BETWEEN:

1935
Nov. 27 & 28.
1936
Jun. 13.

HIS MAJESTY THE KING, ON THE INFORMATION OF THE ATTORNEY-GENERAL OF CANADA..... PLAINTIFF;

AND

A. KUSSNER AND E. J. KUSSNER.. DEFENDANTS.

Revenue—Sales tax—Liability of director for debts of company already incurred at the time the company made a loan to its shareholders or subsequent thereto—Companies Act, R.S.C. 1927, c. 27, s. 112—Companies' Creditors Arrangement Act, 23-24 Geo. V, c. 36—Income War Tax Act, R.S.C. 1927, c. 97, s. 18—Crown not bound by any statute unless statute expressly states otherwise.

Held: That the Companies Act, R.S.C. 1927, c. 27, s. 112, renders the directors of a company liable to its creditors not only for debts of the company existing at the time a loan is made to its shareholders but also for debts contracted between the time of the making of such loan and that of its reimbursement.

2. That the Companies' Creditors Arrangement Act, 23-24 Geo. V, c. 36, does not bind the Crown.

3. That there is no conflict between s. 18 of the Income War Tax Act, R.S.C. 1927, c. 97, and s. 112 of the Companies Act, R.S.C. 1927, c. 27.

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INFORMATION exhibited by the Attorney-General of Canada to recover from the defendants a certain sum for sales tax incurred when defendants were directors of a limited company.

The action was tried before the Honourable Mr. Justice Angers, at Montreal.

O. P. Dorais, K.C., and *Jacques Panneton* for plaintiff.

B. Bernstein, K.C., and *S. Moscovitch* for defendants.

The facts and questions of law raised are stated in the reasons for judgment.

ANGERS J., now (June 13, 1936) delivered the following judgment:

The present action is brought to recover from the defendants Abraham Kussner and E. J. Kussner jointly and severally the sum of $2,613.28 with interest from March 10, 1934, and costs.

The claim is for sales tax incurred by the National Waist Company Limited, a body politic and corporate having its head office in the City of Montreal, during the years 1932, 1933 and 1934, penalties and costs; it is made up as follows:

Date.	Payable.	Paid.	Balance.	
1932				
June	$799 20	$640 76	$158 44	
July	315 44	251 89	63 55	
Aug.	357 83	282 96	74 87	
Sept.	477 20	476 42	78	
Oct.	558 07	556 93	1 14	
				298 78
1933				
Jan.	$477 04	$472 96	$ 4 08	
Feb.	639 66	638 16	1 50	
March	345 51	344 91	60	
April	372 30	371 64	66	
Sept.	432 18	155 28	276 90	
Oct.	469 87		469 87	
Nov.	169 88		169 88	
Dec.	118 50		118 50	
				1,041 99

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1934			
Jan.	$290 35	$290 35	
Feb.	270 77	270 77	
March	114 17	114 17	
			675 29
			2,016 06
Exchequer Court costs			11 00
			2,027 06
Penalties			586 22
			$2,613 28

Plaintiff seeks to hold the defendants responsible for these taxes, penalties and costs as directors of National Waist Company Limited at the time the said taxes became due, in virtue of the provisions of Section 112 of the Companies Act (R.S.C. 1927, ch. 27) which reads:

112. If any loan is made by the company to any shareholder in violation of the provisions of this Part, all directors and other officers of the company making the same, or in anywise assenting thereto, shall be jointly and severally liable for the amount of such loan with interest, to the company, and also to the creditors of the company for all debts of the company then existing, or contracted between the time of the making of such loan and that of the repayment thereof.

National Waist Company Limited was incorporated by federal letters patent some twenty years ago; the exact date was not disclosed and it is immaterial.

In the latter part of March, 1934, National Waist Company Limited made a proposal of compromise to its creditors under the provisions of The Companies' Creditors Arrangement Act, 1933 (23-24 Geo. V, ch. 36) at ten cents on the dollar, which was agreed to by a statutory majority of its creditors and was sanctioned by the Superior Court of the Province of Quebec sitting in and for the district of Montreal by a judgment rendered on April 10, 1934, a duly certified copy whereof was filed as exhibit I.

