1918
*Dec. 18
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GEORGE T. CLARKSON AND ANOTHER (PLAINTIFFS)..... } APPELLANTS;

AND

THE DOMINION BANK (DEFENDANT)..... } RESPONDENT.

ON APPEAL FROM THE APPELLATE DIVISION OF THE SUPREME COURT OF ONTARIO.

Banks and banking—Loan to manufacturer—Security—Written promise—Advance for prior debt—"Bank Act," ss. 88, 90—Mortgage as security—Insolvency—Knowledge of bank—Mortgage on land outside Province.

By section 88 of the "Bank Act" a bank may lend money to a manufacturer on security of his goods or raw material and by section 90 it shall not acquire any such security unless the liability is contracted "(*a*) at the time of the acquisition thereof by the bank; or (*b*) upon the written promise or agreement that such * * * security would be given to the bank."

Held, Anglin J. dissenting, that subsection (*b*) does not contemplate a general promise or agreement to give security for future advances but it must have reference to a specific loan negotiated at the time on the security of specific goods.

A manufacturing company, by application in writing, obtained a line of credit from a bank and agreed to give security under the "Bank Act" on its stock and material for each advance made thereunder. Advances were made and security given as agreed. By similar application the credit was renewed from time to time, and after each renewal the bank took security not only for the present advance but for the total indebtedness of the company to that date.

Held, Anglin J. dissenting, that this security taken for the whole debt was only valid for the amount of the loan made at the time it was acquired; but

Held, Idington and Brodeur JJ. dissenting, that the security acquired for each individual advance was never released and did not merge in the general security so taken; the bank, therefore, was entitled to the benefit of all the securities so acquired.

In May, 1912, the company agreed to give to the bank, as further security, a mortgage on its factory site in St. Thomas, Ont., and also a mortgage on land in Montreal. The former was not executed until Nov., 1913, nor the latter until Jan., 1914. In March, 1914, the bank filed a petition for winding-up the company.

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*PRESENT:—Sir Louis Davies C.J. and Idington, Anglin, Brodeur and Mignault JJ.

Held, that in Ontario it is the date of the promise to give the mortgage that governs and as the mortgagor was solvent at that date the mortgage on land in Ontario was valid; but.

Held, that in Quebec the date when the mortgage was executed can alone be considered, and as the mortgagor was insolvent to the knowledge of the bank when the Quebec mortgage was given it must be set aside.

Per Anglin J.—Insolvency to the knowledge of the bank at that date was not established; and

Qu.—Can an Ontario Court set aside a mortgage on land in Quebec?

After the petition for winding-up the company had been filed the bank advanced $17,600 on security of the stock in trade and material on hand.

Held, Idington and Brodeur JJ. dissenting, that if this advance was made, under the terms of section 20 "Winding-up Act," with the sanction of the liquidator and for the beneficial winding-up of the estate the bank was entitled to the benefit of the security.

Judgment of the Appellate Division (40 Ont. L.R. 245) and of the trial Judge (37 Ont. L.R. 591), reversed in part.

APPEAL from a decision of the Appellate Division of the Supreme Court of Ontario (1), affirming the judgment at the trial (2), in favour of the defendant bank.

The material facts and the questions raised for decision on this appeal are stated in the above headnote.

Hellmuth K.C. and *J. B. Davidson* for the appellant. Under section 90 of the "Bank Act" a bank can take security for a present loan only. A general security to apply to future advances is invalid. See *Bank of Hamilton* v. *Halstead* (3), at p. 241; *Bank of Hamilton* v. *Shepherd* (4).

For a long time before the winding-up order was made the bank knew that the company was unable to pay its debts and knew that it was insolvent when the two mortgages were given as security. See *Molsons Bank* v. *Halter* (5).

(1) 40 Ont. L.R. 245; 38 D.L.R. 232.
(2) 37 Ont. L.R. 591.
(3) 28 Can. S.C.R. 235.
(4) 21 Ont. App. R. 156.
(5) 18 Can. S.C.R. 88.

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D. L. McCarthy K.C. and *Shapley* for the respondent. The written promise provided for in subsection (*b*) of section 90 may refer to future as well as present advances. *Imperial Paper Mills Co.* v. *Quebec Bank* (1).

The promise to give the mortgages was made when the bank had no reason to believe, and evidently did not believe, that the company was insolvent. As to the Quebec mortgage a court in Ontario could not set it aside.

THE CHIEF JUSTICE.—The principal and main question raised and argued on this appeal was as to the proper construction of sections 88 and 90 of the Dominion Act respecting banks and banking.

So far as is material for this case, section 88 provides as follows:—

3. The bank may lend money to any person engaged in business as a wholesale manufacturer of any goods, wares and merchandise manufactured by him, or procured for such manufacture.

* * * * *

6. The security may be taken in the form set forth in Schedule C to this Act, or to the like effect.

Section 90 enacts:—

90. The bank shall not acquire or hold any warehouse receipt or bill of lading, or any such security as aforesaid, to secure the payment of any bill, note, debt or liability, unless such bill, note, debt or liability is negotiated or contracted:

(*a*) At the time of the acquisition thereof by the bank, or

(*b*) Upon the written promise or agreement that such warehouse receipt or bill of lading or security would be given to the bank.

The bank's contention which was adopted and followed in the judgment appealed from was that the written promise referred to in subsection (*b*) was not one required to be given contemporaneously with a proposed loan or advance or having reference to any specific goods or property to be secured, but was a

(1) 110 L.T. 91; 13 D.L.R. 702.

blanket promise sufficient to cover any future loans or advances which the bank might make the promisor up to the time when it was acted upon and security taken. That time might be as counsel boldly put it in argument five or ten years after the promise given, and would enure to cover as well loans subsequently made from time to time to the promisor as property which was not even in existence when the promise was made.

The appellant, on the other hand, submitted that such a written promise as the Act referred to was one having reference to a specific loan then being negotiated for, and to specific goods proposed to be given in security for the loan, stated in the Act as an alternative to the acquisition by the bank of the security itself in those numerous cases in which the loan had necessarily to be advanced to enable the borrower to obtain possession of the goods so that he might give the bank the security.

I have had no hesitation whatever in adopting the appellant's contention on that point. In construing such a very important section as the one in question, which validates a secret and unregistered security on personal property not in possession of the grantee bank and in direct opposition to all provincial laws on the subject requiring registration of such a security, one must exercise one's common sense and common knowledge. I cannot believe it ever was the intention of Parliament to pass a law having the object and purpose contended for by the bank.

The section is a prohibiting one. It declares the bank shall not acquire any warehouse receipt or bill of lading or such security (Form C) as aforesaid to secure payment of any debt or liability unless such debt or liability is contracted *at the time* of the acquisition of the security, or upon a written promise that such security would be given.

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To my mind the object, intent and purpose of the section was plain and is sufficiently well expressed, though perhaps not so clearly as to remove all doubt. Primarily the section required that the taking of the security should be contemporaneous with the negotiation or contracting of the debt or loan. If, however, for any reason that could not be done, and scores of reasons arise to one's mind of conditions in which it could not, then the alternative of a written promise is substituted for the execution of the security. But the written promise to give security had reference, and reference only, not to a future debt or loan to be subsequently made, but to the then debt or loan being negotiated and to the goods and personal property then existing which it was proposed to give security upon, and with reference to which negotiations were taking place. It was only intended in my opinion to cover cases where the actual security could not be given because of the non-possession of the goods or property at the time by the borrower. But it had no reference to future or other loans than the one for a specific amount then being negotiated or to other goods than those specific goods which were to be secured by such loan.

