Friday, July 8.

SECOND DIVISION.

BANK OF SCOTLAND *v.* FAULDS.

Bankrupt—Composition—Discharge—Illegal Preference. A having become insolvent entered into an arrangement with his creditors to pay a composition of 7s. 6d. in the pound. It was a condition of this agreement that the creditors should have power, if they saw fit, to make an additional call of 2s. 6d. in the pound. A was discharged, and the additional call was not insisted in. Between the date of the agreement and the discharge he made an arrangement with Rowan & Co., his largest creditors, and who had been parties to the composition contract, which resulted in his granting in their favour a promissory note for the amount of the 2s. 6d. effeiring to their claim. Rowan & Co. discounted with the Bank of Scotland, who were cognisant of the circumstances under which the note was granted. *Held*, in an action for the amount of the promissory note at the instance of the Bank against A, that the transaction constituted an illegal preference, and that the Bank, as coming in place of Rowan & Co., could not recover.

This was an action brought by the Governor and Company of the Bank of Scotland against Robert Faulds junior, wright and waggon-builder in Glasgow, concluding for the sum of £1732, 3s. 6d., contained in a promissory note by the defender, dated 28th July 1862, payable thirty months after date, to Messrs Rowan & Co., iron merchants, Glasgow; and blank indorsed by them, with interest at the rate of five per cent. from 31st January 1865 till payment. The circumstances in which the promissory note in question was said to have been granted were the following:—In July 1862 the defender, having become embarrassed in his circumstances, entered into a private arrangement with his creditors, whereby it was agreed that they should accept 7s. 6d. per pound on their respective debts, payable by bills at nine, eighteen, and twenty-four months, and whereby an additional composition of 2s. 6d. per pound was made payable provided a committee of the defender's creditors appointed for the purpose should, at the end of twenty-four months, determine that he should pay the same. In respect of this composition arrangement, the defender was formally discharged by discharge dated 19th November 1862, and subsequent dates, subject to the creditors' right to the additional 2s. 6d. per pound in the event of its being determined by the committee of creditors that the same should be paid. The committee of creditors ultimately determined that the additional 2s. 6d. should not be paid, and in the circumstances the body of creditors received nothing beyond the composition of 7s. 6d. per pound from the estate. Between, however, the date of the meeting of creditors when the composition was agreed to and the date of the formal discharge above referred to, the defender, at the request of Messrs Rowan & Co., who were his largest creditors, and who had been parties to the composition, granted them the promissory note libelled, which was in the following terms:—"Thirty months after date, I promise to pay to Messrs Rowan & Co., or order, within the office of the Bank of Scotland, £1732, 3s. 6d. sterling (being my extra contingent 2s. 6d. per pound, with interest), value received." Messrs Rowan & Co. discounted the note with the Bank of Scotland, who, it came to be conceded, were through their agents cognisant of the whole circumstances. The defence maintained was—(1) That the obligation in the note was contingent upon the 2s. 6d. per pound being found payable (2) that if not contingent, as it was meant to be, it constituted an illegal preference. There was no plea stated in the outset raising this latter defence, but the point was argued before the Lord Ordinary, and that plea was added in the Inner House.

The Lord Ordinary (ORMIDALE) pronounced the following interlocutor:—

"*Edinburgh, 8th March* 1870.—The Lord Ordinary having heard counsel for the parties, and considered the argument and proceedings, including the proof, Finds it proved that the defender, having become embarrassed in his circumstances, entered in July 1862 into a private arrangement with his creditors, whereby it was agreed that he was to pay to them, and that they were to accept of 7s. 6d. per pound on their respective debts, payable by bills, at 9, 18, and 24 months, after the 28th of July 1862, and whereby an additional composition of 2s. 6d. per pound should be payable, provided a committee of the defender's creditors, appointed for the purpose, should, at the end of 24 months from said 28th July 1862, determine that he should pay the same: Finds it also proved that, in respect of said composition arrangement, the defender was formally discharged by his creditors, conform to discharge No. 50 of process, subject to their right to said additional 2s. 6d. per pound on their respective debts, in the event of its being determined as aforesaid that the same should be paid: Finds it also proved that it has been determined by said committee of the defender's creditors that said additional 2s. 6d. per pound on their respective debts is not payable by him: Finds it also proved and admitted in the record that the promissory note libelled, although dated 28th July 1862, was not granted by the defender to the payees Messrs Rowan & Co. till in or about November of that year, being some time after the defender's said composition arrangement had been acceeded to by all his creditors: Finds it also proved that said promissory note was blank indorsed for value by Rowan & Co., the payees, to the pursuers, who are now the holders thereof: Finds it also proved that Messrs Rowan & Company were parties to said composition arrangement between the defender and his creditors, but that the pursuer and the Bank of Scotland were not: Finds also that it has not been proved that the pursuer or the Bank of Scotland were parties to, or at the time the promissory note libelled was indorsed to them in the knowledge of any arrangement or understanding, whereby, as averred by the defender, the said promissory note should only be payable by him in the event of the foresaid additional 2s. 6d. per pound becoming payable to all his creditors: Finds also that there is no averment or plea by the defender in the record to the effect that the promissory note libelled was stipulated for by Messrs Rowan & Co., the payees, or any other party, or was *granted* by the defender as an inducement to them to accede to his composition arrangement: Finds, in the foregoing circumstances, that the pursuer must in law be held to be an onerous and *bona fide* holder of the promissory note libelled, and is entitled to

