In the Privy Council.

ON APPEAL FROM THE SUPREME COURT OF CANADA.

BETWEEN THE MOLSONS BANK (PLAINTIFFS) - - APPELLANTS,

AND

COOPER & SMITH, JAMES COOPER AND JOHN C. SMITH (DEFENDANTS) - - RESPONDENTS.

Case

OF THE APPELLANTS.

This is an appeal brought by special leave of Her Majesty in Council given by an Order in Council dated 3rd August, 1897.

1. The appeal is from an order or certificate of the Supreme Court of Canada bearing date the 9th December, 1896, allowing, with costs, an appeal by the respondents from the order or certificate of the Court of Appeal for Ontario, bearing date the 14th January, 1896, which allowed the appeal of the bank, appellant, from the judgment of the Divisional Court composed of Falconbridge and Street, JJ., bearing date the 13th June, 1895, and reversing the judgment of Rose, J., the trial Judge, pronounced on the 19th April, 1895, in favor of the present appellant, the bank. Rec., p. 108. Rec., p. 76. Rec., p. 14. Rec., p. 8.

2. The action was brought by the bank in the High Court of Justice for the Province of Ontario, to recover from the respondents, who were a firm of manufacturers of boots and shoes, carrying on business at Toronto, and who are hereinafter, for convenience, called the firm, the amounts of four certain promissory notes made by the firm, payable to the bank, for the sums of $25,000.00, $10,000.00, $5,000.00 and $10,000.00 respectively.

3. There is no dispute of fact between the parties. The bank had been the firm's banker, and had made advances, from time to time, to the firm, by way of discount of the firm's promissory notes payable to the bank, hereinafter called the principal paper.

4. The agreement, under which such advances were made, is shown by a letter written by the bank's manager to the firm on the 13th June, 1891, as follows : " I am pleased to inform you that our Board have granted you a line
Rec., p. 8, l. 14. " of credit to $150,000.00, to be secured by collections deposited. Rate 6 per " cent. The meaning of the above is not that the advance shall be fully " covered by collections, but as near as you can."

5. As security for the principal paper, the firm, from time to time, in accordance with the agreement, deposited with the bank current promissory notes and acceptances of the firm's customers, received by the firm, from such customers, in the usual course of business, and hereinafter called the collateral paper, and this collateral paper was, from time to time, when deposited, entered in a book held by the bank, which was headed with a memorandum
Rec., p. 8, l. 14. signed by the firm as follows: " The notes enumerated in this book are " deposited with the Molsons Bank as collateral security for advances made " to us by the bank in discounts and overdrafts."

6. About the end of August, 1893, the firm, having become insolvent, suspended payment, being then indebted to the bank for advances to the amount of $145,000.00, represented by principal paper then current, of which the four promissory notes in question were a part, the bank then holding collateral paper to the amount of about $100,000.00.

7. After the suspension, and as the principal paper matured, the bank, from time to time, sued and recovered judgments against the firm upon it, to the amount of $90,000.00. These judgments, with the $50,000.00 in question in this action, and another principal note for $5,000.00 now in suit (awaiting the result of this action), make up the whole principal indebtedness of $145,000.00.

8. After the date of the firm's suspension, payments were, from time to time, made to the bank by the firm's customers upon the collateral paper held by the bank, and upon which such customers were primarily liable. The bank claimed to be entitled, under the agreement, to treat the payments so made as representing the collateral paper in respect of which they were made, and carried such payments to the credit of a suspense account, for the purpose, and with the intention, of applying the same towards satisfaction of any ultimate balance, which might remain due in respect of the principal paper, after resorting to and obtaining a dividend upon such principal paper out of the firm's general estate.

