Court File No. CV-14-10493-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

IN THE MATTER OF Section 101 of the
Courts of Justice Act and Section 243 of the *Bankruptcy and Insolvency Act*

B E T W E E N:

TREZ CAPITAL LIMITED PARTNERSHIP and COMPUTERSHARE TRUST COMPANY OF CANADA

Applicants

and

WYNFORD PROFESSIONAL CENTRE LTD. and GLOBAL MILLS INC.

Respondents

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Case Name:

574095 Alberta Ltd. v. Brendanco Investments Inc.

Between
574095 Alberta Ltd., plaintiff, and
Brendanco Investments Inc., 424657 Alberta Ltd.,
Connorco Investments Inc., 351956 Alberta Ltd.,
Gallatin Resources Inc., 520027 Alberta Ltd.,
Toddco Resources Inc., Superman Resources Inc.,
Omers Resources Limited, 851479 Alberta Ltd.,
1381351 Ontario Inc., Royal Trust Corporation of
Canada and CIBC Mellon Trust Company, defendants

[2002] A.J. No. 511

2002 ABQB 277

308 A.R. 285

120 A.C.W.S. (3d) 897

Action No. 0001-01246

Alberta Court of Queen's Bench
Judicial District of Calgary

Park J.

Heard: April 17, 18 and July 17, 2001.
Judgment: filed March 15, 2002.

(130 paras.)

Counsel:

Don Dear and Neal McLennan, for the plaintiff.
Ken Mills and Phil LaFlair, for the defendants.

REASONS FOR JUDGMENT

PARK J.:--

FACTS

1 This is an action to enforce an alleged lien interest in certain oil and gas assets. Counsel filed a Statement of Agreed Facts (Exhibit 1) at the commencement of the trial for the purpose of shortening and facilitating the trial and the scope of additional evidence. It was agreed that any party could offer further evidence in the trial which was in addition to or consistent with the Statement of Agreed Facts. It was further agreed that no party could offer evidence which was inconsistent with the Statement of Agreed Facts.

2 There was a further agreement, that the documents referenced in the Statement of Agreed Facts, are set out in Tabs 1 - 37 in Exhibit 2. Those documents were admitted into evidence solely on the basis that they were relevant and were sent and received as applicable in a manner consistent with Rule 192 of the Alberta Rules of Court. The documents were not admitted into evidence as proof of the truth of their contents, except insofar as a specific statement in a particular document is otherwise set out in the Statement of Agreed Facts.

3 In addition there were other documents tendered and marked as exhibits in the course of the trial.

4 The Statement of Agreed Facts is set out as follows:

1. 574095 Alberta Ltd. ("574095") is a body corporate duly authorized to carry on business in Alberta engaged in the production of oil and gas.
2. 1381351 Ontario Inc. ("1381351"), is a body corporate duly authorized to carry on business in Alberta engaged in the production of oil and gas.
3. 851479 Alberta Ltd. ("851469") is a body corporate duly authorized to carry on business in Alberta engaged in the production of oil and gas.
4. In the 1960's, Hamilton Brothers Oil & Gas Corporation ("Hamilton") acquired a working interest and a royalty interest in certain, petroleum producing properties in Alberta held under Crown and freehold leases (the "Assets").
5. By letter agreement dated July 19, 1979, ("the Letter Agreement") Carter Oil & Gas Limited ("Carter") agreed to purchase all of Hamilton's interests in the Assets for a purchase price of $32,000,000.00, as adjusted on closing, together with an overriding royalty ("the Hamilton Royalty") payable by Carter on production from the Assets. The royalty was capped at $490,500,000.00.
6. Schedule "B" to the Letter Agreement was a Petroleum, Natural Gas and General Rights Conveyance and Royalty Reservation Agreement dated August 8, 1979 between Carter and Hamilton ("the Hamilton Royalty Reservation Agreement"), and attached as Appendix "A" to the Hamilton Royalty Reservation Agreement was an agreement entitled "Vendor's Royalty Provisions" ("the Vendor's Royalty Provisions"). Under the Vendor's Royalty Provisions, Carter and Hamilton agreed the Hamilton Royalty payable by Carter would be calculated on a sliding scale as follows:

(a) 62.5% of the value of all petroleum substances produced rom and/or allocated to the Assets for the first 6 years from and after the effective date;

(b) 65% of the value of all petroleum substances produced from and/or allocated to the Assets for the 7th and 8th years from and after the effective date;

(c) 70% of the value of all petroleum substances produced from and/or allocated to the Assets from and after the end of the 8th year from and after the effective date.

7. On or about August 8, 1979, Hamilton, Carter and Royal Trust entered into an Agency Agreement ("the Royal Trust Agency Agreement:), under which Royal Trust agreed to become the recorded lessee of all leases comprising the Assets, and to hold the working interests of Carter, and the royalty interests of Hamilton, as bare legal trustee. Royal Trust agreed under the Royal Trust Agency Agreement to continue as trustee and agent until the Hamilton Royalty was paid out in full or until Royal Trust's position as agent was terminated by Carter and Hamilton.

8. On or about August 9, 1979, Hamilton, Hamilton Brothers Canadian Gas Company Ltd. ("Hamilton Canada"), Carter and Royal Trust entered into a Disbursing Agent Agreement ("the Disbursing Agent Agreement"), which was attached as Appendix "B" to the Royal Trust Agency Agreement. Under the Disbursing Agent Agreement it was agreed that all revenues from the sale of petroleum, natural gas and all related hydrocarbons produced from the Assets would be paid to the disbursing agent, Royal Trust, and that Royal Trust would disburse the money in the following priority:

a. Burden's Account;
b. Hamilton Canada Account;
c. Payments to the various operators of the Assets;
d. Hamilton Overriding Royalty Account;
e. Carter Account to pay the manager of the Assets;
f. Carter Account for Distribution.

9. On or about December 11, 1979, Carter entered into a Petroleum, Natural Gas and General Rights Conveyance ("the Petroleum and General Rights Agreement") with the following companies:

(a) 212834 Oil & Gas Ltd.,
(b) 212397 Oil & Gas Ltd.,
(c) 212873 Oil & Gas Ltd.,
(d) 206218 Oil & Gas Ltd.,
(e) LCR Resources Ltd.,
(f) 209579 Oil & Gas Ltd.,
(g) RGO Investments Ltd.,

(h) Carter Resources Ltd.,
(i) 212535 Oil & Gas Ltd., and
(j) St. Ives Resources Ltd.

collectively referred to as the Tencos ("Original Tencos"). The Petroleum and General Rights Agreement was amended by Carter and the Original Tencos on or about March 5, 1980.

10. Under the terms of the Petroleum and General Rights Agreement, Carter assigned an undivided 10% of its right, title and interest in the Assets to each of the Original Tencos (the "Tenco Assets").
11. On or about April 17, 1980 Carter and at least several of the Original Tencos entered into a Management and Agency Agreement (the "Management and Agency Agreement") wherein Carter agreed to act as the manager and agent for the Original Tencos with respect to the Tenco Assets. It is uncertain whether the Management and Agency Agreement was signed by 3 of the Original Tencos.
12. Pursuant to the Disbursing Agent Agreement, Hamilton Brothers Canadian Gas Company Ltd. ("Hamilton Canada") had the responsibility of preparing Disbursing Agent Instructions ("DAI"). The processing of the DAI was to be as follows:

    (a) The DAI were to be provided to Carter by the 25th day of each month;
    (b) If Carter received agreement from all Tencos with respect to the proposed disbursement of funds, then Carter would advise Hamilton Canada of same;
    (c) Hamilton Canada would then provide the DAI to Royal Trust; and
    (d) Royal Trust was obliged to distribute the money as directed by the DAI.

13. On or about May 1, 1986, Carter was advised that $1,827,916.52 was owned to Amoco Canada Petroleum Company Ltd. ("Amoco") as operator. At that time there was $505,267.01 in the Carter account (which had been paid by the Original Tencos or their successors in interest pursuant to the March 30, 1986 DAI). This resulted in a net deficiency of $1,322,469.50. As a result, on May 1, 1986, Carter sent a letter to the following companies advising them that there was a deficiency in the total amount of $1,322,649.51 which had to be made up by payments of $132,264.95 each:

(a) Nucorr Petroleums Ltd.;
(b) 209679 Oil & Gas Ltd.;
(c) Audex Gas & Oil Ltd.;
(d) Jennifer Petroleums Ltd.;
(e) Claude Resources Inc.;
(f) Commercial Oil & Gas Ltd.;

(g) LCR Resources Ltd.;
(h) Hawkness Equities Ltd.;
(i) Red Rock Resources Ltd., and
(j) Agassiz Resources Ltd.

(collectively the "1986 Tencos").

14. On or about May 5, 1986, Claude and Nucorr made payment of $132,264.95 each to Royal Trust as payment on the deficiency of the April 30, 1986 DAI (the "Payments"). None of the 8 other 1986 Tencos (the "Eightcos") made their payment of $132,264.95.
15. On October 10, 1986, Carter, as manager and agent for the 1986 Tencos, called a meeting for October 16, 1986 to discuss, amongst other topics, the payments of Claude and Nucorr.
16. On or about October 16, 1986, the 1986 Tencos and Carter attended a meeting to discuss issues relating to the operation of the 1986 Tencos including the $132,264.95 payments of each of Claude and Nucorr. The letter circulated by Carter following that meeting purported to be a summary of the items discussed.
17. On October 17, 1986, Nucorr sent a letter to Carter confirming their agreement to allow the $505,267.00 (from the March 1986 DAI payment) to be released to Royal Trust for distribution to the Hamilton overriding royalty account.
18. On October 21, 1986 Carter on behalf of the 1986 Tencos sent a letter to Royal Trust advising that the $505,267.01 (plus interest of $10,171.42) previously disputed from the March 1986 DAI should be transferred to the Hamilton overriding royalty account.
19. The accounting spreadsheets prepared by Carter in October, 1986 identifies that Claude and Nucorr made a payment of $132,264.95 each for a total of $264,529.90 for payment of the October 30, 1986 deficiency.
20. By letter of October 22, 1986, J.R. MacNeill of Claude confirmed to Carter that the $515,984.42 from the March 1986 DAI payment (being $505,267.00 plus interest of $10,717.42) should be released to the Hamilton overriding royalty account.
21. Claude or Nucorr did not make a demand of the other 1986 Tencos or their successors in interest for any payment between October, 1986 and September, 1999.
22. Appendix I to the Statement of Agreed Facts sets out how the Plaintiff acquired an interest in some of the Tenco Assets. Appendix 1 is as follows:

1. Carter Resources Ltd. was an Original Tenco;

    a. Carter sold, assigned, transferred or conveyed its right and interest in the Assets to Newpar Oil & Gas Partnership;

b. Newpar Oil & Gas Partnership sold, assigned, transferred or conveyed its right and interest in the Assets to Claude Resources Ltd.; and

c. Claude Resources Ltd. sold, assigned, transferred or conveyed its right and interest in the Assets to 574095.

2. 212535 Oil & Gas Ltd. was an Original Tenco;

a. 212535 Oil & Gas Ltd. sold, assigned, transferred or conveyed its right and interest in the Assets to Liberty Petroleums Inc.;

b. Liberty Petroleums Inc. sold, assigned, transferred or conveyed its right and interest in the Assets to Nucorr Petroleums Ltd.;

c. Nucorr Petroleums Ltd. sold, assigned, transferred or conveyed its right and interest in the Assets to Claude Resources Ltd.;

d. Claude Resources Ltd. sold, assigned, transferred or conveyed its right and interest in the Assets to 574095.

3. St. Ives Resources Ltd. was an Original Tenco;

a. St. Ives Resources Ltd. sold, assigned, transferred or conveyed its right and interest in the Assets to Commercial Oil & Gas Ltd;

b. Commercial Oil & Gas Ltd. sold, assigned, transferred or conveyed its right and interest in the Assets to Claude Resources Ltd.;

c. Claude Resources Ltd. sold, assigned, transferred or conveyed its right and interest in the Assets to 574095.

23. In or about October 1999, the Defendants 851479 and 1381351 entered into agreements (the "Sevenco Agreements") with Brendanco Investments Inc., 424557 Alberta Ltd., Connorco Investments Inc., 351956 Alberta Ltd., Gallatin Resources Inc., 520027 Alberta Ltd., and Toddco Resources Inc., (the "Vendor Tencos") to purchase their interest in the Tenco Assets (the "Purchase"). In the Statement of Agreed Facts there was set out as Appendix II a memo of R. Gordon Cormie, as special counsel to BHP Petroleums (Americas) Inc., of October 21, 1999 to trace title of the working interest held by the Tencos from the interest originally conveyed by Carter Oil & Gas Ltd., in December of 1979 to the working interest title held by each Tenco on October 21, 1999. The memo deals with each Tenco's working interest and sets out 10 schedules with each schedule detailing the history of each Tenco's working interest. These schedules are too voluminous to be set out here, but each is set out in Exhibit 1.

24. On or about October 24, 1991 the offer of 424557 was accepted by the Sheriff, Judicial District of Calgary for the sale of the interests of Trapper Resources Ltd.
25. On or about August 15, 1997, Cooper & Lybrand Limited, in its capacity as agent for the Bank of Montreal and receiver/manager with respect to the undertaking, property and assets of Jennifer Petroleums Ltd. and 212634 Oil & Gas Ltd., assigned the Assets of Jennifer Petroleums Ltd. and 212634 Oil & Gas Ltd. to Brendanco Investments Inc.
26. On or about June 4, 1992, the assets of 209679 Oil & Gas ltd. were sold by BDO Dunwoody Ward Mallette Inc. as agent for the Bank of Montreal to 520027 Alberta Ltd.
27. On or about June 19, 1989, Dix Management Limited ("Dix") became the successor of Carter to the Management and Agency Agreement.
28. Hamilton sold, assigned, transferred or conveyed nterest in the Hamilton Royalty to BHP Petroleum (Canada) Inc. ("BHP").
29. In or about October 1999, BHP sold, assigned, transferred or conveyed its right and interest in the Hamilton Royalty to the Defendants Superman Resources Inc., ("Superman") and Omers Resources Limited ("Omers").
30. It is agreed that paragraphs 31 through 36 of this Statement of Agreed Facts represent accurate principal and interest calculations with respect to the claim of 574095. It is not agreed that 851479 and 1381351 are liable for these amounts.
31. The principal is calculated as follows:

Original payment by Claude	$132,264.95
Original payment by Nucorr	$132,264.95
TOTAL:	$264.529.90 (the "Alleged Debt")

The Plaintiff is the holder of 30% of the original Tencos' interest and, as a result, no claim is being made by the Plaintiff for 30% of the total amount. Therefore, the total outstanding principal amount is 70% of $264,529.90 for a total of $185,170.93.

32. If the Management and Agency Agreement is found to apply, interest on funds advanced were calculated on the basis of: "a rate equal to 6% per annum in excess of the prime lending rate charged from time-to-time to commercial borrowers by the Canadian Commercial & Industrial Bank".
33. The Canadian Commercial & Industrial Bank changed its name to the Canadian Commercial Bank. As the Canadian Commercial Bank is no longer in existence, CCB Prime and commercial agreements shall be calculated using Toronto Dominion Bank prime rates.
34. It could be argued that interest can be calculated on this amount from May 5, 1986 when the funds were first advanced by Claude and Nucorr, or Oc-

tober 16, 1986 when the Plaintiff alleges that an agreement was made by which interest was to be paid to Claude and Nucorr.

35. Based on a yearly compounding of the interest under the Management and Agency Agreement rate, the following interest would be payable to January 1, 2001 on the principal amount of $185,170.93:

From May 6, 1986	$1,166,536.92
From October 16, 1986	$1,154,075.83

36. Alternatively, based on pre-Judgment interest under the Judgment Interest Act, being Ch. J-1 of the 2000 R.S.A., the following interest would be payable to January 1, 2001 on the principal amount of $185,170.93:

From May 5, 1986	$181,994.44
From October 16, 1986	$175,293.43

37. As a consequence of the events surrounding the payments made by Claude and Nucorr in May of 1986, the Plaintiff provided notice of its claim to 851479 and 1381351 by letter of October 28, 1999.

38. On October 28, 1999 the Plaintiff registered a security notice, Registration No. 9909526, (the "Security Notice") against certain oil and gas interests, acquired by 851479 and 1381351 on October 29, 1999 (the "Interests").

39. On October 28, 1999 the Plaintiff registered caveats, Registration Nos. 992333502, 992333503, 992333515, 992333516, 992333541, 992333542, 992333543, 992333544, 992333593, 992333594, 992333595, 992333596, 992333740, 992333741, 992333742, 992333743, 992333744, 992333745, 992333746 and 992333747 (the "Caveats") against the Interests.

40. The Plaintiff also caused a lien to be registered at the Personal Property Registry in the Province of Alberta.

41. In response to the actions of 547095, 851479 and 1381351 filed an Originating Notice on December 23, 1999 returnable on January 10, 2000 for an application for a hearing:

(a) requiring 574095 to show cause why the registration of the Security Notice should not be cancelled, and for an Order directing the Minister of Energy to cancel the registration of the Security Notice to Section 143 of the Mines and Minerals Act, now being Ch.M-17 of the 2000 R.S.A.;

(b) requiring 574095 to show cause why the registration of the Caveats should not be discharged pursuant to s. 139 of the Land Titles Act, now being Ch L-5 of the 2000 R.S.A.; and

(c) for an order discharging the Caveats pursuant to the Land Titles Act.

42. In conjunction with the Notice of Motion, a Demand for Information was served upon 574095 requiring 574095 to deliver a true copy of the security instrument that is subject of the Security Notice.
43. 574095 filed a Statement of Claim in this action against the Defendants for, inter alia, the amount of $185,170.99 plus interest of $1,085,126.42 as at October 31, 1999 together with interest thereafter.
44. 851479 and 1381351 denied liability to 574095 and filed a Statement of Defence on February 7, 2000.
45. 574095 discontinued its action against the Bank of Montreal on November 20, 2000.

5 During the course of the trial leave was given to the Plaintiff to file an Amended Amended Statement of Claim and to the Defendants to file an Amended Amended Statement of Defence.

6 As well as the Agreed Statement of Facts both counsel in argument brought certain proposed additional facts to my attention. I agree with certain of those additional facts and I so find them to be as follows.

7 Plaintiff's counsel pointed out that in 1985 Amoco Canada Petroleum Company Ltd., the operator of the Nipisi oil field (one of the Assets), undertook an experimental Miscible Flood project whereby natural gas and water was injected into the ground in order to enhance the recovery of oil. This project was very costly and resulted in the working interest owners in the Nipisi Field (including the Tencos) being responsible for operating cash calls from time-to-time. Initially one cash call of March 31, 1986 of this deficiency nature was responded to and paid by some of the Tencos. (See Exhibit 3, Tab 5) in the sum of $898,022.50.

8 As mentioned in paragraph 13 of the Statement of Agreed Facts the Tencos as well had earlier paid $505,267.01 to the Carter account in response to the March 20, 1986 DAI. A dispute arose between Hamilton and the Tencos about the allocation of this sum of money. Hamilton wished those funds paid to it and Carter and the Tencos wished to provide it to the operator, Amoco.

9 The sum of $1,827,916.52 (as set out in paragraph 13 of the Statement of Agreed Facts) owed to Amoco as operator was generated from expenses incurred by Amoco as a result of the Miscible Flood program. At that time the aforementioned sum of $505,267.01 was still in the Carter account because agent Carter, and Hamilton had not yet resolved the impasse as to where those funds were to be allocated. Assuming that those funds were to be paid out, there would be a net deficiency of $1,322,649.50 and each Tenco would owe $132,264.95. This was calculated on the basis of each Tenco owning a 10% interest in the undivided whole interest. This amount of $132,264.95 was calculated as follows:

Original March 86 Amoco Invoice	13,528,000.00
The 9.10010% share owned by the Tencos	1,231,061.53

May 1, 1986 Cashcall	1,231,061.53
Joint Venture Billing	596,854.95
TOTAL	1,827,916.48

Cash in Carter Account	(505,267.01)
TOTAL	1,322,649.47

Per Tenco	$	132,264.95

10 This debt of $132,264.95 was brought to each Tenco's attention by Carter as set out in paragraph 16 of the Statement of Agreed Facts.

11 In addition to the facts as set out in the Statement of Agreed Facts and to the aforesaid facts which counsel addressed in argument before me (and with which I agree) I must deal with certain other facts as I find them to be as a result of my consideration of the evidence placed before me in the trial. Counsel had agreed in the Statement of Agreed Facts that either counsel was free to place additional viva voce or documentary evidence before the Court as long as that evidence was not inconsistent with the Statement of Agreed Facts. As well I must deal with findings of fact regarding any proof of the truth of any contents of any documents and which proof is not inconsistent with the Statement of Agreed Facts.

ADDITIONAL FACTS

12 It is important to note the provisions of the Petroleum Natural Gas & General Rights Conveyance (Exhibit 2, Tab 6) dated the 11th day of December, 1979 and made between Carter and the Tencos wherein the Tencos purchased Carter's working interest for $35,000,000.00. Clauses 1(a), 1(g), 2(a) and 5 are of particular importance. Those clauses read as follows:

> 1(a) "Hydrocarbon Rights" means the undivided percentage participating interests of the Assignor as set forth in Schedule "A" hereto in the rights, licenses and privileges to explore for, drill for or take Hydrocarbons from the said lands:
>
> . . .
>
> (g) "Sold Assets" means the Hydrocarbon Rights, the Tangibles and the Miscellaneous Interests;
>
> . . .
>
> 2 SALE AND CONVEYANCE
>
> (a) The assignor hereby sells, assigns, transfer, conveys and set over unto each of the Assignees and each of the Assignees hereby purchases and accepts directly from the Assignor in equal proportions of interest the entire right, title, estate and interest of the Assignor in and to the Sold Assets, for the price and sum of Thirty Five Million ($35,000,000.00) in lawful money of Canada. TO HAVE AND TO HOLD the same, together with all benefit

> and advantage to be derived therefrom, absolutely, subject to the respective terms and conditions of the Leases and the Agreements.

. . .

> 5. INDEMNITY
>
> The Assignor shall continue to remain liable and indemnify the Assignees from and against any liability, loss, costs, claims or damages arising out of any matter or thing relating to the Hydrocarbon Rights hereby assigned occurring or arising prior to the Effective Time, and the Assignees shall indemnify the Assignor from and against similar liability, loss, costs, claims or damages arising subsequent to the Effective Time.

13 It is apparent from reading this document that the Tencos purchased equal proportions in the participating working interest in the assets on an <u>undivided basis</u> (underlining mine).

14 Another equally important document is the Letter Agreement (Exhibit 2, Tab 1) and specifically attached thereto, Appendix "A" to a Petroleum, Natural Gas and General Rights Conveyance and Royalty Reservation dated July 31, 1979 between Hamilton Brothers Oil & Gas Corporation and Carter Oil & Gas Limited for the sale of assets of Hamilton Brothers Oil & Gas Corporation to Carter. This document dealt with the original sale by Hamilton to Carter of the working interest subject to the overriding royalty to Hamilton. In dealing with the Hamilton Overriding Royalty, clause 14 of that Agreement is relevant. It states:

> 14. RIGHTS AND REMEDIES OF VENDOR
>
> Should Purchaser fail to substantially perform any material covenant herein which adversely affects the Vendor, or become insolvent, be adjudged bankrupt or unable to pay its debts generally as they become due, Vendor may in order to protect its Vendor's Royalty designate an agent or its assigns or designees to succeed to all of Purchaser's rights to possession and operation of said lands and production therefrom and apply the proceeds thereof to the costs and expenses of development, operation and maintenance of said lands.

15 This clause gives the royalty holder, Hamilton, the right to protect its royalty by moving to succeed to all the Carter (subsequent Tencos') rights to possession and operation of the lands and the production should the purchaser (Carter and the Tencos subsequently) be unable to pay their debts as the debts become due.

16 This clause, combined with a Bennett Jones legal opinion received by Carter and communicated to the Tencos, certainly provides a basis for any belief by any of the Tencos that there existed a joint and several liability by the Tencos, and possibly Carter, to Hamilton. Each Tenco had a 10% undivided interest in the lands as a whole.

17 It is certainly a background fact that Carter commissioned that Bennett Jones legal opinion dated April 17, 1986 (Exhibit 3, Tab 11), which advised that if any Tenco defaulted in its obligation then all of the Tencos would almost certainly be jointly and severally liable for the deficiency.

Whether or not that advice was correct or partially correct or incorrect, Blair Fox (the manager initially for Carter under the Management and Agency Agreement with the Tencos in 1985) testified that he believed that all of the Tencos, shortly after that letter was communicated to them, began to conduct themselves on the basis of this joint and several liability. As a result of the testimony of Fox, which I accept, I infer that this conduct arose from the state of belief of each Tenco regardless whether that legal opinion was correct. Each Tenco believed it could be held jointly and severally liable to Hamilton for the royalty interest and any deficiency arising from that royalty interest.

18 Against the backdrop of those beliefs, Hamilton, on April 10, 1986 notified Carter and the Tencos that if the terms of its agreement with them were not complied with, it would be seeking remedies against Carter and the Tencos on a joint basis.

19 On April 29, 1986 Hamilton by letter notified Carter and all of the Tencos that if any Tenco did not pay its share of the $89,802.20 (an earlier sum owing under the Agreement as set out in the March 31, 1986 cash call of $898,022.50), then Hamilton would sue to recover those amounts.

20 It was believed by Fox and by Claude that Hamilton had a reputation of being aggressive in its relationship with its trading partners. The Tencos were learning at this time in April of 1986 that Hamilton was adopting a more aggressive stance with respect to the rights it was claiming in its relationship with the Tencos.

21 This knowledge came to the Tencos primarily from Blair Fox. In addition to manag ing the properties forthe Tencos, he was as well responsible for looking after the Carter account. The Carter account reflected any residual monies due to or from the Tencos as working interest owners after the monies were distributed to the various accounts as set out in paragraph 8 of the Statement of Agreed Facts.

22 Fox gave evidence about the nature of the Management and Agency Agreement. I find it was the only agreement which governed his relationship with the Tencos' and which governed the Tencos relationship with each other and with Carter. It was the governing document for all the Tencos and all the Tencos conducted themselves as if it were in effect.

23 I mention all the foregoing to recognise the attitudes of the Tencos dealing with the monetary shortfalls on the royalty interest called by Hamilton prior to May 1, 1986. It was obvious that the Miscible Gas Flood project employed by Amoco was expensive. In turn Amoco in and around July of 1986 began withholding its revenues due to its fear that its operating expenses would not be paid. Hamilton, in turn, wished its royalty interest paid. The earlier cash call deficiencies by Hamilton were not being paid by all of the Tencos and Hamilton was threatening legal action. The Tencos were led to believe rightly or wrongly, that they could be held jointly and severally liable along with Carter to Hamilton if there was a deficiency due to non-payment of the cash calls.

24 Finally, on May 1, 1986 Carter was advised that $1,827,916.52 was owed to Amoco (see paragraph 13 of the Statement of Agreed Facts). Blair Fox, for Carter, and acting under the Management and Agency Agreement advised the Tencos that they each owed the sum of $132,264.95.

25 After Claude and Nucorr made their payments of $132,264.95 each to Royal Trust on or about May 5, 1986, a stalemate developed amongst the Tencos over the summer of 1986 as to the distribution of the $505,267.01 between Hamilton and Amoco and further what should be done regarding the fact that only Claude and Nucorr had made their payments. Accordingly Fox, on behalf

of Carter, prepared a proposed agenda and called a meeting for all the Tencos to be held on October 16, 1986 under the Management and Agency Agreement.

26 At the October 16, 1986 meeting all the Tencos were present. Blair Fox took minutes. As set out in the Statement of Agreed Facts the Tencos subsequently authorized the release of the $505,267.01 to Hamilton. More importantly for the issues in the case at bar the Tencos discussed the fact that Claude and Nucorr had paid the $132,264.95 required under the May 1, 1986 letter demand but none of the other Tencos had made their payment. Fox recorded the following in his minutes:

> How and When is the Additional $132 M Contributed by Each of Claude and Nucorr Equalized?
>
> - all Tencos present agreed that when there first becomes money allocable to the Carter Account, Claude and Nucorr receive all funds in equal proportions until they have each recovered their $132M; thereafter the funds are again split equally amongst all Tencos
> - the discussion acknowledged possible problems with the above if third parties with prior security (eg. Banks) intervened
> - a reduction of Amoco interest to Claude and Nucorr or, alternatively, interest income from the other eight Tencos was discussed, but the issue was left unresolved

27 Fox testified as well that he believed there was uniform agreement by the Tencos that Claude and Nucorr were owed $132,264.95 each and at some point they should get that money back, over and above whatever any other Tenco received. He indicated none of the other Tencos was willing to repay these funds immediately but there was agreement the repayment monies would have to come out of the properties. However, despite discussion, there was no agreement on whether Claude or Nucorr should receive interest on those funds until repayment.

28 Both Claude and Nucorr felt that they should be entitled to interest from the time they send the funds to Royal Trust until the date of the repayment. However the issue of repayment did not arise again until September of 1999 when the Plaintiff wrote a letter to the successors of the original Tencos advising them of its claim.

