *BIA* was not in dispute. Rectification of a title register is available pursuant to ss. 159 and 160 of the *Land Titles Act* (*LTA*). Section 159 provides: "Subject to any estates or rights acquired by registration under this Act, where a court of competent jurisdiction has decided that a person is entitled to an estate, right or interest in or to registered land or a charge and as a consequence of the decision the court is of the opinion that a rectification of the register is required, the court may make an order directing the register to be rectified in such manner as is considered just." Justice Corthorn held that the matter fell squarely within the scope of s. 159 of the *LTA.* The Court noted that the equitable remedy of rectification, based on a unilateral mistake, is available "provided certain demanding preconditions are met", citing Toronto-Dominion Bank v. Novielli, 2014 CarswellOnt 17288, 2014 ONSC 7111 (Ont. S.C.J.), at para. 41. Justice Corthorn noted that the modern principles of rectification are set out by Binnie J. in Sylvan Lake Golf & Tennis Club Ltd. v. Performance Industries Ltd., 2002 CarswellAlta 186, [2002] 1 S.C.R. 678, 2002 SCC 19, [2002] S.C.J. No. 20 (S.C.C.), at para. 31: "Rectification is an equitable remedy whose purpose is to prevent a written document from being used as engine of fraud or misconduct 'equivalent to fraud'. The traditional rule was to permit rectification only for mutual mistake, but rectification is now available for unilateral mistake (as here), provided certain demanding preconditions are met. Insofar as they are relevant to this appeal, these preconditions can be summarized as follows. Rectification is predicated on the existence of a prior oral contract whose terms are definite and ascertainable. The plaintiff must establish that the terms agreed to orally were not written down properly. The error may be fraudulent, or it may be innocent. What is essential is that at the time of execution of the written document the defendant knew or ought to have known of the error and the plaintiff did not. Moreover, the attempt of the defendant to rely on the erroneous written document must amount to 'fraud or the equivalent of fraud'. The court's task in a rectification case is corrective, not speculative. It is to restore the parties to their original bargain, not to rectify a belatedly recognized error of judgment by one party or the other …" [Citations omitted.]

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In this case, Justice Corthorn held that the decision to discharge the mortgage was a deliberate, fully-informed decision and it was anything but a mistake: Truestar Investments Ltd. v. Baer, 2018 CarswellOnt 20819, 2018 ONSC 7372 (Ont. S.C.J.).

The Ontario Superior Court of Justice issued a declaration that the bankrupt's interest in two properties held in joint tenancy with his wife were assets of the estate. The Court found that alleged trust agreements were "sham" trusts: Re McGoey, 2019 CarswellOnt 254, 2019 ONSC 80 (Ont. S.C.J.).

The Ontario Superior Court of Justice allowed the appeal from the master who had denied the plaintiff leave to issue and register a certificate of pending litigation ("CPL") against property that was the subject of a fraudulent conveyance challenge. The Court reviewed the test for a CPL: Jodi L. Feldman Professional Corporation v. Foulidis, 2018 CarswellOnt 21420, 2018 ONSC 7766 (Ont. S.C.J.), additional reasons 2019 CarswellOnt 565, 2019 ONSC 421 (Ont. S.C.J.). For a discussion of this decision, see § 16:90 "Issuing a Certificate of Pending Litigation".

The Ontario Superior Court of Justice held that parties were dealing at arm's length, a transfer did not take place at undervalue, and there was no intention to defraud, defeat, or delay the plaintiff. Justice Penny noted that the voiding of a transfer as fraudulent under the *Fraudulent Conveyances Act* requires: (a) the conveyance of property; (b) an intent to defeat, hinder, delay, or defraud; and (c) a creditor or other towards whom that intent is directed. Justice Penny concluded that the transaction was not at undervalue. The transaction did not defeat, hinder, delay, or defraud any creditor. He therefore dismissed the claim under s. 2 of the *FCA* on this basis: 1085372 Ontario Limited v. Kulawick (2019), 2019 CarswellOnt 6882, 69 C.B.R. (6th) 189, 2019 ONSC 2344 (Ont. S.C.J. [Commercial List]). For a discussion of this judgment, see § 5:486 "Transfers at Undervalue, Generally".

The British Columbia Supreme Court granted judgment to the plaintiff who had sued the defendants for fraudulent conveyances and fraudulent preferences. The plaintiff had advanced $440,000 to invest, through the defendant company, in developing an apartment building. The plaintiff subsequently successfully sued the defendants, alleging that the parties never reached an enforceable agreement for the investment, with the result that it should be refunded, with a judgment for the amount and costs for $643,990. Certificates of pending litigation meant that all was recovered except $121,805. Justice Macintosh found that the defendants were closely affiliated, and the principal of the company caused it to sign a promissory note to himself or to another defendant each time it paid money to either of those entities, and also found "so-called loan agreements", in which payments were made to the defendants instead of satisfying the judgment. Macintosh J. held that in a proceeding relying on the provisions of the *Fraudulent Conveyance Act* (B.C.) and the *Fraudulent Preference Act* (B.C.), the element of fraud may be proven by evidence of actions that are only presumptively fraudulent. The defendants, in the face of such evidence, have the burden of explaining why their conduct is not caught by the legislation. With respect to the *Fraudulent Conveyance Act*, Macintosh J. noted that the only intent required in order to void a transaction is the intent to put assets out of the reach of creditors. No further dishonest or morally blameworthy intent is required. A court can presume the requisite intention if the disposition had the effect of hindering, delaying, or defeating creditors. Where the consideration is inadequate or nominal, a creditor needs to show only that the transferor intended to delay, hinder, or defraud the creditor of its remedies. Where valuable consideration has passed, the creditor must also show that the transferee actively participated in the fraud. Justice Macintosh held that a number of badges of fraud were present in this case. The defendants' transactions, benefiting themselves, had resulted in the defendant company's bank account almost always having close to a nil balance. The three defendants could not be more closely related and their transactions divested the defendant company of its assets. The Court held that the requirements of the *Fraudulent Preference Act* that the transferor was on the eve of insolvency and intended to give the transferee preference over others had been met: Pacific Wagondepot Ltd. v. Hudson West Development Ltd., 2019 CarswellBC 1591, 2019 BCSC 909 (B.C. S.C.).

The British Columbia Supreme Court held that a transfer of property from a son to his parents was a fraudulent conveyance. Defendant "R" transferred his undivided 98% interest in three properties to his parents and two other defendants. The plaintiffs sought a declaration that the transfer was a fraudulent conveyance designed to prevent execution by the plaintiffs of three judgments against the properties. The plaintiffs entered into a tenancy agreement to rent a residential unit to R, who failed to pay rent. The plaintiffs applied to the Residential Tenancy Branch and obtained an order that R pay the plaintiff, which the tenants failed to pay, as well as a second order for rent and a third for damage to the unit. The Residential Tenancy Branch granted the plaintiffs an order of possession for the rental unit and the plaintiffs engaged bailiffs to evict the tenants. Ball J. held that the defendants must have been aware of the deplorable conditions of the premises and would have rightly assumed that a

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claim would be made against R by the plaintiffs based on the condition of the premises. An initial attempt to register the two judgments for the first order and the second order in the Land Title Office against R's properties was rejected by the Land Title Office on the basis that the certificates of judgment had not been attached to the application. The plaintiffs applied to register the certificates of judgment against the title to the properties, but by then R had transferred his interest in the properties for "$1.00 and natural love and affection", and the application to register was rejected because R no longer had a registered interest. Justice Ball noted that under the *Fraudulent Conveyance Act*, where the consideration is inadequate or nominal, a creditor need only show that the transferor intended to delay, hinder, or defraud the creditor. Here, the consideration for the transfer was inadequate or nominal, and, therefore the relevant intentions were those of the transferor. The transfer was made between near relatives, so there was a suspicion that the transaction was not made in good faith. The burden of establishing the *bona fides* of the transaction in this situation shifted from the plaintiffs to the parties to the transaction. Justice Ball found that the evidence was clear that the respondents were fully aware that R was not paying various creditors. The effect of the transfer effectively divested R of his only real estate asset and thereby delayed, hindered, or defrauded creditors. Justice Ball held that the "badges of fraud" were present in this case. Ryan transferred the properties for the purpose of preventing his creditors, including the plaintiffs, from executing against the properties. In the result, the Court ordered that the transfer of the properties was void and of no effect against the plaintiffs, and the plaintiffs held an interest in the properties to the extent of the three judgments of the Residential Tenancy Branch. An award of punitive damages against R was also made: Meleski v. Woodcock, 2019 CarswellBC 1656, 2019 BCSC 935 (B.C. S.C.).

The Ontario Superior Court of Justice reviewed the law relating to civil fraud and conspiracy to cause economic injury. In a civil fraud action, the plaintiff invested his retirement savings with an old friend, and, after the initial returns, he invested further funds from a line of credit secured against his home. Within months of his final investment, his money disappeared and the company in which the funds were invested went into receivership. The plaintiff brought an action for the return of his money, pleading civil fraud, conspiracy, breach of fiduciary duty, and misrepresentation. Justice McSweeney considered the Supreme Court of Canada's elements of the tort of civil fraud, which must be proven on a balance of probabilities, as requiring: (i) a false representation by the defendant; (ii) some level of knowledge of the falsehood of the representation on the part of the defendant (whether knowledge or recklessness); (iii) the false representation caused the plaintiff to act; and (iv) the plaintiff's actions resulted in a loss, citing Hryniak v. Mauldin, 2014 CarswellOnt 640, 21 B.L.R. (5th) 248, 2014 SCC 7, [2014] S.C.J. No. 7 (S.C.C.). Justice McSweeney noted cases that have placed less emphasis on the tortfeasor's intention to deceive the plaintiff, finding that where fraud is proved, the motive of the person committing the fraud is immaterial, citing Bruno Appliance and Furniture Inc. v. Hryniak, 2014 CarswellOnt 642, 2014 CarswellOnt 643, 2014 SCC 8, [2014] S.C.J. No. 8 (S.C.C.). McSweeney J. found, on a balance of probabilities, that the evidence established that misrepresentations to the plaintiff about the company of which the defendant was a director induced the plaintiff to give him his first $60,000 savings to invest; and misrepresentations were made to bolster and encourage the plaintiff's belief that it continued to be a successful electrical supply company that was generating returns for its investors. The evidence established that the defendant committed civil fraud by making representations to the plaintiff which he knew were false. Justice McSweeney found the defendant personally liable to the plaintiff, finding that directors are personally liable for their own tortious conduct at law, even if they claim to have been acting on behalf of a corporation: see ADGA Systems International Ltd. v. Valcom Ltd., 1999 CarswellOnt 29, [1999] O.J. No. 27, 117 O.A.C. 39 (Ont. C.A.), leave to appeal refused 2000 CarswellOnt 1160, [2000] 1 S.C.R. xv (note) (S.C.C.). Justice McSweeney then addressed the issue of whether the defendants conspired to cause economic injury to the plaintiff. The constituent elements of the tort of conspiracy are: (1) two or more defendants' agreement or act with a common design to injure the plaintiff; (2) the defendants use lawful or unlawful means for the predominant purpose of injuring the plaintiff, or use unlawful means by conduct directed at the plaintiff, knowing or constructively knowing that their acts would likely result in injury to the plaintiff; (3) the defendants act in furtherance of their agreement to injure; and, (4) the plaintiff suffers damages as a result of the defendants' conduct. McSweeney J. found that the defendants had acted together to create for investors the false impression of a successful electrical supply company in order to obtain funds; and working together, these defendants planned to obtain funds from the plaintiff, knowing or constructively knowing that he was likely to lose his money; they acted in furtherance of this plan; and the plaintiff suffered damages in the form of lost investment as a result of the defendants' conduct. The defendants were found to be jointly and severally liable to the plaintiff: Mughal v. Bama Inc. et al., 2019 CarswellOnt 12735, 2019 ONSC 4504 (Ont. S.C.J.).

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A master of the Ontario Superior Court of Justice dismissed a motion for leave to issue a certificate of pending litigation ("CPL") in an action to declare the transfer of a matrimonial home a fraudulent conveyance. The master reviewed the test for obtaining a CPL where the plaintiff has no interest in the property other than by way of a fraudulent conveyance allegation: the CPL claimant must satisfy the court that there is a high probability that he or she would successfully recover judgment in the main action; the claimant must introduce evidence demonstrating that the transfer was made with the intent to defeat or delay creditors, and evidence that the transfer was for less than fair market value lightens the burden; and the claimant must demonstrate that the balance of convenience favours issuing a CPL in the circumstances. Master Sugunasiri found that the plaintiff failed to introduce evidence demonstrating that the transfer was made with the intent to defeat or delay creditors other than evidence that the transfer was for less than fair market value. Master Sugunasiri held that the evidence must demonstrate some basis to support the allegation beyond a bald statement; here, the plaintiff had not tendered adequate evidence to support his request. Master Sugunasiri held that while, from a purely legal point of view, a CPL merely serves as notice to non-parties of the claim, in reality its effects are far greater. It prevents the owner from exercising "the most important incidents of ownership" and is a kind of preventive execution by ensuring that the owner continues to own the land so that it is available to satisfy a judgment: Szymanski v. Lozinski, 2019 CarswellOnt 19802, 74 C.B.R. (6th) 73, 2019 ONSC 6968 (Ont. S.C.J.).

The Ontario Superior Court of Justice held that an application seeking a declaration that a conveyance of property was a fraudulent conveyance should proceed by way of action as opposed to application. In determining whether to convert an application into an action, the court will consider whether material facts are in dispute; the presence of complex issues that require expert evidence and/or a weighing of the evidence; whether there is a need for pleadings and discovery; and the importance and impact of the application and of the relief sought. The *Fraudulent Conveyances Act*, specifically s. 2, requires the court to determine the intent of the person conveying the property. Whether that intent is to defeat, hinder, delay, or defraud, it is still essential that the court determine the intent behind the conveyance. Justice Christie referenced the test for fraudulent conveyance is Indcondo Building Corp. v. Sloan, 2014 CarswellOnt 10946, 16 C.B.R. (6th) 220, 2014 ONSC 4018, [2014] O.J. No. 3722 (Ont. S.C.J.), affirmed 2015 CarswellOnt 16689, 31 C.B.R. (6th) 110, 2015 ONCA 752, [2015] O.J. No. 5768 (Ont. C.A.): there must be a conveyance of property; an "intent" to defeat; and a "creditor or other" towards whom that intent is directed. Justice Christie concluded that there were material facts in dispute, including the intent in transferring the property; and when issues of credibility are involved, the matter should proceed by way of action: Liahona Mortgage Investment Corp v. Bazinet, 2019 CarswellOnt 19466, 2019 ONSC 6874 (Ont. S.C.J.).

The British Columbia Supreme Court reviewed the requirements that are to be satisfied in a fraudulent conveyance action. The property in question was subject to two conveyances. The Court provided guidance on the ability of the plaintiff to follow the proceeds from the initial conveyance. The latter conveyance was for good consideration but since the original conveyance was fraudulent, these profits were not theirs to keep, they must be returned to the original defendants for the benefit of their creditors: Balfour v. Tarasenko, 2019 CarswellBC 3834, 2019 BCSC 2212 (B.C. S.C.). For a discussion of this judgment, see § 5:466 "Effect of Finding a Transaction to be a Fraudulent Conveyance".

The Ontario Superior Court of Justice determined that a transaction involving real property was both a fraudulent conveyance and an unlawful preference. The Court reviewed the *Fraudulent Conveyances Act* and the *Assignments and Preferences Act*: Bank of Montreal v. Bibi, 2020 CarswellOnt 7363, 2020 ONSC 2948 (Ont. S.C.J.). For a discussion of this judgment, see § 5:469 "Attacking Fraudulent Conveyances Under Provincial Assignments and Preferences Acts, Fraudulent Preferences Acts and Similar Statutes".

The Ontario Superior Court of Justice granted leave to the plaintiff to register certificates of pending litigation against properties that were the subject of proceedings within the *Fraudulent Conveyances Act*: Jennifer Horrocks v. Bruce McConville et al, 2020 CarswellOnt 10746, 2020 ONSC 4645 (Ont. S.C.J.). For a discussion of this judgment, see § 16:90 "Issuing a Certificate of Pending Litigation".

On a summary judgment motion, the Ontario Superior Court of Justice set aside transactions as being transfers at undervalue, fraudulent conveyances, and/or preferences. A cross-motion seeking dismissal based on an expiry of the limitation period was

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dismissed: *Albert Gelman Inc. v. 1529439 Ontario Limited*, 2020 CarswellOnt 14599, 83 C.B.R. (6th) 126, 2020 ONSC 7917 (Ont. S.C.J.). For a discussion of this judgment, see § 5:261 "Statute of Limitations with Respect to Claims by the Trustee".

The Saskatchewan Court of Queen's Bench held that a pre-receivership transaction was void in its entirety as it constituted a preference under the *Statute of Elizabeth*. The related debtor companies operated fitness gyms and one of their largest creditors, a landlord, obtained a receivership order. Prior to the order, a transfer of membership rights and registration of trademark occurred. Justice Elson observed that the more badges of fraud that are proven, the stronger the *prima facie* case of fraudulent intent. The Court found the transaction was a fraudulent conveyance: the debtor was aware that legal proceedings by creditors were imminent; the conveyance was made in secret and for inadequate consideration; and the grantor retained possession under the veil of another entity. The Court held that there was an intent to defraud, delay, or hinder creditors and declared the transfer void in its entirety: BTA Real Estate Group Inc. v. Family Fitness Inc., 2021 CarswellSask 248, 88 C.B.R. (6th) 161, 2021 SKQB 107 (Sask. Q.B.).

The Ontario Superior Court of Justice granted a declaration that a mortgage granted by a defendant after the conclusion of a trial and before the release of the judgment was void under both the *Fraudulent Conveyances Act* and the *Assignments and Preferences Act*: WED Investments Limited v. Showcase Woodycrest Inc., 2021 CarswellOnt 11982, 2021 ONSC 5614 (Ont. S.C.J.). For a discussion of this judgment, see § 5:469 "Attacking Fraudulent Conveyances under Provincial Assignments and Preferences Acts, Fraudulent Preferences Acts and Similar Statutes".

The Ontario Superior Court of Justice granted a charging order and permitted the charging order to be placed on the property. The property had been transferred but the purchaser was not a *bona fide* purchaser without notice of the claims. The property was the subject of a fraudulent conveyance action: Foulidis v. Foulidis et al., 2021 CarswellOnt 12887, 2021 ONSC 5791 (Ont. S.C.J.), affirmed *Foulidis v. Foulidis*, 2022 CarswellOnt 6267, 2022 ONCA 362 (Ont. C.A.). For a discussion of this decision, see § 2:49 **"**Solicitor's Lien on Property of the Bankrupt".

The Ontario Superior Court of Justice declared a conveyance of property from "Church A" to "Church L" to be a fraudulent conveyance and void as against the Crown and the other creditors, pursuant to the *Fraudulent Conveyances Act* (*FCA*) and granted a declaration that the lands were subject to execution at the instance of the Crown as a creditor of Church A. The Crown had sought and received an order restraining Church A and its directors from directly or indirectly contravening Ontario Regulation 82/20, enacted in response to the COVID-19 pandemic. The Court found that Church A and two of its pastors were in contempt of the restraining order and ordered that Church A pay a fine of $35,000 and ordered that it was jointly and severally liable to pay the Crown's costs of $69,000 within 90 days. The Court subsequently found Church A and its pastors in contempt for a second time and ordered the church to pay a fine of $35,000 for contempt, and costs of $5,000. It subsequently found the church and one of the pastors in contempt for a third time and additionally found two of the pastors in contempt in respect of their active participation in the gathering, ordering the church to pay a fine of $45,000, for contempt and pay costs of $5,000. Regional Senior Judge Thomas noted that no fines or costs had been paid. In the middle of contempt proceedings, Church A conveyed to Church L certain lands. R.S.J. Thomas noted that the conveyance occurred less than seven days after one fine and costs order had been issued and 10 days before a second fine and costs order was issued. The Crown commenced the fraudulent conveyance action. Section 2 of the *FCA* provides that a conveyance is void against creditors if it was made "with the intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts penalties or forfeitures." R.S.J. Thomas noted that where the result of an intentional impugned transfer is to defeat, hinder, delay or defraud creditors, there is a presumption in law that the transfer was done with that intent. R.S.J. Thomas found the following badges of fraud to be present: 1. The conveyance had the effect of defeating, hindering, delaying or defrauding creditors. 2. The conveyance was to a non-arm's length party; the two churches are closely associated. 3. The conveyance was made with suspicious timing and in the face of an outstanding liability. 4. The conveyance was made for grossly inadequate consideration. 5. Church A retained beneficial use of the subject lands after the conveyance. Based upon the foregoing, Thomas R.S.J. held that the presumption that the conveyance was made with fraudulent intent within the meaning of s. 2 of the *FCA* was clearly supported. He was satisfied that the conveyance was made with the fraudulent intent to defeat the plaintiff's just and lawful actions to enforcement of the debt award. The Court held that the subject lands were subject to execution at the instance of the Crown as a creditor: R. v. The Church of God (Restoration) Aylmer, 2021 CarswellOnt 13664, 93 C.B.R. (6th) 95, 2021 ONSC 6143 (Ont. S.C.J.).