9. Under the provisions of the Creditors Relief Act, R.S.O., Cap. 65, priority in respect of any levy made by the Sheriff under execution, among creditors with executions in his hands, is abolished, and all execution creditors are required to share ratably in the proceeds of any such levy made upon the property of the common debtor. The right to so share is, however, confined

to creditors whose executions, or certificates, in the nature of executions, obtained under the summary procedure provided by the Act, reach the Sheriff's hands within a period limited by the Act. The Sheriff of Toronto, in October, 1893, made a levy upon certain property of the firm, under certain executions against the firm, then in his hands, including executions issued by the bank upon the judgments mentioned in the seventh paragraph of this case. The remainder of the principal notes held by the bank being then still current, the bank was not in a position to recover judgment, or share in such levy in respect thereof.

10. The firm, before distribution by the Sheriff of the proceeds of such levy, made an application at Chambers, to compel the bank to reduce the judgments, by virtue of which the bank was then ranking upon such proceeds, by applying thereupon the payments theretofore made to the bank by the firm's customers upon the collateral paper, and which the bank had carried to suspense account, some of which payments had been made before, and some after the recovery of such judgments, contending that the bank was bound to do this under the agreement, upon which the collateral paper was deposited. This application was resisted by the bank on the ground that, under the agreement the bank's legal right was to retain all the proceeds of the collateral paper in suspense, to be ultimately applied towards satisfaction of the balance remaining due, after receiving such dividends as might be recovered out of the firm's general estate, and the bank claimed to be entitled to rank upon the proceeds of the Sheriff's levy, which was part of such general estate, for the full amount of the then existing executions, representing the matured portion of the principal paper.

11. The application was refused by the Master in Chambers, whose decision was affirmed, on appeal, by Mr. Justice MacMahon, both being of opinion that the bank's contention was well founded and must prevail. Upon a further appeal by the firm to a Divisional Court, an issue was directed "to "try the rights and liabilities of the plaintiffs, the Molsons Bank, with regard "to the moneys collected by them upon their collateral securities, and to "determine the manner in which they should be applied under the circum-"stances," Mr. Justice Street, who delivered the judgment of the Court, saying that "the contention of the plaintiffs that, as a matter of law, they are "entitled to hold the money which they have collected, and which they may "collect upon their collaterals as a security for the ultimate balance, which "may be found due to them after all other sources of repayment have been "realized, is one which cannot be said to be by any means beyond dispute." When this direction was given by the Divisional Court on 29th December, 1893, all the principal paper had matured. Rec., p. 15, l. 36. Rec., p. 15, l. 26.

12. The issue so directed was tried by Mr. Justice Rose, who, upon the 20th April, 1894, delivered judgment upon it, upholding the contention of the Rec., p. 22. Rec., p. 45.

bank as to the construction of, and its rights under, the agreement, and his judgment not having been appealed from, was subsequently adopted by the Divisional Court, which had sent the issue for trial, as its judgment upon the
Rec., p. 48. appeal to it from Chambers. There has never been any appeal from this adjudication, and it still remains valid and binding upon the parties to it. Under it the bank was admitted to rank upon the proceeds of the Sheriff's levy for the full amount of the judgments then existing.

13. The Sheriff being subsequently about to make another levy upon other property of the firm, this action was brought to have the residue of the principal paper also turned into judgment, so that the bank might rank for such residue also upon the proceeds of the new levy. The firm thereupon set up
Rec., p. 3. by way of defence the same contention, which had been formerly made, viz., that the bank was, under the agreement, bound to apply upon the principal
Rec., p. 4, l. 47. paper the proceeds of the collateral paper. By way of counterclaim, the firm also asked to have an account taken upon the footing of the defence.

Rec., p. 5. 14. The action came on for trial before Mr. Justice Rose on 18th April, 1895, when, on behalf of the bank, the same contention was made as formerly, with regard to the bank's rights under the agreement, and the further contention that the adjudication upon the trial of the issue was decisive of the question raised by the defence and counterclaim, by way of estoppel or as *res*
Rec., p. 7, l. 17. *judicata*. Mr. Justice Rose determined both points in the bank's favor, and
Rec., p. 8, l. 36. directed judgment for the amount of the principal notes sued on.