29 After Claude and Nucorr each paid their respective share for the $132,264.95 shortly after receiving the notice in the letter of May 1, 1986 from Carter, those two companies did not advance any further monies on behalf of the remaining Tenco companies who had not paid their $132,264.95 share.

30 The Plaintiff called Jonathan MacNeill who was a director of Claude and a director of the Plaintiff. He was an employee of Claude since 1983. He, as well, was a director and a subsequent president of Dix Management Ltd. It was the successor to Carter as the manager of the Tencos for the Tenco assets. He basically took over Blair Fox's role in 1989. MacNeill, as the president of Dix, managed the Tencos from 1989 under the Management and Agency Agreement. The Management and Agency Agreement governed the relationship amongst the Tencos and with Dix (as it did with Dix's predecessor - Carter).

31 He testified that Amoco began to make large cash calls to fund the miscible flood project. The Tencos were required to put up cash. When they did not, Amoco started withholding revenue which would normally be paid to the disbursing agent, Royal Trust, for distribution to the various accounts. With the Amoco hold back, shortfalls were created in the Hamilton Overriding Royalty ("HORR"). The Tencos had to make up these shortfalls or face the legal wrath of the royalty holder, Hamilton. MacNeill was concerned about the Tencos' potential joint and several liability to Hamilton. He noted as well that Claude's bankers were concerned about the bank security on Claude's share of the Tenco assets. Claude in turn worried the concerned bank would call in the loan agreement and realize on its security on those Claude assets.

32 He knew the May 1, 1986 letter from Carter demanding the $132,264.95 was sent under the Management and Agency Agreement. In turn Claude sent its cheque in response on May 5, 1986. The cheque was to be provided to Royal Trust for a specific account to pay Amoco.

33 MacNeill's testimony, on the October 16, 1986 meeting with all of the Tencos present and Blair Fox present, recalled that Claude's position was that it should not be overcontributing. Claude demanded that the eight defaulting Tencos pay their $132,264.95. The eight defaulting Tencos advised at that meeting they would or could not make those payments. He recalled that Claude and Nucorr wanted to receive their money back. Claude and Nucorr took the position that they had paid some money on behalf of the defaulting Tencos. He advised that the eight defaulting Tencos agreed to repay Claude and Nucorr in priority from the first monies available from the properties. He indicated there was no agreement reached on any interest payable on the Claude and Nucorr payments made on behalf of the defaulting Tencos.

34 However, he did testify that all the Tencos were aware that Claude and Nucorr had made a contribution on behalf of the defaulting Tencos. Originally he advised that it was not Claude's intention to make the $132,264.95 payment on behalf of the Tencos. Finally he indicated at the meeting Claude agreed to a postponement of its repayment.

35 McNeill noted that the disputed funds of $505,267.01, eventually through agreement by all parties, made its way into the hands of Hamilton. However, the two payments of $132,264.95 of Claude and Nucorr went to pay down the debt.

36 McNeill advised in his testimony that each month the Tencos would receive on the Disbursing Agent Instructions, a note advising there was still a deficit in the Carter or Hamilton Overriding Royalty account. As a result Claude knew its money would not be repaid for some time until there were funds allocable to the Carter account.

37 The monthly Disbursing Agent Instructions were initially prepared by Hamilton and then subsequently by BHP. It is now prepared by Guard Resources as the agent for the present Defendants.

38 He provided evidence that Claude acquired two further Tencos as a result of a settlement reached between it and Hamilton and the Bank of Montreal. Hamilton had obtained two judgments against all the Tencos on a joint and several liability basis in 1988 and 1989. Accordingly Claude entered into a settlement agreement with Hamilton and its banker, the Bank of Montreal, on April 26, 1989. The essence of this agreement forgave Claude's joint and several liability for the other remaining Tencos on the two law suits if Claude paid its share of the two law suits, kept current on the Hamilton Overriding Royalty deficiencies, and purchased two additional Tencos' assets at a set and pre-determined price from Hamilton and the Bank of Montreal. The latter was exerting pressure

on Hamilton because it had advanced monies to Hamilton on the original loan which allowed Hamilton to obtain the royalty interest. The latter interest was not performing to the expected standards due to the Amoco set off and the defaulting Tencos.

39 Claude purchased the assets of the Nucorr Tenco and the assets of a Tenco owned and controlled by Commercial Oil & Gas Ltd. Claude paid to Hamilton the royalty deficiency that Nucorr and Commercial owed to Hamilton and as well the amounts owing under the two law suits. Additionally it was agreed that if Claude fell behind on any future royalty deficiencies it would revert to a status of joint and several liability with the 7 remaining and defaulting Tencos. Claude remains current on these obligations at the trial date.

40 It was a further condition of the settlement agreement that Claude was required to transfer its interest in the 3 Tencos to the Plaintiff. That requirement was done at the request of the Bank of Montreal and Hamilton. The rationale behind this transfer was to allow the Bank of Montreal and Hamilton to have availability to all of the assets of those Tencos in the event that Claude ran into future financial difficulty. In such an instance Hamilton and the Bank of Montreal would be able to claim the shares of the Plaintiff in the event of any financial difficulties of Claude.

41 McNeill testified that neither Dix nor Claude received any notice of any bankruptcy or Bank Act security actions on or of any of the remaining Tencos.

42 Finally, he indicated Dix never received any notice from any of the Tencos that they were not bound by the Management and Agency Agreement or that the Management and Agency Agreement was not in force.

43 On September 8, 1999 Claude by letter to the 7 remaining successor Tencos demanded payment of the monies owing to it by the 7 Tencos, should those 7 Tencos interests be sold. No response was received by Claude.

44 From October 22, 1986 until September 8, 1999 Claude relied on the monthly Disbursing Agent Instructions which indicated there was still a deficit in the Hamilton Overriding Royalty account and which in turn indicated the monies were not yet due. Claude understood that as long and monies were due and owing to Hamilton on the Hamilton Overriding Royalty account that Claude would not be entitled to payment of the monies advanced to the Tencos.

45 At the date of the trial no monies had been paid by the Tencos or the Defendants to Claude or the Plaintiff on the monies outstanding as claimed by Claude and the Plaintiff.

46 Upon cross-examination MacNeill admitted in the conveyancing documents between Commercial and Claude, wherein Claude acquired the assets of Commercial, there was no mention of a contractual charge or an equitable lien or any encumbrance in favour of Claude on those assets. Further there was no mention by Claude prior to its letter of September of 1999 in any correspondence or documentation to any person or entity referring to a contractual charge or an equitable lien.

47 Neither Claude nor the Plaintiff at any time ever provided notice to any of the intervening purchasers of the assets of the 7 remaining Tencos of any contractual charge or claim of an equitable lien.

48 On further cross-examination MacNeill pointed out the footnote on the monthly Disbursement Agent Instruction sheets. It said:

NOTE: The cumulative deficit column does not reflect payments made by certain of the Tencos in respect of a proportionate percentage of the post-judgment deficits attributable to their interests in the properties subject to the Vendor's Royalty.

49 MacNeill indicated at the trial date the Plaintiff had no idea what made up the cumulative deficit. He disagreed with the cumulative deficit set out in the Disbursing Agency Instruction at January 29, 2001. The Plaintiff does not know the history or the basis of those calculations despite having requested it from Hamilton, BHP and Guard.

50 I note that none of the Defendants reviewed the Vendor's correspondence files as part of their due diligence when Superman and Omers purchased the royalty interests and 851479 and 1381351 purchased the working interests from Hamilton/BHP and the vendor Tencos. Prior to the closing of the purchase of those assets, the Defendants were made aware of the Plaintiff's claim. As well, the numbered company defendants were free to negotiate for indemnities or protections from the vendor Tencos in the asset purchase in respect of the Plaintiffs' claim. The numbered companies did not do that. Part of the purchase funds of the Defendants, Superman and Omers, went to pay out the Bank of Montreal. As a result the Bank of Montreal assigned its security to Superman and Omers. Superman and Omers now have the ability to act on that security to seize any assets of Claude and of any of the numbered companies who fails to make its payments on any monthly deficiencies on the Hamilton Overriding Royalty.

51 The Defendants called one Malcolm Coote, who is the vice-president of land at Guard Resources Ltd. Guard manages the oil and gas assets and maintains the accounting records for the Defendants, Superman and Omers. Superman and Omers are pension fund companies of the municipal employees of Manitoba and Ontario respectively. The Defendant, 851479, is a wholly owned subsidiary of Superman and the Defendant, 1381351, is a wholly owned subsidiary of Omers.

52 Coote is as well the vice-president of land for each of Superman, Omers, 854179 and 1381351.

53 In 1999 Guard on behalf of its clients, the Defendants, made an offer to purchase the working interests of the 7 remaining successor Tencos; an offer to purchase the Hamilton Overriding Royalty; and an offer to purchase the Bank of Montreal security interest held against the Hamilton Overriding Royalty and against the 7 Tencos' working interest. The offers were accepted. The numbered company Defendants became the owners of the Tencos' working interest assets which were subject to the Hamilton Overriding Royalty interest. Superman and Omers became the owners of the Hamilton Overriding Royalty interest. These asset purchases were split between the subsidiaries and the parent companies for the following reasons:

1. To keep any third party, who had a right of first refusal on the working interest, and who might wish to elect to exercise that first right of refusal, from obtaining the Hamilton Overriding Royalty interest in relation to that working interest. In effect this strategy would result in the obtained working interest standing alone and accordingly the Hamilton Overriding Royalty interest would remain with Superman and Omers. It would make it difficult and discouraging for a holder of the right of first refusal to exer-

cise that right of first refusal to acquire a working interest which would be subject to an approximately 70% royalty interest.

2. There was no reason to merge the royalty interest and the working interest into one company.
3. A desire to leave any tax and Alberta Royalty Tax Credit liabilities with the 7 vendor Tencos companies and not have these liabilities moved to the new numbered companies.
4. The litigation problems involving the case at bar. Guard wanted nothing to occur that would jeopardize whether or not the Hamilton Overriding Royalty was a legitimate claim.
5. The vendor Tenco companies had no assets after the sale to the numbered companies and as a result any representations or warranties by the Tenco companies would be of no value.

54 Doyle Bray has been an employee of Carter, a consultant to Carter, a consultant to BHP and now a consultant to Guard. Doyle Bray monthly prepares the Disbursing Agent Instructions. Bray prepared the Hamilton Overriding Royalty deficiency for the month of January of 2001and calculated it to be in the cumulative sum of $9,817,480.40.

55 In the same connection Coote drew my attention to a document called the 574095 Interparty Agreement (Exhibit 10) executed on November 30, 1994. It effectively stated:

> 574095 further acknowledges and agrees that it is liable on a joint and several basis for all past, present and future obligations of Claude in respect of the Vendor's Royalty (the total amounts owing to Hamilton and the Bank of Montreal under the Interparty Agreement) in the amount of $19,091,356.03.

56 The Defendants were aware of the alleged lien claim by the Plaintiff prior to the closing of their purchase of the various assets. The Defendants acknowledged that lien claim possibility in their closing purchase documents. However, the Defendants forged ahead with the purchase in the face of the Plaintiff's alleged lien claim.

57 The Defendant numbered companies have only one asset which is the working interest. The Defendant numbered companies effectively receive no revenues save and except a possibility of Alberta Royalty Tax Credits.

58 At the time of the purchase by Superman and Omers the companies were aware of the deficiency in the Hamilton Overriding Royalty account. It was a debt owed to BHP by the Tencos. It amounted to $12,000,000.00 approximately in October, 1999. However, Superman and Omers paid nothing for that receivable. The reason provided was that it would be just collectible from themselves. However, more importantly under the provisions of the Interparty Agreement, that receivable would also be collectible from Claude. It was the understanding of Guard and the Defendants that in the event that Omers and Superman forgave that debt to the two numbered companies then possibly that debt would be forgiven to Claude and the Plaintiff.

59 It should be noted further that the sale by the vendor Tencos of their working interest provided them with approximately $5,000,000.00. The vendor Tencos were able to distribute that sum without paying any money owing by them on the Hamilton Overriding Royalty cumulative deficiency.

60 Since the purchase the numbered companies have not made any deficiency payments to Superman and Omers on the occasions when there was a monthly deficiency in the Hamilton Overriding Royalty account. However, each and ever month when there was a deficiency in the Hamilton Overriding Royalty Claude made its deficiency payments.

CLAIM UNDER THE MANAGEMENT AND AGENCY AGREEMENT

61 The Plaintiff argued that a contractual lien was created by the advance of $132,264.95 each by Claude and Nucorr on May 5, 1986 pursuant to the Management and Agency Agreement. Section 4 of that agreement provides for the creation of a lien. Subsection 4(d) specifically defines how the granting of a charge and a lien is created.

62 Section 4 reads:

> (a) The Agent shall from time to time give notice to the Companies in the event that additional funds are required from the Companies in order to permit the development of the Sold Assets.
>
> (b) In the event that any of the Companies (the "defaulting Company") fails to make any additional deposit within thirty days of receipt of the notice referred to in Clause 4(a), or such longer period as may be specified in such notice, then the other companies (the "loaning Companies") may advance such amounts (the "make-up amounts") to the Agent pro rata or in such other proportion as they may agree upon, for and on behalf of the defaulting Company whereupon the defaulting Company becomes indebted to the loaning Companies in proportion to the make-up amount paid by the loaning Companies.
>
> (c) Any make-up amount paid by a loaning Company including interest on interest payable by the defaulting Company to the loaning Companies shall bear interest at a rate equal to 6% per annum in excess of the prime lending rate charged from time to time to commercial borrowers by the Canadian Commercial & Industrial Bank.
>
> (d) The loaning Companies to the extent of the make-up amount in respect of a defaulting Company shall be granted a charge and lien, subordinate to the charge and lien held by the Canadian Commercial & Industrial Bank, upon the participating interest of such defaulting Company until all payments in respect of the make-up amounts owed by the defaulting Company to the loaning Companies, together with accrued interest, are made in full in respect of the default in question. Should the circumstances so permit and should the loaning Companies so elect, they may obtain repayment of their make-up amounts plus accrued interest from the defaulting Company's share of distributed cash surplus with such repayments being credited pro rata initially against outstanding interest and thereafter against the make-up amounts.

63 A demand for payment of $132,264.95 from each Tenco was made by Carter under the Management and Agency Agreement on May 1, 1986. It was the only Agreement in full force and effect in May, 1986 that governed the relationship between the Tencos. Claude and Nucorr advanced the requested funds. None of the other Tencos paid the $132,264.95 that was requested. I am

satisfied on the evidence of Fox that the demand was made by Fox under the Management and Agency Agreement and not under any other agreement or some combination of agreements. The Tencos were operating under the Management and Agency Agreement and were bound by its terms. There is no provision for such demand under the Disbursing Agent Agreement. Indeed Hamilton, being a party to the Disbursing Agent Agreement, by its letter of October 22, 1986 took the position that it was not a party to any agreement as amongst the Tencos. Any dispute as to the amounts owing amongst the Tencos was a matter limited to the Tencos.

64 The $132,264.95 provided by Claude was advanced according to the evidence of MacNeill as additional funds initially required to meet Claude's obligation for the deficiency incurred by Amoco in the development of the working assets. The $132,264.95 was advanced by Claude and Nucorr under the provisions of s. 4(a) of the Management and Agency Agreement.

65 However, I disagree with the Plaintiff's argument that the funds of $132,264.95 were advanced under the provisions of s. 4(b) of the Management and Agency Agreement. This clause contemplates a loan by any other Tenco (the "loaning company") to a defaulting Tenco [(which had failed to provide its additional funds under s. 4(a).] The loan provided by the loaning company would be for funds over and above the additional deposit which the loaning company had advanced for its own behalf and obligation under s. 4(a). The $132,264.95 paid by Claude and Nucorr was paid by each on its own behalf pursuant to s. 4(a). Claude and Nucorr did not advance any further amounts (the make-up amounts) for or on behalf of the defaulting Tencos under s. 4(b). The $132,264.95 was not on May 5, 1986 intended to be a loan or additional deposit by Claude and Nucorr to the defaulting companies. The $132,264.95 was advanced by Claude and Nucorr in order to permit the development of the working assets, but was not advanced on behalf of the defaulting company under s. 4(b) on May 5, 1986. I note further that the funds were advanced by both Claude and Nucorr well before the expiry of the 30 days set out in Clause 4(b). The default by the defaulting Tencos did not occur until May 31, 1986. Under s. 4(b) it would be after May 31, 1986 before Claude or Nucorr could advance any further funds as "make-up amounts" so that the defaulting Tencos would become indebted to Claude or Nucorr. Under s. 4 only if a payment fulfills the three preconditions set out therein, is a lien created and which lien would carry a rate of interest at prime plus 6%. The failure of the $132,264.95 payment made by Claude and Nucorr under the three requirements of s. 4 and on the evidence adduced by MacNeill, means that such payments cannot be characterized as a payment under the Management and Agency Agree which gives rise to a contractual lien and its attendant interest rates. These payments were forwarded to Royal Trust by Claude and Nucorr for each of their respective share of the deficit and were not payments advanced on behalf of a subsequent defaulting Tenco. Prior to the meeting of October 16, 1986 each of Claude and Nucorr paid its share and its share alone. The defaulting Tencos did not take an advantage from the funds advanced over the time from May 5, 1986 until October 16, 1986. The Management and Agency Agreement did not create a lien or charge for Claude and Nucorr and the interest under that agreement did not come into effect. The evidence adduced by the Plaintiff did not demonstrate the payments by Claude and Nucorr created a lien under the provisions of s. 4(a) and s. 4(b) of the Management and Agency Agreement.

66 Having found that the funds were not advanced pursuant to the Management and Agency Agreement I now turn to the alternative argument whether 851479 and 1381351 have been unjustly enriched by the two payments made by Claude and Nucorr and as a result an equitable lien exists over the Tencos' assets. The working interest owners in the Tencos were tenants in common with respect to the assets. The Tencos held an undivided interest in the rights granted by the lease. An

interest in an oil and gas lease can be a registerable interest in land. A working interest is an incorporeal hereditament and is capable of being a registerable interest in land. Further an overriding royalty interest can, subject to the intention of the parties, be an interest in land. See the judgment of Major, J. in the Supreme Court of Canada in Bank of Montreal v. Dynex Petroleum Ltd., [2001] S.C.J. No. 70, 2002 SCC 7, File No: 27766.

67 It is noted that the Court has an inherent equitable jurisdiction to declare that properties or assets encumbered by an equitable lien are charged and encumbered with that lien. This declaration will occur where the relationship between the parties is such that one party is entitled to charge the property of another so as to fulfill the objects of a relationship. Equitable liens generally arise in any circumstances where the imposition of that lien performs equity between the parties.

68 The Plaintiff argues that the concept of unjust enrichment should be applied to establish an equitable lien in the absence of a lien being found to exist under the Management and Agency Agreement. It is necessary to look to the background and the facts surrounding the meeting of all the Tencos on October 16, 1986. Hamilton wished its royalty interests be paid. Eight of the Tencos had defaulted on the earlier cash deficiency call of May 1, 1986. Hamilton was threatening legal action. The Tencos were led to believe, rightly or wrongly, that they could be held jointly and severally liable along with Carter to Hamilton if there was a deficiency due to non-payment of the cash calls.

69 At the October 16, 1986 meeting Fox recorded the discussions and thoughts set forth by the Tencos. It was acknowledged that the proforma cash flows indicated a possibility of a long term overriding royalty deficiency. Fox suggested that the Tencos might wish to review their affairs and seek legal counsel specific to each's own specific circumstances. Generally the Tencos discussed Hamilton's potential actions in the face of the insufficient funds being to paid to cover the deficiencies. The Tencos acknowledged that Hamilton could obtain judgments and then realize on those judgments by seizing Tenco properties including other properties of the Tencos outside of the Hamilton Overriding Royalty properties. The Tencos as well discussed the possibility of their bankruptcies if Hamilton pursued the deficiencies. The Tencos by Hamilton's letter of April 10, 1986 were certainly aware of Hamilton's intention of commencing legal action if necessary.

70 I have no doubt that the Tencos believed prior to and during the October 16, 1986 meeting that there existed a serious risk of losing assets or the right to receive product form those assets. Although the law firm of Bennett Jones had proffered a legal opinion that Hamilton might not be able to actually call for a forfeiture of interest by the Tencos, there was a concern amongst the Tencos that Hamilton could obtain the Tencos interests after litigation. The evidence of Fox and MacNeill certainly recognized that Hamilton was an aggressive company which was not afraid to litigate and pursue its remedies. Claude had the added concern that action by Hamilton could result in Claude's bank realizing upon its security and causing a possible forfeiture of Claude's interest in any event.

71 On October 16, 1986 it was acknowledged by all the Tencos that Claude and Nucorr each had contributed $132,264.95 more than the defaulting Tencos. Accordingly it was recognized that Claude and Nucorr should not be over contributing to satisfy the Hamilton deficiencies. Claude and Nucorr, according to MacNeill, wanted the return of their contributions. It is most important to note that Claude and Nucorr took the position at the meeting that they had paid some money on behalf of the defaulting Tencos. In turn the defaulting Tencos were aware that Claude and Nucorr had made a contribution on behalf of the Tencos.

72 Although it was not Claude and Nucorr's original intention to make the $132,264.95 payment on behalf of the defaulting Tencos, that intention changed at the October 16, 1986 meeting. Fox's minutes of that meeting and his subsequent letter of October 21, 1986 on behalf of Carter acknowledged the $132,264.95 over contribution by each of Claude and Nucorr. The $505,267.01 disputed payment held at Royal Trust plus $10,717.41 interest thereon was directed by all of the Tencos to be released to Hamilton to reduce the liability owing on the Hamilton Overriding Royalty. The first two paragraphs of Carter's letter of October 21, 1986 to Royal Trust sets out the situation as follows:

> Claude Resources Inc. and Nucorr Petroleum Ltd. have each contributed $132,264.95 more than the other eight Tencos in recent months. Accordingly, the Tencos have agreed that the funds should be considered contributed as follows:

Nuccor Petroleum Ltd.	$157,410.41
209679 Oil & Gas Ltd.	25,145.45
Audax Gas & Oil Ltd.	25,145.45
Jennifer Petroleums Ltd.	25,145.45
Claude Resources Inc.	157,410.41
Commercial Oil & Gas Ltd.	25,145.45
LCR Resources Ltd.	25,145.45
Hawkness Equities Ltd.	25,145.45
Red Rock Resources Ltd.	25,145.45
Agassiz Resources Ltd.	25,145.45

$515,984.42

73 These funds made their way into Hamilton's hands on the basis of a recognition by the Tencos of the higher contribution by Claude and Nucorr as set out in the letter. These contributions were directly reflective of a payment made by Claude and Nucorr which certainly helped to stave off any legal action by Hamilton against the Tencos and their working interests due to the non-payment of the deficiencies by the eight defaulting Tencos.

74 It must certainly be recognized, that the payments by Claude and Nucorr, although made originally on their own behalf, changed in characterization at the October 16, 1986 meeting when it was acknowledged by all of the Tencos that the $132,264.95 contributed by each of Claude and Nucorr was a contribution on behalf of the defaulting Tencos. I find that this contribution went directly to pay down on behalf of all the Tencos some of the monies owed to Hamilton. It went to save the Tencos' working interests from a possible destructive realization by Hamilton. The payments were as well made for the benefit of all the Tencos in order to preserve their working interesst.

75 The Tencos were enriched by the payments. Their working interests were protected and their collective deficit amount owing to Hamilton under the Hamilton Overriding Royalty was reduced. Claude and Nucorr were deprived of the sums of $132,264.95 each once the characterization and

the nature of the payments changed as a result of the changed intentions of Claude and Nucorr and the Tencos at the October 16, 1986 meeting.

76 The original payment of May 5, 1986 was made by Claude and Nucorr under the compulsion of the Management and Agency Agreement. Those payments changed in nature and characterization at the October 16, 1986 meeting when the defaulting Tencos impliedly acknowledged that they had been unjustly enriched by the over contributions. The Tencos were unjustly enriched. Similarly Claude and Nucorr were correspondingly deprived. Finally, I can see no juristic reason for the unjust enrichment of the defaulting Tencos nor any juristic reason to deprive the Plaintiff. There was no contract or disposition of law for the enrichment. Claude and Nucorr were not required by a contract or by a disposition of law to enrich any of the defaulting Tencos. In answer to the Defendants' argument that there existed a juristic reason for the enrichment, I note that the key words are "for the enrichment". This phrase can only mean that there must be an absence of a juristic reason - such as a contract or disposition of law - for the enrichment. The word "for" contemplates the existence of a juristic reason at the time of the enrichment. It does not contemplate a subsequent agreement as to the time and manner when Claude and Nucorr would be entitled to their obvious overcontributions. Suffice to say, at the time of the unjust enrichment and deprivation there was no juristic reason why Claude and Nucorr would make these payments. Originally the payments were for Claude and Nucorr's own share of the deficiency. However, on October 16, 1986 the payments were made for the benefit of all the Tencos in order to preserve the working interests. There was no contract or disposition of law or any other juristic reason which required Claude and Nucorr to make those payments on the defaulting Tencos' behalf.

77 The Defendants made the submission in argument that there was a juristic reason for such enrichment, should it be found that the original Tencos were unjustly enriched. That juristic reason according to the Defendants' argument revolved around the fact that an agreement was reached at the October 16, 1986 meeting wherein the obligations of the defaulting Tencos created pursuant to the Claude and Nucorr payments were detailed in the meeting. I note that was an agreement as to the time, method and manner of repayment of the monies advanced. That agreement on the obligations occurred subsequent to the unjust enrichment. There was no agreement in place for repayment at the time of the unjust enrichment of the defaulting Tencos and the deprivation of Claude and Nucorr. There was no contract or disposition of law which provided juristic reason for Claude and Nucorr to enrich the defaulting Tencos to the corresponding deprivation of Claude and Nucorr.

78 Since 1980 with the decision of the Supreme Court of Canada in Pettkus v. Becker, 117 D.L.R. (3d) 257 the constructive trust has been clearly and unequivocally recognized as a general remedial device founded squarely on the principle of preventing an unjust enrichment. In the words of Dickson, J.:

> The principle of unjust enrichment lies at the heart of the constructive trust. "Unjust enrichment" has played a role in Anglo-American legal writing for centuries. Lord Mansfield, in the case of Moses v. Macferlan . . . put the matter in these words: ". . . the gist of this kind of action is that the defendant, upon the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money". It would be undesirable, and indeed impossible, to attempt to define all the circumstances in which an unjust enrichment might arise. . .. The great advantage of ancient principles of equity is their flexibility: the judiciary is thus able to shape these malleable principles so as to accommodate the changing

needs and mores of society, in order to achieve justice. The constructive trust has proven to be a useful tool in the judicial armoury.

79 I find the Plaintiff has demonstrated to me on the requisite standard of proof, beyond a balance of probabilities, that the three requirements as set out by Dickson, J. in the Pettkus v. Becker case supra have been met:

1. Unjust enrichment;
2. A corresponding deprivation;
3. Absence of any juristic reason <u>for</u> the enrichment (underlining mine).

80 See as well the cases of: Rathwell v. Rathwell, 83 D.L.R. (3d) 289; Peter Kiewit Sons' Company of Canada Ltd. et al v. Eakins Construction Ltd. 22 D.L.R. (2d) 465.

81 Accordingly the Plaintiff has demonstrated unjust enrichment on the basis of a constructive trust. The Plaintiff is granted an equitable lien on the working assets of the defaulting Tencos since October 16, 1986. The equitable lien extends to the whole undivided interest of the Tencos. In other words the equitable lien attaches to all of the assets covered by the Tencos' working interest. Each Tenco has 10% undivided interest in the assets as a whole and the equitable lien attaches to the assets as a whole. I note that the working interests are no longer in the hands of the defaulting Tencos and have, by their actions and certain intervenors' actions, been transferred to the hands of the Defendants, 1381351 and 851479. The Plaintiff is entitled to a charge on the working interests to secure payment of the contributions of Claude and Nucorr. The equitable lien can be enforced so as to ensure repayment of the monies advanced when there first becomes money allocable to the Carter account. The equitable lien does not become payable until monies become allocable to the Carter account.

82 Having found attachment of the equitable lien to the whole of the undivided interest of the Tencos working interests in the producing properties held under Crown and freehold leases, I now turn my attention to the applicability of the various defences raised by the Defendants

1. FAILURE OF CLAUDE AND THE PLAINTIFF TO MAKE A DEMAND FOR PAYMENT PRIOR TO SEPTEMBER, 1999

83 It was acknowledged that there was no demand made upon the Tencos for payment of the equitable lien debt between October, 1986 and September, 1999. However, the disbursing agent represented that funds were not allocable to the Carter account in the period. It is understandable why no demand for payment was made.

2. THE PLAINTIFF IS NOT A PROPER PARTY

84 Exhibits entered at trial, the evidence of MacNeill and the Statement of Agreed Facts and Appendix I thereto satisfy me that Claude purchased the assets of Nucorr. Nucorr's assets included its equitable lien attached to the whole of the undivided interests of the Tencos' working interests. Further I am satisfied that the Plaintiff acquired the rights and obligations owed to Claude and Nucorr. Claude and Nucorr's assets included the equitable lien attached to the whole of the other Tencos' working interests. The Plaintiff is a proper party to this action.