Take an everyday occurrence and it can be multiplied by scores and hundreds. A merchant purchases a load of produce and it arrives at its destination. The bill of lading and draft for purchase price attached are sent to a bank. The purchaser, to get possession, must pay the draft and possibly the freight, carriage and other charges before he can get possession. He applies to a bank for an advance or loan to enable him to get possession of the goods. The bank makes the loan on his written promise to give warehouse receipt or Form C of the Act, as the case may be, as security

when he gets full possession and not till then can he give the warehouse receipt or the statutory security C. So he gives the bank the alternative written promise in the words of the statute

> that such warehouse receipt or bill of lading or security would be given to the bank.

This is only one illustration of the many hundreds of cases in which the "written promise" is made by statute sufficient to take the case out of the express prohibition in the section of the bank acquiring any of the securities including Form C mentioned. But the "written promise," so made by the section an alternative to the execution of the security itself where the borrower is not in a position to give the security, does not extend nor relate to any other loan than the specific one being negotiated or to any other goods than those to which specifically the negotiations for a loan relate. It is obvious, of course, that some time must elapse before, in the illustration I have given, the borrower is in a position to give the security, and the alternative of the written promise to give it in subsection (*b*) of the section is given so that the bank may not be without security for its money which it had to advance to enable the borrower to get the goods.

I am quite unable to find anything in the case of the *Imperial Paper Mills Co.* v. *Quebec Bank* (1), which touches the construction of section 90 or the true meaning to be given to the words "written promise" in subsection (*b*).

Assuming that I am right in my construction of section 90, I am not sure that it can make a material difference in the ultimate result in this appeal, for the plain reason that the bank in every case where they made a loan to Thomas Brothers, Limited, and took

(1) 110 L.T. 91; 13 D.L.R. 702.

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from that firm security in Form C as provided in section 90, included the contemporaneous advance or loan made by them in the amount for which the security was taken. To that extent, therefore, the security would stand. It is true they also included, along with the contemporaneous loan, other loans which they had made to Thomas Brothers, making the security cover as well the amount they had a right to take it for, viz., the contemporaneous loan, as also a very large number of other loans which they had no right to include. This inclusion not being within the statute in my judgment could not, of course, have the effect of making the security effective *quoad* these outside loans, nor could it invalidate the security so far as the contemporaneous loan was concerned.

Then as regards the mortgages I am of the opinion that the findings of fact of the trial judge as to the insolvency of the Thomas Brothers, Limited, and as to the absence of knowledge on the part of the bank and its manager of the insolvency, and as to the previous promise made to give such mortgage, confirmed as those findings were by the court of appeal, should not be interfered with so far as the Ontario real estate is concerned. The learned trial judge, in making his finding, evidently did so by accepting the evidence of the bank manager, Anderson, as to the insolvency of the manufacturing company, and as to the promise to give the mortgage. It was to some material extent a question of credibility. I therefore think his finding, with regard to the mortgage of the Ontario real estate, confirmed by the appeal court, should not be interfered with. But with respect to the Quebec real estate different considerations arise. A mortgage of such lands cannot be upheld, as I understand the law, based upon conditions existing when the promise to give the

mortgage was made, but upon the conditions existing at the time of the giving of the mortgage. No evidence was given before the trial judge or the court of appeal as to the law of Quebec on the question of the validity of mortgages taken at a time when the mortgagor was insolvent. It is clear that such a mortgage in that province cannot be sustained by virtue of a previous promise. As a federal court it is our right and duty to take judicial notice of Quebec law, and I have reached the conclusion that so far as the mortgage of Quebec real estate is concerned it was invalid and should be so declared because at the time of the giving of the mortgage the Thomas Brothers were insolvent.

I would therefore allow the appeal as to the mortgage on the Quebec lands with one quarter of the costs of the appeal as the point was a minor one. As to the $17,600 advanced by the bank after the filing or presentation of the petition for liquidation, no point or question was raised by the liquidator on the argument of this appeal. We, however, referred the questions arising out of these advances back to the parties for what they might have to say regarding the rights of the bank respecting them. After reading these supplementary factums or statements we are of the opinion that if the parties cannot agree as to the rights of the bank with respect to these advances, and the proceeds of the goods and chattels which these moneys were advanced to improve so as to enable them to be sold more profitably than in their unfinished state they could be, it should be referred to the proper officer of the court below to determine whether any of these advances were made under section 20 of the "Winding-up Act" in which case the bank should be entitled to the benefit of the securities taken and if not so made to determine whether the advances were

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made by the bank in the interest of the estate generally and for the completion of the partially manufactured goods and chattels to make them marketable and saleable, in which case the advances so made should be repaid to the bank out of the proceeds of such sales, and any balance left paid over to the liquidator as part of the assets of the insolvent estate.

IDINGTON J.—The most important question raised herein is whether or not the condition upon which a bank is enabled by sections 88 and 90 of the "Bank Act," ch. 29 R.S.C., 1906, to lend money upon the security of goods as therein specified, was duly observed by respondent in its dealings now in question with Thomas Brothers, Limited.

The parts of said sections relative to that in question herein, being subsections 3 and 5 of sec. 88, are as follows:—

(3) The bank may lend money to any person engaged in business as a wholesale manufacturer of any goods, wares and merchandise, upon the security of the goods, wares and merchandise manufactured by him, or procured for such manufacture.

* * * * *

(5) The security may be taken in the form set forth in Schedule C to this Act, or to the like effect.

Sec. 90, sub-sec. 1, is as follows:—

(1) The bank shall not acquire or hold any warehouse receipt or bill of lading, or any such security as aforesaid, to secure the payment of any bill, note, debt or liability, unless such bill, note, debt or liability is negotiated or contracted:

(*a*) At the time of the acquisition thereof by the bank; or

(*b*) Upon the written promise or agreement that such warehouse receipt or bill of lading or security would be given to the bank;

Provided that such bill, note, debt or liability may be renewed, or at the time for payment thereof extended, without affecting any such security.

As far back as January, 1908, we are informed, the company owed the respondent about $200,000 and so continued up to the time it was put in liquidation early in 1914.

The amount of indebtedness to the bank varied and for some time exceeded that sum. But whatever it was it is claimed by respondent securities had been taken upon goods as specified by writings conformable with Form C in the schedule to the "Bank Act."

I cannot find that any of said writings, in fact, observed the requirements of the Act.

In the latest, dated 12th May, 1914, produced in the printed case as a fair sample of many others in the record, the first, and for our present purpose the most essential, part, reads as follows:—

> In consideration of an advance of two hundred and thirteen thousand, four hundred————dollars, made by the Dominion Bank to the undersigned for which the said Bank holds the following Bills or Notes (1) the products of agriculture, the forest, quarry and mine, the sea, lakes and rivers, the live and dead stock, and the products thereof and the goods, wares and merchandise mentioned below, are hereby assigned to the said Bank as security for the payment of the said Bills or Notes, or renewals thereof or substitutions therefor and interest thereon.
>
> This security is given under the provisions of section 88 of the Bank Act and is subject to the provisions of the said Act.

Those mentioned on the back thereof consist of one hundred and three items headed:—

Date of Note	Promisor	When payable	Amt.

Underneath the word "promisor" is written the words "Thomas Bros. Ltd." and underneath "when payable" "demand."

The dates of these notes run from "Sept. 20" to "May 12." The year in which given is not stated.

If we try to ascertain that, and turn to the foot of the document we find the following:—

> This security is given pursuant to the written promise or agreement of the undersigned and especially of agreement, dated 29th day of January, 1914.
>
> Dated at St. Thomas the 12th day of May, 1914.

