The Corporate Trust Deed under Quebec Law: Article 2692 of the Civil Code of Quebec

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With the repeal of the *Special Corporate Powers Act* in 1994, the Quebec financing institution known as the corporate trust deed was left without a textual grounding in the *Civil Code of Quebec*. The single reference to the corporate trust deed in the new Code is an oblique one, touching only on form, and the absence of regulation has led some to declare the institution dead. The author argues to the contrary, noting that the new, general law of trusts in the *Civil Code of Quebec* is a more satisfying basis than was the exceptional regime under the *Special Corporate Powers Act* and the *Civil Code of Lower Canada*.

The author traces the development of the corporate trust deed from its inception as a creature of special, private bills through to its enactment as a general regime in a special statute for all corporations. The author notes the difficulty that Quebec courts and jurists had in applying the English concept of the trust to the civilian notions of ownership and mandate, especially with regard to the role of the trustee. Overall, despite its general nature for all corporations, the corporate trust deed remained very much an exception under the *Civil Code of Lower Canada*.

As they emerged from reform, trusts have become part of the *droit commun* and no longer stand in such opposition to the civilian tradition. In his canvassing of the essential elements of the new civilian trust, the author finds an affinity between the general regime and the special needs of the corporate trust deed. The author argues that this synergy is present not only with respect to new corporate trust deeds, but also with respect to outstanding deeds concluded prior to 1994 that now come to be interpreted under the *Civil Code of Quebec*. It is his submission that reform has brought about a synthesis of the once disparate elements of common-law terms, civilian traditions, and financing objectives within the confines of the Quebec trust.

Suite à l'abrogation de la *Loi sur les pouvoirs spéciaux des corporations*, l'institution financière connue sous le nom de fiducie corporative s'est retrouvé sans base légale en vertu du *Code civil du Québec*. La seule mention de la fiducie corporative dans le nouveau *Code* est une référence oblique, qui touche simplement à la forme. Cette absence de réglementation en a amené plusieurs à affirmer que cette institution était désormais défunte. L'auteur affirme le contraire, notant que le nouveau régime général du droit des fiducies constitue une base plus solide que ne l'était le régime exceptionnel prévu par la *Loi sur les pouvoirs spéciaux des corporations* et le *Code civil du Bas-Canada*.

L'auteur trace le dévcloppement de la fiducie corporative depuis ses débuts en tant que création de lois privées, à travers son adoption comme régime général dans une loi spéciale touchant les corporations. L'auteur souligne les difficultés rencontrées par les juges et les juristes québécois, qui se devaient d'appliquer le concept anglais de fiducie aux notions civilistes de propriété et de mandat, en particulier en ce qui a trait au rôle du fiduciaire. En définitive, et malgré sa nature générale applicable à toutes les corporations, la fiducie corporative est demeurée une exception sous le *Code civil du Bas-Canada*.

Suite à la réforme, les fiducies ont cessé de s'opposer à la tradition civiliste et font désormais partie du droit commun. En faisant le survol des éléments essentiels de la nouvelle fiducie civiliste, l'auteur note certaines affinités entre le régime général et les besoins spéciaux de la fiducie corporative. L'auteur affirme que cette synergie est présente, non seulement en ce qui a trait à la nouvelle fiducie corporative, mais également pour les documents fiduciaires rédigés avant 1994 qui doivent maintenant être interprétés en vertu du *Code civil du Québec*. Il conclut que la réforme a mené à une synthèse, à l'intérieur des paramètres de la fiducie québécoise, des éléments autrefois disparates qu'étaient la terminologie de *common law*, la tradition civiliste et les objectifs de financement.

* Of Lafleur Brown of Montreal. I am most grateful to my son Edward B. Claxton of Stikeman, Elliott, also of Montreal, for his most helpful and constructive editing. I also wish to thank Professor John E.C. Brierley, of McGill University, for his critical and helpful review. The opinions expressed are my own.

Revue de droit de McGill
To be cited as: (1997) 42 McGill L.J. 797
Mode de référence : (1997) 42 R.D. McGill 797

Introduction

The adoption of the *Civil Code of Quebec* ("C.C.Q."), on January 1, 1994, did not expressly resolve the characterization under Quebec law of the corporate trust deed, particularly the position of the trustee as the representative of the holders of the bonds, debentures or other securities. The C.C.Q. now calls such trustee the "*fondé de pouvoir*" of the debentureholders (2692).[1]

Prior to the adoption of the C.C.Q., and in the absence of general provisions of law permitting trusts, there was much litigation that hinged upon the characterization of the corporate trust deed, the charges thereunder and the position and the powers of the trustee. These problems originally arose because bonds and debentures and the trust deed securing them were authorized under special legislation, which sanctioned the form and the charges (often using language borrowed from the common law) but failed to characterize them under known concepts of civil law. Some of these problems were settled satisfactorily by the jurisprudence and, in my submission, will remain so settled under reform. The position of the trustee as representative of the bondholders was not adequately settled by the jurisprudence and remains unsettled following the adoption of the C.C.Q.

It is my position that the new law of trusts is not only adequate to embrace the corporate-trust-deed concept of financing (including financing by unsecured debentures), but it was designed with the corporate trust deed in mind, as a normal evolution of the law regulating these contracts.[2] As such the term *fondé de pouvoir* is broad enough to include "trustee" and, I submit, was intended to do so.

In this study I propose to examine the need and origin of debenture financing in Quebec. I will briefly review some seventy-five years of legislative experimentation with a variety of security devices; these experiments culminated in the adoption in 1914 of the statutory provisions of what became the *Special Corporate Powers Act* of 1925 ("S.C.P.A.").[3] The ensuing seventy-five years reflect a period of judicial interpretation and characterization of such devices in an attempt to reconcile them with the

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[1] Numbers in brackets in the text, without more, refer to article numbers of the *Civil Code of Quebec.*

[2] In *Security on Property and the Rights of Secured Creditors under the Civil Law of Quebec* (Cowansville, Que.: Yvon Blais, 1994) [hereinafter *Security on Property*], I devoted part of a chapter to the same subject (at 225ff.). Subsequently some senior practising lawyers have expressed opinions at variance with mine which have given me cause for further thought and analysis. Although my views remain essentially the same, it is this further analysis of this subject that underlies the present paper.

[3] These provisions were originally enacted as S.Q. 1914, c. 51, which added sections 6119*a-d* to *The Quebec Companies Act*, R.S.Q. 1909, title XI, c. III, sec. IIff. As amended from time to time, and in particular by *An Act respecting the Powers of Certain Companies to Issue and Re-Issue Bonds, Debentures and Other Securities*, S.Q. 1924, c. 63, these provisions became the *Special Corporate Powers Act* in 1925 (R.S.Q. 1925, c. 227). The successor act is now R.S.Q. c. P-16 [hereinafter S.C.P.A.]. To assist in an understanding of certain judicial interpretations, sections 27 to 31, as they existed in 1977 (the last integrated printing of the traditional sections), are reproduced in an appendix.

traditional Quebec civil-law concepts. This synthesis, which in many respects still provides the basis for the reconciliation of the contractual effects of a corporate trust deed with general principles of our civil law, was also, I submit, in part artificial and not entirely satisfactory. Finally, I intend to explain how the adoption of the C.C.Q. completed the evolution of this part of our law and permitted the continued use of the corporate trust deed securing bonds or debentures, while resolving the unsatisfactory constructions reflected by the jurisprudence.

A. The Corporate Trust Deed and Civil-Code Reform

It is most curious that with the wide reforms brought about by the adoption of the C.C.Q., the legislature failed to clarify the characterization of the position of the trustee under the corporate trust deed. Only four articles of the C.C.Q. make even tangential reference to the structures ordinarily found in the corporate trust deed. The first states that if the object of a trust is to secure the performance of an obligation, the trustee shall in case of default follow the rules respecting hypothecs (1263). The second asserts that a hypothec is valid if granted in anticipation of the creation of the obligation and makes express reference to lines of credit and the issue of bonds (2688). The third provides that a hypothec securing the payment of bonds shall, on pain of nullity, be passed before a Quebec notary public (2692). The fourth provides that immoveable hypothecs securing various obligations including those securing bonds or other evidences of indebtedness cannot be cancelled by the registrar as of right (3060).

Article 2692 makes the most direct reference. It provides:

> **2692.** L'hypothèque qui garantit le paiement des obligations ou autres titres d'emprunt, émis par le fiduciaire, la société en commandite ou la personne morale autorisée à le faire en vertu de la loi, doit, à peine de nullité absolue, être constituée par acte notarié en minute, en faveur du fondé de pouvoir des créanciers.
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> **2692.** A hypothec securing payment of bonds or other titles of indebtedness issued by a trustee, a limited partnership or a legal person authorized to do so by law shall, on pain of absolute nullity, be granted by notarial act *en minute* in favour of the person holding the power of attorney of the creditors.

The term *fondé de pouvoir* could mean a mandatary, a trustee or some other innominate form of representative having no particular characterization that the formal law identifies. It could also mean a trustee under the new Quebec law of trusts. The English expression does not convey any of these concepts, nor is the use of the term "power of attorney" in the context consistent with the ordinary meaning of these words.

Many, perhaps most, practitioners of commercial law feel that the particular characterization or qualification of a contract is unimportant. If the contract is clear and enforceable, why bother to fit it or force it into a given concept of our civil law. Unfortunately, the contract is not always clear. It does not always anticipate every development. The rights that could arise from it, particularly when third parties are involved, are sometimes in apparent conflict. Whether or not the result is enforceable,

and the way in which ambiguities or conflicts are resolved, may well depend on its basic characterization. Both the courts and academics invariably resort to characterization as a means of finding a solution. As Professor Madeleine Cantin Cumyn has said:

> The civil law is an organized system of interrelated principles, distinctions and definitions which aims at coherence and consistency between its constituent parts. To be effective, an innovation must find its proper place within the system. To accomplish this objeetive, civilians resort to the process of "qualification". "Qualification" seeks to determine the juridical nature of a legal relationship in order to classify it within pre-existing categories and to apply to it the rules of the chosen category.[4]

In this paper I have preferred to use the term "characterization" rather than "qualification".

1. Development of the Law of Hypothecs

The corporate trust deed providing for the creation and issue of bonds, debentures or other securities has been one of the most popular financial instruments in Quebec and elsewhere in North America in this century, and indeed earlier. Through a corporate trust deed, a corporation duly empowered to do so could, by way of exception to the general civil law, raise debt capital for its own corporate purposes, evidenced by bonds, debentures or other securities, secured by a fixed charge (a hypothec or pledge without possession) on any or all of its property, both immoveable and moveable and present and future, in favour of a trustee. A form of floating charge could also be included.

The corporate trust deed which enabled the granting of such security was first generally permitted in Quebec, not under the *Civil Code of Lower Canada* of 1866 ("C.C.L.C."), but through the adoption of provisions now found in the S.C.P.A. as exceptional statutory amendments to the Quebec companies law in 1914. Although there were a number of severe technical restrictions[5] under this statutory scheme, the principal limitation was that all four elements (a corporation, a debt evidenced by securities, a charge, in favour of a trustee) had to be present for the instrument to qualify under the statute.

The security device provided for under the S.C.P.A. proved so popular that reform introduced to the C.C.Q. itself analogous security devices as part of the general civil law of the province.[6] The C.C.Q. now permits any enterprise (1525(3)) or trustee

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[4] M. Cantin Cumyn, "The Trust in a Civilian Context: The Quebec Case" [1994] 2 J. Int. P. 69 at 70.

[5] See J. Tétrault, "Pitfalls Under Trust Deeds" in *Meredith Memorial Lectures 1976-77: Corporate Debt Financing* (Toronto: Richard De Boo, 1978) [hereinafter *Corporate Debt Financing*] 17.

[6] See *Commentaires du ministre de la Justice*, vol. 2 (Québec: Publications du Québec, 1993) at 1669, 1719-21 [hereinafter *Commentaires*]. The *Commentaires* also identify as a source of the reformed law the *Bills of Lading Act*, R.S.Q. c. C-53, now repealed, which permitted a pledge of inventory without possession. See also Y. Caron, "La loi des pouvoirs spéciaux des corporations et les recommendations de l'office de révision du Code civil" in *Corporate Debt Financing*, *ibid.*, 81.

carrying on an enterprise (2684) to secure any obligation (1371, 2661) by a hypothec or charge on moveable or immoveable property (2660), both corporeal and incorporeal (899), including a universality or class of property (2665), both present and future (2684), by way of fixed charge, or by way of floating charge (2715) and, where moveables are concerned, without dispossession or delivery of such property (2696). The principal limitations iinposed by the S.C.P.A. have been eliminated.

However, in implementing reform, the Government of Quebec replaced the operative provisions of the S.C.P.A. sanctioning the corporate trust deed by the single article of the C.C.Q. (2692) quoted above. The operative provisions expressly sanctioned, but did not define, the terms "trust deed" and "trustee" in relation to issues of debentures. This express legislative sanction for corporate trust deeds has now gone.[7] The S.C.P.A. has been amended to give the same rights to foreign corporations and to not-for-profit corporations. These provisions reflect an attempt to settle doubts that arose under the S.C.P.A. concerning the power of not-for-profit and foreign corporations to grant security. They also clarify the capacity of corporations that have the power to borrow and to hypothecate property, to assure that they can grant security by availing themselves of all the provisions of the C.C.Q. on hypothecs, including those only available to an "enterprise".

The standard form of security device is now the hypothec (2660).[8] Many security devices which were developed by statute prior to the adoption of the C.C.Q. to address particular lacunae in the C.C.L.C. have been abolished.[9] However, the basic principle that security devices are exceptional and can be employed only where the law expressly permits them has been preserved (2644).

With reform, the Quebec legal concept of trust (previously restricted to gratuitous and testamentary trusts) has also expanded (1260), permitting appropriation of property to a purpose (1260, 1261) and also to secure an obligation (1263). But neither the provisions related to trust nor any other provisions of the C.C.Q. make express reference to the corporate trust deed.

The remedies previously afforded by the corporate trust deed (through the enabling statute and practice) have also been made available for any hypothec. Today a hypothec of any kind on any type of property permits the holder, in the event of default, to obtain surrender of the property (2763) and elect to take possession for purposes of administration (2773), to take-in-payment (2778), to sell privately (2784), or

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[7] S.C.P.A., *supra* note 3, ss. 27 to 34 were repealed and replaced by the *Act Respecting the Implementation of the Reform of the Civil Code*, S.Q. 1992, c. 57, ss. 642 to 648 [hereinafter *Implementation Act*].

[8] Title retention devices employed as security for performance of an obligation, such as conditional sales, leases and *crédit bail*, may still be employed. One limitation remains: "[O]nly a person or trustee carrying on an enterprise may grant a hypothec on a universality of property, moveable or immoveable, present or future, corporeal or incorporeal" (2684).

[9] With reform, special provisions of the law permitting grants of security (pledges) without possession on inventories, on commereial machinery and equipment, and on forest products and crops and agricultural property, were all commuted to moveable hypothecs and the special provisions were repealed (see *Implementation Act*, *supra* note 7, s. 134).

to sell under judicial authority (2791). When accounts receivable or claims are hypothecated, a special procedure permits the creditor upon notice after default to collect directly (2743, 2745). A number of procedural restrictions and restraints on the uses of such remedies (which are not relevant to this paper) have been introduced, but, except for the taking-in-payment remedy, the remedies now available are essentially those which have historically been contracted for under the standard corporate trust deed.

2. Future of the Corporate Trust Deed

The reforms enacted by the C.C.Q. represent a radical departure from the former law, one that has caused some practitioners to observe that the use of the corporate trust deed is likely to diminish substantially, if not disappear. There is no doubt that the use of the corporate trust deed as a vehicle to afford a security interest will diminish. In financings which do not involve the holding of security interests by a wide number of creditors ("close-held" issues), the security interests achieved through the use of the corporate trust deed can now be achieved more simply and at lower costs by means of a direct hypothec in favour of a creditor, without the intervention of a trustee.

However, there remain a significant number of circumstances where the corporate trust deed will continue to be used. Thousands of such deeds are outstanding and will remain outstanding for many years. Furthermore, the corporate trust deed provides various advantages over a simple hypothec. First, no other vehicle can serve as well for the issue of bonds or debentures that are to be widely held, whether in registered or bearer form, and that are to be freely tradeable in the securities markets, either locally or throughout the world's financial markets. Second, even for close-held issues, the trust deed is a very common investment device employed in other jurisdictions and the most acceptable conventional device where the security exists or may in the future exist in several jurisdictions. Deeds in dual form are well known to the practitioner. This technique involves a deed executed in notarial form for Quebec and another before witnesses for the rest of Canada, both containing the different charging clauses required by the various provinces and a declaration asserting that all forms are to be treated as one and the same instrument. Third, in a close-held issue, it is easy to change one lender for another where a corporate trust deed is used, by a simple transfer of the bond from the former lender to the new one without any re-registration of security. This is often a cheaper and more flexible way to substitute creditors than are the alternatives. Fourth, frequently a bank acts as initial and lead lender, with the right to grant loan participations (after the security is initially put in place) to other banks or other financial institutions. The corporate trust deed is still recognized as the vehicle that can most easily achieve this objective, since each bank, as it becomes a lender, can receive a debenture for its share of the security interest and all debentures rank *pari passu*. Fifth, some institutional lenders have taken the view that, although they commit to invest in an entire issue of long-term debenture securities (usually to finance a major project such as a building), they must retain the right to resell their in-

vestment on the public markets if they find it necessary or desirable to do so. Thus they want their investment secured as of the date of the loan but in a marketable form.

Following reform, the issue of bonds, debentures and other securities pursuant to a corporate trust deed has continued, but under the general rules of contract and the common law of the province (the *jus commune*)[10] rather than under express legislation. Under reform, a good number of questions remain unanswered.

B. The Contract

It is important to understand the practical nature of the arrangement between the issuer, the trustee and the debentureholder. The arrangement is reflected by the trust deed, which is essentially a bilateral contract between the issuer and the trustee providing for the issue of the debentures. The debentureholder is never a party.

The use of a trust deed to create debentures that are to be widely-held is the preferred way of creating and issuing debentures and has many advantages over other methods. First, if there is any security to be charged, the relevant hypothecs cannot be vested in thousands of future and often unknown bearer debentureholders, but can be vested in a trustee in trust on their behalf. If shares of subsidiary companies or other securities are involved, they can be registered and delivered to the trustee, who can vote such securities as may be directed by the trust deed. Second, the trustee, acting alone and reasonably impartially, can watch over the debentureholders' interests, the security and, to the extent determined by the trust deed, the performance by the company. Generally, he alone can intervene if such interests are imperilled. The alternative of leaving any such action to a widely dispersed and divergent group of creditors is generally unsatisfactory both to the company and to some of such creditors. Indeed, the existence of an impartial and professional trustee makes it possible for an underwriter, who is to sell the debentures and who anticipates their interests, to negotiate with the issuer further obligations as to disclosure, to filing reports, and to compliance with certain tests of performance. This would prove unsuitable where there is a large number of debentureholders. Finally, in extreme cases of default and in cases of ambiguity under the terms of the trust deed, the trustee can convene meetings of the debentureholders and seek their concurrence with a proposed course of action that will be binding on all debentureholders.

