Judgment of the Lords of the Judicial Committee of the Privy Council on the Appeal of Préfontaine v. *Grenier, from the Court of King's Bench for the Province of Quebec (Appeal Side); delivered the 2nd November* 1906.

Present at the Hearing:

LORD MACNAGHTEN.
LORD DUNEDIN.
LORD ATKINSON.
SIR ARTHUR WILSON.
SIR HENRI ELZÉAR TASCHEREAU.
SIR ALFRED WILLS.

[*Delivered by Sir Arthur Wilson.*]

The controversy between the parties to this Appeal arises out of the collapse of the Banque du Peuple, a bank that carried on business in Montreal and elsewhere in the Province of Quebec, which collapse occurred on the 16th July 1895, when the Bank closed its doors.

The Bank was constituted in 1843 by an Act of the then Canadian Legislature (7 Vict., c. 66). That Act laid down the constitution of the Bank on lines which can be briefly stated. Certain specified persons and their successors were created a Corporation, were to have the management of the affairs of the Bank, and were to be individually, jointly and severally, liable for all the debts contracted by the Corporation. With them also lay the appointment of officers, clerks, and servants. The members of the Corporation have throughout the case also been called "directors." There was to be another class of persons interested in the Bank (commanditaires) who were to be subject to no liability beyond

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the amount of the stock for which they subscribed. The profits were divisible among the shareholders, of both classes alike, according to the amounts of stock held by them.

The third section made it clear that the management of the Bank lay with the members of the Corporation, or so many of them as might be chosen for the purpose by a majority of the body. The same body was to keep regular books of accounts, to be balanced half-yearly. And by Section 17—

"The said books of account which it shall be the duty of "the said Corporation to keep, as aforesaid, and the statement "and inventory which it shall be the duty of the said Cor- "poration to prepare semi-annually as aforesaid, and all "vouchers connected therewith, and generally all the deeds, "books and papers of the said Corporation shall, during the "last fifteen days of the months of February and August, in "each and every year, but at no other period, be open to the "examination of a Board of Audit, to be elected as hereinafter "provided; the said deeds, books and papers shall not, "however, be removed from the office of the said Bank."

By Section 18—

"On the first Monday of March in every year during the "continuance of this Act, a general meeting of all the stock- "holders of the said Corporation, including as well the members "of the said Corporation as each of the said partners *in* "*commendam* (*commanditaires*) shall be held at the office in "Montreal of the said Corporation, of which general meeting "one month's notice shall be given in two or more of the "newspapers published in the said City of Montreal in the "English and French languages; and at the said meeting a "full and clear statement of the affairs of the said Corporation "shall be submitted, containing on the one part the amount "of capital stock paid in, the amount of notes of the Bank in "circulation, the net profits in hand, the balances due to other "banks and institutions, and the cash deposited in the Bank, "distinguishing deposits bearing interest from those not "bearing interest, and, on the other part, the amount of "current coins and gold and silver bullion in the vaults of "the Bank, the value of buildings and other real estate "belonging to the Bank, the balances due to the Bank from "other banks and institutions, and the amount of debts owing "to the Bank, including and particularising the amounts so "owing on bills of exchange, discounted notes, mortgages and "hypothecs, and other securities; thus exhibiting, on the "one hand, the liabilities of, or debts due by, the Bank, and, "on the other hand, the assets and resources thereof; and the

" said statement shall also exhibit the rate and amount of the " then last dividend declared, the amount of profits reserved " at the time of declaring such dividend, and the amount of " debts to the Bank over-due and not paid, with an estimate " of the loss which may probably be incurred from the " non-payment of such debts."