On calling the attention of respondent's counsel to

(1) Those mentioned on back hereof.

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this being founded on a promise dated 29th January, 1914, yet running back to transactions as early as 20th Sept., 1913, if I understand the document aright, he said there were other documents which preceded and covered those items anterior to 29th January, 1914.

Assuming that to be so, how can respondent justify bringing them forward, as it were, to be incorporated with this document? How can it hope to make this document effective for the purpose of comprehending transactions of an earlier date than the promise relied upon? It certainly could not be permitted to so extend retroactively the operation of the later promise, or the still later lien contract as to include earlier advances than the dates of either the promise or the lien contract or as to include under or by virtue of either a claim upon goods over which Thomas Bros. Ltd. had neither actual nor prospective dominion by virtue of any then existent contract, either when the promise made or lien given.

Then where are we to draw the line? If we draw it at the date referred to in the instrument as the date of the promise, can we be quite sure that we cover thereby all that might rightfully have been considered as falling within the statute?

And supposing we do assume we are right in our guess, what of the anterior promises evidently contemplated to have been had in view by the contracting parties.

Again, which of the written promises or agreements are we to adopt?

The draftsman realized as the fact is and, I submit, law also, that the statute contemplates the existence of only a single promise and that in writing which may and must be the basis of the transaction in order to validate it.

But then he presents us with the impossibility of selecting some one, out of possibly many written promises or agreements, and that

especially of agreement dated 29th day of January, 1914,

to support this security which I now present as a test of what the judgment of the Appellate Division rests upon.

I am also oppressed with the language of the instrument presenting the foundation of the whole transaction as, let it be observed, an advance of $213,400.

It is not a group or series of transactions that the statute enables the bank to lend in respect of, and then provides for a security to be given therefor, but a single transaction, a single advance, and an existent single article or assortment of goods definitely specified and ascertainable by following the description thereof in the instrument; is respectively what the statute contemplates and provides for, by its express terms.

It is the certainty of identification both of the subject matter, and of the intended specific contractual relation in respect thereof, which the statute requires. No doubt facility of identification, in order thereby to prevent fraudulent practices, was also aimed at. But above all a strict and complete compliance with the conditions upon which an exceptional power was given banks, is imperatively required. To go beyond those is to produce that which is *ultra vires* and hence void.

And the respondent by its systematic course of conduct clearly indicates a conception of its limitations and duty in accord with such a view of the statute by getting, or perhaps pretending to have got, on each new advance a new lien security to cover it; yet, inconsistently with such view, at each of same steps trying to cover something else.

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It seems to have hoped by a metaphysical process, as it were, to enable the judiciary to reach the conclusion that a repetition once a year or thereabouts of a general promise could be converted, by a transferable mode of thought, into a divisible or multiple promise self-adaptable to meet any such situation that possibly could arise in the course of the contractual relations between itself and the borrower.

Why did the inventor of the annual promise plan not proceed a step further and substitute as a counterpart thereof, periodical loans and acceptances of lien securities therefor, modelled after that in Form C professed to be followed? Am I right in surmising that it possibly was felt the judiciary could not be expected to accept or assent to so much at one time?

However that may be, the transaction must be as to an advance to a wholesale manufacturer upon some of such goods, wares and merchandise as manufactured by him, or procured for such manufacture.

I am unable to see how such an instrument as this resting upon a statute which seems in every line of the relevant sections to contemplate actual specific loans to be made upon the security of specific goods or such as specifically pointed to in writing, or can be manufactured out of those so indicated with such definiteness as to enable them to be effectively traced and identified can be upheld.

I was at first disposed to think that as to the item for advances made at the time when it was given it might become a security upon the goods described, and hence as these instruments were numerous the respondent's claim might be maintained for something substantial.

But the more I have considered the matter the more absurd does such an instrument seem as a means

of executing the power conferred by the statute. In substance as a result of the respective dealings embraced in each, the others are like unto this.

Then again the only promise relied upon is that contained in the request addressed to the bank for a line of credit.

That if held effective would reduce the legislation to something quite ridiculous.

It would be equally good as a compliance with the statute if made when a man opened an account, and signed it then, and acted in accord therewith for the life of his business, whether a year or score of years.

I cannot think that was the sort of thing which was had in view by the conditional requirement of subsection (*b*) of section 90, quoted above.

Nor can I see how the case of *Imperial Paper Mills* v. *Quebec Bank* (1), touches the question at all.

The object of the legislation evidently was to limit the power of the banks, when taking security of that kind at all, within the narrow limit of doing so at the time of each transaction; or at that time having a specific promise in writing relative to a specific advance.

And the evidence in this case furnishes abundant evidence of the wisdom of so restricting the power of the bank.

It would have been better for respondent and all concerned had the statute been observed in the sense in which I now hold it should be read.

In this view the amendment of subsection 4 of section 88 in the "Bank Act" as it now stands, need not be considered.

Nor, upon the material before us, need any of the other like securities be considered.

If in the long course of dealings between the parties

(1) 110 L.T. 91; 13 D.L.R. 702.

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in question there were any isolated cases of securities given, which can possibly fall within the meaning of the statute, there should be a reference, if respondent desires it, to take an account thereof and report, subject to further directions, upon evidence distinctly proving the facts of a present advance, and specific goods being given as security, and not depending merely upon the production of some pieces of paper and evidence of an agent who does not know the facts, but only speaks to a system existent at some time.

In the mortgage securities called in question I, as the result of a perusal of the evidence, and especially the correspondence between the head office and local agent, bearing thereon, am quite convinced that the respondent well knew when the mortgage was taken on the Montreal property that the company was insolvent and that continuing in business was, for its own purposes, a better expedient than winding it up.

It had only been by careful nursing and direction on its part until that and possibly other securities were got, that the insolvency had not been exposed to the world at a much earlier date.

I think there is no difficulty in reaching and setting aside such a contract made in this province between the respondent and its debtor, as this was, and of necessity had to be here—though registration as result thereof had to conform with the Quebec law.

As to the other security I entertain a different view.

The condition of the concern was not so obviously hopeless at the date of the execution of the chief mortgage as of that of the later one.

Again that earlier mortgage was preceded by an agreement which may be upheld so far as restricted to antecedent debts, and within those limits may protect

the mortgage without rendering it offensive against the prohibition restricting banks from making loans on real estate.

With some doubt I have in relation to that aspect of the matters involved, but not touched upon in argument, I incline to hold the mortgage may be upheld.

Yet I must say that with the intimate knowledge the respondent had of the company's actual financial condition and mode of operating, it is difficult to understand how it could have hoped for any other ultimate result than that of its being forced into liquidation.

If called upon to pay, which is the crucial test, it must have been held insolvent by any shrewd business man acquainted with its affairs. It is more in deference to that of others than to my own judgment that I assent to the judgment below in that regard.

I think the appeal should be allowed with costs throughout in regard to the main objects of the appeal as indicated herein.

ANGLIN J.—The appellants, who are the liquidator and a creditor of Thomas Bros., Limited, an insolvent manufacturing company in liquidation, brought this action to set aside two mortgages on real estate and pledges of certain goods, purporting to have been made under subsection 3 of section 88 of the "Bank Act" (R.S.C. 1906, ch. 29, and 3 & 4 Geo. V. ch. 9), held by the respondent bank for an indebtedness of the company which amounted to about $213,400 on the 12th day of May, 1914, twelve days after the winding-up order was made.

