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 March 27.

IN THE MATTER OF THE BAIE DES CHALEURS RAILWAY COMPANY'S SCHEME OF ARRANGEMENT WITH ITS CREDITORS.

*Insolvent railway—The Railway Act, 1903, sec. 285—Unsecured creditor not assenting to scheme of arrangement—Opposition to scheme by another railway whose rights were sought to be affected thereby—Confirmation of scheme where creditors of same class receive unequal treatment.*

An unsecured creditor who does not assent to a scheme of arrangement filed under section 285 of *The Railway Act, 1903*, is not bound thereby.

2. It is however a good objection to such scheme that it purports in terms to discharge the claim of such creditor.
3. By a scheme of arrangement, between an insolvent railway company and its creditors, it was proposed to cancel certain outstanding bonds and to issue new debentures in lieu thereof against property that was at the time in the possession of the trustees for the bondholders of another railway company. Part of such new debentures were to be issued upon the insolvent company acquiring the control of certain claims, bonds and liens against the railway; and part upon a good title to the railway being secured and vested in the trustees for the new debenture holders. The railway company, the trustees for whom bondholders were in possession of the railway objected to the scheme of arrangement. Its rights therein had not been determined or foreclosed.

*Held*, that the railway company was entitled to be heard in opposition to the scheme, and that the latter was open to objection in so far as it purported to give authority to issue a part of the new debentures upon acquiring the control of such claims, bonds and liens, and without any proceedings to foreclose or acquire the rights of such railway company in the railway.

4. No scheme of arrangement under *The Railway Act, 1903*, ought to be confirmed if it appears or is shown that all creditors of the same class are not to receive equal treatment.

APPLICATION by the directors of the Baie des Chaleurs Railway Company for the confirmation of a scheme of arrangement with its creditors, filed in this court in pursuance of section 285 of *The Railway Act, 1903*.

The facts upon which the application was based are set out in the reasons for judgment.

March 11th, 1905.

The argument of the motion to confirm the scheme of arrangement was now proceeded with at Montreal.

The parties entitled to be heard on the motion were represented by counsel as follows:—

*W. D. Hogg, K.C.*, for the Baie des Chaleurs Railway Company; *T. C. Casgrain, K.C.*, and *A. C. Casgrain*, for Galindez Bros., Andrew Haes, A. Campbell, Brown & Wells, the trustees for the Bondholders of the Atlantic and Lake Superior Railway Company, and the Royal Trust Company of Montreal; *F. S. MacLennan, K.C.*, and *J. J. Meagher*, for the Atlantic and Lake Superior Railway Company, Charles N. Armstrong, and Hon. J. R. Thibeaudeau; *N. K. Laflamme*, for Charles Veilleux; *E. N. Armstrong* for himself, and J. Riopel, and Estate Nash; *C. A. Barnard* for J. Beattie; *H. Trudel* for F. D. Shallow; *J. L. Perron, K.C.*, for J. A. Thivierge.

*W. D. Hogg, K.C.* and *T. C. Casgrain, K.C.*, in support of the motion, argued that so far as the objections of the Atlantic & Lake Superior Railway Company to the scheme were concerned they ought not to be heard because that company had no *locus standi* in the matter. The property of the Baie des Chaleurs Railway Company did not pass to that company, because the Act under which the transfer of the railroad purported to be made was not complied with, and no Parliamentary sanction for the transfer was or could be set up. The property of the company could not be sold or transferred simply by a resolution of the Board

Although the Atlantic & Lake Superior Railway Company have possession of the eighty miles of railway in question, they are not the owners. By this scheme of arrangement we seek to obtain possession, and are

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entitled to it, as the transfer to the Atlantic & Lake Superior Railway Company was incomplete and illegal.

As to the unsecured creditors who do not assent to the scheme, there is no valid reason why the scheme should not be confirmed by reason of their objection. They are not bound by it in any event when they decline to assent to it. *In re East & West India Dock Co.* (1); *In re West Cork Railway Co.* (2); *In re Cambrian Rys.* (3); *In re Potteries, Shrewsbury and North Wales Ry. Co.* (4); *In re Bristol and North Somerset Ry. Co.* (5); *Stevens v. Mid Hants Ry. Co.* (6); *Stevens v. Cork and Kinsale Junction Ry. Co.* (7); *In re Somerset and Dorset Ry. Co.* (8); *In re East and West Junction Railway Co.* (9).