Section 19—

" At the annual general meeting so to take place on the first " Monday of March, all the said partners *in commendam* " (*commanditaires*) of the said Corporation then present, shall " by vote elect from among themselves three persons to be a " Board of Audit; and it shall be the duty of the said Board " of Audit so elected to look into all the operations of the said Corporation, and to examine the books of account, papers " and vouchers of the said Corporation, which books, papers " and vouchers shall be accessible to the said Board of Audit " as provided for in the seventeenth section of this Act; " and it shall be the duty of the said Board of Audit to make " their report thereon at the next general meeting of the said " Corporation to be held on the first Monday of March as " aforesaid; and each partner *in commendam* (*comman-* " *ditaire*) shall have one vote and no more, and if there be an " equal division as to the appointment of any person to be a " member of the said Board of Audit, the partner *in com-* " *mendam* (*commanditaire*) then present, having the largest " quantity of stock in the said Corporation, shall have a " casting vote; and it shall be lawful for any absent partner " *in commendam* (*commanditaire*) to give their, his or her " vote respecting the nomination of the said Board of Audit " by proxy, such proxy being also a partner *in commendam* " (*commanditaire*) and being provided with a written authority " from his constituent or constituents, and which authority " shall be lodged in the Bank."

Section 22 empowered the majority of the Corporation, if of opinion that it should be necessary to require one or more of its members to devote an exceptional amount of time to the affairs of the Bank, to compensate such member or members by salary or otherwise.

The Respondent Grenier was President of the Bank. At first he received a remuneration of $1,000, as had his predecessor in office. In March 1887 his remuneration was raised to $2,000, under a resolution, in the following terms:—

Les affaires de routine étant terminées sur la suggestion de M. Brush, vice-président, il est résolu à l'unanimité que la somme de $1,000 soit placée au crédit de M. Jacques Grenier,

en reconnaissance de son zèle, de son assiduité et de ses services comme président de la Banque du Peuple pour l'année se terminant le 1er mars 1887. Cette somme de $1,000 n'affecte en rien l'allocation ordinaire qui comme d'habitude est portée au crédit du président, tous les six mois.

On the 6th May 1889 Grenier was re-elected as President under a resolution which runs as follows:—

" En conformité de l'article cinq de l'acte d'Incorporation, " l'assemblée de ce jour a pour objet d'élire le Président et le " Vice-Président de la Corporation de la Banque du Peuple " pour l'année courante.

" L'ordre de l'assemblée est adoptée sur proposition de " MM. G. S. Brush, Ecr., secondé par A. Leclaire, Ecr., il " fut résolu que J. Grenier, Ecr., soit réélu président de " cette Banque pour l'exercice se terminant le premier lundi " de mai 1890.

" M. Grenier à la condition toute spéciale qu'aucun docu- " ment ou transaction faite au nom de la Banque soient bien " et dûment par le caissier soumis à lui-même pour être " approuvés, signés ou endossés et ce dans le but de partager " en toutes occasions avec le caissier la responsabilité des " engagements de la Banque lesquels devront aussi être " soumis à la direction pour approbation."

Prior to May 1894, Préfontaine, the Appellant, was one of the commanditaires of the Bank, with a holding of 31 shares. He then purchased a further number of 69 shares, and at about the same time he was elected by the directors or members of the Corporation to be one of their number. By accepting that position he, of course, became subject to the special liabilities imposed by the Act upon the members of the body which he thus joined.

From that time down to shortly before the 16th July 1895, when the doors were closed, the Bank went on in apparent prosperity. As to the cause of the collapse that then occurred there is no doubt. It was due entirely to the fact that the cashier of the Bank, without the sanction or knowledge of the Respondent Grenier, or his co-directors, and in disobedience to their general instructions, had allowed large overdrafts, partly in current account and partly in other forms,

to certain favoured customers, overdrafts which amounted in all to a large sum.

Préfontaine instituted the present suit against Grenier on the 24th November 1900. In his declaration, which was further explained by particulars delivered under an order of the Court, he complained that the Defendant, as President of the Bank, had made false representations both to the shareholders generally, and to Préfontaine himself in particular, by means of which the latter had been induced to purchase the additional shares which he did purchase, and had also been induced to become a director or member of the Corporation, in consequence of which he incurred the special liabilities attaching to one of that body. He complained, secondly, that the Defendant had been guilty of negligence in the conduct of the affairs of the Bank, and failed in the duty which lay upon him as President under the circumstances of the case, and had so brought about the failure of the Bank and the losses sustained by the Plaintiff. He claimed as damages $8,625 which he had paid for his shares, and $45,914.89, the amount which he ultimately had to pay, as the result of the liquidation, in respect of his liability as a director or member of the Corporation.

