Features of the Law of Preference

Part of an Address Mr. F. R. McD. Russell Delivered Before the Vancouver Branch of the Canadian Creditmen's Association Held at the Vancouver Hotel, January 20, 1916.

"Time was in British Columbia when creditmen were not considered an essential part of our business institutions as they are today. Then, we had a great many more failures than we appear to do now, and some of them very serious ones. This change has undoubtedly been brought about, to a much greater extent than is generally supposed, by the work of the creditmen. A business without a creditman is like a ship navigating in strange waters without a pilot. The business may be ever so well managed, the buyer or seller may be the best in his class, the accounting or bookkeeping department may be second to none, and so on down the line; but the business without a creditman, to avoid the reefs and shoals and currents of business life, is almost bound, sooner or later, to meet with disaster.

"As regards your association, I am sure it is serving a useful purpose. I take it that you have adopted the course of interchanging reports and information regarding traders who the different firms represented in the association are trading with. This, if effectually carried out, cannot help but be beneficial to all concerned. Your association also provides a means of your getting together on an occasion such as this, and for a time at least forgetting your troubles over the flowing bowl (of tea) and pipe or cigar, unless, as on this occasion, you should so far forget yourself as to invite a lawyer to bore you, as I expect what I am saying, and may say to you, will do.

"Like a great many of our laws, the Law of Preference is hoary with age. Before it was dealt with by Statute, it was a rule of our Common Law (that is, the Law of Custom) that all transactions amounting to a preference were wrong, and should be avoided.

"The first Statute dealing with the subject that I know of was passed as far back as the time of Edward III., and is known by the title of '50 Edward III., Ch. 6.' This Statute provides that 'If it be found that any person shall make a gift fraudulently or by collusion his creditors shall be entitled to proceed against the goods and chattels transferred, as if no such gift had been made.' This was followed by another Statute, '2 Richard II., Ch. 3,' followed up a hundred years later by '3 Henry VII., Ch. 4,' and, finally, in the reign of Elizabeth, '13 Elizabeth, Ch. 5,' the Statute which is still known as the 'Fraudulent Conveyance Act,' was enacted. Followed later by 'The Fraudulent Preference Act,' 'The Creditors Trust Deeds Act,' 'The Creditors Relief Act,' and the 'Bulk Sales Act,' and others of a kindred nature, all of which deal in part at least with the prevention of fraudulent transfers by insolvent debtors.

"Dealing with the question of insolvency, I find it difficult to arrive at a settled definition. One eminent judge, in a case that is looked upon as more or less of an authority, laid it down that a man may be deemed insolvent in the sense of the acts relating to insolvency, etc., if he does not pay his way and is unable to meet the current demands of his creditors and has not the means of paying them in full as their claims mature. Other basis of arriving at insolvency have been adopted by other judges. My view is that the one quoted should not necessarily be followed in every case, each case depending upon the particular circumstances surrounding it. If I were asked to give my opinion of what should constitute insolvency, as applicable to business as in this Province, I would say that insolvency exists where a debtor could not pay his debts in full on a fair and reasonable (not a forced) realization of all his assets. I think you will appreciate the fact, more especially in view of the present stringency, that it frequently happens that business firms, who have ample assets and would be perfectly solvent and able to pay their debts if given time, have sometimes asked for an extension from creditors for different unavoidable and unforseen causes or reasons, but quite justifiable under the circumstances.

"The fact that all the debtor's assets are covered by mortgage or other security is not alone sufficient to render him insolvent, as equities of redemption or the right to redeem are tangible assets which might be sold privately or under execution for enough to pay all his debts.

"To constitute the provisions of a fraudulent preference, the essentials are: First, that there must be a debtor, a creditor who has been preferred, and other creditors who have a grievance, as a result of such preference. The preference must have been created by the debtor at a time when he was in insolvent circumstances, or unable to pay his debts in full, or knew himself to be upon the eve of insolvency.

"The weight of existing authority leans to the view that in order to work a fraudulent preference to a creditor there must be a concurrence of intention on the part of both debtor and creditor—that is, an intention on the part of the debtor to give and on the part of the creditor to get a preference. Circumstantial evidence leading to that conclusion, in the absence of direct affirmative evidence (which is seldom obtainable), will be admitted. Such circumstantial evidence may be, and generally is, the proof of knowledge on the part of the preferred creditor, of the debtor's insolvency; or the proof of pressure exerted by the preferred creditor upon the debtor.

"Our 'Creditor's Relief Act,' which provides that all creditors may get in on an even footing in the case of goods seized and being cold under execution, meets the case of a confession of judgment and execution thereunder. There are, however, quite a number of valid transactions that may be entered into by an insolvent debtor, but these are specifically set out in the provisions of the said Act.

"For bona fide sales or payments made in the course of trade or business to be unimpeachable, there must be an entire absence of intent to prefer. In one case it was held that a payee in good faith meant a payee without any notice that any fraud or fraudulent preference was intended. This was qualified to some extent in another leading case, wherein it was held that if a creditor takes the whole or substantially the whole of the property of his debtor in payment of a past due debt, knowing that there are other creditors, he cannot be said to be acting in good faith.

"Payments of money to a creditor are not open to attack as preferences, and it is not necessary that they should be shown to be bona fide unless they come within the provisions of the 'Winding Up Act,' which makes any payment made by a company within thirty days of the presentation of a petition for winding up avoidable, or of the 'Creditors Trust Deeds Act,' whereby a payment of money made within ten days of an assignment is void. I think these two provinces should be made to coincide.

"The 'Bulk Sales Act' provides for the sale of goods for any trader in bulk, even if the said trader be in insolvent circumstances. But the provisions of the Act must be strictly adhered to. Briefly, such a sale of goods in bulk can only take place when the following conditions are fully complied with:—

"(1.) The vendor or his agent must make and deliver to the purchaser a statutory declaration setting out the names and addresses of all creditors whose claims exceed $50.00, together with the amount owing from each, before any payment or security is given or made by the purchaser."