15. From this judgment the firm appealed to a Divisional Court, composed
Rec., p. 9. of Falconbridge and Street, JJ. Mr. Justice Street delivered the judgment
Rec., p. 10, l. 45. of the Court, on the 13th June, 1895, which was against the bank on both points, holding that the former adjudication constituted no estoppel; that under the agreement the firm was entitled to have the proceeds of the collateral paper applied in payment of the principal paper; that the course taken by the bank in the former proceedings operated as an election to apply the proceeds of the collateral paper upon that portion of the principal paper not then due but now sued for; that being so applied they were sufficient to wipe out such portion, and that the action should therefore be dismissed.

16. From this judgment the bank appealed to the Court of Appeal for
Rec., p. 61. Ontario. The judgment of that Court was delivered on the 14th January, 1896. Hagarty, C.J., agreeing with the decision of Rose, J. upon the issue, was of opinion that, upon the proper construction of the agreement between the parties, the bank was entitled to treat the proceeds of the collateral paper in the way contended for on the bank's behalf. He was also of opinion that the construction placed upon the agreement, and the determination of the bank's rights under it by Rose, J., upon the trial of the issue, unappealed from and unchallenged, were conclusive upon the parties in the present suit.
Rec., p. 64. Burton, J. was of opinion that, so long as there was any part of the debtors' general estate in which the bank desired to share, the agreement entitled

the bank to so share, in respect of the whole principal indebtedness then matured, before making any application of the proceeds of the collateral paper. Osler, J. was of opinion that the adjudication upon the issue was a final and conclusive adjudication upon the cardinal matter then in dispute, which was as to the terms of the agreement upon which the bank held the collateral paper and its proceeds; that the cardinal matter in dispute in this action was the same, though it concerned another portion of the principal indebtedness: that the bank's rights in respect of the whole of the principal paper and the whole of the collateral paper depended upon the one agreement, and that, by the judgment upon the issue, the firm was estopped from denying either that the agreement was what the judgment on the issue had held it to be, or that it applied to all the collateral paper, and that the bank was therefore entitled to have the trial judgment restored, and to rank for the face of it upon the proceeds of the new levy by the Sheriff. Maclennan, J., dissenting, was of opinion that the judgment of Rose, J, upon the trial of the issue was not conclusive in this action, and that, though the bank had the right to withhold in suspense the proceeds of the collaterals during the currency of any portion of the principal paper, yet immediately upon the whole of such principal paper maturing, the bank was bound to apply such proceeds in discharge of some portion of the principal paper.

Rec., p. 66.

Rec., p. 70.

17. From this judgment the firm appealed to the Supreme Court of Canada. The judgment of that Court was delivered by Sir Henry Strong, C.J., on 9th December, 1896. His opinion was that the bank could not rely upon the former adjudication as an estoppel because it had not been pleaded. This objection had not been taken at the trial, nor in the Divisional Court, nor is it referred to in any of the judgments in the Court of Appeal. No doubt an amendment, if necessary, would have been permitted in any of these Courts, had the objection been insisted upon. But he was also of opinion that, if it had been pleaded, it could not have availed the bank. His opinion was, further, that the bank was bound, from time to time, as the same were received, to apply the proceeds of the collateral paper in reduction of the principal paper, and that, upon the counterclaim, the firm was entitled to have a judgment directing an account to be taken upon this footing, and to have the bank restricted to judgment and proof upon the new levy, in the whole, for such balance only of the principal paper, whether in judgment or not, as might appear to remain due after taking such account. The result of the judgment is that, instead of being permitted to rank upon such levy for the whole principal indebtedness of $145,000.00, as it was determined by the Court of Appeal the bank had the right to do, the bank will only be permitted to rank for about $60,000.00, being the difference between the principal paper and the proceeds of the collaterals. It is from this judgment that the bank has been given leave to appeal.

