Privy Council Appeal No. 75 of 1939

Port Royal Pulp and Paper Company Limited - - *Appellant*

v.

The Royal Bank of Canada - - - - - - - *Respondent*

FROM

THE SUPREME COURT OF CANADA

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 30TH JULY, 1941

Present at the Hearing:

THE LORD CHANCELLOR
LORD THANKERTON
LORD RUSSELL OF KILLOWEN
LORD ROMER

[*Delivered by* LORD RUSSELL OF KILLOWEN]

In this case the Supreme Court of Canada has reversed the judgment of the Supreme Court of New Brunswick Appeal Division and has restored the judgment of the trial judge. The defendant to the action has appealed to His Majesty in Council.

The relevant facts must first be stated, and they are so exceptional and peculiar to this case that, as will appear, and as appears to their Lordships, no important point of law really arises for decision on this appeal.

Four personages figure in the story which leads up to the institution of this litigation: (1) a limited company incorporated under the laws of New Brunswick and called New Lepreau, Limited, (2) an individual named Atkinson, (3) the appellant, a paper manufacturing company incorporated under the laws of the Dominion of Canada (hereinafter referred to as the Company) and (4) the respondent, the Royal Bank of Canada (hereinafter referred to as the Bank).

New Lepreau, Limited, held licences to cut pulpwood within certain limits, viz., over an area of 62 sq. miles of Crown lands on the New River Estate, County of Charlotte, in New Brunswick. Of its 489 issued shares Atkinson originally held all except two shares; but at the times material to this litigation the Company held 241 of those shares (as security from Atkinson), and as to the 247 shares, the certificates had been endorsed by Atkinson in blank, and were held as security by the Bank.

In the spring of 1933 New Lepreau, Limited, entered into a contract with the Company for the sale of a quantity of pulpwood. No copy of this contract is in evidence, but its working out resulted in a substantial sum being due from New Lepreau, Limited, to the Company, in respect of moneys advanced by the Company to finance the operations by New Lepreau, Limited, necessary under the contract. The amount of this sum was subsequently ascertained to be $5330.91. This contract will be referred to as the first contract.

On the 31st October, 1933, New Lepreau, Limited, entered into another contract (hereinafter referred to as the second contract) with the Company, for the sale of 1,000 to 4,000 cords of pulpwood to be cut from the New

Lepreau limits. The contract provided for payments to be made by the Company in advance, and on account of price, at different stages of the operations.

During the pendency of that contract, and after advances under it to the extent of some $484.90 had been made by the Company to New Lepreau, Limited, Atkinson (who was already heavily indebted to the Bank) applied to the Bank for further monetary assistance. The Bank, as might be expected, required security; but the Bank's rights and powers to take security are controlled by the Bank Act, 1934, which re-enacted with certain amendments (immaterial for the present purpose) cap. 12 of the R.S.C. 1927.

On the 20th January, 1934, Atkinson gave a notice of his intention to give security to the Bank, which notice was registered on the 22nd January, 1934. On the 24th January, 1934, Atkinson signed an application under seal addressed to the Bank, requesting the Bank to grant and continue for 12 months from that date "a revolving line of credit for my pulpwood business, of $5,000" and to make advances to him thereunder on the security of his pulpwood. On the same day he purported to give this security to the Bank, in respect of the sum of $1,000 advanced to him by the Bank.

The document consists of a printed form in which printed words have been struck out, and blanks have been filled in, the ultimate outcome being a document under seal and signed by Atkinson which runs thus:—

> "In consideration of an advance of one thousand dollars made by "the Royal Bank of Canada to the undersigned for which the said "Bank holds the following bills or notes, January 24, 1934, $1,000.00 "the products of the forest, the goods wares and merchandise "mentioned below are hereby assigned to the said Bank as security for "the payment of the said bills or notes or renewals thereof or "substitutions therefor and interest thereon. This security is given "under the provisions of Section 88 of the Bank Act and is subject to "the provisions of the said Act. The said the products of the forest, "the goods wares and merchandise are now owned by the undersigned "and are now in the possession of Ewart C. Atkinson and are free "from any mortgage lien or charge thereon (except previous assignments "to the Bank) and are the following all the rough or draw shaved "spruce and fir pulpwood and are in the Lawrence flowage on New "River stream in the County of Charlotte or elsewhere."

