Privy Council Appeal No. 9 of 1923.

Frank K. Brown - - - - - - - - *Appellant*

v.

Phil H. Moore - - - - - - - - *Respondent*

FROM

THE SUPREME COURT OF NOVA SCOTIA (EN BANC).

JUDGMENT OF THE LORDS OF JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 10TH MARCH, 1924.

Present at the Hearing:

THE LORD PRESIDENT.
LORD ATKINSON.
LORD SHAW.
LORD WRENBURY.
LORD DARLING.

[*Delivered by* LORD ATKINSON.]

This is an appeal from an order of the Supreme Court of Nova Scotia (en banc) dated the 4th May, 1922, dismissing an appeal by the appellant from the order of Mr. Justice Mellish, dated the 5th January, 1922, ordering *inter alia* that the report of Harvey C. Crowell, a referee to whom certain matters had been referred for enquiry and report by order of Mr. Justice Mellish, dated the 20th November, 1920, be confirmed and decreeing the rights of the parties on the basis of the findings contained in the said report. On the 8th July, 1922, final leave to appeal to His Majesty in Council was granted to the appellant by the Supreme Court.

On the 2nd October, 1916, the respondent obtained from the Nova Scotia Wood Pulp and Paper Company, Limited, hereinafter for convenience called the Nova Scotia Company, a lease of certain mills, lands and water rights belonging to the Company for a term of three years from the 1st October, 1916, at the rent of $2,000 per annum. This lease gave to the lessee the option of, at any time within the aforesaid term, purchasing all the premises demised for a sum of $30,000, with a proviso that all money paid on account of the yearly rentals of $2,000 should be credited on the purchase price. The respondent was by profession an engineer, but, apparently,

was not possessed of the capital necessary to carry on the business of manufacturing pulp in the demised mills. The appellant, however, fortunately for the joint adventure in which he and the respondent became engaged, was possessed of the necessary capital. Under these circumstances the respondent by an agreement of equal date with the lease, assigned the lease and all his rights thereunder, including the privilege and benefits of the aforesaid option, to the appellant. This agreement contained several important provisions affecting the rights of the respective parties to it--

(1) by it the respondent undertook to serve the appellant as the resident manager of any business the latter might carry on from time to time in the aforesaid pulp mills;

(2) the respondent was to receive as remuneration for his services 25 per cent. of the net earnings of such business, which 25 per cent. was to remain invested in the capital account of the business for the purpose of the purchase of the demised property, on the exercise of the option given by the lease;

(3) that on account of the profits the appellant would advance to the respondent the sum of $200 per month during the term of three years from the date of the agreement, or until the purchase of the demised property or until the discontinuance of the business;

(4) that these money payments should be deducted from the share of profits appropriated to the respondent;

(5) that if the appellant should out of the net earnings of the said business purchase the said premises at any time, the respondent was to become the owner of 25 per cent. thereof and the appellant was to assign and transfer to the respondent 25 per cent. or one-quarter interest therein, and further that if the appellant should purchase the aforesaid premises before such net earnings were sufficient for that purpose the respondent was to have the option of drawing from the capital account his portion of the net profits, or of purchasing a one-fourth of the interest in the demised premises with his share of those profits, supplemented by any other money he might have available, the purchase price of the entirety of these premises being taken at $30,000. It is to be observed that as the purchase price of the demised premises was thus fixed at $30,000, the more they were enhanced in value by effecting improvements on them, the more would both the appellant and respondent be, *prima facie*, benefited.

The respondent acted as manager of the business carried on in the demised premises till the end of September, 1919. The appellant carried on the business in the mills under the name of the Medway Pulp and Power Company (a mere alias for himself). On the 26th August, 1919, the appellant wrote to Mr. R. F. Davison (an attesting witness of the lease of 2nd October, 1916) a letter in which he stated that he expected at the proper time to exercise the option reserved to him to purchase the property. On the 10th September following the respondent wrote to the appellant a clear, distinct and straightforward letter asking him on

what date he intended to take over the Pulp Company's property, setting forth that he, the writer, had under his contract the privilege of purchasing one quarter interest in the real estate and plant of that Company for one quarter of the purchase price of $30,000, and further stating that this, his letter, was in the nature of a notice that he intended to do this and that he desired to know when and where the transaction might take place.