The bank apparently received payments and made advances up to that date. The advances between

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March 25th, the date of presentation of the petition for winding-up, and May 1st, the date of the winding-up order, amounted to $15,400. After May 1st $2,200 more was advanced. The company's indebtedness to the bank, however, which on March 24th amounted to $228,827, had been reduced on May 12th, when the last advance of $200 was made, to $213,400. The earliest outstanding note on March 25th, 1914, bore date August 16th, 1913. If those outstanding notes represented actual contemporaneous advances, as the bank maintains they did, they would all fall within subsection 4 of section 88 of the "Bank Act" which came into force in July, 1913. The bank had put its representative in possession on the 24th of March, 1914. By subsequently realizing on its securities (except the St. Thomas mortgage) it had reduced the company's debt to $135,000 at the date of the trial.

Except as to such of the pledged goods as were dealt in but not manufactured by the company, which are not now in question, the action was dismissed by Sutherland J (1), and on appeal by the plaintiffs the Appellate Division sustained his judgment (2).

The attack on the real estate mortgages as fraudulent and void against the liquidator and as calculated to hinder and delay the creditors of the company, which was but faintly pressed at bar, in my opinion fails on the facts stated in the judgment delivered by the learned trial judge and affirmed in the Appellate Division. Anderson's evidence, having been believed by the judge who saw and heard him give it and by the Appellate Division, should not be rejected here unless under very exceptional circumstances.

The Ontario mortgage is supported by the promise of May, 1912. On the facts found by the trial judge

(1) 37 Ont. L.R. 591. (2) 40 Ont. L.R. 245; 38 D.L.R. 232.

and accepted by the Appellate Division, notorious insolvency within art. 2023 C.C. sufficient to invalidate the Quebec security was not established, and the insolvency of the company was not known to the bank when it was taken. Art. 1035 C.C. The plaintiffs' attack on this mortgage, however, was based entirely on the Ontario statute, R.S.O. ch. 134, sec. 5. They did not invoke the Quebec law. But see *Morrow* v. *Hankin* (1), and *Logan* v. *Lee* (2). Before setting aside this hypothec I should have to consider very carefully the jurisdiction of the Ontario courts to do so.

The case presented as to the securities under the "Bank Act" demands fuller consideration. Some facts in addition to those which I state and extracts from the relevant documents that may serve to make more comprehensible the situation out of which the questions discussed arise appear in the judgments below.

Prior to 1908 the company's line of credit with the bank did not exceed $150,000. In that or the next year it was increased to $175,000, and later, in 1909, to $200,000, continuing at about that figure until the date of the insolvency. During the same period the company's indebtedness to the bank varied slightly. Seldom below $200,000, it would appear to have reached a maximum of $233,000 about the 16th of April, 1914.

To quote from the judgment of Maclaren J.A.:—

> The records of the transaction in question were kept in two separate accounts by the bank, called respectively the purchase account and the sales account. The former contained on the credit side the record of all the demand notes which the company gave from time to time, generally for round amounts ranging from $1,000 to $10,000. On the debit side were entered all cheques given for payment of goods, wages, expenses, interest, etc. On the credit side of the sales account were entered the cash deposited, cheques of customers, drafts for collection, etc. On the debit side the demand notes of the company paid off from time to time, customers' notes or drafts returned unpaid, etc.

(1) 58 Can. S.C.R. 74, 45 D.L.R. 685. (2) 39 Can. S.C.R. 311, 313.

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As the learned trial judge said, however:—

> The two accounts had to be looked to to ascertain the exact standing of the customer with the bank, from time to time, and advances were made to the company in the advance account (called by Maclaren J.A. the purchase account), as they had credits in the other account. The two accounts had, of course, relation to each other and seemed in reality to be treated as one account.

The evidence of the bank manager establishes with reasonable certainty that each of the demand notes given from time to time for the sums placed to the credit of the "Purchase Account" was not a renewal note in any sense, but represented an actual advance made at the time the note was taken—an actual increase by the amount of the note (through withdrawals of its proceeds made by the company then or within a day or two afterwards) of the company's indebtedness to the bank as shewn by its net debit balance taking the two accounts together. It should perhaps be noted that discount was not deducted from the notes. Their face amounts were credited to the purchase account and bore interest at six per cent. The learned trial judge says:—

> It seems to me from the evidence in this case that the bank was from time to time making advances and taking security under section 88 of the "Bank Act."

As Maclaren J.A. says, distinguishing this case from *Bank of Hamilton* v. *Halstead* (1):—

> So far as the evidence goes the company had always the privilege of drawing the full amount that had been put to its credit through the negotiation of the demand notes.

The moneys represented by each of the demand notes were actually

placed freely at the disposal of the customer,

as in *Ontario Bank* v. *O'Reilly* (2), at p. 432,

were placed under the control of the company,

Toronto Cream & Butter Co. v. *Crown Bank* (3).

(1) 28 Can. S.C.R. 235; 27 O.R. 435; 24 Ont. App. R. 152.

(2) 12 Ont. L.R. 420.

(3) 16 Ont. L.R. 400, 413.

In the *Halstead Case* (1), as pointed out by Meredith C.J., whose judgment was approved in this court,

> Not a farthing of the amounts which the notes represented could be touched by (the customer) or made available by him for any purpose.

The practice in the case at bar was from time to time to retire the demand notes longest outstanding by cheques of the customer drawn on its "Sales Account" or by charging up the amounts of such notes against its credit balance in that account. The advances were made quite independently of such retirements.

Concurrently with the taking of each demand note and the placing of the moneys represented by it to the credit of the "Purchase Account," from which they were subject to withdrawal by the company at its will, the bank took a pledge under section 88 of the "Bank Act" on all the raw material, manufactured goods and goods in process of manufacture in the customer's premises. Down to the 7th of March, 1914, two separate documents were obtained on each occasion, one a pledge or security for the advance then being made (demand note contract), the other an "omnibus security" (as I shall term it for lack of a better name), for that advance and such prior advances as were represented by demand notes then outstanding (*i.e.*, not yet retired as above explained), a list of which was indorsed on the back. After the 29th of January, 1914, new forms of the omnibus security were used in which the goods are somewhat more fully described but no special allusion is made to the amount of the concurrent advance. Some ten advances, amounting in all to $17,000, appear to have been made between the 7th of March and the date of presentation of the petition for winding-up, the 25th of March, 1914. No document similar to the early "Demand Note Contracts" was

(1) 27 O.R. at p. 439.

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taken as security for any of the advances subsequent to the 6th of March. On the back of the omnibus security obtained when each of them was made was indorsed a list of the then outstanding notes, and the security was stated on its face to be given in consideration of their total amount, the last item in the indorsed list being uniformly the amount of the note for the actual concurrent advance. On the last of these securities taken before the winding-up—that of the 24th of March, 1914—77 of the 103 notes in the indorsed list bear dates between the 16th of August, 1913, and the 29th of January, 1914, and only 26 bear subsequent dates. Yet the document purports, as do all the securities taken after that date, to be given pursuant to a written promise or agreement of the 29th of January, 1914. I shall have occasion again to advert to this fact.

The securities taken before the 29th of January, 1914, contain no explicit reference to an antecedent written promise, although such a promise that security would be given under section 88 of the "Bank Act" had been obtained by the bank annually or oftener when the line of credit for the ensuing period of a year, or less, as the case might be, was arranged for. Whatever may be its value as security for previous advances, I know of no good reason why each of these documents taken on and after the 7th of March, 1914, should not be a perfectly good and valid security under section 88 (3) and clause (*a*) of subsection 1 of section 90 of the "Bank Act" for the actual concurrent advance.