3. THE LAW OF SHELTERING

85 The Defendants argue that, if I hold the Plaintiff has the right to enforce an equitable lien against the working interests in the Tencos' assets, then the failure to register this equitable lien is fatal to the Plaintiff's cause. Equity favours a bona fide purchaser for value. If a lien has not been registered by a party, then a bona fide purchaser for value without notice obtains title to the interest free and clear of any charge which may or may not have existed. The Defendants point out that the Plaintiff has admitted no notice of its equitable lien was given to any of the intervening purchasers of the Tenco assets from the original 1986 Tencos. The Defendants argue that each of the subsequent intervening purchasers obtained the working interests free and clear of notice of any lien or charge that Claude or Nucorr may have possessed against such working interests. The Defendants point out that Schedule II to the Statement of Agreed Facts provides a list of the various purchasers of the Tenco assets. The Defendants argue that each of the interests in the Tenco assets acquired by them were acquired from an intervening purchaser without notice of the Plaintiff's equitable lien. Therefore the Defendants further argue that they obtained the same interests of the intervening purchaser even though the Plaintiff registered its equitable lien on the eve of closing of the Defendants' purchase of the assets. This is known as sheltering. The purpose of the doctrine of sheltering is to protect the interests of a bona fide purchaser for value from the registration of charges of which it had no knowledge and which would adversely affect his or her ability to sell such an interest at a price commensurate with the value (ie. an unencumbered interest) for which it paid for the interest.

86 The doctrine is succinctly stated in "Snell's Equity" 30th Edition by John McGhee at page 60:

> The protection of the doctrine of purchaser without notice extends to any person who claims through such a purchaser, unless that person was himself previously bound by the equity. Thus a purchaser with notice of an equitable interest will nevertheless not be bound by it if he purchases from a person who himself was a purchaser without notice. Here the second purchaser can shelter under the first purchaser, because otherwise a bona fide purchaser might be unable to deal with his property, and the sale of the property would be clogged. But a trustee cannot defeat the equities of his beneficiaries by selling the trust property to an innocent purchaser and then buying it back.

87 The Defendant submitted that it is for the Plaintiff to prove its case. They submitted that the Plaintiff failed to provide evidence proving that its equitable lien is capable of following the chain of purchasers to reach the Defendants. The Defendants point out that there was no notice of equitable lien provided by Claude, Nucorr or the Plaintiff to any intervening purchasers.

88 I agree that there was no such notice from Claude, Nucorr or the Plaintiff to any intervening purchasers. However, there was no evidence placed before me that these intervening purchasers did not have notice of the debt or the circumstances and nature of the debt (ie: the equitable lien) owing to Claude and Nucorr. A lack of notice from the lien holder does not eliminate knowledge by the intervening purchasers. The intervening purchasers could have received notice from other sources other than Claude, Nucorr or the Plaintiff. The Defendants plead lack of notice by the intervening purchasers and it is required that it be established before me that these intervening purchasers received no notice. Proving lack of notice by Claude, Nucorr or the Plaintiff to the intervening purchasers is only one-half the step of demonstrating no notice. To me the remaining one-half step would be to establish a lack of notice by the intervening purchasers. That proof of lack of notice could come from a variety of sources including perhaps the intervening purchasers. Claude, Nucorr

and the Plaintiff's lack of notice to the intervening purchasers does not mean that the intervening purchasers had no notice. Claude, Nucorr and the Plaintiff are only one possible source of that notice. The intervening purchasers could have received this notice from other sources. No evidence was proffered to demonstrate a lack of knowledge of notice by the intervening purchasers. I am not able to speculate that these intervening purchasers had no notice of the equitable lien or the circumstances and nature of the equitable lien from other sources. This lack of evidence demonstrating that the intervening purchasers had no notice whatsoever of the equitable lien from other sources other than Claude, Nucorr or the Plaintiff means the Defendants have failed to establish this defence. There is no evidence before me that the intervening purchasers were bona fide purchasers for value without notice.

89 Thus in light of my findings with respect to the notice of the intervening purchasers, there is no need for me to determine if I do accept the applicability of the doctrine of sheltering in Canada.

THE CURTAIN PRINCIPLE UNDER SECTION S 195 and 66 OF THE ALBERTA LAND TITLES ACT being chapter L4 of the 2000 REVISED STATUTES OF ALBERTA

90 The Defendants argue:

> Finally, the Alberta Land Titles Act contains sections 66 and 195 which act to protect purchasers from unregistered charges or liens. The curtain principle, in essence, upholds the sanctity of the registration system by preventing a party from asserting an unregistered charge against a person, who has acquired the interest in question.
>
> As stated at page 247, Wharton v. Smerychynski, 78 Alta. L.R. (3d) 231:
>
>> The "curtain" principle ensures that a person who wishes to acquire an interest in land can rely on the register to determine the existing interests in land. It is given legislative expression in s. 195 of the Land Titles Act which reads as follows:
>>
>> (2) A person contracting or dealing with or taking or proposing to take a transfer, mortgage, encumbrance, lease or other interest from an owner is not, except in the case of fraud by that person,
>>
>> (a) bound or concerned, for the purpose of obtaining priority over a trust or other interest that is not registered by instrument or caveat, to inquire into or ascertain the circumstances in or the consideration for which the owner or any previous owner of the interest acquired the interest or to see to the application of the purchase money or any part of the money, or
>> (b) affected by any notice, direct, implied or constructive, or any trust or other interest in the land that is not registered by instrument or caveat, any rule of law or equity to the contrary notwithstanding.

> (3) The knowledge of the person that any trust or interest that is not registered by instrument or caveat is in existence shall not of itself be imputed as fraud.

> The curtain principle when examined in conjunction with section 66(2) of the Land Titles Act precludes Defendants from liability even if the Plaintiff is able to prove it has an equitable lien or charge. Sections 66 of the Land Titles Act reads as follows:

> 66(1) Every certificate of the title granted under this Act (except in case of fraud wherein the owner has participated or colluded), so long as it remains in force and uncancelled under this Act, is conclusive proof in all courts as against Her Majesty and all persons whomsoever that the person named therein is entitled to the land included in the certificate for the estate or interest therein specified, subject to the exceptions and reservations mentioned in section 65, except so far as regards any portion of land by wrong description of boundaries or parcels included in the certificate of title and except as against any person claiming under a prior certificate of title granted under this Act or granted under any law heretofore in force relating to titles to real property in respect of the same land.
>
> (2) For the purpose of this section, that person shall be deemed to claim under a prior certificate of title who is holder of or whose claim is derived directly or indirectly form the person who was the holder of the earliest certificate of title granted, notwithstanding that the certificate of title has been surrendered and a new certificate of title has been granted on any transfer or other instrument.

> The Defendants obtained their right to the Tenco Assets through parties who acquired their right absent the registration of the Plaintiff's charges. Pursuant to section 195 the Intervening Purchasers as listed in Schedule II to the Statement of Agreed Facts would obtain the Tenco Assets free and clear fo the Plaintiff's charge. Further, pursuant to section 66(2) the Defendants assumed the same title to the Tenco Assets as was held by the Intervening Purchasers. Hence by operation of section 66 and 195 of the Land Titles Act, the Defendants purchased title to the Tencos Assets free and clear of any lien or charge of the Plaintiff.

That is the essence of the Defendants' argument.

91 Assuming that Sections 195 and 66 apply to the transfers of the royalty and working interests acquired by the Defendants in their respective capacities, I note the following. The intervening purchasers as listed in Appendix II to the Statement of Agreed Facts would appear not to be affected by any notice, direct, implied or constructive, of any trust or other interests by Claude, Nucorr or the Plaintiff in the land that is not registered by instrument or caveat. From the interpretation of sections 195 and 66 the intervening purchasers would under the Land Titles Act obtain the Tenco assets free and clear of the Plaintiff's charge.

92 However, the Defendants and each of them had express notice of the Plaintiff's claim by at least the date of October 28, 1999 and before the closing of the Defendants' purchase. With the caveats having been registered by the Plaintiff at the Land Titles Office on October 28, 1999 the Defendants do not assume the same title to the Tenco assets under s. 66(2) of the Land Titles Act as was perhaps held by the intervening purchasers. Further the Defendants obtained title to the interest subject to the lien and/or the registered caveats of the Plaintiff. Seciton 195 of the Land Titles Act deals specifically with unregistered interests.

93 Having reached the aforesaid finding, I will not deal further with the issue as to whether sections 195 and 66 of the Land Titles Act are applicable to the royalty and working interests which were conveyed to the Defendants.

LIMITATIONS

94 An equitable lien exists and is not payable until funds are allocable to the Carter account. Any limitation period does not commence until the date that the debt obligation becomes payable. At the time the funds become allocable to the Carter account, the debt becomes payable and the lien becomes enforceable. The payments by Claude and Nucorr did not create mere debt, but instead created an equitable lien. A limitation defence does not exist.

LACHES

95 The Defendants argue that if an equitable lien exists, it is barred by the doctrine of laches.

96 However, Claude, Nucorr and the Plaintiff have demonstrated good faith since 1986 in wiating for the funds to be allocable to the Carter account. They demonstrated no unreasonable delay or acquiescence which would render it inequitable to enforce the lien. Any delay is attributable to the funds becoming allocable to the Carter account. Those circumstances are not unreasonable or unjust. There was no waiver or any agreement by Claude, Nucorr or the Plaintiff to abandon or release the claim. Claude, Nucorr and the Plaintiff did not act to induce the Defendants to alter their position on reasonable faith that the claim had been released or abandoned.

97 I see no facts which lead me to conclude there has been any destruction or loss of evidence by which the claim might have been rebutted by the Defendants.

98 In summary, there is no evidence to indicate that the Defendants have been prejudiced in the defence of this action by the passage of years. The Defendants' only complaint is that the Plaintiff's witnesses have a clouded memory or no memory of the key issues in 1996. In that it is up to the Plaintiff to prove its case that lack of memory would strike at the heart of the Plaintiff's case more than the Defendants' case. There was no submission made, which I accepted, that the Defendants' case was in any way prejudiced. The Defendants were unencumbered in the ability to investigate the background of the claim.

99 All the Tencos agreed that Claude and Nucorr's claim would not be payable until there were monies allocable to the Carter account. Claude, Nucorr, the Plaintiff and the Tencos all awaited this event. If anything, the vendor Tencos benefited in that they had the use of the Claude and Nucorr funds a good number of years.

100 Claude, Nucorr and the Plaintiff were not guilty of a lack of due diligence. Any defence based on laches fails.

BANK ACT SECURITY

101 The Defendants submit that a sale under s. 177 of the Bank Act, R.S.C. 1985, c.B-1, extinguishes any charge registered upon the interest being sold pursuant to the enforcement of a Bank Act Security. Upon this realization of Bank Act Security at best, a party possessing an equitable lien could acquire a charge on the equity of redemption. Mr. Justice Mason in the case of Hamilton Bros. Corp. v. Royal Trust Corp. of Canada, [1991] A.J. No. 12, held a Bank Act Security effectively transfers to the bank the beneficial interest in petroleum and natural gas rights and the working interest in those producing wells subject to the equities of redemption. As a result of that decision the Defendants argue that all subsequent encumbrances attach only to the equities of redemption and so any charge on the assets of 209679 Oil & Gas Ltd. was extinguished by the 1992 Bank Act Security sale to 520027 Alberta Ltd. [See the chain of titles set out in Schedule 6 of Appendix II in the Statement of Agreed Facts.

102 It would appear that any charge on the assets of 209679 Oil & Gas Ltd. was extinguished under the s. 177 sale by the Bank of Montreal.

103 However, I found that the equitable lien created in 1986 was a charge upon the entire undivided interest in the rights granted by the leases. Each of the original Tenco companies held 10% of the undivided interest as tenants in common.

104 Although the charge on the assets of 209679 Oil & Gas Ltd. might have been extinguished by the s. 177 sale, the equitable lien remained in effect against the whole undivided interest. As well the equitable lien still remained a charge against the interests of 206218 Oil & Gas Ltd., RGO Investments Ltd., 212873 Oil & Gas Ltd., 212634 Oil & Gas Ltd. and LCR Resources Ltd. Each of these companies transferred its assets on the chain of title as set out in Appendix II and the specific schedules thereto to the Defendant numbered company purchasers, namely 581479 and 1381351. The Defendant numbered companies are now the owners of the undivided working interest assets which are subject to the equitable lien. Thus it is moot whether an equitable lien charge against the assets of 209679 Oil & Gas Ltd. has been extinguished under the s. 177 sale.

BANKRUPTCY

105 The Defendants submit as well the bankruptcy of Trapper Resources Ltd. [originally the assets of 212397 Oil & Gas Ltd. as set out in Schedule 7 of the Appendix II in the Statement of Agreed Facts and transferred to Trapper Resources Ltd.] would extinguish any unregistered equitable lien

106 Again although the equitable lien charge on the assets of Trapper Resources Ltd. might have been extinguished by the company's bankruptcy, the equitable lien remained in effect against the whole undivided working interest. Then too, the equitable lien still remained a charge against the interests of the 5 companies enumerated in the prior paragraph. Again with the findings and the reasoning set out in the prior paragraph the 2 Defendant numbered companies are now the owners of the undivided working interest assets which are subject to the equitable lien. Again in these circumstances it becomes moot whether any charge generated by any equitable lien on the assets of Trapper Resources Ltd. has been extinguished.

107 I have found that the equitable lien has not been defeated by any of the defences advanced by the Defendants. It now becomes necessary to determine when the equitable lien becomes payable. All parties in argument recognize that the agreement amongst all the Tenco companies was that Claude and Nucorr agreed to postpone the enforcement of their lien rights. The Defendants, of course, argued that the postponement was not in relation to a lien but was instead a postponement of

the debt owing to Claude and Nucorr by the defaulting Tencos. However, I have held that the post-ponement was one of an equitable lien.

108 All parties agree that the "trigger event" in this postponement occurs when "there first becomes money allocable to the Carter account". [Minutes of Fox at the October 16, 1986 meeting].

109 The Plaintiff argued that when Superman and Omers and the Defendant numbered companies in effect purchased both sides of the Hamilton Overriding Royalty debt, they are keeping this Hamilton Overriding Royalty debt artificially in existence. By keeping this Hamilton Overriding Royalty debt in existence, there will not be any monies allocable to the Carter account (at least for a number of years to come) and the Defendants will not have to pay for those years the Plaintiff any monies due under the equitable lien.

110 In order to appreciate that argument it is necessary to review the evidence pertaining to the situations both before and subsequent to the purchase of the Tencos assets and working interests by 851479 and 1381351 and the purchase of the Hamilton Overriding Royalty and the Bank of Montreal security by Superman and Omers.

111 Prior to the purchase the vendor Tencos and Claude were paying off the Hamilton Overriding Royalty cumulative deficit to Hamilton/BHP and indirectly the Bank of Montreal with any monies accruing monthly to the Carter account in accordance with the distribution plan detailed in paragraph 8 of the Statement of Agreed Facts.

112 851479 and 1381351 paid approximately $5,000,000.00 to the vendor Tencos for the assets and working interests. 851479 and 1381351 are not responsible for the debt obligations of the vendor Tencos owed prior to the closing date of purchase. 851479 and 1381351 are only liable for obligations in respect of the vendor Tencos assets arising from and after the closing date of the purchases. However, the debt owed by the vendor Tencos regarding the Hamilton Overriding Royalty deficiency was not extinguished. Rather under s. 7 of the Assignment and Novation Agreement signed by all of the vendor Tencos and all of the Defendants in the sale and purchase of all of the various assets, it was stated:

> The parties acknowledge that Superman and Omers have acquired the right to receive any unpaid amount which have accrued in respect of the CLORI (the Hamilton Overriding Royalty)(brackets mine) and nothing contained herein shall restrict its rights to collect such amounts from 851479 and 1381351 as owners of the lands to which the CLORI (the Hamilton Overriding Royalty) relates.

113 Thus Superman and Omers can receive from 851479 and 1381351 monies for the unpaid amount owing prior to the sale and purchase on the Hamilton Overriding Royalty.

114 As part of their purchase of the Hamilton Overriding Royalty Superman and Omers caused the Bank of Montreal to accept a reduced amount for payout of its security interest held against the various assets. That security interest, amongst other things, covered the account receivable of 12 million dollars approximately owned by Hamilton/BHP at October, 1999 on the Hamilton Overriding Royalty cumulative deficit. Coote gave evidence that Superman and Omers in effect paid zero dollars for that Hamilton/BHP account receivable when they purchased the Hamilton Overriding Royalty. Coote indicated that Superman and Omers paid nothing for a 12 million dollar account receivable because that account receivable would be collectible from themselves and possibly from

Claude in the event Claude defaulted under the provisions of the November 30, 1999 Interparty agreement.

115 The result of the purchase of the various assets by the Defendants can be enumerated as follows:

1. 851479 and 1381351 receive no revenue stream at the present save and except a possibility of some Alberta Royalty Tax Credit payments.
2. 851479 and 1381351 are not responsible for any mere debt obligations of the vendor Tencos owed prior to the date of the sale and purchase of the assets and working interests of the vendor Tencos.
3. 851479 and 1381351 can be held responsible by Superman and Omers for any unpaid amounts which have accrued in respect of the CLORI or Hamilton Overriding Royalty cumulative deficiency.
4. The vendor Tencos, although they still have a debt position to various parties incurred prior to the closing of the purchase and sale, received $5,000,000.00 and were free to distribute that $5,000,000.00 after the sale.
5. Superman and Omers purchased the CLORI or Hamilton Overriding Royalty asset from Hamilton/BHP. As part of the transaction the Bank of Montreal for a reduced payment to it by the vendors released its security interest on the various assets held by the vendor Tencos and Hamilton/BHP. In turn the Bank of Montreal assigned its security interests to Superman and Omers. In the purchase of the Hamilton Overriding Royalty by Superman and Omers there was of course an approximate $12,000,000.00 account receivable owed by the vendor Tencos and Claude to Hamilton/BHP. Superman and Omers paid zero dollars for that account receivable in the purchase.
6. Superman and Omers own the account receivable respecting the cumulative deficit due under the Hamilton Overriding Royalty or the CLORI. Superman and Omers have the right to collect that account receivable from 851479 and 1381351 (their subsidiary companies). As well Superman and Omers can collect that account receivalbe from Claude, should Claude default under the provisions of the November 30, 1984 Interparty agreement.
7. Superman and Omers collect the monthly payments from 851479 and 1381351 in accordance with Paragraph 8 of the Statement of Agreed Facts. When there is a monthly surplus, that reduces the deficit owing on the Hamilton Overriding Royalty or CLORI. When there is a monthly deficiency on the Hamilton Overriding Royalty or CLORI, Superman and Omers do not collect that deficiency from 851479 and 1381351.
8. Claude receives any monthly surplus under the provisions of the monies distributed under Paragraph 8 of the Statement of Agreed of Facts.
9. If there is a monthly deficiency on the Hamilton Overriding Royalty or the CLORI account in accordance with Paragraph 8 of the Statement of Agreed Facts, Claude must pay that deficiency amount.
10. Claude to the time of trial had not defaulted under the terms of the 1984 Interparty Agreement.

11. Generally the cumulative deficiency of the Hamilton Overriding Royalty or the CLORI has been steadily diminishing over the last few years.
12. Superman and Omers do not wish to forgive the debt due under the Hamilton Overriding Royalty cumulative deficiency from 851479 and 1381351. In effect to do that might have the possibility of forgiving Claude, any debt due under the Hamilton Overriding Royalty deficiency under the provisions of the 1984 Interparty Agreement. Under that agreement if Claude failed to pay a monthly deficiency on the Hamilton Overriding Royalty or CLORI then Claude would be liable on a joint and several basis for the whole cumulative Hamilton Overriding Royalty or CLORI deficiency.

116 In effect Superman and Omers control both sides of the Hamilton Overriding Royalty or CLORI cumulative debt. They own the account receivable [ie the unpaid amount owing under the Hamilton Overriding Royalty or CLORI]. They receive monthly payments if there is a surplus of funds provided to the working interest owners. However they only receive monthly payments by Claude alone if there is a monthly deficiency on the Hamilton Overriding Royalty or CLORI.

117 Bearing in mind the 5 reasons set out previously in paragraph 53 of this Judgment and further bearing in mind the reasons set out in paragraph 58 of this Judgment I find that the debt is being artificially kept in existence by the actions of the Defendants. Superman and Omers recognize [on the evidence of Coote] that the account receivable in the Hamilton Overriding Royalty agreement prior to October 29, 1999 is now a debt collectible from themselves. The overriding reason for keeping that debt alive is to keep Claude potentially liable for payment of the total deficiency under the 1984 Interparty Agreement (should Claude default). As well by keeping that debt alive it can be argued strongly that there are no monies allocable to the Carter account and hence the Plaintiff cannot enforce the payment of the equitable lien. The first three reasons set out in paragraph 53 would not come into play at this time or any future time if the debt was forgiven by Superman and Omers to their respective subsidiaries, 851479 and 1381351. Reason 4 in paragraph 53 and the potential liability of Claude are the primary reasons why Superman and Omers are keeping that debt in existence.

118 The Plaintiff finally argued that if I found that there are possibly funds owing on the Hamilton Overriding Royalty deficiency, then 851479 and 1381351 are not entitled to rely on that deficiency to operate as a bar to the Plaintiff enforcing its equitable lien rights due to the principle of self-induced frustration. Self-induced frustration exists when a party creates an artificial scenario for the express purpose of frustrating the intent of the agreement. The Plaintiff cited the following 2 authorities in support of its submission:

1. Haupt v. Westcott (1980), 116 D.L.R. (3d) 585, rev'd (1981), 140 D.L.R. (3d) 573 [Alberta C.A.].
2. Steiner v. EHD Investments Ltd. (1977) 78 D.L.R. (3d) 449 [Alberta C.A.].

The Plaintiff further submitted that Superman and Omers entirely in their own discretion, despite having the financial solvency to do so, have decided not to pay off or write off the debt owed by 851479 and 1831351 to them, for the sole purpose of avoiding paying this obligation to the Plaintiff.

119 At the present time and under the present circumstances I agree with the Plaintiff's last submission on this point.

120 However, the Defendants argued that:

> The concept of self induced frustration is based upon the existence of an agreement between two parties which contains a provision stating that the contract is void upon the occurrence of a certain event in control of the parties to the contract. The Courts have found that if the event which voids the contract is under the control of one of the parties through its acts or omissions, then the party who by its act or omission brings about the voiding event cannot be permitted to rely upon the voiding provision to avoid performance under the contract.

121 In this context the Defendants argued that the Plaintiff failed to provide any evidence of a contract which existed between the Defendants and the Plaintiff. In the absence of such a contract the Defendants submitted that the principles of self-induced frustration have no application.

122 Yet Claude, Nucorr and the defaulting Tencos entered into discussion on October 16, 1986 which resulted in the creation of an equitable lien. Its enforcement was postponed until the date when funds were allocable to the Carter account. The Plaintiff and the Defendant numbered companies due to the creation of that equitable lien and its postponement are now successors to that agreement. The Defendant numbered companies are successors due to their purchase of the working interests assets with the equitable lien attached from the vendor Tencos.

123 Thus there is privity of contract between the Plaintiff and the numbered companies. The numbered companies are respective subsidiaries of the Defendants, Superman and Omers. By the creation of two sets of companies, (Superman and Omers and the numbered companies) the debt at this time is being artificially kept alive. I am mindful that Superman and Omers and the two numbered companies are all separate legal entities. But due to the same directors being involved in these companies and the subsidiary relationship existing, I am satisfied that Superman and Omers could forgive this debt to the two numbered companies. They choose not to do so and I am accordingly convinced it is being artificially kept in existence to avail Superman and Omers of the opportunity to pursue Claude and the Plaintiff should Claude fail in its obligations under the 1984 Interparty Agreement.

124 In these overall circumstances wherein Superman and Omers paid nothing to acquire the Hamilton Overriding Royalty deficiency account receivable; and in looking at the relationship between Superman and Omers and their respective subsidiaries; and finally the fact that the Hamilton Overriding Royalty deficiency debt could be retired save and except for the desire by the Defendants to keep the debt alive and thus not trigger the repayment of the equitable lien to the Plaintiff, I find that monies presently could become allocable to the Carter account. The debt is being artificially kept alive and this "triggers" the repayment of the equitable lien.

125 Accordingly the Plaintiff shall have judgment against the Defendants and each of them for the sum of $185,170.93 owing under the equitable lien.

126 In the alternative, if I am incorrect in my finding that the monies now could become allocable to the Carter account, then I find that the Plaintiff is entitled to an Order for Judgment for the outstanding amount of $185,170.93 owing under the equitable lien payable once money becomes allocable to the Carter account.

127 Further in that alternative context, due to the uncertain nature of the accounting method used in the calculation of the Carter account, and bearing in mind all of the evidence adduced at the trial and in particular the memory of Bray and the footnote in the monthly Disbursing Agent Instructions, I order an accounting to be carried out to determine the exact amount of the shortfall in the Carter account by each Tenco. I note that the Defendants in the submissions of their counsel before me have agreed that they are quite willing to help the Plaintiff and the Court understand the Carter account allocation if I should find against the Defendants and hold, (which I did) that the Plaintiff has an enforceable lien. The costs of any such accounting, if carried out, shall be borne 70% by the Defendants jointly and 30% by the Plaintiff. I give leave to any of the parties to seek advice and direction from me on any issues arising from the necessity and/or procedure for such an accounting.

128 If the alternative remedy of my Order for an accounting is utilized, then the Plaintiff will be entitled to a judgment for $185,170.93 once any accounting establishes that there are monies allocable to the Carter account.

129 Finally I must deal with the issue of interest arising out of the equitable lien. I note that Claude and Nucorr initially sent their respective payments of $132,264.95 in May of 1986 to satisfy their own obligations. At the meeting of October 16, 1986 the intentions of the various parties changed. All of the Tencos acknowledged and impliedly agreed that Claude and Nucorr were advancing the monies of behalf of all of the Tencos. That meant the funds benefited the defaulting Tencos at October 16, 1986. Accordingly interest will be payable on the sum of $185,170.93 under the Judgment Interest Act, being chapter J-1 of the 2000 R.S.A., from October 16, 1986 to the date of Judgment. Counsel have set out in the Statement of Agreed Facts that amount of interest from October 16, 1986 to January 1, 2001 is $175,293.43. Counsel will calculate any additional amount of interest under that statute until the date of judgment, or until funds become allocable to the Carter account should I be incorrect on my finding that repayment of the equitable lien has been triggered due to the artificiality of the debt.

130 Counsel are requested to make an appointment with me for the purpose of making representations on the matter of costs.

PARK J.

cp/e/qldrk/qlcas/qlhjk

2

Case Name:

CIBC Mortgages Inc. (c.o.b. Firstline Mortgages) v. Computershare Trust Co. of Canada

Between
CIBC Mortgages Inc., Trading as Firstline Mortgages, Applicant, and
Computershare Trust Company of Canada, Respondent
And between
Computershare Trust Company of Canada, Applicant, and
CIBC Mortgages inc., Trading as Firstline Mortgages and the Director of Titles pursuant to s.57(14) of the Land Titles Act, Respondents
And between
Secure Capital Mic Inc., Applicant, and
CIBC Mortgages Inc., Trading as Firstline Mortgages and Computershare Trust Company of Canada and the Director of Titles pursuant to s.57(14) of the Land Titles Act, Respondents

[2015] O.J. No. 403

2015 ONSC 543

Court File Nos.: 3218/13, 4301/13 and 5501/13

Ontario Superior Court of Justice

J.C. Murray J.

Heard: October 16, 2014.
Judgment: January 23, 2015.

(67 paras.)

Counsel:

Benjamin Frydenberg and Sam Rappos, for the Applicant.

Christine Jonathan, for the Respondent.

Christine Jonathan for the Applicant.

Benjamin Frydenberg and Sam Rappos, for CIBC Mortgages Inc., and Jonathan Sydor for the Director of Titles.

Bobby Brykman, for the Applicant.

Benjamin Frydenberg and Sam Rappos, for CIBC Mortgages Inc., and Jonathan Sydor for the Director of Titles.

REASONS FOR JUDGMENT

J.C. MURRAY J.:--

CIBC Mortgages Inc. Trading as FirstLine Mortgages and Computershare Trust Company of Canada.

1 In this application, the applicant CIBC Mortgages Inc. trading as FirstLine Mortgages (hereinafter "CIBC") seeks, *inter alia*, the following:

a. an order declaring that the CIBC mortgage granted by the Lowtans against the property municipally known as 40 Chipmunk Crescent, Brampton Ontario securing the sum of $252,800 and registered on title on July 28, 2011 as instrument number PR2045899 is of full force and effect and constitutes a valid and effective first ranking charge against the property;

b. an order declaring that the CIBC mortgage has priority over the Computershare mortgage;

Computershare Trust Company of Canada and CIBC Mortgages Inc., trading as FirstLine Mortgages

2 In its application, the applicant, Computershare Trust Company of Canada (hereinafter "Computershare") seeks, *inter alia*, the following:

a. a declaration that the discharge registered on August 26, 2009 on title to the property municipally known as 40 Chipmunk Crescent in Brampton, Ontario (hereinafter "the property") and known by instrument number PR1692570 is a fraudulent instrument and correspondingly void and of no force or effect.

b. rectification of the register for the property restoring the charge granted in favor of Computershare as chargee registered on November 21, 2008 and known by instrument number PR1571875 (the "Computershare charge") in first priority to all other charges/charges on title to the property registered after November 21, 2008.

c. a declaration of the Computershare charge as the first charge on the property.

d. An order directing the Director of Titles to rectify the register relating to the property deleting instrument number PR1692570 and restoring the Computershare charge as if the discharge had not been registered.