On the 1st March, 1934, the Company agreed, at the request of Atkinson, that his name should be substituted for New Lepreau, Limited, in the second contract. This was done apparently by taking the existing document, enclosing the words "New Lepreau, Limited," in brackets, and typing over them the words "E. C. Atkinson." The result was that Atkinson became "the seller" within the meaning of the contract. No re-execution of the document appears to have taken place, nor was any release or agreement for novation executed by New Lepreau, Limited, but it was agreed between Atkinson and the Company that the Company should be entitled to charge against the second contract (i.e., in reduction of the price payable thereunder) the amounts over-advanced under the first contract, and the amounts already advanced to New Lepreau, Limited, under the second contract, before the substitution of Atkinson. Such an agreement would naturally be insisted upon by the Company, so as to ensure that the right of deduction which they could have asserted against New Lepreau, Limited, was not taken away or impaired by the proposed substitution of Atkinson. This agreement is hereinafter referred to as the deduction agreement.

Having obtained the Company's consent to this substitution, Atkinson proceeded to use the contract as a means of affording further security to the Bank; and on the 10th March, 1934, he executed a document, by which he assigned to the Bank all moneys, claims, rights and demands to which he was then or might thereafter be entitled to under the second contract, as collateral security for the fulfilment of all his obligations present and future to the Bank.

The Bank gave notice of this assignment to the Company by letter dated the 12th March, 1934, and the Company in their reply dated the 16th

March, 1934, indicated that the amount of the advances made during the winter amounting to $484.90 and over-advances on the first contract were chargeable against the second contract. The amount of the over-advances were then estimated to be about $4,000 but were eventually ascertained to amount to a sum of $5,300.00. The Bank attempted to challenge this claim of the Company, but it is evident that they must take their assignment of Atkinson's rights under the second contract subject to the existing deduction agreement.

On the 26th April, 1934, Atkinson (therein called the seller) entered into a further contract (hereinafter referred to as the third contract) with the Company for the sale to the Company of 10,000 cords of peeled spruce and fir pulpwood, " to be cut from lands owned or controlled by the seller and situated in Charlotte County, N.B.," at a price of $7.25 per cord; and on the 27th May, 1934, Atkinson assigned to the Bank all moneys, claims, rights and demands to which he was then or might thereafter be entitled under the third contract, as collateral security for the fulfilment of all his obligations present or future to the Bank. Notice of this assignment was given to the Company on the 17th July 1934.

On the 16th July, 1934, Atkinson signed a supplementary application under seal to the Bank requesting the Bank to grant and continue for 12 months from that date " a revolving line of credit for my pulpwood business of $10,000," and to make advances to him thereunder on the security of his pulpwood.

On the 12th July, 1934, the amount then due to the Bank by Atkinson in respect of the revolving line of credit asked for on the 24th January, 1934, was $5,000.00. From time to time sums had been paid off and from time to time other sums (within the limit of $5,000.00) had been advanced by the Bank. On the occasion of each fresh advance the Bank took from Atkinson a document purporting to be a security on pulpwood, in the form above set forth, and covering the total of the principal moneys then due from him.

In response to his request, on the 16th July, 1934, the Bank advanced further sums to Atkinson with the result that on the 29th January, 1935, the amount due to the Bank from Atkinson was a principal sum of $8,000.00. The same practice as before had been pursued since the 12th July, 1934, in regard to taking what purported to be securities on pulpwood, in the form above set forth, for the total amount from time to time due, the only variation being that on and after the 11th Sepfember, 1934, the description of the pulpwood included the words " or sap-peeled."

From early in November, 1934, onwards deliveries of pulpwood to the Company took place under the second and third contracts to the following extents, viz., 707.17 cords under the second contract, and 5,298.26 under the third contract, all cut within the limits of New Lepreau, Limited, with the immaterial exception of some which had been cut in trespass of the rights of a third party, who, however, has been settled with. No question arises in regard thereto. In order, however, to get these deliveries under the second and third contracts, the Company had to disburse moneys in advance of purchase price, and further moneys to meet various expenses which had of necessity to be incurred and discharged before any deliveries under the contracts could be made: but as regards payments made in advance of price all such payments made under a contract after notice of the assignment to the Bank of the rights under that contract, were only made in such a way that the Bank in fact received them.