1. The Scope Generally

The corporate trust deed has become one of the longest and most complex contracts used in corporate law. The relationship between issuer, trustee and debentureholders is entirely the product of contract. This is in marked contrast to the relationship between the issuer and its shareholders, which is today largely governed by statute.[11]

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[10] The "preliminary provision" of the C.C.Q. declares that it comprises a body of rules that lays down the "*jus commune*, expressly or by implication".

[11] The *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 82 and the similar acts of some provinces merely contain provisions (modelled on those of the U.S. *Trust Indenture Act of 1939*, 15

The corporate trust deed must provide, among other things, for the issue of debentures, perhaps in series or in classes, their rank, their parity and equitable treatment, their registration, evidence and transfer, the consents of debentureholders to material changes in capital structure and other fundamental changes, and the rules of meetings of debentureholders and the voting majorities required. It may also provide for the repayment terms of the debenture, which may be complex. It may provide for the charging of property as security, for the substitution of properties charged, for the good administration of the charged property and for a measure of supervision of the issuer's operations. The corporate trust deed often, by covenants monitored by the trustee, provides for measures to protect the debentureholder against actions by the borrower which might jeopardize any security or the borrower's ability to repay the debt. It must also provide the procedures for collective action of the debentureholders in the event of default. Reform has not changed the need for these provisions.[12]

A typical open-ended corporate trust deed (one where there is no stated limit for the principal amount of debentures that may be issued) of a large corporation for the creation and issue of bonds in series secured upon present and future property, both moveable and immoveable, corporeal and incorporeal, or the prospect of property, in Quebec and more than one other province may run to 150 printed pages, excluding property descriptions. The main groups of clauses fall into three categories. The first is the group of clauses providing for the creation of the bonds and their terms. The second embraces that group of administrative clauses permitting dealing with the bonds, their registration and their transfer while they are outstanding. The third establishes the rights and powers of the trustee for the bondholders and also of the bondholders individually. It involves the security, if any, and its enforcement.

2. Creation of the Securities

In the first group of clauses, one finds the framework for the issue of the initial debentures and of every subsequent series, including the tests as to assets, security, earnings and debt ratio that the company must meet to support each issue of a series of debentures. Compliance with the tests for the issue of a new series of debentures is usually attested to by the delivery to the trustee of signed detailed certificates of company officers, auditors and counsel. The fact that the debentures of each series rank

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U.S.C. §§ 77aaa ff.) prescribing minimal qualifications, duties and a standard of care for the trustee for public issues of securities under trust indentures.

[12] It is true that many clauses of corporate trust deeds are initially the same in all corporate trust deeds. These are commonly referred to as "boilerplate" (see *e.g.* American Bar Foundation, *Sample Incorporating Indenture and Model Debenture Indenture Provisions* (Chicago: American Bar Association, 1965) at 1 [hereinafter *Model Provisions*]). Much is to be said for standardization of clauses and of language. Indeed in the United States, under the *Model Provisions*, much has been achieved to this end. However the variations attaching to each type of issue (financial features, closed/open issue, security, substitution and dealing with security, first or subordinate charges (if any), jurisdictions, close held/widely held, negotiable/non-negotiable, financial tests, restrictive covenants, other issuer's covenants, convertibility, etc.) dictate that the practitioner review all clauses and often modify and integrate them for the issue at hand.

either *pari passu* or in some other manner is provided for. The form and basic text of each debenture is included. Standard provisions for redemption or for sinking funds, if they apply generally or to a series, are provided for.

These provisions, created by contract, are the "constating document" of the securities to be issued. They regulate the security, the title constituting the bondholder's claim. They could be constituted merely by a by-law of the issuer. However, with their provision in the corporate trust deed, the trustee has a role to play conjointly with the company. Although issued on the decision of the company, bonds must be certified by the trustee, who acts with the company (but only in strict compliance with the corporate trust deed). In so acting the trustee authenticates the debentures. The debentureholder thus derives an assurance from a third party that the debenture complies with and reflects truly the terms attaching to that class of securities issued by the corporation.

3. Administrative Functions

In the second group — those clauses that permit dealings with outstanding debentures — one finds the provisions for the maintenance of registers and for transfers and their effect. Paying-agent functions provide for the mechanics of payments including payment of coupons, often upon mere presentation at any branch of a major designated bank in the bond-market area, and payment of principal on redemption or by operation of the sinking fund.

All of these functions are essentially of an administrative nature and could also be performed by the company itself. They are in practice vested in the trustee as a professional with the necessary expertise and independence. They could in fact be delegated to a fourth party who would act as mandatary of the company as would a stock-transfer agent. In Eurodollar unsecured issues of bonds, debentures, notes or other securities, often based in Luxembourg and issued by Canadian companies or banks on the London markets, these administrative functions are in fact performed by the paying agent who is simply called "paying agent". The relevant provisions of that agreement are remarkably like the administrative provisions found in the corporate trust deed. In this sense the debenture trustee performs as would a mandatary of the company. But although these administrative functions are an appropriate subject for mandate (2130), they are also an appropriate subject for a contract of services (2098) or for a trust (1260). These provisions are also complementary or corollary to the "constating" terms of the debentures. They can be vested in a trustee to be performed, not as mandatary of the company, but as part of the trustee's duties. Where a trust is involved these powers can be transferred by the issuer company irrevocably as can any other property.

4. Security and Remedies

The third group of corporate-trust-deed clauses is of a different character again. They reflect rights and powers that in the absence of a corporate trust deed would be vested in the creditors alone. They include the initial grant of security, if any, the

charging of any additional property and the administration, uses and release of security. They include accessory contractual obligations or covenants (similar to those found in commercial loan agreements) which if not observed lead to a default, and all the rights and remedies exercisable upon default. They also include all the rights and remedies and the attached powers that are normally accessory to the status of a creditor. Of these, by far the most important is the right to take legal proceedings. In an unsecured debenture issue the right to institute proceedings is still essentially vested in the trustee. I have used the term "essentially", for in practice the debentureholder's right to sue is extensively circumscribed by the trust deed. Generally, the holder may sue only after a clear default, after due notice to the trustee and with provision of security for the trustee's costs and only if, after reasonable delays, the trustee has failed to act after being duly requested to do so by a specified majority of the debentureholders. Even then, the debentureholder's right to sue is subject to the consent and direction of a given majority of debentureholders. Most authority supports this position but also questions whether the debentureholder can be totally deprived of the right to take proceedings.[13] The rigid circumscription of the debentureholder's right to sue, however, has been supported by the strongest authority.[14]

From the point of view of debentureholders, their rights are limited to those defined in the trust indenture. By buying the debenture in the marketplace or by lending money evidenced by a debenture, they become creditors holding a security and accepting as a term of such security that: (i) initially all rights to enforce its payment are vested in the trustee; (ii) should the trustee fail to act, the debentureholders may force the trustee to sue but only on posting security and with the approval of a specified majority of the other debentureholders; and (iii) in the alternative and where the trustee fails to act, the debentureholders may sue to compel the trustee to act or they may act obliquely in the name of the trustee. In all events such proceedings must be for the benefit of all debentureholders. This is how the standard trust deed is written. Effectively, and with perhaps only one exception,[15] all proceedings against the issuer are to be on behalf of the trustee for the benefit of all debentureholders.

Note particularly that there is a clear separation of the remedy (the right to sue) from the right (the *créance*). The debenture represents the debt, the *créance*, and its holder alone is the creditor. In creating the debentures, however, the right and power to sue on such *créance* is ordinarily vested in the debenture trustee. This separation of the right to receive payment from the right to sue has posed serious challenges to the courts in Quebec. The trouble began more than one hundred years ago in respect of

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[13] See V. Mitchell, *A Treatise on the Law Relating to Canadian Commercial Corporations* (Montreal: Southam, 1916) at 1334; A. Tophaw, ed., *Palmer's Company Precedents*, 12th ed., vol. 3 (London: Stevens and Sons, 1920) at 472 [hereinafter *Palmer*]; *Caledonian Insurance Co.* v. *Gilmour*, [1893] A.C. 85; *Spurrier* v. *La Cloche*, [1902] A.C. 446; *Perron* v. *L'Eclaireur (Ltée)* (1934), 57 B.R. 445; see also art. 1590 C.C.Q.

[14] See *Laliberté* v. *Larue* (1930), [1931] S.C.R. 7, (*sub nom. Lafontaine Apts.* v. *Larue*) [1931] 2 D.L.R. 12 [hereinafter cited to S.C.R.].

[15] The exception is where suit is taken on detached bearer interest coupons (see *Morrison* v. *Grand Trunk Railway Company of Canada* (1861), 5 L.C.J. 313 (C.S.) [hereinafter *Grand Trunk Railway*] and *Connolly* v. *Montreal Park and Island Railway Co.* (1902), 22 C.S. 322 (C.R.).

railroad and other special act debentures, long before the enactment of the S.C.P.A. Nor was it settled by the S.C.P.A.

I. Corporate Trust Deeds before 1994

A. Development of Debentures and Corporate Trust Deeds

In order to understand the corporate trust deed and its likely judicial treatment under the C.C.Q., it is useful to understand how the debenture and the corporate trust deed evolved.

1. Origins

Governments that have evolved from the British tradition have issued negotiable debentures for centuries in order to pay their bills or to evidence their borrowings. Many of their agencies, including municipal governments, have received similar powers. Palmer makes the following comment:

> This word [debenture] was the first in the form of acknowledgment of indebtedness used by the Crown in old days and given by it to creditors of the Crown, to soldiers, and to the King's servants, for payment of their wages. Thus the Parliamentary Rolls of 3 Henry V. (1415) mention a petition by a citizen of London praying that he might be paid for certain goods supplied to Henry IV., and alleging that the commission appointed to investigate claims and provide for payment of that king's debts, "*ne voillent paier la somme suis dit a dit suppliant due, a cause q'il ne demonstre pas billes de Debentur, desouth la seal du clerk du spicere du nit nadgairs Roy [i.e., Hen. IV.], tesmoignauntz la dette suit dit.*"[16]

The term "debenture", according to Palmer, has been around for many centuries.[17] It is derived from the latin *debentur* ("there are owing"). Mitchell states: "Debenture is not a term of art, and has no definite legal meaning. It imports a debt; it involves some obligation of repayment, or promise to pay; but apart from that central idea it may take many shapes and cover many different contractual obligations."[18]

One important element of the debenture emerges consistently from a reading of all authorities. Gower states: "Primarily, the expression 'debenture' is applied not to the indebtedness itself but to the document evidencing it."[19] Today a debenture is a

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[16] *Palmer, supra* note 13 at 1.

[17] See *Palmer, ibid.*

[18] Mitchell, *supra* note 13 at 1274 [footnotes omitted]. See also W. Lindley, *The Law of Companies*, 6th ed., vol. 1 (London: Sweet & Maxwell, 1902) at 300; W.J. White, *Canadian Company Law* (Montreal: C. Théoret, 1901) at 383; H. Reid, *Dictionnaire du droit québecois et canadien* (Montreal: Wilson & Lafleur, 1974); and Chitty J. in *Levy* v. *Abercorris Slate & Slab Co.* (1888), 37 Ch.D. 260 and in *Edmunds* v. *Blaina Furnaces Co.* (1887), 36 Ch.D. 215.

[19] L.C.B. Gower, *The Principles of Modern Company Law*, 3d ed. (London: Stevens & Sons, 1969) at 347. A debenture is usually issued as a document under seal: *British India Steam Navigation Co.* v. *Inland Revenue Commissioners* (1881), 7 Q.B.D. 165; a security for money: *Bank of Toronto* v. *Co-*

document, a title evidencing a right to payment, a *valeur mobilière* or security. In the absence of an express term to the contrary, it is negotiable. If it is payable to bearer, or to order but unregistered, it is transferable by delivery. Thus it is not merely a *créance* or a receivable, but a "title" evidencing a claim.[20] Since it is a documentary title, in some respects it has the characteristics of a corporeal moveable.

In Canada, the term "debentures" is often used interchangeably with "bonds". In the past, if the document was under seal it was usually referred to as a debenture in England but as a bond[21] in common law Canada. In the United States, debenture has come to mean an unsecured obligation, while the term bond identifies a secured obligation.[22] Modern Canadian terminology tends to follow this American practice. In England, the term "debenture" is now used for both secured and unsecured obligations. Legally, the terms "debenture" (in both French and English in Quebec) and "bond" (in French "*obligation*" or "*bon*") have the same meaning. In this study I use the terms "bond" and "debenture" interchangeably.

Although the term "debenture" dates back centuries, the practice of granting security by a single charge on a class or classes of property for the repayment of a multitude of debentures is much more recent. It arose in the nineteenth century in the follow-up to the industrial revolution. It must be remembered that this was a period (1825 - 1900) of construction of great public-service undertakings, requiring substantial subscription of capital — more than any individual entrepreneur or banker could provide. It was the period of the building of trunk roads, bridges, canals, improved waterways and especially railways, not only in Quebec, but in all of North America and Europe. Electric-power companies, communications companies and industrial companies followed. The industrial revolution had brought growth and middle-class prosperity; many could lend a thousand pounds while few could lend a million. Moreover, the principal markets for investment were London and New York, and many issues of Quebec companies were sold in those markets. The securities offered were designed to comply with the practices of those markets.

This period also gave rise to the development of the limited-liability corporation. At first, these were the creatures of special statutes. In 1844 the British Parliament passed *An Act for the Registration, Incorporation, and Regulation of Joint Stock Companies*[23] permitting incorporation as a stock company by registration. This act was re-cast in 1862 permitting such incorporation with limited liability.[24] In Quebec,

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bourg Railway Co. (1884), 7 O.R. 1; generally a negotiable instrument: *MacFarlane* v. *St. Césaire (Corporation of)* (1886), 2 M.L.R. 160 (B.R.) [hereinafter *St. Césaire*]; *Levy* v. *Abercorris Slate & Slab Co., ibid.*; various forms of instruments are called debentures: *Edmunds* v. *Blaina Furnaces Co., ibid.*

[20] See Y. Renaud & J. Smith, *Droit québécois des corporations commerciales*, vol. 2 (Montreal: Judico, 1974) at 1027, 1029; Gower, *supra* note 19 at 347.

[21] See Mitchell, *supra* note 13 at 1274.

[22] See *Model Provisions*, *supra* note 12, "Introduction".

[23] (U.K.), 7 & 8 Vict., c. 110, cited in Mitchell, *supra* note 13 at 91.

[24] See Mitchell, *ibid.*; *The Companies Act, 1862* (U.K.), 25 & 26 Vict., c. 89.

the first general corporations clauses act was that of 1850.[25] The borrowing power of such early corporations was extremely restricted, if it existed at all, and generally had to be expressly authorized by the special act of incorporation. Indeed the Quebec companies legislation (re-enacted in 1868) contained no general borrowing power until 1890.[26]

Investor-owned corporations encountered serious legal difficulties in raising funds for these capital-intensive public services in all jurisdictions. Neither a mortgage in common law nor a hypothec in Quebec was readily divisible among a multitude of debentureholders. Pledges of moveables or chattels involved dispossession under both systems of law and did not serve the borrower's interests. The assets of the enterprise were likely to change over a period of years, and one of its most important assets was usually its future revenues from operations. These were not readily chargeable without dispossession. In Quebec the problems were especially acute, since security interests could be granted only by an express exceptional provision of law and the devices permitted were inappropriate both for a charge on all assets, present and future, and for their continued possession by the borrower. Moreover, charges on assets could not be pooled among many creditors through the use of the English concept of "trust".

2. Legislative Experimentation in Quebec

In Quebec, as well as elsewhere, there was a long period of legislative experimentation and evolution. The government of Quebec desired investor-owned enterprises to complete these large undertakings. It had to adopt measures, exceptional to the ordinary law, in order to assure that the necessary capital for their construction could be raised on the international markets. The list of attempted security devices is long and reflects substantial ingenuity on the part of both the legislature and legal counsel. The following developments are illustrative:[27]

1. In 1840, the Turnpike Road Trustees (note they are called "Trustees") were empowered by the Government of Lower Canada to issue debentures evidencing a debt, loan or claim to be privileged over certain other claims (Government subsidies) and to "have priority of lien upon the tolls and other

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[25] See *Incorporated Joint Stock Companies Act*, S.C. 1850, c. 28. According to Renaud & Smith, *supra* note 20, vol. 1 at 22, this Act was virtually a copy of the state of New York's statute of 1848. Renaud & Smith provide a succinct history of company law in Quebec. See also F. Wegenast, *The Law of Canadian Companies* (Toronto: Burroughs, 1931).

[26] See *Quebec Joint Stock Companies General Clauses Act*, S.Q. 1868, c. 24 and *Incorporation of Joint Stock Companies Act*, S.Q. 1868, c. 25; these acts were amended to add the borrowing power by S.Q. 1890 (54 Vict.), c. 35 and S.Q. 1902, c. 30.

[27] For a more extensive examination of some of the debenture legislation after 1890, see S. Le Bel, "Les émissions d'obligations dans le droit de la province de Québec de 1890 à nos jours" (1980) 21 C. de D. 43.

moneys which shall come into the possession and shall be at the disposal of the said Trustees."[28]

2. In 1849, the Saint Lawrence and Atlantic Rail-Road Company was empowered to create "mortgages or *hypothèques*" to secure debentures in statutory form, the debentures to be registered at length to "perfect the mortgage or *hypothèque*". Debentures were to be presented for endorsement by the registrar to evidence cancellation. Registration in more than one office was contemplated. To facilitate registration, numbered blank debentures could be bound in books and presented to the registrar to serve as the register. Bearer debentures were not contemplated.[29]

3. In 1851, *The Railway Clauses Consolidation Act* of the United Provinces of Canada permitted companies governed by that Act to borrow on bonds, debentures or securities and to hypothecate their "lands, tolls, revenues and other property".[30] It was silent as to who would hold such hypothecs.

4. *The Gas and Water Companies Act* of 1853 permitted companies incorporated thereunder to borrow, "to mortgage, secure and assign, real estate, works, rates, revenues, rents and future calls on shareholders of the said Company" for the securing of sums borrowed, and to issue "Bonds, Debentures or other securities" so secured.[31]

5. In 1858, the legislature of the United Provinces enacted the *Debenture Registration Act* providing for the registration in the registry office of all municipal and corporate debentures by presentation of the enabling by-law.[32]

Devices of greater precision and flexibility were also tried. The most notable of all such devices were the following:

6. In 1857, the St. Lawrence Warehouse, Dock and Wharfage Company was incorporated to construct, finance and operate a harbour at Lévis and was authorized to issue bonds, debentures or other securities which, upon their registration in the land-titles office, were to become a "mortgage and *hypothèque*, ranking according to the date of such enregistration, by special privilege, upon all the property, real and personal, of the said Company, in-

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[28] *Quebec Turnpike Roads Act*, S.Q. 1853, c. 235, s. 7, expanding on S.Q. 1839, c. 31; see also S.Q. 1857, c.125, which divided the trust into two (north shore and south shore) and declared them to be corporations.