Thus from the early stages of the case the Plaintiff has been suing upon two alleged causes of action, misrepresentation and negligence. These causes of action have not always been kept apart in argument; but they are perfectly distinct, and governed by different legal principles.

The case was tried before Robidoux, J., who decided in favour of the Plaintiff, so far as concerned the amount which he had been obliged to pay in respect of his liability as Director or

Member of the Corporation, while he dismissed the claim so far as it concerned the price of the shares.

The Defendant brought the case by way of review before three Judges, who agreed with Robidoux, J., on the merits of the case, but by a majority decided that the action was barred by prescription.

From that decision there was a further appeal to the Court of King's Bench, and that Court considered it unnecessary to deal with the question of prescription, because it considered that the Plaintiff's case failed irrespective of that question. Against that Judgment the present Appeal has been brought.

The case of the Plaintiff Appellant, so far as it rested upon misrepresentation, was based, in the argument before their Lordships, upon the report issued for the year 1893, dated the 1st March 1894, with the statements of accounts annexed to that report, read in connection with the like reports and statements relating to previous years.

The alleged misrepresentations thus relied upon were three in number. First, the report said, "All our agencies have been thoroughly "inspected during the year." In fact the agencies outside Montreal had been inspected, but certain branches, or agencies, within that city had not been so inspected. It is unnecessary to enquire whether, on the proper construction of the report, the words in question referred to all the agencies or branches, including those within the City of Montreal, or only to those outside the city, because it was no part of the Plaintiff's case that he was misled into purchasing shares or becoming a Director by any such misrepresentation as that now contended for. In his declaration, supplemented by his

particulars, the Plaintiff defined his case in all points; and he nowhere said that he was induced to act by any such misrepresentation as this. He did in his particulars put forward want of inspection of the head office as an instance of negligence, or default, on the part of the Defendant, but that is a totally different matter, and belongs to a different part of the case.

It was next said that the report and the account annexed to it untruly represented that the Bank possessed a reserve fund of $600,000. But in the opinion of their Lordships the account, which is the more important document of the two, and which was the basis of the report, makes no such representation. That account is of the nature of a balance sheet. It enters the amount of the reserve fund as an item under the head of liabilities, as it was proper to do; but when one turns to the other side of the account, under the heading "Assets," there is nothing to suggest that the Bank held any investment of corresponding amount which could be thought to represent the reserve fund. There was nothing which could properly be understood as conveying that that fund was more than an estimated amount, or was anything separately held or separately invested.

Then it was said that there was a misrepresentation in another respect. The amounts of the overdrafts, improperly allowed by the cashier to certain customers, were included in the amounts which appeared in the account as assets, and there was no complaint that the aggregate on this side of the account was not correct. But the suggestion was that the sums in question ought to have been included in the item "Notes and bills overdue, unsecured" whereas in fact they were included in "Loans and discounts current." It appears to their Lordships that the sums in question were at least

as correctly treated, in the account, in the manner in which they were treated, as they would have been if entered in the manner in which it is said that they ought to have been. Their Lordships therefore agree with the Court of King's Bench that the Plaintiff's case based upon misrepresentation fails on the facts, and it is unnecessary to consider any of the questions of law which might otherwise have arisen.

The second branch of the Plaintiff's case is based on alleged negligence on the part of the Defendant in the discharge of his functions as President of the Bank. It has been already stated that the collapse of the Bank was due to overdrafts, which the cashier had irregularly and improperly allowed to certain customers. The main ground upon which the Defendant was charged with negligence was, that he had not exercised such a control over the details of the Bank's business as to enable him to detect and put a stop to the irregular practices of the cashier.

Before examining the question of his liability, it may be well to notice that the cashier was the principal executive officer of the Bank under the Directors. There is nothing to show that either the Defendant or his brother Directors had any reason to suspect or distrust that officer. The accounts periodically submitted to the Directors were prepared by him, or under his directions. They were duly audited by the Board of Auditors appointed under Section 19 of the Act by the body of commanditaires, such auditors being thus entirely independent of the Directors. In those accounts the total assets and liabilities of the Bank were correctly stated according to the books, but the accounts were so framed as not to disclose the fact that the totals included unauthorized overdrafts. The contention on the part of the Plaintiff was that it

was the duty of the Defendant to have exercised such control as to have detected the overdrafts which were, in fact, concealed from him and from his co-directors.