recover payment of its contents from the defender: Therefore finds the defender liable to the pursuer in terms of the conclusions of the summons, and decerns accordingly: Finds the pursuer entitled to expenses, allows an account thereof to be lodged, and remits it, when lodged, to the auditor to tax and report.

"*Note.*—Two pleas were maintained in argument by the defender, in answer to the pursuers' demand in this action, viz.—(1) That the promissory note libelled being made dependent upon a contingent event which has never happened, cannot be enforced against him; and (2) that at any rate, the promissory note being of the nature of an illegal preference in favour of one of the defender's creditors to the prejudice of himself and his other creditors, he is not bound to pay it.

"In regard to the first of these pleas, which depends entirely upon the terms of the promissory note itself, the Lord Ordinary thinks it is ill-founded. The note no doubt bears, parenthetically, that its amount is his, the defender's, contingent extra 2s. 6d. per pound, with interest; but this does not make its payment depend upon any contingency. It appears to the Lord Ordinary to be merely a description of the debt, and nothing more. Accordingly, the note which bears to be dated 28th July 1862 is payable absolutely and unconditionally 'thirty months after date.' Nor is there any extrinsic writing, or anything else, to which the pursuer, or the Bank he represents, was a party, which can be held to qualify the absolute and unconditional terms of the note itself. The defender, it is true, depones that he told Rowan at the time he gave him the note that he would not come under any obligation to pay him any money if his other creditors were not to get the same; but there is nothing to corroborate this parole statement of the defender, which therefore the Lord Ordinary could not hold to be sufficient to affect the terms of the note itself, according to its true construction, even in a question with Rowan & Company, and much less in a question with the Bank of Scotland, who were no parties, by their agent in Glasgow or any one else, to any understanding or arrangement between the defender and Rowan. Neither does the Lord Ordinary see how the knowledge of the Bank, or what may be taken as the same thing, of Mr Neilson, their agent in Glasgow, of the nature of the composition arrangement entered into between the defender and his creditors on the 28th of July 1862, can make the promissory note in question, as regards its payment, depend upon a contingency, if he be right in holding that, according to its terms, its payment is absolute and unconditional, and in no way dependent on any contingency whatever.

"But then, secondly, the defender pleaded at the debate before the Lord Ordinary, that payment of the promissory note is not enforcible against him, in respect of its being of the nature of an illegal preference to one of the defender's creditors over the others. The Lord Ordinary does not think the evidence supports this plea. The proof shows that the defender's composition arrangement was entered into on the 28th July 1862; that all of his creditors had acceded to it by the middle of October thereafter, and that, in consideration of such arrangement, a regular deed of discharge has been granted to him. The proof also shows that it was not till about the middle of November 1862, some time after the defender's composition contract had been agreed to by all his creditors, that the promissory note in question was granted by him to Rowan & Company. Nor is there a scrap of evidence to the effect that it had been stipulated by Rowan & Company before, or at the time of the defender's composition arrangement, that he should give them the promissory note in question, as preference over his other creditors. The Lord Ordinary therefore could not hold that the promissory note is tainted with illegality, as being of the nature of an illegal preference in a question even with Rowan & Company, and certainly not in the present question with the Bank of Scotland; *Clark* v. *Clark*, 5th January 1869, 7 Macph. 335. It seems, indeed, to have been an afterthought altogether of the defender to set up the plea of illegal preference, for no such plea, or any corresponding averment, is to be found in the record."