That letter, it would appear to their Lordships, called for and deserved from the appellant a straightforward and candid reply. No such reply to it was ever received. On the contrary, after the lapse of a period of eight days during which time the appellant was, as will presently appear, engaged in maturing a scheme to circumvent the respondent and to deprive him of his rights, he wrote to the latter a letter, dated the 18th September, 1919, not containing any answer to the questions the respondent had put to him relative to the exercise of the option to purchase, but bluntly dismissing him from his position of manager, giving him notice that all business relations between them should terminate, and containing the following passage :—

> "I have made arrangements to dispose of the business and will proceed at once to wind up the affairs of the Medway Pulp and Power Company, and I wish to advise you that future business of this operation will be carried on by the Nova-Scotia Wood Pulp and Paper Company who are now the owners of this property."

This paragraph contained a false statement. The appellant had never disposed of, or arranged to dispose of the business he had carried on in these mills as lessee of the Nova Scotia Company. On the contrary, what the appellant had endeavoured to do was to convert himself, in effect, into the Nova Scotia Company by purchasing and having assigned to him practically all the shares of that company. The scheme he adopted was this: All the shares or almost all the shares in this company were held by Reginald Davison above mentioned and his two sisters. On the 15th September, when 15 days still remained in which the option to purchase might be exercised, the appellant entered into an agreement, set forth in the fifth paragraph of the amended statement of claim, with Alma Davison, Louise Davison and Reginald Davison, whereby these latter parties agreed to assign to the appellant 750 shares in the Nova Scotia Company, the numbers of which were given, the vendors undertaking to procure the assignment to the appellant of certain other shares in the said Company held by three other shareholders therein named, and the vendors agreed that there were no other shares and that if there were any further shares, they would procure the assignment to him of any further shares of the Company which should be issued and outstanding in consideration of a sum of $24,000 which the appellant agreed to pay. This sum of $24,000 is arrived at by deducting from the sum of $30,000 (the price fixed in the agreement of 2nd October, 1916, for the demised premises)

the sum of $6,000, being the three years of the yearly rent of $2,000 reserved by the lease of the 2nd October, 1916, which were by the agreement of the 2nd October, 1916, to be credited on the purchase price. The identity of these figures with the figures in the agreement of the 2nd October, 1916, shows that the purchase of the shares was based upon the provisions of the lease of the 2nd October, 1916, dealing with the option to purchase the demised premises. For, as before stated, that document provided that if the lessee should exercise his option to purchase the price should be $30,000, with the proviso that all moneys paid on account of the yearly rentals of $2,000 should be credited against this purchase price. In fact this dealing was by every judge before whom the case has come held to be, in effect, though not in apparent form, an exercise of the option to purchase given by the lease of the 2nd October, 1916, camouflaged as a purchase of the shares of the Nova Scotia Company. If it had been an honest transaction no reason can be suggested why it should from first to last have been carried out in secret as it was. In their Lordships' view it was not an honest transaction. It may have been too strong to style it "larcenous" as Mr. Justice Rogers did, but it certainly was not too strong to style it tortious and *mala fide*. On the 23rd September the respondent, while a week remained in which the option to purchase might have been exercised, wrote to the appellant a letter which ran as follows :—