Atkinson's financial position was obviously an unsatisfactory one from the points of view both of the Company and the Bank. Attempts were made to adjust matters so that further financial assistance could be given in order to work out the pulpwood contracts. They came to nothing, and on the 22nd February, 1936, the Bank commenced the present litigation

by issuing a writ against the Company claiming by the amended endorsement thereon the following relief:—

> "The Plaintiff's claim is for damages for wrongfully depriving the "Plaintiff of certain pulpwood of the Plaintiff which the Defendant "converted to its own use."
>
> "The Plaintiff also claims against the Defendant for the purchase "price of certain goods and merchandise sold and delivered to the "Defendant under two certain contracts in writing, one made between "New Lepreau, Limited, and the Defendant, dated the thirty-first day "of October, 1933, which with the consent of the Defendant was "transferred by New Lepreau, Limited, to one Ewart C. Atkinson; the "other dated the twenty-sixth day of April, 1934, made between the "said Ewart C. Atkinson and the Defendant, and both assigned by "the said Ewart C. Atkinson to the Plaintiff before action brought."

By their amended statement of claim the Bank pleaded these obviously inconsistent and contradictory claims as alternative claims for (1) the purchase price payable by the Company under the second and third contracts or (2) damages for conversion of the pulpwood delivered to the Company under those contracts, the latter claim being made upon the footing that by virtue of the securities on pulpwood purported to be given by Atkinson in the forms hereinbefore mentioned, the pulpwood so delivered to the Company was the property of the Bank. In respect of either claim the Bank only sought to recover a sum of $8,366.66 being, it was alleged, the total amount and interest due by Atkinson to the Bank for the advances made to him.

The Company pleaded as regards the claim for damages for conversion that the Bank's alleged securities on the pulpwood were invalid under the Bank Act, and that the pulpwood delivered to the Company under the second and third contracts was never at any time the property of the Bank, nor was the Bank at any time entitled to possession thereof. As regards the claim in respect of the purchase prices payable under the second and third contracts, the Company pleaded that after crediting those purchase prices against the debit balance due on the first contract and against the moneys paid by the Company in advance of the second and third contract prices and to meet the various expenses which had of necessity to be incurred and discharged before any deliveries under those contracts could be made, there remained an adverse balance of $542.29 due from Atkinson to the Company.

Those being, as their Lordships conceive, the relevant facts of this case, it remains to be seen how the action was dealt with by the Courts in Canada.

The action was tried by Barry C.J. who gave judgment for the Bank for the $8,000 with interest. Their Lordships find themselves in some doubt as to whether the Chief Justice acceded to the Bank's claim for damages for conversion, or to the claim on contract. While he indicates views which as to some are relevant to one claim, and as to others are relevant to the other claim, his judgment is contained in the following sentence:— "Under the facts as disclosed by the evidence, and according to the law as I understand it, I have had no difficulty whatever in arriving at the conclusion that the plaintiff is entitled to recover." Unfortunately, in the absence of any clearer indication of the evidence and the law which the learned Chief Justice had in mind, it is difficult to say which of the Bank's claims was successful. Clearly both cannot have succeeded; they are inconsistent and mutually destructive. On the whole, the many references in the judgment to the Bank's security on the pulpwood make their Lordships think that the Bank was awarded damages for conversion.

An appeal from this judgment came before the Supreme Court of New Brunswick, Appeal Division, and was heard by Baxter C.J. and Grimmer and Fairweather JJ. The judgment of the Court was delivered by Baxter C.J. They took the view that the Bank's alleged securities on the pulpwood were invalid under the Bank Act, and that accordingly the claim for damages for conversion must fail. As regards the claim *ex contractu* they were of opinion that the Bank could not claim more than Atkinson

would have been entitled to receive. They accepted the Company's claims for credit in respect of the moneys paid in advance of purchase price, and to meet the various expenses before mentioned. As regards the deduction agreement, while they were of opinion that it applied to the second contract, and had been made before the assignment by Atkinson to the Bank, they held that no agreement to charge against the third contract had been proved. The result of this view was to establish a balance of $192.02 in Atkinson's favour on the second and third contracts. An order was accordingly made on the 11th June, 1937, "that the judgment in favour of the plaintiff be reduced to the sum of one hundred and ninety-two dollars and two cents ($192.02) with the costs of the action, and that the appellants have the costs of the appeal."