The defender reclaimed.

WATSON and PATERSON for him.

MILLAR, Q.C., and DEAS in answer.

At advising—

LORD COWAN—Two defences to this action on the promissory note libelled are stated by the defender—(1) that the obligation thereby constituted was contingent, being dependent on a condition which has not been purified, and which was known to and appeared *ex facie* of the promissory note when indorsed to the pursuer and the bank; and (2) that, assuming the obligation to be absolute, it constituted an illegal preference, and is not enforceable.

The first ground of defence, had the claimant for this debt been Rowan & Co., might have been availably pleaded, at all events to the extent of £1293, 15s., being the amount of the fourth instalment on the debt ranked at 2s. 6d. per pound. But on the assumption that the findings in the Lord Ordinary's interlocutor are correct—viz., that the note was indorsed to the Bank "for value," and that their managers had no knowledge of the composition arrangement or of any understanding or arrangement under which the amount might not be payable by the defender,—I agree that this defence cannot be sustained. Were the opposite assumption—viz., that the Bank are not in the position of onerous *bona fide* indorsees, and are in no better position than Rowan & Co.—taken to be the true condition of this question, this first defence would have been more formidable, and would have required more careful consideration than it is necessary to give to it,—the facts in evidence in regard to the Bank's position in receiving this promissory note from Rowan & Co. being the same which bear on the other ground of defence.

The material question on which the liability of the defender depends is, whether there are facts established by the proof, written and parole, to support the plea of illegal preference which the defender has been permitted to add to the record. And this depends essentially upon two inquiries as to the import of the evidence—(1) whether the pursuer, as representing the Bank of Scotland, is to be identified in this matter with Rowan & Co., in whose name the claim on the defender's estate was made; and (2) whether, if these parties are to be identified in this matter, there was not an illegal preference obtained by Rowan & Co. by means of this promissory note.

As to the first of these inquiries, it seems to me established that nothing was done by Rowan & Co., as regards their accession to the discharge of the bankrupt on composition, without the knowledge and acquiescence of the Bank manager.

The bills for £10,300, which were the subject of the ranking on the defender's estate in the name of Rowan & Co., were in the hands of the Bank, to whom they were indorsed, and who were therefore the creditors by whom or with whose concurrence alone the debt could be effectually claimed. Rowan & Co., as the drawers, might have ranked for their relief in the event of being subjected in payment of the bills by the Bank. But it is in evidence that Rowan's affairs had also become embarrassed, and that they had become bankrupt through these very bills held by the Bank. Hence it is that Mr White, who acted for the defender, states that he was in constant communication with the Bank relative to these bills, both before the meeting of the creditors in July and subsequently thereto, until the pursuer's final discharge subscribed by Rowan & Co. on 19th November 1862. Indeed, in my view of the proof as to this matter, there was not a step taken by Rowan, or by Mr White as acting for him, with regard to these bills that had not the concurrence of Mr Nelson, the bank manager. Unless this had been the case the debt constituted by the bills could not have been effectually discharged by Rowan & Co., as there must still have been, after payment of the composition, a claim competent to the Bank against the bankrupt for the remaining amount of the bills. Accordingly the defender, when applied to by Rowan, addressed to him the letter of 5th August 1862, in which he undertook, in order to facilitate Rowan's effecting an arrangement with his creditors, "to give the Bank of Scotland composition bills for 10s. per £, with interest added." This letter was communicated to the Bank manager, and the bill now sued on, when granted, was given by Rowan & Co. to the Bank, who also received the other three bills granted by the defender for payment of the composition of 7s. 6d. by instalments, which those of his creditors present at the meeting of 25th July 1862, had agreed to accept. It is needless, however, to prosecute further this inquiry, for the defender's counsel at the debate felt the evidence too strong to be disputed, and, with a just appreciation of the true matter for argument, grappled with the defence of illegal preference on the same footing as if it had arisen with Rowan & Co.

