Privy Council Appeal No. 25 of 1933.

Isaac William Cannon Solloway - - - - - - *Appellant*

v.

W. T. Johnson - - - - - - - - - *Respondent*

FROM

THE COURT OF APPEAL OF BRITISH COLUMBIA.

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 15TH JANUARY, 1934.

Present at the Hearing:

LORD BLANESBURGH.
LORD ATKIN.
LORD THANKERTON.
LORD RUSSELL OF KILLOWEN.
SIR LANCELOT SANDERSON.

[*Delivered by* LORD BLANESBURGH.]

In the action in the Supreme Court of British Columbia out of which this appeal arises, the defendants were Solloway, Mills & Company, Limited, a large brokerage Dominion company, having its head office in Toronto, with many branches throughout Canada and beyond; Isaac William Cannon Solloway and Harvey Mills, the first the president and the other a director of that company; and Solloway & Mills (B.C.), Limited, an associated Provincial concern.

The action was brought against these defendants by the present respondent as trustee in the bankruptcy of Theodore Frontier & Company, Limited, another brokerage company, with its headquarters at Kamloops, B.C. The plaintiff, basing his claim upon allegations which may, with sufficient particularity, be summarised as charges that the Solloway Company, with fraudulent intent, had, with the knowledge and at the instigation of the defendant directors, been guilty of acts of the description condemned in *Brookman* v. *Rothschild*, 5 Bligh N.S. 165, obtained at the trial against that company and the two individual defendants

an order which had as its effect the recovery from the three of the moneys paid by the Frontier Company to the Solloway Company in respect of the purchase and sale of divers mining and oil shares on so-called " open "—that is to say—speculative account. In the first instance the plaintiff, as has been seen, included Solloway & Mills (B.C.), Limited, as a defendant against whom relief was claimed. At the trial, however, no case was made against that company. Since then its name has not appeared in the proceedings. The claim finally allowed was ultimately quantified at the sum of $103,666.34, with interest at 5 per cent. per annum, making a total of $118,086.44. For that sum judgment against the first three defendants was entered.

The tenor and effect of the judgment, as drawn up, was, that these defendants became jointly and severally liable to satisfy it. But that result was reached by a judicial process of reasoning not disclosed on the face of the decree. The Solloway Company was ordered to pay or return with interest the moneys which that company had received from the Frontier Company in respect of the open transactions between the two companies on the footing that these transactions had been avoided. The judgment for the same sum against the defendant directors was one for damages, presumably sustained by the Frontier Company as a result of its entering into the same transactions.

The question whether any order at all in respect of damages could be properly made against the defendant Solloway remains a separate issue on the present appeal.

By the Court of Appeal the judgment of the trial Court was in the result upheld against all three defendants, but Mr. Justice M. A. Macdonald so far dissented from his colleagues there as to hold that judgment at the trial ought to have been entered against the Solloway Company only. As against the individual defendants Solloway and Mills the action, he thought, ought to have been dismissed.

The present appeal is by the defendant Solloway alone. Neither the Solloway Company nor the defendant Mills has sought before the Board to disturb the judgment now standing against them.

But their Lordships have not thereby been dispensed from the duty of considering whether the judgment against the Solloway Company was justified. It is not in contest that while the appellant Solloway on grounds special to himself—one of these has already been indicated—may be entitled to have the judgment against him discharged, he can in no circumstances be properly made liable in these proceedings for any sum in excess of the amount, if any, which the Solloway Company could therein be rightly ordered to return.

Before the Board, accordingly, Mr. Solloway as appellant was entitled to put forward any answer to the judgment appealed from, primarily open to the Solloway Company, as fully as any

answer thereto open to himself separately, and he has through his learned Counsel fully availed himself of that privilege and opportunity.

One of the branches of the Solloway Company was at Vancouver. It was at that branch that the business with the Frontier Company was transacted. The appellant Solloway, president of the Solloway Company, was at all times its principal shareholder.