[29] See *Saint Lawrence and Atlantic Rail-Road Company Act*, S.C. 1849, c. 176, s. 7; see also *Montreal and Lachine Rail-Road Company Act*, S.C. 1849, c. 177, s. 4.

[30] *The Rail-way Clauses Consolidation Act*, S.C. 1851, c. 51, s. 9.

[31] *Gas and Water Companies Act*, S.C. 1853, c. 173, s. 36, re-enacted by *Gas and Water Companies*, R.S.Q. 1888, arts. 4874-79; see also *River Navigation Improvement Act*, S.C. 1853, c. 191, re-enacted by *Companies to Facilitate the Transmission of Timber down Rivers and Streams*, R.S.Q. 1888, art. 4948; *Joint Stock Companies Act*, S.Q. 1870, c. 32, s. 28, re-enacted by *Companies for Stoning Roads*, R.S.Q. 1888, art. 5091; *Building Societies Act*, S.Q. 1879, c. 32.

[32] See *Debenture Registration Act*, S.C. 1858, s. 91; subsequently found in *Registration of Debentures*, R.S.Q. 1888, arts. 4617ff.

cluding the revenues, rates, tolls, dues and duties thereof."[33] The amending statute of 1869 is of interest. According to the recital in this Act, the company had issued debentures and desired legislative ratification of an issue of mortgage bonds (in part issued in exchange for the debentures) under the terms of a trust deed of 1866. The trust deed was a schedule to the Act. It was a deed before a Quebec notary of four and one-half pages in length including recitals. The deed professed to "hereby bind, mortgage, encumber and hypothecate" in favour of the trustees (who were three of the directors of the company — Sir John A. MacDonald was another director) "all and singular the property, estate and effects, of the company, both real and personal whatsoever and wheresoever, including the revenues, rates, tolls, dues and duties thereof" and especially the immoveable property therein described. It purported to give the trustees a power of sale of the charged property as well as the power to collect revenues.

7. In 1869, the Richelieu, Drummond and Arthabaska Railway Company was empowered to issue bonds or debentures "considered to be privileged claims ... and [that] shall bear hypothec upon the said railway without registration".[34]

8. An Act relating to the V. Hudon Cotton Mills Company, Hochelaga, incorporated by letters patent in 1873, provided for the issue of bearer debentures secured by "an equal privilege upon the immoveable or immoveables affected for their payment" through the registration of the by-law of their creation authorizing their issue. The Act also defined as immoveable "all engines, mills, looms and other machines used by the said company".[35]

9. In 1880, the South Eastern Railway Company — in reorganization — was authorized "to convey its railway, franchise and all property, rights and interest owned, possessed or enjoyed by it, and the tolls, income, profits, improvements and renewals thereof and all additions thereto to trustees in trust" to secure its bonds.[36] (The *South Eastern Railway Company Reorganization Act*[37] was judicially construed in 1898, as reviewed later in this study.)

10. In 1890, the Quebec companies general legislation was amended to provide that secured bonds or debentures, after their registration in the registry office where the immoveables described were located, constituted a "privileged

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[33] *St. Lawrence Warehouse, Dock and Wharfage Company Act*, S.C. 1857, c. 174, s. 25, as am. by S.C. 1859, c. 106, S.C. 1861, c. 97, S.Q. 1869, c. 62; see also *Lake Champlain and St. Lawrence Railway Junction Co. Act*, S.Q. 1876, c. 33.

[34] *Richelieu, Drummond and Arthabaska Railway Company Act*, S.Q. 1869, c. 56, s. 17.

[35] *V. Hudon Cotton Mills Company, Hochelaga Debentures Act*, S.Q. 1875 (39 Vict.), c. 66, ss. 5-6.

[36] *South Eastern Railway Company Reorganization Act*, S.Q. 1880, c. 49, s. 1; see also *Montreal Steel Works Act*, S.Q. 1903, c. 100, s. 10.

[37] *Ibid.*

claim" and gave "a right of preference over all other debts and claims against the company, posterior to the issuing of such debentures."[38]

11. In 1899, the Laurentian Water and Power Company was authorized to secure its bonds in favour of trustees by "such mortgages, charges and incumbrances, as may be necessary upon the property, concessions, rights, privileges, advantages, rents and revenues of the company, present or future, or present and future".[39]

12. In the same year the Lake Magantic Pulp Company was empowered to secure its bonds upon "the property and undertaking" of the company.[40]

As regards the use of the term "trust" and "trustee" in Quebec, the legislative history is similar. I have noted the reference to the "trustees" of turnpike roads in the ordinance of 1839.[41] In 1841 the legislature of the United Provinces of Canada adopted an *Act to Regulate Savings Banks* providing for their administration by directors or "trustees" upon "trusts", with vesting of moneys in the "trustees" in "trust" for the purposes of the institution.[42] Other references to "trustees" are found in the list of security devices, as has been noted above. In 1892 the Montreal Trust Company (then operating under another name) charter was amended to permit it to segregate "money, property or securities received, held or administered in trust."[43] In the same year The Royal Trust and Fidelity Company (subsequently The Royal Trust Company) was incorporated, *inter alia*, "to accept, fulfil and execute all such trusts ... [and] [t]o act as trustees for any debenture, bond or other security issued."[44] A general trust-companies act was first enacted only in 1912 and empowered such companies, *inter alia*, to act as "trustee for holders of bonds or debentures."[45] In 1879 an act of the legislature was adopted to permit gratuitous and testamentary trusts. These provisions were incorporated in the *Civil Code of Lower Canada* (arts. 981a ff. C.C.L.C.) in 1888.[46] In none of these enactments was the concept of trust defined, although in the latter legislation trustees were "seized as depositaries and administrators for the benefit of the donees or legatees of the property."[47]

Notwithstanding the absence of any definition of trust or trustee, the practice of granting the security to a trustee as representative of the bondholders through the use of a corporate trust deed had become established in Quebec by 1880. I have noted that one was sanctioned by the legislature in 1869.[48] In Quebec the trust deed is commonly

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[38] *Quebec Joint Stock Companies Amendment Act*, S.Q. 1890 (54 Vict.), c. 35, s. 1, amending R.S.Q. 1888, art. 4705.

[39] *Laurentian Water and Power Company Act*, S.Q. 1899, c. 81, s. 13.

[40] *Lake Magantic Pulp Company Act*, S.Q. 1899, c. 82, s. 5.

[41] See *Quebec Turnpike Roads Act*, *supra* note 28.

[42] *Act to Regulate Savings Banks*, S.C. 1841, c. 32, ss. 3, 6 & *passim*.

[43] *Montreal Safe Deposit Company Amendment Act*, S.Q. 1892, c. 78, s. 5.

[44] *The Royal Trust and Fidelity Company Act*, S.Q. 1892, c. 79, s. 2.

[45] *Quebec Trust Companies Act*, S.Q. 1912, c. 44, s. 1.

[46] *Act Respecting Trusts*, S.Q. 1879, c. 29, re-enacted by R.S.Q. 1888, art. 5803.

[47] Art. 981b C.C.L.C.

[48] See text above, accompanying note 33.

referred to as a "corporate trust deed", or simply a "trust deed" or sometimes a "trust indenture". The term "trust indenture" is usually employed in common-law Canada and in the United States.[49] It is also employed in the *Canada Business Corporations Act*.[50]

3. Development Contemporaneous with U.S. and U.K.

The development of the corporate trust deed in the United States occurred not much earlier than in Quebec. One of the earliest corporate trust deeds on record was that of The Morris Canal and Banking Company to an individual in Amsterdam, conveying "the chartered rights of the said company, and all tolls, incomes and revenues and profits" in trust to secure loans from several individuals aggregating $750,000. In the event of default, the trustee was empowered to take possession. The courts of New Jersey considered proceedings of enforcement in 1843. In the 1840s, scores of such deeds were entered into by railway companies. The deeds were often brief: perhaps three or four pages with no covenants.[51] The trustees were often officers of the issuer company. By 1876, a form of bond much like the modern form had appeared.[52]

In England, if one examines the texts and cases cited by Palmer,[53] the commercial practice of issuing debentures carrying terms not dissimilar to those of today was well settled by the 1870s. So was the use of trustees under trust indentures to hold security. We know that a charge on the "undertaking" was sanctioned by statute in 1845[54] and evolved to become the floating charge, first recognized by the courts in 1870 but only fully defined by the House of Lords in 1904.[55] By then the trust indenture had become the customary vehicle to secure such charges.[56]

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[49] Of English origin, "a word of art, [which] implies that this document is a deed, and sealed by the parties" (P. Allsop, ed., *Stroud's Judicial Dictionary*, 3d ed., vol. 2 (London: Sweet & Maxwell, 1952) at 1434); "In business financing, a written agreement under which bonds and debentures are issued ..." (J. Nolan *et al.*, eds., *Black's Law Dictionary*, 6th ed. (St. Paul, Minn.: West, 1990) at 770). "Indenture", a term foreign to modern civil law, comes from the ancient practice of cutting or indenting in a serrated or wavy line the margin of copies of a deed so that the copies could be proved the same by matching the indentations of the cut.

[50] *Supra* note 11, s. 82.

[51] See generally C.M. Draper, "A Historical Introduction to the Corporate Mortgage" (1930) 2 Rocky Mountain L. Rev. 71.

[52] See C. Rodgers, "Corporate Trust Indentures" (1965) 20 Business Lawyer 551.

[53] See *Palmer*, *supra* note 13 at 1-5.

[54] *The Company Clauses Consolidation Act* (U.K.), 8 & 9 Vict., c. 16, s. 38; see R.R. Pennington, "The Genesis of the Floating Charge" (1960) 23 Mod. L. Rev. 630.

[55] See *Re Panama, New Zealand, and Australian Royal Mail Co.* (1870), 5 L.R. Ch. App. 318, Gifford L.J.; *Illingworth* v. *Houldsworth*, [1904] A.C. 355 at 358, Lord Macnaghten L.J.; Pennington, *ibid.*

[56] Mitchell, *supra* note 13 at 67ff.; Lindley, *supra* note 18 at 317-18.

4. The Evolution of Security Devices

This period of legislative experimentation, which occurred in Quebec largely prior to 1914, reflects several phases of development of security devices. They comprise a continuum, though a rigid chronological progression of phases is more difficult to trace. The phases are (i) unsecured debentures, (ii) debentures secured by a statutory privilege on revenues, (iii) debentures secured by a statutory hypothec, with or without some form of registration, (iv) security through registered fixed charges in favour of trustees, (v) security by a conveyance and transfer to trustees embracing the ideas of entry, possession and sale after default, and finally (vi) security on the corporate undertaking, or words to the effect that future property, including moveable property (both corporeal and incorporeal), is to be included in the charge. By 1914, the last three phases had evolved and were often found to exist together. The terms "trust" and "trustees" were increasingly employed as these security devices developed. They were terms borrowed from the common law but became very much a part of practice in Quebec through the special legislation.

By 1914, hundreds of companies in Quebec had benefitted from such special enactments. There had also been some general enactments covering the powers of whole classes of public-utility companies. Many ordinary commercial corporations had applied for and obtained the same powers.[57] The scene was ripe for the enactment of the provisions of the S.C.P.A.[58] as general legislation, making these special security devices available to all commercial corporations.

B. *Juridical Treatment of the Corporate Trust Deed: Four Fundamental Problems*

As reviewed above, corporate-trust-deed financing developed in Quebec almost contemporaneously with its development throughout the English-speaking world. Its development was co-extensive with the development of the limited-liability company and the late-nineteenth-century financing of great public-utility projects. In Quebec, the practitioner and the legislature had responded to these needs through special (exceptional) legislation. The courts had to uphold these special laws. They responded positively in that corporate trust deeds were invariably upheld and enforced, but conservatively, as the security devices were then forced to be characterized within the concepts of Quebec's general civil law.[59] Because the tripartite arrangement of "trusts"

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[57] See *E.B. Eddy Company Act*, S.Q. 1895, c. 73; *William Dow & Co. Act*, S.Q. 1898, c. 79; *Windsor Hotel Company Act*, S.Q. 1899, c. 87; *La Presse Company Act*, S.Q. 1900, c. 87; *Great Northern Elevator Company Act*, S.Q. 1900, c. 82; *General Trust Company Act*, S.Q. 1912, c. 102; see also *supra* note 31.

[58] S.C.P.A., *supra* note 3. The steps immediately leading to the enactment of the S.C.P.A. provisions and their form are also examined by Le Bel, *supra* note 27.

[59] The only reported cases where the courts failed to enforce a corporate trust deed were those where the form or the registration requirements were deficient (see *Connolly* v. *Montreal Park and Island Railway Co.*, *supra* note 15; *Corporation du Village de la Pointe Gatineau* v. *Hanson* (1901), 10 B.R. 346; *Valin* v. *Lion Nead Rubber Company* (1927), 65 C.S. 410; *Dominion Textile Co.* v. *Angers* (1909), 41 S.C.R. 185; *Carter* v. *Fournier* (1937), 75 C.S. 530).

employed under the special legislation was foreign to our civil law, the methods employed by the courts to integrate such devices were of even greater interest.

The courts had several major problems to overcome in reconciling Quebec's civil law with the three-party arrangement inherent in corporate-trust financing. Although the arrangement had been sanctioned by legislation, the legislation did not address the problems of reconciliation. One might say the courts had to effect a synthesis between the new, legislated security devices and our existing concepts of law, to modify the latter in order to accommodate the former. In the alternative, the courts would have had to import concepts of foreign law, concepts which were not fully developed by the special legislation and not readily compatible with Quebec law.

To reconcile the special legislation both before and after 1914 (which introduced the S.C.P.A.) with the traditional concepts of the civil law of Quebec, the courts had to deal with the following major problems:

1. The characterization of the debenture as a negotiable security and a title to be governed strictly by the civil law of Quebec. If it had been found to be a bill of exchange or similar commercial instrument, the federal *Bills of Exchange Act*,[60] or English law generally, might apply.

2. The characterization of the charges conveyed or granted to the trustee, where the legislation used new terms, such as "mortgage", "convey", "cede" and "transfer", sometimes in combination with "hypothec", "pledge", "privilege" and "as security".

3. The separation of the *créance* of the debentureholder from the right of enforcement exercised by the trustee.

4. The characterization of the relationship between the trustee and the issuer, on the one hand, and the trustee and the debentureholder on the other.[61]

I will summarize briefly how the courts dealt with each problem.

1. Debentures Are Governed by the Civil Law

Quebec courts recognized the essential characteristics of a debenture as early as 1861.[62] There was, however, some early confusion after confederation: first, as to whether the common law of England should apply to commercial matters generally; and secondly, as to whether debentures qualified as negotiable promissory notes, and in consequence whether the English law of bills of exchange (delivery by endorse-

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[60] *Bills of Exchange Act*, now R.S.C. 1985, c. B-4.

[61] The courts also had to reconcile many other problems raised by the terms of the corporate trust deed with the concepts of our general civil law. It is my opinion that these other problems were not truly problems of characterization, but rather problems of reconciliation of competing values: for example, the scope of trust deed charges, the rank of competing interests, etc.

[62] See *Grand Trunk Railway*, *supra* note 15.

ment, good faith, holder in due course, etc.) should apply.[63] In *Young* v. *MacNider*, in the Supreme Court of Canada in 1896, Sir Elzéar Taschereau J. (dissenting on the question of good faith, but otherwise consistent with the majority), stated:

> I have not seen a single case, or a single text book where such securities have been called promissory notes, or considered as such. And if these debentures are not promissory notes the case is governed exclusively by the French law and the Quebec Code. As said by Sir Montague Smith, in the Privy Council, in the case of *Bell* v. *Corporation of Quebec* [(1879), 5 A.C. 84], English and American decisions are not governing authorities in the province.[64]

Our courts concluded that debentures would be governed by our existing concepts of law and not by principles of foreign law. Although in theory a debenture could be written so as to constitute it a promissory note governed by the *Bills of Exchange Act*,[65] I know of no Quebec case deciding so. The characterization in Quebec of a debenture as evidence of a debt governed by civil law has been generally accepted. The view that a debenture should not generally be considered a promissory note or bill of exchange is also consistent with its treatment under the common law.[66]

2. Characterization of Trust-Deed Charging Language

a. *Pre-S.C.P.A.*

By 1880, the use of trustees to hold the security granted to gnarantee repayment of debentures had become reasonably common in Quebec legal practice. But, as noted, the Quebec statutes enabling such practice often used new terminology borrowed from common-law jurisdictions. Perhaps because the securities were to be sold in London or New York, they often spoke of a "mortgage", "conveyance", "cession" or "transfer", as well as a "pledge" or "hypothec". Moreover, they never defined the concept of trust, although they often spoke of a conveyance "in trust" and "to trustees" and "as security" for bonds, debentures or other securities. Before 1914, the year the general legislation that would become the S.C.P.A. was introduced,[67] there were several significant cases.

The first involved provisions of a special statute of 1880 for the reorganization of the South Eastern Railway Company. The company was empowered to issue certain bonds:

> ... and for the purpose of securing the payment of the same and the interest thereon, to convey its railway, franchise and all property, rights and interest owned, possessed or enjoyed by it, and the tolls, income, profits, improvements

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[63] See *St. Césaire*, *supra* note 19; White, *supra* note 18 at 386-87, suggests debentures are promissory notes; Lindley, *supra* note 18 at 301, states they can be promissory notes.

[64] *Young* v. *MacNider* (1896), 25 S.C.R. 272, citing also *R.* v. *Belleau* (1882), 7 A.C. 473, and *Montreal Assurance Co.* v. *McGillivray* (1858), 8 L.C.R. 401 at 423.

[65] *Bills of Exchange Act*, *supra* note 60.

[66] See *Levy* v. *Abercorris Slate & Slab Co.*, *supra* note 18 at 264; *Palmer*, *supra* note 13 at 3.

[67] See *supra* note 3.

> and renewals thereof and all additions thereto, to trustees in trust for that purpose.[68]

The Act went on to provide that the trustees could determine who could have possession, management and control of the railway, and how, in the event of such default being made, "the company shall be absolutely divested of all interest, right of redemption, claim or title" and how "the same shall thereupon immediately be and become vested absolutely in the said trustees or the holders and owners of the said bonds". The trustees were empowered, in the event of default, "to take possession of and run, operate, maintain, manage and control the said railway". The legislation expressly provided that "[t]he said conveyance shall be, to all intents, valid and create a first lien, privilege and mortgage".[69] The authorized bonds were issued under a trust deed of 1881 by which the railway was conveyed to the trustees as security for the repayment of the bonds. It was stipulated in the trust deed that the company should remain in full possession as if the deed had not been passed until 90 days after default. If the bonds remained unpaid after six months, the trustees had the right to become full owners of the railway after certain notices and delays. In 1883, the Company became in default and, upon the request of the trustees, voluntarily gave them possession and control of the railway.

