

Montreal Trust Company and another - - - - - *Appellants*

v.

Canadian National Railway Company - - - - - *Respondents*

FROM

THE COURT OF KING'S BENCH FOR THE PROVINCE OF
QUEBEC (APPEAL SIDE)

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF
THE PRIVY COUNCIL, DELIVERED THE 21ST JULY, 1939.

Present at the Hearing :

LORD ATKIN.

LORD THANKERTON.

LORD RUSSELL OF KILLOWEN.

LORD WRIGHT.

LORD ROMER.

[*Delivered by* LORD RUSSELL OF KILLOWEN]

In this case the Montreal Trust Company and one Séguin, appeal from a judgment of the Court of King's Bench (Appeal Side) of the Province of Quebec, which affirmed a judgment of the Superior Court. The judgment declared a lease by Séguin to the Canadian National Railway Company, to be illegal and void, and dismissed with costs an action for rent thereunder brought by the Montreal Trust Company as transferee of Séguin's rights under the lease. Séguin was summoned as *mis-en-cause*.

The relevant facts which led up to the action must be stated, the Canadian National Railway Company being referred to as the Railway Company, and the Montreal Trust Company being referred to as the Trust Company.

The Railway Company is a company incorporated by a Dominion statute, 9 & 10 Geo. V. c. 13, now represented by R.S.C. 1927, c. 172. It has no capital stock or shareholders. Its corporators are its directors, who (from five to fifteen in number) are all chosen by the Governor General in Council. It is subject to the provisions of the Railway Act of Canada (R.S.C. 1927, c. 170), excepting those provisions which are inconsistent with its own Act.

In September, 1929, the President and Chairman of the Railway Company was Sir Henry Thornton. He had filled those offices for some seven years. He was then serving in those capacities under an agreement with the Railway

Company dated the 2nd September, 1925, at a salary of \$65,000.00 a year. That agreement was due to expire on the 4th October, 1930. He was living, at his own expense, in a house, 1415, Pine Avenue, in the City of Montreal, which he leased from a Mr. Beardmore at a rent of \$6,000.00. His tenure was, however, precarious, because Mr. Beardmore was anxious to sell the house, and the lease contained a clause enabling Mr. Beardmore to terminate the lease on three months' notice.

By an agreement dated the 23rd September, 1929, and made between the Railway Company and Sir Henry Thornton, he was engaged to continue to serve as President and Chairman for a period of five years from the 4th October, 1928, and thereafter from year to year determinable by either party on 12 months' notice, at a salary of \$75,000.00 without any extra fees or remuneration of any description; and the agreement of the 2nd September, 1925, was cancelled as from the 4th October, 1928. Apparently out of abundant caution, Sir Henry Thornton obtained an agreement (dated the 25th October, 1929) from the Crown to the same effect, the salary of \$75,000.00 thereunder being expressed to be payable less the remuneration receivable under his agreement with the Railway Company.

For some reason, not immediately apparent, a proposal was set on foot that the President should (in addition to his salary of \$75,000.00) be provided with free residential quarters, and on the 17th September, 1929, the Executive Committee of the Directors passed a resolution (which was approved by the Board of Directors on the 23rd September, 1929), in the following terms:—

“Whereas in the opinion of the Executive Committee a suitable residence in Montreal for the Chairman and President of the Company is essential for the proper conduct of the Company's business, it was unanimously resolved that the Executive Committee should undertake to lease a suitable and properly equipped residence for the use of the Chairman and President of the Company under such terms and conditions as the Committee may subsequently deem proper.”

Steps were then taken to provide the residence, the most obvious choice, if it were possible, being the house in Pine Avenue which was and had for some time past been Sir Henry's home. A difficulty, however, existed in the fact that Mr. Beardmore would not lease but would only sell, while the Railway Company would not buy but would only rent. At this point Mr. Decary becomes prominent in the story. He was President of the Title Guarantee and Trust Corporation and a director of the Railway Company. He was also the head of a firm of Notaries, Decary Barlow & Joron. He was asked by his co-directors whether he could arrange the financing of a purchase of the Pine Avenue house. He said that the Title Guarantee and Trust Corporation would not finance it; but that he would try to get it financed elsewhere. Ultimately he did arrange with a Mr. Donaldson, the manager of the Trust Company, that the Trust Company would advance the money necessary to

purchase the property on the terms contained in the following letters:—

(1) Letter. Decary to Donaldson. 24th June, 1930.