The business which the Frontier Company carried on at Kamloops was a general stock brokerage business. The Company had an extensive clientele (p. 171), for whom it bought and sold stock exchange securities both for cash and on open account. There was no exchange at Kamloops and the stock exchange business of the Frontier Company had to be transacted through some inside broker or jobber on some convenient recognised exchange. This was well known to the Frontier clients (p. 181), but as they could not be expected to pay to the Frontier Company any brokerage in excess of that with which they would be charged by an inside broker acting on their direct instructions, it became a matter of necessity for that Company, if its profitable business was to be substantial, to have some arrangement with such an inside broker or jobber under which in view of the extent of its business with him he would be willing to return some portion of the commission normally chargeable to clients on stock exchange transactions. The Solloway Company with its Vancouver branch and a seat *inter alia* on the exchange there was such an inside broker, and thus there came about the relation between the two companies now to be examined.

Its nature is to be gathered from certain correspondence with the predecessor in business of the Solloway Company, a firm trading under the same name. It will suffice to refer to the following passages from two letters included in that correspondence. On 21st April, 1928, the Frontier Company wrote :—

> " As stated in our previous letter, we still have our connection with W. F. Irwin Company, and we will retain this connection until we hear definitely from you as to what arrangements can be made with your firm."

The following are passages from the Solloway firm's reply of the 25th April, 1928 :—

> We are prepared to handle your account on the terms mentioned by you—that is, we will . . . divide commission on a fifty-fifty basis. . . . We will deal with you on margin on the basis of 33⅓ per cent., with interest at 8 per cent. per annum on the unpaid balance. . . .
>
> We deal only in mining and oil stocks listed on the Vancouver Stock Exchange, Calgary Stock Exchange, and The Standard Stock and Mining Exchange at Toronto. . . .
>
> In all your orders be careful to specify ' buy ' or ' sell,' ' open order ' or ' day order ' and ' cash ' or ' open account.' We would ask you to scrutinise carefully the class of stock *your clients* will wish carried on margin. We do not wish to accept any order on this basis where the price is below 25 c. per share. We would also ask you at all times to endeavour to keep your margin no lower than one-third, and if possible request *your clients* to put up an amount in excess of that figure.

The significance of the italicised references to " your clients " in this last passage will presently appear.

This proposal, accepted by the Frontier Company, was acted upon by the Solloway Company on its incorporation at a later date. It did not preclude the Frontier Company from transacting any of its business through other inside brokers or jobbers. It did entitle that Company to the benefits stipulated for on all business actually transacted by the Solloway Company on its instructions.

Following upon this correspondence and up to September, 1929, when the Frontier Company became bankrupt, very many separate transactions, thousands, it seems, in number, both " cash " and " open," were in fact carried out with the Solloway Company by the Frontier Company on account of clients. There were also transactions—their number is not in evidence—which were actually the Frontier Company's own speculations. The bankruptcy of the Frontier Company commenced on the 17th September, 1929. The respondent, as has already been said, is trustee in that bankruptcy. The action in which judgment has been given against the appellant was commenced by the respondent on the 17th September, 1930. The claim already referred to extended in the first instance to all the transactions just summarised, whether " cash " or " open ": whether closed at the date of the commencement of the Frontier bankruptcy or not. In the course of the hearing, however, the claim in respect of moneys paid to the Solloway Company in respect of " cash " transactions ceased to be seriously pressed, and was in the result disallowed by the learned trial Judge. Accordingly the judgment pronounced at the trial is confined to moneys paid on the " open " transactions, and it now becomes desirable to analyse it in some detail.

Under it the Solloway Company and the two defendant directors have without any discrimination between them been made jointly and severally liable to the plaintiff as trustee in the Frontier bankruptcy for a sum representing the aggregate of the sums not in the interval re-credited or repaid by the Solloway Company which were paid *to that Company* by the Frontier Company as cover on all the " open " transactions entered into in the name of the Frontier Company with the Solloway Company between the 1st May, 1928, and the middle of September, 1929. These so-called " open " transactions had for the most part been closed, and always, without delivery of shares made, called for, or, it may be assumed, ever intended. They were effected in many different securities quoted on one or other or all the stock exchanges of Vancouver, Calgary and Toronto. They were in amounts varying from ten or even fewer shares to a thousand or more. The " cash " transactions in shares between the two companies under which delivery was intended and, in every instance, in due course made, were many,

although not so many as the "open" transactions. The fact that in respect of them no relief has been awarded to the plaintiff, and none is now claimed, becomes, as will be seen, one of significance, when it is remembered that in respect of voidability, if any, there was no distinction at all between these cash transactions and the open transactions.