The Bank appealed to the Supreme Court of Canada. The appeal was argued on the 17th and 18th May, 1938, and on the 19th December, 1938, that Court (consisting of Cannon, Crocket, Davis, Kerwin and Hudson JJ.) allowed the appeal, set aside the order appealed from and restored the judgment of Barry C.J.

Crocket J. (with whom Cannon and Hudson JJ. concurred) was of opinion that the Bank's claim to damages for conversion should succeed. As regards the claim *ex contractu*, he deals with it thus:—"If the Appeal Court is right in its conclusion that the Bank's securities under section 88 of the Bank Act were invalid because Atkinson was not the owner of the pulpwood within the meaning of that section, and the case is one which rests entirely, so far as the Bank is concerned, upon the assignments to it . . . of Atkinson's rights under the two contracts of 31st October, 1933, and 26th April, 1934, the result at which it arrived might be difficult to impeach." He then states that in his view the appeal turned "entirely upon the question of the validity of the Bank's assignments under section 88 in respect of the two contracts of 31st October, 1933, and 26th April, 1934, and their relation to each other." Their Lordships are somewhat puzzled by this sentence, with its allusion to the second and third contracts; for section 88 has no reference to securities such as the assignments of Atkinson's rights thereunder. The sentence can, they think, only mean that the learned judge is treating the securities purported to be given by Atkinson on pulpwood as being (which they are not) assignments of pulpwood to be delivered to a purchaser under a contract specified therein. If they were assignments in that form, the claim for damages for conversion would indeed be a strange one. The learned Judge then proceeds to rely on what he terms "the reasons by which Barry C.J. so lucidly and logically supports his judgment." He gives no reasons of his own, but merely states:—"I have no hesitation in holding for my part that upon the undisputed facts as disclosed by the evidence, Atkinson must be treated as the owner of the pulpwood when it was cut, within the meaning of section 88 of the Bank Act, and that his assignments to the plaintiff Bank were valid thereunder."

Davis J. (with whom Hudson J. also agreed) thought that the Bank was entitled to damages for conversion by the Company of the pulpwood delivered under the second and third contracts. After a caustic, but justifiable, reference to the loose and unbusinesslike manner in which the transactions in question were carried on by the Bank, the Company and Atkinson, the learned judge stated that: "All that is plain in the evidence is that the timber involved in this case was cut upon Crown land in respect of which New Lepreau, Limited, held a licence to cut." He then states that no one appears to have paid the slightest attention to the rights of that Company, which, for the purposes of the second and third contracts was obliterated from the picture. He accepts the view that Atkinson agreed that the Company could charge up against him the loss on the first contract, though it is not clear whether he thinks that this agreement applies to the third contract as well as the second contract. But on the question of conversion he holds that the security given by Atkinson to the Bank on pulpwood was valid. His judgment on this point is contained in the following words:—"It seems quite plain to me that Atkinson had at all times a qualified

ownership or interest in the wood, as soon as it was cut from the standing timber, sufficient to entitle the Bank to take from him section 88 security. I think the attack upon the Bank's security fails."

Kerwin J. had no hesitation in coming to the conclusion that the security under section 88 must be given by the owner, and that otherwise it is of no avail; but after stating that New Lepreau, Limited, made no claim that it was owner, and that the Company's interest in the logs arose only by virtue of the second and third contracts, he continued: " I think the proper inference from the evidence is that Atkinson was the owner and that he gave security to the Bank under section 88." He then held that the Bank had acquired all the right and title of the owner Atkinson, and that the Company had converted the logs to its own use and was liable in damages for the value of the logs at the time and place of conversion. The damages, however, he assessed, upon grounds immaterial to consider, at a figure considerably lower than the Bank's claim.

On appeal by special leave to His Majesty in Council by the Company the case was argued in careful detail before their Lordships, with the result that in their Lordships' opinion the appeal should be allowed and the order of the Appeal Division of the Supreme Court of New Brunswick should be restored.

As stated earlier in this judgment the relevant facts are exceptional and peculiar to this case. They are of such a nature that a declaration of the invalidity of the Bank's pulpwood securities, so far from being a decision of far-reaching and evil consequences under the Bank Act, as was somewhat menacingly suggested by counsel for the Bank, simply amounts to a decision that upon the facts of this case Atkinson was not an owner of the pulpwood here in question within the meaning of section 88 of the Bank Act. The authorities cited in the course of the argument gave no real assistance to their Lordships.