“ Referring to our conversation of the other day in connection with the Beardmore property on Pine Avenue, I, or my nominee subject to my personal guarantee, will purchase the above property for \$185,000.00 cash, the property subsequently to be rented to the Canadian National Railways for ten years, at a price representing $8\frac{1}{2}$ per cent. per year, net, outside of taxes of any kind, repairs and improvements.

“ You will make a loan for this amount of \$185,000.00 for ten years, at $6\frac{1}{2}$ per cent., the difference between the amount of interest paid and $8\frac{1}{2}$ per cent. to be applied as a sinking fund on the amount of the loan. Your Company will be given a first mortgage on the property and an absolute transfer of the Canadian National lease as guarantee for the loan.

“ We should be in a position to complete this transaction during the first days of the month of July. Will you please advise if this is convenient to you, and oblige.”

(2) Letter. Donaldson to Decary. 25th June, 1930.

“ I have your letter of the 24th instant, in connection with the Beardmore property on Pine Avenue. The arrangement as outlined by you is quite satisfactory to us and we are prepared to make the loan for the amount stated, subject to satisfactory Title.”

Meanwhile Mr. Beardmore and Sir Henry Thornton had already come to terms, under which Mr. Beardmore agreed to accept and Sir Henry agreed to pay \$175,000.00 for the house and \$10,000.00 for sundry furnishings therein; and the benefit of this contract was on the 9th July, 1930, at the request of Mr. Decary assigned by Sir Henry Thornton to the mis-en-cause Séguin. Séguin was described by Mr. Decary in this request, which was made by letter dated the 4th July, 1930, as “ my nominee ”. Séguin is himself a notary, and is in the employ of Mr. Decary’s firm.

On the 16th June, 1930, the Executive Committee had passed a resolution which was worded thus:—

“ RESOLVED that the Company rent from GEORGE H. SÉGUIN for a term of ten (10) years, commencing on the first day of August, Nineteen hundred and thirty (1930), and expiring on the first day of July, Nineteen hundred and forty (1940), that certain house bearing No. 1415, Pine Avenue West, in the City of Montreal, for an annual rental of FIFTEEN THOUSAND SEVEN HUNDRED AND TWENTY-FIVE DOLLARS (\$15,725.00) payable quarterly on the first days of February, May, August and November of each year, the first payment to become due on the first day of November next (1930) and subject to the following conditions on the part of the Company, namely:—

“ To keep the house in good order of repairs during the entire term of the lease;

“ To use the premises as a private residence only, and for no other purposes;

“ To pay all taxes and assessments, general or special, or of any nature whatsoever which may be imposed on said property during the term of the lease.”

The sum of \$15,725.00 is $8\frac{1}{2}$ per cent. on the total sum payable to Mr. Beardmore for the house and furniture. This resolution was approved by the Directors of the Railway Company on the 19th August, 1930.

On the 8th August, 1930, three notarial documents were executed and subsequently registered, viz. (1) a deed of sale by Mr. Beardmore to Séguin of the house and its contents and furnishings, the price being stated to be \$175,000.00 for the immovable properties and \$10,000.00 for the contents and furnishings of the house; (2) a lease by Séguin to the Railway Company for the term of ten years from the 1st August, 1930, of the house in consideration of \$157,250.00 payable by 40 quarterly instalments as therein mentioned; and (3) a deed of loan between the Trust Company and Séguin by which the Trust Company lent \$185,000.00 to Séguin, and Séguin bound himself to repay the loan on the 1st August, 1940, to pay interest at 6½ per cent. in the meantime, and also to reduce the principal by annual repayments of 2 per cent. of the amount of the loan. As security Séguin hypothecated in favour of the Trust Company the house in Pine Avenue, and transferred to it his rights under the lease to the Railway Company.