The plaintiff was not represented at any of the meetings of the creditors of the company having to deal with this proposal of compromise and the said proposal was not accepted by or on behalf of the plaintiff.

A cheque for $200.58, purporting to represent 10% of the plaintiff's claim, was sent to the Commissioner of Excise but the same was not accepted.

The information alleges (*inter alia*) that National Waist Company Limited was indebted to plaintiff in the sum of

$2,613.28, with interest, for sales tax incurred when the defendants were directors of the company, that the company made an arrangement under the Companies' Creditors Arrangement Act on April 10, 1934, which was not accepted by plaintiff and that the defendants are jointly and severally liable for the said debt as a consequence of misfeasance and appropriation to their own use, when directors of the company, of funds of the company contrary to Section 112 of the Companies Act. The information then refers to and quotes in part the minutes of a directors' meeting held on February 5, 1934, at which a resolution was passed whereby certain shares of the Eagle Building, transferred by the defendants to the company in reduction of their indebtedness to the latter, were surrendered to the defendants and whereby it was declared that the amount of said indebtedness was to be considered as a bonus earned by the defendants during the previous years when it was actually paid out and when the company was showing a profit. I shall revert to this resolution later.

The defendants pleaded separately; the statements in defence are substantially the same.

The defendants admit that they were directors of National Waist Company Limited; they deny that the company was indebted to plaintiff in the sum of $2,613.28 for sales tax; they deny having appropriated, to their own use, funds of the company; they admit that the company made an arrangement under the Companies' Creditors Arrangement Act at ten cents on the dollar and say that this arrangement was binding on all the creditors of the company including plaintiff; they state that the company remitted to plaintiff a cheque for $200.58 being 10% of the amount of his claim, that this cheque was accepted by the plaintiff, that this acceptance constituted a full discharge of any indebtedness of the company and that the plaintiff had no further recourse against the company or against its directors.

The defendant Abraham Kussner, in addition to the foregoing, pleads that no actual loan, as contemplated by Section 112 of the Companies Act, was ever made by National Waist Company Limited to the defendants and that the sums in question received by them were in the nature of salaries, profits and bonuses earned in the regular

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course of the business of the company which they controlled, at a time when the company was earning profits; and he adds that in any case the said sums were paid to him prior to the existence of the plaintiff's claim.

The proof discloses that National Waist Company Limited made loans to E. J. Kussner and A. Kussner, the defendants, who at all material times were shareholders and respectively president and secretary-treasurer of the company, starting around 1925 or 1926.

The indebtedness of the defendants to the company in that respect from the 31st of January, 1931, was as follows:

For year ending January 31, 1931:
E. J. Kussner, $22,163.56; A. Kussner, $17,026.83.
For year ending January 31, 1932:
E. J. Kussner, $23,672.35; A. Kussner, $18,240.12.
For year ending January 31, 1933:
E. J. Kussner, $24,527.03; A. Kussner, $18,736.74.
On December 7, 1933, date on which the debt was written off to profit and loss:
E. J. Kussner, $22,352.61; A. Kussner, $17,907.36.

As may be noted the bulk of these sums was received prior to January 31, 1931. In fact subsequent to that date the loans to E. J. Kussner totalled $440.93 and the loans to A. Kussner $182.64. The amount of the defendants' indebtedness varies as the result, on the one hand, of certain refunds made by them and credited to their loan accounts and, on the other hand, of interest charged from time to time to the same accounts.

It was contended on behalf of defendants that the sums thus advanced to the latter by the company were not loans but profits or earnings which the defendants were entitled to withdraw and shared between them proportionately to their interests in the company.

This contention is, in my opinion, untenable. From the very outset these advances were treated as loans. A special account was opened in the company's books in the name of each of the defendants, under the heading "loan account" or occasionally "drawing account."

