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May 30 & 31
June 29.

HIS MAJESTY THE KING.....PLAINTIFF;

v.

THE CANADIAN SURETY COMPANY...DEFENDANT.

Revenue—Customs—Bond—Cancellation—Fraud—Effect upon surety

The facts in this case are similar to that in the *The King* v. *The Fidelity Insurance Company of Canada,* (1929) Ex. C.R. 1, except that in this case the bond given for the due exportation of the liquor according to its terms, and which was sued on, had been cancelled by the Customs authorities and had been surrendered to the surety. This cancellation was procured by fraud; the same having been obtained upon production of a forged document which the Collector believed to be genuine.

Held,—That when the release of the principal debtor by the creditor is accomplished by means of fraud, on the part of the former, the surety is not discharged, even if he is not a party to the fraud by which the release was secured.

ACTION upon a bond executed by the defendant for the payment to His Majesty of the sum of $41,500 for the due exportation of certain whiskey out of Canada.

The action was tried before the Honourable Mr. Justice Maclean, President of the Court, at Ottawa.

N. W. Rowell, K.C., and *Gordon Lindsay* for plaintiff.

W. L. Scott, K.C., for defendant.

The facts are stated in the reasons for judgment.

THE PRESIDENT, now (June 29, 1929), delivered judgment.

This is an action upon a bond executed by the defendant for the payment to His Majesty of the sum of $41,500. On the 31st day of January, 1925, the defendant executed a bond for the payment to His Majesty of the sum just stated. The conditions of the bond were to the effect that, if certain goods, namely twelve bags of whisky and six hundred and forty-two kegs of whisky, entered at the port of Halifax, N.S., by the Scotia Import and Export Co., Ltd., for exportation to Georgetown, Grand Cayman, B.W.I., by the steamer *Gemma,* were actually exported to the place provided for in the said export entry, unless the said goods were after leaving Canada lost and destroyed; and that if such proof or certificate, as was required by regulations of the Minister of Customs and Excise, that such goods had

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been so exported or lost and destroyed, as the case might be, were produced to the Collector or other proper officer of Customs and Excise at the port of Halifax, N.S., within thirty days of the date of the said bond, then the bond should be void, but otherwise to remain in full force and virtue.

Such a bond was required by a proviso to section 101 of the Customs Act, which proviso specifically relates to the exportation of wines and spirituous liquors. The regulation of the Minister of Customs and Excise relating to the entry outward of wines and spirituous liquors to be exported from a Customs warehouse provided, that if within the period appointed in such bond, there was produced to the Collector or other proper officer of Customs, the written certificate of some principal officer of Customs, or some other designated person, at the place to which the goods were exported, showing that the goods named in the said bond were actually landed and left at the place named in the bond, or if within the said period appointed, it was proved to the satisfaction of the Collector or other proper officer that the said goods were, after leaving Canada lost and destroyed, the bond might be cancelled.

The steamer *Gemma* reported outwards from Halifax, N.S., on February 3, 1925, for Georgetown, Grand Cayman, B.W.I., via St. John, N.B., which latter port she reached on February 5 where a further quantity of liquor in transit to Havana, Cuba, was taken on board. There she remained until February 25 when she cleared for Georgetown. On March 3, she reported inwards at Shelburne, N.S., in ballast, and cleared therefrom for Halifax on March 10. When the Master of the *Gemma* reported inwards at Shelburne he made a sworn statement before a Customs officer there, that since he had cleared from St. John, the "merchandise" then laden in the *Gemma* had been disposed of on the high seas, thirty miles off the United States coast on board lighters, and that no part of the cargo was disposed of in Canada. I shall refer to this matter later. It is not contended that the liquor entered outwards at Halifax was ever forwarded to Georgetown.

On the 27th of February, a written certificate was deposited with the Collector of Customs at Halifax, purporting to certify under the signature of the Collector of Cus-

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toms at Georgetown, and having impressed thereon what purported to be the Customs Stamp of that port bearing the date February 16, 1925, that the goods referred to in the bond in suit and laden on the *Gemma* at Halifax, had been landed at Georgetown. This certificate turns out to be a forgery. The Collector of Customs at Halifax, however, acted on this certificate, believing it to be genuine, and thereupon cancelled the bond and surrendered the same to the Halifax agents of the defendant, for delivery to it. These facts, it is claimed, became known to the Department of Customs in consequence of a public inquiry directed by a Royal Commission, into the administration of the Department of Customs. After retaining the cancelled bond for two years, the same was destroyed in accordance with the company's usual practice; there is no question of bad faith on the part of the defendant company in this connection. The plaintiff commenced action upon the bond in September, 1928, more than three years subsequent to the cancellation of the bond.