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The Court of Appeal for Ontario upheld the decision of the application judge. At issue was the interpretation of s. 96 of the *BIA* concerning transfers at undervalue. The Court of Appeal imputed the fraudulent intent of the directing mind of the bankrupt corporations to the bankrupts: Ernst & Young Inc. v. Aquino, 2022 CarswellOnt 3170, 2022 ONCA 202 (Ont. C.A.). For a discussion of this judgment, see § 5:485 Preferences and Transfers at Undervalue.

The Ontario Superior Court of Justice held that certain mortgages were void under both *The Fraudulent Conveyances Act* and *The Assignments and Preferences Act*. The mortgages had been granted with the intent to prefer and were also given for insufficient consideration: Stevens et al. v. Hutchens et al., 2022 CarswellOnt 3266, 98 C.B.R. (6th) 246, 2022 ONSC 1508 (Ont. S.C.J. [Commercial List]) ; appeal dismissed Stevens v. Hutchens, 2022 CarswellOnt 16182, 3 C.B.R. (7th) 312, 2022 ONCA 771 (Ont. C.A.)For a discussion of this judgment, see § 5:469 Attacking Fraudulent Conveyances under Provincial Assignments and Preferences Acts, Fraudulent Preferences Acts and Similar Statutes.

On appeal of a decision of the British Columbia Supreme Court finding a fraudulent conveyance (Global Pacific Financial Services Ltd. v. Canlas, 2021 CarswellBC 3928, 2021 BCSC 2419, 19 C.C.L.I. (6th) 14 (B.C. S.C.), affirmed 2022 CarswellBC 3608, 2022 BCCA 438 (B.C. C.A.)), the British Columbia Court of Appeal upheld the trial judge's decision to set aside a transaction under the *Fraudulent Conveyance Act (FCA)*. The Court of Appeal concluded that the judge had not erred in finding that the transfer had not been for good and valuable consideration and that the defendant had intended to hinder the creditor's claim when he had agreed to be removed from title. Inadequate or nominal consideration does not amount to good consideration for purposes of s. 2 of the *FCA*: Canlas v. Global Pacific Financial Services Ltd., 2022 CarswellBC 3608, 2022 BCCA 438 (B.C. C.A.).

The British Columbia Court of Appeal dismissed an appeal from the decision of the trial judge, declaring that a transfer of property between family members was a fraudulent conveyance. In making his order, the trial judge had appropriately exercised his jurisdiction to vary a desk order of divorce: Brar v. Kootenay Savings Credit Union, 2023 CarswellBC 353, 2023 BCCA 68 (B.C. C.A.). For a discussion of this judgment, see § 5:463 "Fraudulent Conveyances—Conveyances without Consideration".

The respondents had been successful on a motion to strike the plaintiff's claim on the basis that the facts as pleaded were not sufficient to establish standing to bring such a claim under s. 2 of the *Fraudulent Conveyance Act*. The Court of Appeal for Ontario reversed the decision, holding that a claimant who was not a creditor at the time of the transfer can attack the transfer if the transfer was made with the intent to defraud creditors: Ontario Securities Commission v. Camerlengo Holdings Inc., 2023 CarswellOnt 1537, 5 C.B.R. (7th) 212, 2023 ONCA 93 (Ont. C.A.). For a discussion of this judgment, see § 5:461 "Fraudulent Conveyances—Intent to Defeat, Hinder, Delay or Defraud Creditors or Others".

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TAB 23

KERR

ON THE LAW OF

FRAUD AND MISTAKE

INCLUDING

MISREPRESENTATION GENERALLY, UNDUE INFLUENCE,
FIDUCIARY RELATIONSHIP, CONSTRUCTIVE AND
IMPUTED NOTICE, ETC.

SEVENTH EDITION

BY

DENIS LANE McDONNELL, O.B.E., M.A.
of the Middle Temple, Barrister-at-Law

AND

JOHN GEORGE MONROE, B.A.
of the Middle Temple and Lincoln's Inn, Barrister-at-Law

LONDON
SWEET & MAXWELL LIMITED
3 CHANCERY LANE
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CHAPTER VI

FRAUD UPON CREDITORS

SECTION 1—FRAUDULENT CONVEYANCES GENERALLY

13 Eliz. c. 5.

The statute 13 Eliz. c. 5, was made for the protection of creditors. It provided, in effect, that all conveyances and dispositions of property real or personal, made with the intention of delaying, hindering, or defrauding creditors, should be null and void as against them, their heirs, etc., and assigns. It also provided that nothing therein contained should extend to any estate or interest made on good consideration and *bona fide* to any person not having, at the time, any notice of such fraud.

Law of Property Act, 1925, s. 172.

The whole of the Act has now been repealed by the Law of Property Act, 1925 (*a*), and has been replaced by s. 172, which provides as follows :—

" 172.—(1) Save as provided in this section, every conveyance of property, made whether before or after the commencement of this Act, with intent to defraud creditors, shall be voidable, at the instance of any person thereby prejudiced.

(2) This section does not affect the operation of a disentailing assurance, or the law of bankruptcy for the time being in force.

(3) This section does not extend to any estate or interest in property conveyed for valuable consideration and in good faith or upon good consideration and in good faith to any person not having, at the time of the conveyance, notice of the intent to defraud creditors."

It will be noticed that the Law of Property Act, 1925, contains no provision with regard to penalties, but otherwise it seems in effect to re-enact the provisions of 13 Eliz. c. 5, and it seems that cases decided under the former Act are applicable to the latter (*b*).

(*a*) 15 Geo. 5, c. 20.
(*b*) *Holt* v. *Heatherfield Trust*, [1942] 2 K. B. 1. Reported on this point more fully (1942), 111 L. J. K. B. 465.

Parallel enactments in Dominions.

By the Irish statute 10 Car. 1, sess. 2, c. 3, this statute was re-enacted for Ireland.

In the colonial dominions of the Crown—except those in which the general law is not based on the law of England (*c*)—the statute has been adopted as part of the original law of the colony (*d*); but in some of the colonies the Act is no longer in force, having been superseded by local legislation dealing with the same subject-matter (*e*). In British India, provisions of the Indian Transfer of Property Act of 1822, s. 53, similar to those of the statute 13 Eliz. c. 5, have been substituted in the territories to which the Act extends (*f*).

A statute of the Isle of Man (1736) has enacted that " all fraudulent assignments or transfers of the debtor's goods or effects shall be void, and of no effect, against his just creditors (*g*) ".

In the United States of America, the law, as enacted by the provisions, above referred to, of 13 Eliz. c. 5, has been adopted in every State of the Union; in some of the older States, as part of their common law; but more generally by express legislation (*h*).

13 Eliz. c. 5 said to be declaratory of the common law.

It has been frequently observed that 13 Eliz. c. 5 was merely declaratory of what was previously the common law of the land (*l*). But it may well be doubted whether anything more was intended by these expressions than that " whatever offends against the order and good morals of society is an offence against the law of England, and punishable at common law " (*m*); and that " the law abhors covin, and therefore every covinous act shall be void " (*n*). But be this as it may, the statute expressly laid down, and more clearly defined, the law on the subject; whereas the doctrine of the common law was so general as to be vague and difficult of application.

(*c*) *Viz.*, Canada (Province of Quebec), Cape of Good Hope, Natal, Transvaal, Orange River Colony, Ceylon, St. Lucia, Mauritius, British Guiana, Trinidad.

(*d*) Burge, Colonial Law, vol. 4, p. 200; see Tarring, Law of Colonies, 4, 6 (3rd ed.).

(*e*) See, for instance, *Arnold* v. *Fleming*, [1923] 1 D. L. R. 1026 (Can.); *Huss* v. *Lakin*, [1925] 1 D. L. R. 38 (Can.); *Bank of Montreal* v. *Reis*, [1925] 3 D. L. R. 687.

(*f*) S. 2, which repeals 13 Eliz. c. 5 in the territories to which the Act extends—*i.e.*, British India, exclusive of the Punjab and Burma (except the town of Rangoon) *Abdul Hye* v. *Mahomed Mozaffar Hossein* (1884), L. R. 11 Ind. App. 10.

(*g*) Mills' Statute Law of the Isle of Man, p. 238.

(*h*) Story, Eq. Jurisp., s. 353.

(*l*) *Per* Lord Campbell in *Richards* v. *Att.-Gen.* (1844), 12 Cl. & F. 42; and see *Barton* v. *Vanheythuysen* (1853), 11 Hare 126, 132.

(*m*) Lofft 385.

(*n*) 3 Com. Dig., p. 295.

The importance of this statute has very greatly diminished with the evolution of more recent statutes under which many of the transactions at which the statute was directed can be set aside without the necessity of proving fraud (*o*). The treatment of this subject has accordingly been abbreviated in this edition and the reader is referred for a more detailed treatment of the subject to the sixth edition of this book (*p*).

Simplicity of 13 Eliz. c. 5.

In one respect, however, this statute was moulded in strict conformity with the rules of the common law. If " simplicity was the striking feature of the common law " (*q*), it was, in an almost equal degree, the chief feature of the statutes of Elizabeth, which are couched in very general terms, so as to include, and allow their application by the Courts to, any fraudulent contrivances to which the fertility of man's imagination might have resorted, as a means of eluding a more precise and inflexible law.

The statute 13 Eliz. c. 5 was expressed to be directed against fraudulent feoffments, etc., " more commonly used and practised in these days, than hath been seen or heard of heretofore " (*r*). So it has been since, and may ever be; for fraud is infinite, and will always attempt to evade whatever is done for its suppression; to prune it back on one side is but to give it a stimulus to branch out with fresh vigour in another direction. But the simplicity of the enactment and its expansiveness have enabled the Judges to bring within its scope, and extend its operations to, almost every kind of transaction resorted to by debtors to the prejudice of their creditors.

The statute, said Lord Mansfield, C.J., " cannot receive too liberal a construction, or be too much extended, in suppression of fraud " (*s*). So, in *Twyne's Case* (*t*), it was resolved that " because fraud and deceit abound in these days more than in former times, all statutes made against fraud should be liberally and beneficially expounded to suppress the fraud ".

(*o*) See in particular Bankruptcy Act, 1914 (4 & 5 Geo. 5, c. 59), s. 42, which is considered in detail in Section 8 of this chapter, *post*, p. 399, and the Bills of Sale Acts, 1878 (41 & 42 Vic. c. 31), and 1882 (45 & 46 Vic. c. 43), under which many transactions which are reduced to writing and which aim at separating the ownership and possession of goods are made void if not registered.

(*p*) Kerr on Fraud and Mistake, 6th ed., Ch. IV, p. 216.

(*q*) Sug. Pow. (8th ed.) Introduction, p. 1.

(*r*) See Story, Eq. Jur., s. 186.

(*s*) In *Cadogan* v. *Kennett* (1776), 2 Cowp. 434; Moo. 617.

(*t*) (1602), 3 Rep. 82 a.

The statute was not only directed against such transfers of property as were made with the express intention of defrauding creditors; but, as has been justly remarked, it extended as well to such as virtually and indirectly operate the same mischief, by abusing their confidence, misleading their judgment, or secretly undermining their interests. To obviate this, it has gradually grown into a practice to regard certain acts or circumstances as indicative of a so-called fraudulent intention, in the construction of the statute, although, perhaps, there was in fact, no actual fraud or moral turpitude. It is difficult, in many cases of this sort, to separate the ingredients which belong to positive and intentional fraud from those of a mere constructive nature, which the law thus pronounces fraudulent upon principles of public policy (*u*).

To draw any definite invariable line of distinction between moral and technical fraud, on the one hand, or between actual and constructive fraud on the other, would be next to impossible, and could rarely serve any useful purpose. But there are certain circumstances, the presence of which has been taken as conclusive evidence of fraud, and as invariably avoiding the conveyance.

The ordinary form of this constructive fraud under 13 Eliz. c. 5, is a voluntary conveyance made by a man deeply indebted, which accordingly is void, under the statute, as against the grantor's creditors.

Section 172 of the Law of Property Act, 1925 (*a*), makes void against creditors, in very general terms, all kinds of alienation of property, bonds, judgments, etc., had or made with the intention of delaying or defrauding them. In this it follows not only the common law of England but also the Roman civil law. By that law it was provided that all acts, of whatever nature, done by debtors to defraud their creditors should be revoked (*b*).

The common law of Scotland, adopting the principles of the Roman civil law, sets aside dispositions by debtors in fraud of their creditors (*c*). And these principles were enforced, and their application rendered more effectual, in various cases, by a Scottish statute of the year 1621 (*d*).

(*u*) Story, Eq. Jur. s. 349.
(*a*) 15 Geo. 5, c. 20.
(*b*) Dig. lib. 42, tit. 8, par. 1, secs. 1, 2; Domat's Civil Law, book 2, tit. 10, sec. 1, par. 1; 1 Fonbl. Eq. 270.
(*c*) 3 Burge, Col. Law, 618-20.
(*d*) C. 18. As to this statute, and generally on the subject, see 3 Burge, Col. Law, 620; 7 Green, Ency. of Scots Law, 12-20.

The Roman Dutch law, which is the common law in several of the British Dominions and colonies (*e*), adopts the principles, above mentioned, of the Roman civil law (*f*).

13 Eliz. c. 5, concurrent with other Acts.

The operation of s. 172 of the Law of Property Act, 1925 (*g*), is not affected by the provisions of the Bills of Sale Acts, but as has been seen (*h*) these and other Acts have greatly diminished the importance of the section. Those Acts protect creditors against frauds through secret dispositions by their debtors of personal chattels, by providing for the registration of bills of sale; but a bill of sale may be valid, so far as the requirements of the Bills of Sale Acts (*k*) are concerned, and may nevertheless be void against creditors, under the statute of Elizabeth. On the other hand, some dispositions of personal chattels, by which creditors may be prejudiced, but which are not reached by the section, are within the Bills of Sale Acts.

The section is, and the statute 13 Eliz. c. 5 always was, in both principle and practical operation, quite distinct from and independent of the bankruptcy laws; but it has operated concurrently, and for the most part harmoniously, with the long series of Bankruptcy Acts which have succeeded one another, with various provisions and amendments which the growth of commerce and civilisation has rendered necessary for the time being, and which the changing nature of the relations between debtor and creditor has required.

The one great object of the section is to prevent debtors from dealing with their property in any way to the prejudice of their creditors; it, in fact, considers a man deeply indebted as no longer the true owner of his property, but, as it were, a trustee of it for the benefit of his creditors. As it was an old rule that, where a man devised land for the payment of debts and legacies, the debts should first be satisfied, so the section gives a priority to debts over voluntary and fraudulent conveyances, and attempts to prevent a man in his lifetime from sinning against his just creditors. The meaning of

(*e*) Ceylon, Cape of Good Hope, Natal, Transvaal, Orange River Colony, British Guiana.

(*f*) See 1 Van Leeuwen's Comm. on Roman Dutch Law, translated by Kotze, pp. 94-97.

(*g*) 15 Geo. 5, c. 20.

(*h*) See p. 300, *ante*.

(*k*) Chiefly Bills of Sale Act, 1878 (41 & 42 Vic. c. 31), and Bills of Sale Act, (1878), Amendment Act, 1882 (45 & 46 Vic. c. 43).

the section as Jessel, M.R., said, in *Middleton* v. *Pollock* (*l*), " is that the debtor must not retain a benefit for himself. It has no regard whatever to the question of preference or priority among the creditors of the debtor ". A settlement, therefore, which preferred certain creditors, and tended to defeat the others, might be good under the section.

The primary aim of all the successive Bankruptcy Acts, however, is to obtain an equal distribution of the debtor's assets among his creditors. The assumption, when a man is made bankrupt, is that his debts are in excess of his available assets; and the ruling object of the statutes on the subject is to take, and divide amongst the creditors in proportion to their debts, whatever assets there may be; and then, in consideration of the debtor giving up the whole of his property, to discharge him from any future liability with respect to his then debts.

It follows that a disposition of property, which is void in bankruptcy, whether as being an act of bankruptcy, or under an express provision of a statute of bankruptcy, or as being opposed to the policy of the bankruptcy law, is not necessarily void against creditors, under s. 172 of the Law of Property Act, 1925 (*m*).

On the other hand, any conveyance which is void against creditors under the section is also an act of bankruptcy, and, as such, is void, under the bankruptcy law, against the trustee in the grantor's bankruptcy (*n*).

Fraud is complete at the time of conveyance.

Under the section, the fraud against creditors, if any, exists, theoretically at least, at the time the conveyance, etc., is made (*o*). As soon as that is executed, an act has been done upon which the statute is capable of operating at once. The ground on which a disposition of property has been held fraudulent against future creditors, when not made with the intention of prejudicing any existing creditor, has been that the intention of defeating those future creditors must be taken to have been in the mind of the debtor at the time.

(*l*) (1876) 2 Ch. D. 108, 109.
(*m*) 15 Geo. 5, c. 20.
(*n*) See Bankruptcy Act, 1914 (4 & 5 Geo. 5, c. 59), s. 1.
(*o*) *Re Maddever* (1884), 27 Ch. D. 523, 526, 530; *Re Reis, ex p. Clough*, [1904] 2 K. B., at p. 774; See *Hopkinson* v. *Westerman* (1919), 45 O. L. R. 208 (Can.).

Property to which section applies.

The section applies to every conveyance of property. 13 Eliz. c. 5 employed several words more or less synonymous with conveyance and several words more or less synonymous with property. There is no reason to suppose that the new section is in any respect narrower or wider than the old statute. Early decisions under the statute limited its application to property which could be taken to satisfy debts and the long historical development by which almost all property can now be taken in satisfaction of its owner's debts is traced in the preceding edition of this book (*p*). It is now safe to say that the section applies to any property.

Where, by an improvement or alteration of the law, subsequent to the fraudulent conveyance, a better and more effectual, or a different, mode of affecting the property by way of execution has been created, this is immaterial, so long as there was, at the date of the settlement, any remedy against the property; nor does it make any difference that the new mode has been resorted to, rather than that which was in force when the conveyance was made (*q*).

And this principle seems now to apply to such cases, even if the subject-matter of the sale, as the goodwill of a trade, cannot itself be taken in execution (*r*).

The pay or half-pay of officers is not assignable; nor is the salary of an office of trust; and therefore no question with regard to them can arise under the statute (*s*).

Where a man makes a gift of goods which is fraudulent and void against his creditors, and dies, he is considered to have died in full possession, with respect to the claims of the creditors; and the goods are therefore assets in the hands of his personal representative, as to creditors (*t*).

These rights of creditors of a deceased person apply to a fraudulent transfer by him of any kind of property that may be assets of a person on his death; even though the property transferred be not of a kind that could have been taken in execution under a judgment against him. Thus, even before the Judgments Act, 1838 (*u*), a fraudulent

(*p*) Kerr on Fraud and Mistake (6th ed.), pp. 222 *et seq.*
(*q*) *Blenkinsopp* v. *Blenkinsopp* (1852), 1 D. M. & G. 495.
(*r*) *French* v. *French* (1855), 6 D. M. & G. 95; *Neale* v. *Day* (1858), 28 L. J. Ch. 45.
(*s*) *Lucas* v. *Harris* (1886), 18 Q. B. D. 127; *Crowe* v. *Price* (1889), 22 Q. B. D. 429; 58 L. J. Q. B. 215.
(*t*) *Shears* v. *Rogers* (1832), 3 B. & Ad. 362.
(*u*) 1 & 2 Vict. c. 110.

transfer of a *chose in action* or money, which could not be impeached during the transferor's lifetime—at least, where he was not a bankrupt or declared insolvent—owing to property of these kinds not being then liable to be taken in execution, could always be avoided under 13 Eliz. c. 5, after his death (*a*). The creditors could, at law, sue the person claiming under the fraudulent instrument as executor *de son tort*, the property settled being assets in his hands (*b*); and, in equity, the Court would administer the property, at the suit of creditors, as assets of the deceased (*c*).

But an alienation fraudulent against creditors of the deceased is good against the rightful executor or administrator; for he is not a creditor, nor does he represent creditors; and therefore it is no *devastavit* for him to deliver the goods to the fraudulent grantee, who can be sued for them by creditors, but not by any other person (*d*).

An alienation of property may, it seems, be impeachable under the section, where the settlor has become bankrupt, without reference to the question whether or not the property is of a kind that could have been taken in execution for debt at the time of alienation; provided it is property of a kind that is divisible among creditors, under the bankruptcy law (*e*).

The section declares certain conveyances to be voidable. Conveyance is defined in s. 205 (1) (ii) of the Law of Property Act, 1925 (*f*) as including a mortgage, charge, lease, assent, vesting declaration, vesting instrument, disclaimer, release and every other assurance of property by any instrument except a will.

The jurisdiction of the Court, however, was not strictly confined by the words of the statute 13 Eliz. c. 5, where the words were rather wider. In whatever way the disposition of property be effected, it will probably be held within the meaning of the section, which is

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(*a*) See *per* Lord Cottenham, C., in *Norcutt* v. *Dodd* (1841), Cr. & Ph. 100, 102; *Whittington* v. *Jennings* (1834), 6 Sim. 493.

(*b*) See *Shears* v. *Rogers* (1832), 3 B. & Ad. 326; *Shee* v. *French* (1857), 3 Drew. 716; *Re Mouat*, [1899] 1 Ch. 831, 833, *per* Stirling, J.; *Edmunds* v. *Edmunds*, [1904] P. 362, 375, *per* Barnes, J.