So long as a scheme of arrangement is reasonable it ought to be confirmed so as to bind those assenting to it. The bondholders feel that this scheme is the best possible arrangement in the interest of the railway and the creditors.

The bondholders have a title to the bonds against the world, having acquired them for value and in good faith. *Cotebrooke on Collateral Securities* (10); *Jones on Pledges* (11); *American & English Ency. of Law* (12); *Cook on Corporations* (13); *Ritchie v. Burke* (14); *In re Olathe Silver Mining Co.* (15); *West Cumberland Iron & Steel Co. v. Winnipeg & Hudson's Bay Ry. Co.*

*F.S. Maclellan, K.C.* and *E. Armstrong*, for the Atlantic & Lake Superior Railway Company, *contra*, contended that the Baie des Chaleurs railway had

(1) 44 Ch. D. 38.

(2) Ir. R. 7 Eq. 96.

(3) 3 Ch. App. 278.

(4) 5 Ch. App. 67.

(5) L. R. 6 Eq. 448.

(6) 8 Ch. App. 1064.

(7) Ir. R. 6 Eq. 604.

(8) 21 L. T. 656.

(9) L. R. 8 Eq. 87.

(10) 2nd ed. p. 72 sec. 43.

(11) 2nd ed. pp. 89, 95.

(12) 2nd ed. vol. 22 p. 896.

(13) 5th ed. vol. 3 sec. 763, pp. 1984

*et seq.*

(14) 109 Fed. Rep. at pp. 16 and 20.

(15) 27 Ch. D. 278.

(16) 6 Man. R. 388.

become the property of the Atlantic & Lake Superior Railway Company by deed of sale in 1894, and that all the rights and property of the former, including its bonds, passed to the latter company under such deed. Furthermore, the latter company was put in possession of the former company's railway in 1895, and has retained possession ever since. The Atlantic & Lake Superior Railway Company was confirmed in its possession by 1 Edw. VII., c. 48, and authorized to operate and maintain it. Therefore, the Baie des Chaleurs Railway Company is not entitled to a confirmation by this court of a scheme of arrangement providing, among other things, for a resumption of possession of the railway by such company.

There have been no proper proceedings taken by the Baie des Chaleurs Railway Company for a revocation of the sale. (C.C.L.C. Arts. 1478, 1980, 1981.)

Under such circumstances, the scheme of arrangement is a nullity, and ought not to be confirmed by the court. (In re *Letterkenny Ry. Co.* (1); in re *Empire Mining Co.* (2); in re *Alabama &c. Railway Co.* (3); in re *English &c. Chartered Bank* (4).

As to Galindez<sup>r</sup>Bros., and their right to be heard on this motion, the pledgees of bonds are not the owners and have no *locus standi* here. There was no sale to them of the bonds, but they were only deposited with them as collateral security. *Addison on Contracts*, (5); *Jones on Pledges* (6); *Paget on Banking* (7); *Jerome v. McCarter* (8); *Union Cattle Co. v. International Trust Co.* (9); *Colebrooke on Collateral Security* (10); *West Cumberland Iron and Steel Co. v. Winnipeg and Hudson's Bay Ry. Co.* (11); 26 *Am. & Eng. Ency of Law* (12).

(1) Ir. R. 4 Eq. 538.

(2) L. R. 44 Ch. D. 402.

(3) [1891] 1 Ch. 213.

(4) [1893] 3 Ch. 385.

(5) 10th ed. pp. 752, 761, 762.

(6) 2nd ed. secs. 304, 603, 716.

(7) p. 273.

(8) 94 U.S. 734.

(9) 149 Mass. 492, 501.

(10) 2nd ed. secs. 93, 103.

(11) 6 Man. Rep. 388.

(12) 2nd ed. p. 903.

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Galindez Bros. not being registered as holders of the stock of the railway company, but being merely pledgees, could not vote upon the stock. *Jones on Pledges*, (1); *26 Am. and Eng. Ency. of Law*, (2); *Helliwell on Stockholders* (3).

*Mr. Hogg*, replied.

THE JUDGE OF THE EXCHEQUER COURT now (March 27th, 1905,) delivered judgment.

This is an application by the directors of the Baie des Chaleurs Railway Company for the confirmation of a scheme of arrangement with its creditors, filed in this court in pursuance of section 285 of *The Railway Act*, 1903.