Secure Capital MIC Inc. and CIBC Mortgages Inc., trading as FirstLine Mortgages and Computershare Trust Company of Canada and Director of Titles Pursuant to Section 57(14) of the Land Titles Act.

3 In the application brought by Secure Capital MIC Inc. (hereinafter "Secure Capital") seeks, *inter alia*, the following:

a. a declaration that the mortgage granted by the Lowtans to Secure Capital securing the amount of $32,000 and registered against title to the property on December 11, 2012 as instrument number PR230945 is the second ranking charge on the property ranking behind the CIBC charge.

4 These three applications were heard together. All three applications are brought by secured lenders seeking a determination of priorities of their respective charges registered against the property owned by Dhanraj and Sumatie Lowtan.

Facts

5 Dhanraj Lowtan and Sumatie Lowtan (the "Lowtans") owned the property known as 40 Chipmunk Crescent in Brampton, Ontario (hereinafter "the property"). The legal description of the property is as follows:

PCL BLOCK 396-7, SEC 43M1026; PT BLK 396, PL 43M1026.

PARTS 11, 43, 44, 53 & 54, 43R19433

City of Brampton, Regional Municipality of Peel

PIN 14303-0457

6 The Lowtans applied to Computershare for a loan to be secured by a first charge on the property. The proceeds of the loan were be used to refinance existing charges on the property. After the charge loan was approved, the principal amount of $280,801.95 was advanced. The majority of funds were used to pay off previous charges registered on title to the property in favor of the Bank of Montréal and CitiFinancial Canada Inc. Coincidental with the advancing of the funds, a charge was registered on title to the property in favour of Computershare on November 21, 2008 as instrument number PR1571875 (the "Computershare charge"). When the discharge of the charges in favor of the Bank of Montréal and CitiFinancial Canada Inc. were registered, the Computershare charge was the first charge on the property. Part of the charge loan agreement permitted the monthly payments to be paid directly to Computershare from Sumatie Lowtan's bank account.

7 On August 26, 2009, without the knowledge or consent of Computershare, a discharge of the Computershare charge was registered on title to the property by the registration of a discharge

bearing instrument number PR1692750. The discharge shows the discharging party to be Computershare and on the copy of the discharge placed in evidence, a person named Shekh Naeed Pabla represents that she has the authority to bind Computershare. The discharge was signed by Naveena Khanna and was submitted by 6613021 Canada Corp. The address for both Khanna and 6613021 Canada Corp. is shown as 10 Jayzell Drive, Toronto, Ontario. None of the individuals, Pabla or Khanna are known to Computershare. Neither person is registered as a lawyer or paralegal in the Province of Ontario. The numbered company is not known to Computershare. Neither Pabla or Khanna nor 6613021 Canada Corp. were known to or had authority from Computershare to register any discharge. Computershare never received a request to discharge the charge.

8 After the discharge of the Computershare mortgage was registered, payments continued to be made by the Lowtans pursuant to the terms of the Computershare charge more or less regularly for the next 4 1 2 years until January 2013. On January 4, 2013 the last payment was made by the Lowtans. Thereafter the Computershare charge went into default on account of nonpayment.

9 On or about March 3, 2011, the Lowtans granted a charge/charge in favor of Maria Giovanni and Darlene Geraci in the principal amount of $87,500 which was registered against title to the lands as instrument number PR1970026.

10 The Lowtans, through a mortgage broker, contacted CIBC on or about July 12, 2011 to discuss the possibility of obtaining a loan. CIBC was informed by the Lowtan's agent/broker that the Lowtans were seeking a first charge from CIBC to refinance an existing private charge registered against the lands in the outstanding amount of approximately $87,500 and to obtain a line of credit. Notwithstanding that the Lowtans were making monthly payments to Computershare pursuant to their agreement with Computershare, the Lowtans' indebtedness to Computershare was not disclosed to CIBC at the time of the loan application. When making their application their application for a first charge from CIBC, the Lowtans advised CIBC that they had aggregate debts of approximately $106,000 an amount which included the amount owed to Giovanni and Geraci. CIBC was advised by the Lowtans that they had no secured indebtedness other than the charge for approximately $87,500 in favor of Giovanni and Geraci. On July 15, 2011, CIBC entered into a commitment with the Lowtans for a loan secured by a first charge on the property. The CIBC charge securing the sum of $252,800 was registered on title on July 28, 2011 as instrument number PR2045899.

11 The proceeds of CIBC charge were used to discharge the Giovanni Geraci charge on August 9, 2011.

12 In December, 2012, the Lowtans approached Secure Capital and sought financing to take additional equity from their residence to be registered as a second mortgage. The Lowtans represented to Secure Capital that they wished some additional financing in order to pay off credit card debt and to provide some immediate financial resources. Secure Capital was informed by the Lowtans that there was one other mortgage registered against the property, that is, the CIBC mortgage registered on July 28, 2011. The Lowtans represented that, in addition to the indebtedness owed to the CIBC, they owed approximately $81,715. No information was provided by the Lowtans to Secure Capital indicating that they were indebted to Computershare. The Lowtans granted a mortgage to Secure Capital in the amount of $32,000 which was the maximum commitment that Secure Capital was prepared to make to them. This loan was secured by a charge registered against title to the property on December 11, 2012 as instrument number PR230945. Secure Capital had no knowledge of any other charge registered against the property other than the CIBC mortgage at the time the

Secure Capital mortgage was granted and registered against title to the property. Secure Capital understood that it had obtained a second mortgage against the property with priority to the CIBC mortgage which had been registered against the property on or about July 28, 2011.

13 The Lowtans defaulted under the CIBC mortgage on or about February 1, 2013.

14 The Lowtans defaulted under the Secure Capital mortgage by failing to make payments on February 1, 2013 and thereafter. On April 9, 2013, Secured Capital's solicitor issued a notice of sale.

15 On or about April 12, 2013, Computershare discovered for the first time that the Computershare charge had been fraudulently discharged by the registration of the discharge bearing instrument number PR169-2750.

16 On or about April 25, 2013, both the Lowtans made an assignment into bankruptcy. By April 25, 2013 the Lowtans had vacated the property as they were unable to maintain payments.

17 On or about May 30, 2013, a Caution was registered against the property by the Director of Titles as instrument number PR2375145 indicating that the discharge of charge registered on the lands on August 26, 2009, as instrument number PR 169-2750 relating to the Computershare charge may be a fraudulent instrument and that no dealings could be had with the property until the matter was resolved.

18 On or about June 4, 2013 CIBC issued a notice of sale.

19 CIBC, Computershare and Secure Capital subsequently commenced these applications.

20 The sale of the property occurred pursuant to court order dated December 5, 2013 obtained by CIBC with the consent of Computershare, Secure Capital, the Lowtans' trustee in bankruptcy and the Director of Titles. The proceeds of sale, which as of September 23, 2014 amounted to $297,754, are being held in trust pending the resolution of the priorities litigation. Needless to say, the funds being held in trust are not sufficient to satisfy the three claimants, Computershare, CIBC and Secure Capital.

21 Paradigm Quest Inc. (hereinafter "Paradigm") is a company responsible for providing services to mortgage companies, including Computershare, which include collections, mortgage administration and the registration of mortgage discharges. Arrangements for the Computershare mortgage were made by the Lowtans through Paradigm. After the discharge of the Computershare mortgage was registered (such registration without the knowledge of Computershare or Paradigm) Paradigm continued to have contact with the Lowtans. For example, in the affidavit of Mario Brown, a recovery officer with Paradigm, Mr. Brown deposes that in late 2011 one of the Lowtans called the recovery department at Paradigm and asked to make a double mortgage payment on January 21, 2012. In addition, there were numerous phone contacts between the Lowtans and representatives of Paradigm in the fall of 2012 when the Computershare mortgage payments were not being made regularly. Dhanraj Lowtan called Paradigm and requested payments on the Computershare mortgage be deferred explaining to the Paradigm representative that he was in financial difficulty. In the course of these conversations, the Lowtans continued to acknowledge their obligation to make payments on the Computershare mortgage.

22 By early 2013, when the Lowtans failure to make regular mortgage payments had become problematic, a notice of default was sent to them by Computershare.

23 As a result of the Computershare mortgage being in default, Paradigm referred the matter to counsel for enforcement after which it was discovered that the Computershare mortgage had been discharged. Paradigm does not execute mortgage discharges but rather sends them to the lender for execution by persons authorized to sign mortgage discharges. Paradigm then registers the discharge on title in cases where they are authorized by Computershare to do so. Paradigm does not use third parties to register discharges and has never delegated this task to 6613021 Canada Corp. or to Shekh Naeed Pabla or to Naveena Khanna.

24 There is no disagreement among the parties with any of the above stated facts. There remains however an issue of whether Computershare knew or ought to have known about the fraudulent discharge prior to the registration of the CIBC charge.

Did Computershare have actual knowledge of the fraudulent discharge prior to enforcement proceedings being commenced in 2013?

25 CIBC argued that Computershare should be estopped from asserting that the discharge of its charge constituted a fraudulent instrument subject to reinstatement in priority of the CIBC charge because it had learned of the discharge almost 2 years before CIBC advanced funds under its charge and took no steps to reinstate the Computershare charge.

26 Fidelity National Financial Canada (hereinafter "FNF") is a company that provides services to various clients including various branches of the Canadian Imperial Bank of Commerce (hereinafter "the Bank"). The services provided by FNF include performing title searches of properties and preparing mortgage documentation for lenders. In March of 2010, FNF was requested by a branch of the Bank located in Brampton, Ontario to make inquiries with respect to the property in the context of the Lowtans' request to the Bank for a loan to be secured by a collateral charge against the property. As a result, FNF performed a title search of the property. In the course of the title search, FNF communicated to the branch of the Bank that although the collateral charge was to be a second charge on the property, there was no existing first mortgage registered on title. FNF asked the Bank to confirm the priority of the proposed collateral mortgage as a result of the title discrepancy. Ms. Sherri Frank, a manager of client services at FNF, has given evidence that she believes that she made a call to Paradigm on April 6, 2010 at approximately 10:50 a.m. Her note of the call which was made contemporaneously is as follows: "transferred to Manager, Sean.dacosta@paradigmquest.com x2268, advised of situation and advised once approval received from CIBC, Borrower, we will send an e-mail copy of search, mortgage and discharge. The customer can call him directly as they need to get this mortgage reinstated." Understandably when examined on February 5, 2014, Ms. Frank had no independent recollection of a conversation but based on her note, Ms. Frank believed she had spoken to Mr. Dacosta and that she would have given Paradigm enough information that they would have understood that there was no charge on title. Ms. Frank confirmed that she did not send an e-mail to Mr. Dacosta and did not send copies of any title or any documentation to FNF. Ms. Frank said that she would not send a copy of the search, mortgage and discharge to Paradigm or to Mr. Dacosta without getting approval from both the Bank and the borrower i.e. the Lowtans. The Lowtans did not qualify for the loan they were seeking from the Bank. FNF then closed its file. In cross-examination, Ms. Frank did not recall whether she had a conversation with Mr. Dacosta or left a voicemail message. Ms. Frank stated that initially she did not call Paradigm but called the number of the company called Merix and believes that she was transferred to Mr. Dacosta's extension at Paradigm. Merix, as I understand, is a company related to Paradigm.

27 Mr. Dacosta filed an affidavit in which he confirmed that he was employed by Paradigm and in 2010 was a supervisor of Paradigm's customer service department. Mr. Dacosta has deposed that he has no recollection or record of receiving any call or message from Ms. Frank and that he has no record of making a return phone call to her. In cross-examination, Mr. Dacosta testified that if he had been advised of the potential fraudulent discharge of the Computershare mortgage registered on title not only would he have made a note of it but also would have done something about it. However, if someone told him simply that a Paradigm administered mortgage had been discharged, without saying it had been fraudulently discharged, it would have been of no moment to him because every day Paradigm may be responsible for registering the discharges of numbers of mortgages. Mr. Dacosta did receive a request from the Lowtans on or about April 8, 2010 to provide them with an information statement showing the current status of the mortgage. Mr. Dacosta's records show that on April 8, 2010 he instructed an employee of Merix, Ms. Katarina Koutros, to prepare and send an information sheet to the Lowtans which gave the current status of the Computershare mortgage indicating that it was in good standing. A copy of that information statement was appended to his affidavit. On April 8, 2010, the Lowtans forwarded the information statement received from Paradigm to the branch of the Bank from whom they were seeking a loan. After reviewing the Statement, CIBC rejected the Lowtans mortgage application. No copy of the parcel abstract showing the discharge or of the discharge of the mortgage was ever sent to Dacosta at Paradigm by anyone at the Bank or by Ms. Frank.

28 Ms. Frank has no recollection of what, if anything, she said to Mr. Dacosta. Mr. Dacosta has no recollection of ever being advised that the Computershare mortgage had been fraudulently discharged. His instruction to Ms. Koutros to send an information statement regarding the status of the mortgage and his failure to act on such information is inconsistent with his having been informed that the mortgage had been fraudulently discharged.

29 On the basis of the material before me, I am not prepared to find that Computershare or CIBC ought to have been aware that the fraudulent discharge had been registered. Therefore, Computershare is not estopped from claiming that it was unaware of the registration of the fraudulent discharge in April, 2010.

Were the Lowtans privy to the fraudulent discharge of the Computershare mortgage?

30 CIBC takes the position that the Lowtans were not privy to the fraudulent discharge of the charge. I disagree.

31 It is reasonable to conclude that the Lowtans made representations to Giovanni and Geraci that their indebtedness would be secured by a first charge on the property in the amount of $87,500. These representations were made at the same time that they were making monthly payments towards the Computershare charge and were fully aware of their obligations to Computershare.

32 Additionally, as is made clear from the CIBC material, when applying for a first mortgage loan in July 2011, the Lowtans advised CIBC that there was no charge against the lands other than the Giovanni/Geraci charge. Furthermore, the Lowtans advised CIBC that they had debts of approximately $106,000 and that this amount included the amount owed to Giovanni and Geraci. These representations were made to the CIBC at the same time they were continuing to make monthly payments to Computershare pursuant to their obligation under the Computershare charge. The representations made by the Lowtans to CIBC were false and designed to keep secret from CIBC their existing obligations to Computershare.

33 In December, 2012, when they were paying the Computershare mortgage, the Lowtans sought a loan from Secure Capital to be secured by a second mortgage, the Lowtans represented to Secure Capital that, in addition to the indebtedness owed to the CIBC, they owed approximately $81,715. No information was provided to Secure Capital indicating that the Lowtans were indebted to Computershare. The representations made by the Lowtans to Secure Capital were false and designed to keep secret from Secure Capital their existing mortgage obligations to Computershare.

34 The Lowtans granted a mortgage to Secure Capital in the amount of $32,000 being the maximum commitment that Secure Capital was prepared to make to them. This loan was secured by a charge registered against title to the property on December 11, 2012 as instrument number PR230945. Secure Capital had no knowledge of any other charge registered against the property other than the CIBC mortgage at the time the Secure Capital mortgage was granted and registered against title to the property. Secure Capital understood that it had obtained a second mortgage against the property with priority to the CIBC mortgage registered against the property on or about July 28, 2011.

35 The inescapable conclusion is that the reason the Lowtans continued to make monthly payments to Computershare was to ensure that Computershare did not become aware that the discharge of the Computershare charge had been registered on title. The Lowtans knew that default by them in paying the Computershare charge would have led to a discovery by Computershare of the fraudulent discharge registered on title. They continued to make mortgage payments in order to keep the discharge secret from Computershare.

36 On a balance of probabilities, I have no doubt in concluding that the Lowtans were fully aware of and responsible for the registration of the fraudulent discharge. After the registration of the discharge, they knowingly made false representations to subsequent lenders that their loans would be secured by a first charge in the case of CIBC and a second charge in the case of Secure Capital. The registration of the fraudulent discharge was caused by the Lowtans and relied on by them as part of a scheme to obtain additional financing from subsequent chargees which financing would not otherwise have been available to them. The dishonesty of the Lowtans is made abundantly clear by the evidence.

The Positions of the Parties

The position of Computershare

37 Computershare argues that the first charge granted to the Lowtans should remain in first position unaffected by the fraudulent discharge and that the subsequently registered CIBC charge should take second position and the Secure Capital charge should take third position. Computershare seeks a declaration that the Computershare charge is the first charge/charge registered against the property and that it stands in priority to the CIBC charge and the Secured Capital charge. Computershare asserts two main arguments:

1. The Lowtans were responsible for registering the fraudulent discharge of the Computershare charge. CIBC acquired its interest in the property from the Lowtans and is an intermediate owner having had the last and best opportunity to avoid the fraud. The CIBC charge therefore is defeasible in favour of Computershare's charge. In accordance with section 78(4.2) of the *Land Titles Act*, the CIBC charge is a valid charge which remains in

second position behind the Computershare charge and ahead of the Secured Capital charge;

2. In the alternative, the discharge of the Computershare charge being fraudulently obtained and registered is void leaving the Computershare charge as a valid and effective first charge against the property.

The position of CIBC

38 CIBC takes the position that it relied on the discharge registered on title and that its charge should rank first, the Secure Capital charge should rank second and the Computershare charge should rank third. CIBC asserts that it obtained its charge for value and with no notice that the registration of the discharge of the Computershare charge was fraudulent. Relying on the "mirror" and "curtain" principles which inform the *Land Titles Act*, CIBC asserts that the discharge was not a "fraudulent instrument" within the meaning of the *Land Titles Act* and that it was entitled to rely on the register when it granted the Lowtans what it believed in good faith to be a valid first charge. CIBC's position may be stated simply as follows:

> Even if the discharge is a fraudulent instrument for the purposes of section 78(4.1) the reinstatement of the Computershare charge under section 78(4.1) cannot invalidate the effect of CIBC's charge as a valid and effective first ranking charge because CIBC's charge is not a "fraudulent instrument" as defined in s.(1) of the LTA.

The position of Secure Capital

39 Secure Capital agrees with the position advanced by CIBC except that it asks that all interest, expenses, penalties and further costs incurred by CIBC should be stayed as of June 7, 2014 being the date the first application in this proceeding was brought by CIBC by way of notice of application as court file number 3218/13. Secure Capital asserts that the delay and expenses caused by the dispute related to the priority of charges should not create adversely affect subsequent encumbrancers and that it would cause undue hardship to Secure Capital if the further interest, expenses, costs and penalties of CIBC incurred after the commencement of these applications are added to the CIBC charge and rank in priority to what it asserts is a valid second charge.

Analysis

40 The registration of the discharge of the Computershare mortgage raises questions that were not answered by the parties or by the evidence. How was the security system of electronic registration of documents circumvented? The discharge was filed by 6613021 Canada Corporation. How is it possible that the numbered company could submit a document on behalf of Computershare for electronic registration without being authorized by Computershare or Paradigm to do so? The answer to this question is speculative and this and other questions remain unresolved.

41 This case is about which innocent party should have the priority of its charge adversely affected because of the fraudulent discharge purported to discharge the first registered Computershare charge. There is no suggestion that CIBC or Secure Capital were aware of the fraudulent nature of the discharge registered on title.

42 CIBC and Secure Capital assert that they were entitled to rely on the register when it determined to advance mortgage funds to the Lowtans and therefore their mortgages should rate in first and second priority with Computershare having the right to have their fraudulently discharged mortgage reinstated but in third priority to the CIBC and Secure Capital charges. CIBC and Secure Capital are supported in this contention by counsel representing the Director of Titles.

43 It is obvious that reliance on the registry however is not a one-way street. Computershare also had a legitimate expectation that registration of its charge on title would act as effective notice to any subsequent transferee, mortgagee or other encumbrancer that any subsequently acquired interest in the property would be subject to the priority of the Computershare mortgage.

44 There is no dispute that the registered discharge was a fraudulent instrument within the meaning of the *Land Titles Act,* R.S.O. 1990, c. L.5 (hereinafter referred to as the "LTA").

45 A fraudulent instrument is defined in s.1 of the LTA as follows:

> "fraudulent instrument" means an instrument,
>
> (a) under which a fraudulent person purports to receive or transfer an estate or interest in land,
>
> (b) that is given under the purported authority of a power of attorney that is forged,
>
> (c) that is a transfer of a charge where the charge is given by a fraudulent person, or
>
> (d) that perpetrates a fraud as prescribed with respect to the estate or interest in land affected by the instrument.
>
> A "fraudulent person" as defined in section 1 of the LTA as "a person who executes or purports to execute an instrument if,
>
> (a) the person forged the instrument,
>
> (b) the person is a fictitious person, or
>
> (c) the person holds oneself out in the instrument to be, but knows that the person is not, the registered owner of the estate or interest in land affected by the instrument;

46 As noted above, all parties agree that the discharge of the Computershare charge was a fraudulent instrument. I have found the Lowtans to be responsible for the registration of the fraudulent discharge. The Lowtans made a false document - the Computershare discharge - which was designed to have subsequent lenders rely on it to their detriment. The Lowtans were the registered owners of the property when they granted CIBC and Secure Capital the first and second charges on the property. However, they did not own the property free and clear of encumbrances. The Lowtans knew full well that they were the registered owners of a property which was subject to a first charge

in favour of Computershare and that the Computershare charge was intended to have first priority against any other subsequent registered security interest in the property. The interest in the property that they purported to convey to CIBC -- a first charge on the property -- to their knowledge had already been conveyed to Computershare. The Lowtans were not the owners of the "interest in land" conveyed to CIBC and Secure Capital by the charges registered in their favour. The Lowtans fraudulently conveyed to themselves the Computershare interest in the property and then held themselves out to the CIBC as the registered owners of the property whose interests as owner were not subject to any registered encumbrance.

47 CIBC and Secure Capital rely on s. 78(4) of the LTA which provides as follows:

> 78 (4) When registered, an instrument shall be deemed to be embodied in the register and to be effective according to its nature and intent, and to create, transfer, charge or discharge, as the case requires, the land or estate or interest therein mentioned in the register.

48 Computershare relies on sections 78(4.1) and 78(4.2) of the LTA which provide:

> 78 (4.1) Subsection (4) does not apply to a fraudulent instrument that is registered on or after October 19, 2006
>
> 78 (4.2) Nothing in subsection (4.1) invalidates the effect of a registered instrument that is not a fraudulent instrument described in that subsection, including instruments registered subsequent to such a fraudulent instrument.

49 Computershare also relies on section 155 of the LTA which states:

> 155. Subject to the provisions of this Act, with respect to registered dispositions for valuable consideration, any disposition of the land or of a charge on land that, if unregistered, would be fraudulent and void is, despite registration, fraudulent and void in like manner.

50 Before turning to the case of *Lawrence v. Maple Trust Company*, 84 O.R. (3d) 94, which instructs us with respect to the interpretation of these sections as well as to the historical and current interpretation of the LTA, I would like to deal with the assertion by CIBC, Secure Capital and by counsel for the Director of Titles that the charges granted by the Lowtans to CIBC and to Secure Capital are not fraudulent documents within the meaning of the LTA with which I disagree.

51 A person is a fraudulent person within the meaning of the LTA when the person "holds oneself out in the instrument to be, but knows that the person is not, the registered owner of the estate or interest in land affected by the instrument." As noted above, a "fraudulent instrument" is defined as including an instrument under which a fraudulent person purports to transfer an interest in land. The Lowtans did not own the interest in the property purported to be conveyed to CIBC and to Secure Capital. The Lowtans were fraudulent persons within the meaning of the LTA in their dealings both with CIBC and with Secure Capital. Therefore, I conclude that the mortgages given by the Lowtans to CIBC and Secure Capital were fraudulent instruments within the meaning of s. 78(4.2) of the LTA. Although I have concluded that the subsequent mortgages to CIBC and Secure Capital are fraudulent instruments, I of course do not mean to imply that CIBC and Secure Capital acted

other than in good faith. Their good faith is not challenged by any party and certainly not by this court.

52 The tension between the sections reproduced above has been discussed most recently in *Lawrence v. Maple Trust Company*, 84 O.R. (3d) 94. In *Lawrence*, the Court of Appeal began its analysis with a description of the purpose of the land titles system. At para. 30, the Court of Appeal adopted the statement of Epstein J.in *Durrani v Augier*, 50 O.R. (3d) 353 at paras. 40-42 where she stated as follows:

> The land titles system was established in Ontario in 1885, and was modeled on the English Land Transfer Act of 1875. It is currently known as the Land Titles Act R.S.O. 1990, c. L.5. Most Canadian provinces have similar legislation.
>
> The essential purpose of land titles legislation is to provide the public with security of title and facility of transfer: Di Castri Registration of Title to Land vol. 2 looseleaf (Toronto: Carswell, 1987) at 17-32. The notion of title registration establishes title by setting up a register and guaranteeing that a person named as the owner has perfect title, subject only to registered encumbrances and enumerated statutory exceptions.
>
> The philosophy of a land titles system embodies three principles; namely, the mirror principle, where the register is a perfect mirror of the state of title, the curtain principle, which holds that a purchaser need not investigate the history of past dealings with the land, or search behind the title as depicted on the register, and the insurance principle, where the state guarantees accuracy of the register and compensates any person who suffers loss as the result of an inaccuracy. These principles form the doctrine of indefeasibility of title and is the essence of the land titles system...

53 In *Lawrence,* the Court of Appeal affirmed that under the LTA, it is the theory of deferred indefeasibility that prevails in Ontario. The theory of deferred indefeasibility is consistent with the object of the legislation which is to save individuals dealing with registered proprietors from the trouble and expense of going behind the register in order to investigate the history of title and to satisfy themselves of its validity. See *Gibbs v. Messer*, [1891] A.C. 248. However, as is stated in *Falconbridge on Mortgages*, (4th edition) at page 202:

> It is important to bear in mind the exact nature of the "main object" of the legislation. A purchaser in good faith is entitled to rely upon the register and need not go behind the title of the registered owner, but, of course, he must satisfy himself that an instrument purporting to be made by the registered owner is itself a valid. Registration will not render an invalid instrument valid in favor of the purchaser therein named. But if the purchaser registers the instrument and becomes the registered owner of an estate or interest, then, even though the instrument as regards him is invalid, a purchaser from him is protected by the statute, because this second purchaser is entitled to rely upon the register and need not go behind it. Thus the instrument which is invalid so far as the immediate purchaser is concerned becomes a good root of title in favour of the subsequent purchaser.

54 Pursuant to the theory of deferred indefeasibility, registration of an invalid instrument does not make the instrument valid in favor of an immediate purchaser but if the purchaser becomes the registered owner, a purchaser from the immediate purchaser is protected by the statute because the second purchaser is entitled to rely upon the register and need not go behind it. As stated in *Falconbridge* at p. 203: "Thus, the instrument which is invalid so far as the immediate purchaser is concerned becomes a good root of title in favour of the subsequent purchaser."

55 Applying the theory of deferred indefeasibility in the *Lawrence* case, the Court of Appeal determined that Maple Trust, which had been granted a mortgage from Wright who had obtained title by fraud, was vulnerable to a claim from the true owner. It is the intermediate owner who has the opportunity to investigate the transaction and avoid the fraud. The Court of Appeal also stated that in accordance with the theory of deferred indefeasibility, any subsequent *bona fide* purchaser or encumbrancer would have no such opportunity and could obtain good title from Maple Trust.

56 How does the theory of deferred indefeasibility have application in this case? It is not disputed that the discharge of the Computershare mortgage was fraudulent. I have concluded that the Lowtans were responsible for registration of the fraudulent discharge. The fact that the register showed the Lowtans on title as the registered owners of the property unencumbered by any charge in favor of Computershare is as a result of their fraud. *Lawrence* confirms that a fraudster can never take good title so as to become an owner.

57 CIBC relied on the registry that showed the Computershare mortgage to have been discharged. It relied on the fact that the registry disclosed that the Lowtans owned the property without encumbrance. In fact, the Lowtans had conveyed away an interest in the property to Computershare in the form of a first charge. This first charge granted Computershare both an interest in the property and certain statutory rights pursuant to its mortgage to obtain possession and to sell the property in the event of default.

58 In this case, CIBC is in a position analogous to that of Maple Trust in the *Lawrence* case. In *Lawrence*, Maple Trust was found by the Court of Appeal to be an intermediate owner having received its interest in the property from a fraudulent transferee who appeared on the register as the registered owner. In this case, the Lowtans are fraudulent transferees having fraudulently conveyed Computershare's interest in the property to themselves by the registration of the fraudulent discharge. In my view, the CIBC is, in accordance with the theory of deferred indefeasibility, an intermediate owner. CIBC acquired an interest in title from a fraudster, and had an opportunity to investigate the transaction and avoid the fraud. For example, an inquiry as to how the Lowtans were able to pay off the Computershare mortgage given their financial circumstances might have raised concerns. In any event, according to the Court of Appeal in *Lawrence*, registration of a void instrument does not cure its defect and a void instrument or its registration cannot give good title. The discharge of the Computershare mortgage was void and registration of that discharge did not give clear title to the fraudsters.