(*c*) *Scarf* v. *Soulby* (1849), 1 Mac. & G. 364; *Taylor* v. *Coenen* (1876), 1 Ch. D. 636; *per* Stirling, J., in *Re Mouat*, [1899] 1 Ch. 831, 833; *Freeman* v. *Pope* (1870), L. R. 5 Ch. 538.

(*d*) *Hawes* v. *Leader* (1611), Cro. Jac. 271; *French* v. *French* (1855), 6 De G. M. & G. 95; *Cornish* v. *Clark* (1872), L. R. 14 Eq. 184.

(*e*) As to which, see Bankruptcy Act, 1914 (4 & 5 Geo. 5, c. 59), s. 37.

(*f*) 15 Geo. 5, c. 20.

general, for the suppression of fraud (*g*); and a man will not be allowed to do in one way that which he cannot do in another (*h*).

A judgment (*l*), therefore, or a confession of judgment, even for a debt really due (*m*) (and *a fortiori* where there is no real debt) (*n*), and a fraudulent judgment and execution (*o*), may be conveyances within the section. The same may be said of a covenant not to enforce a bond (*p*); or (it would seem) the release or forgiveness of debts due (*q*); for, as debts due to a debtor can now be made available for payment of his debts, the release of them is an injury to his creditors.

So, where judgment was given against one in debt, and he suffered himself to be outlawed in felony, to the intent to defraud his creditors, and afterwards purchased a pardon and had restitution, the creditor was allowed to sue out execution on account of the manifest fraud; and, by the common law, such circuitous evasions of justice were not allowed to take effect (*r*).

So, where tenant for life, being in debt, colluded with the remainderman and committed a forfeiture, Sir Matthew Hale, C.J., was of opinion that creditors were entitled to avoid this, as much as any fraudulent conveyance (*s*).

The exercise of a general power of appointment by deed, either of land (*t*) or of a sum of money (*u*), has been held to be a disposition within 13 Eliz. c. 5, and fraudulent and void under that statute, as against creditors of the appointor; but, it seems, only if, and to the extent that, the appointor is entitled to the property in default of appointment (*v*). This appears to be a rule distinct from that under which property appointed by deed or will, in favour of a volunteer, in exercise of a general power of appointment, is assets for the benefit of the appointor's creditors on his death (*w*). It would seem that,

(*g*) *Twyne's Case* (1602), 3 Rep. 82a; see also Lord Mansfield in *Cadogan* v. *Kennett* (1776), 2 Cowp. 434.

(*h*) *Fitzer* v. *Fitzer* (1743), 2 Atk. 511.

(*l*) *Clavey* v. *Hayley*, (1776), 2 Cowp. 427.

(*m*) *Holbird* v. *Anderson* (1793), 5 T. R. 235; *Meux* v. *Howell* (1803), 4 East 1.

(*n*) *Billiter* v. *Young* (1856), 6 E. & B. 1.

(*o*) *Imray* v. *Magnay* (1843), 11 M. & W. 267; *Hunt* v. *Hooper* (1844), 12 M. & W. 664.

(*p*) *Slack* v. *Tolson* (1826), 1 Russ. 553.

(*q*) See *Sibthorp* v. *Moxom* (1747), 3 Atk. 581.

(*r*) *Verney's Case* (1695), 2 Dyer 245b.

(*s*) Vin. Abr. tit. Fraud (F.), pl. 14.

(*t*) *Townshend* v. *Windham* (1750), 2 Ves. Sen. 1, 10.

(*u*) See *Whittington* v. *Jennings* (1834), 6 Sim. 493; Sug. Pow. 651.

(*v*) Sug. Pow. 651; Chance on Powers, Secs. 1819, 1849; cf. also *Re Mathieson*, [1927] 1 Ch. 283, a case under s. 42 of the Bankruptcy Act, 1914 (4 & 5 Geo. 5, c. 59).

(*w*) As to this rule see *Martyn* v. *Macnamara* (1843), 4 Dru. & War, at p. 426; *Fleming* v. *Buchanan* (1853), 3 D. M. & G. 976; *Re Lawley*, [1902] 2 Ch. 675.

in the case last mentioned, a fraudulent intent, express or implied, at the time of making the appointment, is not essential, as it is in the case of disposition within 13 Eliz. c. 5, and that the property becomes assets of the appointor, although he has not an interest in it, in default of appointment.

A contract for the conveyance or settlement of property, if made for valuable consideration, and enforceable specifically, was an alienation within the meaning of 13 Eliz. c. 5 (*a*); and if the contract was not impeachable under that statute as a fraudulent alienation, a subsequent conveyance or settlement of the property, in performance of the contract according to its terms, will not be void under the statute, by reason of indebtedness of the grantor at the time of the conveyance or settlement (*b*). It would seem, however, that if the contract were merely voluntary, and therefore not enforceable specifically, it would not have the effect of protecting the subsequent conveyance or settlement against avoidance under the statute (*c*). But it has been held (in a different context) that a contract is not a conveyance for the purpose of the Law of Property Act, 1925 (*d*). Presumably the Court would now look at the contract and conveyance together.

Married women.

A married woman is now in the same position as a feme sole with regard to contractual capacity (*e*), and there are now no valid subsisting restraints on anticipation (*f*).

SECTION 2—WHAT VOLUNTARY CONVEYANCES ARE VOID AS AGAINST EXISTING CREDITORS

Only intent of donor is material.

In considering whether a voluntary conveyance is voidable under section 172 of the Law of Property Act, 1925 (*g*), the intent or purpose

(*a*) See *Barton* v. *Vanheythuysen, Stone* v. *Vanheythuysen* (1853), 11 Hare 126.
(*b*) See *Re Reis, ex p. Clough*, [1904] 2 K. B. 769; overruling *Ex p. Bolland, re Clint* (1873), L. R. 17 Eq. 115; *Re Holland*, [1902] 2 Ch. 360.
(*c*) See *Honywood* v. *Honywood* (1855), 20 Beav. 451, 452; *Warden* v. *Jones* (1857), 2 De G. & J. 76.
(*d*) 15 Geo. 5, c. 20. *Borman* v. *Griffith*, [1930] 1 Ch. 493.
(*e*) Law Reform (Married Women and Tortfeasors) Act, 1935 (25 & 26 Geo. 5, c. 30), s. 1.
(*f*) Married Women (Restraint upon Anticipation) Act, 1949 (12, 13 & 14 Geo. 6, c. 78).
(*g*) 15 Geo. 5, c. 20.

TAB 24

CHAPTER 17 Common Law

PART 3 RELIANCE ON COMMON LAW TO SUPPLEMENT LEGISLATION

§ 17.02 Continued Recourse to Common Law Rules, Remedies and Courts

[3] Interference with legislative policies or purpose

Resort to the common law is impermissible if it would interfere with the policies embodied in legislation or defeat its purpose. This was an important consideration in *Zaidan Group Ltd. v. London (City)*,[1] a case concerning the right of a municipal ratepayer to claim interest on an overpayment of its taxes. This overpayment had been refunded by the City of London without interest, as allowed under Ontario's *Assessment Act*. Although another provincial enactment conferred power on municipalities to pass by-laws authorizing the payment of interest on overpaid taxes, no by-law on the subject had been passed by the City of London. In these circumstances the ratepayer sought to rely on the common law doctrine of unjust enrichment. It argued that the municipality's use of money to which it was not entitled represented an enrichment for which there was no legal justification. This strategy did not succeed. As Carthy J.A. explained:

> ... There is no question of a gap being left in the legislation for the common law to fill. The taxes are a statutory creation and the conditions surrounding their payment and repayment must be in the statutes associated with their creation. The common law cannot characterize competent legislation as unjust, and it would be doing so if it imposed an additional duty to pay interest on a statutory duty to levy and to refund a specific amount of money.[2]

Giving each municipality discretion to decide whether interest should be paid in these circumstances was a definitive solution, expressing a policy adopted by the legislature. To permit recourse to the common law to force the recovery of interest would undermine this policy; it would effectively take back the discretion which the legislature had chosen to confer on the municipality.

Footnote(s)

1 *[1990] O.J. No. 33*, *71 O.R. (2d) 65* (Ont. C.A.), affd *[1991] S.C.J. No. 92*, *[1991] 3 S.C.R. 593* (S.C.C.).

2 *Zaidan Group Ltd. v. London (City)*, *[1990] O.J. No. 33*, *71 O.R. (2d) 65* at para. 11 (Ont. C.A.), affd *[1991] S.C.J. No. 92*, *[1991] 3 S.C.R. 593* (S.C.C.). See also *Regina Police Assn. v. Regina (City) Board of Police*Commissioners, *[2000] S.C.J. No. 15*, *[2000] 1 S.C.R. 360* (S.C.C.), discussed below at §17.02[8]; *Jackson v. Canadian National Railway*, *[2013] A.J. No. 1397*, *2013 ABCA 440* at para. 41 (Alta. C.A.), leave to appeal refused *[2014] S.C.C.A. No. 57* (S.C.C.).

[1] Incorporation of common law terms or concepts

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Ruth Sullivan

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CHAPTER 17 Common Law

PART 2 RELIANCE ON COMMON LAW TO INTERPRET LEGISLATION

[1] Incorporation of common law terms or concepts

When used in legislation, common law terms and concepts are presumed to retain their common law meaning. In *R. v. Holmes*,[1] for example, the Supreme Court of Canada was concerned with the scope of the word "excuse" in the phrase "without lawful excuse" appearing in several provisions of the *Criminal Code*. Although the majority adopted a restrictive reading of this phrase, Dickson C.J. wrote:

> There is no doubt that Parliament can redefine the meaning of "excuse".... The important point is that Parliament should give some indication, express or implied, that it has changed the meaning of "excuse" when it uses it in a statute. Otherwise, the word will be understood to have the meaning of "excuse" under the common law....[2]

More recently, speaking for a majority of the Supreme Court of Canada in *R. v. W. (D.L.)*, Cromwell J. wrote:

> When Parliament uses a term with a legal meaning, it intends the term to be given that meaning. Words that have a well-understood legal meaning when used in a statute should be given that meaning unless Parliament clearly indicates otherwise.[3]

The presumption in favour of common law meaning can be rebutted, using the standard techniques of statutory interpretation. In *Prebushewski v. Dodge City Auto (1984) Ltd.*,[4] for example, the Supreme Court of Canada had to determine whether the reference to exemplary damages in s. 65(1) of Ontario's *Consumer Protection Act* was meant to create a new remedy or merely codify the common law. Subsection 65(1) provided:

> 65(1) In addition to any other remedy provided by this Part or any other law in force in the province, a consumer ... may recover exemplary damages from any manufacturer, retail seller or warrantor who has committed a wilful violation of this Part.

In concluding that the section was meant to create a new remedy, Abella J. wrote:

> At common law, exemplary or punitive damages are awarded only in exceptional cases ... of "malicious, oppressive and high-handed" conduct that "offends the court's sense of decency"....
>
> In my view a different test for exemplary damages is anticipated by s. 65(1). The language of s. 65(1) is clear and unambiguous: once a wilful — or deliberate — violation has been found, the trial judge has a discretion to award exemplary damages. Had the legislature intended that the common law — and more exacting — test apply, it could easily have used words affiliated with the traditional approach to exemplary damages, such as "malicious" or "oppressive". By designating instead that "wilful" violations of the Act are sufficient to trigger a judge's discretion, the legislature has signalled an intention to lower the threshold and grant easier access to the remedy of exemplary damages.[5]

Abella J. went on to point out that this interpretation was in keeping with the purpose of the provision and the scheme of the Act.

In *All Trans Financial Services Credit Union Ltd. v. Financial Institutions Commission*,[6] the issue was whether it was reasonable for the Financial Institutions Commission to rely on the ordinary meaning of "deposit" as opposed to its common law meaning in interpreting s.1 of B.C.'s *Financial Institutions Act*. It provided that "'deposit business' means the business of receiving on deposit or soliciting for deposit money that is repayable [under specified circumstances]." In determining that reliance on the dictionary definition of "deposit" was reasonable, B.C.'s Court of Appeal wrote:

[1] Incorporation of common law terms or concepts

I have difficulty with the use of the term "common law definition" for two reasons. First, I am not persuaded that there is such a thing as the common law definition of deposit businesses. Regulation of financial institutions does not occur in the absence of legislation. Second, the sources relied upon in determining the contours of the "common law definition" also operate within highly technical, specialized spheres.

On that basis, I am not persuaded that the presumption that legislation is consistent with the common law unless the contrary intention is expressed or implied in the legislation is a useful principle in this case.[7]

Footnote(s)

1 *[1988] S.C.J. No. 39*, *[1988] 1 S.C.R. 914* (S.C.C.).

2 *R. v. Holmes*, *[1988] S.C.J. No. 39*, *[1988] 1 S.C.R. 914* at para. 25 (S.C.C.). See also *A.Y.S.A. Amateur Youth Soccer Association v. Canada (Revenue Agency)*, *[2007] S.C.J. No. 42*, *2007 SCC 42* at paras. 24*ff* (S.C.C.); *Blank v. Canada (Minister of Justice)*, *[2006] S.C.J. No. 39*, *[2006] 2 S.C.R. 319* at paras. 4, 69 (S.C.C.); *Amos v. Insurance Corp. of British Columbia*, *[1995] S.C.J. No. 74*, *[1995] 3 S.C.R. 405* at para. 15 (S.C.C.); *H.C.I. Ventures Ltd. v. S.O.L. Acres*, *[2020] S.J. No. 73*, *2020 SKCA 24* at para. 32 (Sask. C.A.); *R. v. Pootlass*, *[2019] B.C.J. No. 403*, *2019 BCCA 96* at paras. 17*ff* (B.C.C.A.); *Namdarpour v. Vahman*, *[2019] B.C.J. No. 765*, *2019 BCCA 153* at paras. 30*ff* (B.C.C.A.); *Sparks v. Holland*, *[2019] N.S.J. No. 20*, *2019 NSCA 3* at para. 53 (N.S.C.A.); *Yip v. H.S.B.C. Holdings plc.*, *[2018] O.J. No. 3681*, *2018 ONCA 626* at paras. 32-34 (Ont. C.A.) (leave to appeal refused, *[2018] S.C.C.A. No. 410* (S.C.C.); *Mueller v. Oko*, *[2015] A.J. No. 613*, *2015 ABCA 194* at paras. 14-16 (Alta. C.A.); *R. v. Cosh*, *[2015] N.S.J. No. 324*, *2015 NSCA 76* at paras. 71*ff* (N.S.C.A.); *Canada v. Berg*, *[2014] F.C.J. No. 109*, *2014 FCA 25* at para. 23 (F.C.A.); *Manitoba Public Insurance Corp. v. University of Waterloo*, *[2007] M.J. No. 321*, *2007 MBCA 107* at paras. 34-35 (Man. C.A.); *Payne v. Alb*, *[1999] O.J. No. 1954*, *44 O.R. (3d) 598* at 604-605 (Ont. C.A.). For this presumption to apply it is not necessary that the legislation exactly reproduce the common law terminology. So long as it uses language that is apt to refer to the common law term or concept, the presumption applies: see *Woelk v. Halvorson*,*[1980] S.C.J. No. 82*, *[1980] 2 S.C.R. 430* at 437 (S.C.C.); *Cabezas v. Maxim*, *[2016] B.C.J. No. 321*, *2016 BCCA 82* at paras. 36-39 (B.C.C.A.).

3 *R. v. W. (D.L.)*, *[2016] S.C.J. No. 22*, *2016 SCC 22* at para. 20 (S.C.C.); see also para. 43.

4 *[2005] S.C.J. No. 10*, *[2005] 1 S.C.R. 649* (S.C.C.).

5 *Prebushewski v. Dodge City Auto (1984) Ltd.*, *[2005] S.C.J. No. 10*, *[2005] 1 S.C.R. 649* at paras. 24-25 (S.C.C.). See also *R. v. Husbands*, *[2017] O.J. No. 3795*, *2017 ONCA 607* at paras. 35-36 (Ont. C.A.).

6 *[2018] B.C.J. No. 1259*, *2018 BCCA 270* at paras. 139-140 (B.C.C.A.).

7 *All Trans Financial Services Credit Union Ltd. v. Financial Institutions Commission*,*[2018] B.C.J. No. 1259*, *2018 BCCA 270* at paras. 139-140 (B.C.C.A.).

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TAB 25

ESSENTIALS OF
CANADIAN LAW

BANKRUPTCY AND INSOLVENCY LAW

RODERICK J. WOOD

Faculty of Law
University of Alberta

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CHAPTER 1

AN INTRODUCTION TO INSOLVENCY LAW

A. THE NATURE, PURPOSE, AND BOUNDARIES OF INSOLVENCY LAW

1) The Relationship between Bankruptcy Law and Insolvency Law

In Canada, it is common to see the terms bankruptcy and insolvency law used in tandem. The *Constitution Act, 1867* confers exclusive authority on the Parliament of Canada to make laws in relation to bankruptcy and insolvency,[1] and the primary federal statute in the field is named the *Bankruptcy and Insolvency Act* (*BIA*). The only danger with this usage is that it might suggest to some that bankruptcy law and insolvency law are two distinct though related legal fields. In fact, insolvency law is the wider concept, encompassing bankruptcy law but also including other non-bankruptcy insolvency systems. The usage has probably come about because bankruptcy is the oldest and most established of the insolvency regimes and therefore takes pride of place at the beginning of the phrase, with all of the other insolvency regimes lumped together at the end. This terminology should not obscure the fact that bankruptcy is merely one of several different legal regimes that respond to the insolvency of a debtor.

1 30 & 31 Vict., c. 3 (U.K.), reprinted in R.S.C. 1985, App. II, No. 5, s. 91(21).

2) The Single Proceeding Model of Insolvency Law

At its core, insolvency law is concerned with the inability of a person to pay claims owing to others. A person who is in this state of affairs is considered to be insolvent, and insolvency law provides a set of legal responses to address this problem. Insolvency law is premised upon a debtor's inability to pay, rather than upon a debtor's unwillingness to pay. If the debtor has the means to pay but simply refuses to do so, a claimant can commence and prosecute a civil action against the debtor. If the claimant is successful, the claimant will obtain a judgment from the court. This permits the claimant to invoke judgment enforcement law in order to obtain satisfaction of the claim. The judgment enforcement system is established by provincial law and gives the claimant a set of enforcement remedies against the assets of the debtor.

Insolvency law is not primarily concerned with coercing payment from reluctant debtors. Rather, it comes into play when the debtor does not have sufficient assets to satisfy the claims of all of the claimants. In most cases, the debtor's insolvency results from an inability to pay contractual claims voluntarily incurred by the debtor. Some of these claims may arise from the extension of credit by a person who has provided goods or services to the debtor and who has agreed to accept payment for them at some future date. Others may arise from contracts of loan under which the debtor borrows a specific sum of money from a lender and agrees to repay it according to a fixed schedule (term loans) or under which amounts that are advanced are repayable on demand (demand loans). However, insolvencies may also occur because the debtor does not have sufficient assets to satisfy claims that are not associated with an extension of credit. These may involve claims against the debtor for breach of contract, as in the case of a construction firm that is liable in contract for the shoddy construction of a building. They may also involve claims against the debtor in tort for injuries caused by wrongful acts or omissions, as in the case of a manufacturer whose use of asbestos in a product has rendered it liable in negligence to victims suffering from asbestosis and mesothelioma.

The various insolvency regimes have different objectives. Some are primarily concerned with the liquidation of the debtor's assets. Others provide a means by which a debtor can attempt to rescue a business by seeking an arrangement or compromise in which creditors agree to accept less than they are entitled to. Some are concerned with the economic rehabilitation of the debtor. Others are not. In spite of these differences, there is one feature that is common to all insolvency regimes. They all provide a collective proceeding that supersedes the

usual civil process available to creditors to enforce their claims. The creditors' remedies are collectivized in order to prevent the free-for-all that would otherwise prevail if creditors were permitted to exercise their remedies. In the absence of a collective process, each creditor is armed with the knowledge that if they do not strike hard and swift to seize the debtor's assets, they will be beaten out by other creditors. The fundamental importance of "single control" in a collective insolvency proceeding has long been recognized in Canadian law.[2] The single control policy furthers the "public interest in the expeditious, efficient and economical clean-up of the aftermath of a financial collapse."[3]

The race to grab assets in the absence of a collective insolvency regime does not provide an environment within which an efficient and orderly liquidation can occur. The process is inefficient because each creditor must separately attempt to enforce their claims against the debtor's assets, and this produces duplication in enforcement costs. The piecemeal selling off of assets also results in a much smaller recovery than if a single person were in control of the liquidation. Similarly, the race to seize assets does not produce an environment within which negotiations with creditors can easily occur. A reasonable creditor who is inclined to negotiate with the debtor will be unlikely to do so if other creditors are actively taking steps to make away with the debtor's realizable assets; instead, the creditor will feel compelled to join the wild dash to seize assets. Although some of the creditors (those who are able to strike first) are better off in such a scenario, the creditors as a group receive less than if a more orderly liquidation or negotiated arrangement had taken place.