The company was incorporated in the year 1882 by an Act of the Legislature of Quebec, 45 Vict. c. 53, with power to build and operate a railway from some point on the Intercolonial Railway in the vicinity of the Restigouche River to New Carlisle, or Paspebiac Bay, with the right of continuing the line to Gaspé Basin. The Act of Incorporation was amended in 1886 (49-50 Vict. c. 80). On the 2nd of January, 1889, the company issued first mortgage five per centum coupon bonds to the extent of four hundred and nine thousand four hundred pounds sterling, on which no interest has ever been paid. It is said that the whole of these bonds are now in circulation, and constitute a liability of the company; but that with only trifling exceptions they are held as security for certain claims and advances.

By an Act of the Parliament of Canada, 54-55 Vict. c. 97, the Baie des Chaleurs Railway was declared to be a work for the general advantage of Canada; and it was also declared that thereafter the company

(1) 2nd ed. secs. 441, 442, 443.

(2) 2nd ed. p. 1006.

(3) Secs. 219, 367.

should be subject to the legislative authority of the Parliament of Canada. These declarations were followed by a number of provisions in respect to the company and its undertaking. On the 16th of April, 1894, the Baie des Chaleurs Railway Company having completed the railway from Metapedia to Caplin, a distance of about eighty miles, sold the railway and its appurtenances to the Atlantic and Lake Superior Railway Company, upon the terms set out in schedule "A" to the Act of the Parliament of Canada, 57-58 Vict. c. 63, by which, among other things, such agreement was confirmed. This agreement was to be "null and void and of no effect" if certain payments in cash, bonds and shares therein mentioned were not made within six months from the date of the agreement. Notwithstanding that such payments were not made within the time mentioned, or afterwards, the Baie des Chaleurs Railway Company put the Atlantic and Lake Superior Railway Company in possession of the railway and its appurtenances, and did what it could to enable the latter company to retain such possession. The Atlantic and Lake Superior Railway Company conveyed its property, including its rights and interests in the Baie des Chaleurs Railway, to trustees to secure its bondholders, and the trustees took possession of the railway, and were by an Act of the Parliament of Canada, 1 Edward VII., c. 48, authorized to operate it, to repair and renew the road-bed and bridges between Metapedia and Caplin, and to complete the railway from Caplin to Paspebiac, the cost of such repairs, renewals and completion to constitute liens upon the railway as therein mentioned. In the preamble to the Act last cited, it is stated that certain questions were then pending concerning the rights of the Baie des Chaleurs Railway Company and of its creditors and bondholders respecting the railway from

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Metapedia to Caplin, and concerning the rights of the Atlantic and Lake Superior Railway Company and its creditors and bondholders respecting the railway (including the above mentioned railway) from Metapedia to Paspébiac. And some at least, if not all of these questions, are still pending and undetermined.

The scheme of arrangement before the court is prefaced by a statement in explanation of its provisions. The scheme itself is divided into two parts intended however to operate as a whole. The first part of the scheme of arrangement purports to be made between the Baie des Chaleurs Railway Company of the first part and the holders of £409,400 0s. 0d. of first mortgage five per cent. coupon bonds of the said company, of the second part. These bonds amount approximately to two million dollars, with a large amount of interest accrued, and it is proposed to cancel them and to issue in lieu thereof five hundred thousand dollars of four per cent. first debentures; and one million dollars of five per cent. second debentures. On the face of matters that looks like a considerable reduction of the bonded debt of the company. But as has been stated, the outstanding bonds are in the main held as security for claims against or advances made to one or other of the two companies mentioned, or to persons interested therein. But these claims and advances do not amount to anything like the face value of such bonds.

Of the new debentures it is proposed to issue two hundred thousand dollars of first debentures and five hundred thousand of second debentures whenever the company, by acquisition or otherwise, is entitled to make use for its own purposes of all the rights appertaining to the claims against the trustees for the bondholders of the Atlantic and Lake Superior Railway Company which are now held by Messrs. Galindez Brothers, of London, and to the bonds of the said com-

pany also held by the said Galindez Brothers subject to an equity of redemption therein referred to. (See clauses 8 and 9 of the scheme of arrangement.)