59 Meredith J.A. stated in *In re Skill and Thompson*, [1908] O.J. No. 41, 17 O.L.R .186 (in a passage approved by the Court of Appeal in *Lawrence*) at paras. 39-40:

> The *Land Titles Act* is not an Act to abolish the law of real property; it is an Act far more harmless in that respect than in some quarters seems to be imagined, at times, at all events, when the wish is father to the imagination. It is an Act to simplify titles and facilitate the transfer of land; and, doubtless, greater familiari-

> ty with it will tend to remove a good many false notions regarding its revolutionary character.
>
> Its main purpose is to assure that title to a purchaser from a registered owner; but, surely, it is not one of its purposes to protect the registered owner against his own obligations, much less against his own fraud.

The words of Meredith J.A. are apposite in this case: the LTA is not designed to protect the registered owner against his own fraud.

60 In *Lawrence* the Court of Appeal decided that the earlier Court of Appeal decision in *Household Realty Corporation Ltd. v. Liu*, [2005] O.J. No. 5001 was wrongly decided. I will not set out the facts of *Household Realty* in any detail. Suffice to say, in *Household Realty* a matrimonial home was owned jointly by a husband and wife. The wife forged her husband's signature on a power of attorney, naming her as his attorney, and then registered the power of attorney on title. She then mortgaged the property placing two separate charges on the property. The mortgagees both acted in good faith and were both unaware that the registered power of attorney was fraudulent. The Court of Appeal held that the mortgages were immediately effective once they were registered because they were given for valuable consideration and without notice of the fraud and pursuant to section 78(4) of the LTA, they were immediately effective according to their nature and intent.

61 In *Lawrence*, the Court of Appeal held that the *Household Realty* case was wrongly decided. The mortgagees in *Household Realty* had relied on the power of attorney registered in the land titles office to conclude that the named attorney, the wife, had authority to charge the property. Applying the deferred indefeasibility theory, the Court of Appeal -- in reversing its earlier decision -- concluded that in *Household Realty* the mortgages ought to have been invalid as against the true owner. The position of CIBC and of Secure Capital in this case is analogous to the position of the mortgagee in *Household Realty*.

Conclusion

62 I conclude that the Computershare mortgage retains its priority as the first charge in the property and that the CIBC and the Secure Capital charges rank second and third respectively.

63 This court therefore orders that the Director of Titles rectify the register by deleting instrument number PR1692579 being the discharge of the Computershare charge and restoring the Computershare charge (instrument number PR1571875) as if the discharge had not been registered.

Costs

64 Each party has been an innocent victim of fraud. Each party has acted in good faith. I conclude that no costs should be awarded in this case.

65 I also agree with the submissions of Secure Capital that the costs of the priorities litigation should not be added to the costs of mortgage enforcement proceedings against the Lowtans. Secure Capital has argued that the delay and expenses caused by the dispute related to the priority of charges should not adversely affect its position as a subsequent encumbrancer and that it would cause undue hardship if the further interest, expenses, costs and penalties incurred after the commencement of these applications are added to the CIBC charges that it conceded ranks in priority to what it asserted is a valid second charge. I agree that with some modification, this is a fair approach.

66 I therefore order that the further expenses, penalties and costs of the priorities litigation incurred from the commencement of the CIBC application should not be added to the costs of enforcement proceedings against the Lowtans. This will preserve as much as possible of the sale proceeds for the second and third mortgagees, CIBC and Secure Capital. Regrettably, this outcome will probably not help Secure Capital at least with respect to its claim against the sale proceeds because the magnitude of the debt owing under the charges of Computershare and CIBC will likely consume the entirety of the proceeds of sale but it will make a difference to CIBC.

67 To the extent there is a shortfall in recovery from the proceeds of sale of the property for CIBC and Secure Capital, judgments obtained by CIBC and Secure Capital against the Lowtans on their mortgage covenants should survive bankruptcy of the Lowtans since both mortgages were obtained by fraud.

J.C. MURRAY J.

3

Maria Elena Hoffstein (Contributor)

Halsbury's Laws of Canada - Trusts

IV. TRUSTS ARISING BY OPERATION OF LAW

2. Constructive Trusts

(3) Circumstances in Which Constructive Trusts Arise

(c) Profits of Wrongs

(vi) Common Law Claims

HTR-70 Acquisition of property through improper means.

HTR-70 Acquisition of property through improper means. Constructive trusts arise also in the context of some claims at common law. Where the tortfeasor acquires property by tortious means, the true owner can sometimes assert beneficial title to the property. Where a party acquires possession and control of property to which he or she does not have title, and then intermingles it with indistinguishable property of the same kind; or transmutes the property into a new form, as happens when stolen iron is used to make a steam engine; or exchanges it for a new asset, the value of the misappropriated property can be traced into the new property by means of a constructive trust.

Fraud and theft. To deter would-be fraudsters and thieves, equity does not allow a tortfeasor to acquire beneficial title to the proceeds of fraud or theft. If a transfer of property is accomplished by the tort of deceit[1] or theft,[2] any asset into which such proceeds of crime can be traced may be impressed with a constructive trust.[3] The victim of fraud may elect either to enforce a constructive trust upon the property, or to convert the constructive trust into an equitable lien upon the assets for the amount of his loss.[4] When legal title passes to a fraudster or thief, the proceeds of their wrongdoing are subject to an equity in favour of their victim. In the case of theft or a fraudulent transaction by which the true owner does not intend to convey beneficial title, the original owner retains full beneficial ownership of the stolen asset. A transaction whereby the defrauded party is induced by a misrepresentation to transfer beneficial ownership to the fraudster is voidable at the election of the defrauded party. Until such election occurs, the fraudster receives beneficial title subject to the original owner's equity of rescission. The original owner's continuing equity in the proceeds of fraud crystallizes into a constructive trust when he or she elects to void the transaction which was induced by fraud.[5]

Proprietary claims and tracing at common law. A party who makes a proprietary claim at common law asserts that while he or she has lost possession and control of the property, he or she has not been deprived of legal title thereof. Thus, for example, when chattel is stolen, title does not pass to the thief, and the thief has no title to sell to another: *nemo dat quad non habet.*[6] Consequently, the true owner may follow the property as it passes from hand to hand, and assert his or her title as the continuous legal owner.[7]

History of equitable tracing remedy. Anciently, courts of common law would not allow proprietary claims against intermixtures and products of, or substitutions for the original property. Once the original owner had lost legal title to the property by those means, the original owner's claim at law was defeated. For example, if the proceeds of theft were used to purchase land, the land would belong to the thief at common law -- and the victim would be the thief's creditor. This limitation is a necessary consequence of the nature of legal ownership. Only equity can allow, via the medium of a constructive trust, a claimant to not only follow his or her property from hand to hand, but to also trace the value of the property into intermixed, transformed, or substituted property, and assert a claim to be beneficial owner of the new property. However, prior to the merger of the courts, Lord Ellenborough asserted the equitable jurisdiction of King's Bench[8] to trace beneficial title even where the true owner's legal title was extinguished.[9] This jurisdiction to enforce constructive trusts in aid of proprietary claims was confirmed subsequently,[10] under the misapprehension that Lord Ellenborough had developed a legal doctrine distinct from its equitable counterpart.[11] This misclassification has led to the regular enforcement of constructive trusts under the rubric of tracing at common law.

Common law cases restoring traced property are constructive trusts. All cases which purport to uphold a common law proprietary claim and restore property to its rightful owner, but do so despite the transformation, intermingling, or substitution of the original property into, with, or for the asset claimed by the true owner are instances of constructive trusts in all but name.[12]

Footnote(s)

1 *Hamilton Provident & Loan Soc. v. Gilbert*, [1884] O.J. No. 162, 6 O.R. 434 (Ont. H.C.J.).

2 *Merchant Express Co. v. Morton*, [1868] O.J. No. 311, 15 Gr. 274 (Ont. U. Ct. Ch.).

3 *Shute v. Premier Trust Co.*, [1993] O.J. No. 2758, 35 R.P.R. (2d) 141 (Ont. Gen. Div.).

4 *Hallett's Estate (Re)* (1879), 13 Ch. D. 696 at 709 (C.A.).

5 *Bank of Montreal v. iTrade Finance Inc.* (2009), [2009] O.J. No. 3400, 96 O.R. (3d) 561 (Ont. C.A.).

6 *Gunsbourg (Re)*, [1920] 2 K.B. 426, [1920] All E.R. Rep. 492 (C.A.).

7 *Cooper v. Shepherd* (1846), 3 C.B. 266, 136 E.R. 107 (C.P.); *Sinclair v. Brougham*, [1914] A.C. 398 at 419 (H.L.).

8 See Blackstone, *Commentaries*, Chapter 4, Book 3, at 49, note c.

9 *Taylor v. Plumer* (1815), 3 M & S 562

10 *Banque Belge pour l'Etranger v. Hambrouck*, [1921] 1 K.B. 321 (C.A.).

11 *FC Jones & Sons v. Jones*, [1996] 4 All E.R. 721 at 729 (C.A.). See Lionel Smith, *Tracing in Taylor v. Plumer: Equity in the Court of King's Bench* (1995), L.M.C.L.Q. 240.

12 *Merchant Express Co. v. Morton*, [1868] O.J. No. 311, (1868), 15 Gr. 274 (Ont. U. Ct. Ch.).

ICLR: Chancery Division/1879/Volume 13/In re HALLETT'S ESTATE. KNATCHBULL v. HALLETT. [1878 H. 147.] - (1879) 13 Ch.D. 696

(1879) 13 Ch.D. 696

[COURT OF APPEAL]

In re HALLETT'S ESTATE. KNATCHBULL v. HALLETT. [1878 H. 147.]

1879 July 10, 12.

FRY, J.

1879 Nov. 26; Dec. 3.

JESSEL, M.R., BAGGALLAY and THESIGER, L.JJ.

1880 Feb. 11.

JESSEL, M.R., BAGGALLAY, THESIGER, L.JJ.

Banker - Lien - Following Trust Money - Entry by Banker - Order of Payment - Appropriation - Rule in Clayton's Case - Trustee.

If money held by a person in a fiduciary character, though not as trustee, has been paid by him to his account at his bankers, the person for whom he held the money can follow it, and has a charge on the balance in the bankers' hands.

Ex parte Dale & Co.(1) dissented from.

If a person who holds money as a trustee or in a fiduciary character pays it to his account at his bankers, and mixes it with his own money, and afterwards draws out sums by cheques in the

ordinary manner:-

Held, by the Court of Appeal (*dissentiente Thesiger*, L.J.), that the rule in *Clayton's Case* (2), attributing the first drawings out to the first payments in, does not apply; and that the drawer must be taken to have drawn out his own money in preference to the trust money.

Pennell v. Deffell (3) on this point not followed.

Held, by *Fry*, J., that, as between two *cestuis que trust* whose money the trustee has paid into his own account at his bankers, the rule in *Clayton's Case* applies, so that the first sum paid in will be held to have been first drawn out.

THIS case came on upon claims by several persons against money in the hands of the bankers of *Henry Hughes Hallett*, deceased. The action was brought by a general creditor for the administration of his estate.

As to a claim by the trustees of *Hallett's* settlement. By the marriage settlement of *Henry Hughes Hallett*, made in 1847, a sum of £2300 was settled for the benefit of *Hallett*, his wife and his children. Several changes were made in the investment of this fund, and the trustees had allowed the fund to come into the hands of *Hallett*. These changes were effected by *Hallett*, and were noted in a memorandum in his handwriting in the fold of the draft settlement, which terminated as follows: "The money remained in the *Great George Street* mortgage until September,

(1) 11 Ch. D. 772.

(2) 1 Mer. 572.

(3) 4 D. M. & G. 372.

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1865, when it was invested in Mr. *Walker's* estate. *Walker's* mortgage was paid off in November, 1870, and invested in £2590 Russian 5 *per* Cent. Stock." This was not strictly correct, as *Walker's* mortgage was really paid off in 1869.

Hallett held a considerable number of Russian bonds, and in the opinion of the Court it was proved that he had in 1877 allotted Russian bonds of the nominal amount of £1554 and £1036, making together £2590, as representing the trust funds under the settlement. The bonds for £1554 he retained in his own hands; and his son, shortly before his death, found them and delivered them to the trustees of the settlement by whom they were sold. The bonds for £1036 were deposited by *Hallett* with his bankers, Messrs. *Twining*, and were afterwards sold as mentioned below.

As to a claim by Mrs. *Cotterill. Henry Hughes Hallett* had for many years been employed by Mrs. *Cotterill* as her solicitor; and she had been in the habit of depositing with him securities for money, and in the opinion of the Court it was proved that he had bought or appropriated and did in 1877 hold for her Russian bonds of £450 and £2242, nominal amount. The facts of her case are fully stated in the judgment of Mr. Justice *Fry*.

In November, 1877, *Hallett*, without any authority from the trustees or from Mrs. *Cotterill*, directed his bankers, Messrs. *Twining*, to sell, and they accordingly sold, one of the sets of bonds representing the trust fund and both sets of Mrs. *Cotterill's* bonds. The following entries (with other entries of cash, &c.) appeared to his credit in the books of the bankers:- £ *s. d.* Nov. 3. Sale £450 Russian 5 per cent. 1871, at 76 less commission . . . . 341 8 9 Nov. 14. Sale £1036 Russian 5 per cent. 1822, at 74½ less commission ... 770 10 5 " Sale £2442 Russian 5 per cent. 1822, at 74 less commission 1804 0 7

Hallett had before his death drawn out different sums for his own purposes, so that the balance to his credit at the time of his death (if nothing more had been paid in by him after the 14th of November) would have been £1708 16*s*. He had, however, paid

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in other sums, so that he had at the time of his death, which was in February, 1878, a balance at his bankers of £3029 15*s*. 1*d*., of which £2600 had been paid into Court to the credit of an action for the administration of his estate.

The trustees of the settlement applied by summons in the action for payment of £770 10*s*. 5

d. out of the £2600, and for a declaration that the produce of the sale of the bonds for £1554 belonged to them. Mrs. *Cotterill* applied for payment of the £1708 16*s.* balance. A Mrs. *Gatliff* also applied for payment of some of the money as having arisen from the sale of Russian bonds belonging to her. The summonses came on for hearing together before Mr. Justice *Fry* on the 10th of July, 1879.

E. Beaumont, for Mrs. Cotterill:-

Mrs. *Cotterill* claims £1708 16*s.* as the sum remaining in the bankers' hands out of the produce of the sales of her £2442 Russian bonds. These bonds were simply deposited with *Hallett*, and he had no right to sell them. He has, however, sold them, but the money can be traced and is ear-marked. He is said to have similarly sold the bonds of his trustees, but if he did so the £770 10*s.* 5*d.* for which he sold them has, like the produce of the sale of Mrs. *Cotterill's* £450, been already drawn out under his cheques, and the balance left is not enough even to satisfy Mrs. *Cotterill's* claim for the produce of her £2442 Russian bonds. That is the rule in *Clayton's Case* (1); *Brown v. Adams* (2).

Phear, for Mrs. *Gatliff.*

J. Pearson, Q.C., and ***D. Gardiner***, for the trustees of the settlement:-

We claim the £770 10*s.* 5*d.* as the produce of the sale of our Russian bonds, and we also claim the produce of the bonds for £1554. As to the £770 10*s.* 5*d.*, *Clayton's Case* does not apply, as both sums were paid in on the 14th of November; and at all events the remaining money must be rateably apportioned between the trustees and Mrs. *Cotterill.*

(1) 1 Mer. 572.

(2) Law Rep. 4 Ch. 764.

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Higgins, Q.C., and ***B. Fossett Lock***, for the Plaintiff in the suit:-

The applicants have no priority; and this case is exactly like *Ex parte Dale & Co.* (1), which shews that when money has been paid to a general account at a bankers it cannot be followed. *Ex parte Cooke* (2) was different, as the person paying in was a broker. The law is shewn by *Pennell v. Deffell* (3) and *Middleton v. Pollock* (4).

A. T. Watson, for Hallett's executrix, cited *Taylor v. Plumer* (5).

FRY, J. , after expressing his intention of giving counsel an opportunity of arguing Mrs. Cotterill's summons on the cases which had been cited, and after stating the facts as to the claim of Hallett's trustees, and deciding that they were entitled to retain the proceeds of the sale of the £1554 Russian bonds, and that they had proved that the Russian bonds for £1036 were part of the trust fund, continued:-

The second question is whether *Clayton's Case* (6) applies. Now, if the matter were unfettered by authority, it would appear to me clear that where a man has a balance to his credit consisting in part of funds which are his own, and which he may lawfully draw out and apply for his own purposes, and in part of funds which he may not lawfully draw out and apply for his own purposes, his drawings for his own purposes ought to be attributed to his own funds, and not to the trust funds. But it appears to me that I am not at liberty, in the existing state of the authorities, to act according to the inclination of my own mind. In *Pennell v. Deffell* (7), Lord Justice *Knight Bruce* said, "It may be, however, and, as I think, is true, that cheques drawn by the trustee in a general manner upon the bank would, for every purpose, be ascribed and affect the account in the mode explained and laid down by Sir *W. Grant* in *Clayton's Case.* The principles there stated would, I conceive, be applicable, notwithstanding the different nature and character of the sums

(1) 11 Ch. D. 772.

(2) 4 Ch. D. 123.

(3) 4 D. M. & G. 372.

(4) 4 Ch. D. 49.

(5) 3 M. & S. 562.

(6) 1 Mer. 572.

(7) 4 D. M. & G. 372, 384.

forming together the balance due from the bank to the trustee, whatever the purposes and objects of the cheques." On that view the Court of Appeal acted, and held that as between the persons who intrusted the testator with trust moneys and his general creditors the claims of the former must prevail. In *Frith v. Cartland* (1) Vice-Chancellor *Wood* said, "The Court attributes the ownership of the trust property to the *cestui que trust* so long as it can be traced. Here there is no difficulty in identifying it. Throughout the whole series of transformations the bankrupt always held a fund available to meet the claim of the trust. ... So long, however, as the fund can be traced, the trustee cannot assert his own title to it." That case was followed by *Brown v. Adams* (2), where the trust money paid in had been drawn out, and it was held that it had been appropriated to answer the cheques. The rights of the different parties must be governed by *Clayton's Case* (3).

His Lordship then gave his decision that Mrs. *Gatliff's* claim was not maintained by the evidence.

July 12. ***E. Beaumont***, continuing the argument for Mrs. *Cotterill*:-

This case is distinguishable from *Ex parte Dale & Co.* (4), especially as *Hallett* was a trustee for Mrs. *Cotterill*. But even if *Hallett* was only an agent the money can be followed: *Taylor v. Plumer* (5). If the money can only be followed in the hands of a trustee, *Brown v. Adams* would not have been arguable. In many cases there is a physical difficulty in tracing the money, but when that has been got over the law is clear: *Ex parte Cooke* (6). Why should the trustees of the settlement take the balance? *Hallett* was not a banker, and the moneys were not mixed up in his hands, and each

sum can be and has been traced. Even if *Hallett* was not technically trustee for Mrs. *Cotterill* he stood in a fiduciary relation to her, and the result would be the same.

Higgins, in reply, on the cases cited.

(1) 2 H. & M. 417, 422.

(2) Law Rep. 4 Ch. 764.

(3) 1 Mer. 572.

(4) 11 Ch. D. 772.

(5) 3 M. & S. 562.

(6) 4 Ch. D. 123.

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FRY. J. :-

In this case Mrs. *Cotterill* claims to have such portion of the residue of the balance standing to the credit of the late Mr. *Hallett's* banking account as may be attributable to her after applying the rule

in *Clayton's Case* (1) to that account.

For more than twenty years before the death of Mr. *Hallett* in 1878 he had acted as the solicitor for this lady, and in the year 1860 he had purchased for her Russian bonds to the nominal value of £1251, and on the 10th of February, 1868, Mrs. *Cotterill* deposited those bonds with Mr. *Hallett*, together with £1000 stock of the *Midland Waggon Company of Birmingham*, and thereupon he gave her a receipt for those bonds. It appears from the evidence before me that Mr. *Hallett* was in the habit of receiving the dividends on these and the other bonds which afterwards came to his hands for safe custody, and paying them to Mrs. *Cotterill*. In March, 1871, the *Midland Waggon Company's* bond was paid off; and it appears that the sum of £1010 9*s*. 4*d*. reached *Hallett's* hands, and on the 23rd of March that was invested in £1184 Russian bonds. I hesitate to say "in the purchase," because it appears that Mr. *Hallett* had at that time in his hands Russian bonds to a considerable amount, and he probably appropriated to her, bonds to the value of £1184, which he acknowledged himself to hold on that day for her safe custody, for on that day he gave her a receipt in these terms, "Received of Mrs. *Amelia Cotterill* for safe custody £1258 Russian bonds of 1862, also £1184 like bonds, the investment of the *Midland Waggon Company's* bond paid off." The result was that he held for her £2442 Russian bonds. It has been said that these Russian bonds were not appropriated; but it appears to me that I am bound to hold that they were appropriated. He gave her that receipt, and there are entries in his books which also support the appropriation by him of certain specific bonds on her behalf. He appears, further, to have received the dividends on the bonds to that extent, and to have paid them to her. In 1871 she further deposited with him some other bonds, including £450 Russian bonds.

So matters went on from 1871 down to 1877. On the 3rd of November, 1877, Mr. *Hallett* sold the £450 Russian bonds through

(1) 1 Mer. 572.

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the intervention of his bankers, Messrs. *Twining*, and the amount produced by that sale was entered in his bankers' book specifically as the produce of the sale of £450 Russian 5 *per* Cent. Bonds. Then, on the 14th of November, he sold the £2242 bonds which he held for Mrs. *Cotterill*, and he sold on the same day another bond belonging to the trustees of his settlement. The entry in his bankers' book keeps separate those two amounts; and with regard to the amount now claimed by

Mrs. *Cotterill*, it is entered as the produce of £2242 5 *per* Cent. Russian Bonds. The money, therefore, is as clearly ear-marked in the bankers' account as it is possible to be by means of an entry.

Further than that, it is to be borne in mind that *Hallett* charges himself on the 14th of November with a sum of £2994 9*s.* 4*d.* as the produce of Russian bonds, £2442 and £450. And that sum was the exact result of adding together the two sums I have mentioned as passing into his bankers' account. There is, therefore, no doubt that that sum was the produce of Mrs. *Cotterill's* bonds. It is not necessary to say much more than that on the 2nd of February, 1878, Mr. *Hallett* died, leaving a balance of about £3000 at his bankers.

In that state of circumstances the question arises whether Mrs. *Cotterill* is entitled to follow this money. It has been argued that Mr. *Hallett* was a trustee for Mrs. *Cotterill.* In that view I cannot concur; but it appears to me that he was solicitor for her, that he was agent for her, and that he was bailee for her. I think, therefore, that he stood in what has been called a fiduciary relation towards her. Now if he had been merely the agent and bailee, and had received from her an authority to sell these bonds - an authority which, according to the proper interpretation to be put on it by the course of dealing between them, implied a right in him to mix the produce of the sale with his own moneys, I should very probably have held that Mrs. *Cotterill* was merely a creditor of Mr. *Hallett.* But that is not the case here. The authority which she gave him was merely to hold these bonds for her; and the sale of these bonds was, in my judgment, a distinct violation of the duty he had undertaken. Therefore there was no authority from her which would justify him in mixing the produce of the bonds with his own moneys. There was nothing from which

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you could infer that she was minded that the property should be converted, or that she would look to him as the mere paymaster of the produce of the securities. Those circumstances, in my judgment, make the case entirely different from the series of authorities to which I referred in *Ex parte Dale & Co.* (1), where I came to the conclusion, rightly or wrongly, that the factor properly converted the goods into money, and that the money got mixed with his own money in accordance with the intention of the parties, and that in such a case the money could not be followed. That appears to me to be the law, both at Common Law and in Equity; some of the decisions to which I then referred being decisions of a Court of Equity. But for the reasons I have indicated, that line of authority does not appear to me to touch this matter, and therefore I think that in this case - finding the fiduciary relationship, and finding the violation of that duty in the manner I have described - I am bound to give Mrs. *Cotterill* the same relief as if Mr. *Hallett* had been a trustee for her. That being so, the result is that she is entitled to follow the balance standing to his credit in his bankers' account, in the manner indicated when I gave judgment on the summons of the trustees.

I will only make this further observation, that it may very well be that the distinction which I have

now drawn, and to which necessarily my attention was not so fully directed when I gave judgment in *Ex parte Dale & Co.*, may remove some of the force of the observations which I made at the end of that judgment as to the difficulty of reconciling the other authorities with the case of *Pennell v. Deffell* (2).

J. Pearson, Q.C., and ***Dundas Gardiner*** then claimed that the balance in the bank should be divided rateably between *Hallett's* trustees and Mrs. *Cotterill.* A banker pays the cheques drawn on him out of the general balance, and does not appropriate the money first paid to the first cheque drawn. The rights of claimants cannot depend on the accident of which entry is made first by the banker's clerk. At all events a day cannot be divided, and all payments on one day must be treated as one. Suppose the clerk had entered them on one line. If the cheques are held to

(1) 11 Ch. D. 772.

(2) 4 D. M. & G. 372.

have been paid out of our £770 10*s.* 5*d.* alone, the trustees will get nothing, and all the balance will go to Mrs. *Cotterill,* although she is in the same position as the trustees.

FRY, J. , said in the course of the discussion:-

As to the £341 8*s.* 9*d.*, that sum was gone, and Mrs. *Cotterill* would get no part of it. According to *Clayton's Case* (1) the result depends upon the entries. Sir *W. Grant* in that case said: "But this is the case of a banking account where all the sums paid in form one blended fund, the parts of which have no longer any distinct existence. Neither banker nor customer ever thinks of saying, This draft is to be placed to the account of the £500 paid in on Monday, and this other to the account of the £500 paid in on Tuesday. There is a fund of £1000 to draw upon, and that is enough. In such a case there is no room for any other appropriation than that which arises from the order in which the receipts and payments take place and are carried into the account. Presumably it is the sum first paid in that is first drawn out. It is the first item on the debit side of the account that is discharged or

reduced by the first item on the credit side. The appropriation is made by the very act of setting the two items against each other." The difficulty seems to be that the rule in that case has been applied by the Court of Appeal to a case between trustee and *cestui que trust*. I have already stated how I should be inclined to act if I had liberty, but I am not at liberty. It is for the payer to appropriate, but, failing that, the payee may appropriate and may enter the payments as he likes. As between banker and customer the banker is the payee and the customer is the payer, and if the customer says nothing the banker may appropriate. The Courts have said that that principle binds trustee and *cestui que trust*. If the two sums had been entered in one line of a double column, that might have shewn that it was the same sum, but that has not been clone. The trustees have failed, and will get nothing.

From this judgment appeals were brought by the Plaintiff, by the trustees of *Hallett's* settlement, and by Mrs. *Cotterill*.

(1) 1 Mer. 572, 608.

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The appeals came on for hearing on the 26th of November, 1879.

The Plaintiff's appeal was heard first.

As to the claim of the trustees of *Hallett's* settlement,

Higgins, Q.C., and ***B. Fossett Lock***, for the Plaintiff:-

The trustees have no priority over the general creditors. There is no sufficient evidence that the Russian bonds were purchased with trust money, or that there was any appropriation of them to the trust. The memorandum in the fold of the settlement did not amount to a declaration of trust. It was never communicated to the trustees of the settlement.

J. Pearson, Q.C., and ***Dundas Gardiner***, for the trustees of *Hallett's* settlement:-

There is sufficient evidence of the appropriation of Russian bonds to the trusts of the settlement. It

was *Hallett's* duty to invest the fund, and less evidence is required in the case of a person who is bound to appropriate than in the case of one who is not. The memorandum is a good declaration of trust by *Hallett:* at all events it is an admission against his own interest: *In re Strahan* (1).

Higgins, in reply.

THE COURT reserved judgment on this claim.

As to Mrs. *Cotterill's* claim,

Higgins, Q.C., and ***B. Fossett Lock***, for the Plaintiff:-

In this case *Hallett* was not a trustee at all. He was a mere bailee of Mrs. *Cotterill's* money. He was not even in a fiduciary position. Therefore the money cannot be followed into his hands. The fact of his receiving the dividends for her makes no difference. A banker does not become a trustee because bonds are deposited with him, but he may receive the coupons: *Ex parte Dale & Co*. (2); *Scott v. Surman* (3); *Whitecomb v. Jacob* (4).

[JESSEL, M.R.:- The decision in *Whitecomb v. Jacob* is based

(1) 8 D. M. & G. 291.

(2) 11 Ch. D. 772.

(3) Willes, 400.

(4) 1 Salk. 161.

upon a wrong reason. It is said there, "In regard that money has no ear-mark, equity cannot follow that in behalf of him that employed the factor." It has been often held since that money may be ear-marked.]