There is one insolvency regime that only partially conforms to the single proceeding model. The privately appointed receiver is sometimes viewed as an insolvency regime but at other times is characterized as being primarily a secured creditor remedy. Although the commencement of a private receivership does not give rise to a stay of proceedings on the other claimants, the priority afforded to the secured creditor is such that the other creditors have little to gain in attempting to seize assets. The lack of a stay of proceedings, therefore, is not a particular impediment to the sale of a going concern. Because the statutes have imposed obligations on receivers that are owed to persons other than the secured creditor and because the statutory priority rules that apply to bankruptcy are increasingly being extended to cover receiverships

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2 *Re J. McCarthy & Sons Co.* (1916), 38 O.L.R. 3 (S.C.A.D.); *Stewart v. LePage* (1916), 53 S.C.R. 337.

3 *Re Eagle River International Ltd.*, [2001] 3 S.C.R. 978 at para. 27.

as well, it is now sensible to treat the privately appointed receiver as a type of insolvency regime.

3) The Objectives of Insolvency Law

The various insolvency regimes impose a single, collective proceeding within which the creditors must participate in order to vindicate their claims against an insolvent person. However, the fundamental objective of the process is not always the same across the various insolvency regimes. In respect of the commercial insolvency regimes, there are two fundamentally different objectives—liquidation and rescue. Liquidation regimes, such as bankruptcy, seek to liquidate the debtor's assets and distribute the proceeds to the creditors. Restructuring regimes (which are also referred to as reorganization regimes) seek to preserve the business as an operating entity by reducing or adjusting the claims of the creditors so as to provide the debtor with a new viable capital structure.

Consumer insolvency regimes similarly involve either the liquidation of the debtor's assets or an alternative to liquidation in which the consumer debtor retains his or her assets and satisfies all or part of the claims out of future earnings. Despite this difference, the fundamental objective that underlies all consumer insolvency regimes is that of economic rehabilitation of the debtor. Although consumer bankruptcy is formally a liquidation regime, the reality is that in many instances the consumer has very little property of value and therefore the liquidation process is not engaged.

In addition to these fundamental objectives, there are several second-order objectives that are pursued in the design of insolvency regimes. The UNCITRAL *Legislative Guide on Insolvency Law* states that, in order to establish and develop an effective insolvency law, the following key goals should be considered:

- Provide certainty in the market to promote economic stability and growth.
- Maximize value of assets.
- Strike a balance between liquidation and reorganization.
- Ensure equitable treatment of similarly situated creditors.
- Provide for timely, efficient and impartial resolution of insolvency.
- Preserve the insolvency estate to allow equitable distribution to creditors.
- Ensure a transparent and predictable insolvency law that contains incentives for gathering and dispensing information.

- Recognize existing creditors' rights and establish clear rules for ranking of priority claims.[4]

Many of these objectives are directed towards increasing the efficiency, predictability, and transparency of the insolvency process. This ensures that there will be more assets available to satisfy the claims of creditors and reduces the costs of credit by making it easier for creditors to predict future outcomes.

4) The Relationship between Private Law and Insolvency Law

Private law is the part of our legal system that involves relations between legal persons as opposed to relations between a person and the state. Private law is made up of three components: (1) the law of persons; (2) the law of rights; and (3) the law of procedure.[5] The law of persons defines the entities that are afforded legal personality—those who are considered to be persons in law and who are thereby capable of holding and enforcing rights. The law of rights is concerned with the nature and scope of rights. It deals with three fundamental questions. The first is about the reach of the right and whether the right can be demanded against the world in general (a proprietary right) or whether it can be demanded against only a particular person (a personal right). The second question deals with the content of the right—what the right gives to the holder. The third question looks to the events that create the right—whether the right arises out of a consensual agreement, a wrong, through unjust enrichment, or out of some other event. The law of procedure describes the legal processes that must be invoked when seeking to enforce a right.

Insolvency law, in large measure, is procedural in nature.[6] The commencement of insolvency proceedings will typically prevent a claimant from pursuing a claim through an ordinary civil action before a court or enforcing it through the judgment enforcement system. Instead, the person holding the right must assert the right through the collective procedure provided for by insolvency law. The mechanism provided by insolvency law for asserting, proving, and enforcing a claim is radically

4 (New York: United Nations, 2005) at 14.

5 See P. Birks, ed., *English Private Law*, vol. 1 (Oxford: Oxford University Press, 2000) at xxv–li.

6 See J. Duns, *Insolvency: Law and Policy* (Oxford: Oxford University Press, 2002) at 12.

different from the ordinary civil process that is used when the debtor is not insolvent.

Insolvency law does not generally affect the law of persons, but it may restrict access to certain of the insolvency regimes on the basis of the kind of person involved. For example, the *Companies' Creditors Arrangement Act* (*CCAA*) applies only to corporations, while the consumer proposal provisions apply only to individuals. However, insolvency law does not involve itself with the creation of legal personality, instead leaving this to be determined by other branches of private law.

Insolvency law does not generally involve itself with the content or creation of rights. For the most part, pre-insolvency rights remain unaltered in insolvency. A claim for damages for breach of contract is validated and enforced through a different legal process under an insolvency regime, but the basic legal entitlement is not otherwise affected. There are, however, several important exceptions to this principle. For example, insolvency law gives a supplier of goods a special right of repossession that can be exercised against a receiver or a trustee in bankruptcy. This right carries with it a priority over secured creditors and has no counterpart in ordinary private law principles. Insolvency law proceeds from the premise that private law rights are not affected by insolvency unless an insolvency law rule specifically alters the private law right.

5) The Relevance of Proprietary Rights and Personal Rights in Insolvency Law

There are two fundamentally different kinds of rights that are recognized in private law: proprietary rights (also referred to as real rights or rights *in rem*) and personal rights (also referred to as rights *in personam*). This forms the division between property and obligation, between what I own and what I am owed. The difference between these kinds of rights is the extent to which the right can be demanded against other persons. A proprietary right is a right in relation to a thing. The right can be demanded against any other person who takes possession or control of or who asserts an interest in the thing. By way of contrast, a personal right can be asserted only against the person who owes the obligation.

Insolvency law, for the most part, preserves the distinction between proprietary rights and personal rights. The distinction is most critical when analysing the position of persons who have claims against the insolvent debtor. Those who have personal rights against the debtor can recover only out of the assets of the debtor. These claimants cannot

look to property that belongs to third parties to satisfy their claims; the purpose of insolvency law is not to confiscate property of others or to redistribute wealth in society. Those who have proprietary claims are generally free to assert those rights unaffected by the claims of those who have personal claims against the debtor. This explains why secured creditors are entitled to look to their collateral to satisfy their claims free from the claims of ordinary unsecured creditors.

This is not to say that those with proprietary rights are unaffected by the insolvency regime. In some cases, the insolvency regime treats proprietary claims as largely falling outside the scope and ambit of the insolvency regime. For example, in bankruptcy a secured creditor is permitted to withdraw its collateral from the bankrupt estate and to realize on it outside the bankruptcy proceedings.[7] In other cases, persons with proprietary rights are participants in the insolvency proceedings. For example, in restructuring proceedings a secured creditor cannot enforce its remedies, is entitled to vote on the plan, and is bound by a compromise or arrangement that is approved by a majority of the creditors and the court. However, the priority afforded to secured creditors over unsecured creditors is recognized and preserved in the restructuring proceedings.[8]

6) The Relationship between Insolvency Law and Provincial Law

Private law is comprised of common law principle as modified by statutory enactment. As the provinces have the legislative authority to enact laws pertaining to property and civil rights, statutory modification of common law principles is predominantly provincial in origin. For example, provincial statutes have extensively modified the common law position respecting secured transaction law through the enactment of personal property security legislation. Insolvency law is primarily procedural and does not generally redefine the substantive rights held by claimants. As a result, provincial statutes that alter common law rights are usually fully effective in insolvency.[9] Occasionally, there is a con-

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7 See Chapter 5, Section B(2).

8 See Chapter 16, Section D.

9 This idea is codified in the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 72(1) [*BIA*], which provides that the Act does not abrogate or supersede the substantive provisions of any other law or statute relating to property and civil rights that are not in conflict, and gives a trustee all rights and remedies provided by that law or statute as supplementary to and in addition to the rights and remedies provided by the *BIA*.

flict between the federal and provincial statutes. In these instances, the federal insolvency provision is given pre-eminence.

Provincial legislation also plays a supplementary role by creating additional rights that can be exercised by an insolvency administrator. For example, a trustee in bankruptcy can invoke provincial fraudulent preference legislation to avoid a pre-bankruptcy transfer, and can invoke personal property security legislation to subordinate an unperfected security interest.[10] A trustee can also resort to provincial legislation in order to occupy temporarily the leased premises following the bankruptcy.[11] In other instances, the federal insolvency statute expressly incorporates a rule or concept created by a provincial statute. For example, the bankruptcy statute provides that property that is exempt under provincial law is not divisible among the creditors.[12]

B. THE CONSTITUTIONAL DIMENSIONS OF INSOLVENCY LAW

The Parliament of Canada has the exclusive legislative authority to enact law in relation to bankruptcy and insolvency. Until the Great Depression of the 1930s, Canadian insolvency legislation was primarily concerned with proceedings under which an insolvency administrator liquidated the insolvent debtor's assets and distributed the proceeds to creditors. Two statutes passed by Parliament in the wake of the Depression, the *Companies' Creditors Arrangement Act*[13] and the *Farm Creditors Arrangement Act*,[14] adopted a fundamentally different approach in that they created insolvency proceedings where the objective was the negotiation of an arrangement under which the creditors compromised their claims and the debtor was permitted to carry on the business or farming operations. Both of these statutes were challenged, and in both cases the constitutional validity of the legislation was upheld.[15] The Privy Council held that the power to enact laws in relation to bankruptcy and insolvency was not intended to be "stereotyped" so as to confine Parliament to the types of insolvency regimes then in existence. The

10 See Chapter 5, Section B(3) and Chapter 7, Section A(1).
11 See Chapter 6, Section B(3).
12 See Chapter 4, Section C(2).
13 S.C. 1933, c. 36.
14 S.C. 1934, c. 53.
15 *In re Companies' Creditors Arrangement Act*, [1934] S.C.R. 659; *Attorney General for British Columbia v. Attorney General for Canada* (1937), 18 C.B.R. 217 (P.C.).

element essential to constitutional validity is that the legislation must be directed towards debtors who are unable to meet their liabilities.

The attitude towards provincial attempts to establish insolvency regimes has evolved significantly over time. Following the wholesale repeal of Canadian insolvency legislation in 1880, provinces enacted voluntary assignment legislation to partially fill the gap. The legislation permitted a debtor to make an assignment of his or her property to a trustee who would liquidate it and distribute it among the creditors. The Privy Council held that this legislation was *intra vires*.[16] It noted that the proceedings were not compulsory and that the legislation did not require that the debtor be insolvent. This led to the belief that provincial insolvency legislation might be valid in the absence of a similar federal insolvency regime. Subsequent cases have rendered this view doubtful.

In 1937 Alberta enacted the *Debt Adjustment Act*.[17] This legislation prevented creditors from enforcing their remedies against a debtor without first obtaining a permit from the Debt Adjustment Board. The board also had the power to compel a creditor to accept a compromise or arrangement. Both the Supreme Court of Canada[18] and the Privy Council[19] held that the statute was *ultra vires* of the Alberta legislature. In 1959 the Alberta *Orderly Payment of Debts Act*[20] was struck down as beyond the powers of the provincial legislature for essentially similar reasons.[21] The majority opinion of the Supreme Court of Canada expressly cast doubt upon the decision of the Privy Council in the *Voluntary Assignments* case.

Although it is beyond the powers of the provincial legislatures to create insolvency regimes, provincial laws that create or adjust rights within the context of a bankruptcy or insolvency have been upheld. Provincial fraudulent preference legislation gives a creditor the right to set aside preferential transfers made by an insolvent debtor to a creditor. The Supreme Court of Canada in *Robinson v. Countrywide Factors Ltd.*[22] upheld the legislation. The majority opinion accepted the proposition that many of the institutions concerning credit and security are explicitly or implicitly predicated on the risk of insolvency, and that the fed-

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16 *Attorney General of Ontario v. Attorney General for Canada (Voluntary Assignments)*, [1894] A.C. 189.

17 S.A. 1937, c. 9.

18 *Reference Re: Debt Adjustment Act, 1937 (Alberta)*, [1942] S.C.R. 31.

19 (1943), 24 C.B.R. 129 (P.C.).

20 S.A. 1959, c. 61.

21 *Reference re: Orderly Payment of Debts Act, 1959 (Alta.)*, [1960] S.C.R. 571.

22 [1978] 1 S.C.R. 753.

eral power to enact legislation in relation to bankruptcy and insolvency should not deprive provinces from regulating property and civil rights. This recognizes that there may be some degree of overlap between federal and provincial legislation as long as the provincial legislation is concerned with rights in insolvency and does not purport to create an insolvency regime. The Supreme Court of Canada has also upheld provincial personal property security legislation that permits a trustee in bankruptcy to subordinate an unperfected security interest.[23]

Questions of constitutional law also come into play when valid provincial legislation comes into conflict with federal insolvency legislation. This issue has arisen most often in relation to priorities in insolvency. Provincial legislation confers a special proprietary right on certain classes of claimants, such as employees, a right that usually takes the form of a non-consensual security interest or deemed trust. The Supreme Court of Canada has held in a series of decisions that, to the extent that federal bankruptcy legislation mandates the affording of some other priority status to such claims, provisions conferring a special proprietary right on certain claimants are inoperative.[24]

C. THE SOURCES OF INSOLVENCY LAW

The framework for Canadian insolvency law is found in several statutes enacted by the Parliament of Canada. However, these statutes are not the only sources of insolvency law, and for a full picture it is necessary to understand the interplay between the federal insolvency statutes and the other sources of insolvency law.

1) The Common Law

Although most of the insolvency regimes are overwhelmingly legislative in character, there is one that has its origins primarily in the common law. Receivership law began as a mixture of contract law and equitable principle. Although there has been a significant overlay of provincial and federal legislation, the common law core of receivership law remains in place and defines many of the operative concepts

23 *Re Giffen*, [1998] 1 S.C.R. 91.

24 *Quebec (Deputy Minister of Revenue) v. Rainville*, [1980] 1 S.C.R. 35; *Deloitte, Haskins & Sells Ltd. v. Alberta (Workers' Compensation Board)*, [1985] 1 S.C.R. 785; *Husky Oil Operations Ltd. v. Canada (Minister of National Revenue)*, [1995] 3 S.C.R. 453.

and principles. It is impossible to understand the current state of the receivership law without having a detailed knowledge of these common law principles.

Even in insolvency regimes that are predominantly statutory in nature, such as the bankruptcy regime, there is a residue of common law principle that continues to operate. For example, a common law rule, referred to as the rule in *Ex parte James; Re Condon*,[25] confers upon a bankruptcy court the power to prevent the trustee from acting in a high-handed or unreasonable manner. As well, courts have used their inherent jurisdiction in order to fill gaps in the statutory rules.[26]

2) Statute Law

The following federal insolvency statutes create or regulate the various insolvency regimes:

- *Bankruptcy and Insolvency Act*;
- *Companies' Creditors Arrangement Act*
- *Winding-up and Restructuring Act* (*WURA*);
- *Farm Debt Mediation Act* (*FDMA*);
- *Canada Business Corporations Act* (Part IX, ss. 94–101); and
- *Canada Transportation Act* (sections 106–10);

By far, the largest and most encompassing of the federal insolvency statutes is the *BIA*. This statute governs the bankruptcy regime but also creates or governs several of the other non-bankruptcy insolvency regimes. The last three statutes in the list are more specialized. Part IX of the *Canada Business Corporations Act* contains provisions governing receiverships in relation to corporations that are incorporated under the federal Act. The *FDMA* applies only in respect of farmers. The provisions of the *Canada Transportation Act* apply only to insolvent railway companies.

Provincial statutes play a less central role. These statutes also set out rules governing receiverships in business corporation legislation and personal property security legislation. There are as well a number of provincial statutes that have an auxiliary or supplementary function in that they confer additional powers on an insolvency administrator.

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25 (1874), L.R. 9 Ch. App. 609. And see Chapter 4, Section E.

26 *Re Residential Warranty Co. of Canada Inc.* (2006), 25 C.B.R. (5th) 38 (Alta. C.A.). And see Chapter 11, Section D(1).

3) Subordinate Legislation

The *BIA* gives the Governor in Council the power to make General Rules.[27] The *Bankruptcy and Insolvency General Rules*[28] cover a broad range of procedural matters concerning applications before a bankruptcy court, as well as rules governing consumer proposals, rules governing mediations in bankruptcy proceedings, and an extensive code of ethics for trustees. Regulations promulgated under the *Farm Debt Mediation Act* also provide procedural rules respecting mediations.[29]

4) Superintendent's Directives and Forms

The *BIA* provides that the Superintendent of Bankruptcy may issue directives to facilitate the carrying out of the purposes and provisions of the Act.[30] Several important directives have been issued, such as the Surplus Income Directive, which is an essential component of the rules governing the distribution of post-bankruptcy income earned by the debtor. The Act also gives the Superintendent of Bankruptcy the power to prescribe forms of documents,[31] and a large number of forms have been prescribed pursuant to this power.

D. THE VARIOUS INSOLVENCY REGIMES

The various insolvency regimes will be discussed in depth in later chapters of this book. It is useful at the outset to outline the salient characteristics of the different regimes in order to identify their objectives and to highlight the means through which they attempt to achieve these objectives. There are nine[32] different insolvency regimes in Canada, namely:

- bankruptcy;
- restructuring under the *CCAA;*

27 *BIA*, above note 9, s. 209.
28 C.R.C., c. 368.
29 *Farm Debt Mediation Regulations*, S.O.R./98-168.
30 *BIA*, above note 9, s. 5(4)(c).
31 *Ibid*, s. 5(4)(e).
32 This treats court-appointed receivers and privately appointed receivers as a single insolvency regime. Although there are important differences between the two types of receiverships, many of the statutory provisions that govern receiverships apply to both kinds. Therefore, it is preferable to regard them as two variants within the same insolvency regime.

- restructuring under the *BIA*;
- receivership;
- consumer proposals;
- orderly payment of debts (OPD);
- mediation under the *FDMA*;
- liquidation or restructuring under the *WURA*; and
- railway insolvency

This book is primarily concerned with insolvency regimes of general application rather than those that pertain to particular regions or special types of debtors. For this reason, its focus will be primarily upon the first five of these insolvency regimes.

1) Bankruptcy

Bankruptcy law is the oldest insolvency regime. In Canada, it applies to both natural persons and artificial entities such as corporations. Bankruptcy proceedings may be initiated either by the debtor (voluntary bankruptcy) or by the creditors (involuntary bankruptcy). Bankruptcy utilizes a liquidation approach to the debtor's insolvency. Upon the occurrence of bankruptcy, the assets of the debtor vest in a trustee in bankruptcy. The trustee then sells or otherwise disposes of the assets and distributes their proceeds among the creditors who prove their claims in the bankruptcy. This distribution is made according to a specified scheme of distribution. In the case of a natural person, bankruptcy law also pursues a policy of debtor rehabilitation by the discharge of most pre-bankruptcy claims in order to give the debtor a fresh start. The statutory framework governing bankruptcy is set out in the *BIA*.

2) Restructuring under the *CCAA*

The *Companies' Creditors Arrangement Act* is one of two commercial restructuring regimes that are of general application. A reorganization or restructuring regime (the terms are used interchangeably) usually does not involve a liquidation of the debtor's assets. It is premised on the idea that the business may be more valuable as a going concern and that all parties may benefit if a forced liquidation can be avoided. An insolvent debtor initiates the proceedings by bringing an application before a court for a stay of proceedings. The debtor then attempts to negotiate a compromise or arrangement with its creditors. The plan is then placed before the creditors and voted on. If a specified majority accepts the plan and a court approves it, the plan will bind all the affected creditors. The *CCAA* is the restructuring regime under which most of

the largest financially distressed Canadian corporations have restructured. The *CCAA* applies only if the debtor is a corporation and if the total claims against the debtor exceed $5 million. It is characterized by a high degree of court involvement.

3) Restructuring under the *BIA*

Division 1 of Part III of the *BIA* was enacted in 1992. It establishes a second commercial restructuring regime of general application. Unlike the *CCAA*, it is not restricted to corporations but also applies to natural persons and to artificial entities other than corporations. Nor does its application depend upon the size of the indebtedness owed by the debtor. The debtor is given a specified period of time within which to devise a commercial proposal to place before the creditors for consideration. The commercial proposal provisions use a more rule-based approach than the *CCAA* in order to reduce the costs associated with multiple court applications. In spite of this basic difference in approach, the commercial proposal regime and the *CCAA* share many key features and elements, and case law decided in respect of one of the regimes is often applicable to the other. As with the *CCAA*, the debtor usually remains in control of the assets while the reorganization is being attempted.

4) Receiverships

A receivership involves the appointment of a receiver-manager who takes possession and control of the debtor's business. The receiver-manager may operate the business, but in most cases the ultimate goal is to liquidate the assets either as a going concern or through their break-up and sale. Unlike a bankruptcy, the debtor's assets do not vest in the receiver-manager. A receiver-manager may be appointed by a secured creditor pursuant to a contractual power in a security agreement or may be appointed by a court. Although the legal distinctions between these two types of appointments have been diminished by legislation, there remain many important differences. A complex mixture of common law and equitable principle and federal and provincial legislation governs receiverships.