> "Under the written agreement between yourself and the undersigned dated 2nd October, 1916, to which reference is hereby made for full particulars thereof, the undersigned is entitled, in certain events therein specified :—
>
> "(A) To have assigned and transferred to him by you 25 per cent. or one-quarter interest in the premises described in the lease, dated 2nd October, 1916, made between Nova Scotia Wood Pulp and Paper Company, Limited, as lessor and the undersigned as lessee by good and sufficient deeds thereof, etc.
>
> "(B) To have the option of purchasing, etc., an interest in said property not to exceed 25 per cent. thereof at the same valuation as you would pay to said Nova Scotia Wood Pulp and Paper Company, Limited, for the purchase of said property, namely, $30,000.
>
> "And whereas you have purchased the property pursuant to said agreement, the undersigned hereby tenders to you the sum of $7,500, lawful money of Canada, and hereby demands the assignment and transfer to him of 25 per cent. of, or a one-quarter interest in the premises and property described in said lease above mentioned, the undersigned reserving all his rights to an accounting under said agreement as to profits and to reimbursement out of the profits."

The respondent Moore on the 8th December, 1919, instituted an action against the appellant. In the statement of claim are set out the relevant provisions of the two deeds of the 2nd October, 1916, as well as of the letter of the 23rd September, 1919, and a tender to the appellant of the sum of $7,500 being a quarter of the sum of $30,000 mentioned in the said deeds, is averred. The relief claimed was (1) payment of a sum of $5,100 for work and labour done by the respondent for the appellant.

(2) A declaration that the respondent was entitled to have assigned and transferred to him by the appellant by a good and sufficient deed 25 per cent. or one-quarter interest in the premises described in the aforesaid lease, or in the alternative a declaration that the respondent was entitled to the option of purchasing an interest in the said property up to 25 per cent. thereof at the same valuation as the appellant paid to the Nova Scotia Company, namely, $30,000.

(3) An account of the sums due to the respondent in connection with the business of the Medway Pulp and Power Company.

(4) Further and other relief.

The appellant filed his defence on the 5th February, 1920, admitting the statements contained in the first three paragraphs of the statement of claim, denying that he had exercised the option to purchase the demised premises mentioned in the agreement of the 2nd October, 1916, or that he had ever in fact purchased those premises for the sum of $30,000, or at all. The remainder of his defences consist practically of mere traverses of all the material averments in the respondent's statement of claim. In addition the appellant counterclaimed to recover from the respondent a sum of $5,052.78 alleged to have been paid by him to the respondent in excess of the 25 per cent. to which the latter was by the above-mentioned agreement entitled. The respondent filed a reply traversing all the material averments in the appellant's defence, and as to his counterclaim denying that he received the sums therein mentioned or any other sum in excess of what he was entitled to as resident manager of the aforesaid business in which they were jointly interested, that the appellant's account, showing the profits of the said business was inaccurate, and that on a true account of them large sums would be found to be due to him by the appellant.

The trial of the various issues raised by these pleadings came on before Mr. Justice Mellish on the 30th July, 1920. A considerable body of evidence was given. The learned judge delivered judgment on the 8th November, 1920, holding that the agreement thereafter dealt with, entered into between the appellant and the Davisons to purchase, practically the whole stock of the Nova Scotia Company, was designed to get in effect the whole property of this company into the appellant's hands; that the stock was acquired by him for the sum mentioned in the agreement of the 2nd October, 1916, namely, $30,000, less a deduction of $6,000, three years' rent of the demised premises, which by the terms of that agreement were, if the option given to purchase was exercised, to be deducted; that as between the appellant and the respondent the purchase made by the former must be held to be referable to the third or fourth clauses of this latter agreement; and that the former should be held to have purchased the property by virtue of the provision relative thereto contained in this agreement of the 2nd October, 1916. The learned judge also found that on the 23rd September, 1919, the respondent had tendered to the appellant the $7,500,

one-fourth of the purchase price mentioned in the last-mentioned agreement, which was refused ; that the respondent was entitled to judgment with the costs of the action, and that an account should be taken of the profits of the business from the date of the aforesaid agreement of the 2nd October, 1916. A formal order, dated the 20th November, 1920, was drawn up based upon and carrying out this judgment, and, amongst other things, directing that full accounts and enquiries should be taken and made before a named referee including—

"(A) An inquiry as to all the businesses which defendant engaged in under the name of the Medway Pulp and Power Company in connection with the premises described in the lease set out in paragraph 1 of the Statement of Claim, and referred to in the Agreement set out in paragraph 2 of the Statement of Claim, covering the period from 1st October, 1916, to 1st October, 1919.