The plaintiff contends that the cancellation of the bond was procured by fraud; that the goods were never shipped to the place mentioned in the bond as already explained, and that no certificate or proof was ever produced by the defendant, or any other person, that the goods mentioned in the bond had been exported to the place there mentioned, or that they had been lost or destroyed; and that the conditions of the bond not having been performed it is still in full force and effect.

Several defences are pleaded in the defendant's answer to the Information, some of which I think are not substantial and do not call for any discussion. One of the defences is, that the true intention of the bond and the provisions of the Customs Act under which it was given, was to ensure the export out of Canada of the goods referred to in the bond, and that they would not be brought back to Canada without payment of duty; that the goods were not brought back to Canada and accordingly the public revenues of Canada did not suffer any loss or damage, even if actual export was not made of the goods to the place mentioned in the bond; that the Collector of Customs at Halifax was the judge of the sufficiency of the compliance with the conditions of the bond,

and having acted on the evidence before him and having cancelled the bond, that concludes the matter; and that the defendant did "otherwise account for the said goods", this accounting it is claimed, was made to the Collector of Customs at Shelburne, when as explained, the master of the *Gemma* made the sworn declaration that the goods were landed into lighters thirty miles off the coast of the United States and were not landed in Canada. It is also claimed that the officers of His Majesty's Customs service knew, or should have known, that the certificate produced was not genuine, and that its falsity should have been discovered earlier. One of the principal defences is, that as the bond was cancelled by the Collector of Customs at Halifax, and as no action was commenced for more than three years subsequent to the date of such cancellation, the position of the defendant has been materially changed, because it had an indemnity agreement from one McDonnell, and also reinsurance with the American Insurance Company of the United States against its liability in part on the bond, and therefore the plaintiff is in equity estopped from suing on the bond at this time.

This case is similar to that of *The King* v. *Fidelity Insurance Company of Canada,* reported in 1929 Exchequer Court Reports, part 1, page 1, to which I would refer, except that in this case there was a cancellation of the bond by the customs authorities and its surrender to the surety. In that case, as here, the goods were not landed at the place mentioned in the bond, nor was it shown in either case that they were landed at all; it was only shown that in each case the goods were delivered to other carriers on the high seas. It is not necessary to repeat here much that I said in the case just mentioned, and I am thus relieved of a discussion of several points raised here, which I dealt with in that case. The first question arising for decision is, what is the legal effect of the cancellation of the bond. The cancellation was procured by fraud; that cannot be denied. No landing certificate was ever produced as required by the Customs regulations, already referred to. A forged document only was produced, which the Collector of Customs acted upon, believing it to be genuine. It is well settled law that when the release of the principal debtor by the creditor is accomplished by means of fraud, on the part of

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the former, the surety is not discharged, even if he is not a party to the fraud, by which the release was secured. *Scholefield* v. *Templer* (1), *and County of Frontenac* v. *Breden* (2).

According to the doctrine of the law of suretyship, a surety is not released by something which happens in consequence of that which amounts to a fraudulent breach of contract, against which the surety has guaranteed the party with whom he has contracted. The defendant contracted that the goods in question, if not lost or destroyed, would be landed at Georgetown. They were not so landed, they were not lost or destroyed, and the cancellation and surrender of the contract was procured by fraud. Can the defendant be heard to say, that it is to benefit by the fraud of those whom it guaranteed would land the goods at Georgetown. The fraud was in representing that a certain undertaking had been carried out, which was not in fact carried out, and which if not carried out the defendant agreed to pay a stated sum as liquidated damages. That, I think, is the meaning of the contract. In *Mayor, etc.*, v. *Kingston-upon-Hull* v. *Harding* (3) to which I would refer, Bowen L.J. said:—

> The broad principle of law, which is the root of our decision is that a surety cannot claim to be discharged on the ground that his position has been altered by the conduct of the person with whom he is contracting, where that conduct has been caused by a fraudulent act or omission against which the surety by the contract of surety has guaranteed the employer. This seems to be good sense and I think it is good law.