Then it is proposed to make a further issue of two hundred thousand dollars of first debentures and two hundred thousand dollars of second debentures upon the surrender or conveyance to the Royal Trust Company (the trustees named in the scheme of arrangement) or to other trustees appointed in their place, of the privileged liens upon the first eighty miles of the railway from Metapedia towards Paspebiac, now held by the trustees of the Atlantic and Lake Superior bondholders and by the estate of Henry McFarlane & Son. (Clause 10.)

A further issue of one hundred thousand dollars second debentures is to be made upon a clear title, without charge or encumbrance, to at least the first eighty miles of the railway being properly conveyed to the trustees in trust for the debenture holders. (Clause 11.)

And it is proposed to issue the balance of one hundred thousand dollars of first debentures and of two hundred thousand dollars of the second debentures upon a clear title, without charge or encumbrance, to the hundred miles of railway now built from Metapedia to Paspebiac being properly conveyed to the trustees in trust for the debenture holders (Clause 12.)

Of the total issue of one million five hundred thousand dollars of debentures it is proposed to give the present bondholders first debentures to the amount of six and two thirds per centum of the face value of the bonds now held by them ; and twenty per centum of such face value in second debentures. The scheme of arrangement does not make it clear as to what is to be done with the balance of the new debentures ; but I infer that they are to be used to get in the liens men-

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tioned and to obtain a clear title to the railway and its appurtenances.

The second part of the scheme of arrangement purports to be made between the Baie des Chaleurs Railway Company of the first part, and the unsecured creditors holding claims against the company, of the second part. By the sixth paragraph it is provided that upon the confirmation of the scheme of arrangement the directors of the company, by resolution of the board, shall issue a sufficient number of fully paid preference shares to allot to each creditor an amount equal to one half of the claim of such creditor calculated in the manner thereafter set out. By the second paragraph of the scheme it is provided as follows:—"The claims of the creditors are hereby discharged and shall no longer be binding upon the company either as to principal or as to interest"

The confirmation of the scheme of arrangement is opposed by a number of creditors,—some holding security and others unsecured. It is also opposed by the Atlantic and Lake Superior Railway Company and by a number of the creditors of that company.

For the unsecured creditors it is objected that the scheme of arrangement purports to discharge the claims of unsecured creditors who do not assent thereto and who are unwilling to accept the preference shares offered. In reply to that objection it is argued that the scheme must be read in connection with the statute under which it is filed; that when confirmed it will be binding, and have the effect of an Act of Parliament, against and in favour of the company and those persons only who assent thereto or are bound thereby (*The Railway Act, 1903, s. 287, ss. 4*); and ordinary creditors who do not assent are not bound by the provisions of the scheme. I agree that ordinary creditors who do not assent to a scheme of arrangement

between an insolvent railway company and its creditors are not bound thereby. That appears to be well settled. It does not follow, however, that their rights may not in some way be affected or prejudiced by provisions in the scheme that become binding on the company. And the weight of judicial opinion appears to me to be that a scheme which purports, as this does, to discharge the claims of creditors, whether they assent or not, ought not to be confirmed. Such a provision is no doubt in excess of the powers given by the statute. But that in itself is an objection to the scheme of which any non-assenting creditor may take advantage (1).

Then with regard to the opposition of the Atlantic and Lake Superior Railway Company and of certain of its creditors, it seems to me that they are persons who under the Act are entitled to be heard (see s. 287, ss. 3). The Baie des Chaleurs Railway Company are not at present in possession of any part of the railway or property against which it is proposed to issue new debentures. The railway is, as has been stated, in the possession of and is being operated by the trustees of the bondholders of the Atlantic and Lake Superior Railway Company, and the rights of the company therein have not been foreclosed. So far as the scheme makes provision, as it does, for the issue of debentures upon the security of such property after a clear title thereto, without charge or incumbrance, has been properly conveyed to the trustees mentioned in the scheme, there is probably no objection to the scheme. The rights of the company will have to be foreclosed or acquired in

(1) See in re *Cambrian Railways Dorset Railway Company*, 21 L. T. *Company's Scheme*. L. R. 3, Ch. N.S. 656 ; In re *West Cork Railway* App. 278 ; In re *Bristol and North Company*, Ir. R. 7 Eq. 96 ; *Stevens v. Somerset Railway Company*. L. R. *The Mid-Hants Railway Company*; 6 Eq. 448 ; In re *East and West L.R. 8 Ch. App. 1064* ; and In re *Junction Railway Company*. L. R. *East and West India Dock Company*, 8 Eq. 87 ; In re *The Somerset and* 44 Ch. Div. 38.