From the time these accounts were opened to the date on which the balance owing by the defendants was written off as aforesaid (December 7, 1933), the defendants, at different intervals, reimbursed certain sums and periodically interest on the balance outstanding was charged. In addition to the various amounts which the defendants refunded,

they transferred to the company, in partial reduction of their indebtedness, their interests in a property known as the Eagle Building estimated at $16,625.12, of which $9,559.44 were credited to E. J. Kussner and $7,065.68 to A. Kussner.

It is quite obvious that the company, from the beginning, considered these advances as loans and treated them as such and this lasted until the end of 1933 or the beginning of 1934, when the company, on the eve of making its proposal of compromise to its creditors, decided to grant the defendants a release of their indebtedness to the company.

I may mention here that all the shares of National Waist Company Limited were held by the defendants and their wives and that all four constituted the board of directors.

On December 7, 1933, as previously stated, the balance due by the defendants on the advances made to them was written off the books. On February 5, 1934, at a meeting of the board of directors, at which the four directors were present, resolutions were adopted on the vote of the wives of the defendants, the latter refraining from voting because personally interested in the said resolutions, the material part whereof I believe expedient to quote verbatim:

After discussion the following resolution was duly moved and seconded:

That where the equity in the said shares of the Eagle Building was practically negligible in view of the fact that they were already pledged for the personal indebtedness of Messrs. A. and E. J. Kussner and there would be no use in retaining the said shares or showing them as an available asset in the Company;

That the said shares be surrendered to Messrs. A. and E. J. Kussner and that the amount whereby their overdraft had been reduced in consideration of the said shares having been originally transferred to the Company, be written off from the assets of the Company to be considered as a bonus allowed to the said Directors for services rendered to the Company in the past.

Messrs. A. and E. J. Kussner being personally interested in the said resolution refrained from voting thereon.

It being established to the satisfaction of the meeting that the said Directors were not in a financial position in any case to pay off or meet their obligations for the amount of their overdraft or not likely to be in a position to meet same in the immediate future, the said resolution was thereupon unanimously adopted.

In view of the above representations it was thereupon resolved and seconded that the balance of the overdraft and loans made by the Company to Messrs. A. and E. J. Kussner be written off from the assets of the Company, the amount of the said overdraft to be considered as a bonus earned by the said Directors during the previous years when it was actually paid out and when the Company was showing a profit.

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Messrs. A. and E. J. Kussner being personally interested in the said resolution refrained from voting thereon. Carried unanimously.

The notion of treating these advances as bonuses or remuneration for services only occurred when the company decided to make a proposal of compromise to its creditors; up to that moment the advances were considered as loans.

I am satisfied that the advances in question were really loans by the company to two of its shareholders and that section 112 of the Companies Act applies to the case now under consideration.

It was submitted on behalf of defendants that the advances were made and the indebtedness of the defendants created before the sales tax claimed in the present action became due and exigible. This is quite true: except for interest the bulk of the defendants' indebtedness was incurred prior to 1931; on the other hand the unpaid sales tax is for the years 1932, 1933 and 1934. But this, in my opinion, is wholly immaterial, seeing that section 112 renders the directors of the company liable to its creditors not only for debts of the company existing at the time the loan was made but also for debts contracted between the time of the making of such loan and that of its reimbursement.

I have reached the conclusion that the defendants, who at the time the loans in question were made were directors of the company, became liable for the sales tax incurred by the company during the years 1932, 1933 and 1934.

It was urged on behalf of defendants that, in view of the proposal of compromise made by the company which was accepted by a statutory majority of its creditors and sanctioned by the Court, the plaintiff has no further recourse against the company nor against its directors under section 112 of the Companies Act.

This compromise is undoubtedly binding on the ordinary creditors. I do not think it is binding on the Crown.