I am satisfied that all prior securities were not discharged by substitution or merger as the result of the taking of the new general security given when each fresh advance was made. This in my view is really the crucial question in this case, and it is perhaps

regrettable that more attention was not given to it in argument. If there was no merger of earlier in later securities—if the securities taken concurrently with each advance are still alive and enforceable—the bank's position seems to me to be free from difficulty, since the requirements of clause (*a*) of subsection 1 of section 90 are met. On the other hand, if there was a merger or substitution—if the last security taken absorbed and extinguished all prior securities held for the advances for which the outstanding notes indorsed upon it had been given—the stated consideration included them—it is obvious that it would be necessary to establish that as to such prior advances—past indebtedness—the absorbing or substituted security was given pursuant to a promise or agreement that would satisfy clause (*b*) of subsection 1 of section 90. The question of merger or substitution is only of importance if the omnibus securities taken on the occasion of each advance cannot be supported in respect of the prior indebtedness included in the stated consideration; and it is on that assumption that it is now discussed.

Strong as the legal presumption of merger of an earlier security, which arises upon the taking of a new security of a higher nature for the same debt, undoubtedly is (*Price* v. *Moulton* (1)), it yields to satisfactory proof of a contrary intention (*Commissioner of Stamps* v. *Hope* (2)); and there is no such presumption where the new and the old securities are of equal degree. 7 Hals. Laws of England 457; *Preston* v. *Perton* (1601) (3).

A good prior security will not be held to merge in a later inoperative one.

Chetwynd v. *Allen* (4), at page 358, *per* Romer J.

(1) 10 C.B. 561, 574.
(2) [1891] A.C. 476, 483-4.
(3) Cro. Eliz. 817.
(4) [1899] 1 Ch. 353.

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Substitution, like merger, is largely a question of intention. *Ex parte Whitmore* (1). Where the taking of further security is the real purpose of the new instrument there is no extinguishment of the earlier security. *Twopenny* v. *Young* (2). The principle underlying the equitable doctrine that merger of estates and merger in the fee of a paid-off mortgage security on real estate are questions of intention actual or presumed, and that an intention to keep a charge alive will be presumed when that is for the benefit of the person against whom it is sought to set up merger; *In re Pride* (3); *Adams* v. *Angel* (4), may well be applied where merger or substitution of securities on personal property is claimed under circumstances such as those now before us. No reason can be suggested why the bank would willingly part with or permit the extinguishment of any security held by it in a case such as this. It would be so contrary to what is commonly well understood to be the practice of bankers—so obviously contrary to the bank's interest, that I should require clear and convincing evidence that such a merger or substitution was intended before admitting that it had in fact taken place.

In the securities taken before the 29th of January, 1914, the customer is made to represent that the goods pledged

are free from any mortgage, lien or charge thereon.

I take it that was intended to mean other than liens or charges held by the bank itself, although it would certainly have been more satisfactory had this exception been expressed as it is in the securities taken on the new forms in use after that date.

(1) 3 Deac. 365, 372.
(2) 3 B. & C. 208.
(3) [1891] 2 Ch. 135, 142.
(4) 5 Ch. D. 634, 641-2, 645.

I agree with the observation made by counsel for the plaintiffs in the course of the trial that

there is nothing in the documents themselves to shew whether they are in substitution or not.

Yet my inference from them, paying due regard to the surrounding circumstances, would be that no merger or substitution was intended.

The question of intention, however, is not left entirely to mere inference. The bank manager was called as a witness by the plaintiffs. In answer to questions put by their counsel on direct examination (of course without objection being taken on behalf of the defendant), he gives this evidence:—

Q.—Looking again at this last receipt (exhibit 8) taken under section 88 I see it is for $213,400? A.—Yes.

Q.—That amount represents the amount of notes going back to what date? A.—Represents the amount of notes going back to September 20th, 1913.

Q.—All those notes that are represented on the back of this contract were also represented in numerous other contracts which you took after the 20th day of September? A.—All the notes that were unpaid would be.

Q.—You took a new contract with every note? A.—With every note.

Q.—So that at the time you took this contract (exhibit 8) did you hold all these other contracts? A.—We held all those other contracts.

Q.—You held contracts dated the date of each of those notes? A.—We held contracts dated the date of each of those notes.

Later in his direct examination, in answer to a question pressed by counsel for the plaintiffs, notwithstanding objection, the witness first said positively that there was no substitution of new securities for older ones and, a moment or two later, that

it never entered into my head until now whether I took it (the later security) in substitution or not.

The plaintiffs can scarcely complain if this evidence elicited by them from their own witness is used against them. So far as it may be admissible it goes to confirm the inference that I should draw without it from the

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circumstances that merger of, or substitution for, earlier securities was not intended.

From the whole case I gather that the banker's idea in taking securities in this omnibus form after July, 1913, was that something of the kind was necessary in order to obtain security on the new goods brought in to replace those sold and taken away in the ordinary course of business. That I think may fairly be said to be the purport of the bank manager's testimony. Whatever advantages it may have had before the amendment to the "Bank Act" of 1913, this practice has been unnecessarily, and I cannot but think unwisely, continued since. Subsection 4 of section 88, first introduced at that time, provides that in the event of goods held under a security given for money loaned under that section being removed with the consent of the bank and similar goods brought in substitution therefor, the goods

> so substituted shall be covered by such security as if originally covered thereby,

i.e., by the security held upon the goods so removed. A new security is neither contemplated nor required. The nature of Thomas Brothers' business leaves no room for doubt that the sale and consequent "removal" of their products was "with the consent of the bank." See, too, the last clause of subsection 4. Securities held upon goods so removed attached automatically under that subsection to goods

> substantially the same in character * * * substituted therefor.

Yet we find in the new form of promise adopted by the bank in 1914, presumably drafted because of the amendment of 1913, this clause:—

> 6. If with the consent of the bank, the goods or any part thereof are removed, other goods, of substantially the same character and of at least the same value as those so removed, shall be thereupon forthwith substituted therefor and the customer hereby agrees, so often as every

such removal and substitution shall take place, to give and shall give warehouse receipts, bills of lading or securities under the "Bank Act," covering such substituted goods, all of which shall be subject to the provisions hereof.

Acting under this clause and taking the further security which it indicated as proper, if not necessary, the bank manager had no idea of relinquishing any security already in hand. To do so would never occur to him.

Elaborate (and perhaps in the respect indicated misleading) as the bank's new forms of 1914 are, the new form of pledge then adopted omits what should have been one of its prominent features, if, as was apparently the case, it was intended to continue the former practice of including in each new security all outstanding notes, namely, a clause explicitly providing that there should be no merger or absorption in it of, or substitution of it for, any securities given for past advances. Without such a clause the taking of securities in the omnibus form adopted by the bank is unavoidably fraught with the danger of affording some colour to the contention put forward in this case that substitution for, or merger and extinguishment of, prior securities was thereby affected.

That no such merger in fact took place was the view of the learned trial judge. He says:—

It is contended on the part of the plaintiffs that there was in reality the same course of dealing between the bank and its customer in this case as was held to be invalid in the *Halstead Case* (1). It seesm to me, however, from the evidence in this case, that the bank was from time to time making advances and taking security under section 88 of the "Bank Act" on the new goods which were coming in. The goods were from time to time changing as old stock was sold and new stock brought in to replace. A separate note and security was taken for each advance. A general security was also taken referring to all outstanding notes as to each of which a previous individual security had been taken. This it seems to me could not be called a substitution, but rather a consolidation.

(1) 28 Can. S.C.R. 235.