The basis of the judgment is made clear when interpreted in the light of Mr. Fraser's argument for the plaintiff, which led to it. It may thus be summarised. The separate transactions, both open and cash, were merely the details of one entire trading in stocks between the two companies on the terms of the arrangement already stated. In the performance of its duty under that arrangement the Solloway Company adopted a system under which as occasion arose or its convenience required, that company, to put it shortly, fraudulently resorted to some part or all of the procedure condemned in *Brookman* v. *Rothschild* : the use of this system, even although not proved in the case of any single individual transaction, tainted with fraud the entire performance of the comprehensive contract, and its use, being known to and presumably directed by the two defendant directors of the Solloway Company, justified the plaintiff as the trustee in bankruptcy of the Frontier Company in his claim to avoid all the transactions and to recover from the Solloway Company and from the individual defendant directors, in the name of damages, the amounts thereby represented.

Now that case, finally accepted by the learned trial Judge, so far as the open transactions were concerned, has with many submissions as to the admissibility of evidence, its sufficiency and other matters, some of them perhaps needlessly technical, been supported and attacked with the greatest elaboration by Counsel on both sides.

Their Lordships do not enter into that discussion, beset as it is with much difficulty at many points. In their view the case accepted by the learned trial Judge was based upon a wrong principle, so that it becomes unnecessary to canvass in detail the reasoning or the sufficiency of the findings by which he supported his conclusion. Rather has it become incumbent upon their Lordships to embark upon an inquiry, not hitherto judicially undertaken, so as, in its result, to ascertain what was the real relation in which on facts not as such in controversy the different parties stood to each other. Can support be found for the statement of the learned Judge at page 361D—on which his whole judgment is based, viz., that on Frontier's bankrupty, "all that remained was a right of action on the part of the trustee *for the benefit of the estate*." ?

In other words, their Lordships proceed to inquire whether the plaintiff, whose sole title to sue is as trustee in the Frontier bankruptcy, has as to part of the sum adjudged any title to sue at all, and whether as to the residue of the same sum

his claim does not fail for want of the evidence essential to support it.

If these questions are answered adversely to the plaintiff trustee it is obvious that, without more, the present appeal must succeed, without invoking any considerations personal to the appellant.

Now the nature of the Frontier Company's business and the terms of its arrangement with the Solloway Company have already in part been detailed. Apparently the Frontier Company's account was throughout well known to the Solloway Company to be one mainly, if not exclusively, on behalf of clients of Frontier's, with names, in the first instance at all events, undisclosed to the Solloway Company. The reference to "your clients" in the letter of the 25th April, 1928, already emphasised, does not stand alone. The full commission was in the first instance paid to Solloway's on every transaction, and it was at the end of each month that half of it was returned to Frontier's. Again, Exhibit 56 (page 509) is a full statement, prepared by Frontier's (page 172), and in some way sent to Solloway's, detailing the participation at its date of each interested client of Frontier's in the accounts then outstanding with Solloway's.

Exhibit 61 (page 487) is the form in which Frontier's clients gave their instructions to them. A separate account for each client was kept in Frontier's books (page 175). Clients' orders, although in Frontier's name, were sent on to Solloway's separately as received, so as to enable the posting of their respective accounts to be made with less difficulty (page 167). Exhibit 41 (page 527), as printed, consists of two specimen examples of "sold" and "bought" notes sent by Solloway's to Frontier's in cases where a client's instructions had been carried out by Frontier. The actual exhibit is composed of many of these notes, and on each of them is written, in Frontier's office, the name of the client to whom it was referable.