Subsequently Séguin as "owner" of the house entered into an agreement to make certain repairs thereto at a cost not to exceed \$50,000.00. This fact need only be stated for the purpose of explaining the reference to that sum in the following letter. On the 6th November, 1930, Mr. Decary wrote a letter to Sir Henry Thornton containing the following passage:—

"As you have asked me also, I hereby agree on behalf of the owner of property 1415, Pine Avenue, which you now occupy, to sell you this property at any time during the term of its lease to Canadian National Railways for the sum remaining due to us on the advances of \$185,000.00 and \$50,000.00. In order, however, not to encumber my estate in any way this option would have to be exercised within six months following my death should I die before the expiry of your lease."

On the 20th November, 1930, Sir Henry Thornton (by letter of that date) informed the Minister of Railways of this option to purchase and stated that it was "of course assignable to any nominee of my own".

The rest of the story is soon told. Sir Henry Thornton died in March, 1933; and on the 27th April, 1933, the legal advisers of the Railway Company wrote to Séguin alleging that "the lease executed on the 8th August, 1930, . . . between the Railway and yourself—acting for the benefit of Mr. Ernest Decary—is a nullity". The present action was commenced on the 13th October, 1933, claiming payment of the instalments of rent due on the 1st May, 1933, and the 1st August, 1933, respectively.

The point of the case can now be stated. It is claimed by the Railway Company that the lease is a nullity by reason of the provision contained in section 121 of the Railway Act (R.S.C. c. 170) which enacts:—

"No person who is a Director of the Company shall enter into or be directly or indirectly for his own use and benefit interested in any contract with the Company other than a contract which relates to the purchase of land necessary for the railway, nor shall any such person be or become a partner of or surety for any contractor of the Company."

It is said that by reason of the part played by Mr. Decary in relation to the lease and the purchase of the property, the section operates to make the lease a nullity and of no effect.

The Trial Judge and the Appeal Court have both taken this view, but as the result of different reasoning. Their Lordships also are of opinion that the action was rightly dismissed by reason of the section; but they prefer to base their view on a branch of the section different from that which found favour with the Judges of the Court of King's Bench.

Their Lordships are not concerned with any question but the validity of the lease. No question can arise in this action (to which Mr. Beardmore is not a party) in relation to the purchase from him and the conveyance by him to Séguin, or in relation to the hypothec by Séguin to the Trust Company. Indeed by no stretch of the imagination can either transaction come within the section; they cannot in any sense be described as contracts with the Railway Company.

The case is otherwise with regard to the lease. To that document the Railway Company is a party, and by that document it enters into contractual relationship with Séguin. But Séguin was admittedly, and to the knowledge of the Railway Company, merely the nominee of Mr. Decary. Subject to the rights of the Trust Company under the deed of hypothec, Séguin would have to account to Mr. Decary for the rent payable by the Railway Company under the lease. On the other hand Mr. Decary would be bound to indemnify Séguin and keep him harmless from all liability imposed upon him as a lessor by virtue of the lease. In these circumstances their Lordships feel no doubt that the lease was a contract with the Railway Company in which Mr. Decary was directly or indirectly interested. So far the case falls directly within the words of the section.

The appellants, however, contended that the whole transaction was not a profitable one, that Mr. Decary only acted in the matter at the instance of the Railway Company and with no expectation of profit, that Sir Henry Thornton's option to purchase existed for the benefit of the Railway Company, and that in these circumstances it could not be said that Mr. Decary, if interested in a contract with the Railway Company, was interested therein "for his own use and benefit". Their Lordships cannot accede to this contention. Mr. Decary no doubt acted as he did at the request of the Railway Company and in order to achieve the result which was desired, viz., that a purchase by the Railway Company should be avoided and a lease from a purchaser should be obtained. This result was achieved by Mr. Decary finding a purchaser in the shape of his nominee who granted the desired lease, with the inevitable consequence that Mr. Decary became interested and for his own use and benefit. Nor can the fact, if it be the fact, that the transaction is deemed unprofitable affect the question. The lessor was Mr. Decary's nominee, and Mr. Decary represented no one

but himself in procuring his nominee first to become the registered owner of the property and then to execute the lease. Mr. Decary's interest in the lease was an interest which enured for his own use and benefit, and for the use and benefit of no one else. Nor can the existence of an option to purchase affect the question, for unless and until the option is exercised the position remains unchanged.