The question of liability thus resolves into the second inquiry, whether the granting and receiving of this note took place in such circumstances as to vitiate the transaction, and render the obligation not enforceable in law. That the existence of this bill was kept secret, and not known to the other creditors of the defender, is certain. Even Mr White, who acted for the defender and as trustee for his creditors under the conveyance to him in security for the composition bills, states that he was not aware, in December 1862, "that this bill existed, and that he did not know of its existence till some time in 1865." And that the granting and receiving of the obligation placed the Bank, through Rowan, in a more favourable position than the other creditors, is equally undoubted. The composition agreed to was 7s. 6d. per £, payable by three instalments, at six, twelve and eighteen months, and for these three instalments composition bills were granted to all the creditors. But it was farther stipulated that an additional dividend of 2s. 6d., payable in twenty-four months, should be paid, provided a committee of the creditors named by the meeting found that the estate of the defender at the time could afford to pay that additional dividend. No interest whatever was exigible on any of these instalments, and certainly none on the contingent one, should it be declared payable, but which, as found by the Lord Ordinary's interlocutor, was determined by the committee not to be exigible. Now, when in addition to the three first bills the bill now sued on was granted by the defender, not merely for the fourth instalment of 2s. 6d., which never became exigible, but for interest on the whole of these instalments,—the effect certainly was to place this creditor in a situation of having obtained a preference over the other creditors to the large amount of £1732, 3s. 6d. This sum was composed of £1293, 15s., being the fourth instalment of 2s. 6d., to which the other creditors never became entitled, and from £400 to £500 of interest on the successive instalments. This, however, is said to have been merely a gratuitous boon conferred on the Bank, not constituting an illegal preference, and therefore not to be regarded and treated as such.

What constitutes an illegal preference in such a question as the present is explained by Mr Bell in his Commentaries, vol. ii, p. 504-505. He says, in treating of discharge of the debtor on a composition contract, whether under the statute or by private agreement, "One essential condition implied is that there shall be *perfect equality* among the creditors;" that "a creditor who discovers the fraud, although he may receive the full proportion which from the first he expected, may take exception to the unfair execution of the contract, or may reduce it after it has taken effect;" and that "this is a necessary consequence of what has always been judicially regarded as a fraud upon the creditors, as it does not appear that they would have agreed to the composition contract at all had they been aware that, under cover of a fair and equal agreement, preferences to particular creditors were intended;" and he farther adds that any agreement, even by the debtor to secure a creditor's assent to pay to him a consideration out of his future acquisition, is also against the true spirit of the contract. And for this last doctrine he refers to Lord Kenyon's observations in *Cockshott* v. *Bennet*. I cannot doubt, therefore, that there was here constituted an illegal preference; assuming always that this bill was given and received to secure the assent of Rowan & Co., and of the Bank as identified with them in this matter, to the composition contract under which the bankrupt was discharged.

The defender's counsel urged that the agreement to accept the composition by all the creditors had been intimated, if not before, at least soon after August 1862, when the letter already referred to agreeing to grant this bill was written to satisfy the Bank in their negotiations with Rowan. And hence it was maintained that this bill, although dated 28th July 1862, having been truly granted in November 1862, must be viewed as the act of the bankrupt after he had secured his discharge and was a free man. I apprehend this to be an entire mistake. It may be that the creditors had generally agreed to grant a discharge to the defender on receiving the composition bills at the time alleged; but the transaction was not completed until the bills were granted and the discharge subscribed by the creditors respectively. Now, the signatures to the deed of discharge were severally attached, according to Mr White's evidence, between 15th

October 1862 and 31st January 1863, Rowan and Co.'s signature being on 19th November 1862. I cannot doubt that, until this discharge was subscribed, it was in the power of any one or all of the creditors, on hearing of the preference secured by the Bank through Rowan & Co., to have withdrawn their concurrence. The vital point, in my apprehension, is whether, prior to the execution of the discharge by the creditors, this promissory note was granted to and accepted by Rowan & Co. for the debt of the Bank. And of this there is no doubt whatever upon the evidence, parole and documentary. Rowan has not been examined, for what cause does not appear; but the Bank's manager, Mr Nelson, was, and he says that he received the bill from Mr Rowan in November 1862, that he got it about the middle of November, and that he was quite aware of the terms of the composition before that date: And in cross-examination he farther states that he received the letter of 5th August 1862 along with the bill, and that the letter and the bill were sent to him by Rowan in a letter dated 13th November 1862. Hence it is clear that, before the discharge was subscribed by Rowan & Co. on 19th November, the Bank's concurrence in that act of Rowan was secured by this obligation having been granted; and only then it was that Rowan finally assented to this arrangement by signing the deed. The conclusion at which I arrive is, that the assent of the creditors in this debt was secured by the preference thus conferred, and this, I apprehend, is sufficient to stamp the transaction as an illegal preference. And I do not think that the record, as it stands, opposes any obstacle to our now pronouncing decree of absolvitor.