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There was consolidation, however, only in the sense that as a convenient method of keeping track of the total secured indebtedness and apparently as something erroneously thought to be necessary in order to secure the benefit in regard to them of subsection 4 of section 88, the outstanding notes were included in the statement of the consideration for each new omnibus security and were scheduled by indorsement upon it. There was no consolidation in the sense of any merger or absorption of the earlier securities such as would extinguish them or render them unenforceable.

This question is not dealt with in the opinion delivered by Maclaren J.A. in the Appellate Division probably because he held the omnibus securities good by virtue of the antecedent promises given under clause (*b*) of section 90, in respect of the past advances which they purported to cover as well as the advances made concurrently.

I am of the opinion that the lien taken on the occasion of obtaining each of the advances represented by notes that were still outstanding at the date of the commencement of the winding-up may be regarded as a valid and subsisting security on such of the goods covered by it as remained in the hands of the company at that date (including in the case of liens taken after the 1st of July, 1913, substituted goods), since each of such demand notes represented an actual present advance, and the security was given concurrently with the making of it as required by clause (*a*) of subsection 1 of section 90 of the "Bank Act," and was not merged in or otherwise extinguished by any of the securities subsequently taken in omnibus form.

Since the 1st of July, 1913, when subsection 4 of section 88 of the "Bank Act" (3 & 4 Geo. V. ch. 9) came into force, the advances by the bank amounted

to over $300,000. The goods within subsection 3 of section 88 on hand at the date when the winding-up began were valued at $83,637.92. The annual turnover of the company had been over $450,000. The earliest outstanding note when the winding-up began bore date the 13th August, 1913. There can be little room for doubt, therefore, having regard to the provision for substitution made by subsection 4, that all the goods in stock at that time were covered by valid securities in the hands of the bank.

In case there should be any difficulty in sustaining its claim under clause (*a*) of subsection 1 of section 90, counsel for the bank also contended that he was entitled to support each of the omnibus liens taken for all outstanding notes by the promises for security which the bank had obtained annually or oftener from the company. Counsel for the appellants challenged this position, maintaining that a promise in order to meet the requirements of clause (*b*) of subsection 1 of section 90 must be made contemporaneously with the advance in respect of which the promisor undertakes to furnish security. I am unable to read such a restriction into clause (*b*).

Section 90 so far as material reads as follows:—

> 90. The bank shall not acquire or hold any warehouse receipt or bill of lading, or any such security as aforesaid, to secure the payment of any bill, note, debt or liability, unless such bill, note, debt or liability is negotiated or contracted:
>
> (*a*) At the time of the acquisition thereof by the bank; or
>
> (*b*) Upon the written promise or agreement that such warehouse receipt or bill of lading or security would be given to the bank.

A promise to furnish security for advances to be made in the future is not within the mischief against which section 90 was meant to provide. The mischief aimed at is the taking of security for past indebtedness. The canon embodied in the maxim *expressio unius est*

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exclusio alterius would seem to preclude the narrow construction which the appellants seek to place on clause (*b*). Clause (*a*) and clause (*b*) are independent alternatives. Clause (*a*) explicitly prescribes that in the case of a security to which it applies, the bill, note, debt or liability, to secure which it is given, must be negotiated or contracted at the time the bank acquires the security. Clause (*b*) alternatively provides that, if not so taken, the security must be given pursuant to a written promise or agreement to give it, on the faith of which the bill, note, debt or liability has been negotiated or contracted. The mischief against which the section was designed to provide of course excludes from the purview of clause (*b*) a promise or agreement given or entered into after the advance has been made. But I find nothing to warrant excluding a prior promise —nothing to justify importing into clause (*b*) the restriction as to time which Parliament has placed in clause (*a*)—no reason for substituting for the introductory words of clause (*b*), "upon the," which clearly mean "on the faith of the," some such words as "at the time of obtaining a." The use in it of the preterite-subjunctive form of the verb, "would be given," tends to confirm this view of the proper construction of clause (*b*); if the construction contended for by the appellants were correct one would expect to find the verb in the future tense—"will be given."

Apart entirely from authority, my view of the proper construction of clause (*b*) is that the written promise or agreement for which it provides may be given prior to, or at, the time when the bill, note, debt or liability to be secured is negotiated or contracted. Of course it must be possible to identify the advance as one to which the promise was intended to apply, and the goods as property on which the security was promised by it.

As Maclaren J.A. points out, however, although not explicitly referred to in the judgment of the Privy Council in *Imperial Paper Mills Co.* v. *Quebec Bank* (1), the question now raised as to the construction of clause (*b*) can scarcely have escaped their Lordships' attention in view of Lord Shaw's detailed statement, at page 92, of the course of business pursued, and of the fact that the judgment appealed from (2), at pages 645, 653, 655, itself shewed that in one instance, although the promise for security was made in August, 1905, the demand note for $120,000 and the security therefor were given only in February, 1906, the actual advances having been made from time to time in the interval. This security was upheld.

The decision of their Lordships is chiefly valuable, however, as affording an answer to the objection taken by the present appellants to the sufficiency of the description of the goods in the securities taken by the respondent bank.

No doubt the promise of the 29th of January, 1914, would not suffice under clause (*b*) of subsection 1 of section 90 to support the securities subsequently taken in so far as they were for advances represented by notes of earlier date. For that purpose the earlier promises should have been referred to as well. But if there was no substitution for the earlier securities, or merger of them in, or extinguishment of them by, the later securities taken, this omission is not of much moment. In any case, since the earlier written promises in fact existed, I think they might be proved and relied upon notwithstanding the fact that the promise of the 29th of January, 1914, is alone mentioned in the liens taken after that date.

(1) 110 L.T. 91; 13 D.L.R. 702.

(2) 26 Ont. L.R. 637; 6 D.L.R. 475.

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A more serious objection to supporting any of the liens as a security for any advance earlier than that actually made contemporaneously with it would seem to be that the promise to give security for such earlier advance was probably fulfilled and satisfied by the security taken at the time it was made and cannot, therefore, be relied on to support subsequent security for it. Except perhaps for the purpose of clause 6 of the "promise" of the 29th of January, 1914, which I have quoted, there was no promise for any further security.

But if the view I hold that the security taken for each advance at the time it was made was efficacious and continued in force is sound, it is unnecessary and it would probably be unwise to dwell further upon other phases of this case. I have referred to them merely to make it clear that I do not share the views upon the construction of clause (*b*) of subsection 1 of section 90 which I understand some of my learned brothers entertain.

As to the advances, amounting to $17,600, made by the bank after the presentation of the petition for winding-up (R.S.C. ch. 144, sec. 5) it can claim only in so far as the liquidator may have sanctioned them as necessary for a beneficial winding-up (*ibid.* sec. 20), or as the court may consider it entitled under the doctrine of equitable subrogation to the benefit of securities (including under them substituted goods within subsection 4 of section 88) held by it for so much of its indebtedness as was paid off during the same period.

I would dismiss the appeal with costs.

BRODEUR J.—This is an action by the liquidator and a large creditor of the insolvent company, Thomas

Brothers, Limited, to set aside certain securities held by the respondent bank on the goods of that company, and also to set aside two mortgages given in favour of the bank.

The courts below dismissed that action, except as to a small item which is not in issue in this appeal.

It is claimed by the appellant that those securities are contrary to the provisions of sections 88 and 90 of the "Bank Act," and that the mortgages were signed when the debtor was insolvent to the knowledge of the creditor and that the effect of those mortgages gave the bank an unjust preference over the other creditors.