The mistaken foundation of the opposite view which appears in the judgments in favour of the Bank, is in part a failure to treat New Lepreau, Limited, as an entity separate from the body of its shareholders, and in part (as a consequence thereof) a failure to appreciate the true position in law of Atkinson under the second and third contracts.

Undoubtedly, as pointed out by Baxter C.J., Atkinson thought of and treated himself and New Lepreau, Limited, as one. " I am the New Lepreau, Limited," he says; and so in his opinion it makes no difference if the second and third contracts are in his name. He will still, nevertheless, be dealing with timber which is to be cut within the New Lepreau, Limited, limits, and which in law belongs to the Crown, but which New Lepreau, Limited, alone is licensed to cut, and which when cut and stumpage paid will be that Company's property to deliver to a purchaser. There is no suggestion in the evidence that in dealing with timber to be cut within the New Lepreau, Limited, limits, he was setting up or attempting to set up a claim to deal with the timber adversely to New Lepreau, Limited. There was never any surrender by New Lepreau, Limited, of its rights, such as they were, in the timber within its limits; nor was there, nor in the circumstances of this case could there have been, any taking of possession of the limits, or of the timber adversely to New Lepreau, Limited. The licences to cut continued throughout to be licences to New Lepreau, Limited, only. The state of affairs so far as concerns the physical possession of the limits, and the persons engaged in the operations carried on within the limits, was just the same from March, 1934, onwards, as it had existed previously. The attitude of mind, " I am the New Lepreau. Limited." (shared as it seems to have been by the parties to this action) carries with it the implication, " What I do, is done by New Lepreau, Limited," just as much as the implication, " What New Lepreau, Limited, does, is done by me." Their Lordships find it impossible to hold that in this case anything happened to confer upon Atkinson, or that Atkinson had, any interest proprietary or possessory in the pulpwood which is alleged to have been converted by the Company. Whoever was the owner within

the meaning of the Act, Atkinson certainly was not. In these circumstances the Bank's alleged security on pulpwood was invalid, and the claim to damages for conversion necessarily fails.

Another answer to this claim (and this is upon the footing of the security being valid) is to be found in agreements entered into by Atkinson with the Bank on the 24th January, 1934, and the 16th July, 1934, when the Bank granted the revolving lines of credit on the security of pulpwood. These agreements need not be referred to in detail; it is sufficient to say that under them Atkinson was authorised to sell the pulpwood. It is difficult to see how the taking delivery of goods under a sale which was authorised by the secured creditor, could be the foundation of a claim by that creditor for damages for conversion of his goods.

As regards the alternative claim for the price of the pulpwood sold and delivered under the second and third contracts, their Lordships agree with the views of the Appeal Division.

The Bank's security consists of an assignment of the rights of a vendor under a contract for the sale of a commodity, which can only be produced and delivered to the purchaser after expenses have been incurred by or on behalf of the vendor, in the shape of wages, stumpage payments, freight and so forth. The circumstances are such that in order to obtain delivery of what is agreed to be sold, the purchaser has been compelled to provide these essential payments. Then and only then can he obtain delivery; then and only then does he become liable for the purchase price or the balance thereof then due. In these circumstances it appears to their Lordships (quite apart from the doctrine of salvage advances) that credit must be given to the purchaser, against any claim to the purchase price by an assignee by way of security of the vendor's rights, for all payments which were essential to the production of the subject matter of the sale, and without which there would have been no sale completed, no purchase price payable, and consequently no subject matter of the security.

Their Lordships also agree with the Appeal Division in holding that the deduction agreement between Atkinson and the Company (made before the assignment of the 10th March, 1934, to the Bank, and therefore binding on the Bank) was not proved to have been made in relation to the third contract.

The result is that their Lordships are of opinion that this appeal should be allowed. The order of the Supreme Court of Canada should be discharged and the order of the Supreme Court of New Brunswick, Appeal Division, restored. They will humbly advise His Majesty accordingly.

The respondents will pay the appellant's costs here, and in the Supreme Court of Canada.

(13688) Wt. 8794—7 150 8/41 P.L.

In the Privy Council

PORT ROYAL PULP AND PAPER COMPANY LIMITED

v.

THE ROYAL BANK OF CANADA

DELIVERED BY

LORD RUSSELL OF KILLOWEN

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