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some legal way before that event can happen. But the scheme goes further than this. By the 8th, 9th and 10th clauses of that part of the scheme of arrangement, which is made between the company and the holders of outstanding bonds, it is proposed, as has been seen, to issue a portion of the new debentures upon the company acquiring control of certain claims and bonds therein mentioned; and to issue another portion of such new debentures upon the conveyance to the trustees mentioned in the scheme of certain privileged liens upon the railway. In that way it might happen that a large part of the new debentures would be issued, and become a charge upon the railway and its appurtenances before the rights of the Atlantic and Lake Superior Railway Company therein had either been acquired or foreclosed. And that it seems to me is a very reasonable and strong objection from the standpoint of the latter company and of its creditors.

There is no doubt some question as to what the true position of the latter company in respect of the property is, and possibly the affairs of both companies are so involved, and the mortgages and liens upon the property so considerable, that any right or interest, which the Atlantic and Lake Superior Railway Company has in the property, may in the end realize very little, if anything, for the company or its creditors. But these are questions that should be left to be determined in the usual way and by the ordinary processes of law. And nothing should be done in this proceeding to prejudicially affect any such rights as the Atlantic and Lake Superior Railway Company has in this railway and its appurtenances.

These are two only of a number of objections urged against the confirmation of the scheme of arrangement. It is also objected that the special general meeting of the company, at which the assent of the

ordinary shareholders to the scheme of arrangement was given, was irregular, and that certain shareholders were improperly prevented from voting at such meeting; also that those who held the outstanding bonds of the company, as security for claims and advances as mentioned, are not holders of such bonds within the meaning of section 286 of *The Railway Act, 1903*, and are not entitled to assent to the scheme without reference to or against the wishes of other persons having an equity or interest in such bonds. I do not find it necessary to deal with these objections, or to express any opinion as to their weight or sufficiency. There is however one matter to which perhaps some reference should be made. Messrs. Galindez Brothers, who have been mentioned, have a very large sum of money invested in the undertaking in question, and are the chief promoters of the present scheme of arrangement. Mr. Archibald Campbell is a creditor of the company for a sum stated at \$269,111 against which he holds bonds to the amount of £10.100, 0s. 0d. sterling. By an agreement made on the 10th of December, 1904, between Mr. J. D. Galindez, acting for his firm, and Mr. Campbell, the former undertook to give the latter \$20,000 nominal of first debentures and \$25,000 nominal of second debentures upon the basis of an issue of \$500,000 nominal of first debentures and \$1,000,000 nominal of second debentures. The understanding was to hold good whether the present scheme of arrangement went through or not. Mr. Campbell was to get the above number of bonds out of any solution upon the general line of the scheme and whenever Mr. Galindez got his debentures. In consideration of the foregoing Mr. Campbell undertook to give his assent both as to his bonds and as to his unsecured claims, as and whenever necessary or required to forward the scheme of arrangement then

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before the court, or any other. Mr. Campbell also agreed to discharge Mr. C. N. Armstrong and the Honourable J. R. Thibaudeau from any claim he had against them in connection with the Baie des Chaleurs Railway Company. By this agreement Mr. Campbell is, with reference to that part of his claim that is unsecured, put in a position differing from that occupied by other unsecured creditors. Whether or not that position is also better than theirs depends upon the value to be attached to the claims that he has agreed to discharge. But it is a part of the agreement that Mr. Campbell, in consideration of the bonds to be given to him, was to assent to the scheme. He is to get something more than the other unsecured creditors are to get; and as part, at least, of the consideration therefor he undertakes to give his assent to the scheme. That, it seems to me, constitutes an objection of the gravest character to any order to confirm the scheme. No scheme of arrangement under the Act ought to be confirmed where it appears or is shown that all creditors of the same class are not to receive equal treatment.

The application to confirm the scheme of arrangement in question here will be dismissed, but without costs. There is no fund out of which such costs can be paid. An order for costs against the company will, I understand, be of no advantage to those who have opposed the petition; and the case is not one in which the petitioners, the directors of the insolvent company, should be ordered to pay the costs.

*Judgment accordingly.*

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