Dealing first with the securities. I see that from 1906 until the petition for a winding-up order was presented by the bank on the 25th of March, 1914, the company was indebted to the bank for the sum of about $200,000. On the 24th of March, 1914, on the eve of the presentation of the petition, the indebtedness, as appears by the security given that day, was of $228,827. As stated in the document the security was given

> pursuant to a written promise or agreement of the undersigned (Thomas Brothers Limited), and especially of agreement dated 29th January, 1914,

and it was

> in consideration of an advance of $228,827 made by the Dominion Bank to the undersigned for which the said bank holds the following bills or notes:

and then follows a list of 103 notes ranging in amount from $127 to $5,500 and dated from the 16th of August, 1913, to the 24th of March, 1914. It appears rather peculiar that the security was given in virtue of a promise made in January, 1914, when most of the notes covered by the security were dated before this last date.

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The promise or agreement relied upon by the bank was in the form of a request signed by Thomas Brothers to the bank

> to makes advances to the undersigned (herein called the customer) from time to time and in consideration thereof the customer doth hereby promise and agree as follows: (1) To give from time to time to the bank security for every advance and interest by way of warehouse receipts, bills of lading or securities under sections 86-87-88 & 90 of the "Bank Act."

It cannot be pretended that a promise made under section 90 of the "Bank Act" could cover advances made before it was signed. Besides, the terms of the promise itself in this case were not to cover past indebtedness but future advances. So the promise of the 24th of March, 1914, could not validly cover the notes discounted or signed before the date of the promise.

Could that promise, however, validate notes negotiated after it was made? This is the main question at issue in this case.

By section 88 of the "Bank Act," it is provided in subsection 3 that

> the bank may lend money to any person engaged in business as a wholesale manufacturer of any goods, wares and merchandise upon the security of the goods, wares and merchandise manufactured by him or procured for such manufacture.

Section 90 of the "Bank Act" is the section which has to be construed in order to find out whether the promise above mentioned was valid or not. It provides that the bank shall not acquire any security

> to secure the payment of any bill, note, debt or liability, unless such bill, note, debt or liability is negotiated or contracted:
>
> (*a*) at the time of the acquisition thereof by the bank; or
>
> (*b*) upon the written promise or agreement that such warehouse receipt or bill of lading or security would be given to the bank.

That provision of the "Bank Act" is a derogation from the prohibition in section 76 concerning lending

money upon the security of goods, wares and merchandise.

This section is also a derogation from the law concerning chattel mortgages. In some provinces, statutes relating to bills of sale, to chattel mortgages, etc., have been passed to recognize change of ownership or of legal relations respecting personal property without change of possession or change of possession without change of ownership. Those chattel mortgages have to be registered and are surrounded with provisions which, if not absolutely carried out, render the bills of sale or chattel mortgages null and void. The provincial law surrounds with extraordinary precautions the validity of chattel mortgages and where the procedure enacted by the legislature is not scrupulously followed those mortgages are held not to be valid against the assignee. *Gault Bros.* v. *Winter* (1).

The Canadian Parliament thought it advisable, however, with regard to the banks to give them the power to take security in the nature of chattel mortgages or bills of sales upon the property of the wholesale manufacturers; and those securities might be taken without any publicity being given to the existence of such chattel mortgages or such bills of sale.

Then I say, applying the principle that we have laid down in the case of *Gault Bros.* v. *Winter* (1), that the procedure which is enacted by the legislature should be followed entirely to render valid the securities taken by the bank.

The object of the law is not to give to the bank an authorization to take securities or bills of lading, for money which had been previously lent, in other words, for past indebtedness, but the loan must be made contemporaneously with the taking of the security or

(1) 49 Can. S.C.R. 541; 19 D.L.R. 281.

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the giving of the promise. The bill or note must be negotiated at the time the bank acquires the securities or at the time at which a written promise is made that security shall be given; otherwise the bank could for years in advance hold a promise that a security will be given and when they see that their customer is in financial difficulty take a security upon all his goods.

That was practically what was done in this case. The promise relied upon was given in the month of January, 1914, and similar promises had been made also in the previous years every time the customer was applying for a line of credit or for the continuation of his line of credit. Then on the 24th of March, 1914, on the day previous to the presentation of the petition for winding-up the company, the bank takes a security upon all the stock of the company. That security given on the 24th of March constituted not only a preference given by an insolvent debtor to one of his creditors who was aware of his insolvency but also constituted a formal violation of the provisions of section 90 of the "Bank Act."

Then applying the principle that we have laid down in the case of *Gault Bros.* v. *Winter* (1), the procedure which is enacted by the legislature should be followed entirely to render valid the securities taken by the bank.

As I have said the object of the law is to give to the bank an authorization to take securities for contemporaneous indebtedness. It may happen that a manufacturer has to pay cash for some goods, even before their delivery; then the "Bank Act" authorizes the bank to advance the money to the manufacturer on the promise then made that the latter will give it security on those goods. In such a case, the security would

(1) 49 Can. S.C.R. 541; 19 D.L.R. 281.

be valid. It is the case contemplated by subsection (*b*) of section 90.

It is contended, however, that if the security is not valid as a security based on a promise, it would be valid as a security based upon advances made at the time of its acquisition under the provisions of paragraph (*a*) of section 90.

In that respect it becomes necessary to examine the agreements made after the 29th of January, 1914, and those made before that date, since they were made in different ways.

After the 29th of January, 1914, the securities were all based on the promise of that day and they all contain this provision:—

> This security is given pursuant to the written promise or agreement of the undersigned and especially of agreement dated 29th January, 1914.

Those securities profess then to have been given under paragraph (*b*) of section 90. I do not see how we could now ignore that and say that they should be considered as having been given under paragraph (*a*) of that section.

If it were only a question of agreement between two parties, and there would be some ambiguity, we might perhaps try to find the true intention of the parties and apply with less stringency the ordinary rules of construction, but those securities affect not only the contracting parties but also all the creditors of the party who gave the security. The "Bank Act" enacts positively that the banks shall not lend money upon the security of any goods (art. 76, subsec. 2), except as specifically authorized by the Act. It is then of principle that the banks should make advances to their clients without looking for any special security. There are exceptions; but those exceptions must be strictly construed.

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In the case of a manufacturer the bank could, when they discount a note, take then a security on his stock for the amount of that note, or they could then take from him a promise that in a few days he would give them, to protect their claim, warehouse receipts, bills of lading, or other security; but the provisions of the law in that respect must be rigorously followed. If the customer and the bank have found it advisable to give and take a security based upon a promise, they could not substitute later on a security based upon advances.

This court has virtually laid down the above principle in the case of *Bank of Hamilton* v. *Halstead* (1). Mr. Justice Girouard, who rendered the decision for the court, stated that the Act does not authorize the substitution of one assignment for another.

As to the agreements made before the 29th of January, 1914, Thomas Brothers were, when they had an advance made, in the habit of giving a security on their goods for that specific sum. That was unquestionably valid.

But they were, at the same time, giving a security for all the notes previously discounted, including the one discounted on that day, and the agreement contained the following provision:—

> This security is given under the provisions of section 88 of the "Bank Act" and is subject to the provisions of said Act. The said goods, wares and merchandise are now owned by Thomas Brothers, Limited, and are now in possession of Thomas Brothers, *and are free from any mortgage, lien or charge thereon.*

The agreement with the provision that the goods of Thomas Brothers were free from any mortgage, lien or charge thereon was then handed over to and accepted by the bank. That constituted, according to my

(1) 28 Can. S.C.R. 235.

opinion, an implied renunciation, on the part of the bank, of the lien or charge which existed before on the goods of Thomas Brothers in its favour.