It was contended for the defendants that the omission on the part of the Minister to vote against the proposal of compromise as well as his failure to return the cheque for $200.58, purporting to represent 10% of the amount of his claim, constituted an acceptance of compromise and a discharge of the company's indebtedness and that the company's directors could not be held liable in the circumstances. I do not believe that this contention has any foundation. The absence of a creditor from a meeting

held for the purpose of considering a proposal of compromise or his abstention from voting thereat must be considered as a vote against the proposal. As far as the cheque is concerned, it is clear from the letters of the Department of National Revenue dated respectively April 25 and May 7, 1934 (exhibits C and D), that it was not accepted. The plaintiff's position would perhaps have been more regular had this cheque been either returned to the sender or tendered in court as alleged in the information, but I do not think that the omission of doing either can be interpreted as being an acceptance of the same in satisfaction of the plaintiff's claim.

It was argued on behalf of defendants that the proposal of compromise, sanctioned by the Court as it was, became binding on the plaintiff as well as on the other creditors. I feel unable to agree with this view.

I do not think that the Companies' Creditors Arrangement Act can affect the rights of the Crown. Section 16 of the Interpretation Act (R.S.C. 1927, ch. 1) stipulates that "no provision or enactment in any Act shall affect, in any manner whatsoever, the rights of His Majesty, his heirs or successors, unless it is expressly stated therein that His Majesty shall be bound thereby." There is no such statement in the Companies' Creditors Arrangement Act.

My attention was drawn to a judgment of the Honourable Mr. Justice Boyer of the Superior Court of the Province of Quebec, dated April 22, 1936, in the case of *Roxy Frocks Manufacturing Company Limited and the Minister of National Revenue,* under the Companies' Creditors Arrangement Act, so far to my knowledge unreported, in which the learned judge said (*inter alia*):

> Au surplus la loi des Arrangements n'est qu'un accessoire de la loi de faillite qui s'applique à la Couronne et d'après laquelle elle n'a aucun privilège et il n'y a pas plus de raison d'accorder un privilège à la Couronne en vertue de la loi des Arrangements avant faillite, qu'après faillite sur compromis en vertu de la loi de faillite.

With all due deference I must say that I am not inclined to consider the Companies' Creditors Arrangement Act as an accessory to the Bankruptcy Act. The latter Act contains provisions dealing with Composition or Scheme of Arrangement (sections 11 *et seq.*) after the granting of a receiving order against the debtor or the making of an authorized assignment by him; it applies to insolvent debtors in general, whether a corporation, a firm or part-

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The proposal for a composition or scheme of arrangement under the Bankruptcy Act is incidental to and must follow a receiving order or an assignment. Before the amendment enacted by 13-14 Geo. V, chap. 31, s. 15, a debtor could make a proposal for a composition or a scheme of arrangement either before or after the making of a receiving order against him or the making of an authorized assignment by him: see 9-10 Geo. V, chap. 36, s. 13. But since the statute 13-14 Geo. V, chap. 31, came into force a debtor wishing to avail himself of the provisions of the Bankruptcy Act regarding a composition or scheme of arrangement must first be declared bankrupt or make an assignment for the benefit of his creditors. By section 188 of the Bankruptcy Act the provisions thereof relating to, among other things, the effect of a composition or scheme of arrangement and the effect of a discharge are made binding upon the Crown; section 188 reads as follows:

> 188. Save as provided in this Act, the provisions of this Act relating to the remedies against the property of a debtor, the priorities of debts, the effect of a composition or scheme of arrangement, and the effect of a discharge, shall bind the Crown.

The Companies' Creditors Arrangement Act contains no similar stipulation. I think I must assume that the legislators, when enacting the Act known as the Companies' Creditors Arrangement Act, enabling a company or corporation to submit to its creditors a proposal of compromise or arrangement without the necessity of a receiving order or an authorized assignment, intentionally omitted to mention that the Act would bind the Crown. It is to be surmised, as I think, that the legislators were aware that there was a clause in the Bankruptcy Act in virtue of which certain provisions thereof were expressly declared to bind the Crown. But be that as it may, it matters not, to my mind, whether the omission of a binding clause in the Companies' Creditors Arrangement Act was intentional or not; the absence of a provision in the Act relieves the Crown of any obligation thereunder: Maxwell on the Interpretation of Statutes, 7th ed., p. 117; Chitty, Prerogatives of the Crown, 383; Bacon's Abridgment of the Law, Prerogative (E) 5, pp. 92 *et seq.*; *Attorney-General* v. *Allgood* (1); *In re Henley & Co.* (2); *In re Oriental*

(1) (1743) Parker, 1 at 3.