De Gex, Q.C., and ***E. Beaumont***, for Mrs. *Cotterill*, were not called on.

Dec. 3. The judgments on these two claims were delivered this day.

Claim of the Trustees of Hallett's Settlement.

JESSEL, M.R. :-

In the first appeal from Mr. Justice *Fry* the question is purely one of facts, or rather, as there is no dispute about the facts, what is the proper inference to he derived from the undisputed facts. Substantially the question is whether a considerable sum of trust money was invested by *Hallett* along with other trust money in the purchase of £2590 Russian bonds. Mr. Justice *Fry* has come to the conclusion that it was, and I am not disposed to differ from him. *Hallett* was a solicitor, and the case unfortunately presents one more instance of a solicitor betraying his trust; and the question is whether his numerous other clients, whose money he had misappropriated, or the trustees of his marriage settlement, whose money he had also misappropriated, are to suffer. The trust money appears to have been invested by *Hallett* at first in some mortgages. That was not made payable to the trustee, but to *Hallett*, and he received the interest, as he was entitled to do under the settlement, during his life. The last mortgage on which the money was invested was on the estate of a Mr. *Walker*. That mortgage was paid off in 1869. *Hallett* received the money. What he did with it is not clear, but there can be no doubt he appropriated it in some way to his own use. He had in his possession a large quantity of Russian bonds, and among them the £2590 Russian bonds in question, and whereas he used before 1870 to enter the interest on them in a lump sum, he now carried the bonds for £2590 to a separate account, and made entries of them as "self trust," entering the interest separately from the

interest on the other bonds. At some time or other he made a memorandum in the fold of the draft of his marriage settlement which contained this sentence: "The money remained in *Great George Street* until September, 1865, when it was invested in *Walker's* estate. *Walker's* mortgage was paid off in November, 1870, and invested in £2590 Russian £5 *per* Cent. Stock." This being in his handwriting is evidence against him. There is in addition this singular fact. He took to his bankers a

large quantity of Russian bonds in two parcels. The envelope of one parcel has not been found, but the envelope of the other has an indorsement on it shewing that it contained bonds for £2442, the correct amount of bonds which he held in trust for another person, Mrs. *Cotterill*; and this amount, added to the bonds for £2590 claimed by *Hallett's* trustees, would make up the £5032 which he deposited on that occasion. When you see that he had other Russian bonds of his own, and took out some and deposited them in separate parcels, and that one of those parcels contained bonds held by him in a fiduciary relation, we may conclude that the other parcel was kept separate for no other purpose but appropriation. This is a circumstance corroborating the statement in his own handwriting. I am therefore of opinion that the trustees are entitled to the bonds which they claim, and are entitled to the produce of the sale of them. The judgment of Mr. Justice *Fry* on this point must therefore be affirmed.

BAGGALLAY andTHESIGER, L.JJ. , concurred.

Claim of Mrs. Cotterill.

JESSEL, M.R. :-

The second appeal from Mr. Justice *Fry* in this case raises, in my opinion, not a question of fact, for the fact is indisputable, but a question of law of very considerable importance. The facts necessary to be stated are very few. A Mrs. *Cotterill* either had some money, which Mr. *Hallett* had invested for her in the purchase of Russian bonds, which I think is the more probable version of the transaction, for her memory does not appear to be very accurate, or she had some Russian bonds which he had delivered

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to her and she re-delivered to him; it is utterly immaterial. What is proved in the case is that he gave her a receipt, which of course is binding against him and his estate, for a *Russian Bond and Waggon Company* debenture bonds. It appears that he had bonds to that amount in his possession, and it also appears that the exact amount was deposited by him with his bankers in a separate parcel in 1873. I think Mrs. *Cotterill* is not called upon to prove any more, and therefore as against Mr. *Hallett* and his legal personal representative these bonds are her bonds deposited with Mr. *Hallett*, according to the receipt, for safe custody, which would make him, no doubt, an ordinary bailee. In addition to that, it appears that Mr. *Hallett* was in the habit of receiving the income arising from these bonds on behalf of Mrs. *Cotterill.* I suppose he or the bankers cut off the coupons, and he received the money and accounted for the exact amount to her every half year. This receivership, of course, was the receivership of an agent - it was as bailee; therefore he was bailee of the bonds, and an agent to receive the dividends on the bonds. There is no doubt, therefore, that Mr. *Hallett* stood in a fiduciary position towards Mrs. *Cotterill*. Mr. *Hallett*, before his death, I regret to say, improperly

sold the bonds and put the money to his general account at his bankers. It is not disputed that the money remained at his bankers mixed with his own money at the time of his death; that is, he had not drawn out that money from his bankers. In that position of matters Mrs. *Cotterill* claimed to be entitled to receive the proceeds, or the amount of the proceeds, of the bonds out of the money in the hands of Mr. *Hallett's* bankers at the time of his death, and that claim was allowed by the learned Judge of the Court below, and I think was properly so allowed. Indeed, as I understand the doctrines of Equity, it would have been too clear a case for argument, except for another decision of that learned Judge himself, *Ex parte Dale & Co.* (1). The modern doctrine of Equity as regards property disposed of by persons in a fiduciary position is a very clear and well-established doctrine. You can, if the sale was rightful, take the proceeds of the sale, if you can identify them. If the sale was wrongful, you can still take the proceeds of the sale, in a sense adopting the sale for the purpose of

(1) 11 Ch. D. 772.

taking the proceeds, if you can identify them. There is no distinction, therefore, between a rightful and a wrongful disposition of the property, so far as regards the right of the beneficial owner to follow the proceeds. But it very often happens that you cannot identify the proceeds. The proceeds may have been invested together with money belonging to the person in a fiduciary position, in a purchase. He may have bought land with it, for instance, or he may have bought chattels with it. Now, what is the position of the beneficial owner as regards such purchases? I will, first of all, take his position when the purchase is clearly made with what I will call, for shortness, the trust money, although it is not confined, as I will shew presently, to express trusts. In that case, according to the now well-established doctrine of Equity, the beneficial owner has a right to elect either to take the property purchased, or to hold it as a security for the amount of the trust money laid out in the purchase; or, as we generally express it, he is entitled at his election either to take the property, or to have a charge on the property for the amount of the trust money. But in the second case, where a trustee has mixed the money with his own, there is this distinction, that the *cestui que trust*, or beneficial owner, can no longer elect to take the property, because it is no longer bought with the trust-money simply and purely, but with a mixed fund. He is, however, still entitled to a charge on the property purchased, for the amount of the trust-money laid out in the purchase; and that charge is quite independent of the fact of the amount laid out by the trustee. The moment you get a substantial portion of it furnished by the trustee, using the word "trustee" in the sense I have mentioned, as including all persons in a fiduciary relation, the right to the charge follows. That is the modern doctrine of Equity. Has it ever been suggested, until very recently, that there is any distinction between au express trustee, or an agent, or a bailee, or a collector of rents, or anybody

else in a fiduciary position? I have never heard, until quite recently, such a distinction suggested. It cannot, as far as I am aware (and since this Court sat last to hear this case, I have taken the trouble to look for authority), be found in any reported case even suggested, except in the recent decision of Mr. Justice *Fry*, to which I shall draw attention presently. It can have no foundation in principle,

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because the beneficial ownership is the same, wherever the legal ownership may be. If you have goods bargained and sold to a man upon trust to sell and hand over the net proceeds to another, that other is the beneficial owner; but if instead of being bargained and sold, so as to vest the legal ownership in the trustee, they are deposited with him to sell as agent, so that the legal ownership remains in the beneficial owner, can it be supposed, in a Court of Equity, that the rights of the beneficial owner are different, he being entire beneficial owner in both cases? I say on principle it is impossible to imagine there can be any difference. In practice we know there is no difference, because the moment you get into a Court of Equity, where a principal can sue an agent as well as a *cestui que trust* can sue a trustee, no such distinction was ever suggested, as far as I am aware. Therefore, the moment you establish the fiduciary relation, the modern rules of Equity, as regards following trust money, apply. I intentionally say modern rules, because it must not be forgotten that the rules of Courts of Equity are not, like the rules of the Common Law, supposed to have been established from time immemorial. It is perfectly well known that they have been established from time to time - altered, improved, and refined from time to time. In many cases we know the names of the Chancellors who invented them. No doubt they were invented for the purpose of securing the better administration of justice, but still they were invented. Take such things as these: the separate use of a married woman, the restraint on alienation, the modern rule against perpetuities, and the rules of equitable waste. We can name the Chancellors who first invented them, and state the date when they were first introduced into Equity jurisprudence; and, therefore, in cases of this kind, the older precedents in Equity are of very little value. The doctrines are progressive, refined, and improved; and if we want to know what the rules of Equity ale, we must look, of course, rather to the more modern than the more ancient cases.

Now that being the established doctrine of Equity on this point, I will take the case of the pure bailee. If the bailee sells the goods bailed, the bailor can in Equity follow the proceeds, and can follow the proceeds wherever they can be distinguished, either being actually kept separate, or being mixed up with other

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moneys. I have only to advert to one other point, and that is this - supposing, instead of being invested in the purchase of land or goods, the moneys were simply mixed with other moneys of the trustee, using the term again in its full sense as including every person in a fiduciary relation, does it make any difference according to the modern doctrine of Equity? I say none. It would be very remarkable if it were to do so. Supposing the trust money was 1000 sovereigns, and the trustee put them into a bag, and by mistake, or accident, or otherwise, dropped a sovereign of his own into the

bag. Could anybody suppose that a Judge in Equity would find any difficulty in saying that the *cestui que trust* has a right to take 1000 sovereigns out of that bag? I do not like to call it a charge of 1000 sovereigns on the 1001 sovereigns, but that is the effect of it. I have no doubt of it. It would make no difference if, instead of one sovereign, it was another 1000 sovereigns; but if instead of putting it into his bag, or after putting it into his bag, he carries the bag to his bankers, what then? According to law, the bankers are his debtors for the total amount; but if you lend the trust money to a third person, you can follow it. If in the case supposed the trustee had lent the £1000 to a man without security, you could follow the debt, and take it from the debtor. If he lent it on a promissory note, you could take the promissory note; or the bond, if it were a bond. If, instead of lending the whole amount in one sum simply, he had added a sovereign, or had added £500 of his own to the £1000, the only difference is this, that instead of taking the bond or the promissory note, the *cestui que trust* would have a charge for the amount of the trust money on the bond or promissory note. So it would be on the simple contract debt; that is, if the debt were of such a nature as that, between the creditor and the debtor, you could not sever the debt into two, so as to shew what part was trust money, then the *cestui que trust* would have a right to a charge upon the whole. Therefore, there is no difficulty in following out the rules of Equity and deciding that in a case of a mere bailee, as Mr. Justice *Fry* has decided, you can follow the money.

Having said so much, I feel bound to say something about the authorities, and for two reasons. First of all, this decision of Mr. Justice *Fry's* to which I have referred is reported, and therefore,

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in my opinion, may do mischief if not corrected; and, secondly, because it appears to me, speaking with the greatest possible respect of such an eminent master of Equity as Mr. Justice *Fry*, that he has entirely misconceived the proper use of authorities in holding himself to be bound by a long line of authorities, to decide against that which he saw most clearly was good equity; in other words, he decided against his own opinion as to the rules of Equity, in obedience, as he thought, to a series of authorities, opposed, as he conceived, to all principle, because he thought he was bound so to do, as it appears to me, in utter oblivion of what I will take the liberty of stating is the right mode of viewing authorities, and also in oblivion of that salutary provision of the *Judicature Act* which says that where there is a difference between the principles of Law and Equity, the rules of Equity are to prevail.

First of all, what is the proper use of authorities? This is almost elementary, but I am bound to state it, because, as I will shew presently, that use has not been made in the case on which I am going to comment. The only use of authorities, or decided cases, is the establishment of some principle which the Judge can follow out in deciding the case before him. There is, perhaps, nothing more important in our law than that great respect for the authority of decided cases which is shewn by our tribunals. Were it not for that our law would be in a most distressing state of uncertainty; and so strong has that been my view, that where a case has decided a principle, although I myself do not

concur in it, and although it has been only the decision of a tribunal of co-ordinate jurisdiction, I have felt bound to follow it where it is of respectable age and has been used by lawyers as settling the law, leaving to the Appellate Court to say that case is wrongly decided, if the Appellate Court should so think.

Now when we come to look at the case which was before Mr. Justice *Fry*, the case of *Ex parte Dale & Co.* (1), we shall find him saying this: "Does it make any difference that instead of trustee and *cestui que trust* it is a case of fiduciary relationship? What is a fiduciary relationship? It is one in respect of which, if a wrong arise, the same remedy exists against the wrongdoer on

(1) 11 Ch. D. 772, 778.

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behalf of the principal as would exist against a trustee on behalf of the *cestui que trust*. If that be a just description of the relationship, it would follow that wherever fiduciary relationship exists, and money coming from the trust lies in the hands of persons standing in that relationship, it can be followed and separated from any money of their own. That seems to me to be the logical result of *Pennell v. Deffell*" (1). Up to that point I agree with every syllable, and I think it would be impossible to express the doctrine more clearly than it is there expressed by Mr. Justice *Fry*. But now comes the unfortunate result, "but that result is opposed to the long line of authorities to which I have referred, and from which I do not feel myself justified upon any reasoning of my own in departing." So he here decided the case wrongly and against his own opinion and against the case of *Pennell v. Deffell* in deference to a long line of authorities. That being so, I feel bound to examine his supposed long line of authorities, which are not very numerous, and shew that not one of them lends any support whatever to the doctrine or principle which he thinks is established by them.

The first case is the well-known case of *Whitecomb v. Jacob* (2). I may say the cases are so fully extracted, if I may use the word, in Mr. Justice *Fry's* judgment as regards the material portions of them, that it is more convenient to read them from that than it is from the reports themselves, which I have looked at. "If one employs a factor and entrusts him with the disposal of merchandise, and the factor receives the money and dies indebted in debts of a higher nature, and it appears by evidence that this money was vested in other goods and remains unpaid, those goods shall be taken as part of the merchant's estate and not the factor's" (that is, you may follow the money or the goods); "but if the factor have the money, it shall be looked upon as the factor's estate, and must

first answer the debts of a superior creditor, &c.; for, in regard that money has no ear-mark, Equity cannot follow that in behalf of him that employed the factor"(3). Now let us see, therefore, what *Whitecomb v. Jacob* decides. It decides that the equity as to following the proceeds attaches to the case of a factor

(1) 4 D. M. & G. 372.

(2) 1 Salk. 161.

(3) 11 Ch. D. 775.

as well as to the case of *cestui que trust* and trustee. That is what it decides; but it decides, secondly, that you could not follow money because it had no ear-mark. The first part is good law at the present day; the second is not. Whether it was good law or not at the time of *Salkeld* it is immaterial to consider. It is very doubtful whether Equity had got quite so far at that date as since, and therefore I will not say it was not: but it is not so now. The first part is good law and the second part is not, and therefore *Whitecomb v. Jacob* (1) is no authority at all on the second point on which it was decided, and so Mr. Justice *Fry* said. Then Mr. Justice *Fry* proceeds in his judgment to say, "Now, with the single exception that it appears to have been held subsequently that money may be so far ear-marked that it may be followed if it has been kept separate, that case appears to have been always held to be an authority;" that is to say, with the single exception that the sole ground for the decision has been overruled, it is to be an authority! Did ever any one hear anything, if I may say so, so extraordinary as such a comment on an old case? The sole ground of that decision was that, although as a general rule you may follow the proceeds as against the factor, as you may against the trustee in Equity, yet, because money has no ear-mark, you cannot follow it. That is overruled, and still the Judge holds it to be an authority. It appears to me no authority at all, the sole ground of the decision having been long since overruled - indeed it was overruled by some of the authorities which Mr. Justice *Fry* cites. He goes on, "In the celebrated case of *Ryall v. Rolle* (2) Mr. Justice *Burnet*, in delivering judgment, says: 'Suppose goods are consigned to a factor who sells them and breaks, the merchant for the money must come in as a creditor under the commission; but if the money is laid out in other goods these goods will not be subject to the bankruptcy.'" It is the same as

Whitecomb v. Jacob. You may follow the goods, but you cannot follow the money. That is no longer law. In bankruptcy no part of the law is better settled than that if the money be kept separate it does not fall into the general estate. It has been decided by a long line of cases in bankruptcy, and there is no doubt about it if it is kept separate; but Mr. Justice *Burnet* only said what was said in the

(1) 1 Salk. 161.

(2) 1 Atk. 165.

case in *Salkeld*; the notion being that yon could not follow money, a notion which was prevalent at that time. That part of *Ryall v. Rolle* (1) is as much overruled as the case of *Whitecomb v. Jacob* (2). But it is to be observed that the Judges thought then that you could not follow money in Equity, not that you could not follow it between principal and agent or merchant and factor, they thought that you could not follow it at all, even as between trustee and *cestui que true* trust, because money had no ear-mark. It is not an authority for a distinction between the case of principal and agent and the case of *cestui que trust* and trustee; it is an authority, if it is an authority for anything, that you cannot follow money in that way. Then Mr. Justice *Fry* says, "In another case of *Ex parte Dumas* (3), before Lord *Hardwicke*, the petitioners were certain persons who bad claimed bills arising from the produce of certain goods transmitted to them, and the Lord Chancellor said: 'Suppose the petitioners had consigned over goods to *Jullian* as their factor, and he had sold them and turned them into money, the principal then could only have come in as a general creditor under the commission; but if the goods had continued in specie and bad been found in *Jullian's* hands at the time of his bankruptcy, it would have been otherwise, and has been so determined in several cases.'" There it is to be noticed that the expression is "turned them into money," but nothing is said about the money being kept separate or not. I looked into the late Mr. *Lewin's* book on Trustees to see what he said about this case, because it is very odd that Lord *Hardwicke* should say so, and what Mr. *Lewin* says is that it seems in the time of Lord *Hardwicke* it was supposed that you could not follow money in Equity, which perhaps is the explanation, namely, that the doctrine is more modern than his decision. This is certainly not law now. As I said before there is no doubt in bankruptcy if the money is kept separate it can be followed; but it is the same proposition. It is not as if there were any difference between the position of factor and the position of trustee, but it is that you cannot follow the money. That he treats as well ascertained law at that time. Then Mr. Justice *Fry* goes on to say this, "Mr. Justice *Willes*, in delivering the considered

(1) 1 Atk. 165.

(2) 1 Salk. 161.

(3) 1 Atk. 232.

judgment of the Court of Common Pleas in the case of *Scott v. Surman* (1)" - I do not understand that a judgment is any better for being held over a long time, for I think judgments are perhaps best if delivered when the facts are fresh in the Judge's mind; but I do not say that they are either better or worse - "says: 'We are all agreed that if the money for which the tar had been sold had been all paid to the bankrupt before his bankruptcy, and had not been laid out again by him in any specific thing to distinguish it from the rest of his estate, in that case the Plaintiffs could not have recovered anything in this action, but must have come in as creditors under the commission, as is laid down in the case of *Whitecomb v. Jacob* (2) and in many other cases.'"

Now, first of all, that is merely a *dictum* of that very eminent Judge, Mr. Justice *Willes*, and he has not adverted to the distinction between money ear-marked and money not ear-marked. He has simply quoted from *Whitecomb v. Jacob* without considering it at all. If you read it literally, it means if it has not been laid out on any specific thing. Now that was not law in his time in bankruptcy, and I am quite sure if Mr. Justice *Willes*' attention had been called to the phrase used he would have said it was too general. If the money had been laid aside by the bankrupt, and put into a bag, and marked, you could take the money. I think Mr. Justice *Willes* would have qualified it. It is a mere dictum, and it really only follows *Whitecomb v. Jacob*. Then Mr. Justice *Fry* says: "In the year 1800 the Lord Chancellor, in *Ex parte Sayers* (3), adopted the same view." That was Lord *Thurlow*. "He considered that there were in that case special circumstances which shewed that, although the money had got into the general fund constituting the estate of the bankrupt, it had got out again; and he said it had acquired an identity and a distinction from the rest of the fund. Still he adopted the general principle that if it had been in the form of money at the time of the bankruptcy, the creditor could only rank with the other creditors." It is quite true he said so, but again the same

observation applies. He states it generally on the supposition of the factor having turned the goods into money, without distinguishing, between the cases of the

(1) Willes, 400.

(2) 1 Salk. 161.

(3) 5 Ves. 169.

money being kept separate and the cases where it was mixed with his own, and could not be followed.

Now we come to a case which I am glad to say is the last - the well-known case of *Taylor v. Plumer* (1), where we have the decision of a great Judge, no doubt, Lord *Ellenborough*; and there he entirely throws over all the prior decisions as to money not ear-marked not being followed. At that time it was well known it could be ear-marked in Equity; and therefore when you come to look at it you will find it an express decision in conflict with all the others cited as to the ear-marking of money. Lord *Ellenborough* says this: "It makes no difference in reason or law into what other form different from the original the change may have been made" - there I agree with him most cordially in reason and in law - "whether it be into that of promissory notes for the security of the money which was produced by the sale of the goods of the principal, as in *Scott v. Surman* (2)" - and I say whether it be a simple contract debt or not it is the same thing - "or into other merchandise, as in *Whitecomb v. Jacob* (3), for the product of or substitute for the original thing still follows the nature of the thing itself as long as it can be ascertained to be such." That, it I may say so, is law at the present moment; and though I cannot say it always was law, it always ought to have been law, because it is consonant with principle. Now comes the point, "and the right only ceases when the means of ascertainment fail." That is correct. Now there comes a point which is not correct, but which I am afraid only ceases to be correct because Lord *Ellenborough's* knowledge of the rules of Equity was not quite commensurate with his knowledge of the rules of Common Law, "which is the case when the subject is turned into money, and mixed and confounded in a general mass of the

same description." He was not aware of the rule of Equity which gave you a charge - that if you lent £1000 of your own and £1000 trust money on a bond for £2000, or on a mortgage for £2000, or on a promissory note for £2000, Equity could follow it, and create a charge; but he gives that, not as law - the law is that it only fails when the means of ascertainment fail - he gives it as a case

(1) 3 M. & S. 562.

(2) Willes, 400.

(3) 1 Salk. 161.

in which the means of ascertainment fail, not being aware of this refinement of Equity by which the means of ascertainment still remain. With the exception of that one fact, which is rather a fact than a statement of law, the rest of the judgment is in my opinion admirable. It goes on: "The difficulty which arises in such a case is a difficulty of fact, and not of law, and the *dictum* that money has no ear-mark must be understood in the same way, *i.e.*, as predicated only of an undivided and undistinguishable mass of current money." There, again, as I say, he did not know that Equity would have followed the money, even if put into a bag or into an undistinguishable mass, by taking out the same quantity.

Now, I have finished the authorities cited by Mr. Justice *Fry*. Is there one of them (and I say there is not) which suggests there is any difference in the position of the factor and the position of the trustee as regards following money? So far from that being the case, they all proceed on the ground that there is no such distinction, and the only reason of the difficulty was that which was so lucidly expressed by Lord *Ellenborough*, the difficulty of ascertainment.

Now I come, before parting with the case, to the decision of *Pennell v. Deffell* (1), which is an Equity case decided by the Court of Appeal in Chancery, and therefore of as high authority as any of those cases cited, and of greater weight, because it is more modern than the decisions of Lord

Hardwicke and Lord *Thurlow*; and, if inconsistent with them, would have overruled them. What is said in *Pennell v. Deffell*? Lord Justice Knight *Bruce* there supposes the case of a trust fund kept separate, and he then refers to the case of a trust fund mingled with the other money; that is, if the trustee in the case I suppose put the money in a box with his other money, it would make no difference to the *cestui que trust* except that he would have the right to take the first money out of the box; and then he says, "But not in either case, as I conceive, would the blending together of the trust moneys, however confusedly, be of any moment as between the various *cestuis que trustent* on the one hand and the executors, as representing the general creditors, on the other."

Now, in addition to that, I will only refer to one other case. It

(1) 4 D. M. & G. 372.

is a very good case, and it is again the decision of a well-known Equity Judge, whom we are delighted still to have living among us. It is the case of *Frith v. Cartland* (1). I will read the marginal note: "The rules as to following trust funds in the hands of a defaulting trustee apply against the assignees of a defaulting trustee as fully as against the trustee himself" (that is, they apply in bankruptcy as well as they do on death), "and the circumstance that the trust fund was acquired on the eve of the bankruptcy, and when the bankrupt was about to abscond with that and his other moneys: held, not to raise any equity in favour of the assignees." Now I read that because the man, as it will be seen, was an agent, and Vice-Chancellor *Wood* never dreamt it made any difference, nor anybody else. The facts of the case are these. [His Lordship then referred to the facts as stated in the report, and continued:-] Now the Vice-Chancellor says this(2): "*Pennell v. Deffell* (3) is a very instructive case upon all questions of this kind." I am citing the case for the next remark which, I think, would have presented itself to Mr. Justice *Fry*. "It does not, indeed, lay down any new principle, but it contains a particularly clear and able enunciation of established doctrines in their bearing upon circumstances of some difficulty. The guiding principle is, that a trustee cannot assert a title of his own to trust property. If he destroys a trust fund by dissipating it altogether there remains nothing to be the subject of the trust. But so long as the trust property can be traced and followed into other property into which it has been converted that remains subject to the trust. A second principle is, that if a man mixes trust funds with his own, the whole will be treated as the trust property, except so far as he may be able to distinguish what is his own," that is, that the trust property comes first. Now, I think it would have been well if this, which was stated as established Equity law in *Frith v. Cartland* by Vice-Chancellor *Wood*, had been accepted and

adopted in the case of *Ex parte Dale & Co.* (4). Then he says: "If a man has £1000 of his own in a box on one side and £1000 of trust property in the same box on the other side, and then takes out £500 and applies it to his own

(1) 2 H. & M. 417.

(2) Ibid. 420, 421.

(3) 4 D. M. & G. 372.

(4) 11 Ch. D. 772.

purposes, the Court will not allow him to say that that money was taken from the trust fund. The trust must have its £1000 so long as a sufficient sum remains in the box. So here, *Edwards* could not be allowed to say that the £284 deposited in the *Bank of England* was his own, and that the trust portion of the fund was that which he took abroad with him, and from which he drew as he required for his own purposes. There is therefore no difficulty in treating that sum at the bank as belonging to the trust together with what remains of the sum which he took abroad."

I think after those authorities it must now be considered settled that there is no distinction, and never was a distinction, between a person occupying one fiduciary position or another fiduciary position as to the right of the beneficial owner to follow the trust fund, and that those cases which have been cited at Law so far from establishing a distinction, establish the contrary; and that the mere error of supposing that Equity could not follow or distinguish money in the cases supposed, if error it was, and perhaps it was not so originally (I am not sure that the doctrine of equity had got so far at the first start, but it was certainly an error at a later period), is attributable really to the fact that the Judges who followed the earlier cases were not aware of what I may call the gradual refinement of the doctrine of equity. Therefore, looking at the authorities to find out the principle,

you do not find out any such distinction established as that suggested by Mr. Justice *Fry*, or anything of the kind even mentioned in them; and I do not know of anything more mischievous than for a Judge to say, "The cases before me establish no principle, but they quite establish something else which I will now enunciate, and therefore hold myself bound by those cases to establish another principle which was never suggested or thought of by the Judges who decided the original cases." It is only out of my great respect and esteem for the learned Judge from whom this appeal comes that I have thought it right to go so fully into the cases to shew that there is no foundation whatever for the suggested distinction, and therefore his decision in this case rests on no trivial or slight distinction between this case and the case of *Ex parte Dale & Co.* (1), but is grounded on the well-ascertained doctrines of equity.

(1) 11 Ch. D. 772.

Before I part with the case I will only say a word or two more. There was cited to Mr. Justice *Fry* a decision of the Appeal Court. It is reported in a note to the case of *Ex parte Dale & Co.* (1), and the name of it is *Birt v. Burt*. That was a case of money put into the bank. The only reason why I have not referred to it in the course of my judgment is, that I took part in the decision of the appeal, together with Chief Justice *Coleridge* and Lord Justice *Baggallay*, and we considered the case too clear for argument, and dismissed the appeal with costs.

BAGGALLAY, L.J. :-

I am also of opinion that this appeal should be dismissed. It appears to me sufficient, to support the conclusion at which I have arrived, to say that I entirely agree with Mr. Justice *Fry* in opinion that, upon the facts and the law of the case, *Hallett* stood in a fiduciary position, that he violated his duty, that Mrs. *Cotterill* consequently had the same right to relief against him as if he had been a trustee under the more common designation of the term, and that under those circumstances she had a right to follow the produce of the sale of the bonds. Nor should I have thought it necessary to have at all adverted to the case of *Ex parte Dale & Co.*, which had been previously decided by Mr. Justice *Fry*, had it not been that the Master of the Rolls has very closely examined the judgment in that case, and expressed his disapprobation of the decision arrived at. Now I cannot forget that *Ex parte Dale & Co.* is a decision of very recent date, and that it may possibly come before the Court of which I am a

member by way of appeal; and for this reason I should desire to keep my mind as free from any bias or prejudice upon it as possible; but at the same time, so far as the grounds of the decision in that case appear in the printed report of the judgment, and accepting that report as being perfectly and in all respects correct, I think it right to express an opinion upon it. It must be borne in mind that Mr. Justice *Fry* arrived at the conclusion, at which he did arrive in that case, with much hesitation, and that he apparently would have arrived at a different conclusion, had he not felt himself bound by certain authorities, to which he alluded,

(1) 11 Ch. D. 772.

and from which he stated that he did not feel himself justified in departing, though he regarded them as inconsistent with the general principles of equity applicable to cases involving fiduciary relationship. Assuming there to have been nothing more in the case than appears in the printed report, I feel bound to say that I cannot concur in the view expressed by Mr. Justice *Fry* as to the binding character of the authorities to which he referred.