These provisions of the Act were no doubt inspired by the common-law concepts of mortgage (with its concept of transfer of title and equity of redemption) and of trusts, even though the railway in question operated solely in Quebec. It had been declared a work for the general advantage of Canada[70] and subject to the *Consolidated Railway Act* of Canada,[71] but upon terms under which the Quebec statute continued to apply. There is no doubt that the interests of the trustees and the security of the bondholders remained governed by Quebec law.

The construction of this statute came before the courts on two occasions. The first case was *Redfield* v. *Wickham (Corporation of)*,[72] which held that the railway in the hands of the trustees was not precluded from being seized and sold, subject to its statutory mortgages, for the judgment debts of the company. Lord Watson, of the Privy Council, stated:

> Their Lordships do not doubt that the effect of the trust conveyance of the 12th of August, 1881, followed by possession in terms of the deed, was to vest the property of the railway and its appurtenances in the appellants, and to reduce the interest of the South-Eastern Company to a bare right of redemption.[73]

He again stated:

> On the one hand, the railway taken in execution by the respondents must, for all the purposes of these proceedings, be deemed to be still the property and in

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[68] *South Eastern Railway Company Reorganization Act, supra* note 36, s. 1.
[69] *Ibid.*, ss. 5, 6, 7.
[70] See *Constitution Act, 1867* (U.K.), 30 & 31 Vict., c. 3, s. 92(10)(c).
[71] *Consolidated Railway Act*, S.C. 1879, c. 9, as am. by S.C. 1883, c. 24.
[72] (1888), 13 A.C. 467.
[73] *Ibid.* at 473.

> the possession of the South-Eastern Railway Company; and, on the other hand, the appellants, as representing the present holders of mortgage bonds, must be taken as standing in the shoes of the bond holders whose debts were unpaid at the passing of the Act.[74]

The status of the trustees was considered by the courts for a second time in two cases heard together in the Supreme Court of Canada. They were *Wallbridge* v. *Farwell* and *Ontario Car and Foundry Company* v. *Farwell*.[75] The first involved a claim against the company arising after the conveyance in trust, but prior to possession of the railway by the trustees, and in consequence it involved the nature of the continued possession by the company. The second involved a similar claim, allegedly secured by a vendor's privilege, and its rank after possession. The claimant had sold rolling stock for which it had not been fully paid. The principal decision in each case was given by Sir Elzéar Taschereau J. He said:

> To follow Mr. Laflamme's able argument for the appellant, I have so far considered the deed of trust of 1881, before the respondents came into possession, either as creating a pledge or as an actual and complete sale of this railway, and I have said why, in my opinion, admitting it to be either one or the other, the appellant has no action against the trustees. I need hardly remark the contradiction between these two grounds of reasoning. If a pledge, the railway company remained the owners. If, a sale, the trustees became owners. Was that deed, however, anything else than a mortgage or hypothec of of [*sic*] this railway, as long as the company remained in possession, within of course the sense and meaning that these words have in the Province of Quebec, where the hypothec is a kind of pledge in which the pledger retains both ownership and possession of the thing pledged, in contradistinction to the contract of pledge, *pignus*, where the pledgee is put in possession, the title remaining in the pledger. It seems to me impossible to see in that deed, as interpreted in the light of the statute of 1880, anything else than a hypothecation of this railway in favour of the bondholders, not precisely the hypothecation of article 2016, C.C., but with the exceptional right, given by the statute, of the mortgagee to enter into possession, in default of payment, after the exercise of which right the contract between the parties became one of *nantissement*, with, of course, *droit de rétention*, till paid, joined to the hypothec. The term "sold" is used in the deed, it is true. But the statute of 1880 authorizes only to *convey* as security. *Transporter*, says the French version.[76]

After reviewing some French authority on the characteristics of a hypothec, he concludes:

> This is, in my opinion, precisely the nature of the contract that has taken place between the parties here. The company were to remain in possession as long as they satisfied, as accrued, their liabilities to the bondholders. They might never have lost the possession, and have continued to work the railway themselves, the railway, however, by the authority of this statute, all the time remaining

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[74] *Ibid.* at 477.

[75] *Wallbridge* v. *Farwell, Ontario Car and Foundry Co.* v. *Farwell* (1890), 18 S.C.R. 1 [hereinafter *Farwell*]. Much of Mr. Justice Taschereau's judgment in French was quoted in *Connolly v. Montreal Park and Island Railway Co.*, *supra* note 15.

[76] *Farwell*, *ibid.* at 11-12.

> vested in the bondholders, or in the trustees for them, till the complete satisfaction of their bonds, in 1901, as security therefor. I must confess that I can see nothing else in this deed, before the trustees took possession, than a hypothecation of the railway, which hypothecation took the character of an antichresis, when the trustees took possession, or, to use the English law terms of their Lordships of the Privy Council, in the *Redfield* case — a conveyance by a debtor to his creditor, coupled with possession, with right of redemption, in security of a debt.[77]

In the second case, Mr. Justice Taschereau disposed of the claim of the car company on several grounds, including the following:

> The railway company here were the buyers, not the trustees. The contention that they, the company, acted merely as agent or *negotiorum gestor* for the trustees is untenable. I have referred to this point in the previous case. The railway company was then the owner in possession with a statutory mortgage on the property in favour of the bondholders. When the statute gives to the trustees a lien or mortgage on the railway, it clearly implies that the trustees were not, at first, to be owners. One does not require a lien or mortgage on his own property for the payment of his claims. Then the statute and the deed provide when and under what circumstances the trustees might become later absolutely owners of the railway. This also implies that they were not yet owners, and still further, there was no price of sale, so there was no sale; *pretium* is a requisite of this contract, as much as *res et consensus*. The fact that trustees for the bondholders, benefited by the sale of these cars to the railway company does not help the plaintiffs. A hypothecary creditor always benefits from the improvements made and expenses incurred by his debtor on the property hypothecated.[78]

One may draw several conclusions from the Court's construction of this nineteenth-century statute. First, the hypothecation language of the statute considered was similar to that of the S.C.P.A. It used the words "convey" as security to "trustees" so as to constitute a "first lien, privilege and mortgage". The S.C.P.A., as originally enacted in 1914,[79] employed the words "hypothecate, mortgage or pledge" to a "trustee" "as security"; and, as amended in 1924,[80] "cede and transfer" for the same purposes. Accordingly, one must conclude that the trustee's right of entry and possession under the *South Eastern Railway Company Act* was similar to its right of entry and possession under the S.C.P.A.

Second, the conveyance in trust was not to be treated as a common-law mortgage or a sale with a right of redemption or a conveyance in trust, but as equivalent to a civil-law hypothec. "The grantor remained owner subject to the hypothecary charge. The trustee did not become owner under the special statute until after default and possession.

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[77] *Ibid.* at 13.

[78] *Ibid.* at 19.

[79] S.Q. 1914, c. 51, *supra* note 3, s. 1.

[80] S.Q. 1924, c. 63, *supra* note 3, s. 1.

Third, the trustees were parties quite separate from the company and were not liable to the company or its creditors for debts incurred for the preservation of the property. The trustees, by inference, formed a party quite separate from the bondholders, although their function was clearly to represent the interests of the latter and to realize upon the security for their benefit.[81]

This approach to the construction of the statute had an earlier basis in our jurisprudence. In *Drummond (County of)* v. *South Eastern Railway Company*,[82] the Superior Court considered whether or not a railway (or part of it) could be seized and sold at the hands of justice in satisfaction of defaulted bonds that benefitted from a statutory "hypothec upon the said railway without registration"[83] and yet by related act, a "mortgage on any real estate."[84] Mr. Justice Dorkin said:

> [W]e have here to deal merely with the wording of a Quebec statute, and with its application to the machinery of our Quebec Courts of law. In section 17 we read "privileged claims" and "hypothec;" in form B, "do hereby mortgage and hypothecate," rendered in French as "engage, mortgage and hypothèque." The one word that has not for us a clear meaning of its own, is the word "mortgage." Was it used to convey the notion of a *vente à réméré*, the nearest approach we have to a fair equivalent for the English mortgage? Had it been, it could not have been put with the word hypothec, as it is. The two things are no match. What is sold *à réméré* is not hypothecated; and what is hypothecated is not sold *à réméré*. ... The transaction thought of, whatever it may be, cannot at once be both. In a word, for all ends of judicial interpretation, we have no choice but to hold that the Legislature meant the word as a mere equivalent for the word hypothec, and must confine ourselves, in our application of it, to that meaning.[85]

This decision was overruled in the Quebec Court of Appeal on the question of seizability of the railway but not as to the expression of the principles last noted. Mr. Justice Ramsay, supporting Chief Justice Sir A. A. Dorion to the effect that the railway was seizable, then added:

> When the title "of obligations" was being prepared, the incorrect expression mortgage was carefully excluded, as expressing something quite different from *hypothèque*, and there being no English word, the word "hypothec" was borrowed from the Scotch law.[86]

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[81] See also *Hatherton* v. *Temiscouata Railway Co.* (1896), 12 C.S. 481 [hereinafter *Hatherton*], holding that debenture trustees are not merely agents and attorneys of debentureholders (*ibid.* at 489).

[82] *Drummond (County of)* v. *South Eastern Railway Company* (1878), 22 L.C.J. 25 (Sup. Ct.) [hereinafter *Drummond*].

[83] *Richelieu, Drummond and Arthabaska Ry. Co. Act*, S.Q. 1869, c. 56, s. 17.

[84] *Richelieu, Drummond and Arthabaska Ry. Co. Amendment Act*, S.Q. 1872, c. 51, s. 2, amending *South Eastern Counties Junction Railway Company Act*, S.C. 1866, c. 100.

[85] *Drummond, supra* note 82 at 32.

[86] *Drummond (County of)* v. *South Eastern Railway Company* (1879), 24 L.C.J. 276 at 285 (C.A.).

b. Post-S.C.P.A.

In 1914, the provisions of the Quebec *Joint Stock Companies, General Clauses Act* and *The Quebec Companies' Act* were expanded to empower a corporation generally to secure its bonds, debentures or other securities by hypothec, mortgage or pledge of its properties, moveable and immoveable, present and future, by trust deed in favour of a trustee. These particular powers were then recast as a special statute of general application to most corporations; this became the S.C.P.A. in 1925.[87] The provisions did not define the characteristics of the trust deed, nor of the powers of the trustee. In 1924, these provisions were amended with retroactive effect to empower the borrower to "cede and transfer" his properties to the trustee "for the same purposes", permitting the trustee, in the event of default, to take possession, to administer and sell the charged property "for the benefit of the bondholders".[88]

The leading case on subsequent corporate-trust-deed construction is *Laliberté* v. *Larue*.[89] The facts are of interest. Les Appartements Lafontaine issued mortgage bonds under a trust deed with the Sun Trust Company and subsequently became bankrupt. The bankruptcy trustee, without opposition from the bond trustee, sold the property as an asset of the bankrupt's estate. Certain of the bondholders sued to set aside the sale, alleging that the earlier "cession and transfer" under the trust deed had removed the property from the issuer/bankrupt's estate. On the direction of the Supreme Court of Canada, the bond trustee was named a party. The bond trustee attested that in its discretion it did not oppose the bankruptcy sale, as such sale would clear a number of prior-ranking privileges. The Quebec Court of Appeal had rejected the action on the ground that, by the terms of the trust deed, only the trustee could take such proceedings, unless holders representing at least twenty-five percent of the bonds posted security for costs and possible damages; these conditions had not been met.[90] In the circumstances, the status of the trustee and his power to take proceedings were not at issue.

The principal decision of the Supreme Court was rendered by Mr. Justice Rinfret (as he then was). The findings of the Supreme Court were extensive and may be summarized as follows:

1. The clause restricting the right of the bondholder to sue is normal and assures the trustee the discretion to act in the best interests of all bondholders generally. The Court of Appeal's finding that the appellant bondholders did not fulfil the trust-deed conditions to permit them to sue in the stead of the trustee was well founded (unless the appellant could show the property sold did not form part of the debtor's estate). The company contracts with the trustee to this end:

> Elles ont pour but d'assurer au fiduciaire la discrétion convenue dans l'exercice de ses pouvoirs et surtout de concentrer entre ses mains l'institution des procé-

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[87] See *supra* note 3.

[88] S.Q. 1924, c. 63, *supra* note 3, s. 1.

[89] *Laliberté* v. *Larue*, *supra* note 14.

[90] *Laliberté* v. *Larue* (1930), 48 B.R. 390.

> dures et l'adoption contre la compagnie des recours exigés par les circonstances, afin d'éviter précisément que le bon fonctionnement de la fiducie ne soit compromis par les activités d'une petite minorité ou même d'un seul des porteurs d'obligations, dont le nombre et le personnel varient suivant le jeu des négociations. Il est reconnu que ces stipulations tendent à protéger l'intérêt général.[91]

2. It is the contract (trust deed) that must determine the relationships between the bankrupt, the trustee and the bondholders. Mr. Justice Rinfret stated:

> [C]'est le contrat, et non le statut, qui doit déterminer la nature des relations de la faillie, du fiduciaire et des porteurs d'obligations.
>
> Il peut être utile toutefois de référer au statut pour mieux pénétrer le sens du contrat, car il est avéré que ce dernier est calqué sur le premier ...[92]

3. Quebec law does not admit of the common-law concept of the division of property between beneficial ownership and legal title. Title in Quebec is singular and unique. On occasion it is subject to various real rights.[93]

4. The "hypothec, mortgage [*nantissement* in French] and pledge" of the S.C.P.A. are purely the ordinary civil-law devices, with the innovation that they extend to moveable property and to future property and leave the debtor with their possession and use:

> [C]'est l'hypothèque telle qu'elle a toujours existé, ce sont le nantissement et le gage tels qu'ils ont toujours été conçus dans le droit français et dans le régime légal de la province de Québec.[94]

5. The term "mortgage" used in the English version of the S.C.P.A. is confusing and inappropriate and does not introduce the common-law notion of mortgage.[95]

6. The permission to grant such charges by "trust deed" in favour of a "trustee" does not introduce the common-law concept of trusts, but is merely the name given to the contract:

> Elles n'impliquent donc aucunement le "trust", tel qu'on l'envisage en droit anglais. Le statut dit que l'hypothèque, le nantissement ou le gage "peuvent être constitués" par "acte de fidéicommis" et la version anglaise s'exprime: "by trust deed". Il est à peine besoin d'insister pour démontrer que c'est seulement un nom ou une étiquette que l'on donne au contrat. Le "trust", sauf dans la forme restreinte où on le trouve au chapitre de la fiducie (Code civil, livre troisième, titre deuxième, chapitre IVa), n'a jamais existé dans le système légal de la province de Québec, qui ne comprend d'ailleurs aucun mécanisme (machinery) pour le faire fonctionner.[96]

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[91] *Laliberté* v. *Larue*, *supra* note 14 at 14.
[92] *Ibid.* at 15.
[93] See *ibid.* at 16.
[94] *Ibid.* at 17.
[95] See *ibid.*
[96] *Ibid.* at 17-18.

7. The "conveyance" ["*transporter*" in French] in trust permitted by the *Civil Code of Lower Canada* for dispositions of property by will and by gift (981a C.C.L.C.) is different and less qualified.[97] By inference this is not such a transfer and the rules of such a trust do not apply.[98]

8. The right to "cede and transfer for the same purposes the said properties to the trustee" means to guarantee payment of the bonds and does not involve an absolute cession and transfer or alienation of the property. It does not exist separately from "hypothecate, mortgage and pledge" as both are "for the same purposes", that is, to secure:

> *"Pour les mêmes fins"* réfèrent aux "fins mentionnées auxdits articles", qui les précèdent immédiatement dans la même phrase. Or, "les fins mentionnées auxdits articles" et pour lesquelles la compagnie est autorisée à "hypothèquer, nantir et mettre en gage" sont (art. 10): "pour garantir le paiement des bons, obligations etc". Céder pour garantir, transporter pour garantir, c'est la même chose que céder ou transporter en garantie; et ce n'est pas céder et transporter d'une façon absolue. Une cession ou un transport pur et simple est final et constitue une aliénation définitive. Une cession ou un transport en garantie implique une idée de retour. Les mots "céder et transporter" ne sont donc pas employés ici dans leur sens intégral et ne signifient pas une aliénation de la propriété.[99]

9. The added right "to take possession of the property ceded and transferred to administer and to sell them for the benefit of the bondholders" functions to afford the trustee these powers when granted by the deed; these powers are not normally available to the holder of a hypothec or pledge. These powers affirm that the rights are hypothecary in nature.[100]

10. The cession and transfer contemplated by the S.C.P.A. does not embody the common-law concept of a transfer in trust. An analysis of the trust deed reveals clearly that the trust deed is a contract of loan and hypothec and not one of alienation making the trustee owner.

> Bien entendu, ce n'est pas le "trust" dans le sens du *common law*. Le texte même de l'article 13 le prouve. Il est admis que jusque là le "trust" n'existait pas dans la loi de Québec. Or, l'article 13 est déclaratoire. Il spécifie qu'il n'institue aucun droit nouveau. Il dit que ce qui est permis par cet article "est et a toujours été loisible". Ce ne peut dont [*sic*] être le "trust".[101]

In consequence, the charged property never ceased to be property of the bankrupt.

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[97] See *ibid.* at 20. The court held that on this point the Privy Council decision in *Re O'Meara* v. *Bennett*, [1922] 1 A.C. 80 at 85 was instructive.

[98] This effectively overruled the decision in *Turgeon* v. *Vermette* (1928), 31 R.P. 191 (Sup. Ct.).

[99] *Laliberté* v. *Larue*, *supra* note 14 at 19.

[100] See *ibid.*

[101] *Ibid.* at 20.

11. The corporate trust deed is an enforceable *sui generis* contract. Mr. Justice Rinfret made the following important general statement:

> Par là, il est devenu certain qu'un contrat de ce genre pouvait se faire. C'est un contrat particulier avec des stipulations spéciales, en dehors de celles prévues dans les chapitres du code relatifs au nantissement, au gage et à l'hypothèque, mais restant quand même subordonné aux règles du droit commun dans ses principes généraux et dans tout ce qui n'est pas déclaré y déroger expressément.[102]

This construction of the S.C.P.A. and trust deeds written thereunder is entirely consistent with the pre-1914 judicial construction of the various special statutes examined earlier. Some of these statutes involved terminology borrowed from common-law jurisdictions that presented much greater problems of synthesis with civil-law concepts than did the language of the S.C.P.A. It is curious that the Supreme Court of Canada made no reference whatsoever to these earlier decisions.