Rec., p. 97.

Rec., p. 100, l. 25

Rec., p. 100, l. 35.

Rec. p. 108.

18. It is submitted that the judgment appealed from is erroneous and ought to be reversed, and the judgment of the Court of Appeal for Ontario restored for the following among other

REASONS:

1. The bank had the right unless and until the debtors are prepared to pay the debt, and subject to the restriction that no more than 20s. in the £ can be recovered from all sources, to resort to the general estate of the debtors for a dividend upon the whole of the matured principal debt, without bringing into account collateral securities held on account of such principal debt, or the proceeds of such collateral securities. To hold otherwise is to deny the bank the very right which the deposit of the collateral securities was intended to give.

2. The judgment appealed from concedes this right so long as the collateral securities remain unmatured or dormant, but denies it when they have ripened by realization in ordinary course. It is submitted that no such distinction can be satisfactorily maintained. The securities remain none the less collateral because they are turned into money, so long as the principal debt is still unpaid, and so long as the proceeds of the collateral securities, if applied on the principal debt, are insufficient to satisfy it. Otherwise, collaterals maturing only at long dates and after the debtor's general estate has been distributed are *ceteris paribus*, more valuable to the creditor than collaterals maturing at short dates and before such distribution.

3. This is not a question of allowing or not allowing in account with the debtor, interest upon the proceeds of collateral securities, while charging interest upon the principal debt. Such a question can only arise when determining whether or not the creditor has been paid in full, or what sum presently paid to him will satisfy the balance of the debt. No such question arises here.

4. The Creditors' Relief Act, R.S.O. Cap. 65, is the complement of the Act respecting Assignments, R.S.O. Cap. 124. The latter provides for the voluntary liquidation of insolvent estates and the former for their compulsory liquidation. The latter provides methods of proof for ranking upon estates voluntarily assigned for liquidation to a Sheriff or other assignee. The former provides methods of proof for ranking upon estates in course of compulsory liquidation by a Sheriff under a writ or writs of execution. In both cases preference and priority in ranking are abolished. The main differences, so far as the present appeal is concerned, are :

   (1) A creditor in a voluntary liquidation under Cap. 124 may prove by affidavit, while a creditor in a liquidation under Cap. 65 may only prove by execution or by a certificate in the nature of an execution obtained under the Summary Procedure provided by the Act.

(2) A creditor may under Cap. 124 prove unmatured as well as matured claims, while a creditor who is proving under Cap. 65, inasmuch as he must recover a judgment or its equivalent, to found an execution or certificate, may only prove matured claims.

(3) A creditor in a liquidation under Cap. 124 is expressly required to value his securities, while no such requirement is made of a creditor seeking to prove in a liquidation under Cap. 65.

10 5. In making proof in bankruptcy it has always been held, in the absence of legislation to the contrary, that a creditor holding security upon two estates has the right to prove for and obtain dividends upon his whole debt out of both till he is paid in full.

6. The judgment of Rose, J. upon the trial of the issue directed by the Divisional Court, adopted by that Court and unappealed from, was a final adjudication *inter partes* in favor of the right asserted by the bank under the agreement. That judgment was concerned with the same agreement, the same debt, and the same collateral securities, and was between the same parties.

20 7. The point taken in the judgment appealed from, that this estoppel was not pleaded, was not at that stage open to the respondents. They went down to trial knowing what the questions to be raised were, permitted the estoppel to be raised and argued it, both without objection, and appealed from the judgment to the Divisional Court without raising or even suggesting the point, and do not anywhere pretend to have been taken by surprise.

GEO. F. SHEPLEY,
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BETWEEN

THE MOLSONS BANK - - - (*Plaintiffs*) APPELLANTS,

AND

COOPER & SMITH, JAMES COOPER, AND JOHN C. SMITH - (*Defendants*) RESPONDENTS.

Case

OF THE APPELLANTS.

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