5) Consumer Proposals

The consumer proposal provisions were added to the *BIA* in 1992 as Division II of Part III of the Act. They provide individuals with an al-

ternative to consumer bankruptcy. A consumer proposal may be made only by a natural person whose debts, excluding any debts secured by the person's principal residence, do not exceed $250,000. In order to make a consumer proposal, the debtor must obtain the assistance of an administrator who assists the debtor in preparing the proposal, investigates the consumer debtor's property and financial affairs, and provides counselling to the debtor. A meeting of creditors is not ordinarily required. The creditors may simply indicate their assent or dissent regarding the consumer proposal when they file their proof of claim.

6) Orderly Payment of Debts

Part X of the *BIA* sets out the orderly payment of debts procedure. These provisions were added in 1965 after the Supreme Court of Canada struck down similar provincial legislation as *ultra vires*. The OPD provides an inexpensive procedure under which a debtor can apply to a clerk of a court for a consolidation order. The consolidation order fixes the amounts to be paid into court by the debtor and the times of payment until the amounts owing to all creditors are paid in full. The OPD provisions are in force only in those provinces that accept it. Alberta, Saskatchewan, Nova Scotia, and Prince Edward Island have all elected to do so.

7) *Farm Debt Mediation Act*

The *Farm Debt Mediation Act* was enacted in 1998. It attempted to improve the efficiency of earlier federal legislation enacted in 1986, which it replaces. The proceedings are initiated when an insolvent farmer applies to an administrator for a review of his financial affairs and mediation for the purpose of facilitating an arrangement with creditors. The administrator assists the farmer in preparing a financial recovery plan. The administrator then appoints a professional mediator who will attempt to arrive at a mutually acceptable arrangement between the farmer and the creditors. No party is bound to the arrangement unless they consent to it.

8) *Winding-Up and Restructuring Act*

Federal winding-up legislation was originally the means through which insolvent corporations were liquidated. Its role was substantially undercut in 1919 upon the enactment of bankruptcy legislation that applied to both natural persons and to artificial entities such as corporations. The *Winding-Up and Restructuring Act* is the only insolvency regime that can

be used in connection with the insolvency of banks, insurance companies, trust companies, and loan companies. Proceedings under the *WURA* are characterized by a higher degree of court involvement; the court appoints a liquidator and supervises the liquidation of the debtor's assets. The *WURA* contains some brief and skeletal provisions for restructuring, as well as special provisions governing insolvencies of authorized foreign banks and the restructuring of insurance companies.

9) Railway Insolvency

Sections 106 to 110 of the *Canada Transportation Act* provide an insolvency regime in respect of insolvent railway companies. This is the only insolvency regime that can be invoked, since railway companies are excluded from the scope of the *BIA*, the *CCAA*, and the *WURA*. The provisions are very brief and do not contemplate liquidation of the debtor. The Act provides skeletal rules for the filing of a scheme of arrangement in the federal court.

E. THE CONCEPT OF INSOLVENCY

1) The Legal Significance of Insolvency

It is important from the outset to distinguish between the insolvency of a debtor and the initiation of an insolvency regime. Insolvency is a fact. It occurs when a debtor is unable to pay his or her creditors. The insolvency regimes provide a legal definition of insolvency in order to determine precisely when this state of affairs is considered to exist. The various insolvency regimes provide different legal responses to the fact of the debtor's insolvency. These insolvency regimes do not come into operation simply by the occurrence of insolvency. They must be initiated by some action or proceeding taken by the creditors or the debtor. Often the initiating party must make a choice between two or more insolvency regimes in order to pick the one that provides the most appropriate solution to the problem.

The concept of insolvency serves a number of different purposes. First, it has a gatekeeping role. The various insolvency regimes typically require that the debtor be insolvent before insolvency proceedings can be initiated.[33] The federal insolvency regimes that use insolvency as a precondition are enumerated below:

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33 The initiation of involuntary bankruptcy proceedings by creditors does not conform to this pattern. The creditors do not need to prove that the debtor is

- voluntary assignments in bankruptcy;[34]
- restructuring proceedings under the *CCAA*;[35]
- commercial proposals;[36]
- receiverships;[37]
- consumer proposals;[38]
- orderly payment of debts;[39]
- liquidation or restructuring under the *WURA*;[40]
- farm debt mediation;[41] and
- railway insolvencies.[42]

Second, the concept of insolvency is used in a number of provisions that give the trustee the right to impugn pre-bankruptcy transactions. In order to attack a pre-bankruptcy transaction as a fraudulent preference, the trustee must prove that the debtor was insolvent at the time of the transaction.[43] An insolvency requirement is also imposed where the trustee seeks to recover against the directors or shareholder of a corporation in respect of a dividend, redemption, or share purchase.[44]

Third, provincial law uses the concept of insolvency in fraudulent preference statutes as well as statutes that impose liability on directors for distributions to shareholders that were made at a time when the corporation was insolvent. These provincial statutes do not create insolvency regimes. However, a trustee in bankruptcy is able to use these provisions and therefore their operation is of great significance. Although the federal and provincial insolvency tests are roughly comparable, they are not identical.

Fourth, a court cannot grant an absolute discharge in bankruptcy if the debtor has continued to trade after becoming aware of being insolvent.[45]

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insolvent. It is sufficient if they prove an act of bankruptcy. However, the application must be dismissed on proof that the debtor is able to pay creditors.

34 *BIA*, above note 9, s. 49.

35 *Companies' Creditors Arrangements Act*, R.S.C. 1985, c. C-36, s. 2(1) "debtor company" [*CCAA*].

36 *BIA*, above note 9, s. 50.

37 *Ibid.*, ss. 243(1) & (2).

38 *Ibid.*, s. 66.1 "consumer debtor."

39 *Ibid.*, s. 217 "debtor."

40 *Winding-up and Restructuring Act*, R.S.C. 1985, c. W-11, s. 6(1)(a) [*WURA*].

41 *Farm Debt Mediation Act*, S.C. 1997, c. 21, s. 6 [*FDMA*].

42 *Canada Transportation Act*, S.C. 1996, c. 10, s. 106(1).

43 *BIA*, above note 9, s. 95(1).

44 *Ibid.*, s. 101.

45 *Ibid.*, s. 173(1)(c).

2) The Definition of Insolvent Person

The legal definition of insolvency in the *BIA* is contained in the definition of "insolvent person."[46] The definition contains the following tests of insolvency:

(*a*) [The debtor] is for any reason unable to meet obligations as they generally become due.

(*b*) [The debtor] has ceased paying his current obligations in the ordinary course of business as they generally become due.

(*c*) The aggregate of [the debtor's] property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all obligations, due and accruing due.

The three tests set out in the definition are alternatives. It is sufficient to show that any one of them is satisfied.[47]

The Canadian approach[48] differs slightly from that in two other common law countries, the United States and the United Kingdom, which provide two tests for insolvency rather than three. The first test, known as the cash flow test, examines if the debtor is able to pay debts as they fall due. The second test, known as the balance sheet test, determines if the debtor's liabilities exceed the debtor's assets. The first two tests in the Canadian formulation are essentially cash flow tests, while the third is a balance sheet test. However, there is an important difference between the two cash flow tests in that the first is forward-looking while the second is backward-looking.

3) The Cash Flow Tests

The first insolvency test requires proof of the debtor's inability to meet current obligations as they generally become due. This is a cash flow test that contains an element of futurity. It is not directly concerned with whether the debtor has not paid his or her current obligations in the past. The question is whether the debtor is able to pay. A debtor who is able but unwilling to pay does not satisfy this test of insolvency.[49] A

46 *Ibid.*, s. 2(1).

47 *Re Selmas-Cromie Ltd.* (1975), 21 C.B.R. (N.S.) 10 (B.C.S.C.).

48 The insolvency tests contained in the definition have remained substantially unchanged since the enactment of the first Canadian bankruptcy statute in 1919.

49 *Thorne Riddell v. Fleishman* (1983), 47 C.B.R. (N.S.) 233 (Ont. H.C.J.) [*Thorne Riddell*].

debtor is insolvent under this test even though there are no payments currently due if it is shown that the payments will become due in the immediate future and the debtor does not have the means to satisfy these obligations.[50] In order to determine the debtor's ability to pay, it is necessary to assess the assets available to the debtor to meet these obligations. A lack of liquid funds is not determinative. A debtor who has a line of credit or other credit facility that can be drawn on to satisfy the obligations is not insolvent under this test.[51] However, the assets that are to be considered do not include assets that are not normally liquidated in the ordinary course of business.[52]

The second cash flow test requires proof that the debtor has ceased paying current obligations in the ordinary course of business as they generally become due. This test looks to the past. It is not concerned with the debtor's inability to pay obligations in the immediate future. The question is whether the debtor has ceased to pay them. The second test is more limited than the first in that it applies only to a debtor who carries on a business.

Under either of these cash flow tests, it may be necessary to determine if a particular obligation qualifies as a current obligation. Long-term liabilities that are payable at some future date should not be considered.[53] Unliquidated claims or debts that are subject to a *bona fide* dispute should also be excluded. A debt may be presently due and payable, but the creditors may have agreed to defer payment to a later date. If this is the case, the debtor will not be insolvent under the cash flow tests.[54] The mere failure by a creditor to seek recovery by commencing a legal action or taking some other step is not enough to qualify as an agreement to defer payment.[55] In principle, the date specified in the contract should be used to determine the date that the debt is due and payable unless there is some express or implied agreement between the parties, or a course of conduct sufficient to ground an estoppel.[56]

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50 *King Petroleum Ltd., Re* (1978), 29 C.B.R. (N.S.) 76 (Ont. H.C.J.) [*King Petroleum*]; *Re Viteway Natural Foods Ltd.* (1986), 63 C.B.R. (N.S.) 157 (B.C.S.C.) [*Viteway*].

51 *Re Bel Air Electric Inc.* (1962), 3 C.B.R. (N.S.) 252 (Que. S.C.).

52 *Re Pacific Mobile Corp.* (1979), 32 C.B.R. (N.S.) 209 (Que. S.C.).

53 This is subject to what has been said concerning obligations that are payable in the immediate future in relation to the first insolvency test.

54 *Thorne Riddell*, above note 49.

55 *Viteway*, above note 50.

56 See *Southern Cross Interiors Pty Ltd. v. Deputy Commissioner of Taxation*, [2001] NSWSC 621.

4) The Balance Sheet Test

Under the balance sheet test, a debtor is insolvent if the assets of the debtor are insufficient to satisfy all liabilities of the debtor. In applying this insolvency test, it is necessary to decide what things constitute assets, and then appraise their value. It is also necessary to decide what things constitute liabilities, and then assess their amount. The assets that can be considered are those that belong to the debtor at the time that the insolvency test is conducted. They do not encompass assets that may be acquired in the future or an anticipated profit or increase in value of the assets that may occur sometime in the future.[57] Exempt assets must be included, even though these assets will not be available to satisfy the claims of creditors in insolvency or other enforcement proceedings.[58]

The balance sheet test contemplates two methods for the valuation of assets — the fair valuation of the assets, and the disposal of the assets at a fairly conducted sale under legal process. The valuation of assets set out on the debtor's balance sheet is the starting point, but the liquidation value of the assets must also be considered.[59] The values set out on the balance sheet reflect the historic cost of assets, rather than their current value. The valuation of assets on the balance sheet can be departed from if it is shown that some of the accounts receivable are unlikely to be collected or that certain of the assets have depreciated in value.[60]

There is some disagreement over which liabilities must be taken into account under the balance sheet test. The statutory language refers to "all obligations, due and accruing due." Some cases have held that this does not encompass all future liabilities but only "obligations currently payable or properly chargeable to the accounting period during which the test is being applied."[61] Other cases have held that all future obligations, including contingent liabilities, must be included.[62] In principle, the balance sheet test should include all future liabilities.

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57 *Re Consolidated Seed Exports Ltd.* (1986), 62 C.B.R. (N.S.) 156 (B.C.S.C.).

58 *Re Schroeder* (2000), 17 C.B.R. (4th) 135 (Man. Q.B.); *Re Derksen* (1995), 34 C.B.R. (3d) 252 (Man. Q.B.).

59 *King Petroleum*, above note 50.

60 *Touche Ross Ltd. v. Weldwood of Canada Sales Ltd.* (1983), 48 C.B.R. (N.S.) 83 (Ont. H.C.J.); *633746 Ontario Inc. (Trustee of) v. Salvati* (1990), 79 C.B.R. (N.S.) 72 (Ont. H.C.J.).

61 *Enterprise Capital Management Inc. v. Semi-Tech Corp.* (1999), 10 C.B.R. (4th) 133 (Ont. S.C.J.) [*Enterprise*]; *Re Oblats de Marie Immaculée du Manitoba* (2004), 1 C.B.R. (5th) 279 (Man. Q.B.).

62 *Re Stelco Inc.* (2004), 48 C.B.R. (4th) 299 (Ont. S.C.J.) [*Stelco*]; *Viteway*, above note 50; *Optical Recording Laboratories Inc. v. Digital Recording Corp.* (1990), 2 C.B.R. (3d) 64 (Ont. C.A.).

A failure to include these into the calculation unfairly prejudices long-term creditors. The insolvency test must be met before a payment or transfer of property can be impugned as a preference. A failure to include all liabilities would permit short-term creditors to be paid despite the fact that this will result in insufficient assets to satisfy the claims of long-term creditors. Courts that have refused to include all obligations have expressed a concern that this may result in too many businesses falling within the definition.[63] This concern is misplaced. The excess of liabilities over assets is not an act of bankruptcy, and therefore involuntary bankruptcy proceedings cannot be forced upon a debtor even if the debtor is insolvent under the balance sheet test.

The statutory language associated with the balance sheet test refers to obligations rather than debts. Contingent claims and unliquidated claims are therefore included.[64] The valuation of contingent claims poses a particular difficulty. The contingency may or may not arise, and the probability that it will can range from an almost complete certainty to a very remote possibility. Where the probability is at one of these extremes, the courts will simply include the full value of the high probability claim[65] and reduce to zero the value of the low-probability claim. Matters become less certain when the likelihood of occurrence is somewhere in between these two extremes.

Professor Goode identifies two approaches to valuation of contingent liabilities.[66] One approach is to determine if there is a probability that the claim will occur (i.e., a greater than 50 percent chance). If so, the full value of the claim is included; if not, the obligation is valued at zero. The alternative approach would be to value the claim at the percentage likelihood of its occurrence. Under this approach, a claim for $100 that has a 60 percent chance of occurring would be valued at $60. Courts have adopted the second valuation approach to deal with problems of valuation that arise in connection with the proof of contingent claims by claimants who wish to participate in the proceeds of bankruptcy liquidation. There is no reason why this approach should not also be applied in connection with the balance sheet test.[67]

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63 *Enterprise*, above note 61.

64 *Re Challmie* (1976), 22 C.B.R. (N.S.) 78 (B.C.S.C.).

65 *Ibid.* The contingent liability was a personal guarantee in respect of a company that was in financial difficulties. The court simply added the full value of this claim to the liabilities of the debtor.

66 R. Goode, *Principles of Corporate Insolvency Law*, 3d ed. (London: Sweet and Maxwell, 2005) at 117–18.

67 *Re Wiebe* (1995), 30 C.B.R. (3d) 109 (Ont. Ct. Gen. Div.). And see Chapter 9, Section A(8).

5) The Insolvency Tests in Restructuring Proceedings

In order for a company to attempt a restructuring under the *CCAA*, the company must be insolvent. The *CCAA* does not define the term and does not expressly incorporate the insolvency tests of the *BIA*. The *BIA* restructuring provisions apply to an "insolvent person," and this brings into play the insolvency tests embedded in that definition. This raises a number of important questions. Is the test of insolvency contained in the *CCAA* the same as that used in the *BIA*? If it is not, what formulation is to be used? And, in respect of restructurings under the *BIA*, are the insolvency tests applied in precisely the same manner to both liquidations and restructurings?

Justice Farley considered these questions in *Re Stelco*.[68] The case involved a looming insolvency crisis. The company had not failed to meet any of its current obligations, but it was anticipated that it would run out of funding in ten months. Justice Farley held that the insolvency test in the *CCAA* is distinct from that contained in the *BIA*. Although there is an element of futurity in the first of the cash flow tests in the *BIA*, this encompasses only debts that become payable in the immediate future. Justice Farley was of the opinion that this insolvency test was inappropriate when the issue involved restructuring proceedings. He observed that often debtors wait too long before initiating restructuring proceedings, and that to be successful the proceedings must be commenced before the death spiral of the company. For this reason, he held that a company is insolvent under the *CCAA* "if it is reasonably expected to run out of liquidity within reasonable proximity of time as compared with the time reasonably required to implement a restructuring."[69] As virtually all *CCAA* proceedings will take at least six months and complex ones will frequently exceed a year, the ten-month period fell within the normal range and the company was held to be insolvent.

Justice Farley also considered the matter on the basis that the *BIA* insolvency tests applied to the proceedings. He held that the first cash flow test in the *BIA* operates differently depending on the nature of the proceedings. In bankruptcy proceedings or proceedings to set aside a transfer of property as a preference, the conventional test with a short horizon is employed. But in restructuring proceedings, a much longer time horizon is used. This interpretation would equally apply to restructuring proceedings under the commercial proposal provisions of

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68 *Stelco*, above note 62.
69 *Ibid*. at para. 26.

the *BIA*, although the time frame would be limited to six months since that is the maximum length of those proceedings.

Although the judgment clearly seeks to enhance the effectiveness of restructuring proceedings, the reasoning is problematic in a number of respects. As a matter of statutory interpretation, the idea that the meaning of the *BIA* insolvency test changes depending on whether bankruptcy or restructuring proceedings are involved is difficult to accept. Additionally, the proposed insolvency test for restructurings requires a more speculative prediction about events in the future, and this introduces a higher degree of uncertainty in determining the eligibility requirements for commencing restructuring proceedings. A further difficulty is that the constitution gives the federal Parliament the power to legislate in respect of bankruptcy and insolvency. It is questionable whether Parliament has the jurisdiction to legislate where there is merely an anticipated insolvency that might never occur.

FURTHER READINGS

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TAB 26

COMMENTARIES

Ernst & Young Inc. v. Aquino: Attributing Fraudulent Intent to a Defrauded Corporation

1. Introduction

The transfer at undervalue provisions in the *Bankruptcy and Insolvency Act*[1] [BIA] are an amalgam of very old and very new approaches to an ancient problem.[2] The old parts are directly derived from the language of the *Statute of Elizabeth*[3] enacted in 1571 – also known as the *Fraudulent Conveyances Act*.[4] Section 96 of the BIA provides that a transfer at undervalue can be impugned by a trustee if it can be proven that the debtor intended to "defraud, defeat or delay a creditor."[5] Courts have employed the basic methodology of fraudulent conveyance law in applying this element of section 96, including the hunt for "badges of fraud"[6] that dates back to the celebrated decision of *Twyne's Case* in 1602.[7]

Given the heavy corpus of case law that has since accumulated in this branch of the law, it comes as a bit of a surprise to discover that lurking in the shadows for several decades was an untested argument rooted in the highest level of Canadian judicial authority that, if successful, would significantly limit the ability of creditors to attack fraudulent transactions. Ordinarily, the state of mind of a person who is the directing mind of the corporation and who acts

1. R.S.C. 1985, c. B-3.
2. See Roderick J. Wood, "Transfers at Undervalue: New Wine in Old Wineskins?" [2017] Ann. Rev. Insol. L. 1.
3. 13 Eliz., ch. 5 (U.K.).
4. See Dick Dunlop and Tamara M. Buckwold, *Debt Recovery in Alberta,* (Toronto: Carswell, 2012), p. 941.
5. *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 96(1)(a)(iii) and s. 96(1)(b)(ii)(B). This language is a direct descendent of the language in the *Statute of Elizabeth* that speaks of an intention to hinder, delay or defeat creditors and others.
6. See Dick Dunlop and Tamara M. Buckwold, *Debt Recovery in Alberta,* (Toronto: Carswell, 2012), pp. 1015-17 for a discussion of badges of fraud.
7. *Twyne's Case* (1601), 76 E.R. 809 (Star Chamber)). And see Emily Kadens, "New Light on *Twyne's Case*" (2020), 94 Am. Bankr. L.J. 1 for the legal history of the case as well as an explanation why the decision is frequently and incorrectly dated as 1601. Although the term "badges of fraud" is usually associated with *Twyne's Case*, the report actually refers to "signs and marks of fraud".

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within his or her scope of authority is attributed to the corporation itself. The Supreme Court of Canada in *Canadian Dredge & Dock Co v. The Queen*[8] limited this attribution of intention in criminal proceedings. The corporation is immunized from liability if the directing mind of the corporation acted totally in fraud of the corporation and the corporation did not benefit from these actions. This limitation was later extended to cover civil actions in fraud against the defrauded corporation.[9]

The question is whether one further extension is warranted. Should the corporate attribution principle be applied to reviewable transaction provisions such as those contained in the federal bankruptcy and insolvency statutes? This argument was raised and ultimately rejected in connection with section 96 of the BIA by the Ontario Court of Appeal in *Ernst & Young Inc. v. Aquino*.[10]

The case involved a corporate executive who siphoned funds from the corporation through a false invoicing scheme. These actions were in total fraud of the corporation and to its prejudice. They also harmed the corporation's creditors by reducing the capacity of the corporation to pay its creditors – and this gave rise to the section 96 challenge. A critical issue was whether the corporate attribution doctrine should be invoked when applying section 96 of the BIA. If so applied, the fraudulent intent of the directing mind of a corporation responsible for the fraud would not be attributed to the corporation. This would mean that the defrauded debtor corporation would not have the requisite intent to defraud, defeat or delay a creditor, and therefore any value received by recipients could not be recovered using section 96 of the BIA in those situations where the fraudulent intent of the debtor must be proven.