The LORD JUSTICE-CLERK and LORD BENHOLME concurred.

LORD NEAVES agreed with the Lord Ordinary's view, but proceeded very much upon the structure of the record, and the absence of any averment of illegal preference.

The defender was only found entitled to expenses from the date of the Lord Ordinary's interlocutor.

Agents for the Pursuers — Tods, Murray, & Jamieson, W.S.
Agents for the Defender—J. & A. Peddie, W.S.

Saturday, July 9.

FIRST DIVISION.

HAMILTON *v.* HAMILTON AND OTHERS.

General Police (Scotland) Act 1862—*Burgh-Clerk. Held* that the clerk to the police commissioners of a burgh constituted under the General Police (Scotland) Act 1862 (25 and 26 Vict. c. 101), is not necessarily to be regarded as removeable at the pleasure of the commissioners, and proof allowed as to the terms of the appointment to the office, and the understanding of parties at its date.

The pursuer of this action, Mr Gavin Hamilton, writer in Glasgow, was appointed clerk to the Dunoon Police Commissioners in the year 1868 "at a salary of £40 for the first year." Dunoon is a burgh within the provisions of the General Police (Scotland) Act 1862, and the pursuer's appointment as clerk was made in terms of the 67th section of that statute. At a meeting of the Police Commissioners of the burgh on 17th January 1870, a motion was carried removing the pursuer from his office of clerk, and at a subsequent meeting Mr David Gray, writer in Glasgow, was appointed in his place. The pursuer thereupon raised this action against the Police Commissioners, in order to have it found and declared that he as clerk, duly appointed under the provisions of the Police Act of 1862, held his office *ad vitam aut culpam*, and that it was *ultra vires* of the Commissioners to supersede him without reasonable ground, and without proving *culpa* on his part. The summons further craved reduction of the minutes and resolutions under which his removal from office was effected, and also prayed to have the Commissioners interdicted from carrying out said minutes and resolutions. The first plea in law for the defenders was as follows:—"Under the 64th section of the Act 25 and 26 Vict., cap. 101, the pursuer was removeable from his office of clerk at the pleasure of the Police Commissioners." They also pleaded that the appointment, as proved by their minute-book, bore to be and was for one year only, and that in any event the pursuer's conduct while in office was such as to justify his removal. Two of the defenders, Bailies Stirling and Somerville, put in separate defences to the effect that, having disapproved of and opposed in every way the proceedings of the Commissioners complained of by the pursuer, they now offered no opposition to the conclusions of the summons, and disclaimed all liability for any expense that might be incurred.

A debate took place in the Outer House on the first plea in law for the defenders.

The Lord Ordinary (MURE) pronounced the following interlocutor:—"The Lord Ordinary having heard parties' procurators, and considered the closed record, repels, *hoc statu*, the first plea in law for the defenders, the Commissioners of Police, and, before further answer, allows both parties a proof of their averments, and to each a conjunct probation, and appoints the proof to be taken before the Lord Ordinary on a day to be afterwards fixed.

"*Note.*—After considering the provisions of the General Police Act, which are in many respects neither consistent nor explicit in regard to the conditions under which certain of the offices created by it were to be held, the Lord Ordinary, as at present advised, is not prepared to hold that clerks appointed to discharge the duties required of the clerk appointed under section 67 of the statute are removeable at the pleasure of the Commissioners in the summary way in which the pursuer appears to have been removed. If, however, the defenders can show, as alleged by them, that the pursuer's original appointment was only for one year, and thereafter renewed *ad interim* merely, of which there is at present no satisfactory evidence, that may place the defenders in a different position in the above respects. If, on the other hand, it should be decided that the pursuer's appointment as clerk was one *ad vitam aut culpam*, the Lord Ordinary does not think he would be warranted in holding, without inquiry, and assuming the facts set forth in the defence to be true, that the grounds upon which it is alleged that the defenders acted in removing the pursuer were insufficient to justify the removal. Before, therefore, disposing of the abstract question of law raised in the record, the Lord Ordinary has deemed it necessary to have the facts on which parties are at issue ascertained."