Laliberté v. *Larue* is still the leading, and indeed the landmark, case on the characterization of the security under the corporate trust deed as known to this day. It was followed by the Supreme Court again in 1962 in *General Trust of Canada* v. *Roland Chalifoux Ltée.*,[103] which also noted that property charged under the S.C.P.A. remained part of the debtor's assets and constituted the common pledge of its creditors.[104] *Laliberté* v. *Larue* has been followed in every subsequent case.[105]

Thus both before and after the adoption of the S.C.P.A. our courts determined that the charges under the special legislation were to be equated to and construed as hypothecs. Such charges represented not the strict hypothecary charge contemplated by the *Civil Code of Lower Canada*, but a charge (not involving a transfer of title) on property of whatever kind, without dispossession, and, if contracted for, the additional right of entry into possession and sale after default. A further step had been taken in synthesizing the provisions of the special legislation and the traditional institutions of Quebec's civil law.

The judicial characterization of the charges under a trust deed as a form of hypothec or pledge without possession has proved to be an acceptable solution. Indeed, the existing jurisprudence based on *Laliberté* v. *Larue* should apply as regards the status and effect of the charges under the many thousands of trust deeds that are now outstanding. Following reform, the remedies resulting from such charges are now commuted to those found for enforcement of hypothecs under the C.C.Q. Regardless of the language of the charging clauses under outstanding trust deeds, the remedies available to the trustee are to take possession of the charged property in order to administer it, to take it in payment of the claim, to have it sold by judicial authority or to sell it by private sale (2748). The procedures prescribed by the C.C.Q. must be fol-

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[102] *Ibid.*

[103] [1962] S.C.R. 456.

[104] See *ibid.* at 460.

[105] A review of Quebec jurisprudence to the end of 1996 revealed there were at least 95 reported cases that followed or cited *Laliberté v. Larue.*

lowed and the effects decreed by the C.C.Q. will result. All such results will flow from any outstanding trust deed where the charging language contains any of the words "hypothecate", "pledge", "mortgage", "charge", "cede", "transfer" or the equivalent, provided that it is clear in the context that the conveyance or charge is always "as security" for an obligation.

3. Trustee's Right to Sue

It is a fundamental maxim of law in the western world, both civil law and common law, that "there is no right without a remedy".[106] Article 20 of the *Code of Civil Procedure* ("C.C.P.") reflects this principle in providing that when the law expresses no specific procedure at law for the exercise of any right, any proceeding may be adopted which is not inconsistent with the C.C.P. or some other provision of law.

There are also several related principles, at least in Quebec civil law, that are pertinent here. The first is the reciprocal principle, that to bring an action at law one must have sufficient interest (art. 55 C.C.P.). The second (art. 59 C.C.P.) is that one cannot use the name of another to plead (*personne ne plaide par procureur*), except in specifically enumerated cases, all of which have been sanctioned by amendment over the years.[107] A third related principle is that every person has the full enjoyment of, and is fully able to exercise, his civil rights and cannot, in anticipation of the opening of such right, renounce such rights (art. 1, 4, 8 C.C.Q.). Although newly framed by the C.C.P., these principles are not new to our civil law. The courts have fairly consistently found that, in the absence of express legislation, a person cannot transfer, or in anticipation renounce, his right to take proceedings.[108]

An obvious and essential aspect of the foregoing principles is that the remedy (the right to take proceedings at law) is an inherent part of the right giving rise to the proceedings.[109] Normally the one is not separated from the other and both vest in the same party.

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[106] "*Ubi jus ibi remedium*". See L.-P. Pigeon, *Rédaction et interprétation des lois* (Québec: Publications du Québec, 1986) at 23; A. Mayrand, *Dictionnaire de maximes et locutions latine utilisées en droit*, 3d ed. (Cowansville, Que.: Yvon Blais, 1994) at 518; E. Garsonnet, *De procédure*, 2d ed., vol. 1 (Paris: L. Larose, 1898) at para. 290; A.V. Dicey, *Law of the Constitution*, 9th ed. (London: MacMillan, 1927) at 198-99; H. Manisty, ed., *Broom's Legal Maxims*, 7th ed. (London: Sweet & Maxwell, 1900) at 150; *Board* v. *Board*, [1919] A.C. 957 at 962; *American Cyanamid* v. *Novopharm Ltd.*, [1972] C.F. 739 at 746 and at 770 n. 4 (C.A.).

[107] The exceptions are: the case of the State, class actions, the case of tutors, curators and others not in the full exercise of their rights and the case of those administering the property of others in respect of their administration. This last item was added by the *Implementation Act*, *supra* note 7, s. 190.

[108] This, more than another factor, led the Quebec courts to find compulsory arbitration clauses invalid (see P. Ferland, "La controverse au sujet de la validité de la promesse d'arbitrage" (1973) 33 R. du B. 136). The invalidity was ultimately overcome by express legislation, completed only in 1986, in *An Act to amend the Civil Code and the Code of Civil Procedure in respect of arbitration*, S.Q. 1986, c. 73 (see art. 940ff. C.C.P.).

[109] In proceedings that are, to a degree, analogous, the Supreme Court held that the right to sue was inherent in the federal law of bills of exchange, that it was a substantive right, and could not be inter-

In Quebec law prior to reform, a significant exception to this principle evolved through the jurisprudence. It involved the position of a "trustee" as one acting for "the benefit of" the creditor or creditors. There were two separate circumstances in which the exception arose.

a. *Trustee for Creditors of an Insolvent*

The first circumstance concerned a number of cases where the power of a trustee for creditors of an insolvent, who entered into a voluntary deed of assignment of all assets of the insolvent to recover assets forming a part of the insolvent's estate, was put in question. It was repeatedly argued that the trustee was merely an agent or mandatary for the creditors and could not sue in his own name while acting on behalf of the creditors. The rule *personne ne plaide par procureur* was invoked in each case.

Four such cases went to the highest courts. In *Browne* v. *Pinsoneault*[110] and in *Burland* v. *Moffatt*[111] the Supreme Court of Canada applied the rule. In *Porteous* v. *Reynar*,[112] however, the Privy Council affirmed that a trustee for creditors, acting under a voluntary contract, could sue in his own name for recovery of monies owing to the insolvent.[113] Lord FitzGerald, after expressly declaring that the two cases first noted were wrongly decided by the Supreme Court (Sir Elzéar Taschereau J.), adopted by reference the decision of Dorion C.J.A. in the Quebec Court of Appeal in *Moffatt* v. *Burland* (1884). There, the Chief Justice, after an extensive review of both Quebec and French authorities, stated:

> As far as we can refer back for precedents in the Courts of Lower Canada, we find that assignees or trustees vested by voluntary agreements with the estate of insolvent debtors, for the benefit of their creditors, have invariably with one or two exceptional cases ... been admitted to urge before Courts of Justice the claims and rights of the estates which they represented as such assignees or trustees.[114]

Lord FitzGerald in *Porteous v. Reynar* then said:

> Their Lordships entertain the view that art.19 [now art. 59 C.C.P.] is applicable to mere agents or mandatories who are authorized to act for another or others, and who have no estate or interest in the subject of the trusts, but is not applicable to trustees in whom the subject of the trust has been vested in property

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fered with by provincial legislation (see *A.G. Alberta* v. *Atlas Lumber Co.* (1940), [1941] S.C.R. 87, 1 D.L.R. 625, Rinfret J.).

[110] (1879), 3 S.C.R. 102.

[111] (1885), 11 S.C.R. 76.

[112] (1887), [1888] 13 A.C. 120, [1890] 16 Q.L.R. 37 (P.C.) [hereinafter cited to A.C.].

[113] The trustee was acting under a voluntary deed of composition, joined in by the insolvent and the official insolvency assignee under *The Insolvency Act* (S.C. 1875, c. 16).The trustee's powers were derived from the contract, not from the Act.

[114] *Moffatt* v. *Burland*, [1884] 4 Q.B.R. Dorion 59 at 68-69.

> and in possession for the benefit of third parties, and who have duties to perform in the protection or realization of the trust estate.[115]

The question once again came before the Supreme Court in *Mitchell* v. *Holland*[116] in 1889. Mr. Justice Taschereau then affirmed the right of a trustee for creditors (pursuant to a voluntary general assignment by an insolvent) to sue for the recovery of hypothecary debts for a balance of price of the sale of land.[117]

The judgment of Chief Justice Dorion in the Quebec Court of Appeal in *Moffatt* v. *Burland* is of further interest in that he attempted to characterize the position of a trustee in these cases. In speaking of the deed of general assignment, he said:

> This is not an ordinary Power of Attorney, it is a deed conveying to the Appellant a title or at least an apparent title to the property therein mentioned, which gave him a right to claim this property as his own from all other parties except Gebhardt & Co. and their creditors, to whom he was bound by the trust created by the deed, but to no others.
>
> At most this was but an irrevocable mandate, resulting from a contract between parties having adverse interests.
>
> ...
>
> It would be a contradiction to say that the mandate is irrevocable, and yet that those who gave it must sue to recover the assets which form the subject of it, and thereby indirectly remove from the control of their agent, those assets, while they cannot revoke his powers to deal with them. In the present case by whom should the suits be brought; is it by Gebhardt & Co., but the deed was passed for the very purpose of removing their estate from their control; is it the creditors, but no transfer has been made to them of the estate. They have been satisfied with accepting the delegation by which the Appellant agreed to realize the estate conveyed to him, and pay them the proceeds to the extent of their respective claims.
>
> ...
>
> It is upon these grounds that voluntary assignments by insolvent debtors, for the benefit of their creditors, have always been considered both in France and in this country, as conferring to the assignees (*cessionnaires*) the right to sue and be sued with reference to the assets and property assigned.[118]

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[115] *Supra* note 112 at 131.

[116] (1889), 16 S.C.R. 687 [hereinafter *Holland*]. These decisions were further examined at some length by Mr. Justice Jean Martineau in the Court of Appeal in *Cyr* v. *Weldon* (1956), [1957] B.R. 477 at 487ff., as to the application of the principle *personne ne plaide par procureur.*

[117] Justice Taschereau, *Holland, ibid.* at 696, felt obliged to assert that the Privy Council had misunderstood the basis of his decisions in the earlier cases. He expressly noted that he had held in *Burland* v. *Moffatt* (*supra* note 111) that the trustee could not sue in a creditor's action to rescind a sale made by the insolvent in fraud of the rights of the creditors since, being merely the assignee of the debtor not under the *Insolvency Act*, he had no more rights than the assignor had. He then acknowledged that the trustee, as assignee of the insolvent, could always take suit respecting the property rights transferred.

[118] *Moffatt* v. *Burland, supra* note 114 at 80-82.

Two noteworthy principles emerge from this line of cases. First, a trustee for creditors under a voluntary assignment by an insolvent may sue in his own name. He may do so even though he has no personal interest in the estate assigned since, by his trust, he acts for the creditors. He may have ostensible title to the estate, but only as representative of the creditors. Second, the instrument of assignment is constantly referred to as imposing a trust. The nature of the trust, its characteristics, and the characteristics of the property rights vested in the trustee were not disputed. It was merely assumed that the trustee had a fiduciary duty to discharge the trust according to the terms of the contract. The trustee's position, however, was likened to that of an irrevocable mandate conferred by the insolvent for the benefit of his creditors and, perhaps by inference, by the creditors for the *pro rata* satisfaction of their claims to the extent of the assets recovered and liquidated.

b. *Trustee for Debentureholders*

The second circumstance in which the exception arose was where both the right constituting the *créance* and the right to sue on the *créance* arose under a trust deed providing for the issue of debentures. The *créance* is reflected by the debentures and vests in the debentureholder. The right to take proceedings to enforce the debentureholder's claim vests in the trustee under the trust deed.

The first such case was that of *Hatherton* v. *Temiscouata Railway Co.*[119] The railway, authorized by special act[120] to issue bonds secured by a conveyance (cession) of the railway to trustees by trust deed, while remaining in possession defaulted on two series of bonds issued in London. Suit for certain payments and possession was instituted by the trustees. The defence questioned their right to sue. Cimon J., of the Superior Court, relying on *Porteous* v. *Reynar*,[121] based his decision entirely on a construction of the contract. He stated:

> Ces fidéicommissaires sont investis des titres à tous les droits, priviléges et créances stipulés aux dits actes (*trust deeds*) en faveur des porteurs de débentures; et ils ont, notamment, le devoir d'agir en leurs noms, ès-qualités, pour instituer en justice les actions requises pour la bonne exécution de leur fidéicommis, et pour forcer la défenderesse d'accomplir les obligations qu'elle a assumées dans ces deux actes.[122]

But the most significant decision relating to the bond trustee's right to sue was that of *Trois Rivières (Cité de)* v. *Sun Trust Company*.[123] The case went to the Supreme Court of Canada on the question of the construction of a guarantee of the City of Three Rivers (Trois Rivières).[124] However, it is the Quebec Court of Appeal decision that is of particular interest. The Three Rivers Shipyards defaulted on payment of its

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[119] *Supra* note 81.
[120] S.C. 1887, c. 71, ss. 14ff.
[121] *Supra* note 112.
[122] *Hatherton, supra* note 81 at 483.
[123] (1922), [1923] 34 B.R. 351 (C.A.).
[124] See *Three Rivers (City of)* v. *Sun Trust Company*, [1923] S.C.R. 496.

bonds, which were guaranteed by the city and issued under a trust deed pursuant to the S.C.P.A. Suit by the trustee was contested by the city on the grounds that, in view of article 81 (now article 59) C.C.P., the trustee, being the representative of the bondholders, had no right to sue. Chief Justice Lamothe disposed of this defence with the following statement:

> La convention des parties consacre le droit de la compagnie intimée de demander judiciairement l'accomplissement des obligations contractées. C'est envers la *Sun Trust Company*, que la dite ville s'est obligée; c'est à cette compagnie qu'elle doit payer le capital et les intérêts en cas de défaut du débiteur principal; c'est la *Sun Trust Company* qui est autorisée à donner quittance. Ces sortes d'actes sont devenus fréquents. La jurisprudence a toujours considéré le fiduciaire choisi par les deux parties comme étant le véritable créancier. Les porteurs des débentures sont inconnus; ils changent constamment par le simple transport du document constatant l'obligation. Comme dans la cause de *Porteous v. Raynor* [*sic*], ce fiduciaire est le véritable créancier, c'est à lui seul que le débiteur principal ainsi que la municipalité ont affaire.[125]

The trust deed contained the usual clause restricting the bondholders' right to sue to circumstances where the trustee failed to do so. Here the court relied upon the contractual right of the trustee to obtain payment from the guarantor.

Mr. Justice Martin, on the issue of the trustee's power to sue, held as follows:

> Since the decision of the Privy Council in the case of *Porteous v. Reynard* [*sic*], overruling as it did the decisions of the Supreme Court in the cases of *Browne v. Pinsonneault* and *Burland v. Moffatt*, and what was said by the Supreme Court in the later case of *Mitchell v. Holland*, I do not think it has ever been seriously contended, except in the present case, that a trustee for bondholders could not maintain an action as such trustee to enforce the provisions of the trust deed. Later cases have followed these decisions. In *Hatherton v. Temiscouata Railway*, the late Mr. Justice Caron, in his usual able and exhaustive manner, dealt with this question.[126]

Thus the courts reconciled the contractual scheme of the corporate trust deed with Quebec's civil law by recognizing the right of the trustee to sue, even though the trustee is not the ultimate holder of the debt. One further large step of reconciliation was achieved.

As noted earlier, the trustee's right to sue was reaffirmed, to a degree, by sections 27 to 31 of the S.C.P.A. Through the various stages of reform, these provisions were repealed.[127] But in the process the principle *personne ne plaide par procureur* was modified. Article 59 C.C.P. now contains an exceptional paragraph expressly sanctioning the right to sue of trustees, curators and others representing persons who are not fully able to exercise their rights to plead. In particular, the following sentence was added:

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[125] *Trois Rivières (Cité de)* v. *Sun Trust Company*, *supra* note 123 at 352-53.

[126] *Ibid.* at 356 [footnotes omitted]. Mr. Justice Martin also cited *Fysche* v. *Tombyll*, [1900] 6 R. de J. 556 (C.S.); *Levis County Railway Company* v. *Fontaine*, [1904] 13 B.R. 523 [hereinafter *Levis*].

[127] See *supra* notes 3 and 7.

> Il en est de même de l'administrateur du bien d'autrui pour tout ce qui touche à son administration...
>
> This also applies to an administrator of the property of others in respect of anything connected with his administration ...[128]

Thus the trustee's power to sue on behalf of the debentureholders continues to be recognized following reform. However, to achieve certainty it is important that the trust deed define these powers as well as the trustee's responsibilities. In our history of trust-deed litigation, the most constant theme developed by the courts is that the intention of the parties governs their rights and that their intentions must be determined by reference to the express language of the trust deed, as understood within the civil law.[129] Reform has not changed this principle.

4. Characterization of the Relationship between the Trustee, the Issuer and the Debentureholder

The process of synthesizing the concept of three-party corporate trust financing with the traditional institutions of Quebec's civil law led inevitably to judicial consideration of the trustee's relationship to the issuer-debtor on the one hand, and the bondholder, on the other.

a. Trustee As Veritable Creditor

In 1923, in *Trois Rivières (Cité de)* v. *Sun Trust Company*,[130] the Quebec Court of Appeal held that jurisprudence had always considered the trustee the veritable creditor.[131] More recently, in *Zoltom Investments Inc.* v. *Rodgers*,[132] Mr. Justice Lamer (then of the Quebec Court of Appeal) held that a Quebec trustee for foreign bondholders need not post security for costs: "[q]uoique représentant des obligataires le fidéicommissaire en sa qualité de créancier délégué et le véritable demandeur."[133] He also stated:

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[128] *Implementation Act, supra* note 7, s. 190.

[129] See *Hatherton, supra* note 81; *Drummond, supra* note 82; *Levis, supra* note 126; *Laliberté* v. *Larue, supra* note 14; *Perron* v. *l'Eclaireur (Ltée)* (1933), [1934] 57 B.R. 445; *Quebec Productions Corporation* v. *Lavigne* (1971), [1972] C.A. 172; *Ivey* v. *R.*, [1938] 76 C.S. 543, rev'd [1939] 66 B.R. 37, 1 D.L.R. 631.

[130] *Supra* note 123.

[131] Three subsequent Superior Court cases suggested strongly that he was not the creditor for purposes of a 60-day notice under article 1040A C.C.L.C. The 60-day-notice question was decided in the opposite sense in three further cases (see L. Payette, "La fiduciaire pour obligataires et l'avis de soixante jours" (1971-72) 74 R. du N. 412 and the unreported judgments appended thereto; J.R. Hannan, "Trust Deed Security and Competing Creditors" in *Corporate Debt Financing, supra* note 5, 29). *Contra*: *Snowlarks Ski School Inc.* v. *Mont Gabriel Lodge (1973) Inc.*, [1975] C.S. 790; *Immeubles Patenaude Ltée.* v. *Trust Général du Canada*, [1975] C.S. 983; *Gauthier* v. *Banque canadienne nationale*, [1978] C.S. 875.