These bought and sold notes, in the evidence referred to as "confirmations" or "Solloway's confirmations," have bulked largely in the case. Therein, if anywhere, are to be found the actual fraudulent misstatements or misrepresentations alleged against the Solloway Company. It is accordingly convenient here to observe that no one of them was sent on to, or apparently ever seen by the Frontier client concerned in the transaction. All that he received from Frontier's was a statement of account in which the result of the transaction, whether by way of charge or discharge, is embodied (page 179, Exhibit 63). In open transactions the cover was found by the client, paid into Frontier's general account, and ultimately transmitted to Solloway's by Frontier's own cheque. No default in the actual delivery of shares called for was ever made. There was no record of any complaint in respect of any of these

transactions, cash or open. As to the cash transactions, they had been closed up long before action. Frontier had no interest in them one way or another, said Miss Nuyens, a very intelligent employee of the Frontier Company, called by the plaintiff. And the same may be said of the open transactions closed prior to the bankruptcy of the Frontier Company. It is nowhere suggested in the record that in respect of these any money remains unpaid to Frontier by any client. As to Solloway's, it was admitted by Mr. Fraser at page 295 that up to October, 1929—a month *after* Frontier's bankruptcy—Solloway's had *ex facie* fulfilled all their mandates, an admission which has to be taken in conjunction with this further fact that no evidence was adduced to show that the client, or the Frontier Company itself, had in any instance suffered any loss or damage at all by the fulfilment of any mandate otherwise than as represented by the Solloway confirmation, if in fact such was the case. It is on such facts—there are many others similar in tendency to be found in the record—that the question must be answered whether, as trustee in bankruptcy of Frontier, and in that character alone, the plaintiff has any title at all to maintain the action or hold the judgment as against the appellant.

Now, first, in all these closed transactions, whether originally open or cash, excepting for the moment only those which may have been Frontier's own speculations, it is, their Lordships think, manifest that the Frontier Company's interest, whatever it originally may have been, had at the commencement of its bankruptcy ceased; or that if any scintilla of interest then remained, it was that of a bare trustee which did not pass to the plaintiff as trustee in its bankruptcy.

Be it observed that in this matter there is no difference in principle *quoad* the plaintiff, between closed cash transactions and closed open transactions. The plaintiff did not in the first instance discriminate between the two, and the only reason why the trial Judge did not extend his decree to the moneys paid on any closed cash transaction seems to have been that those moneys would be balanced by the scrip which, as a condition of any order declaring such a transaction void, would have to be returned to the defendant company. Let the plaintiff's position at this point, then, be viewed by reference both to the closed open transactions and to the closed cash transactions, in which, as Miss Nuyens agreed, Frontier's retained no interest one way or another: and let this test be put in the form of three questions:—

(1) What right or title had Frontier's trustee in bankruptcy to avoid *of his own motion* any of these transactions?

(2) What right or title had he to recover for the benefit of Frontier's creditors moneys paid in respect of them by Frontier's clients?

(3) What right or title had he to demand back from any client of Frontier's the shares received by that client on completion of his cash contracts?

These questions other than the last may be asked with as much pertinence in relation to the *closed* " open " transactions as to the *closed* " cash " transactions, and to all three it appears to their Lordships that only one answer is justified—an answer which discloses the fact that possibly, as to the whole, certainly as to the preponderant part of the sums included in the judgment, the plaintiff as trustee in bankruptcy has no right or title to them at all.

But this matter may equally well be approached from another angle. In what relation, it may be asked, did the Frontier Company stand to each one of these transactions entered into by it with Solloway's on the instructions of a client ? The answer made on indisputable authority must surely be that while the Frontier Company may have been personally liable to the Solloway Company on the contract, it was at the same time merely an agent for an undisclosed principal, the client. The trial Judge apparently treated this possible position as being negatived by the facts that the cover provided by the client passed through Frontier's general account before being paid over by Frontier to Solloway's, and that in Solloway's hands the money could no longer be earmarked as the money of any client. Then, by what seems to be a complete *non sequitur*, the learned Judge, using the words already quoted from his judgment, treated this last fact as a justification for the plaintiff being allowed to recover the moneys for Frontier's general estate. A reference, however, to the judgment of Vaughan Williams L.J. in *King* v. *Hutton* [1900] 2 Q.B., at page 505, will show how small in the circumstances is this fact to which the learned Judge attached final importance. The truth is that these considerations of his are hardly relevant to the question. The conclusion that in each transaction the client was the undisclosed principal is reached by reference to such facts as have here already been detailed, facts which show that there are absent from this case the only circumstances which caused any difficulty in reaching that conclusion in :—

Beckhusen and Gibbs v. *Hamblet* [1900], 2 Q.B., 18, 23 and 24.