THESIGER, L.J. :-

The facts of this case are undisputed, and the inference to be drawn from them is so clear, that I need say no more than that I entirely agree with the view that was taken by Mr. Justice *Fry* with reference to that inference. With regard to the law applicable to the case, we have had an elaborate exposition of that law from the Master of the Rolls, and in the main features of that exposition I entirely agree; but I must add, at the same time, that the principles which have been laid down to-day are no new principles, and have been laid down recently in this Court, not only in the case to which the Master of the Rolls has referred of *Birt v. Burt* (1), but also in the case of *Ex parte Cooke* (2). If the judgment of Lord Justice *Bramwell* is looked at in that case, it will appear that even to the mind of a Common Law Judge the principles of law which have been applied now for some time in Equity have been made perfectly plain. It has been established for a very long period, in cases at Law as well as in cases in Equity, that the principles relating to the following of trust property are equally applicable to the case of a trustee, using the term in the narrow and technical sense which is applied to it in the Court below, and to the case of factors, bailees, or other ands of agents. It has been also established, and for a long period, and I think, notwithstanding the observations of the

Master of the Rolls that that has been present to the mind of the Common Law Judges as well as to the mind of Equity Judges, that those principles may, under certain circumstances, be applicable to money as well as to specific chattels. The principle of law may be stated, as it appears to me, in the form of a very simple, although at the same time very wide and general proposition. I would state that proposition in these

(1) 11 Ch. D. 773, n.

(2) 4 Ch. D. 123.

terms, namely, that wherever a specific chattel is intrusted by one man to another, either for the purposes of safe custody or for the purpose of being disposed of for the benefit of the person intrusting the chattel; then, either the chattel itself, or the proceeds of the chattel, whether the chattel has been rightfully or wrongfully disposed of, may be followed at any time, although either the chattel itself, or the money constituting the proceeds of that chattel, may have been mixed and confounded in a mass of the like material. I may say that that proposition, wide as it is, was adopted almost in those terms by Lord Justice *Bramwell* in the case to which I have referred. There is no doubt that there are to be found here and there in the books, *dicta*, principally of Common Law Judges, which would appear to militate against the generality of that proposition, and which would appear to shew that in the minds of those Judges there was the view, that while chattels might be followed, or money so long as it could be looked upon as a specific chattel, as moneys numbered and placed in a bag, yet when those moneys had been mixed with other moneys that there was no ear-mark, and neither at Law nor in Equity could they be followed. With reference, however, to those *dicta*, it appears to me there are two observations to be made. In the first place I cannot find any decision which has followed out those *dicta* to their consequence, assuming that those *dicta* are to be treated as having the generality which at first sight attaches to them. And, in the second place, it appears to me that in many cases those *dicta*, looking to the facts of the particular case, may be restrained to those facts, and possibly may have a more limited meaning than that which has been attached to them by Mr. Justice *Fry* in the case of *Ex parte Dale & Co.* (1), or by the Master of the Rolls in his judgment in the present case. As far as I can judge, the only exception to the general proposition which I have stated is not a real exception, but an apparent exception, for all cases where it has been held that moneys mixed and confounded, but still existing, in a mass cannot be followed, may, I think, be resolved into cases where, although there may have been a trust with

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reference to the disposition of the particular chattel which those moneys subsequently represented, there was no trust, no

(1) 11 Ch. D. 772.

duty in reference to the moneys themselves beyond the ordinary duty of a man to pay his debts; in other words, that they were cases where the relationship of debtor and creditor had been constituted, instead of the relation either of trustee and *cestui que trust*, or principal and agent. I think it unnecessary, and to my mind it is undesirable, to give an opinion upon the case of *Ex parte Dale & Co.* (1) until we see upon a case properly brought upon appeal, and when it is necessary to decide the point, whether that case does or does not come within the exception to which I have referred.

The appeals of the trustees of *Hallett's* settlement and Mrs. *Cotterill* were then heard.

J. Pearson, Q.C., and ***Dundas Gardiner***, for the Appellants:-

We appeal from so much of Mr. Justice *Fry's* order as directed that the claim of the trustees is to be governed by *Clayton's Case* (2). Mrs *Cotterill* appeals from the same decision, and if the Court allows the appeal, the balance left to *Hallett's* credit at his bankers will be sufficient for both of us; but if the Court is against us, a further question will arise as to the division of what is applicable to our claims between us and Mrs. *Cotterill.*

We contend, then, that the rule in *Clayton's Case*, by which the earliest drawings are to be appropriated to the earliest payments, does not apply to a case like this, in which trust moneys were mixed with the customer's own moneys. It is only a general rule based on a presumption of law which may be rebutted by the intention of the parties or the circumstances: *City Discount Company v. McLean* (3). It is well settled that if an act which has been done may have been done honestly, the man who does it cannot say that he has done it dishonestly. If a man mixes his own money with trust money, and draws some out, he must be taken to have drawn out his own money, and cannot be allowed to say that he has stolen the money deposited with him: *Pinkett v. Wright* (4); *Ex parte Kelly & Co.* (5). There is no difference in

(1) 11 Ch. D. 772.

(2) 1 Mer. 572.

(3) Law Rep. 9 C. P. 692.

(4) 2 Hare, 120.

(5) 11 Ch. D. 306.

principle between money kept by a trustee himself, and any deposits by him at a banker's to his own account. Mr. Justice *Fry* agreed with us in principle, but felt himself bound by the authority of *Pennell v. Deffell* (1). But the decision of the Lords Justices on that particular point is not borne out by the principles stated by them in the rest of their judgment. At all events this Court is not bound to follow that decision if it is contrary to the principles on which the Court has always acted.

De Gex, Q.C., and ***E. Beaumont***, for Mrs. *Cotterill*, supported the same view.

Higgins, Q.C., and ***B. Fossett Lock***, for the Plaintiff:-

The point in dispute was solemnly decided in *Pennell v. Deffell* after full argument, and this Court is bound by that authority. The principle of the decision has been recognised in subsequent cases: *Merriman v. Ward* (2); *Ex parte Dickin* (3); *Hooper v. Keay* (4); *Frith v. Cartland* (5); *Brown v. Adams* (6); *Middleton v. Pollock* (7); *Ex parte Cooke* (8). That decision was consistent with the law as previously recognised. The appropriation of payments is a question of fact, and is the same in Equity as Law. If one party wishes to appropriate, he must communicate his election to the other

party: *Simson v. Ingham* (9). If neither party appropriates, the earliest sums paid and repaid are set against one another. There is a broad distinction between sovereigns placed in a bag and money deposited with a banker. The latter ceases to exist in specie, and becomes a debt due from the banker. The principle of following trust money has never been carried to this extent. *Lord Chedworth v. Edwards* (10) is a distinct authority against it. If you can follow trust money into a banker's account, where can you stop? The account might be carried back to any length of time. The Plaintiff, who is a creditor of *Hallett*, is not estopped from saying that *Hallett* acted dishonestly, even though *Hallett* may have been estopped himself.

(1) 4 D. M. & G. 372, 384.

(2) 1 J. & H. 371.

(3) 8 Ch. D. 377, 384.

(4) 1 Q. B. D. 178.

(5) 2 H. & M. 417.

(6) Law Rep. 4 Ch. 764.

(7) 4 Ch. D. 49.

(8) Ibid. 123.

(9) 2 B. & C. 65.

(10) 8 Ves. 46.

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1880. Feb. 11.JESSEL, M.R. :-

This is an appeal from a decision of Mr. Justice *Fry*, and the singularity of the appeal is this, that it is an appeal in favour of Mr. Justice *Fry's* opinion and against his decision; the explanation of that being, that the learned Judge conceived himself bound by some decisions of the Appeal Court to decide against his own opinion; and I am far from saying that I dissent from him on either point - either on principle, as to how he thought the case ought to be decided, or on the question whether a Judge in his position as a Judge of first instance could very well have decided otherwise.

The question we have to consider depends on very few facts. I will first state all those which I think material, and on which it appears to me my judgment ought to be based. A Mr. *Hallett*, a solicitor, was a trustee of some bonds. Without authority and improperly he sold them, and on the 14th of November, 1877, by his direction the proceeds of these bonds were paid to his credit at Messrs. *Twinings' Bank*, and there mixed with moneys belonging to himself, to the credit of the same banking account, and he also drew out by ordinary cheque moneys from the banking account, which he used for his own purposes. He died in February, 1878, and at his death the account stood in this way: that there was more money to the credit of the account than the sum of trust money paid into it; but if you applied every payment made after November, 1877, to the first items on the credit side in order of date, a large portion of the trust money would have been paid out. The question really is, whether or not, under these circumstances, the beneficiaries - that is, the persons entitled to the trust moneys, who are the present Appellants - are or are not entitled to say that the moneys subsequently drawn out - that is, drawn out by Mr. *Hallett* subsequently to November, 1877 - and applied for his own use, are to be treated as appropriated to the repayment of his own moneys, or whether the Respondents, the executors, are right in their contention that they are to be treated as appropriated in the way I have mentioned, so as to diminish the amount now applicable to the repayment of the

trust; funds.

I will first of all consider the case on principle, and then I will

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consider how far we are bound by authority to come to a decision opposed to principle. It may well be, and sometimes does so happen, that we are bound to come to a decision opposed to principle. Now, first upon principle, nothing can be better settled, either in our own law, or, I suppose, the law of all civilised countries, than this, that where a man does an act which may be rightfully performed, he cannot say that that act was intentionally and in fact done wrongly. A man who has a right of entry cannot say he committed a trespass in entering. A man who sells the goods of another as agent for the owner cannot prevent the owner adopting the sale, and deny that he acted as agent for the owner. It runs throughout our law, and we are familiar with numerous instances in the law of real property. A man who grants a lease believing he has sufficient estate to grant it, although it turns out that he has not, but has a power which enables him to grant it, is not allowed to say he did not grant it under the power. Whereever it can be done rightfully, he is not allowed to say, against the person entitled to the property or the right, that he has done it wrongfully. That is the universal law.

When we come to apply that principle to the case of a trustee who has blended trust moneys with his own, it seems to me perfectly plain that he cannot be heard to say that he took away the trust money when he had a right to take away his own money. The simplest case put is the mingling of trust moneys in a bag with money of the trustee's own. Suppose he has a hundred sovereigns in a bag, and he adds to them another hundred sovereigns of his own, so that they are commingled in such a way that they cannot be distinguished, and the next day he draws out for his own purposes £100, is it tolerable for anybody to allege that what he drew out was the first £100, the trust money, and that he misappropriated it, and left his own £100 in the bag? It is obvious he must have taken away that which he had a right to take away, his own £100. What difference does it make if, instead of being in a hag, he deposits it with his banker, and then pays in other money of his own, and draws out some money for his own purposes? Could he say that he had actually drawn out anything but his own money? His money was there, and he had a right to draw it out, and why should the natural act of simply drawing

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out the money be attributed to anything except to his ownership of money which was at his bankers.

It is said, no doubt, that according to the modern theory of banking, the deposit banker is a debtor for the money. So he is, and not a trustee in the strict sense of the word. At the same time one must recollect that the position of a deposit banker is different from that of an ordinary debtor. Still he is for some purposes a debtor, and it is said if a debt of this kind is paid by a banker, although the total balance is the amount owing by the banker, yet considering the repayments and the sums paid in by

the depositor, you attribute the first sum drawn out to the first sum paid in. That was a rule first established by Sir *William Grant* in *Clayton's Case* (1); a very convenient rule, and I have nothing to say against it unless there is evidence either of agreement to the contrary or of circumstances from which a contrary intention must be presumed, and then of course that which is a mere presumption of law gives way to those other considerations. Therefore, it does appear to me there is nothing in the world laid down by Sir *William Grant* in *Clayton's Case*, or in the numerous cases which follow it, which in the slightest degree affects the principle, which I consider to be clearly established.

Then I come to the great difficulty in the case, the difficulty which, as I shall shew from an extract or two from Mr. Justice *Fry's* judgment, weighed with him. What he says is this: "If the matter were unfettered by authority, it would appear to me clear that where a man has a balance to his credit consisting in part of funds which are his own, and which he may legally draw out and apply for his own purposes, and in part of trust funds which he cannot lawfully draw out and apply for his own purposes, his drawings for his own purposes ought to be attributed to his own funds and not to the trust funds. But it appears to me that I am not at liberty, in the existing state of the authorities, to act according to the inclination of my own mind;" and then he refers to *Pennell v. Deffell* (2), and one or two cases that have followed it. In a second judgment in the same case, Mr. Justice *Fry* says this: "I have already expressed the opinion I should have been inclined to act on if I had been at liberty, but I

(1) 1 Mer. 572.

(2) 4 D. M. & G. 372.

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am not at liberty." So it is plain that, as far as Mr. Justice *Fry* was concerned, he would have decided otherwise if he had not been fettered by authority.

Now, the only authority worth considering for this purpose is the case of *Pennell v. Deffell* (1) itself. I will, in a moment, say a word about the subsequent decisions. First of all *Pennell v. Deffell*, one must remember, is the decision of a Court of co-ordinate jurisdiction with this Court, namely, the

Court of Appeal in Chancery, and was decided several years ago. But, on the other hand, we must remember that the law ascertained or laid down in the decision or judgment which guides a future Judge or another Judge in applying it, is simply the expression of principle which is to be ascertained from the judgment. No doubt a part of the decision in *Pennell v. Deffell* was exactly this case, and the Court applied the law, as correctly stated by Mr. Justice *Fry*, by applying *Clayton's Case* (2) even to such a case as this, and to that extent destroyed the claim of the *cestui que trust*. But that was not the whole case of *Pennell v. Deffell*. The main part of *Pennell v. Deffell* was giving effect to the right of *cestuis que trust* in the case of blended trust moneys, and upon the very principle which I have endeavoured to explain, and which, if I may say so, was so clearly explained by Mr. Justice *Fry* in his judgment. If, therefore, we are to ascertain the principle on which *Pennell v. Deffell* is decided, we must look at the whole of the judgment, and not at one part of it only. That being so, I have come to this conclusion, that the principle is rightly laid down, and it is rightly applied throughout the judgment except as to this portion, and that as to this portion of the case there has been a mistake, not in the principle, but in the application of the principle. Therefore, if I am to be guided by the principle as laid down, I think the principle must prevail without regard to a mere slip in its application.

But it will be said that this part of *Pennell v. Deffell* has been followed in subsequent cases. So it has. As regards subsequent cases in the inferior Courts we need not trouble ourselves with them. Judges of first instance would not have overruled the mistaken application of principle. As regards the Court of Appeal,

(1) 4 D. M. & G. 372.

(2) 1 Mer. 572.

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it seems to have been followed certainly in one, if not in two cases, without question; but although there are cases in our law where erroneous decisions, not reconcilable even with the judgment on which the decision proceeded, have created a rule of conduct, and as to which, after the lapse of years, Judges have not felt themselves at liberty to review the decision even by the light of the judgment on which the first decision was pronounced, yet no such considerations apply to this case. No human being ever gave credit to a man on the theory that he would misappropriate trust money,

and thereby increase his assets. No human being ever gave credit, even beyond that theory, that he should not only misappropriate trust moneys to increase his assets, but that he should pay the trust moneys so misappropriated to his own banking account with his own moneys, and draw out after that a larger sum than the first sums paid in for the trust moneys. It never could have been made a rule of conduct, or have affected the transactions of mankind, and therefore it does not come within the line of cases which, having established a rule of conduct, no Judge could interfere with. It appears to me we should not be deferring to authority but making a misuse of authority, which is to declare the law, if by reason of this, which appears to me a mere slip in the case of *Pennell v. Deffell* (1), and which, it must be recollected, was a very small portion of the contest in that case, we were to consider ourselves bound to decide against what is the settled principle. Therefore, in my opinion, the appeal must be allowed.

BAGGALLAY, L.J. :-

The circumstances under which this appeal is brought may be concisely stated as follows: on the morning of the 14th of November, 1877, there was a balance of £1796 5*s.* 2*d.* to the credit of Mr. *Hallett* on his banking account with Messrs. *Twining*, this balance was in no respect composed of trust moneys over which he had control, but had been entirely derived from his own resources. On that day he paid in to the credit of the account two sums, one of £770 10*s.* 5*d.* and the other of £1804 0*s.* 7*d.*, as to which I entirely concur in the opinion expressed by Mr. Justice *Fry*, that for the purposes of those proceedings they must ba regarded as trust

(1) 4 D. M. & G. 372.

moneys. With reference to these two sums it is to be observed that, though both were paid in on the same day, the entry of the receipt of the £770 10*s.* 5*d.* preceded that of the £1804 0*s.* 7*d.* in the books of Messrs. *Twining* and also in Mr. *Hallett's* pass-book. The account was continued until the death of Mr. *Hallett* on the 2nd of February, 1878, during which period Mr. *Hallett* drew out and paid in further sums, all of which were in respect of his private affairs. The banking account did not contain on either side any entry in respect of trust moneys other than the two already mentioned as having been paid in on the 14th of November. The sums drawn out amounted in the aggregate to £2662 0*s.* 2*d.*, whilst those paid in amounted to £1320 19*s.* 1*d.* only, and the balance to the credit of

the account on the clay of Mr. *Hallett's* death was £3029 15*s.* 1*d.* It is further to be noted, and it is to my mind a material circumstance, that the balance to the credit of the account never fell below the aggregate of the two sums of trust moneys.

An action having been commenced for the administration of Mr. *Hallett's* estate, summonses were taken out by the trustees of his marriage settlement and by a lady named *Cotterill*, who were respectively interested in the two trust funds, the former claiming payment in full of the sum of £770 10*s.* 5*d.* out of the balance which at the time of Mr. *Hallett's* death was standing to the credit of his banking account, and the latter claiming payment, out of the same balance, of £1708 16*s.*, part of the before-mentioned sum of £1804 0*s.* 7*d.* The claim of the trustees was based upon this, that the drawings of Mr. *Hallett* ought to be appropriated to such portions of the balances from time to time standing to his credit as had arisen from his own moneys, as distinguished from those of which he was a trustee; if this claim is well founded an application of the same principle would have entitled Mrs. *Cotterill* to the full sum of £1804 0*s.* 7*d.*, and not to the portion of it only which she claimed; her claim, however, was based upon an application of the well-known rule in *Clayton's Case* (1) that the drawings out from a banking account should be appropriated in strict order of date to the payments in, a rule which, it was contended, had been extended to cases similar to that under consideration

(1) 1 Mer. 572.

by the decisions of the Lords Justices in the case of *Pennell v. Deffell* (1), and in other cases which have followed it. If the rule was applicable to the present case, the aggregate amount of Mr. *Hallett's* drawings was sufficient, as will appear from the figures I have quoted, to exhaust not only the original balance of £1796 5*s.* 2*d.* which had arisen from Mr. *Hallett's* private moneys, but the whole of the sum of £770 10*s.* 5*d.* which consisted of trust moneys. Mr. Justice *Fry* considered himself bound by the decisions referred to and disallowed the claim of the trustees, but allowed that of Mrs. *Cotterill.* Thus of the two trust funds paid in on the same day the *cestui que trust* of the one would lose everything whilst the *cestui que trust* of the other one would lose to the extent only of a very small sum. Whilst, however, Mr. Justice *Fry* felt bound to follow these decisions, he distinctly intimated that, if he had been unfettered by authority, he would have been prepared to hold that, where a man has a balance to his credit at his banker's, consisting in part of funds which he may properly apply to his own purposes and in part of trust funds which he cannot lawfully so apply, his drawings for his own purposes ought to be attributed to his own funds and not to the trust funds.

From this decision of Mr. Justice *Fry* the trustees of Mr. *Hallett's* settlement have appealed.

Now, inasmuch as my own views as to what ought to be done in respect of the claim of the trustees are, except so far as I may feel that they ought to be controlled by authority, entirely in accordance with those expressed by Mr. Justice *Fry*, I propose to examine somewhat in detail the case of *Pennell v. Deffell* with the view of ascertaining, first, what principles were enunciated by the Lords Justices in the course of their judgments in that case; secondly, how those principles were applied by them to the circumstances of that case; and, thirdly, having regard to the principles enunciated and to the decision arrived at, how far the case of *Pennell v. Deffell* is an authority binding upon us in our dealing with the case now under consideration.

Mr. *Green*, whose estate was in course of administration in *Pennell v. Deffell*, died on the 22nd of October, 1849; for some time previously to his death he had two banking accounts, one

(1) 4 D. M. & G. 372.

with the *Bank of England* and the other with the *London Joint Stock Bank*; at the time of his death there was a balance to his credit of £1988 11*s.* 8*d.* at the former, and of £2174 0*s.* 10*d.* at the latter. I shall have occasion later to examine these accounts more closely, as they varied considerably in the character of their details, but for the present it is sufficient to say that each of these accounts embraced moneys paid in and drawn out by *Green*, partly on account of the trust estates which he represented, and partly on his own private account. Inquiries as to the balances having been directed by the decree, the Master found that the whole of one balance and the greater part of the other belonged to the trust estates, but, upon exceptions to the Master's report, the Master of the Rolls held that the trust moneys could not be followed into either of the banking accounts, and directed that the whole of both balances should be treated as part of *Green's* general estate, and the substantial question involved in the appeal to the Lords Justices was whether the Master of the Rolls was right in holding that the trust moneys could not be followed into the banking accounts. Upon this question Lord Justice *Turner* in the course of his judgment expressed himself as follows(1): "It is, I apprehend, an undoubted principle of this Court that as between *cestui que trust* and trustee, and all parties claiming under the trustee otherwise than by purchase for valuable consideration without notice, all property belonging to a trust, however much it may be changed or altered in its nature or character, and all the fruit of such property, whether in its original or in its altered state,

continues to be subject to or affected by the trust." And after illustrating this principle by a reference to the way in which the Court was in the habit of dealing with cases in which trust property had been invested in trade, the Lord Justice proceeded as follows: "But of course in those cases as in other cases the property which is the subject of the trust must in some manner be ascertained." He then refers to the judgment of the Master of the Rolls as having proceeded upon a supposed impossibility of ascertaining what portions of the balances belonged to the trusts, and what portions to *Green's* general estate, and answers, in the terms I am about to read, an inquiry suggested by himself,

(1) 4 D. M. & G. 388.

whether there were not rules and principles for ascertaining what belonged to the trusts in such a case as that under consideration. "Suppose," said the Lord Justice, "a trustee pays into a bank moneys belonging to his trust to an account not marked or distinguished as a trust account and pays in no other moneys, could it for one moment be denied that the moneys standing to the account of the debt due from the bankers, arising from the moneys so paid in, would belong to the trust, and not to the private estate of the trustee? Then, suppose the trustee subsequently pays in moneys of his own not belonging to the trust to the same account, would the character of the moneys which he had before paid in - of the debt which had before accrued - be altered? Again, suppose the trustee, instead of subsequently paying moneys into the bank, draws out part of the trust moneys which he has before paid in, would the remainder of those moneys and of the debt contracted in respect of them lose their trust character? Then can the circumstance of the account consisting of a continued series of moneys paid in and drawn out alter the principle? It may, indeed, increase the difficulty of ascertaining what belongs to the trust, but I can see no possible ground on which it can affect the principle." And Lord Justice *Knight Bruce*, in the course of his judgment, after some previous suggestions leading up to that to which I am about to refer, put the case of a trustee placing in a particular repository, such as a chest, certain moneys held by him in trust, and also certain other moneys of his own, and of his so mixing and blending the two that the particular notes or coins of which each consisted could not be identified, and of his taking a sum of money from the repository after such mixing and blending and applying it to his own purposes, and in expressing his opinion as to the conclusion to be arrived at in such a case the Lord Justice used the following language(1): "I apprehend that, in Equity at least if not at Law also, what he so took would be solely or primarily ascribed to those contents of the repository, which were in every sense his own. He would in the absence of any evidence that he intended a wrong be deemed to have intended and done what was right, and if the act could not in that way be wholly justified, it would be deemed to have been just

to the utmost amount possible,"

(1) 4 D. M. & G. 382.

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The Lord Justice added, and no one will, I think, dissent from what he said, that the proposition which he had just stated was founded on principle and supported by authority. But is there any reason why, if the proposition is founded on principle, it should be limited to moneys placed in and taken out of a particular repository? Why should it not be applicable also to a case of moneys paid into and drawn out from a banking account kept in the sole name of the trustee? It is true that in *Sleech's Case* (1), which immediately preceded *Clayton's Case* (2), Sir *W. Grant* held that, as between the banker and the customer, the payment of a sum of money into a banking account created a debt, and was not a mere deposit, but, as between the customer who is a trustee and his *cestui que trust*, is there any reason why an honest intention should not, as far as possible, be attributed to him in the one case as well as in the other?

Let me illustrate my meaning. On a certain day I receive £10 of trust money in sovereigns, and place them in a drawer in my desk, the next day I receive £10 of my own moneys, also in sovereigns, and place them in the same drawer; on the third day I require £5 for my own private purposes, and I take out five sovereigns from the mixed fund in the drawer - an application of the principle embodied in the proposition of Lord Justice *Knight Bruce* would appropriate the five sovereigns taken out on the third day to the £10 of my own moneys placed in the drawer on the second day, and not to the £10 of trust money placed there on the first day. Again, I receive a cheque for £100 on a trust account, it will not be required for a few days, and it is too large a sum to be kept in my desk, I pay it into a bank, and on the following day receive £100 on my own private account, and not wanting it for a few days I pay it into the same account; I require £50 or £100 for my own purposes before the time arrives fur requiring any money for trust purposes, and I accordingly draw against the mixed fund for the £50 or £100. Can any reason be assigned why in this latter case, as well as in the former, I should not, as between myself and my *cestui que trust*, have the honest intention attributed to me of drawing against my own private funds, and not against the trust fund, though it was the first paid in?

(1) 1 Mer. 539.

(2) 1 Mer. 572.

(1879) 13 Ch.D. 696 Page 736

That Lord Justice *Knight Bruce* saw no distinction in principle between the two cases is, I think, clear from the next proposition, which he enunciated in the following terms: "When a trustee pays trust money into a bank to his credit, the account being a simple account with himself, not marked or distinguished in any other manner, the debt thus constituted from the bank to him is one which, as long as it remains due, belongs specifically to the trust as much and as effectually as the money so paid would have done had it specifically been placed by the trustee in a particular repository and so remained; that is to say, if the specific debt shall be claimed on behalf of the *cestui que trust*, it must be deemed specifically theirs as between the trustee, and his executors and the general creditors after his death, on the one hand, and the trust on the other;" and, after some observations not material to be now noted, the Lord Justice continued as follows: "This state of things would not, I apprehend, be varied by the circumstance of the bank holding also for the trustee, or owing also to him money in every sense his own."

The language of this latter sentence is, perhaps, somewhat vague. The previous sentence had reference to a trustee paying in trust moneys to a banking account; did the Lord Justice, when speaking of the bank holding also for the trustee money in every sense his own, refer to, or intend to include, private moneys of the trustee paid in by him to the same account? This appears to me to be the reasonable construction of the language used, and for the following reason: in the various steps by which the Lord Justice had arrived at his previous proposition he had taken, first, the case of trust money placed in a particular repository, then the addition to such trust moneys of the trustee's own moneys; thirdly, the abstraction from the mixed fund of moneys applied to his own purposes; and in advancing his second proposition, he first takes the case of trust moneys paid into a banking account, and insists upon their being regarded as if placed in a particular repository; and then follows the passage the effect of which I am now considering. The inference appears to me to be irresistible that the Lord Justice intended to adopt exactly the same steps in connection with a banking account as he had previously suggested with reference to moneys placed in a particular repository. If

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the proposition as a whole is so read, it has the effect of extending to blended funds in a banking account the like rule or principle of attributing, where possible and as far as possible, an honest intention to a trustee drawing out money for his private purposes, as the Lord Justice had previously

enunciated with reference to blended funds in a particular repository.

The principles thus enunciated by the Lords Justices (for the Lord Justice *Turner* expressed his full concurrence in the views expressed by Lord Justice *Knight Bruce*), taken and considered by themselves, amount to this: first, that trust moneys may be followed into a banking account; and, secondly, that in dealing with an account composed in part of trust and in part of private funds, an honest intention should, if and as far as possible, be attributed to a trustee; apart from the application of a third principle, also enunciated by the Lords Justices, and which I will consider presently, they would have fully justified the order which Mr. Justice *Fry* expressed himself ready to make, had he not felt himself fettered by authority.