It was further contended by the appellants that the case fell within the words of exception contained in the section, viz., "other than a contract which relates to the purchase of land necessary for the Railway". Their Lordships will assume, without in any way indicating an opinion upon the point, that a lease of land is a contract which relates to the purchase of land. They are, however, of opinion that the land here in question was not "necessary to the Railway" within the meaning of the section. "Railway" is defined by the Act (section 2 (21)) in such a way as to restrict its meaning, unless the context otherwise requires, to the track and its physical appurtenances. Their Lordships are unable to conceive how providing a residence for an official of the company could be a purchase of land necessary for the railway as defined by the Act.

The result is that the case falls exactly within that branch of the section which prohibits a director from being interested in any contract with the Company. Their Lordships prefer to base their decision upon that branch of the section, as they feel that there might well be a difficulty in saying that the lease in this case, in fact entered into by Séguin, though chosen for that purpose by Mr. Decary, was a contract "entered into" by Mr. Decary.

The question then remains, what is the effect of the prohibition contained in the section? It was contended that the effect was not to invalidate the contract, but only to avoid the director's interest in it, and to give rise to penalties under section 444. It was said that the effect produced by section 121 was no different from that produced by sections 85 and 86 of our Companies Clauses Consolidation Act, 1845, as exemplified by the case of *Foster v. The Oxford Railway Co.*, (13 C.B. 200) in which it was held that a contract between the company and a director was not avoided. The language of the two enactments is not, however, comparable, and the Courts in Quebec decided that the contract was a nullity, being bound, as they said, by the decision of the Supreme Court of Canada in the case of *McDonald v. Riordon* (8 Quebec, K.B. 555, 30 S.C.R. 619). That case was concerned with section 19 (16) of the Consolidated Railway Act, 1879, which was framed thus:—

"No person holding any office, place or employment in or being concerned or interested in any contracts under or with the Company shall be capable of being chosen as a director, or of holding the office of director, nor shall any person being a director of the Company enter into, or be directly or indirectly for his own use and benefit interested in any contract with the Company, not relating to the purchase of land necessary for the railway, or be or become a partner of any contractor with the Company."

In that case a director of a railway company had by agreements with the firm of contractors who were constructing the company's line, become entitled to a share of the payments made by the railway company to the contractors. He brought an action to recover his share against the contractors, who pleaded that the agreements were null and void because they were prohibited by section 19 (16) of the above-mentioned Act. The Trial Judge allowed the claim holding that making such contracts was merely a punishable offence which did not affect the civil rights of the parties. That judgment was reversed by the Court of Review (Montreal) on the ground that the contracts were prohibited by law and therefore void. The judgment of the Court of Review was affirmed on appeal by the Court of Queen's Bench for Lower Canada (Appeal Side), whose judgment was in turn affirmed by the Supreme Court of Canada and for the reasons given in the Court of Queen's Bench. It is sufficient, their Lordships think, to quote a passage from the judgment of Wurteli J. in the Court of Queen's Bench. After referring to the contracts which sub-section 16 of section 19 prohibited, he continued:—

“ . . . and the effect of such a prohibition is to render such a contract illegal and void, although the statute itself does not state that it is so and only imposes a penalty on the offender. Our civil code, in Article 14, declares that prohibitive laws import nullity although such nullity is not expressed. . . .

“ . . . In the present case the contracts were entered into in transgression of the provisions of the Consolidated Railway Act of 1879 which prohibited the appellant from entering into such contracts and which declared his act in becoming a party to them a misdemeanour and they are therefore void and without effect.”

It is true that the contracts there in question were not contracts with the company, but contracts which made the director interested in a contract with the company. Their Lordships, however, agree with the principle there laid down, that prohibition of a contract by statute renders the contract void and of no effect.

Their Lordships are of opinion that in the present case, the Railway Company, in taking a lease in which to its knowledge one of its directors was interested, made a contract prohibited by section 121. That contract is accordingly void and of no effect; and the action to recover rent thereunder was rightly dismissed.

This appeal should accordingly be dismissed, and their Lordships will humbly advise His Majesty accordingly. The appellants must pay the costs of the appeal.

In the Privy Council

MONTREAL TRUST COMPANY AND
ANOTHER

vs.

CANADIAN NATIONAL RAILWAY
COMPANY

DELIVERED BY LORD RUSSELL OF
KILLOWEN

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