Anderson v. *Beard* [1900], 2 Q.B., 260.

Scott and Horton v. *Godfrey* [1901], 2 K.B., 726. See particularly pages 733, 734, 737, 738, 739.

The difference of opinion between Bigham J. in the last case and Kennedy J. in the first does not, in view of Miss Nuyens's evidence, here arise.

But in this case it seems unnecessary to go further than this statement of Collins L.J. in *Levitt* v. *Hamblet* [1901], 2 K.B., 53, 63 :—" With regard to the question of whether privity can be created between the jobber and the client of the broker who gives the order, clearly at common law such privity would be raised."

Accordingly it is hardly possible to support the judgment of the trial Judge for the figure contained in it. With

its bankruptcy all authority of the Frontier Company as agent came to an end, and in relation to any question arising out of any transaction—certainly any closed transaction—the two contracting parties, Frontier's client and the Solloway Company, thereafter stood face to face. And be it observed that this difficulty is in no way met by conceding to Frontier's clients a right of proof in the bankruptcy in respect of any money of theirs paid to the trustee under the judgment. These clients have no more claim against Frontier's general assets in respect of these moneys than have Frontier's general creditors any right to participate in them. In the same way these moneys when recovered can never properly become general assets in the bankruptcy. They would constitute a separate trust fund for the benefit of Frontier's different clients, who in the first instance provided them. All of which is another way of saying that even if they might have been recoverable by the Frontier Company before its bankruptcy no title to sue for them ever vested in the plaintiff as trustee in that bankruptcy.

But even if the decree cannot be supported in its entirety, the question remains whether it may not be supported for some less figure? It may be said, and possibly quite truly, that the present figure represents, *inter alia*, moneys provided by the Frontier Company itself, recoverable on cause shown by the plaintiff as trustee in its bankruptcy. Even so, however, no case has been proved or attempted to be proved by the plaintiff justifying a decree for even such sums could their respective amounts be ascertained.

The truth is that the plaintiff here stakes everything in the risky adventure of endeavouring in one proceeding to secure the benefit of *Brookman* v. *Rothschild* in its application to a multitude of separate contracts and that without tendering any evidence at all that in the case of any one of these contracts Solloway's had been guilty of the conduct condemned in *Brookman* v. *Rothschild*.

The complete lack of proof from this point of view is striking. There is, for instance, no evidence at all as to any transaction prior to November, 1928: no documents from Solloway's Vancouver office before that month were in evidence (*see* page 47), and yet payments made in respect of the previous open transactions are all included in the decree, and amount at the least to $7,842.99 (*see* page 424). In fact, the plaintiff, for lack of evidence that any one of the impugned transactions was within the mischief of *Brookman* v. *Rothschild*, sought to rely for judgment merely on an attempted proof of a general system. He forgot that a *Brookman* v. *Rothschild* decree is only obtainable on proof that in carrying out the particular transaction the defendant was guilty of the conduct there condemned. Nothing of this kind has in fact been shown. It is a most striking circumstance that the only individual contracts to which

attention was directed, of course, at the instance of the defendants, were contracts free, in their carrying out, of all offence whatever.

So far their Lordships have been dealing with the case as it affects indifferently both the defendant company and the appellant. But the actual liability of the appellant is a thing distinct and apart from that of the company, and the judgment, even if well founded as against the company, may be incapable of support as against him. It will not, however, be necessary now to do more than indicate these separate difficulties which stand in the way of the judgment as affecting the appellant :—

1. While as against the company a *Brookman* v. *Rothschild* decree " may be made without proof of loss or of fraud " (*see* 5 Bligh N.S. at 189 : *Parker* v. *McKenna*, 10 Ch. 96, 107), there is no liability for damages upon the appellant as a director unless as against him both are proved.