The third principle was enunciated by the Lords Justices in the following terms. Lord Justice *Knight Bruce* said: "It may be, however, and, as I think is true, that cheques drawn by the trustee in a general manner upon the bank would for every purpose be ascribed to and affect the account in the mode explained and laid down by Sir *W. Grant* in *Clayton's Case* (1). The principles there stated would, I conceive, be applicable, notwithstanding the different nature and character of the sums forming together the balance due from the bank to the trustee, whatever the purposes and objects of the cheques." And Lord Justice *Turner* enunciated the same principle in the following terms(2): "We must see, however, whether the law does not furnish the means of meeting even the difficulty arising from such a continued series of moneys paid in and drawn out. I think that it does. I take it to be now well settled that moneys drawn out on a banking account are to be applied to the earlier items on the opposite side of the account. By every payment which he makes, the banker discharges so much of the debt which he first contracted. If that debt arose from trust moneys paid in by the customer, so much of

(1) 1 Mer. 572.

(2) 4 D. M. & G. 391.

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those trust moneys is paid off, and unless otherwise invested an account of the trust, falls into the customer's general estate and is lost to the trust, because it cannot be distinguished from the general

estate of which it has become part. If, on the other hand, the earliest debt due from the bank arose from the customer's own moneys paid in by him, that debt is *pro tanto* discharged, and the trust moneys subsequently paid in remain unaffected. The same principle runs through the whole account. Each sum drawn out goes to discharge the earliest debt due from the banker which is remaining unpaid; and thus, when it is ascertained what moneys have been paid in belonging to the trust, it becomes clear to what portion of the balance which remains the trust estate is entitled."

In these clear and forcible terms the Lords Justices enunciated the proposition that, as a general principle, the rule in *Clayton's Case* (1) must be applied to the banking accounts of trustees for the purpose of determining the proportions in which the *cestuis que trust* and general creditors, or the several classes of their *cestuis que trust*, are entitled to the debt due from the bankers in closing the account. To the general principle so enunciated I readily accede. But was it more than the enunciation of a general principle; that is to say, a principle to be applied in the absence of special circumstances, but liable to be modified in its application by reason of the necessity or propriety of applying some other general principle of equal or paramount importance?

In *Clayton's Case* Sir *W. Grant* held that in dealing with an account between a banker and his customer, and in the absence of any evidence of contrary intention, the law would imply an appropriation in the order of their respective dates of the items drawn out to the items of debt constituted by the several payments of the customer; and he further held, that the respective liabilities of successive partnerships in the banking firm must be regulated by the results of taking the accounts in the manner he had previously indicated.

Now *Clayton's Case* was decided upon the principle that in the absence of any expressed intention to the contrary, or of special circumstances from which such an intention could be implied, the appropriation of drawings out to the payments in as adopted in

(1) 1 Mer. 572.

(1879) 13 Ch.D. 696 Page 739

that case represented what must be presumed to have been the intention of the parties concerned; and so viewed the decision is quite consistent with the like presumption being rebutted or modified in another case in which the circumstances were such as to negative any intention to make such an appropriation of the drawings out to the payments in. That such presumption could be so rebutted

was held in the cases of *Henniker v. Wigg* (1), decided by the Court of Queen's Bench before the decision in *Pennell v. Deffell* (2), and more recently in the case of the *City Discount Co. v. McLean* (3), in the Exchequer Chamber, in which latter case, however, no reference appears to have been made to *Pennell v. Deffell*. In *Clayton's Case* (4) there were no circumstances from which it could be inferred that, either as between the bankers and their customers, or as between the successive partnerships in the banking firm, the parties had any intention other than that presumably to be attributed to them of appropriating, in order of date, the drawings out to the payments in; but the adjustment of the liabilities of the several partnerships which was effected in that case by the application of the general principle enunciated by Sir *W. Grant*, might have been materially modified had there been any special contracts between the parties or any equities affecting them.

And so, also, in my opinion, the general principle enunciated by the Lords Justices in *Pennell v. Deffell* was based, or ought to be regarded as having been based, upon the like presumption as that acted upon by Sir *W. Grant* in *Clayton's Case*; and that such presumption was liable to be rebutted, or its effects modified, by any equities affecting Mr. *Greenwood*, and those claiming through him, unless there was sufficient reason to the contrary. The questions then arise, did any such equities exist in *Pennell v. Deffell*? and if so, was there any sufficient reason for not giving effect to them?

That an equity might have existed sufficient to very materially modify the application of the general rule that the drawings out should be appropriated in order of date to the payments in, I cannot doubt; that equity was the obligation so forcibly insisted

(1) 4 Q. B. 492.

(2) 4 D. M. & G. 372.

(3) Law Rep. 9 C. P. 692, 701.

(4) 1 Mer. 572.

upon by Lord Justice *Knight Bruce*, of attributing to the trustee, when the circumstances would admit of it, an intention to act honestly. It is, however, equally clear that the Lords Justices did not modify the application of the general rule by reason of the existence of this equity: and upon this circumstance the Respondents have laid much stress, and in support of their contention they have relied upon the following passage in the judgment of Vice-Chancellor *Wood* in the case of *Merriman v. Ward* (1), in which, referring to *Pennell v. Deffell* (2), that learned Judge said: "The Lords Justices had to consider whether the doctrine of appropriation could be overruled by another principle, namely, that the assignee must be presumed, so far ag possible, to have drawn against his own fund, because the opposite presumption would be a presumption of fraud. Nevertheless the Court held that the ordinary rule must apply of appropriating the earlier payments to the earlier debts."

If the Lords Justices had the question alluded to by the Vice-Chancellor present to their minds when they delivered their judgments in *Pennell v. Deffell*, and deliberately solved it in the manner mentioned by him, it is much to be regretted that they did not make some specific reference to it; but I can find no reason, assigned in the judgment of either Lord Justice, why the rule, which had been so elaborately laid down, of attributing honest motives to a trustee was treated as having no application when the order to be made upon the facts of the case came under consideration; the absence of any such assigned reason leads me to the conclusion that either the suggested question was neither solved nor discussed as one in controversy, or that some special circumstances existed which are not noticed in the report.

And the comparative unimportance to the parties concerned of having this question decided or discussed may perhaps explain the omission. I have already referred to the fact that *Green* had two banking accounts, upon each of which there was a considerable balance in his favour when it was closed. As regards the account with the *London Joint Stock Bank*, the two first items to his credit consisted entirely of his own moneys and amounted together to upwards of £800, whilst the aggregate of all the moneys drawn

(1) 1 J. & H. 371.

(2) 4 D. M. & G. 372.

out by him, whether on trust account or on private account, fell short of £800, so that it was wholly immaterial as regarded the result whether the account was taken upon the principle of appropriating the sums drawn out to the earlier items paid in, or to that portion of the balance which was composed of his own private moneys; whichever principle was adopted the result would have been the same, viz., that the *cestui que trust* would recover the full amount of all the trust moneys paid in.

But as regards the account with the *Bank of England* the facts were somewhat different; that account had commenced with a balance entirely composed of trust moneys, from which, on the 4th of October, 1849, *Green* had drawn out for his private purposes several sums amounting together to £107. Had the account been then closed there would have been no blending of trust moneys with private funds; the sums drawn out would have been simply a misapplication of trust moneys to the extent of £107. On the following day, however, *Green* paid in to the credit of the account a sum of £72 16*s*. 3*d.* of his private moneys, and another sum of £442 12*s.* of trust moneys, and on the same day drew out £18 18*s.* for his private purposes and £49 17*s.* 10*d.* for trust purposes. The sum of £72 16*s*. 3*d.* was the only sum paid in by *Green* to the credit of this account in respect of his private moneys, but subsequently to the 5th of October he drew out and applied for his private purposes various sums which, being added to the £18 18*s*., exceeded by a small sum the amount of £72 16*s*. 3*d.* paid in by him on the 5th.

By the decision of the Lords Justices, the drawings of *Green*, as well before as on and after the 5th of October, were appropriated to the part extinguishment of the original balance consisting entirely of trust moneys, and the general creditors were allowed out of the ultimate balance the full amount of the £72 16*s*. 3*d.* paid in by *Green* on the 5th of October. With this result, therefore, the rule in *Clayton's Case* (1) was acted upon in dealing with the balance at the *Bank of England.* Had it been argued on the part of the Appellants that the payment of the £72 16*s*. 3*d.* by *Green* on the 5th of October ought to be treated as a repayment *pro tanto* of the £107 improperly drawn out by him

(1) 1 Mer. 572.

on the 4th, before any blended account existed, the contention could hardly have been deemed unreasonable; no such contention however, appears to have been raised.

But the difference between the result of the system of appropriation adopted by the Lords Justices and what would have been the result if, on both accounts, the moneys drawn out by *Green* had been set off against the moneys paid in from his private resources, is very trifling. Had the latter system been adopted, the Appellants would have been entitled to £4077 5*s.* 4*d.*, whilst under the order of the Lords Justices they took £4011 13*s.* 5*d.*, a difference of £65 only. They had succeeded in reversing the decision of the Master of the Rolls who had deprived them of everything, and, as before observed, the substantial question argued was not, whether the Respondents were entitled to the £72 16*s.* 3*d.*, but whether the Appellants were entitled to anything. It is not an improbable view of the case that at the close of a judgment which had given them within a fraction all that they had claimed, the Appellants should have abstained from questioning a portion of that judgment with the view of obtaining an allowance of the additional fraction. And this view of the case appears to be borne out by the fact that, although judgment was reserved, it was eventually given without hearing a reply from the Appellants, which would hardly have been the case if the Appellants had objected to the allowance of the £72 16*s.* 3*d.* to the Respondent; and it may fairly be inferred, as well from the opening words of Lord Justice *Knight Bruce*, who offered to the counsel for the Appellants a right of reply after judgment, if they thought fit to claim it, as from the concluding words of Lord Justice *Turner*, that a claim on behalf of the Appellants for something more than was given them was at least arguable. Lord Justice *Turner's* observation was, that he had no doubt Lord *Eldon*, would have gone at least as far as the Lords Justices were then going, and that his only doubt was, whether he would not have gone further. Upon what was the doubt based? Upon what could it have been based? The Lords Justices could only have gone further than they did go by depriving the Respondents of the £72 16*s.* 3*d.*, and giving it to the Appellants.

But, dealing with the decision of the Lords Justices in *Pennell*

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v. Deffell (1), as I find it reported, I cannot regard it as satisfactory, if it is to be considered as establishing as a general proposition that in all such cases as that then under their consideration the presumption of an honest intention on the part of the trustee is to be altogether disregarded, however favourable to such a presumption the circumstances of any particular case may be, and that the rule of appropriating in strict order of date the drawings out to the payments in is alone to be applied. On the contrary, I entertain a very decided opinion that in cases like *Pennell v. Deffell*, or in such as that which is the subject of the present appeal, full effect should be given to the principle of attributing the honest intention whenever the circumstances of the case admit of such a presumption. It may, of course, happen that, through the acts of a trustee, whether wilfully dishonest or not, the ultimate balance may not be sufficient to meet the full amounts of all the trust moneys which may have been paid into a blended banking account, and the question then raised may be as to the various claims in

respect of distinct trusts; in such a case the strict application of the general rule of appropriating in order of date the drawings out to the payments in may, and probably would, be correct. But in a case of another class, in which, as in that under consideration, the trustee has paid in trust moneys to the credit of his private account, and in his subsequent dealings with that account for his private purposes has never reduced his balance below the amount of the trust moneys so paid in, it is, to my mind, difficult to attribute to the trustee any other intention than that of appropriating his drawings to his own private moneys, so as to leave the trust moneys intact. If it is ever proper to follow trust moneys into a banking account in the interests of the *cestuis que trust*, I am unable to suggest a case more proper than that which we are now considering for the application of the principle that an honest intention should be attributed to the trustee. Now, if it can properly be considered that the decision in *Pennell v. Deffell* proceeded upon the special circumstances of that case, it is, of course, not an authority by which this Court is bound in dealing with the present appeal; but, however strong may be the impression upon my own mind, and it is very strong, that all the

(1) 4 D. M. & G. 372.

circumstances of that case necessary for rightly appreciating it are not to be found in the report, I cannot ignore the fact that for nearly thirty years it has been recognised as an authority in no way depending on special circumstances, but as establishing a general principle applicable to all cases of a similar character. In the case of *Brown v. Adams* (1), to which our attention has been directed in argument, Lord Justice *Giffard* not only held himself bound by the authority of *Pennell v. Deffell* (2), but stated that he should have arrived at the same conclusion in the case before him even if not bound by that authority. With reference, however, to the case of *Brown v. Adams*, it is to be observed that Lord Justice (then Vice-Chancellor) *James*, from whose decision the appeal was brought, had arrived at a different conclusion. The question, then, remains whether *Pennell v. Deffell* is an authority so binding upon this Court that, however decided may be the collective or individual opinions of its members as to what, in the absence of authority, should be done in the matter of this appeal, we are bound to disregard them, and to shape our decision in accordance with what was decided in that case. My answer to that question must be in the negative. I fully recognise and appreciate the evils which in many cases would arise if the Judges of the Court of Appeal, or, indeed, if any other Court or Judge, were to act upon their individual views, regardless of what is generally understood by the expression "authority." Repeated decisions have established rules for determining the construction of particular words when used in wills, and other wills have been prepared and executed upon the faith of such words receiving the like construction. Titles have been acquired and lands dealt with upon the footing of the law being as enunciated in the judgments

pronounced in other cases. And so, again, in matters of commercial business, contracts have been entered into upon the faith of certain rules, originating in the decisions of the Courts, being recognised as conclusive. Now, in such cases as these, and in others which will readily suggest themselves, the greatest injustice might be occasioned by a Court or a Judge treating such decisions as having been erroneously arrived at, and thereby creating doubt and uncertainty as to a rule of law which had previously been

(1) Law Rep. 4 Ch. 764.

(2) 4 D. M. & G. 372.

treated as well and clearly defined. But no such injustice could arise in consequence of our dissenting from the decision in *Pennell v. Deffell* (1), and giving effect to such dissent. It can hardly be suggested that since that decision any trustee has kept and dealt with a blended banking account upon the faith that, as between his general creditors and his *cestuis que trust*, the rule adopted in that case would also be adopted after his death in dealing with his ultimate balance. If a trustee had acted upon any such view, he could hardly be considered as having had an honest intention. If, however, the actual decision in *Pennell v. Deffell* had been a logical consequence of an application of the principles enunciated by the Lords Justices, I should certainly have felt myself bound to follow it; but, having to decide between the general principles enunciated in that well-known case in which, as understood by me, I entirely concur, and the decision arrived at in the same case, and apparently upon an intended application of the same principles, but which would give to those principles a construction and an effect in which I cannot concur, I feel myself bound to adopt and give effect to the general principles, and to treat myself as unfettered by the actual decision. For these reasons I agree with the Master of the Rolls in thinking that the appeal should be allowed.

THESIGER, L.J. :-

I feel myself bound by authority to affirm the judgment of Mr. Justice *Fry*. Upon principle there is great strength in the argument for the Appellants. If specific coins, the proceeds of trust property,

are deposited by a trustee in a box, either in his own custody or in that of another person, and in that box are mixed confusedly with coins, in every sense the property of the trustee, and being so mixed are subjected to dealings analogous to the drawings out and payings in of moneys standing in a banker's account, the trust is impressed upon the coins remaining in the box to the full amount of the proceeds of the trust property, if it be that at no time the mixed fund has been reduced below that amount, or if the mixed fund has at any time been reduced below that amount, then to any lesser amount below which it can be shewn that the mixed fund has never been reduced. So much is

(1) 4 D. M. & G. 372.

admitted by Lord Justice *Knight Bruce* in *Pennell v. Deffell* (1). But in that case, and in other cases, it has been held that the proceeds of that trust property may be traced, followed, and claimed by the trust creditor when, instead of their being placed in a box or other special repository, they are paid to a banker to be placed by him to the credit of the trustee's private account, and are so placed subject to the qualification at least that upon an appropriation of payment in accordance with the rule laid down in *Clayton's Case*, (2) it appears that the money claimed has not been drawn out. It has been argued that the qualification cannot be supported, and that when once it is admitted that money may be followed into a banker's account equally with money placed in a special repository, the money so followed must be subject to the same conditions and be recoverable under the same circumstances in the one case as in the other. True it is that in the case of money paid into the banker's account it is converted into a debt, while in the case of money placed in a special repository it remains in specie; but it may be said with reason that this distinction would rather afford a ground for not following the money into the banker's account at all, than a ground, when it is held that it may be followed, for not carrying out to their logical consequences considerations drawn from the analogy of the money placed in the special repository; and it is no doubt difficult to see why the rule as to appropriation of payments, which is a rule which embodies a presumption of fact rather than of law, and is founded upon the notion that in the absence of any expression of intention an appropriation of drawings out and payings in of moneys upon a banker's account in order of date would in most cases meet the intentions of the parties, should not bend before the fact that in the particular case such an appropriation would involve a breach of trust, if not a distinct fraud. That the rule is what I have stated it to be is shewn by the cases of *Henniker v. Wigg* (3) and the *City Discount Company v. McLean* (4), and those cases are good illustrations of the character of circumstances which would be sufficient to prevent the application of the rule. A bond in one case, a guarantee in the other, given by third parties, and covering a portion of the

(1) 4 D. M. & G. 381.

(2) 1 Mer. 572.

(3) 4 Q. B. 492.

(4) Law Rep. 9 C. P. 692.

customer's account with his bankers, was held to rebut the presumption that the balance covered by the security had been paid.

In each of these cases the presumption, if it had been acted upon, would have put an end to a civil remedy which from the facts of the case it was manifest was intended by all parties to be kept active. In the present case, and in cases of a similar kind, if the presumption is acted upon it would not only result in trust property, the proceeds of which are traced to the banking account, being lost to its proper owners, but would entail the further consequence of the customer being presumed to have committed a fraud, and this by an arbitrary rule not founded upon any equitable considerations (for general creditors have no equity as against the equity of a *cestui que trust* to trace and follow into a banking account the moneys arising from the sale of the trust property: *Frith v. Cartland* (1)), but established for the purpose of dealing with general accounts in the absence of special indications by the parties of their intentions.

The presumption of a man's innocence of crime may reasonably be set off against the presumption that he intended such an appropriation of payments upon his banking account as could only exist if he intended to commit a crime; and to the argument adduced by Mr. *Hallett's* representatives in the present case that the facts proved indicate that he did in fact intend to misappropriate, and had misappropriated, the trust property, the answer might be given, as it might have been given to Mr.

Hallett himself if he had been alive to use the argument, *"Allegans suam turpitu-dinem non est audiendus."* Giving, however, full effect to this reasoning, which, be it observed, is reasoning that is not difficult for even an uncultivated mind to follow, it remains to be seen how eminent Judges have dealt with the matter.

Clayton's Case (2) is capable of being, and has been, distinguished from the present. It with other similar cases shews, according to Mr. Justice *Blackburn*, in *City Discount Company v. McLean* (3), "that when a partner dies, and there is a change of the partnership, and the transactions with the new and old firms are all mixed up together in one account, the law treats the whole

(1) 2 H. & M. 417.

(2) 1 Mer. 608.

(3) Law Rep. 9 C. P. 701.

as one entire account, and it applies the items of credit to those of debit according to date in favour of the estate of the deceased partner." The decision of Sir *W. Grant* so explained is quite consistent with the general rule clearly laid down in the Common Law cases, that accounts rendered are only evidence of the appropriation of payments to the earlier items, which may be rebutted by evidence to the contrary. The two cases already cited of *Henniker v. Wigg* (1) and *City Discount Company v. McLean* (2) affirmed, as already pointed out, that general rule, and although they contained special features which might distinguish them to some extent from the present case, their *ratio decidendi* was wide enough to apply to the case of a person following his trust property into a banking account, and claiming to have that account adjusted so as to preserve his rights. Still it must be borne in mind that in these Common Law cases the inference arising upon the facts was that banker, customer, and third party all actually intended that the payments in and out of the account should not be taken in order of date, while here, bankers and third party could have had no intention in the matter, for they were ignorant of the fact that the trust funds had got into the account, and the intention of the customer is only derived from a presumption of law contrary to the probable facts of

the case. This being so, we have in the case of *Pennell v. Deffell* (3), and in a Court of co-ordinate jurisdiction with this Court, or rather in a Court, to the functions of which, among other functions, this Court has succeeded, a decision by which, not only the principles applicable to a case like the present, were considered and laid down, but in which the very point raised upon this appeal was discussed and decided. The steps which, as pointed out at the commencement of my judgment, seem to lead to the conclusion, as a matter of logical argument, in favour of the Appellant's contention, were the steps taken by Lord Justice *Knight Bruce* in *Pennell v. Deffell*, and which led him to an exactly opposite conclusion, arrived at also by his colleague, Lord Justice *Turner*. Their judgment was given in 1853. In 1860, Vice-Chancellor *Wood*, in the case of *Merriman v. Ward* (4), following, as he was no doubt bound to do, that judgment, epitomised

(1) 4 Q. B. 492.

(2) Law Rep. 9 C. P. 692.

(3) 4 D. M. & G. 372.

(4) 1 J. & H. 377.

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it in these terms: "The Lords Justices had to consider whether the doctrine of appropriation could be over-ruled by another principle, namely, that the assignee must be presumed, so far as possible, to have drawn against his own fund, because the opposite presumption would be a presumption of fraud. Nevertheless, the Court held that the ordinary rule must apply of appropriating the earlier payments to the earlier debts." The effect of *Pennell v. Deffell* (1) could not be put in terms more clear, or more distinctly negativing the argument as regards the presumption of fraud which I have used. In *Frith v. Cartland* (2) again, the same learned Vice-Chancellor, while distinguishing the case before him from that of *Pennell v. Deffell*, said of the latter that in it part of the trust fund had been paid into a bank, but it was not ear-marked, and was wiped out by subsequent drawings, and the whole ultimate balance could not be fixed with the trust any more than a second £1000 of stock

which a trustee might happen to acquire after selling £1000 of trust stock and spending the proceeds. In the year 1869 the point arose before Lord Justice *Giffard* in *Brown v. Adams* (3) in the same simple form in which it has been discussed before us, for the only question the Lord Justice had to decide was whether in a banker's account the appropriation of payments according to the rule in *Clayton's Case* (4) was to take place, so as to wipe off an item of £5000, which was admittedly trust moneys, and the case came before the Lord Justice under circumstances favourable to the reconsideration of the decision upon the point in *Pennell v. Deffell*, for the present Lord Justice, then Vice-Chancellor *James*, had granted an interlocutory injunction in favour of the trust creditor. But Lord Justice *Giffard* dissolved the injunction, not merely saying that he considered himself bound by the authority of *Pennell v. Deffell*, but adding that, even without that authority, he should have had no doubt in the case before him. Again, in *Ex parte Cooke* (5), decided in 1876, Lord Justice *Bramwell*, one of the Judges who took part in the decision in 1874 of the case of the *City Discount Company v. McLean* (6), is reported to have said in reference

(1) 4 D. M. & G. 372.

(2) 2 H. & M. 417.

(3) Law Rep. 4 Ch. 764.

(4) 1 Mer. 572.

(5) 4 Ch. D. 123.

(6) Law Rep. 9 C. P. 692.

to the point under consideration(1), "If the whole of the money had remained in the hands of the bankers without being drawn out, I think it clear that the *cestui que trust* could have claimed it as trust money traced into their hands, and if on properly attributing the payments any part of it is found to remain there the same rule must apply to what so remains." In that case the matter was referred to the Registrar, and we are informed by Mr. *De Gex*, who was engaged as counsel in the case, that upon the Registrar appropriating the payments in accordance with those observations, and upon an appeal from the Registrar to this Court, the case of *Pennell v. Deffell* (2) was treated as binding authority, and the appeal was dismissed.

I have purposely refrained from citing, as authority in the same direction, the case of *Lord Chedworth v. Edwards* (3), before Lord *Eldon*, as Chancellor, in 1802, because there may possibly be a doubt as to what he meant when he spoke of it being too much to infer that money at the bankers was the same money unconverted which had been paid in two years before, and the point does not appear to have been particularly argued before him. Putting aside, however, that case, the matter, as regards authority, stands thus: For a period of twenty-one years the judgment in *Pennell v. Deffell* stood unchallenged, and was followed as laying down a correct rule, and even when at the end of that period the case of the *City Discount Company v. McLean* (4) was decided, it was decided without reference to *Pennell v. Deffell.* As regards this last observation, it may be pointed out that the Lords Justices decided *Pennell v. Deffell* without reference to the previous case of *Henniker v. Wigg* (5); and it may be said that they had proceeded upon a misapprehension of the principle of Common Law applicable to the appropriation of payments in a banking or any other account. This may possibly be so, and if it was so, I am inclined to think that the misapprehension was shared by Sir *William Grant*, in laying down the rule in *Clayton's Case* (6), and although his decision may be distinguished, as it has been distinguished in the Common Law cases already cited, I cannot but think that the terms in

(1) 4 Ch. D. 127.

(2) 4 D. M. & G. 372.

(3) 8 Ves. 46.

(4) Law Rep. 9 C. P. 692.

(5) 4 Q. B. 492.

(6) 1 Mer. 572.

which he laid down the rule were intended by him to go beyond the limits of the particular case before him, and were wide enough, as they were assumed by the Lords Justices *Knight Bruce* and *Turner* to be, to cover the later case of *Pennell v. Deffell* (1). The character of the banking account where, to use the words of Sir *William Grant* himself, "all the sums paid in form one blended fund, the parts of which have no longer any distinct existence," was the keynote of his decision, and would have been scarcely necessary to be dwelt upon so prominently if any equity of the retired or deceased partner had been sufficient in itself to call for an appropriation of payments at least not contrary to any rule of law.

In this state of the authorities, I cannot feel myself justified in acceding to the Appellants' contention, and thereby taking upon myself to overrule judgments by which I think that in this Court we ought to consider ourselves bound. I fully realize that in overruling those judgments no injustice or inconvenience would be worked such as would arise in cases where, upon the faith and footing of a particular rule of law having been correctly laid down, business affairs have been for some time conducted, the practice of conveyancers has been regulated, or titles to property of any kind have been acquired. But that consideration appears to me to be one proper to influence the mind of a superior tribunal asked to overrule the judgment of inferior tribunals, although of long standing and often followed, rather than to afford a ground for this or any other Court disregarding such judgments when given by and followed in tribunals of co-ordinate jurisdiction. In other words, it constitutes a reason for holding that a decision in a particular Court has not so passed into and become part of the common and recognised law of the land as to prevent any Court overruling it, rather than for holding that it is not a binding decision upon all Courts of co-ordinate jurisdiction. It is said, further, that the point for our decision formed so insignificant a part of the judgment of the Lords Justices in *Pennell v. Deffell*, and may, perhaps, have been, or even probably was, so little dwelt upon in the argument before them, especially as no reply was heard by them, that their

decision upon it is entitled to less weight than might otherwise

(1) 4 D. M. & G. 372.

have been given to it. The fact is manifest that the sum which was affected by the particular decision was a mere nothing compared with the amount of which the then Master of the Rolls' judgment had deprived the Appellants, upon the ground that the trust moneys could not be traced and followed into the banker's account at all, and which amount the Lords Justices held was recoverable by the trust creditor. Granting, however, this fact, it is still equally manifest that the Lords Justices did not overlook the minor point, or, indeed, treat it as a minor point. Their judgments contain on the face of them signs from which one cannot but collect that the point was carefully considered by them. It is lastly said that the principles they themselves laid down in their judgment so clearly demonstrate the erroneousness of their conclusion upon the particular point in question, that it is just one of those cases in which no Court ought to be bound by such a conclusion. But here, again, however desirable it may be, as suggested in argument, that a Judge should have the courage of his convictions, it is equally desirable that he should have respect for those of other Judges, and I should attribute to myself another quality than that of courage if I were to hold that a conclusion which appeared a rational one to no less eminent Judges than the late Lords Justices *Knight Bruce* and *Turner*, the present Lord *Hatherley*, and the late Lord Justice *Giffard*, and which did not appear open to review to the learned Judges before whom upon the second occasion the case of *Ex parte Cooke* (1) came to be discussed, was necessarily illogical and absurd. Equity has gone very far in aid of trust creditors when it holds that they may follow and obtain, in priority to general creditors, moneys paid to a banker, and therefore no longer existing in specie, as moneys numbered and ear-marked, but converted into a debt; and it may be that the distinguished Judges I have referred to may have thought that Equity had gone far enough, and that, in the absence of express appropriation, the general rule of appropriation of payments in and out of a banker's account should apply to that debt when forming part of a larger debt made up as to the rest of moneys, not trust moneys, paid into the bank. However this may be, and notwithstanding the hesitation which I naturally feel in differing upon

(1) 4 Ch. D. 123.

(1879) 13 Ch.D. 696 Page 753

the question of the binding effect of the authorities from the other members of the Court, I must express my opinion that the law laid down in *Pennell v. Deffell* (1) is binding upon this Court, and that the appeal ought, therefore, to be dismissed.

Appeal allowed.

Solicitor for Plaintiff: *H. A. Dowse.*

Solicitors for Mrs. *Cotterill: Fladgate & Co.*

Solicitors for *Hallett's* Trustees: *Fairfoot & Webb.*

Solicitors for other parties: *Humphreys & Son; F. Howse.*

(1) 4 D. M. & G. 372.