[132] [1979] C.A. 534 [hereinafter *Zoltom*]; see also *Sous-ministre du Revenu du Québec* v. *Formulations Epoxyde Beaudry Inc.* (6 July 1984), Terrebonne 700-05-002009-821, J.E. 84-790 (Sup. Ct.).

[133] *Zoltom, ibid.* at 536.

> De l'ensemble de la jurisprudence il est depuis longtemps accepté que le fidéicommissaire ne plaide pas au nom d'autrui mais en son propre nom ès qualités de représentant de la masse des obligataires. Il est, pour ainsi dire, en vertu de l'acte de fidéicommis ... «le créancier «délégué» ou créancier des qualités de fiduciaire». Sans pour autant posséder tous les attributs du «*Trustee*» du *Common Law* qui résultent du morcellement du droit de propriété en «*beneficial ownership*» et au «*Legal Title*» et du partage de celui-ci entre le trustee et les obligataires, le fidéicommissaire en droit québécois a, en regard des stipulations que l'on retrouve généralement dans les actes de fiducie et que l'on retrouve dans le cas sous étude, une existence beaucoup plus autonome que le simple mandataire ou celui que de façon générale représente un autre.[134]

He cited *Trois Rivières (Cité de)* v. *Sun Trust Company* among other authorities.

b. Trustee As Mandatary

In *Trust Général du Canada* v. *Marois*,[135] Mme Justice l'Heureux-Dubé (then of the Quebec Court of Appeal) stated: "La fiduciaire, en principe, est un mandataire d'une part de la débitrice et d'autre part de l'obligataire."[136] She noted that in respect of a widely held issue of bonds, authority considers the trustee to be the "véritable créancier de l'obligation",[137] but found it unnecessary to consider the question of who is the true creditor, as in the case before her there was only one bank as creditor-holder of the bonds.

The Quebec Court of Appeal again characterized the trustee as both the mandatary of the bondholder and the nominal creditor for enforcement of the security in *Société nationale de fiducie* v. *Québec (Sous-ministre du Revenu)*.[138] Here, the deputy revenue minister, acting under section 14 of the act governing the Ministry of Revenue,[139] attempted to collect from the trustee under the corporate trust deed taxes owing by the debtor, on the ground that the trustee was a *concessionnaire*, liquidator or administrator of the debtor's property. Mr. Justice LeBel, in determining that the trustee was in the position of a hypothecary creditor, examined the S.C.P.A. and the trust deed and concluded:

> Le système de garantie créé pour assurer le paiement des obligations a une première conséquence sur le statut du fiduciaire. Celui-ci, pour les fins de l'application de la *Loi sur les pouvoirs spéciaux des corporations* et de l'acte de fiducie, peut être considéré comme le créancier. Les sûretés sont créées en

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[134] *Ibid.*

[135] [1986] R.J.Q. 1029 (C.A.) [hereinafter *Marois*]. The judgment cites with approval Payette, *supra* note 131; R. Demers, *Le financement de l'entreprise: aspects juridiques* (Sherbrooke, Qué.: Revue de droit, Université de Sherbrooke, 1985) at 95; L. Lilkoff, "La responsabilité du banquier dispensateur de crédit en droit québécois" (1985) 19 R.J.T. 145 at 160; *Attillasoy* v. *Crown Trust Co.*, [1974] C.A. 442; *Crown Trust Co.* v. *Higher* (1975), [1977] 1 S.C.R. 418, (*sub nom. Atillasoy* v. *Crown Trust Co.*) 69 D.L.R. (3d) 404. It also cites *Zoltom*, *supra* note 132.

[136] *Marois*, *ibid.* at 1049.

[137] *Ibid.* at 1052.

[138] [1990] R.J.Q. 92 (C.A.) [hereinafter *Société nationale de fiducie*].

[139] *An Act respecting the Ministère du Revenu*, R.S.Q. c. M-31.

> sa faveur. Les droits qui en résultent, notamment celui de prendre possession d'administrés et de vendre sont conférés. Ils ne sont pas accordés directement aux obligataires, bien que le fiduciaire ne les détienne certes pas pour lui-même mais pour leur bénéfice et leur protection.[140]

c. *Attempted Reconciliation*

Thus the cases studied reveal that we have a trustee who, at one and the same time: (i) acts as the creditor, (ii) has more autonomy than a simple mandatary, (iii) is a mandatary for the debtor, and (iv) is a mandatary of the debentureholders. Mr. Justice LeBel, in a feat of some intellectual agility, attempted to reconcile these ideas in *Société nationale de fiducie* v. *Québec*:

> Le fiduciaire a le droit d'agir lui-même. La règle est la même, qu'il s'agisse de l'exercice des pouvoirs particuliers que lui accorde la loi ou des recours ordinaires qui lui appartiendraient, comme à tout créancier en vertu du droit commun, pour exercer ses sûretés, comme l'action en réclamation de la *créance*, les recours hypothécaires, etc.
>
> Créancière, l'appelante apparaît aussi comme le mandataire de l'obligataire dans un cas comme celui-ci. L'on n'a pas examiné, dans cette affaire, le cas des émissions d'obligations à caractère public, où pourraient être impliqués des centaines ou des milliers de détenteurs d'obligations et où le statut du fiduciaire mériterait d'être analysé de façon spéciale. L'on se trouve devant un prêt consenti par une institution financière particulière, unique même, en l'espèce. L'acte de fiducie n'est qu'un instrument destiné à lui fournir les sûretés qu'elle recherche. Le fiduciaire n'agit souvent, dans plusieurs cas, que sur instruction spécifique de l'obligataire unique, qui est l'institution financière, la Caisse d'entraide économique de Frontenac. Il en va ainsi d'un acte comme de la demande de paiement.
>
> . . .
>
> On pourrait certes citer des dispositions de l'acte de fiducie qui confèrent à certains égards, au fiduciaire, le statut de mandataire du débiteur ...
>
> . . .
>
> Ces dispositions autorisent l'appelante à poser certains actes au nom ou au lieu et place du débiteur. Ce mandat, toutefois, est subordonné en lui-même au mandat principal, qui résulte de l'acte de fiducie en pareil cas et vise à faciliter l'exécution de celui-ci:
>
> > Le rôle du fiduciaire, même si on peut dire strictement qu'il inclut un mandat de la part du débiteur à celui-ci, est un mandat forcé qui n'existe que pour mettre en oeuvre l'abandon par le débiteur de son immeuble entre les mains du fiduciaire et faciliter l'obligation que celui-ci assume d'en disposer pour le bénéfice des créanciers.

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[140] *Société nationale de fiducie*, *supra* note 138 at 102.

> Les mandats du fiduciaire ont comme objet la protection des intérêts des obligataires et la facilitation de la réalisation des garanties.[141]

Mr. Justice LeBel, quoting Mr. Justice Paré, attempted to rationalize the confusing and conflicting descriptions of the bond trustee's role. He settled principally on the notion that the trustee is a mandatary. He was very careful to distinguish the circumstances requiring the characterization of the trustee in a public (widely-held) bond issue. There is much other authority in the same sense.[142] Note, however, that for widely-held issues, Justices Lamothe and Martin in *Trois Rivières (Cité de)* v. *Sun Trust Company* and l'Heureux-Dubé in *Trust Général du Canada* v. *Marois* found the trustee to be the veritable creditor of the bond issuer, as did Mr. Justice Rinfret in *Laliberté* v. *Larue* and Mr. Justice Lamer in *Zoltom Investments Inc.* v. *Rodgers*.

C. Judicial Characterization of the Trustee Unsatisfactory

The long history of the courts' attempts to characterize the corporate trust deed in terms of the known institutions of the civil law has left a rich legacy of judicial constructs. The adaptation of the concepts of Quebec law to the issue of debentures and the rights of the parties under the debenture trust deed has provided satisfactory solutions to the first three major problems of characterization (debentures governed by Quebec law, charges equated to hypothecs, and trustee's capacity to sue on behalf of the debentureholders).

However, the characterization of the position of the trustee as creditor or as a mandatary or double mandatary was not, and today is not, satisfactory. Moreover, it seems to a degree to hinge on whether the issue of debentures is close-held or widely-held. When is an issue of debentures close-held and when is it widely-held? Generally, the trust deed does not tell you, as the same form is employed for both types of issue. Moreover, one type of outstanding issue may become the other. Does the characterization of the trustee change in this event? Is it close-held when debentureholders number less than five, ten or fifty? Is it widely-held only when some debentures are payable to bearer or traded publicly? Here the process of synthesis did not work very well. The inadequacy of this approach warrants further illustration.

In the notes which follow, codal references are to the C.C.Q., as it now will govern the thousands of outstanding trust deeds. But generally speaking the principles that applied under the C.C.L.C. (although perhaps less fully articulated) were the same.

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[141] *Ibid.* at 103, quoting *Gaz Métropolitain Inc.* v. *Société nationale de fiducie*, [1984] C.A. 140 at 144, Paré J., a decision with essentially the same analysis.

[142] See *Banque canadienne nationale* v. *Normandeau*, [1976] C.S. 285; *Mercure, Béliveau et Associés* v. *Gaz métropolitain*, [1980] C.S. 471, 35 C.B.R. 174; *Commission des normes du travail* v. *Cie de gestion Thomcor* (26 February 1986), Montreal 500-05-005867-831, J.E. 86-400 (Sup. Ct.); *Commission des normes du travail* v. *Cie de gestion Welfab*, [1989] R.J.Q. 2547 (Sup. Ct.); *Vermatex Inc. (Syndic de)*, [1988] R.J.Q. 2136 (C.A.); L. Lévesque, *L'acte de fiducie* (Cowansville, Que.: Yvon Blais, 1991) at 72-73.

1. Trustee As Veritable Creditor Unsatisfactory

The trustee can be characterized as the creditor — or delegated or veritable creditor — for purposes of exercising the right to sue on the debentures, but is clearly not the creditor for purposes of agreeing to a compromise, a settlement, an exchange, a novation of securities, or to alternate security or for purposes of a release of the original security in the absence of complete payment. Some trust deeds do empower the trustee to do some of these things under defined circumstances, but such provisions are not commonly found and are unlikely to provide exhaustively for all circumstances which might arise. They are likely to fail for uncertainty.

The position of being both the veritable creditor and a mandatary of the creditors is also most likely to place the bond trustee in a conflict of interest.

2. Trustee As Mandatary Unsatisfactory

The idea that the trustee is a mandatary of the bondholders, or is likened to a mandatary at all, is most inappropriate in the context of widely-held issues of securities. In such issues the necessary consent of the mandator is absent (2130), since on creation of the deed and the debentures he is unknown.

Various other fundamental rules of mandate are also inconsistent with the trustee's role under the corporate trust deed. The public debentureholders would never accept that they are responsible for the acts of the trustee (2152), that they must indemnify the trustee (2154), or cover the trustee's expenses (2150), or pay interest on the trustee's advances (2151), or be liable for damages caused to third parties (2160) unless such debentureholders were first called to a meeting and advised of a specific plan of action and of the consequences, a consultation which rarely happens. The debentureholder expects the trustee to act unilaterally and to use his or her discretion.

Similarly, neither the trustee (nor the issuer) would accept that the relationship between the debentureholder and the trustee terminates if the debentureholder dies or becomes bankrupt (2175). What if the bankrupt is one of fifty debentureholders? What if he is one of two? Two of five, etc.? As Professor Lubin Lilkoff has stated, "[a]insi le mandat du fidéicommissaire est confus et boiteux."[143]

3. Double Mandatary Unsatisfactory

The double-mandate concept is also extremely awkward as the mandatary is obliged to act in the best interests of both mandators and to avoid conflicts of interest (2138). Particularly after default, he cannot always act in the best interests of both the debtor and the creditor.

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[143] Lilkoff, *supra* note 135 at 160.

4. Other Incidents Where Mandate Unsatisfactory

Under many corporate trust deeds, the powers granted by the debtor to the bond trustee often extend well beyond the ordinary scope of mandate or the ordinary execution procedures of a creditor. Two examples illustrate clearly why the "mandatary" analysis is inadequate.

The trustee is often empowered to intervene and to negotiate in any expropriation or insurance-loss settlement. Once this has been achieved, any indemnity is usually received by the trustee. The security lost may not be the entire security; the indemnity may be less than the secured debt. Upon receipt of the indemnity, the trustee has at least four choices: (i) release the money to the debtor, (ii) release it against substitution of new adequate security or release it by progress advances against reconstruction, (iii) invest it at interest and hold it as a part of the security or (iv) apply it in payment or part payment of the bonds. The trust deed may contain clauses providing the trustee with some guidance or direction on these matters, but in most cases it does not. There may be no default and accordingly no requirement to proceed to realize on the security. If the rules of mandate applied, the trustee would have to use his discretion *in the best interest of the bondholders* (1309). This may not be in the issuer-company's perceived best interests and may also not be consistent with the desires of one or more bondholders. The conflict of interest is manifest if the trustee is a double-mandatary.

Most trust deeds also permit the trustee to consent to a consolidation, amalgamation or merger of the company with other companies upon terms which assure protection of the bondholders' interests. Thus if such protection is provided for, according to the terms of the transaction, the bonds will ordinarily remain outstanding. Such terms typically involve preserving the rank and continued security of the rights of the bondholders against the continuing or merged entity. Dilution of the value of the security or of the debtor's expected cash flow, and ability to pay the service charges of the bonds, may also be a factor. Again, the deed may contain clauses giving the trustee some guidance, but essentially the trustee will be obliged to exercise discretion. If the rules of mandate applied, the trustee would be almost certain to demand further instruction from the bondholders and from the company. And these instructions could conflict.

The alternative solution is that the deed creates a true "trust" as now understood under the C.C.Q. To understand how the new law of trusts would apply, one should first examine the essential elements of the new Quebec trust.

II. Corporate Trust Deeds after 1994

A. Civil-Code Reform and the Trust

1. Introduction

One of the most radical of the reforms introduced by the C.C.Q. is an extension of the law of trusts. It is radical as it is an institution heretofore used in only limited respects in civil-law systems and, accordingly, little understood by most civilian practitioners. However, as a concept it is not entirely foreign to Quebec civil law. Family trusts created by will or by gift have been with us since 1879.[144] As examined above, the corporate trust deed securing debentures, although not called a trust, has been with us since the middle of the nineteenth century. Charitable foundations have been known for centuries. They are reflected in article 869 C.C.L.C., which uses the term "trustees" in describing the legatees of such bequests. In more recent times, trusteed pension funds and investment trusts, many of which purport to be governed by principles of the law of trusts, have become common. So have forms of deposit, escrow, voting trusts, mandate and other devices for the separation and designation of property intended for specified uses. Many of these have been the creatures of special statute, others the development of contract. The function of trust companies and their segregation of trust funds from their own patrimonies (and from the patrimonies of their other clients) have been with us since the last century.[145]

In my opinion the draftsmen of the C.C.Q. developed the trust as an institution of our civil law in a most ingenious way. They have expanded and rendered more universal our relatively primitive law of testamentary trusts. They have dropped the provision of the former law that the trustee is seized of the property as depositary and administrator for the beneficiaries, and they have developed extensive and flexible rules for the administration of property of others to assure responsible behaviour. They have defined adequately, and through a concept reasonably understandable within existing principles of civil law, the relationship between settlor, beneficiary and trustee. They have dealt with the problem of ownership of trust property (one that has bothered common-law theoreticians for nearly 300 years) with a stroke of the pen, by the introduction of the concept of a patrimony by appropriation (1261), an ownerless patrimony. A patrimony by appropriation is now an express exception to the principle that all property has an owner (915). At the same time the traditional inherent attributes of ownership, the *usus*, *fructus* and *abusus*, would seem to be reflected in the expanded notion of the trust and dealt with by reasonably comprehensive rules.

But the draftsmen of our new law have done much more. In formulating the thirty-nine articles of the C.C.Q. on the trust (1260-1298), and the intrinsically related seventy-one articles providing the rules on the administration of the property of oth-

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[144] See *Act Respecting Trusts*, *supra* note 46.

[145] See *Montreal Safe Deposit Company Amendment Act*, *supra* note 43; *The Royal Trust and Fidelity Company Act*, *supra* note 44.

ers, they have provided a statement of the principles behind the many statutory trusts that already existed in Quebec.

2. What Is a Trust?

As has been noted by Professor John E.C. Brierley, in his paper on trusts in *La réforme du Code civil*,[146] the C.C.Q. does not truly provide a definition of a trust. Brierley recognizes that, fundamentally, any definition is likely to be incomplete (*lacunaire*). He then states: "Il s'agit, en somme, d'une relation juridique triangulaire reconnue en vue d'une affectation des biens aux finalités permises par la loi."[147] Brierley has also noted that "the trust proceeds upon the idea that, as a matter of fundamental principle, the beneficial enjoyment of property can be separated from its management."[148]

Professor D.W.M. Waters has attempted to describe a trust as "a relationship based on property control and property enjoyment between two persons, the trustee who controls and the beneficiary who enjoys."[149] After reviewing several common law definitions, Waters states that a civilian would be more likely to see the trust simply as "the dedication of property to the carrying out of a purpose."[150]

But what is a trust in the civil law of Quebec? Two features of the C.C.Q. establish fundamental principles that warrant further examination.

First, the trust represents a distinct way in which ownership of property may be held. It is not a mode, a dismemberment or a restriction on ownership. It is on a plane apart from ownership. The law of trusts is found in Book Four of the C.C.Q. — "Property". The Book on Property, after describing various kinds or classes of property, contains a series of titles or parts describing the various permitted interests in property. These include ownership, modes of ownership (undivided and divided co-ownership and superficies), dismemberments of the right of ownership (usufruct, servitudes and emphyteusis), restrictions on disposition (inalienability and substitution), and finally, patrimonies by appropriation (foundations and trusts). After "ownership", all these titles, except the last, address either an interest in the thing that may be shared, or the ways in which an interest in the thing may be less than ownership. The last, "patrimonies by appropriation", however, sets out the conditions according to which all interests in the property, including ownership itself, are dedicated to a purpose. The C.C.Q. treats the *corpus* of the trust, the trust patrimony once the

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[146] J.E.C. Brierley, "De certains patrimoines d'affectation: Les articles 1256-1298" in *La réforme du Code civil*, vol. 1 (Sainte-Foy, Que.: Presses de l'Université Laval, 1993) 735 [hereinafter "Certains patrimoines d'affectation"].

[147] *Ibid.* at 745.

[148] J.E.C. Brierley, "The New Quebec Law of Trusts: The Adaptation of Common Law Thought to Civil Law Concepts" in H.P. Glenn, ed., *Droit québecois et droit français: communauté, autonomie, concordance* (Cowansville, Que.: Yvon Blais, 1993) 383 at 385.

[149] D.W.M. Waters, *Law of Trusts in Canada*, 2d. ed (Toronto: Carswell, 1984) at 4.