"(B) An account of the net earnings of any and all business so carried on by Defendant under the name of the Medway Pulp and Power Company in connection with said premises.

"(C) An inquiry as to what use has been made of said premises since 1st October, 1918, to date of Report of Referee.

"(D) An account of the net earnings of any or all businesses carried on in connection with said premises, covering the period from the 1st day of October, 1919, to date of Report of Referee ;

"(E) An account of Defendant's dealing with the Zinc lot, so called.

"and that said Referee should make his report and file same with the Prothonotary of this Honourable Court at Halifax, N.S., on or before 31st December, 1920, unless the said time is extended by further order."

And in conformity with the oral judgment delivered by the learned judge on the 8th November, 1920, the order decided—

"7. That Defendant, before the 1st day of October, 1919, exercised the option for purchase of the premises described in the lease set out in paragraph 1 of the Statement of Claim and referred to in the Agreement set out in paragraph 2 of the Statement of Claim, and that Plaintiff did, on the 30th day of September, 1919, and after said option for purchase had been so exercised by Defendant, tender to defendant the sum of $7,500 and did demand from defendant a transfer and assignment of a one-quarter interest in said premises under the terms of the Agreement in paragraph 2 of the Statement of Claim set out, and that plaintiff was entitled to have defendant assign and transfer or cause to be assigned and transferred to plaintiff a one-quarter interest in said premises by good and sufficient deeds thereof, to be dated the 1st day of October, A.D. 1919, conveying all title thereto which was vested in the Nova Scotia Wood Pulp and Paper Company, Limited, on the 2nd day of October, 1916, free from any and all encumbrances since said 2nd day of October, 1916 ; upon plaintiff tendering to defendant the difference between the sum of $7,500 and one quarter of the net earnings (if said net earnings do not exceed an amount which, after deducting $7,390.93, will aggregate the sum of $7,500) of the Medway Pulp and Power Company, covering the period from 1st October, 1916, to 1st of October, 1919, when finally ascertained and determined by the Court.

"8. That the further consideration of this action and of the costs not hereinbefore otherwise provided for or disposed of be adjourned and that the parties are to be at liberty to apply generally as they may be advised."

The referee made his report, a very voluminous one, in the month of February, 1921. He found, amongst other things, that

the net profits made by the Medway Pulp Company during the three years ending on the 30th September, 1919, amounted to $40,669.18. The particulars upon which this finding appears to be based are thus set out at p. 93 of the record—

"Amended statement of net profits of the Medway Pulp and Power Company for the three-year period ending 30th September, 1919.

	$
Amount as shown on statement "E.4" submitted by defendant	9,352.59
Plus the following items which I do not consider are chargeable as expenses of the period :—	
Mill, Flume, Dam and Property Repairs	18,120.45
Fish Hole, Gateway and Log Roll	108.93
Mill Supplies	816.93
Government Share Fishway	*208.90*
Income Tax	2,998.27
Interest, F. K. Brown	1,321.49
Interest, Bank	1,906.44
Commissions Penn Lumber Company	3,431.87
10 per cent. allowance on purchases from the Union Supply Company and Nova Scotia Motor Sales Company ...	2,395.41
F. K. Brown, personal account, Paid Paton and Robertson ...	7.90
Net Profits to be apportioned between the parties entitled to same	$40,669.18"