The bank, seeing evidently that this declaration on the part of Thomas Brothers that there was no previous lien or charge was a declaration which might affect the validity of their security, changed the provisions of the agreement and we find later on that the securities contain the following:—

> The goods, wares and merchandise are now owned by and are now in the possession of the undersigned and are free from any mortgage, lien or charge thereon (excepting only previous assignments to the said bank, if any.)

I am then on that point of opinion that the securities which have been given before the 24th of March, 1914, or before the petition for winding-up, are not valid and cannot be invoked against the liquidator and creditors of Thomas Brothers and should be set aside.

Now coming to the question of mortgages, I find that the trial judge—and in that respect he is confirmed by the Appellate Division—was of opinion that the mortgages are valid.

In 1912, Thomas Brothers had given a promise that the securities by way of mortgages would be given on or before the 1st of October, 1912. These mortgages were not given at the time stipulated.

In 1913, a statement was prepared which seemed to shew a considerable profit in the company's business to the end of August, 1912. But in the fall of 1913, the bank produced a note by Clarkson & Co. which seemed to shew that the previous statement was inaccurate.

This naturally made the bank more anxious and they became insistent as to the real estate securities. They then signed a first mortgage on property situate in Ontario.

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In view of the findings of fact made by the trial judge, and confirmed on that point by the Appellate Division, I would not be ready to disturb that judgment as far as the Ontario mortgage is concerned; but on the 22nd of January, 1914, just two months before the petition for winding-up was presented, a mortgage was taken upon a property situate in the Province of Quebec.

I am of opinion that with respect to that mortgage, the law of the place where the property was situate and where the mortgage has been given should govern. According to articles 2023 and 1032 *et seq.* of the Civil Code, where a creditor has knowledge of the insolvency of his debtor, he cannot take a valid mortgage on the property of his debtor.

There is no doubt that on the 22nd January, 1914, the bank knew that Thomas Brothers were unable to meet their liabilities. Then, according to my opinion, the Quebec mortgage should be set aside.

For these reasons, the appeal should be allowed with regard to the securities and with regard to the Quebec mortgage with costs throughout.

MIGNAULT J.—I agree with my brother Anglin that there was no merger of previous securities given by Thomas Brothers, Limited, to the respondent by the fact that the prior advances by the latter were mentioned along with the contemporaneous advance made on the date when the new security was given to the bank. Each security was good for the contemporaneous advance and void as to the prior advances, but inasmuch as each of these prior advances was accompanied by the giving of security under section 88 of the "Bank Act," and as these prior securities were not merged in the subsequent security taken by the bank

for another advance, the respondent holds securities for all its advances which meet the requirements of clause (*a*) of subsection 1 of section 90 of the "Bank Act."

It may, however, be remarked that the form of these securities is most misleading. Taking, for example, that of the 12th May, 1914, on which date an actual advance of $200 only was made, the contract or security begins by the words:—

> In consideration of an advance of two hundred and thirteen thousand four hundred dollars, made by the Dominion Bank to the undersigned, for which the said bank holds the following bills or notes:

This was almost inviting disaster in view of the imperative terms of clause (*a*), for out of this so-called advance of $213,400, the sum of $213,200 represented bills, notes, debts or liabilities which were not

> negotiated or contracted at the time of the acquisition thereof by the bank.

It is only because the subsequent security did not supersede the prior securities given to the bank at the time of each advance, that the respondent can claim to have security under section 88 of the "Bank Act" for more than the amount actually advanced by it at the time the last security was given by Thomas Brothers, Limited.

It was contended, however, by Mr. McCarthy that each security was covered by a prior promise given by Thomas Brothers, Limited, and that this would validate the security as to the prior advances under clause (*b*) of subsection 1 of section 90. This clause, taken in connection with the first paragraph of subsection 1, states that

> The bank shall not acquire or hold any warehouse receipt or bill of lading, or any such security as aforesaid, to secure the payment of any bill, note, debt or liability, unless such bill, note, debt or liability is negotiated or contracted:
>
> (*a*) .....
>
> (*b*) upon the written promise or agreement that such warehouse receipt or bill of lading or security would be given to the bank.

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I think the meaning of section 90, as a whole, is that there must be, when the bill or note is discounted by the bank, either

(a) The giving of security under section 88 contemporaneously with the discounting of the note; or

(b) An existing written promise to give such security to the bank at some future time.

In my opinion this written promise must be a specific promise to give a specific security at a subsequent date, and not a general promise to give security for any advance which the bank may make to the customer from time to time. It does not appear necessary that the note be discounted at the time the promise is made, provided that the note be discounted by the bank upon, *i.e.*, in pursuance of, such a promise. When this written promise has been given, security may be taken by the bank to cover prior advances made by the bank upon such a specific promise.

Referring again to the security of the 12th May, 1914, it states:—

> This security is given pursuant to the written promise or agreement of the undersigned, and especially of agreement dated 29th day of January, 1914.

The written promise of 29th of January, 1914, says:—

> The Dominion Bank (herein called the "bank") is hereby requested by the undersigned to make advances to the undersigned (herein called the "customer") from time to time, and in consideration thereof, the customer doth hereby promise and agree as follows:—
>
> 1. To give from time to time the bank security for every such advance and interest by way of warehouse receipts, bills of lading, or securities under sections 86, 87, 88 and 90 of the "Bank Act."

In my opinion this promise being a general promise referring to no specific security to be given in pursuance of the promise, but merely undertaking to give security for any advance which the bank may make from time to time, does not meet with the requirements of clause

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(*b*). I may add that if clause (*b*) were construed so as to validate securities for any prior advances which the bank might have made to the customer from time to time in pursuance of such a general promise made possibly years before the advances, the whole object of section 90 would be defeated.

Fortunately, however, for the respondent each security taken by it is good for each contemporaneous advance, and the prior securities are not merged into the subsequent ones, so that the claim against Thomas Brothers, Limited, is secured.

I have referred to the security given to the bank on the 12th May, 1914, merely as an example of the course of dealing between the respondent and Thomas Brothers, Limited. I must say, however, that there is nother difficulty in the way of the respondent. Thee petition putting Thomas Brothers into liquidation was filed on the 28th of March, 1914. Subsequently to that date, the bank advanced to Thomas Brothers, Limited, the sum of $17,600, and took security therefor. The winding-up order bears the date of 1st May, 1914. I have duly considered the supplemental factums filed by the parties with regard to these advances and I fully concur in the opinion of His Lordship the Chief Justice as to the declaration that should be made in the judgment.

I think that the appeal should be allowed with respect to the hypothec taken by the bank on the Montreal property on the 22nd January, 1914. I have no doubt that at the date of this mortgage Thomas Brothers, Limited, were insolvent. I am also of the opinion that this state of insolvency was known to the bank, for the latter then controlled the business of Thomas Brothers, Limited, and had received a report on their financial position up to August, 1913, shewing

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a considerable deficit on their operations during the preceding year. This question of the validity of the Montreal hypothec must be determined under the provisions of the Civil Code of the Province of Quebec. Reading article 2023 C. C. with articles 1032 *et seq.*, I think that where a creditor has knowledge of the insolvency of his debtor, whether this state of insolvency be notorious or not, he cannot take a valid hypothec on the property of his debtor.

On the whole, therefore, I think the appeal should be allowed to the extent stated in the opinion of His Lordship the Chief Justice.

Appeal allowed in part with costs.

Solicitor for the appellant: *John B. Davidson.*
Solicitors for the respondent: *Osler, Hoskin & Harcourt.*