The alleged duty of the Defendant was based, *first*, upon the fact that he was the President of the Bank, and *secondly*, that he received a salary for acting in that capacity. Reliance was further placed upon the resolution already cited of the 6th May 1889.

In this country questions as to the nature and extent of the duty and responsibility of directors and others, in respect of the conduct of the affairs of companies, have been frequently under consideration. Attempts have repeatedly been made to render them personally liable, on the ground that they have trusted the regularly authorized officers of the Company; that they have failed to detect, and been misled by, misrepresentation or concealment by such officers, when there was no reason for doubting their fidelity. But such attempts have not been successful. It is sufficient to refer to the case of *Dovey* v. *Cory*, 1901, A.C. 477, in which the subject was fully considered by the House of Lords.

Their Lordships think that in the absence of any legislation in force in Quebec inconsistent with the law as acted upon in England, and in the absence of any evidence of custom and course of business to the contrary, the Court of King's Bench was right in accepting the English rulings, because they were based, not upon any special rule of English law, nor upon any circumstances of a local character, but upon the broadest considerations of the nature of the position and the exigencies of business.

The fact that the Defendant was remunerated for his services as President does not seem to their Lordships to strengthen the case against

him. Indeed, the modest scale of his remuneration is scarcely consistent with the idea that he, a man of considerable position, and with a business of his own, was ever expected to give his time and labour to the detailed control of the work of the Bank. It is much more consistent with the idea that he was expected to do what he did, that is to say, to devote some two hours a day to the business of the Bank, two hours largely taken up by official interviews.

The resolution of the 6th May 1889 is very hard to follow, and no one has succeeded in construing it clearly, but it seems to their Lordships certainly not to strengthen the case of the Plaintiff. So far as anything can be collected from it, it seems to show that the obligation of the Defendant to share responsibility with the cashier was limited to the "engagements of the Bank," whatever those words may mean; and, further, that the Directors were also to be bound to approve each transaction falling within that class. The grounds, therefore, put forward by the Plaintiff as supporting the general allegation of the Defendant's liability, appear to their Lordships insufficient to do so. And, further, the Court of King's Bench was, in their Lordships' opinion, right in laying stress upon the fact that the accounts laid before the Defendant and his co-directors, in which it is said that the Defendant ought to have detected what was concealed, had been audited by a wholly independent body of auditors, and certified by them as correct, and there is nothing shown which should have led the Defendant to doubt the sufficiency of the audit.

A special charge of negligence was pressed against the Defendant in the argument of the Appeal, based upon the evidence of a M. Gagnon, who held the post of inspector under the Bank. There is nothing in the

evidence to show the terms of his appointment, and no formal definition of the extent of his duties. The Defendant said in his evidence that Gagnon's duties were limited to the inspection of branches and agencies outside the City of Montreal. On one occasion Gagnon was specially employed to examine into a matter in the head office. He says he was dissatisfied with what he found, and that he pressed upon the Defendant that he, Gagnon, should be empowered to make a completer inspection. He says that his suggestion was not very well received, that the Defendant rejected the idea that the inspector should be put to supervise the work of the head official of the Bank.

It was contended that the omission to authorize the suggested inspection was an act of negligence on the part of the Defendant, and that if the suggested inspection had been carried out the overdrafts which led to the fall of the Bank, would, or might have been, brought to light. Their Lordships are not prepared to say that there was negligence in omitting to sanction an inspection inconsistent with the ordinary method of conducting the affairs of the Bank, nor has it been shown that there was any direct connection between the matters excepted to by Gagnon and the fatal overdrafts.

Their Lordships agree with the Court of King's Bench that the charge of negligence has not been established in fact. It is therefore unnecessary to consider (what might have been a difficult question of law) whether the obligation of the Defendant,. which, whatever its nature and extent, was primarily a contractual obligation, could be made the ground of an action by an individual member of the Corporation, as distinguished from the Bank in its entirety, and from the smaller body, the directors or members of the Corporation.

Their Lordships will humbly advise His Majesty that the Appeal should be dismissed. The Appellant will pay the costs.