2. It may be agreed that in a case under " the system " in a transaction where fraud has in fact been established against his company, fraud may, readily enough, be imputed to a director (especially if, as in this case, he gives no evidence) on proof that he was cognisant or responsible for the system and that, even although the working of the system is not necessarily fraudulent.

3. But even in such a case the remedy against the director is not the same as that against the company. This *Brookman* v. *Rothschild* claim that the transaction is void is in this respect closely analogous to an action for rescission against a company and its directors based on a fraudulent prospectus. There the company is ordered to return all the moneys paid under the contract rescinded. No such order, however, can be made against the directors either separately or jointly. This point is concluded by Lord Cairns' judgment in *Ross* v. *Estates Investment Company*, 3 Ch. 682, 689–90. His words are now transcribed for convenience of reference :—

> " But it seems that probably *per incuriam* the decree has ordered that Mr. Sarl [the defendant director implicated in the fraud] shall not only pay the costs of the suit, that is to say, be jointly and severally liable for the costs of the suit, which I think is quite right, but, further, that he shall be jointly and severally liable for the repayment of the £10 which was paid as a deposit on the plaintiff's shares. That money was not paid directly to him nor was he in any way the custodian of it. That direction must have crept into the decree by an oversight and it ought now to be varied."

In other words, the decree now appealed from cannot in its present form, on that ground alone, as against Solloway, be supported.

4. Nor is it on this point to be justified by reference to *Barnes* v. *Addy*, 9 Ch. 244. That case is doubtless an authority for the existence of some liability on the part of a director in the position of the appellant, against whose company a *Brookman* v. *Rothschild* decree based upon fraud has been properly made. But it supplies no measure of the extent of such a liability. The

order in *Barnes* v. *Addy* was to restore a trust fund which had been wrongfully paid away by the joint act of the trustee and the defendant, his solicitor. There the liability was clearly joint and several in respect of the only relief given. It is quite otherwise in this case.

For, as has already been pointed out, no loss or damage attributable to the fraud is here proved: no benefit from any proved fraud is shown to have accrued to the appellant. In these circumstances it would appear that no order beyond one for costs could properly be made against him. See *Ross* v. *Estates Investment Company ubi supra*. Adopting, however, the suggestion of Lindley M.R. in *Frankenburg* v. *Great Horseless Carriage Co.* [1900], 1 Q.B. 504, it is just conceivable that the appellant might ultimately have to answer in some damages in the event of the defendant company failing to meet a valid judgment against it. The observation of the Master of the Rolls, however, in that case was made on an interlocutory application to strike out a director as defendant in an action for rescission brought against his company and himself. It was not made at the trial, and their Lordships' attention has not been drawn to any succeeding English authority in which such a judgment as there contemplated has ever in fact been pronounced. But assuming that a decree for such damages may at some time be given against the appellant, the time for it has not yet arrived. And for what amount would it be? For no more, it would seem, than a nominal sum in the absence of proof of any damage to the plaintiff from any established fraud of the defendant company or of any benefit to the appellant accruing therefrom. In other words, damage resulting to the Frontier estate from the appellant's fraud is, as distinct from the claim against the Solloway Company, the gist of the cause of action against him. And no such damage has been proved.

But their Lordships need not further pursue this subject. For reasons already given the judgment appealed from cannot, as against the appellant, be allowed to stand. On that footing it is superfluous to consider the modifications which for other reasons would, so far as he is concerned, have to be made in it. If the judgment is to be *supported* as against him it must be proof against *all* attack.

Brookman v. *Rothschild pace* Lord Bramwell in *Waddell* v. *Blockey*, 4 Q.B. D. 678, 680, is good equity. Nothing here said will weaken its effect.

But neither *Brookman* v. *Rothschild*, nor any finding of the learned Judge, justifies in the absence of such evidence as that to which their Lordships have referred the judgment pronounced against the appellant.

Their Lordships will accordingly humbly advise His Majesty that the judgment appealed from be set aside so far as it affects the appellant. The respondent must pay to the appellant his costs in both the Provincial Courts as well as of this appeal.

In the Privy Council.

ISAAC WILLIAM CANNON SOLLOWAY

v.

W. T. JOHNSON.

DELIVERED BY LORD BLANESBURGH.

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