The Ontario Court of Appeal held that the corporate attribution doctrine is not applicable to section 96 of the BIA. In this comment, I will argue that the Court came to the correct conclusion but that the reasons provided do not adequately explain why this should be the case.

2. Facts

Bondfield Construction Company Limited (Bondfield) was a family-owned construction company that worked on large scale construction projects in Ontario. Its affiliate, Forma-Con, was in

8. *Canadian Dredge & Dock Co v. The Queen*, [1985] 1 S.C.R. 662 (S.C.C.).
9. *Deloitte & Touche v. Livent Inc. (Receiver of)*, 2017 SCC 63 (S.C.C.).
10. *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.).

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the concrete forming business. Both corporations were part of the Bondfield Group of Companies (Bondfield Group). The Bondfield Group was founded by Ralph Aquino and he was joined by his sons, John Aquino and Steven Aquino.

By 2018, the Bondfield Group was experiencing financial difficulties. Zurich Insurance Company Limited, Bondfield Groups' bonding company, engaged Ernst & Young Inc. to review the financial situation of the Bondfield Group. This precipitated the commencement of proceedings under the *Companies' Creditors Arrangement Act*[11] [CCAA] in respect of Bondfield on April 3, 2019, and the commencement of bankruptcy proceedings against Forma-Con on December 19, 2019.

The monitor and the trustee discovered that Bondfield and Forma-Con had paid tens of millions of dollars to John Aquino and to several purported suppliers under a false invoicing scheme. In fact, no value had been given by the recipients of these payments. None of the recipients were legitimate suppliers. None had given value to Bondfield or Forma-Con to justify the payments received. Payments were also made to John Aquino's holding company. Bondfield paid $21,807,693 and Forma-Con paid $11,366,890 in connection with these schemes during the five-year period preceding the commencement of insolvency proceedings within which transfers at undervalue to non-arm's length parties can be reviewed. The monitor and the trustee sought to impugn these transactions under section 96 of the BIA as transfers at undervalue.

3. The Transfer at Undervalue Provisions

The transfer at undervalue provisions in section 96 of the BIA are divided into two parts. Section 96(1)(a) covers transfers at undervalue to arm's length parties. It is subject to a one-year review period and it must be shown both that the debtor was insolvent at the time of the transfer or rendered insolvent by it and that the debtor intended to defraud, defeat or delay a creditor.

Section 96(1)(b) covers transfers at undervalue to parties who are not dealing at arm's length with the debtor. Two review periods are created. If the transfer at undervalue falls within a one-year review period, the transaction can be impugned. Neither proof of insolvency nor proof of intention to defraud, defeat or delay a creditor is needed. A longer period covers the four-year period

11. R.S.C. 1985, c. C-36.

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preceding the shorter period. To impugn a transfer at undervalue that falls within this period, it must be shown either that the debtor was insolvent at the time of the transfer or rendered insolvent by it or that the debtor intended to defraud, defeat or delay a creditor.

Section 4 of the BIA sets out the rules that are to be applied in determining if a dealing is at arm's length. Subsection 4(4) provides that it is a question of fact whether persons not related to one another were at a particular time dealing with each other at arm's length. Subsection 4(5) creates a rebuttable presumption that persons related to each other are deemed not to deal with each other at arm's length.

4. The Decision of the Application Judge

The application was heard by Justice Dietrich who concluded that the monitor and trustee had established that the payments were transfers at undervalue and that the monies paid by Bondfield and Forma-Con could be recovered by the monitor and the trustee.[12] The transfers were clearly at undervalue as tens of millions of dollars were paid to the recipients who gave no value.

The next step was to determine whether the dealing was at arm's length. Although the suppliers who participated in the false invoice scheme were not related to Bondfield or Forma-Con, they were found to be dealing not at arm's length. Their knowing participation in a false invoicing scheme indicated an absence of any of the generally accepted commercial incentives such as bargaining and negotiation with a view to maximizing a party's economic self-interest that are the hallmarks of arm's length dealing.[13] The payment to John Aquino's holding company was to a related party and therefore it was deemed to be a dealing not at arm's length. Accordingly, both matters fell to be determined through the application of section 96(1)(b) of the BIA.

One of the payments to John Aquino occurred within the one-year review period, and therefore nothing more was required in order to impugn it. All the other payments fell outside the shorter review period but within the longer review period. Because it could not be shown that Bondfield or Forma-Con were insolvent at the time of the transfers, it was necessary to prove that they acted with the intention to defraud, defeat or delay a creditor.

12. *Ernst & Young Inc. v. Aquino*, 2021 ONSC 527 (Ont. S.C.J.).
13. This approach was first developed by Justice Meyers in *National Telecommunications (Re)*, 2017 ONSC 1475.

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Justice Dietrich held that there were several badges of fraud present – the transfers were made in secret, in haste, to non-arm's length persons, and for no consideration.[14] These badges of fraud gave rise to a rebuttable presumption of the intention to defraud, defeat or delay creditors. The onus then shifted to the recipients to adduce evidence to show the absence of fraudulent intent. Justice Dietrich found that the recipients were unable to rebut this presumption of fraudulent intent.

Justice Dietrich next considered whether the fraudulent intent of John Aquino could be attributed to Bondfield and Forma-Con. Under the corporate attribution doctrine the intention of a corporation's "directing mind" can be imputed to the corporation. However, the corporate attribution doctrine does not apply where the directing mind acts totally in fraud of the corporation and the corporation does not benefit from it.[15] Justice Dietrich held that as a matter of statutory interpretation the corporate attribution doctrine should not be applied in connection with the operation of section 96, and that instead a large and liberal interpretation should be given to the legislative provisions in order to protect the creditors of the debtor.[16]

Justice Dietrich held that the suppliers who participated in the false invoice scheme were privy to the transaction and adjudged them to be jointly and severally liable.[17] This meant that every bogus supplier was liable in respect of all the impugned transactions, and not merely for the benefit received by that particular supplier.

14. *Ernst & Young Inc. v. Aquino*, 2021 ONSC 527 (Ont. S.C.J.), at para. 160. Justice Dietrich at para. 204 found that this fraudulent intent was directed towards a creditor.
15. *Canadian Dredge & Dock Co v. The Queen*, [1985] 1 S.C.R. 662 (S.C.C.), at para. 66. See also *Deloitte & Touche v. Livent Inc. (Receiver of)*, 2017 SCC 63 (S.C.C.), at para. 100.
16. *Ernst & Young Inc. v. Aquino*, 2021 ONSC 527 (Ont. S.C.J.), at paras. 227-9.
17. *Ernst & Young Inc. v. Aquino*, 2021 ONSC 527 (Ont. S.C.J.), at para. 241. Section 96(1) permits a court to grant an order for payment of the difference in value against "any other person who is privy to the transfer." Section 96(3) provides that a "**person who is privy** means a person who is not dealing at arm's length with a party to a transfer and, by reason of the transfer, directly or indirectly, receives a benefit or causes a benefit to be received by another person." In one instance, due to the limited role played by the recipient, the judgment was limited to the benefit received by that recipient. Although the matter is not discussed at length, it is likely that the decision to make transferees additionally liable for payments received by other transferees will depend on the degree to which the transferees acted in concert with one another in connection with the fraudulent scheme.

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5. The Decision of the Ontario Court of Appeal

The decision of Justice Dietrich was appealed to the Ontario Court of Appeal. There were two major grounds connected with the application of section 96 of the BIA. The first involved an attempt to undermine the application judge's factual findings concerning the intention to defraud creditors. Justice Lauwers reviewed the record and held that the application judge "mustered a phalanx of facts"[18] in support of the conclusion that "the interests of creditors were imperilled by the transfers because Bondfield and Forma-Con were already experiencing mounting financial difficulties"[19] and that John Aquino intended to defraud those creditors.[20]

The second ground was that the fraudulent intention of John Aquino should not be imputed to Bondfield and Forma-Con. I expect that the Court of Appeal's decision in *Aquino* will be remembered for establishing the proposition that the corporate attribution doctrine should not be used in connection with section 96 of the BIA. For this reason, my discussion will focus on this aspect of the decision.[21]

Justice Lauwers began with a discussion of the intersection between the common law and the BIA. The starting point was the statement of the Supreme Court of Canada that "Parliament is presumed to intend not to change the existing common law unless it does so clearly and unambiguously."[22] There are several

18. *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at para. 38.
19. *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at para. 45.
20. Some passages in the judgment might seem to suggest that the intention of the transferees was relevant to the outcome. See for example, *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at paras. 26 to 28 referring to the fraudulent intention of the "other participants" and the "associates" of John Aquino. However, as the Ontario Court of Appeal's subsequent discussion centres wholly on the intention of John Aquino as the directing mind of the debtor corporation, these references to the other participants should not be regarded as germane to the decision.
21. One other issue considered by the Court of Appeal was whether John Aquino was entitled to assert a right of set-off such that his liability for any s. 96 repayments would be reduced by the alleged amount of his shareholder's loan to Bondfield. The Court, in *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at para. 89 rejected this argument on the basis that s. 97(3) of the BIA preserves a right of set-off "except in so far as any claim for set-off or compensation is affected by the provisions of this Act respecting frauds or fraudulent preferences."
22. *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at para. 58, citing *Chandos Construction Ltd. v. Deloitte Restructuring Inc.*, 2020 SCC 25 (S.C.C.), at para. 29.

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important areas of bankruptcy law that involve the interplay between the common law and the legislative provisions. Justice Lauwers observed that: "The use of common law doctrine must respect the policy of the BIA. But these principles do not license a court to do whatever it likes; the common law doctrines impose their own discipline."[23]

The common law approach to corporate attribution was developed by courts in connection with criminal and civil law proceedings against corporations based on the actions of representative individuals. The issue addressed by the doctrine is when the intention of those individuals may be attributed to the corporation. The question addressed here was whether the doctrine should also be applied in connection with bankruptcy proceedings under section 96 of the BIA. Justice Lauwers extracted three principles from the authorities, namely: (1) courts are sensitive to the context when imputing intention; (2) the attribution exercise is grounded in public policy; and (3) the principles of attribution provide a sufficient basis but not a necessary basis for imputing intention, and a departure from these principles is possible when the rationale underlying the principles no longer holds.[24]

Justice Lauwers was of the view that the criminal and civil contexts where the corporate attribution doctrine has traditionally been applied are quite different from the bankruptcy context. In civil and criminal proceedings, it is necessary to show that the corporation received some benefit from the fraudulent acts of the directing mind. In the absence of a benefit there is no liability. Justice Lauwers thought that these considerations played out differently in bankruptcy proceedings:

> The application of these principles is not clear in the bankruptcy arena, where the policy currents flow rather differently. In particular, attributing the intent of a company's directing mind to the company itself can hardly be said to unjustly prejudice the company in the bankruptcy context, when the company is no longer anything more than a bundle of assets to be liquidated with the proceeds distributed to creditors. An approach that would favour the interests of fraudsters over those of creditors seems counterintuitive and should not be quickly adopted.[25]

The Ontario Court of Appeal therefore found that the application judge did not err in finding that for the purposes of section 96 of the BIA, the intention of the debtor corporation can include the

23. *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at para. 64.
24. *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at paras. 71-3.
25. *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at para. 77.

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intention of its directing mind even if the directing mind intended to defraud the corporation itself.

6. Discussion

The recipients of the payments in *Aquino* clearly deserved no sympathy – they gave no value and were participants in the false invoicing scheme. The Court of Appeal cast the underlying question in the following terms: "who should bear responsibility for the fraudulent acts of a company's directing mind that are done within the scope of his or her authority – the fraudsters or the creditors?"[26]

I do not think that this is the best way to frame the question as it misdirects the focus of analysis. It must be remembered that the transfer at undervalue provisions have the potential to cause serious inconvenience and loss to innocent parties. Indeed, the position of the innocent purchaser is the single most controversial element in the design of reviewable transactions legislation.[27]

Consider the case where a house is sold to an innocent buyer in an arm's length dealing for a price that is conspicuously less than its market value. If the debtor intended to defeat creditors and was insolvent at the time of the transfer, the trustee will be able to set aside the sale or require the buyer to pay the difference in value under section 96(1)(a) of the BIA. This holds true even though the buyer may have incurred considerable expense in moving into the house and may also not have the funds to pay the difference in value. Despite searching in the land registration system and finding nothing, the innocent buyer is placed in a precarious position. If fraud is involved it lies with the seller, but the buyer is the party who stands to lose to the seller's creditors. This is not a contest between fraudsters and creditors so an allocation of responsibility on the basis suggested by the Court is misconceived.[28]

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26. *Ernst & Young Inc. v. Aquino*, 2022 ONCA 202 (Ont. C.A.), at para. 78.
27. See Anthony Duggan and Thomas G.W. Telfer, "Gifts and Transfers at Undervalue" in S. Ben-Ishai & A. Duggan, eds., *Canadian Bankruptcy and Insolvency Law: Bill C-55, Statute c. 47 and Beyond* (Markham: LexisNexis Canada, 2007), pp. 195-8; Tamara M. Buckwold, "Reforming the Law of Fraudulent Conveyances and Fraudulent Preferences" (2012), 52 Can. Bus. L.J. 333, at pp. 344-7.
28. One should be careful to keep the requirements of common law fraud distinct from the requirements of fraudulent conveyances law. In *Abakhan & Associates Inc. v. Braydon Investments Ltd.*, 2009 BCCA 521 (B.C. C.A.), Finch C.J. states at para. 57: "[I]t is instructive to consider the substantial body of authority holding it unnecessary to establish *male fides* on the part of the transferor to commit

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The Court of Appeal said that the issue involved the interplay between the common law and the federal bankruptcy and insolvency provisions, and that the bankruptcy context differs from criminal and civil proceedings because there is no longer any prejudice to the debtor corporation. The corporation is in the process of liquidation and is therefore simply of bundle of assets to be distributed to its creditors.

This hits on a crucial point but does not quite connect. The important insight is that the corporate attribution principle is inappropriate in the context of section 96 of the BIA because the corporation is not prejudiced by a section 96 remedy. However, the lack of prejudice is not due to the liquidation of the debtor corporation. The reason that the debtor corporation suffers no prejudice is because the remedy is directed against the transferee who receives the property and not against the debtor corporation who transfers it. Moreover, this is not something that is peculiar to bankruptcy or insolvency proceedings – it holds true whenever reviewable transactions are impeached by creditors.

This point is easy to demonstrate. Suppose that the false invoicing scheme had been uncovered, but insolvency proceedings had not been commenced in respect of the debtor corporations. The creditors would be entitled to bring an action under provincial fraudulent conveyances law to impeach the payments and recover their value from the transferees. Because the transferees gave no consideration, the creditors would prevail if they could show that the debtor corporation intended to defraud, delay or hinder a creditor. The same issue of corporate attribution would therefore arise in this non-insolvency context – whether the intention of the directing mind could be attributed to the defrauded corporation.

The corporate attribution principle is applied in criminal and civil proceedings where liability is sought to be imposed on the corporation. As we have seen, this liability is curtailed when the directing mind is acting in total fraud of the corporation and to its prejudice. The Supreme Court of Canada in *Dredge* explains why this should be the case:

> It has been said by many authors that no social purpose is served by convicting a corporation whose directing mind has acted throughout in fraud of that corporation and its undertaking. Similarly, where the wrongful act is conceived and designed to benefit only the directing mind and without any benefit to the corporate employer, it has been said that

fraud. The focus in the case law has been on the provision of a civil remedy for creditors disadvantaged by the conduct of their debtors."

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no social purpose is served by convicting a corporation in such a circumstance.[29]

The reason why the corporate attribution principle is inappropriate in connection with both the transfer at undervalue provisions of the BIA and fraudulent conveyances law has to do with the highly distinctive nature of the rights at stake. The underlying goal is not to punish or deter the debtor or to award damages against the debtor, but rather to protect the interests of creditors. If successful, the action will result in the avoidance of the transaction or the granting of a judgment against the transferee. Although the creditors or their insolvency representatives must show that the debtor had the intention to defraud, defeat or delay creditors, it is the transferee rather than the debtor that suffers a loss if the transaction is impeached.[30] It is for this reason that the corporate attribution principle must be modified when applying it to the reviewable transactions remedies. The social purpose of the legislation is to protect creditors from actions of the debtor that diminish the assets that are available for recovery of the creditor's claims, and this social purpose is served whether or not the directing mind is acting in fraud of the corporation.

It will still be necessary to prove that the person who entered the transaction was the directing mind of the corporation and that this person intended to defraud, defeat or delay a creditor. However, it will be irrelevant whether the act was totally in fraud of the debtor corporation or if the debtor corporation received any benefit from it. These factors will be relevant if the debtor corporation is charged criminally or if fraud actions are brought against it. But the reviewable transactions remedies are aimed against the transferee rather than the debtor corporation, and the defences and protections afforded to transferees are to be found in the legislation itself and not from the application of the corporate attribution principle. The issue of attribution in this context is simply whether the person acting on behalf of the company was in

29. *Canadian Dredge & Dock Co v. The Queen*, [1985] 1 S.C.R. 662 (S.C.C.), at para. 52.

30. See John C. McCoid, II, "Constructively Fraudulent Conveyances: Transfers for Inadequate Consideration" (1983), 62 Tex. L. Rev. 639, at p. 658 who points out that "transferees, not debtors, bear the brunt of invalidation of fraudulent conveyances." And see Tamara M. Buckwold, "Reforming the Law of Fraudulent Conveyances and Fraudulent Preferences" (2012), 52 Can. Bus. L.J. 333, at p. 336 who states that "[t]he debtor is affected incidentally, if at all, when that person is at arm's length, since the debtor would have lost the assets transferred away to his or her creditors in any event had the transaction under challenge not occurred."

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fact in a position to exercise control with respect to the transaction in question.

One should also not be too quick to assume that recovery by the creditors will hinge entirely on the ability of the trustee or monitor to successfully invoke the transfer at undervalue provisions of the BIA. The defrauded corporation has an action under the applicable business corporations legislation against the wrong-doing director for breach of duty. Recipients will also be liable in the tort of deceit if they participated in the fraud. In bankruptcy proceedings, these rights of action vest in the trustee.[31] In receivership proceedings, the receiver can prosecute these actions on behalf of the debtor corporation.[32] And in proceedings under the CCAA,[33] the supervising judge can authorize the monitor to bring legal proceedings on behalf of the debtor corporation. Funds recovered for the corporation by these means will flow through to creditors.

We therefore should not think that the issue inevitably resolves itself into a contest between fraudsters and creditors, nor should we assume that the transfer at undervalue provisions are the only means for recovery by the creditors.

7. Conclusion

It should be obvious from all this that the trustee or monitor in insolvency proceedings must work through a complex matrix of potential actions. The transfer at undervalue provisions of the BIA do not preclude the insolvency professional from invoking provincial fraudulent conveyance law.[34] As well, the insolvency professional will need to consider whether it may be beneficial to commence ordinary corporate litigation against the directing mind for breach of fiduciary duty or common law actions for fraud. Fraud actions against transferees may also be available against transferees if they were parties to the fraud. The oppression remedy is another avenue that can be considered.[35]

These actions will be subject to different limitation periods or review periods and their substantive elements also will differ. It should also be kept in mind that fraudulent conveyance actions and common law actions for fraud are not coextensive.[36] Douglas

31. *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 71.
32. See, e.g., *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 95.
33. *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, s. 11.
34. See *Robinson v. Countrywide Factors Ltd.*, [1978] 1 S.C.R. 753 (S.C.C.).
35. See, e.g., *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 241.

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Baird points out that "[a] transaction could 'hinder, delay, or defraud' creditors even when there was no proof of the deceit that is essential to an action for common law fraud."[37]

The application of the corporate attribution principle to the transfer at undervalue provisions of the BIA would have introduced a further complexity to an already complicated situation as it would invite arguments on whether there was total or only partial fraud of the debtor corporation and whether there was some or no value to the debtor corporation. The decision of the Ontario Court of Appeal in *Aquino* has fortunately foreclosed this line of argument and has ensured that the policy of creditor protection in the BIA is not undermined.

Roderick J. Wood*

36. See *Abakhan & Associates Inc. v. Braydon Investments Ltd.*, 2009 BCCA 521 (B.C.C.A.).

37. Douglas G. Baird, "The Fraudulent Conveyance Origins of Chapter 11: An Essay on the Unwritten Law of Corporate Reorganizations" (2020), 36 Emory Bankr. Dev. J. 699 at p. 701. See also Robert Clark, "The Duties of the Corporate Debtor to Its Creditors" (1977), 90 Harv. L. Rev. 505.

* F.R. (Dick) Matthews, Q.C. Professor of Business Law, Faculty of Law, University of Alberta. I would like to thank Tamara Buckwold for her valuable comments and suggestions.

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TAB 27

9-10 GEORGE V.

CHAP. 36.

An Act respecting Bankruptcy.