I am of the opinion that the cancellation and delivery up of the bond, procured as it was, does not of itself void the obligation, but that it remains in full force and effect, unless upon other grounds it is in law unenforceable.

It is specifically contended that the position of the surety was altered by reason of the cancellation of the bond, and the long period intervening between the cancellation of the bond, and the commencement of this action. Upon the evidence submitted, I am bound to conclude that on discovery of the fraud, in 1927 I think, following the revelation of the facts before a Royal Commission, the plaintiff, within a reasonable period elected to avoid the cancellation and delivery up of the bond by the commencement of this

(1) (1859) 4 De G. & J. 429, at p. 434.

(2) (1870) 17 Gr. Chan. Rep., 645.

(3) (1892) 2 Q.B.D. 494.

action. Had the plaintiff taken no steps, for a long period after gaining such knowledge, to repudiate the cancellation, it might have stood; but the plaintiff has impugned it by this action, and he says it is not binding upon him.

Unless something has happened to alter the position of the defendant since the delivery up of the bond, and before the plaintiff elected to treat the cancellation as void, the cancellation will not avail the defendant. The defendant had an indemnity agreement with one McDonnell, who has been brought in by the defendant as a third party in this action, as also has the Scotia Import and Export Co. From the evidence, I assume that McDonnell and the Scotia Import and Export Co., the exporters mentioned in the bond, are one and the same. The defendant claims it has been unable to obtain any admission or assumption of liability from McDonnell for the amount here sued upon, which is about what one would expect. The defendant also reinsured with the American Insurance Company against a portion of its liability upon the bond, but it is not suggested that the position of the company giving the counter-bond has been altered by the cancellation of the bond. There is no proof that within the period intervening between the cancellation of the bond and the bringing of this action, the position of the defendant had been altered in such a way as to make it inequitable as against it, that the cancellation should be treated as avoided. Whether the position of defendant as surety has been altered is a question of fact and not of law; in this case it is not to be presumed from the mere cancellation of the bond. The defendant has not released the third party, McDonnell, from his indemnity agreement, nor the American Insurance Company upon its counter-bond. That being so how can it be said that the position of the defendant has been altered? The defendant here seeks judgment against McDonnell and the Scotia Import and Export Co., if judgment in this action is against it; and it is admitted that to the extent of the reinsurance with the American Insurance Company, it was not expected that this company would not honour its obligation, in the event of judgment being against the defendant in this action. Even if it were established, that neither McDonnell or the American Insurance Company were not, in fact, able to answer for their several obligations to the defendant if called upon so to do, by reason of

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financial losses occurring to them since the cancellation of the bond, that would not, I think, be an answer to the plaintiff's claim. That could not be attributable to the plaintiff. The continuing solvency of the defendant's guarantors was a risk assumed by it when selecting insurers against its liability upon the bond. If the cancellation of the bond has in any way altered the position of the defendant, the fact remains that this was brought about by the fraud of a principal, against which act the defendant had contracted with the plaintiff. The contract of suretyship provides by implication, that the defendant is not to be discharged in consequence of an act, which the defendant had guaranteed to the plaintiff would not occur. In the facts of this case, I am unable to see how the defendant can successfully contend, that its position has been so changed by any act of commission or omission on the part of the plaintiff, as to afford a defence in equity to the claim here sought to be enforced against it.

It was suggested that Customs officers should have in some way superintended the movements of the *Gemma*, and should have known before the cancellation of the bond that her master had not landed the goods at the place mentioned in the bond. The obvious remark upon this point is, that there was no contract between the plaintiff and the defendant that the officers of Customs should follow the movements of the *Gemma*. Where the omission of one who contracts to do something deprives a surety of a right under the contract, such an omission might so affect or alter his position as to avoid the obligation of the surety. That is not this case. It would appear rather absurd to say that officers of Customs were obliged to follow the movements of the *Gemma*, and to see that she actually went to the port mentioned in the bond. It was no part of the duty of Customs Officers to do this. The defendant guaranteed to the plaintiff that this would be done, and it is because it was not done, that the plaintiff claims the surety is liable. Then it is said that the goods were accounted for at Shelburne, and that the Collector of Customs at Halifax accepted this accounting as sufficient, and certain words of the first paragraph of sec. 101 of the Customs Act are relied upon. These words are: " to otherwise account for the said goods, etc." It is to be pointed out that this action is not founded

