Privy Council Appeal No. 1 *of* 1930.

The Bank of Montreal - - - - - - - *Appellants*

v.

The Dominion Gresham Guarantee and Casualty Company - *Respondents*

FROM

THE SUPREME COURT OF CANADA.

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 17TH JULY, 1930.

Present at the Hearing:
THE LORD CHANCELLOR.
LORD BLANESBURGH.
LORD DARLING.
LORD TOMLIN.
LORD RUSSELL OF KILLOWEN.

[*Delivered by* LORD TOMLIN.]

This is an appeal from a judgment dated the 27th May, 1929, of the Supreme Court of Canada, whereby the Court by a majority reversed a judgment of the Court of King's Bench in appeal and directed judgment for 7,565.61 dollars and costs in all Courts to be entered in favour of the present respondents against the present appellants.

The action arises out of frauds committed by one K. V. Rogers while employed as chief accountant by Willis Faber & Company of Canada, Ltd., who will be hereafter referred to as the customers.

Rogers had entered the customers' service in 1907 and became their chief accountant in 1912. The fidelity of Rogers was insured by the customers with the respondents for one year from the 23rd May, 1921. During that year frauds were committed by Rogers and the customers recovered under their policy from the respondents 7,565.61 dollars in respect thereof.

Thereupon the respondents, being admittedly subrogated to the rights of the customers, began the action of which this appeal before their Lordships' Board is the final stage to recover from the appellants, who were the customers' bankers, the amount paid by the respondents to the customers under the policy on the ground that the frauds of Rogers were the outcome of the appellants' negligence.

The customers carried on business as insurance brokers. In the ordinary course of their business the customers had occasion from time to time, in order to discharge obligations to creditors in New York, to purchase from the appellants, bank drafts on New York.

On the 8th July, 1912, the Board of Directors of the customers passed a resolution in the following terms :—

> " That any two of the following persons, namely, Mr. Raymond Willis, President, Mr. O. W. Dettmers, Director, Mr. E. N. Mercer, Director, and K. V. Rogers, Accountant, be and they are hereby authorized to make, draw, sign, accept or endorse bills of exchange, promissory notes, cheques, orders for payment or other commercial paper on behalf of the Company, and that Mr. Raymond Willis, President, and Mr. O. W. Dettmers, Director, and Mr. E. N. Mercer, Director, and either of them singly, be and they are hereby authorized to make all contracts and engagements other than the foregoing for and on behalf of the Company."

This resolution upon being passed was communicated to the appellants and remained operative throughout the period of the transactions to which the present appeal relates.

Between November, 1918, and January, 1922, a series of bank drafts on New York were purchased by the customers from the appellants.

The course of business when a bank draft was required to pay a creditor was as follows : The customers, usually through Rogers, first ascertained from the appellants on the telephone the current rate of exchange. Rogers then prepared a cheque payable to the appellants' order but never to his own order for a sum approximately corresponding in amount (after allowing for difference in exchange) to the sum for which the bank draft was required. The cheque so prepared was placed by Rogers before one of the directors, Mr. Dettmers or Mr. Mercer, for their signature, either with a statement in writing prepared in the office of the customers, purporting to show the amount due to the creditor, or with an oral explanation by Rogers of the purpose for which the cheque and corresponding draft were required. The cheque was then signed on behalf of the customers by two of the persons named in the resolution of the 8th July, 1912. In fact, Rogers was one of the signatories to almost all the cheques used in connection with the purchase of drafts.

When the cheque had been signed Rogers took it, without any other document or written instructions, to the appellants' bank. At the bank Rogers first handed in the cheque for certification, and having received it back certified, went to the draft department of the bank and filled in upon one of the appellants'

forms a requisition note indicating (1) that a draft on New York was required, (2) the amount of the draft, (3) the name of the person in whose favour the draft was to be made out, and (4) the name of the applicant for the draft.

In every case Rogers inserted the name of the customers as applicants for the draft.

Having filled in the requisition note, the note and certified cheque were handed by Rogers to the appellants' clerk, whose duty it was to issue drafts, and the draft was thereupon handed out to Rogers, any slight difference due to the rate of exchange between the amount of the cheque and the amount actually required for the purchase of the draft being adjusted by Rogers by the payment or receipt of cash.

Between November, 1918, and January, 1922, 106 drafts were purchased in the manner which has been described. Of these purchases, 50 were made during the currency of the policy.

After January, 1922, it was for the first time discovered that Rogers had on 41 purchases out of the 106, by inserting in the requisition notes his own name as that of the person in whose favour the drafts were to be prepared, obtained from the appellants drafts in his own favour and had misappropriated to his own use the proceeds of the drafts, covering his defalcations by falsifying the customers' books.

Of the 41 misappropriations, 20 occurred before the policy was issued. The remaining 21 occurred during the currency of and were covered by the policy, and constitute the matters in respect of which the 7,565.61 dollars were recovered by the customers from the respondents.