[*Assented to 7th July, 1919.*]

HIS Majesty, by and with the advice and consent of the Senate and House of Commons of Canada, enacts as follows:—

SHORT TITLE.

1. This Act may be cited as *The Bankruptcy Act.* — Short title.

INTERPRETATION.

2. In this Act, unless the context otherwise requires or implies, the expression,— — Definitions.

(a) "affidavit" includes statutory declaration and affirmation; — "Affidavit."

(b) "alimentary debt" means a debt incurred for necessaries or maintenance; — "Alimentary debt."

(c) "appeal court" means the court having jurisdiction in bankruptcy, under this Act, on appeal; — "Appeal court."

(d) "assignment" includes conveyance; — "Assignment."

(e) "assignor" means the maker of an assignment, whether under this Act such maker may lawfully make such assignment or such assignment may lawfully be made, or not; — "Assignor."

(f) "authorized assignment" means an assignment made as provided in this Act to an authorized trustee by an authorized assignor of all his property for the general benefit of his creditors; — "Authorized assignment."

(g) "authorized assignor" means an insolvent assignor whose debts provable under this Act exceed five hundred dollars; — "Authorized assignor."

(h) "available act of bankruptcy" means an act of bankruptcy available for a bankruptcy petition at the date of the presentation of a petition on which a receiving order is made; — "Available act of bankruptcy."

"Property." (*dd*) "property" includes money, goods, things in action, land, and every description of property, whether real or personal, movable or immovable, legal or equitable, and whether situate in Canada or elsewhere; also obligations, easements and every description of estate, interest and profit, present or future, vested or contingent, in, arising out of, or incident to property as above defined;

"Registrar." (*ee*) "registrar" includes any other officer who performs duties like to those of a registrar;

"Resolution." (*ff*) "resolution" means ordinary resolution;

"Secured creditor." (*gg*) "secured creditor" means a person holding a mortgage, hypothec, pledge, charge, lien or privilege on or against the property of the debtor, or any part thereof, as security for a debt due or accruing due to him from the debtor;

"Sheriff." (*hh*) "sheriff" includes bailiff and any officer charged with the execution of a writ or other process;

"Special resolution." (*ii*) "special resolution" means a resolution decided by a majority in number of the creditors present, personally or by proxy, at a meeting of creditors and voting three-fourths in value of the proved debts on the resolution;

"Trustee." "Authorized trustee." (*jj*) "trustee" or "authorized trustee" means, dependent upon the context, (*a*) one of the persons appointed by the Governor in Council, under authority of this Act as proper persons to be trustees in bankruptcy or otherwise hereunder, or (*b*) one of such persons named in a receiving order or in an authorized assignment to act, or who is otherwise hereunder authorized to act, as a trustee in bankruptcy, or under an authorized assignment or in connection with a proposal by a debtor for a composition, extension or arrangement to or with his creditors;

"Wage-earner." (*kk*) "wage-earner" means one who works for wages, salary, commission or hire at a rate of compensation not exceeding fifteen hundred dollars per year, and who does not on his own account carry on business.

PART I.

Bankruptcy and Receiving Orders.

Acts of Bankruptcy.

Acts of bankruptcy. **3.** A debtor commits an act of bankruptcy in each of the following cases:—

Assignment. (*a*) If in Canada or elsewhere he makes an assignment of his property to a trustee or trustees for the benefit of his creditors generally, whether it is an assignment authorized by this Act or not;

(*b*) If in Canada or elsewhere he makes a fraudulent conveyance, gift, delivery, or transfer of his property, or of any part thereof; **Fraudulent conveyance.**

(*c*) If in Canada or elsewhere he makes any conveyance or transfer of his property or any part thereof, or creates any charge thereon, which would under this Act be void as a fraudulent preference if he were adjudged bankrupt; **Fraudulent preference.**

(*d*) If with intent to defeat or delay his creditors he does any of the following things, namely, departs out of Canada, or, being out of Canada, remains out of Canada, or departs from his dwelling house or otherwise absents himself, or begins to keep house; **Absconding.**

(*e*) If he permits any execution or other process issued against him under which any of his goods are seized, levied upon or taken in execution to remain unsatisfied until within four days from the time fixed by the sheriff for the sale thereof, or for fourteen days after such seizure, levy or taking in execution, or if the goods have been sold by the sheriff or the execution or other process has been held by him after written demand for payment without seizure, levy or taking in execution or satisfaction by payment for fourteen days, or if it is returned endorsed to the effect that the sheriff can find no goods whereon to levy or to seize or take; provided that where interpleader proceedings have been instituted in regard to the goods seized, the time elapsing between the date at which such proceedings were instituted and the date at which such proceedings are finally disposed of, settled or abandoned, shall not be taken into account in calculating any such period of fourteen days; **Execution unsatisfied, goods sold by sheriff or no goods to be found.** **Proviso.**

(*f*) If he exhibits to any meeting of his creditors any statement of his assets and liabilities which shows that he is insolvent, or presents or causes to be presented to any such meeting a written admission of his inability to pay his debts; **Exhibits statement showing insolvency.**

(*g*) If he assigns, removes, secretes or disposes of or attempts or is about to assign, remove, secrete or dispose of any of his goods with intent to defraud, defeat or delay his creditors or any of them; **Intent to defraud.**

(*h*) If he makes any bulk sale of his goods without complying with the provisions of any Bulk Sales Act applicable to such goods in force in the province within which he carries on business or within which such goods are at the time of such bulk sale. **Bulk sale.**

Petition and Receiving Order.

4. (1) Subject to the conditions hereinafter specified, if a debtor commits an act of bankruptcy a creditor may present to the court a bankruptcy petition. **Bankruptcy petition.**

of one or more different co-partnerships, the claims shall rank first upon the estate by which the debts they represent were contracted, and shall only rank upon the other or others after all the creditors of such other estate or estates have been paid in full.

Settlement and Preferences.

29. (1) Any settlement of property hereafter made, not being a settlement made before and in consideration of marriage, or made in favour of a purchaser or incumbrancer in good faith and for valuable consideration, or a settlement made on or for the wife or children of the settlor of property which has accrued to the settlor after marriage in right of his wife, shall, if the settlor becomes bankrupt or insolvent or makes an authorized assignment within one year after the date of the settlement, be void against the trustee in the bankruptcy or of the assignment and shall, if the settlor becomes bankrupt or insolvent or makes an assignment as aforesaid at any subsequent time within five years after the date of the settlement, be void against such trustee, unless the parties claiming under the settlement can prove that the settlor was, at the time of making the settlement, able to pay all his debts without the aid of the property comprised in the settlement, and that the interest of the settlor in such property passed to the trustee of such settlement on the execution thereof.

Avoidance of certain settlements.

(2) Any covenant or contract hereafter made by any person (hereinafter called "the settlor") in consideration of his or her marriage, either for the future payment of money for the benefit of the settlor's wife or husband or children, or for the future settlement on or for the settlor's wife or husband or children, of property, wherein the settlor had not at the date of the marriage any estate or interest, whether vested or contingent, in possession or remainder, and not being money or property in right of the settlor's wife or husband, shall, if the settlor is adjudged bankrupt or makes an authorized assignment as aforesaid, and the covenant or contract has not been executed at the date of the petition in bankruptcy or said assignment, be void against such trustee except so far as it enables the persons entitled under the covenant or contract to claim for dividend in the settlor's bankruptcy or assignment proceedings under or in respect of the covenant or contract, but any such claim to dividend shall be postponed until all claims of the other creditors for valuable consideration in money or money's worth have been satisfied.

Certain marriage contracts void as against trustee.

(3) Any payment of money hereafter made (not being payment of premiums on a policy of life insurance in favour of the husband, wife, child or children of the settlor) or

Payments and transfers void, subject to proof of certain facts.

or any transfer of property hereafter made by the settlor in pursuance of such a covenant or contract as aforesaid, shall be void against the trustee unless the person to whom the payment or transfer was made prove either,—

(*a*) that the payment or transfer was made more than six months before the date of the petition in bankruptcy or the date of the authorized assignment; or,

(*b*) that at the date of the payment or transfer the settlor was able to pay all his debts without the aid of the money so paid or the property so transferred; or,

(*c*) that the payment or transfer was made in pursuance of a covenant or contract to pay or transfer money or property expected to come to the settlor from or on the death of a particular person named in the covenant or contract and was made within three months after the money or property came into the possession or under the control of the settlor;

but, in the event of any such payment or transfer being declared void, the persons to whom it was made shall be entitled to claim for dividend under or in respect of the covenant or contract in like manner as if it had not been executed at the date of the said petition or assignment.

"Settlement" defined.

(4) "Settlement" shall, for the purpose of this section, include any conveyance or transfer of property.

Avoidance of general assignment of book debts.

30. (1) Where a person engaged in any trade or business makes an assignment to any other person of his existing or future book debts, or any class or part thereof, and is subsequently adjudicated bankrupt or makes an authorized assignment, the assignment of book debts shall be void against the trustee in the bankruptcy, or under the authorized assignment, as regards any book debts which have not been paid at the date of the petition in bankruptcy or of the authorized assignment, unless there has been compliance with the provisions of any statute which now is or at any time hereafter may be in force in the province wherein such person resides or is engaged in said trade or business as to registration, notice and publication of such assignments. Provided that nothing in this section shall have effect so as to render void any assignment of book debts, due at the date of the assignment from specified debtors, or of debts growing due under specified contracts, or any assignment of book debts included in a transfer of a business made *bona fide* and for value, or in any authorized assignment.

"Assignment" defined.

(2) For the purposes of this section "assignment" includes assignment by way of security and other charges on book debts.

Avoidance of preference in certain cases.

31. (1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred,

TAB 28

13 GEORGE VI.

CHAP. 7.

An Act respecting Bankruptcy.

[*Assented to 10th December, 1949.*]

HIS Majesty, by and with the advice and consent of the Senate and House of Commons of Canada, enacts as follows:—

1. This Act may be cited as the *Bankruptcy Act, 1949*. Short title.

*INTERPRETATION.

2. In this Act, Definitions.

(a) "affidavit" includes statutory declaration and affirmation; *(a)* "affidavit".

(b) "assignment" means an assignment filed with the official receiver; *(c)* "assignment".

(c) "bankrupt" means a person who has made an assignment or against whom a receiving order has been made or the legal status of such a person; *(i)* "bankrupt".

(d) "bankruptcy" means the state of being bankrupt or the fact of becoming bankrupt; *(j)* "bankruptcy".

(e) "claim provable in bankruptcy" or "provable claim" or "claim provable" includes any claim or liability provable in proceedings under this Act by a preferred, secured or unsecured creditor; *(q)* "claim provable in bankruptcy".

(f) "corporation" includes any company incorporated or authorized to carry on business by or under an Act of the Parliament of Canada or of any of the provinces of Canada, and any incorporated company, wheresoever incorporated, that has an office in or carries on business within Canada, but does not include building societies having a capital stock, nor incorporated banks, savings banks, insurance companies, trust companies, loan companies or railway companies; *(d)* "corporation".

* The definitions are arranged alphabetically. At the end of each is found the letter of the corresponding definition in the French version of this Act, the alphabetical order being necessarily different in the two languages.

(*a*) in respect of any act done or default made by him in the administration of the property of the bankrupt, and

(*b*) in relation to his conduct as trustee,

but any discharge may be revoked by the court on proof that it was obtained by fraud or by suppression or concealment of any material fact.

Security released.

(9) The discharge of a trustee under this section operates as a release of the security provided pursuant to subsection one of section eight.

Trustee on discharge remains *de facto* trustee.

(10) Notwithstanding his discharge, the trustee shall remain *de facto* the trustee of the estate for the performance of such duties as may be incidental to the full administration of the estate.

Appointment of trustee by court to complete administration.

(11) The court, upon being satisfied that there are assets which have not been realized or distributed, may, on the application of any interested person, appoint a trustee to complete the administration of the estate, and the trustee shall be governed by the provisions of the Act, in so far as they are applicable.

PART II.

Receiving Orders and Assignments.

Acts of Bankruptcy.

Acts of bankruptcy.

20. (1) A debtor commits an act of bankruptcy in each of the following cases:—

Assignment.

(*a*) if in Canada or elsewhere he makes an assignment of his property to a trustee for the benefit of his creditors generally, whether it is an assignment authorized by this Act or not;

Fraudulent conveyance.

(*b*) if in Canada or elsewhere he makes a fraudulent conveyance, gift, delivery, or transfer of his property or of any part thereof;

Fraudulent preference.

(*c*) if in Canada or elsewhere he makes any conveyance or transfer of his property or any part thereof, or creates any charge thereon, that would under this Act be void as a fraudulent preference;

Absconding.

(*d*) if with intent to defeat or delay his creditors he does any of the following things, namely, departs out of Canada, or, being out of Canada, remains out of Canada, or departs from his dwelling house or otherwise absents himself;

Execution unsatisfied, property sold by sheriff or no property to be found.

(*e*) if he permits any execution or other process issued against him under which any of his property is seized, levied upon or taken in execution to remain unsatisfied until within four days from the time fixed by the

sheriff for the sale thereof or for fourteen days after such seizure, levy or taking in execution, or if the property has been sold by the sheriff, or if the execution or other process has been held by him for fourteen days after written demand for payment without seizure, levy or taking in execution or satisfaction by payment, or if it is returned endorsed to the effect that the sheriff can find no property whereon to levy or to seize or take, but where interpleader proceedings have been instituted in regard to the property seized the time elapsing between the date at which such proceedings were instituted and the date at which such proceedings are finally disposed of, settled or abandoned shall not be taken into account in calculating any such period of fourteen days;

(f) if he exhibits to any meeting of his creditors any statement of his assets and liabilities that shows that he is insolvent, or presents or causes to be presented to any such meeting a written admission of his inability to pay his debts; **Exhibits statement showing insolvency.**

(g) if he assigns, removes, secretes or disposes of or attempts or is about to assign, remove, secrete or dispose of any of his property with intent to defraud, defeat or delay his creditors or any of them; **Fraudulent disposition of property**

(h) if he gives notice to any of his creditors that he has suspended or that he is about to suspend payment of his debts; **Notice of suspension of payment**

(i) if he defaults in any proposal made under this Act; **Default in proposal.**

(j) if he ceases to meet his liabilities generally as they become due. **Ceasing to meet liabilities.**

(2) Every assignment of his property other than an assignment pursuant to this Act, made by an insolvent debtor for the general benefit of his creditors, shall be null and void. **Unauthorized assignments are void.**

Petition for Receiving Order.

21. (1) Subject to this section one or more creditors may file in court a petition for a receiving order against a debtor if, and if it is alleged in the petition that, **Bankruptcy petition.**

(a) the debt or debts owing to the petitioning creditor or creditors amount to one thousand dollars; and **Conditions on which creditor may petition.**

(b) the debtor has committed an act of bankruptcy within six months next preceding the filing of the petition.

(2) Where the petitioning creditor is a secured creditor, he shall in his petition either state that he is willing to give up his security for the benefit of the creditors in the event of a receiving order being made against the debtor, or give an estimate of the value of his security, and in the latter **If petitioning creditor is a secured creditor**

case

Settlements and Preferences.

Avoidance of certain settlements.

60. (1) Any settlement of property, if the settlor becomes bankrupt within one year after the date of the settlement, is void against the trustee.

If bankrupt within five years

(2) Any settlement of property, if the settlor becomes bankrupt within five years after the date of the settlement, is void against the trustee if the trustee can prove that the settlor was, at the time of making the settlement, unable to pay all his debts without the aid of the property comprised in the settlement or that the interest of the settlor in the property did not pass on the execution thereof.

Non-application of section.

(3) This section shall not extend to any settlement made

(a) before and in consideration of marriage, or

(b) in favour of a purchaser or incumbrancer in good faith and for valuable consideration, or

(c) on or for the wife or children of the settlor of property which has accrued to the settlor after marriage in right of his wife.

Certain marriage contracts void as against trustee.

61. Any covenant or contract made by any person (hereinafter called "the settlor") in consideration of his or her marriage, either for the future payment of money for the benefit of the settlor's wife or husband or children, or for the future settlement on or for the settlor's wife or husband or children, of property wherein the settlor had not at the date of the marriage any estate or interest, whether vested or contingent, in possession or remainder, and not being money or property in right of the settlor's wife or husband, if the settlor becomes bankrupt and the covenant or contract has not been executed at the date of the bankruptcy, is void against the trustee except so far as it enables the persons entitled under the covenant or contract to claim for dividend in the settlor's bankruptcy proceedings under or in respect of the covenant or contract, but any such claim to dividend shall be postponed until all claims of the other creditors have been satisfied.

Payments and transfers void, subject to proof of certain facts.

62. (1) Any payment of money, not being payment of premiums on a policy of life insurance in favour of the husband, wife, child or children of the settlor, or any transfer of property made by the settlor in pursuance of a covenant or contract mentioned in section sixty-one, is void against the trustee unless the person to whom the payment or transfer was made proves.

(a) that the payment or transfer was made more than six months before the date of the bankruptcy; or

 (b)

(*b*) that at the date of the payment or transfer the settlor was able to pay all his debts without the aid of the money so paid or the property so transferred; or

(*c*) that the payment or transfer was made in pursuance of a covenant or contract to pay or transfer money or property expected to come to the settlor from or on the death of a particular person named in the covenant or contract and was made within three months after the money or property came into the possession or under the control of the settlor.

If declared void.

(2) Where any payment or transfer mentioned in subsection one is declared void, the persons to whom it was made shall be entitled to claim for dividend under or in respect of the covenant or contract in like manner as if it had not been executed at the date of the bankruptcy.

Avoidance of general assignment of book debts.

63. (1) Where a person engaged in any trade or business makes an assignment of his existing or future book debts or any class or part thereof and subsequently becomes bankrupt, the assignment of book debts is void against the trustee as regards any book debts that have not been paid at the date of the bankruptcy.

Foregoing provisions not to apply in some cases.

(2) This section does not apply to an assignment of book debts which is registered pursuant to any statute of any province providing for the registration thereof if the assignment is valid in accordance with the laws of the province.

Further cases where this section not to void assignments.

(3) Nothing in this section renders void any assignment of book debts due at the date of the assignment from specified debtors, or of debts growing due under specified contracts, or any assignment of book debts included in a transfer of a business made *bona fide* and for adequate valuable consideration.

"assignment" defined.

(4) For the purposes of this section, "assignment" includes assignment by way of security and other charges on book debts.

Avoidance of preference in certain cases.

64. (1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view of giving such creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering the same becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in the bankruptcy.

When view to prefer presumed *prima facie*.

(2) If any such conveyance, transfer, payment, obligation or judicial proceeding has the effect of giving any creditor a preference over other creditors, or over any one or more

of

of them, it shall be presumed *prima facie* to have been made, incurred, taken, paid or suffered with such view as aforesaid whether or not it was made voluntarily or under pressure and evidence of pressure shall not be receivable or avail to support such transaction.

"creditor" defined.

(3) For the purpose of this section, the expression "creditor" shall include a surety or guarantor for the debt due to such creditor.

Payments conveyances and contracts for adequate consideration, protected.

65. (1) Subject to the foregoing provisions of this Act with respect to the effect of bankruptcy on an execution, attachment or other process against property, and with respect to the avoidance of certain settlements and preferences, nothing in this Act shall invalidate, in the case of a bankruptcy

(a) any payment by the bankrupt to any of his creditors;

(b) any payment or delivery to the bankrupt;

(c) any conveyance or transfer by the bankrupt for adequate valuable consideration;

(d) any contract, dealing, or transaction by or with the bankrupt for adequate valuable consideration;

Provided that both the following conditions are complied with, namely:—

(i) That the payment, delivery, conveyance, assignment, transfer, contract, dealing, or transaction, as the case may be, is in good faith and takes place before the date of the bankruptcy; and

(ii) That the person, other than the debtor, to, by, or with whom the payment, delivery, conveyance, assignment, transfer, contract, dealing or transaction was made, executed or entered into, has not at the time of the payment, delivery, conveyance, assignment, transfer, contract, dealing or transaction, notice of any act of bankruptcy committed by the bankrupt.

"adequate valuable consideration" defined.

(2) The expression "adequate valuable consideration" in paragraph *(c)* of this section means a consideration of fair and reasonable money value with relation to that of the property conveyed, assigned or transferred, and in paragraph *(d)* hereof means a consideration of fair and reasonable money value with relation to the known or reasonably to be anticipated benefits of the contract, dealing or transaction.

Law of set-off to apply.

(3) The law of set-off applies to all claims made against the estate and also to all actions instituted by the trustee for the recovery of debts due to the bankrupt in the same manner and to the same extent as if the bankrupt were plaintiff or defendant, as the case may be, except in so far as any claim for set-off is affected by the provisions of this Act respecting frauds or fraudulent preferences.

66.

TAB 29

Dominion, or any public writ, deed or other document thereof, signed, sealed or executed after the passing of this Act, or any portion of any such document, should be on parchment, but the same being written or printed wholly or in part on paper, shall be as valid in all respects as if written or printed on parchment;—any law, usage or custom to the contrary notwithstanding;—but nothing herein contained shall be construed as declaring that it was necessary to the validity of any such document signed, sealed or executed before the passing of this Act, that such document or any part thereof should be on parchment.

CAP. XVI.

An Act respecting Insolvency.

[*Assented to 22nd June,* 1869.]