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upon that part of that section of the Customs Act, but upon the proviso to that paragraph and these words are not there to be found. The proviso was expressly enacted to cover the exports of wines and spirituous liquors from a Customs warehouse, and its terms are most exacting and rigid, and I assume that was intended to mean just what it says. A distinction seems to be made between "wines and spirituous liquors" and other goods. With the purpose of the enactment I am not concerned. The contentions that the goods were not brought back to Canada, assuming the fact to be proven; that the revenues of Canada had not suffered; and that to exact the performance of the bond is unjust because the goods went out of Canada, do not seem to be of substance in view of the terms of the statute, the Customs regulations and the bond itself. To suggest that there is ground for suspicion, that it was the practice at many Canadian ports of Customs to turn a blind eye upon landing certificates required by the Customs Act, in connection with the export of wines and spirituous liquors, as in this case, may have some justification, but there is no satisfactory evidence of that before me. What its effect would be upon this case, if established, I need not pass upon.

A number of authorities in support of the doctrine that the Crown is bound by estoppel in pais, or equitable estoppel, were cited by counsel for the defendant, and to that doctrine I agree, because, I think, it is now well settled law. I do not think, however, that the line of decisions referred to by counsel, are applicable in this case. The principle laid down in these cases is expressed by Lord Cranworth in *Ramsden* v. *Dyson* (1), as follows:—

> If a stranger begins to build on my land supposing it to be his own, and I perceiving his mistake abstain from setting him right, and leave him to persevere in his error, a court of equity will not allow me afterwards to assert my title to the land on which he expended money, on the supposition that the land was his own. It considers that when I saw the mistake into which he had fallen, it was my duty to be active and to state my title; and that it would be dishonest in me to remain wilfully passive on such an occasion, in order afterwards to profit by the mistake which I might have prevented. But it will be observed that to raise such an equity two things are required, first that the person expending the money supposes himself to be building on his own land; and secondly that the

(1) (1865) L.R. 1 H.L.R. 129 (E. & I. App.)

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real owner at the time of the expenditure knows that the land belongs to him and not to the person expending the money in the belief that he is the owner.

That principle is hardly applicable to the facts here. It has not been shown that the plaintiff knowingly did anything to justify the defendant in believing or continuing to believe, that the plaintiff was aware that the goods had been delivered at a place other than that mentioned in the bond. Anything that might lead the defendant to believe that the plaintiff was satisfied that there had been a fulfilment of the obligation of the defendant under the bond, was brought about by the defendant's principal fraudulently representing something as done which was not done, but which the defendant had contracted would be done. I must go by the evidence before me, and there is nothing here to show that the plaintiff stood by for three years and more, knowing or suspecting that the obligations of the bond had not been actually fulfilled according to its precise terms. But this contention is answered, I think, by the fact that whatever Customs officers or others did, was brought about by the fraud of those to whom the defendant stood in the position of surety to the plaintiff. No bona fide landing certificate was ever presented in fact to Customs, and the bond was in the same position as if it had been stolen by the defendant's principal. I have referred to the affidavit made by the master of *Gemma* at Shelburne. It is true this was done in virtue of departmental directions, in the cases where a ship enters a port without cargo, as in this case, after leaving her last port of departure with a cargo, in this case, St. John. This may show knowledge or suspicion on the part of a Customs officer at Shelburne that the goods in question had not been landed at the declared port of destination, but of that I am not sure, as I do not think it was made clear to me that the Customs officer at Shelburne was made aware of the nature of the "merchandise" aboard the *Gemma*, when she cleared from St. John. In any event this suspicion or knowledge was not communicated to the Collector of Customs or other proper Customs officer at Halifax, who alone could cancel the bond, or to the chief executive officers of Customs at Ottawa, either before or after the act of cancellation was made, and there was nothing requiring it to be done.

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The plaintiff is in my opinion entitled to judgment for the amount sued upon together with his costs of action.

As already stated Mr. P. A. McDonnell was by leave of the Court served with a third party notice, as also was the Scotia Import and Export Company Ltd., to which neither have entered appearance. I am not satisfied that the Court has jurisdiction in these third party proceedings and I reserve leave to counsel for the defendant to argue the question of the jurisdiction of the Court, as arising upon such third party proceedings.

Judgment accordingly.