[150] *Ibid.* at 5.

trust has come into existence, as fully as it does ownership itself (947). It introduces a new concept respecting the retention, use and disposition of property.

Second, the C.C.Q. now describes a trust, not in terms of a contract, but in terms of a result. This principle is of paramount importance. The C.C.Q. declares:

> **1260.** La fiducie résulte d'un acte par lequel une personne, le constituant, transfère de son patrimoine à un autre patrimoine qu'il constitue, des biens qu'il affecte à une fin particulière et qu'un fiduciaire s'oblige, par le fait de son acceptation, à détenir et à administrer.
>
> **1260.** A trust results from an act whereby a person, the settlor, transfers property from his patrimony to another patrimony constituted by him which he appropriates to a particular purpose and which a trustee undertakes, by his acceptance, to hold and administer.

The essential elements are (i) a settlor, (ii) a transfer of property, (iii) an appropriation of the property to a particular purpose, and (iv) a trustee. These essential elements reflect the list established by Rinfret J. in *Curran* v. *Davis*.[151]

The reference to a "particular purpose" in article 1260 takes us to article 1266, the first paragraph of which identifies, and limits, the purposes for which trusts may be established:

> **1266.** Les fiducies sont constituées à des fins personnelles, ou à des fins d'utilité privée ou sociale.
>
> **1266.** Trusts are constituted for personal purposes or for purposes of private or social utility.

The articles of the C.C.Q. which immediately follow article 1266 define these different classes of trust, contrasting each type with the others. These articles establish that, generally speaking, "particular purpose" means that a trust must be in favour of one or more beneficiaries. The beneficiary may be more or less directly determined or determinable or abstract, according to the characterization of the type of trust. Thus in a personal trust the beneficiary must be one or more determinable persons (1267), while in a social trust the benefit may be one of general interest such as education (1270). The beneficiary of a private trust can be in between these two:

> **1268.** La fiducie d'utilité privée est celle qui a pour objet l'érection, l'entretien ou la conservation d'un bien corporel, ou l'utilisation d'un bien affecté à un usage déterminé, soit à l'avantage indirect d'une personne ou à sa mémoire, soit dans un autre but de nature privée.
>
> **1268.** A private trust is a trust created for the object of erecting, maintaining or preserving a thing or of using a property appropriated to a specific use, whether for the indirect benefit of a person or in his memory, or for some other private purpose.

Note also that the duration of a private trust or of a social trust (unlike a personal trust) may be indefinite (1273). It is only the private trust that is of interest in this paper.

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[151] [1933] S.C.R. 283 at 304, respecting the form of trust found in the C.C.L.C. See also *Darling* v. *Québec (Sous-ministre du Revenu)*, [1996] R.D.F.Q. 28 (C.A.).

Three additional rules, and only these, must be complied with for a trust to result. First, there must be a contract or other express juridical act (1262). Second, if the trustee is a corporation, it must be a trust company authorized to do business in Quebec (1274).[152] Third (which would rarely be put in question in relation to a corporate trust deed), if either the settlor or beneficiary is a trustee, at least one other trustee must be neither settlor nor beneficiary (1275).[153]

Note also that article 2 of the C.C.Q. provides that a trust may exist only where the law admits of it. Since a trust arises not merely where one is intended to be created according to the terms of a contract, but "results" automatically when the essential criteria of article 1260 are present, then if the four elements noted above are found together, the courts will be obliged to characterize the resulting juridical relationship as a trust. Reciprocally, to determine if any contract or other act that purports to create a trust does in fact do so, the courts must assess whether the fundamental elements are in fact present.

B. The Trust and the Corporate Trust Deed

There is little doubt that the legislature intended the new law of trusts to apply to the corporate trust deed. This is affirmed by the *Commentaires* on article 1260:

> Elle permet, par sa généralité, de couvrir les manifestations du concept de fiducie que connaissent les lois particulières, y compris la fiducie pour obligataires, prévue par la *Loi sur les pouvoirs spéciaux des compagnies* ...[154]

In relation to the trust established by contract (1262), the *Commentaires* state:

> Il suffit de penser, en effet, à la fiducie pour obligataires, prévue par la *Loi sur les pouvoirs spéciaux des compagnies* ou aux diverses fiducies visées par la *Loi sur les impôts*, telles les fiducies d'investissement à participation unitaire, les fiducies de fonds mutuels ou les fiducies constituées en vertu d'un régime enregistré d'épargne-retraite, d'épargne-études ou autres, pour constater que les fiducies établies par contrat à titre onéreux existent dans notre droit. Le code consacre désormais l'évolution du concept de fiducie en droit statutaire.[155]

With regard to article 2692, the *Commentaires* disclose: "Cet article est conforme au droit antérieur".[156]

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[152] See also *An Act respecting Trust Companies and Savings Companies*, R.S.Q. c. S-29.01.

[153] It is my opinion that this rule affords no real legal purpose and that if the concept of trust takes hold in Quebec, both it and the requirement that a corporate trustee must be a trust company will be read down by the courts in many commercial trust situations. They are unnecessary to assure either competence or avoidance of conflicts and detract from the fundamental idea that a trust results from a property situation.

[154] *Commentaires, supra* note 6, vol. 1 at 748. In *Verdun (Municipalité de)* v. *Doré*, [1995] R.J.Q. 1321 (C.A.) at 1327, the Court held that the *Commentaires* were admissible, not as absolute authority, but to aid in the evaluation of legislative intention.

[155] *Ibid.* at 751.

[156] *Commentaires, supra* note 6, vol. 2 at 1686.

Let us now see if the required criteria of article 1260 are met by the corporate trust deed. Under a corporate trust deed there is a settlor, the debtor-issuer of the securities. There is also a trustee, usually an independent trust company which is neither settlor nor beneficiary. The trustee may either be identified in the trust deed as the "trustee", or, as has sometimes occurred since reform, as the "holder of the power of attorney" or the *fondé de pouvoir*. There is acceptance by the trustee. There is a particular purpose, reflected in the trustee's agreement to act for the benefit of the debentureholders in discharging the cumulation of duties assumed by the trustee under the terms of the corporate trust deed. Typically these duties include the holding of security (if any), exercising the right to represent and sue on behalf of the debentureholders and discharging the extensive administrative duties transferred to the trustee. This purpose is clearly of benefit to the bondholder. The bondholder is the beneficiary.

The only question which requires further consideration is: Do the rights vested in the trustee under the corporate trust deed constitute a transfer of property? More simply put: Is property transferred to the trustee? Here one must consider both the secured issue of bonds (where the trustee holds hypothecs on property or holds other security) and the unsecured issue of debentures (where the trustee acts for the debentureholders and may sue on their behalf, but holds no other security).

1. What Is Property?

What is property? Given the variety of rights which may be transferred to, and be exercisable by, a trustee under a corporate trust deed, this question deserves fairly extensive examination.

Under the C.C.Q., as under the C.C.L.C. and indeed in Roman law, property comprises both things and rights appropriated or able to be appropriated to one's patrimony. The concept of a patrimony is now enshrined in article 2 C.C.Q. The concept of patrimonial rights is also reflected in article 3148 C.C.Q., which affirms the jurisdiction of the Quebec courts respecting patrimonial claims. "Rights" means anything for which a cause of action exists. If the cause of action has economic worth, it is a patrimonial right. As such (and as illustrated below) it is property. This is not a change brought about by the reform of the Civil Code, but to some degree this reform has changed the use of certain terminology. The term "property" (*biens*) was systematically substituted for "things" (*choses*) in much of the redrafting. The use of the term "things" is now restricted to corporeal property (934ff.).[157] Thus in principle all "things" are property, but "property" can refer to more than "things".[158]

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[157] Under the old terminology, some authorities questioned whether all "rights" were property, since the C.C.L.C. often used the term "things" for "property". For example, uncalled capital was found not to be "property" in *Desmarteau* v. *Lord*, [1924] 62 C.S. 297; see also Demers, *supra* note 135 at 81.

[158] See D.-C. Lamontagne, *Biens et propriété*, 2d ed. (Cowansville, Que.: Yvon Blais, 1995) at 2, 18, 41, 43, 48, 106, and 131; see also J.E.C. Brierley & R.A. Macdonald, eds., *Quebec Civil Law: An Introduction to Quebec Private Law* (Toronto: Emond Montgomery, 1993) at 266, 268, 271 and 375. For exceptions to the principle, see arts. 913 and 914 C.C.Q.

The C.C.Q. contains no definition of "property". Nor is "property" confined to the subject matter of Book Four (899ff.). Book Four, with some exceptions, is confined to the rules respecting corporeal property, or material things. To begin with, the scope of the term "property" is revealed through the classifications of "property" found in Book Four. We know that property is either corporeal or incorporeal and is divided into immoveables and moveables (899). Book Four makes reference to incorporeal property almost casually or incidentally. Incorporeal property must include everything that is not a "thing". The C.C.Q. declares that "[r]eal rights in immoveables, as well as actions to assert such rights or to obtain possession of immoveables, are immoveables" (904). Thus real rights in immoveables are a form of property. An immoveable hypothec is a real right giving rise to an action to assert such right, and as such is a form of property (2660).[159]

All property that is not qualified as immoveable is moveable (907). As with real rights in immoveables, real rights in moveables are property (911, 912). A moveable hypothec is stated to be a real right (2660) and as such is a form of property. In fact, real rights in property, and the action to enforce such rights, are assimilated to a right in the property itself.[160]

Many property rights are in fact personal rights. Indeed, all rights in corporeal property and all personal rights are also property,[161] except for certain purely personal rights such as rights to integrity of the person, to privacy, to reputation, conjugal rights and certain familial rights (3,10,32,35). These are also known as "personality" rights (but even some of these personality rights are a form of property, as they may give rise to a claim for damages and may also be transmissible). This characteristic of rights as property is revealed further in Book Five of the C.C.Q. — "Obligations". An assignment of claims (1637ff.) gives to the assignee a right of action for an incorporeal right, the account receivable. The provisions of the law of sale (1708ff.) lead one to conclude that anything that can be the object of sale is property. They include the sale of an enterprise (1767ff.), which as a concept is an incorporeal thing and of necessity involves many rights including claims, both receivable and payable. The sale of rights of succession (1779) is expressly mentioned. The C.C.Q. also mentions the sale of litigious rights (1782), including delictual rights (1457). Rights in contracts of insurance may be both assigned and hypothecated (2461) and as such are property (2660).

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[159] See *Caisse Populaire Notre-Dame de Trois Rivières* v. *Mondou*, [1995] R.J.Q. 950 (C.S.), 23 C.L.R. (2d) 314.

[160] See Lamontagne, *supra* note 158.

[161] *Ibid.* Computer "software" was found to be chargeable property in *Cogebec Inc.* v. *Fiducie Desjardins Inc.* (8 October 1993), Montreal 500-11-004138-927, J.E. 93-1789 (Sup. Ct.). In *Trust Général du Canada* v. *Cie du Trust National* (1989), [1990] R.J.Q. 52 (C.A.), transportation permits were found to be property. The debtor's interest in moveable property as lessee under a *crédit-bail* was chargeable property in *Canada Trust Co.* v. *Banque provinciale du Canada* (7 Augnst 1984), Montreal 500-09-000003-798, J.E. 84-769 (C.A.). In *Hindle* v. *Cornish*, [1991] R.J.Q. 1723 (C.S.), the intellectual content of a lawyer's title opinions and abstracts of title or "know how" were treated as property.

Book Six — "Prior Claims and Hypothecs" — reveals the extent of "property" more fully. A hypothec is stated to be a real right on moveable or immoveable property (2660). Only "property" can be hypothecated.[162] A hypothec is a charge on one or several specific corporeal or incorporeal properties (2666). But is a hypothec itself "property"? It is an accessory to a debt owing, a creditor's claim. As noted above, the claim is property as it carries a cause of action for its collection. It would be unreasonable to suggest that the right of action on a claim is property, but that the rights of action for enforcement of a hypothec are not, or that the right in the hypothec itself is not property. Thus the hypothec itself is also "property".

The rules on hypothecs identify other incorporeal properties. They describe a hypothec on a universality or class of properties, present and future (2665, 2674, 2675, 2676, 2697, 2711), and a floating hypothec thereon (2721). They speak of hypothecs on customers' accounts, patents and trade marks (2684). They make express reference to the hypothecation of present and future rents and insurance indemnities (2695), and of bills of lading representing property and of negotiable instruments (2699). They speak of a hypothec on claims (2676, 2710) and on claims secured by hypothec (2712), in effect a hypothec on a hypothec.

Article 2670 deserves examination. It provides that "[a] hypothec on the property of another or on future property begins to affect it only when the grantor acquires title to the hypothecated right." The term "hypothecated right" ("*droit hypothéqué*") used in article 2670 could, based on a purely grammatical interpretation, refer to both a right of ownership in property and the right to acquire future property. One must infer that a right to acquire future property (most frequently a personal right) can be hypothecated, and that the right to acquire is itself "property". Thus the right of the buyer under an instalment sale and the right of the vendor to redeem property he has sold are property and can be hypothecated. Since a hypothec can only be on "property", such rights themselves must be "property".

It could be argued, I believe erroneously, that article 2670 identifies conditional hypothecs that become effective only when the debtor acquires the property that is the subject of the hypothecated right; and that in consequence the "property" subject of the hypothec comes into being only at that future time. Consider, however, the hypothec on a universality. Future property would only become "property" as each future item of the class (claims, inventory, plant machinery, etc.) is acquired. It would then follow that the hypothec on a universality is not really a hypothec (as a hypothec can only be on property — 2660) until each item of property of the class is acquired. It would also follow that the hypothec on the universality would die if at any moment there were no property to constitute that universality. This appears to contradict article 2674 and cannot be the consequence intended by the legislator.

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[162] The extension of the object of hypothecs to all "property" (2660) harmonizes with the new definition of ownership (947), but the use of the term "real right" is certainly at odds with its classical concept, and may be inappropriate. Traditionally, one could have a real right only in a thing (*chose* or *res*). Thus "ownership" was confined also to "things", even though one had "title" and a personal right in incorporeal property. Article 947 has also departed from classical terminology.

In sum, all things and rights that can constitute the assets of a person's patrimony, all patrimonial assets and rights, are property.[163] This includes all rights, whether real or personal, that can be transferred by contract.

2. Property and the Corporate Trust Deed

Accordingly, the establishment of a corporate trust deed providing for the issue of bonds or debentures involves a transfer of "property". The property transferred is composed not only of the hypothecs or other real or corporeal property interests granted or transferred, but also of the rights of enforcement for recovery of the sums owing to the security holder. This includes the right to sue for payment of the debentures.

Some may question whether the grant of the purely administrative powers (of registrar and bond-transfer agent) constitute a transfer of property. They would argue that a grant of a mandate to perform these functions is not a transfer of property; that the object of a transfer must exist prior to the act of transfer and not be merely a consequence of the power conferred. I would reply that the rigbt to maintain registers, to effect transfers and to perform related services, usually for a fee, whether they pre-exist or are created by the act of transfer, are personal rights that are patrimonial in nature and are enforceable at law. As such, they constitute a transfer of property.

To paraphrase article 1268 (words in brackets added): "A private trust is a trust created [by the corporate trust deed] for the object of ... using a property [administrative functions, rights of action, the security] appropriated to a specific use [administration of the debentures, enforcement of payment, realization of the security] ... for the indirect benefit of a person [the debentureholders]". Thus, all corporate trust deeds, even those where debentures are unsecured, contain a transfer of property sufficient for a trust to result.

This conclusion has its parallel in the common law of England and in the United States. There, under the law of trusts, a *chose in action* may be the subject of a trust and, if vested in the trustee, will give the trustee the right to sue for its enforcement.[164] A *chose in action* has been defined as "[a] personal right not reduced into possession, but recoverable by a suit at law"; and as "[a] right to receive or recover a debt, demand, or damages on a cause of action *ex contractu* or for tort or omission of a duty".[165]

A question collateral to characterizing the corporate trust deed as a true trust warrants examination. Article 1261 of the Code states that the trustee and the beneficiary

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[163] See P.B. Mignault, *Droit civil canadien*, vol. 2 (Montreal: C. Theoret, 1896) at 389; A. Montpetit & G. Taillefer, *Traité de droit civil du Québec*, vol. 3 (Montreal: Wilson & Lafleur, 1945) at 16; Lamontagne, *supra* note 158 at 1; Cantin Cumyn, *supra* note 4 at 71.

[164] See W.J. Mowbray, ed., *Lewin on Trusts*, 16th ed. (London: Sweet & Maxwell, 1964) at 4; D.J. Hayton, ed., *Underhill's Law Relating to Trusts and Trustees*, 13th ed. (London: Butterworths, 1979) at 122-23; Waters, *supra* note 149 at 48.

[165] *Black's Law Dictionary*, *supra* note 49 at 241.

have no real right in the trust property, while article 2660 states that a hypothec is a real right in a property made liable for the performance of an obligation. If the trustee holds no real right does he hold a hypothec or a right of action? The thrust of article 1261 is to affirm that the property of the trust is a separate patrimony and that neither the trustee nor the beneficiary (subject to the terms of the trust instrument) can appropriate its use and enjoyment (the *usus* and *fructus*) to their individual, personal patrimony (see art. 2 C.C.Q.). The economic utility of the property (the right of action, the hypothec) is vested in the trust patrimony and also in the trustee as trustee only (1278), while only the benefit, but not the property, is vested in the beneficiary (1284). The *property* of the trust, the *res*, can thus accommodate a right of action for the benefit of another (59 C.C.P.) as readily as it can accommodate a corporeal thing.

C. Interlude: Alternative Juridical Analysis of the Corporate Trust Deed

Prior to reform, enforcement of trust deeds by the courts always occurred in the context of the special legislation that sanctioned the contract through the mention of the term "trust deed", "trustees" or both. With reform, the express legislative sanction of the use of trust deeds in this context was withdrawn. The repeal of sections 27 to 34 of the S.C.P.A.,[166] as then drafted, removed all reference to "trust deed" or bond "trustee" contained in the S.C.P.A., and none now appears in the C.C.Q. Thus one might argue that the withdrawal of legislative sanction of the contract renders it no longer expressly contemplated by our law, particularly as the charges and remedies of the S.C.P.A., as interpreted by the courts, have now been made a part of our general law.

It is, however, inconceivable that the withdrawal of the relevant sections of the S.C.P.A. should mean that the corporate trust deed is no longer a type of contract recognized by our civil law. It would also be a step backwards to insist that, in the absence of express legislative sanction, the contract must be forced into a different characterization merely to reflect an earlier jurisprudence, a forced jurisprudence that resulted from a lacuna in the provisions of the civil law of the time. If, as I contend, the corporate trust deed involves a disposition, a transfer of property to a trustee, Quebec's new law of trusts must apply. This principle is consistent with the approach of our highest courts.[167]

I believe that a court would conclude that a corporate trust deed results in a trust where the elements required for the formation of a trust are found to exist. But assuming for the sake of argument that such elements are found not to exist, the alternative characterizations must be examined.