The present action was begun on the 15th May, 1924, by the respondents against the appellants.

On the 5th May, 1927, Mr. Justice Duclos dismissed the action with costs on the ground (*a*) that the customers were estopped by their own negligence, (*b*) that they could not impose a greater standard of care upon the appellants than they exercised themselves, (*c*) that the customers held out Rogers as their agent and gave the appellants every reason to believe he was acting within their authority, (*d*) that the fact of Rogers asking for drafts to his own order was not sufficient to put the appellants on enquiry, and (*e*) that even if the appellants' suspicion might have been aroused on the first occasion such suspicion was allayed and lulled to sleep by the long series of similar transactions without objection or demur on the part of the customers and without notice to the appellants of any irregularity.

An appeal to the Court of King's Bench in appeal was dismissed on the 16th April, 1928.

The respondents appealed to the Supreme Court of Canada. On the 27th May, 1929, the Supreme Court by a majority allowed the appeal. The judgment of the majority was delivered by Mr. Justice Duff and was concurred in by Newcombe, Lamont and Smith JJ. Mr. Justice Rinfret dissented.

Their Lordships are of opinion that the majority of the Judges of the Supreme Court of Canada arrived at a right conclusion in holding that the appellants were liable.

It is to be observed *in limine* that the customers being a limited company were capable of speaking and acting only through agents duly authorised in that behalf in accordance with their constitution and that as between the appellants and the customers the duty of the former must *prima facie* be measured in the light of the resolution of the 8th July, 1912, which had been communicated to them.

In each of the instances under consideration the cheque drawn upon the appellants was duly signed in accordance with the resolution, and the appellants were justified in debiting the customers' account with the amount.

But nothing was owing from the customers to the appellants in whose favour the cheque was drawn. The money, therefore, in the hands of the appellants remained the money of the customers. What was the duty of the appellants in dealing with it?

In their Lordships' judgment the appellants were not entitled to deal with it except upon a proper authority from the customers. If after certification each cheque had been retained by the appellants until the proper authority was forthcoming, no question could have arisen. The appellants did not take this course. They were content to rest on the fact that Rogers produced a cheque duly signed. They returned the certified cheque to Rogers and accepted his sole direction as to how the money was to be applied. The requisition note was nothing but a direction by Rogers together with a representation by him as to the party on whose behalf he made it. If the requisition was made on behalf of the customers it did not answer the requirements of the resolution the existence of which excluded the possibility of an inference that any officer of the customers had a general authority to direct the application of the customers' money. Rogers, in fact, had no authority, actual or ostensible, to select the person in whose favour the bankers' draft was to be prepared.

If the case had related to a single transaction the appellants could, in their Lordships' judgment, have had no defence. Does the matter stand otherwise because the customers' officers were negligent in their business methods or because a number of instances forming part of a series of similar transactions are involved?

As between the customers and the appellants the duty of the appellants was constitutionally prescribed by the resolution of the 8th July, 1912, and could only be altered by some direction of equal constitutional validity. No act or omission of the customers' officers lacking such constitutional validity, whether such acts or omissions were or were not negligent as between such officers and the customers, could relieve the appellants of

any part of their obligations. The negligence relied on here was nothing more than a series of acts and omissions which might well have given the customers ground of complaint against their own officers, but did not justify any relaxation by the appellants of the vigilance which they owed to the customers.

Nor, in their Lordships' judgment, can the appellants find comfort in the fact that the transactions complained of were incidents in a series of similar transactions. In this connection the so-called doctrine of lulling to sleep has been invoked. Neglect of duty does not cease by repetition to be neglect of duty. If there be any doctrine of lulling to sleep it must depend upon and can only be another way of expressing estoppel or ratification.

It was admitted before their Lordships that estoppel had no place in this case.

Effective ratification necessarily involves knowledge of all the material facts on the part of him who ratifies.

Here the ratification, if any, must have been ratification of authority in Rogers to direct the appellants how to deal with the proceeds of the cheques and in particular to specify at his discretion in what names the drafts were to be prepared.

As the customers and their directors were throughout in ignorance of what Rogers was from time to time doing and never intended him to have authority in any instance to select for insertion in the draft his own name or any name except a particular name, their Lordships are of opinion that in the circumstances of this case ratification cannot be made out.

In the result, therefore, none of the points upon which the appellants have relied can avail them, and in their Lordships' judgment the appeal fails and should be dismissed with costs.

Their Lordships will humbly advise His Majesty accordingly.

In the Privy Council.

THE BANK OF MONTREAL

v.

THE DOMINION GRESHAM GUARANTEE AND CASUALTY COMPANY, LIMITED.

DELIVERED BY LORD TOMLIN.

Printed by
Harrison & Sons, Ltd., St. Martin's Lane, W.C.2,

1930.