To one-fourth of these profits, $10,167.29, the respondent would, under the terms of his agreement of the 2nd October, 1916, fairly become entitled. This report came, on the 20th May, 1921, before Mr. Justice Mellish, who then confirmed it. He began his judgment with these words: "The referee's report should be confirmed, but I have difficulty in determining what amount should be awarded to the plaintiff (*i.e.*, the present respondent) for the defendant (*i.e.*, the present appellant), using the property for the year ending the 30th September, 1920. The defendant contends that nothing should be allowed as it was property owned in common which either of the owners could use without accounting to the other. In this case, however, the property was used by the defendant to the exclusion of the plaintiff, who was ousted by the defendant from it. Under these circumstances, I think the latter is entitled to damages. Those damages are not to be measured by the profits made by the defendant in using the property, nor by the rental. The parties were not partners but should be treated as co-owners. The damages to which the plaintiff is entitled resembled mesne profits." He then formally fixed the damages to which the respondent was entitled by reason of his being deprived of the enjoyment of this property to which he was entitled under the agreement of 2nd October, 1916, at $15,000.

The further consideration of the action had by the order dated the 20th November, 1920, been adjourned, with liberty to the parties to apply as they might be advised, and then on the 5th January, 1922, a proceeding was adopted most unusual in actions such as this, and as embarrassing as could well be conceived. Counsel, on behalf of the respondent, in

exercise of the liberty so reserved applied to the Court that, as it appeared that the appellant had all the shares of the Nova Scotia Company that company should be made a party defendant in the action in order that the Court might be enabled to adjudicate upon, and settle all questions involved in the cause and that the plaintiff (*i.e.*, the respondent) might have the relief to which he was entitled. The order made upon this application is rather peculiar. It directs that unless the Nova Scotia Company should within 10 days, from the date of the order deliver to the plaintiff a deed conveying to him one-fourth of the property demised by the lease of the 2nd October, 1916, that company should be added as a party defendant in the pending action. It then proceeds to confirm, for the second time, the findings of the Referee on the four contested questions, namely: the net earnings of the Medway Pulp Company for the three years ending the 30th September, 1919, $40,699; the net earnings of the Nova Scotia Company in the business carried on in the demised premises from 1st October, 1919, to 30th September, 1920, $90,387: it further rules that the respondent should recover from the appellant the sum of $15,000 damages in respect of the former's expulsion from the demised premises from the 1st October, 1919, to the 30th September, 1920, and, lastly, that the counterclaim of the appellant do stand dismissed. But this order does not contain any provision whatever to the effect that all further proceedings in the only action then pending, namely, that between the appellant and respondent should be stayed pending the trial of the issues which the Nova Scotia Company might raise after it had been added as a defendant, nor any provision to the effect that the rights which the present respondent had been already declared to be entitled to should not be affected, nor any provision suggesting that the Nova Scotia Company was disqualified by any statute from making the lease of the 2nd October, 1916. It does provide no doubt that further consideration was reserved.

The appellant did not deliver to the respondent any deed of conveyance in pursuance of this order; but within nine days after its date served notice of appeal from the decision of Mr. Justice Mellish of the 20th May, 1921, and from the order made by him on the 5th January, 1922, and stated that a motion would be made to the Supreme Court *en banc* to set aside both of these decisions and to order that the same might be reversed or varied in respect (1) of the sum of $40,699.18 fixed as the net earnings of the Company in the three years from the 1st October, 1916, to the 1st October, 1919; (2) in so far as the amounts expended during this period in repairs or improvements of the demised premises were not deducted from the gross earnings or receipts; (3) in so far as the plaintiff (*i.e.*, the respondent) was allowed $10,167.29 as his share of the net earnings, and in so far as the two decisions awarded the plaintiff $15,000 for being deprived for twelve months of the use and occupation of the demised premises, and in so far as it dismisses the plaintiff's counterclaim.