Preamble

WHEREAS it is expedient that the Acts respecting Bankruptcy and Insolvency in the several Provinces of Ontario, Quebec, New Brunswick and Nova Scotia, be amended and consolidated, and the Law on those subjects assimilated in the several Provinces of the Dominion: Therefore, Her Majesty, by and with the advice and consent of the Senate and House of Commons of Canada, enacts as follows:

Application of Act.

1. This Act shall apply to traders only.

OF VOLUNTARY ASSIGNMENTS.

Assignment to be made to Interim Assignee

2. Any debtor unable to meet his engagements, and desirous of making an assignment of his estate, and any debtor who is required to make an assignment, as hereinafter provided, shall make an assignment of his estate and effects to any official assignee resident within the county or place wherein the Insolvent has his domicile; or if there be no official assignee therein then to an official assignee in the county or place nearest to the domicile of the Insolvent wherein an official assignee has been appointed, and the official assignee to whom such assignment is made shall be known as the Interim Assignee; and forthwith upon the execution of the deed of assignment to him, a meeting of the creditors of the Insolvent for the appointment of an assignee, shall be called by the interim assignee to be held at the place of business of the Insolvent within a period not exceeding three weeks from the execution of the deed of assignment.

Meeting of creditors to be called.

Calling of meeting and proceedings thereat

3. Such meeting shall be called by advertisement (Form A), and previous to such meeting the interim assignee shall prepare, and shall then exhibit, statements showing the position of the affairs of the Insolvent, and particularly a schedule (Form B), containing the names and residence of all his creditors, and the amount

be in the Province of Quebec and the deeds of assignment and of transfer be executed elsewhere in the Dominion they may be enregistered at full length in the usual manner; but it shall not be necessary to enregister, or to refer on registration in any manner to, the list of creditors annexed to the deed of transfer.

COMPULSORY LIQUIDATION.

When a debtor's estate shall be subject to compulsory liquidation.

13.—A debtor shall be deemed insolvent and his estate shall become subject to compulsory liquidation:

a. If he absconds or is immediately about to abscond from any Province in Canada with intent to defraud any creditor, or to defeat or delay the remedy of any creditor, or to avoid being arrested or served with legal process; or if being out of any such Province in Canada he so remains with a like intent; or if he conceals himself within the limits of Canada with a like intent;

b. Or if he secretes or is immediately about to secrete any part of his estate and effects with intent to defraud his creditors, or to defeat or delay their demands or any of them;

c. Or if he assigns, removes or disposes of, or is about or attempts to assign, remove or dispose of, any of his property with intent to defraud, defeat or delay his creditors, or any of them;

d. Or if with such intent he has procured his money, goods, chattels, lands or property to be seized, levied on or taken under or by any process or execution, having operation where the debtor resides or has property, founded upon a demand in its nature proveable under this Act, and for a sum exceeding two hundred dollars, and if such process is in force and not discharged by payment or in any manner provided for by law;

e. Or if he has been actually imprisoned or upon the gaol limits for more than thirty days in a civil action founded on contract for the sum of two hundred dollars or upwards, and still is so imprisoned or on the limits; or if in case of such imprisonment he has escaped out of prison or from custody or from the limits;

f. Or if he wilfully neglects or refuses to appear on any rule or order requiring his appearance, to be examined as to his debts under any statute or law in that behalf;

g. Or if he wilfully refuses or neglects to obey or comply with any such rule or order made for payment of his debts or of any part of them;

h. Or if he wilfully neglects or refuses to obey or comply with the order or decree of the Court of Chancery or of any of the judges thereof, for payment of money;

i,

All contracts made with intent to impede or defraud creditors, with the knowledge of party contracting, to be void.

88. All contracts, or conveyances made and acts done by a debtor, respecting either real or personal estate, with intent fraudulently to impede, obstruct or delay his creditors in their remedies against him, or with intent to defraud his creditors, or any of them, and so made, done and intended with the knowledge of the person contracting or acting with the debtor, whether such person be his creditor or not, and which have the effect of impeding, obstructing, or delaying the creditors of their remedies, or of injuring them or any of them, are prohibited and are null and void, notwithstanding that such contracts, conveyances, or acts be in consideration, or in contemplation of marriage.

Fraudulent preferential sales, &c., to be void.

89. If any sale, deposit, pledge, or transfer be made of any property real or personal by any person in contemplation of insolvency, by way of security for payment to any creditor, or if any property real or personal, moveable or immoveable, goods, effects, or valuable security, be given by way of payment by such person to any creditor, whereby such creditor obtains or will obtain an unjust preference over the other creditors, such sale, deposit, pledge, transfer, or payment shall be null and void, and the subject thereof may be recovered back for the benefit of the estate by the Assignee, in any Court of competent jurisdiction; and if the same be made within thirty days next before the execution of a deed of assignment, or the issue of a Writ of Attachment under this Act, it shall be presumed to have been so made in contemplation of insolvency.

And presumed fraudulent, if made within a certain time before assignment, &c.

Payments made under certain circumstances by a debtor to be void.

90. Every payment made within thirty days next before the execution of a deed of assignment, or the issue of a Writ of Attachment under this Act, by a debtor unable to meet his engagements in full, to a person knowing such inability, or having probable cause for believing the same to exist, is void, and the amount paid may be recovered back by suit in any competent Court, for the benefit of the estate; Provided always that if any valuable security be given up in consideration of such payment, such security or the value thereof, shall be restored to the creditor before the return of such payment can be demanded.

Transfers of debts of insolvent within thirty days of his insolvency to his debtors to enable them to set-off, void.

91. Any transfer of a debt due by the Insolvent, made within thirty days next previous to the execution of a deed of assignment or the issue of a Writ of Attachment under this Act, or at any time afterwards, to a debtor knowing or having probable cause for believing the Insolvent to be unable to meet his engagements, or in contemplation of his insolvency, for the purpose of enabling the debtor to set up by way of compensation or set-off the debt so transferred, is null and void as regards the estate of the Insolvent; and the debt due to the estate of the Insolvent shall not be compensated or affected in any manner by a claim so acquired; but the purchaser thereof may rank on the estate in the place and stead of the original creditor.

TAB 30

embarked on board the ship, and the number to be landed in Canada; and no such entry made at any such time, shall be deemed validly made, or have any legal effect whatever, unless such numbers are correctly stated and such duty has been fully paid.

Proclamation to fix amount of duty, and when and where this Act shall or shall not be in force.

4. This Act shall take effect upon, from and after the day, and in the Province or Provinces, and for the amount of duty (within the limit aforesaid) specified by Proclamation in that behalf issued under an Order of the Governor General in Council, and not before; and the Governor General may, from time to time, by Proclamation issued under an Order in Council suspend the operation of this Act in any one or more or in all of the Provinces forming this Dominion; and from and after the period specified in any such suspending proclamation, this Act shall be suspended in such Province or Provinces; but nothing herein contained shall prevent or be construed to prevent the Governor General from again declaring by Proclamation issued under an Order in Council, that this Act shall again have effect in such Province or Provinces, or in any of such Provinces, and for the amount of duty (within the limit aforesaid) in such last mentioned proclamation specified; and upon such proclamation this Act shall be revived and have effect again accordingly; and so on, from time to time, *toties quoties*:—And every such proclamation shall be published in the *Canada Gazette.*

And so from time to time.

Proviso.

Publication.

CHAP. 16.

An Act respecting Insolvency.

[*Assented to 8th April*, 1875.]

Preamble.

HER MAJESTY, by and with the advice and consent of the Senate and House of Commons of Canada, enacts as follows:—

Application of Act.

1. This Act shall apply to traders and to trading copartnerships and to trading companies whether incorporated or not, except Incorporated Banks, Insurance, Railway, and Telegraph Companies.

Who are Traders, under this Act.

The following persons and partnerships or companies exercising like trades, callings or employments, shall be held to be traders within the meaning of this Act:—

Apothecaries, auctioneers, bankers, brokers, brickmakers, builders, carpenters, carriers, cattle or sheep salesmen, coach proprietors,

Collocated.

i. The word "collocated" shall mean ranked or placed in the dividend sheet for some dividend or sum of money :

Partnerships and companies.

j. In the case of any partnership or any company, incorporate or not, the word "he," "him," or "his" used in relation to any Insolvent or creditor, shall mean "the partnership" or "the company" or of "the partnership" or "of the company," (as the case may be) unless the context requires another interpretation to give such effect as the purposes of this Act require, to the provision in which the word occurs.

Acts of insolvency.

3. A debtor shall be deemed insolvent—

Acknowledging insolvency.

a. If he has called a meeting of his creditors for the purpose of compounding with them, or if he has exhibited a statement shewing his inability to meet his liabilities, or if he has otherwise acknowledged his insolvency ;

Absconding.

b. If he absconds or is immediately about to abscond from any Province in Canada with intent to defraud any creditor, or to defeat or delay the remedy of any creditor, or to avoid being arrested or served with legal process ; or if, being out of any such Province in Canada, he so remains with a like intent ; or if he conceals himself within the limits of Canada with a like intent ;

Secreting effects.

c. Or if he secretes or is immediately about to secrete any part of his estate and effects with intent to defraud his creditors, or to defeat or delay their demands or any of them ;

Fraudulently assigning.

d. Or if he assigns, removes or disposes of, or is about or attempts to assign, remove or dispose of any of his property with intent to defraud, defeat or delay his creditors or any of them ;

Conniving at seizure.

e. Or if with such intent he has procured his money, goods, chattels, lands or property to be seized, levied on or taken under or by any process or execution, having operation where the debtor resides or has property, founded upon a demand in its nature provable under this Act, and for a sum exceeding two hundred dollars, and if such process is in force and not discharged by payment or in any manner provided for by law ;

Being imprisoned.

f. Or if he has been actually imprisoned or upon the gaol limits for more than thirty days, in a civil action founded on contract for the sum of two hundred dollars or upwards, and still is so imprisoned or on the limits ; or if, in case of such imprisonment, he has escaped out of prison, or from custody, or from the limits ;

g.

be his creditor or not, within three months next preceding the date of a demand of an assignment or for the issue of a writ of attachment under this Act whenever such demand shall have been followed by an assignment or by the issue of such writ of attachment, or at any time afterwards, and all contracts by which creditors are injured, obstructed or delayed, made by a debtor unable to meet his engagements, and afterwards becoming an Insolvent, with a person knowing such inability or having probable cause for believing such inability to exist, or after such inability is public and notorious, whether such person be his creditor or not, are presumed to be made with intent to defraud his creditors.

Certain other contracts voidable.

131. A contract or conveyance for consideration, respecting either real or personal estate, by which creditors are injured or obstructed, made by a debtor unable to meet his engagements with a person ignorant of such inability, whether such person be his creditor or not, and before such inability has become public and notorious, but within thirty days next before a demand of an assignment or the issue of a writ of attachment under this Act, or at any time afterwards, whenever such demand shall have been followed by an assignment or by the issue of such writ of attachment, is voidable, and may be set aside by any court of competent jurisdiction, upon such terms as to the protection of such person from actual loss or liability by reason of such contract, as the court may order.

Contracts made with intent to defraud creditors to be void.

132. All contracts, or conveyances made and acts done by a debtor, respecting either real or personal estate, with intent fraudulently to impede, obstruct or delay his creditors in their remedies against him, or with intent to defraud his creditors, or any of them, and so made, done and intended with the knowledge of the person contracting or acting with the debtor, whether such person be his creditor or not, and which have the effect of impeding, obstructing, or delaying the creditors of their remedies, or of injuring them or any of them, are prohibited and are null and void, notwithstanding that such contracts, conveyances, or acts be in consideration, or in contemplation of marriage.

Fraudulent preferential sales, &c., to be void.

133. If any sale, deposit, pledge or transfer be made of any property real or personal by any person in contemplation of insolvency, by way of security for payment to any creditor; or if any property real or personal, movable or immovable, goods, effects, or valuable security, be given by way of payment by such person, to any creditor whereby such creditor obtains or will obtain an unjust preference over the other creditors, such sale, deposit, pledge, transfer or payment shall be null and void, and the subject thereof may be recovered back for the benefit of the estate by the Assignee, in

TAB 31

CHAP. 22.

An Act to further amend "The Patent Act of 1872."

[*Assented to 17th May*, 1882.]

Preamble.

HER Majesty, by and with the advice and consent of the Senate and House of Commons of Canada, enacts as follows:—

Sect. 28 of Patent Act, amended.

1. Section twenty-eight of "*The Patent Act of* 1872," is hereby amended by the addition of the following subsection:—

Further provision as to extension of patent.

"3. The Commissioner may grant to the patentee or his assignee or assignees for the whole or any part of the patent, an extension for a further period of time, not exceeding one year beyond the twelve months limited by the first paragraph of this section, during which he may import or cause to be imported into Canada the invention for which the patent is granted: Provided, that the patentee or his assignee or assignees for the whole or any part of the patent, shall show cause satisfactory to the Commissioner to warrant the granting of such extension; but no extension shall be granted, unless application be made to the Commissioner at some time within three months before the expiry of the twelve months aforesaid or any extension thereof."

Proviso: cause must be shewn.

Time for application limited.

CHAP. 23.

An Act respecting Insolvent Banks, Insurance Companies, Loan Companies, Building Societies, and Trading Corporations.

[*Assented to 17th May*, 1882.]

Preamble.

HER Majesty, by and with the advice and consent of the Senate and House of Commons of Canada, enacts as follows:—

APPLICATION OF ACT.

Application of Act.

1. This Act applies to incorporated Banks (including Savings Banks), incorporated Insurance Companies, Loan Companies having borrowing powers, Building Societies having a capital stock, which are insolvent or in process of being wound up either under a general or a special Act and which, on petition as in this Act set forth, by its shareholders or creditors, assignees or liquidators, ask to be brought within and under the provisions of this Act.

As to railways, &c.

(*a*). This Act does not apply to railway or telegraph companies, or to building societies that have not a capital stock.

2.

72. A contract or conveyance for consideration, respecting either real or personal estate, by which creditors are injured or obstructed, made by a company unable to meet its engagements with a person ignorant of such inability, whether such person be its creditor or not, and before such inability has become public and notorious, but within thirty days next before the commencement of the winding up of the business of such company under this Act, or at any time afterwards, is voidable, and may be set aside by any court of competent jurisdiction, upon such terms as to the protection of such person from actual loss or liability by reason of such contract, as the court may order.

When contracts with consideration shall be voidable.

73. All contracts, or conveyances made and acts done by a company respecting either real or personal estate, with intent fraudulently to impede, obstruct or delay its creditors in their remedies against it, or with intent to defraud its creditors or any of them, and so made, done and intended with the knowledge of the person contracting or acting with the company, whether such person be its creditor or not, and which have the effect of impeding, obstructing or delaying the creditors of their remedies, or of injuring them or any of them, are prohibited and are null and void.

As to contracts made in fraud or to obstruct or delay creditors.

74. If any sale, deposit, pledge or transfer be made of any property real or personal by a company in contemplation of insolvency under this Act, by way of security for payment to any creditor; or if any property, real or personal, movable or immovable, goods, effects or valuable security, be given by way of payment by such company to any creditor whereby such creditor obtains or will obtain an unjust preference over the other creditors, such sale, deposit, pledge, transfer or payment is null and void; and the subject thereof may be recovered back for the benefit of the estate by the liquidator, in any court of competent jurisdiction; and if the same be made within thirty days next before the commencement of the winding up under this Act, or at any time afterwards, it is presumed to have been so made in contemplation of insolvency.

Securities given by company for payment, when to be void.

75. Every payment made within thirty days next before the commencement of the winding up under this Act by a company unable to meet its engagements in full, to a person knowing such inability, or having probable cause for believing the same to exist, is void, and the amount paid may be recovered back by the liquidator by suit in any court of competent jurisdiction: Provided always, that if any valuable security be given up in consideration of such payment, such security or the value thereof must be restored to the creditor upon the return of such payment.

Payments by Co. when to be void.

Proviso.

TAB 32

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43 VICTORIA.

CHAP. I.

An Act to repeal the Acts respecting Insolvency now in force in Canada.

[*Assented to* 1st *April*, 1880.]

WHEREAS it is expedient to repeal the Acts hereinafter mentioned subject to the provision hereinafter made: Therefore Her Majesty, by and with the advice and consent of the Senate and House of Commons of Canada, enacts as follows:—

Preamble.

Acts 38 V., c. 16, 39 V., c. 30, 40 V., c. 16, repealed.

1. "*The Insolvent Act of* 1875," and the Acts amending it, passed in the thirty-ninth and fortieth years of Her Majesty's reign, and intituled, respectively: "*An Act to amend the Insolvent Act of* 1875," and "*An Act to amend the Insolvent Act of* 1875, *and the Act amending the same*," shall be and are hereby repealed, and no Act repealed by the said Acts, or either of them, shall be revived: Provided, that all proceedings under "*The Insolvent Act of* 1875," and the amending Acts aforesaid, in any case where the estate of an insolvent has been vested in an official assignee before the passing of this Act, may be continued and completed thereunder; and the provisions of the said Acts hereby repealed shall continue to apply to such proceedings, and to every insolvent affected thereby, and to his estate and effects, and to all assignees and official assignees appointed or acting in respect thereof in the same manner and with the same effect as if this Act had not been passed.

Proviso: Proceedings commenced under them to be completed.

TAB 33

13 Eliz., c. 5.

An Act against Fraudulent Deeds, Alienations, &c.

Fraudulent deeds made to avoid the debts of others shall be void, and the penalties of the parties to such fraudulent assurances.

FOR the avoiding and abolishing of feigned, covinous, and fraudulent feoffments, gifts, grants, alienations, conveyances, bonds, suits, judgments, and executions, as well of lands and tenements as of goods and chattels, more commonly used and practised in these days than hath been seen or heard of heretofore: Which feoffments, gifts, grants, alienations, conveyances, bonds, suits, judgments, and executions have been and are devised and contrived of malice, fraud, covin, collusion, or guile, to the end, purpose, and intent to delay, hinder, or defraud creditors and others of their just and lawful actions, suits, debts, accounts, damages, penalties, forfeitures, heriots, mortuaries, and reliefs, not only to the let or hindrance of the due course and execution of law and justice, but also to the overthrow of all true and plain dealing, bargaining, and chevisance between man and man, without the which no commonwealth or civil society can be maintained or continued:

All fraudulent conveyances made to avoid the debt or duty of others shall be void.

1. All and every feoffment, gift, grant, alienation, bargain, and conveyance of lands, tenements, hereditaments, goods and chattels, or of any of them, or of any lease, rent, common or other profit or charge out of the same lands, tenements, hereditaments, goods and chattels, or any of them, by writing or otherwise, and all and every bond, suit, judgment, and execution, at any time had or made sithence the beginning of the Queen's Majesty's reign that now is, or at any time hereafter to be had or made, to or for any intent or purpose before declared and expressed, shall be from henceforth deemed and taken (only as against that person or persons, his or their heirs, successors, executors, administrators, and assigns, and every of them, whose actions, suits, debts, accounts, damages, penalties, forfeitures, heriots, mortuaries, and reliefs, by such guileful, covinous, or fraudulent devices and practices as is aforesaid, are, shall, or might be in any ways disturbed, hindered, delayed, or defrauded) to be clearly and utterly void, frustrate, and of none

effect; any pretence, colour, feigned consideration, expressing of use, or any other matter or thing to the contrary notwithstanding.

13 *Eliz.*, c. 5.

The forfeiture of the parties to fraudulent deeds.

2. All and every the parties to such feigned, covinous, or fraudulent feoffment, gift, grant, alienation, bargain, conveyance, bonds, suits, judgments, executions, and other things before expressed, or being privy and knowing of the same, or any of them, which at any time . . . . . shall wittingly and willingly put in ure, avow, maintain, justify, or defend the same, or any of them, as true, simple, and done, had, or made *bonâ fide* and upon good consideration; or shall alien or assign any the lands, tenements, goods, leases, or other things before mentioned, to him or them conveyed as is aforesaid, or any part thereof; shall incur the penalty and forfeiture of one year's value of the said lands, tenements and hereditaments, leases, rents, commons, or other profits of or out of the same; and the whole value of the said goods and chattels; and also so much money as are or shall be contained in any such covinous and feigned bond; the one moiety whereof to be to the Queen's Majesty, her heirs and successors, and the other moiety to the party or parties grieved by such feigned and fraudulent feoffment, gift, grant, alienation, bargain, conveyance, bonds, suits, judgments, executions, leases, rents, commons, profits, charges, and other things aforesaid, to be recovered in any of the Queen's Courts of Record by action of debt, bill, plaint, or information, wherein none essoin, protection, or wager of law shall be admitted for the defendant or defendants; and also, being thereof lawfully convicted, shall suffer imprisonment for one half-year without bail or mainprize.

Who shall have the forfeiture, and by what means.

* * * * *

Estates made upon good consideration and *bonâ fide*.

5. Provided that this Act, or anything therein contained, shall not extend to any estate or interest in lands, tenements, hereditaments, leases, rents, commons, profits, goods, or chattels, had, made, conveyed, or assured, or hereafter to be had, made, conveyed, or assured, which estate or interest is or shall be upon good consideration and *bonâ fide* lawfully conveyed or assured to any person or persons, or bodies politic or corporate, not having, at the time of such conveyance or assurance to them made, any manner of notice or knowledge of such covin, fraud, or collusion as is aforesaid; anything before mentioned to the contrary hereof notwithstanding.

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