(2) (1878) L.R. 9 Ch. D., 469, at 481 and 482.

Bank Corporation (1); *Ex parte Postmaster General. In re Bonham* (2); *Perry* v. *Eames* (3); *The Queen* v. *Bank of Nova Scotia* (4); *The Liquidators of the Maritime Bank* v. *The Queen* (5); *North Pacific Lumber Co.* v. *The Minister of National Revenue* (6).

It has been held that the doctrine that a statute does not affect the rights of His Majesty unless it is expressly mentioned therein that His Majesty shall be bound by it applies only to such rights and prerogatives as are the attributes of sovereignty and that it does not apply to minor prerogatives nor to such rights as may be possessed equally by all his subjects: see *Campbell* v. *Judah* (7); *In re Colonial Piano Limited* (8); *Monk* v. *Ouimet* (9). These decisions, in my opinion, have no bearing on the present case: the prerogative or right which the plaintiff is pleading is neither what has been termed a minor prerogative nor even less a right enjoyed by His Majesty's subjects.

The question as to whether the Crown had or not a preferential claim for sales tax was raised at the hearing but was not discussed at any great length, counsel for plaintiff declaring that he did not rely on a matter of privilege but on the fact that the Companies' Creditors Arrangement Act does not bind the Crown; I do not think that the question of privilege is relevant.

Prescription does not run against the Crown. Counsel for defendants submitted, however, that the plaintiff's claim was stale, and, relying on *Brooks* v. *Muckleston* (10), contended that it ought to be dismissed. The doctrine of staleness is not applicable in the present case.

It was argued by counsel for defendants that the Minister of National Revenue having assessed as income the advances received by the defendants and charged to their "loan" or "drawing" accounts was now precluded from claiming that they were loans; in support of his contention

(1) (1885) L.R. 28 Ch. D., 634, at 647.
(2) (1878-79) L.R. 10 Ch. D. 595 at 600.
(3) (1891) L.J. 60 Ch. D. 345 at 349.
(4) (1885) 11 S.C.R., 1 at 21.
(5) (1888) 17 S.C.R. 657 at 660, 661 and 668.
(6) (1928) Ex.C.R. 68
(7) (1884) 7 L.N., 147.
(8) (1926-27) 8 C.B.R., 266; (1928-29) 10 C.B.R., 111.
(9) (1874) 19 L.C.J., 71.
(10) (1909) 2 Ch. 519.

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counsel referred to section 18 of the Income War Tax Act (R.S.C. 1927, chap. 97). The first paragraph of section 18 reads as follows:

> *For the purposes of this Act,* any loan or advance by a corporation, *or appropriation of its funds to a shareholder thereof, other than a loan* or advance incidental to the business of the corporation shall be deemed to be a dividend to the extent that such corporation has on hand undistributed income and such dividend shall be deemed to be income received by such shareholder in the year in which made.

This section deals with income; it does not conflict with section 112 of the Companies Act which deals with an entirely different subject. The evidence does not disclose if the defendants complied with these assessment notices and if the income tax therein mentioned were paid; the proof in this connection is incomplete and unsatisfactory. But, assuming that the defendants paid income tax in compliance with the said assessment notices, I do not think that this can affect in any way the plaintiff's recourse under section 112 of the Companies Act.

The plaintiff has established his claim to the extent of $2,602.28; the evidence with regard to the sum of $11 for costs is not satisfactory.

There will be judgment against the defendants jointly and severally for $2,602.28 with interest from March 10, 1934, and costs.

The plaintiff will either return the cheque for $200.58 received pursuant to the arrangement hereinabove mentioned or give credit to the defendants for the amount thereof.

Judgment accordingly.