Then, on the 28th February, 1922, about six weeks after this notice of appeal had been served, an amended statement of claim, in which the Nova Scotia Company is a defendant, was delivered by the plaintiff (*i.e.*, the respondent) setting out the agreement made between the appellant and the Davisons for the purchase of the shares of the defendant Company, and claiming a declaration that the plaintiff was entitled to have assigned to him by the defendant 25 per cent. or one-quarter's interest in the demised premises by good and sufficient deeds, or in the alternative a declaration that the plaintiff was entitled to the option of purchasing an interest in the said property up to 25 per cent. thereof at the same valuation as the defendant Brown paid to the Nova Scotia Company, and for an account and further relief. On the 24th April, 1922, a defence to this amended statement of claim was filed by the Nova Scotia Company, alleging for the first time, amongst other things, that this company was incorporated by charter under Chapter 71 of the Nova Scotia Acts of the year 1881, that this statute deprived the Company of all power or authority to sell or dispose of its real estate ; that the lease of the 2nd October, 1916, covered and was intended to cover all the property of the Company ; that the Company had no power to make such a lease or to give the option for the purchase of the demised property therein contained, and that the granting of the lease was *ultra vires* of the Company, and the lease was accordingly void. The issues thus raised have never been tried. Their Lordships have no power to determine them on the hearing of this appeal. They therefore abstain from expressing any opinion upon them. It may well be that if this defence of the Company should be sustained the respondent might still be entitled to recover damages, in lieu of the decree for specific performance, on the failure of the appellant to make title to the premises purporting to have been demised by the lease of the 2nd October, 1916, or even entitled to damages on a different ground, namely, for breach by the appellant of his contract contained in the agreement of the 2nd October, 1916, that he had power, express or implied, to purchase the fee simple of the demised premises and to assign to the respondent one-quarter interest therein on the terms mentioned ; but of course it is obvious that the respondent could not be entitled to recover damages on each of these two inconsistent grounds, and care should be taken by any Court dealing ultimately with the defence of the Company to guard against this result. It is clear, however, in their Lordships' view, that as the questions raised by the defence of the Nova Scotia Company have never been decided, they must deal with this appeal as if that Company had never been made a defendant in the respondent's action. The confusion in the proceedings renders any other course impossible, unsatisfactory though that course may be. On the hearing of the appeal before the Supreme Court of Nova Scotia all the four learned judges who sat upheld the judgment delivered by Mr. Justice Mellish on the 20th November, 1920, to the effect that the appellant before the 1st October, 1919, exercised the option to purchase the demised

premises given by the lease of the 2nd October, 1916, that after this option had been exercised the respondent tendered the sum of $7,500 to the appellant and demanded a transfer to him of one-quarter's interest in the demised premises, and that the respondent was entitled to have the defendant assign and transfer to or cause to be assigned a one-quarter's interest in the demised premises by good and sufficient deeds to be dated the 1st October, 1919, conveying all the title thereto which was vested in the Nova Scotia Wood Pulp and Paper Company on the 2nd October, 1916, free from any and all encumbrances since that date upon the respondent tendering to the appellant the difference between the sum of $7,500 and one-quarter of the net earnings (if said net earnings do not exceed the amount which after deducting $7,390.93 will aggregate the sum of $7,500) of the Medway Pulp and Power Company covering the period from the 1st October, 1916, to 1st October, 1919, when finally ascertained and determined.

It appears to their Lordships that what really was done was this: the appellant omitted to draw out of the business the portion of the net profits to which he would be entitled, and the respondent on his part omitted to draw out and appropriate his share of them to the augmentation of the fund needed for the purchase of the demised premises if the option to purchase were exercised, and both of them really in effect invested the whole or portion of their respective shares of the profits in making improvements which enhanced the value of the premises which they could purchase at a fixed sum.

Their Lordships think that the appeal fails, that the order of the 4th May, 1922, is right, and they will humbly advise His Majesty accordingly.

The appellant will pay the costs of the appeal.

In the Privy Council.

FRANK K. BROWN

v.

PHIL H. MOORE.

DELIVERED BY LORD ATKINSON.

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