One might suggest, for example, that the contract, or at least a similar type of contract having the same objects, has been preserved through use of the term *fondé de*

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[166] See *supra* note 7.

[167] There is of course no case on point, but see *Laliberté* v. *Larue*, *supra* note 14; *Royal Trust Company* v. *Tucker*, [1982] 1 S.C.R. 250 at 272.

pouvoir in article 2692. This term is intended to refer to the trustee, whether he is called the trustee or something else. Etymologically, the term *fondé de pouvoir* could simply mean "mandatary", just as it could also imply "trustee". The corporate trust deed could also be viewed as a form of *sui generis* contract which appoints an innominate representative of the bondholders, whose rights and duties are determined by the contract alone. Such a representative would now also be subject to the rules respecting the administration of the property of others (1299ff.). Indeed, article 1316 gives the administrator express power to sue and be sued in respect of anything connected with his administration. There is certainly no doubt that these articles of the C.C.Q. now apply to the trust deed and to the rights and duties of the bond trustee to the extent that the deed does not vary them (1299) or is unclear or incomplete. This solution would be entirely consistent with the jurisprudence. The courts have consistently held that the trustee's rights and duties are to be determined primarily by a reading of the contract.[168] This result would preserve the *status quo*, supplemented by the further regulation of the contract by the provisions of the C.C.Q. on the administration of the property of others. The title on the administration of the property of others does not create a new civil-law institution.[169] It merely consolidates the basic rules of administration of property that are to apply to many types of administrator. These include the tutor (208), the Public Curator (262), the curator (282), the usufructuary in part (1142), the manager of property in undivided co-ownership (1029) and of the syndicate in divided co-ownership (1085), the trustee (1278), and the hypothecary creditor in possession (2768, 2773). They apply equally to a mandatary charged with the administration of property of his mandator (2135).

This alternative solution would continue the unsatisfactory characterization of the trustee's role without the interpretive advantage provided by the legislative identification of the contract previously found in the S.C.P.A.[170] It would also be inconsistent with the assertions in the *Commentaires* to the effect that article 2692 was not intended to change the law and that the new law of trusts was intended to embrace trusts formerly contemplated by the S.C.P.A.

D. The Principal Consequences of a Trust

There are a number of consequences that flow from the creation of a trust. First, a trust is not simply a nominate or special contract. A trust creates a legal relationship that goes beyond merely contractual obligations. The obligations of the trustee, if breached, give rise to more than mere damages (see "fifth" consequence below). The trustee is a debtor in the sense that an obligation is owed to another in relation to property, in this case the property forming the trust. Once it is created, a separate patrimony exists (1261). A trust does, however, arise as a result of a contract, a will or another juridical act, and one must turn to the juridical act in order to determine the

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[168] See cases cited *supra* note 129.

[169] *Contra* F. Rainville, "De l'administration du bien d'autrui" in *La réforme du Code civil*, vol. 1, *supra* note 146, 783 at 785: "le legislateur crée un nouveau personnage juridique".

[170] *Supra* note 3.

extent of the trust property and the rights of the beneficiary in the trust. But once a trust "results", the settlor and his heirs, successors and assigns cease to be owners of the property in trust. Equally, the beneficiaries have no real right in the property. To quote Professor Brierley: "En principe, une fois la fiducie créée, elle échappe à son créateur et *a fortiori*, à ses héritiers."[171]

This does not mean that the creation of a trust cannot also be accompanied by a continuing contractual relationship between the settlor and the trustee or the beneficiary and the trustee. The continuing contractual obligations may define the modalities whereby the trustee is to fulfil his or her duties as trustee: for instance, how the trustee is to apply the patrimony to such purpose. They may also stipulate the conditions to be met by the beneficiary before the latter is to receive the benefit. Some trusts, such as estate trusts and pension trusts, may operate without the obligations of the trustee having been defined by or being governed by a contract. Where the trustee's role is defined by contract, however, the contractually defined obligations may form the essence of the trust itself. They may even form an intrinsic part of the trust property. For example, the bond trustee might be appointed registrar and be obliged to maintain the register at Montreal. The reference to Montreal limits and defines the property right of being registrar. The investment trustee may be obliged to create and issue investment units as a form of property. The obligations that must be fulfilled define and determine the characteristics of the investment units and the property right to issue them. In contrast, where ownership of a corporeal property is concerned, such contractual terms are distinct from the essence of ownership. By way of analogy, in a conditional sale there are continuing contractual obligations between the buyer and the seller. Indeed, the fulfilment (or non-fulfilment) of the contractual provisions may determine where ownership of the property that is the object of the sale will lie; but such contractual obligations are not of the essence of the ownership. They cannot modify the quality of ownership. Where they relate to the use of a trust patrimony, however, they may well be an intrinsic part of the trust property.

Second, the property constituting the trust, and comprising either things or rights or both, belongs to the trust. It comprises the trust patrimony. These properties are held by the trustee and are administered by him (1265, 1278). The trustee has the powers conferred by, and limited by, the trust instrument, which can include all the powers of "full administration" (1306, 1307). Full administration includes the power of alienation and the power to change the destination of the trust property. The trustee acts on his own behalf as trustee, not as the representative of the settlor or of the beneficiary. He has title as trustee to such property (1278), although such property does not form part of his patrimony but is a separate patrimony (1261). He administers the trust patrimony *to the exclusion* of the settlor and the beneficiary (1278).

Third, in consequence, the trustee, unlike a mandatary, is not a personal representative. In mandate, personal representation is of the essence of the relationship (2130, 2143). In trust, the trustee has full autonomy, subject always to the restrictions set out

[171] Brierley, "Certaines patrimoines d'affectation", *supra* note 146 at 771.

in the juridical act that constitutes the trust's constating instrument.[172] He has control (1278). In mandate, the rights and powers of the mandatary are limited to those of the mandator and are ultimately subject to the supervision and control of the mandator (2175). The mandator may always renounce a mandate, even if it is irrevocable according to its terms, although the mandator may be liable to damages as a result of renunciation (2179, 2681).[173] In contrast, the beneficiary and the settlor have no power to terminate the trust or to replace the trustee in the absence of fraud (1290) or unless expressly provided for in the trust deed. Subject to the terms of the mandate, the mandatary has "simple administration" only (1301, 1302). The mandator cannot escape responsibility for the lawful acts of the mandatary, while the mandatary can escape responsibility if acting within the mandate. This flows inevitably from the concept of representation.[174] The trustee, in contrast, cannot escape his responsibilities, although he may benefit from certain contractual exculpatory provisions.[175]

Fourth, the trustee is not liable to the beneficiaries on the trustee's own property, as contemplated by article 2645 of the C.C.Q.; the beneficiaries will not ordinarily have recourse against the trustee's own property to satisfy their claims. The trustee remains, however, the debtor of the beneficiaries (and the settlor) in the fulfilment of the obligations respecting the trust property. The trustee must "act with prudence and diligence" and "honestly and faithfully in the best interest of the beneficiary or the object pursued" (1309). In this sense the beneficiary is more than an ordinary creditor.

Fifth, the C.C.Q. gives the beneficiary of a trust several rights to ensure that the trustee fulfils the obligations. The causes of action are: (i) the right to require the trustee to provide the benefit contemplated by the trust (1284); (ii) the right of supervision (1287); (iii) the right to impugn acts of the trustee in fraud of the rights of the beneficiary (1290(2) — a form of Paulian action (1631)); and (iv) with the permission of the court, the right to act instead of the trustee where the trustee refuses, neglects or is prevented from doing so (1291 — a form of oblique action (1627)). These statutory rights are distinct from, but parallel to, the rights arising from contract. Perhaps for greater certainty, these rights are separately provided for in the C.C.Q. because the beneficiary's rights against the trustee are not of their essence contractual, and in many trusts there is no contractual relationship between the trustee and the beneficiary.

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[172] Lamontagne, *supra* note 158 at 47, states that the beneficiary's right in the trust is both personal and real — personal against the trustee but real with respect to the trust property in the event of any abuse by the trustee.

[173] See C. Fabien, "Le nouveau droit du mandat" in *La réforme du Code civil*, *supra* note 146, vol. 2, 881 at 893; C. Fabien, *Les règles du mandat* (Montreal: Chambres des notaires du Québec, 1989) at 73.

[174] See P.B. Mignault, *Droit civil canadien*, vol. 8 (Montreal: Wilson & Lafleur, 1909) at 4 and 56; H. Roch & R. Paré, *Traité de droit civil du Québec*, vol. 13 (Montreal: Wilson & Lafleur, 1952) at 64.

[175] See M. Faribault, *Traité théorique et pratique de la fiducie ou trust du droit civil dans la province de Québec* (Montreal: Wilson & Lafleur, 1936) at 105ff. His preferred description of a trust in civil law is as an autonomous responsible institution, effectively a *personne morale*. He rejects Pierre Lepaulle's "patrimoine approprié" (see P.G. Lepaulle, *Traité théorique et pratique des trusts en droits interne, en droit fiscal et en droit international* (Paris: Rousseau, 1932) at 31). See also *Royal Trust Company* v. *Tucker*, *supra* note 167 at 265.

The remedies for the first two rights (the right to obtain the benefit and the right of supervision) are found in the first paragraph of article 1290 C.C.Q.:

> **1290.** Le constituant, le bénéficiaire ou un autre intéressé peut, malgré toute stipulation contraire, agir contre le fiduciaire pour le contraindre à exécuter ses obligations ou à faire un acte nécessaire à la fiducie, pour lui enjoindre de s'abstenir de tout acte dommageable à la fiducie ou pour obtenir sa destitution.
>
> **1290.** The settlor, the beneficiary or any other interested person may, notwithstanding any stipulation to the contrary, take action against the trustee to compel him to perform his obligations or to perform any act which is necessary in the interest of the trust, to enjoin him to abstain from any action harmful to the trust or to have him removed.

It is clearly of public order. The right to impugn fraudulent acts of the trustee, found in the second paragraph of article 1290, is of the same nature. But in my opinion, article 1290 is also likely to be interpreted as limiting the general extent of the rights of the beneficiary (as well as other interested parties). Thus the right of supervision (1287) should be limited essentially to compelling the trustee to do his duty — to fulfil the object or purpose of the trust for which property was appropriated under article 1260. To compel the trustee "to perform his obligations" (1290) embraces the beneficiary's "right to require the trustee to provide the benefit" (1284). It should also embrace the right of supervision. The right of supervision should not, however, be construed to permit the beneficiary to direct the trustee in the normal day-to-day exercise of the trustee's duties, or to substitute in any way the acts of the beneficiary for those of the trustee taken in the valid exercise of the trustee's discretion. It should be restricted essentially to a demand for an accounting and for the benefit, if the benefit is withheld without right. Beyond receipt of an accounting, the right of supervision should give rise to relief only where the beneficiary establishes that the trustee is not acting "with prudence and diligence" or "honestly and faithfully in the best interests of the beneficiary or the object pursued" (1309). To give supervision a broader meaning would be to deny the trustee the discretion necessary to discharge his duties and would reduce his role to that of a mandatary.

Sixth, and perhaps most important of all, third parties with whom the trustee deals have no recourse against the settlor or the beneficiary:

> **1322.** Le bénéficiaire ne répond envers les tiers du préjudice causé par la faute de l'administrateur dans l'exercice de ses fonctions qu'à concurrence des avantages qu'il a retirés de l'acte. En cas de fiducie, ces obligations retombent sur le patrimoine fiduciaire.
>
> **1322.** The beneficiary is liable towards third persons for the damage caused by the fault of the administrator in carrying out his duties only up to the amount of the benefit he has derived from the act. In the case of a trust, these obligations fall back upou the trust patrimony.

It is the last sentence that is significant. If an obligation "falls back on" ("*retombent sur*") anyone it is no longer *upon* the original party. Under the first sentence the liability is on the beneficiary to the extent of the benefit. Under the second, it is upon the trust patrimony alone. Unlike the mandator, neither the trust beneficiary nor the

settlor is liable to third parties for the acts of the trustee. The third party's recourse is limited to the trust patrimony.

Seventh, it must also be noted that nothing prohibits an aggrieved beneficiary or a settlor who has reserved rights, as permitted by article 1281, from claiming damages from the trustee personally under article 1607 of the C.C.Q. This general right, in contrast to the specific rights established by articles 1284, 1287 and 1290, did not require restatement under the law governing trusts.

Finally, two further observations respecting the liabilities and rights of the trustee are warranted. The beneficiary's rights are essentially personal rights against the trustee, as the settlor, the trustee and the beneficiary have no real rights in the trust patrimony (1261, 1265). By exception, in the event of fraud, the beneficiary has a right to impugn the acts of the trustee and, presumably, to recover for the trust the property affected by such fraudulent acts. This gives the beneficiary a form of *droit de suite* which may be equated to a real right.

E. The Consequences of the Corporate Trust Deed Resulting in a Trust

1. Resulting Relationships

What are the relationships between the company-issuer, the trustee and the debentureholder? They should be explained in terms of, and as defined by, the corporate trust deed itself.

a. The Company and the Bondholders

The legal relationship between the company-issuer and the purchaser-holder of the bonds is that of debtor-creditor (1590, 2644). The corporate trust deed is the constating document which defines that relationship, and by its terms places limits on the creditor's rights to enforce the claim. Such rights are vested in the trustee.

b. The Company and the Trustee

The legal relationship between the company and the trustee is that of settlor and trustee (1260). The settlor transfers to the trustee the property consisting of the administrative functions pertaining to the bonds, the rights of enforcement and the security, if any. All such rights are vested in the trustee by the settlor on behalf of the settlor and of the bondholders, and constitute a term of the bonds when they are acquired by the bondholder. The general theory of trusts under the C.C.Q. can accommodate the transfer of administrative rights and rights of action, as well as security, to the benefit of another, just as it recognizes the transfer of a corporeal thing. In contrast, the statutory trust contemplated by the provisions of the S.C.P.A., combined with the concepts of the C.C.L.C., could not readily accommodate that relationship.

c. *The Trustee and the Bondholders*

The legal relationship between the trustee and the bondholders is that of trustee and beneficiary (1268). The rights (that is the property held by the trustee) are held for the benefit of the bondholders. The rights to take proceedings and to enforce the security must be exercised for their benefit.

2. Effects Generally

All of the general consequences of the creation of a trust (discussed in Part II.D above) should apply, I submit, to the corporate trust deed. There are a number of other specific consequences that also warrant attention.

The principles respecting the recourses of the debentureholder apply both to the widely-held issue, where there are many (even thousands) of debentureholders, and to the close-held issue, where there are a few debentureholders (or even a single debentureholder). The law of trusts makes no distinction between trusts with a multitude of equal beneficiaries and trusts with a single beneficiary.

Since the corporate trust deed results in the creation of a trust, outstanding corporate trust deeds, and new deeds supplemental thereto, also result in trusts. As noted, the legislature has introduced the revised institution of the trust as a new relationship between persons and property and has defined the conditions that must exist for it to "result" (1260). Once they exist, the "result" must follow, whether or not the circumstances arose prior to reform. The C.C.Q. does not state that the result occurs only for future events, nor does it link the trust's creation to the intention of the parties. Accordingly, the new rules on trusts must also apply to situations that already existed on January 1, 1994. By analogy, this is similar to the transformation that takes place for pre-reform assignments of claims, assignments of stocks, builders' privileges and other rights: reform declared these other rights to be hypothecs.[176] The C.C.Q. declares outstanding relationships that qualify as "trusts" to now be "trusts".

Sections 71 to 74 of the *Implementation Act* also deal with various aspects of trusts. Section 73 is the most pertinent:[177]

> **73.** L'administration du bien d'autrui confiée par contrat au gérant de biens indivis ou au fiduciaire avant l'entrée en vigueur de la loi nouvelle est régie par cette loi, de la même manière que l'administration du bien d'autrui confiée par un autre mode.
>
> **73.** Administration of the property of others eutrusted by contract to a manager of undivided property or to a trustee before the new legislation comes into force is goverued by that legislation, as in the case of the administration of the property of others entrusted otherwise than by contract.

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[176] See *Implementation Act, supra* note 7, ss. 133, 135, 137.

[177] *Ibid.*, s. 73; see also *Des Marais* v. *Des Marais*, [1996] R.J.Q. 951 (Sup. Ct.) (leave to appeal granted (C.A. 500-09-002432-961)).

Since the remedies of possession and sale are now available to all hypothecary creditors, those remedies are therefore also available to the bond trustee under a trust who holds hypothecs as security (2773 and 2784). The C.C.Q., moreover, in article 1263, expressly states that in the event of default, the trustee must follow the rules for enforcement of hypothecary rights. In consequence, the various powers contained in the trust deed — permitting the trustee to take possession, to manage and to do all things necessary, and to sell as attorney of the debtor — may no longer be necessary. Reform expressly provides that the "creditor sells in the name of the owner" (2786), which implies that the creditor in some respects acts on behalf of the owner (that is, in the case of a corporate trust deed, on behalf of the issuer). The C.C.Q. also states, however, that the trustee must sell "in the best interests" of the owner (2785). Paradoxically, this provision perpetuates, to some degree, the trustee's conflict of interest that existed under the theory of double mandate.

The provisions of a corporate trust deed that give these powers do not make the trustee a mandatary of the company in the traditional civil-law sense (representation for the performance of a juridical act) but constitute an irrevocable grant of these powers. The idea of a continuing "representation" of the mandator that the mandator may withdraw, and that is still fundamental to the idea of mandate (2130), is incompatible with this intent. The grant of the power is to permit the trustee to demonstrate to third parties that the trustee has this power and can give good title or warranty in the company's name, as fully as the company itself may do. This was effectively noted in *Gaz métropolitain Inc.* v. *Société nationale de fiducie.*[178] This concept of an irrevocable grant of a power to another is also much more consistent with the concept of trust than it is with that of mandate. It should be equated to the capacity conferred on the creditor under article 2786 C.C.Q.

It is also tempting to believe that the inherent conflict in double mandate (should, for argument's sake, such theory continue to apply) is attenuated where administrative possession is elected as a remedy, because a creditor exercising powers of administration now has powers of "full administration" (2773, 1306). Powers of "full administration" include powers of alienation by onerous title, of granting real rights or changing the destination of the property and of charging it with real rights (1307). This should permit the trustee in administration to dismiss employees, to shut down a business, or to cancel leases — not as mandatary of the debtor, but of the bondholders. (In fact there may well be limitations to these full powers for the hypothecary creditor in possession.) If the trustee *qua* mandatary does in fact have these powers, most bondholders would still be extremely upset to learn that they may be individually responsible to third parties for the trustee's actions as an administrator with *full* administrative powers. It seems implausible that a court would hold them to that obligation.

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[178] *Gaz Métropolitain Inc.* v. *Société nationale de fiducie, supra* note 141; see also *Vermatex Inc. (Syndic de), supra* note 142; *Société nationale de fiducie, supra* note 138.

3. Terminology

In view of the language of article 2692, can the terms "trust deed" and "trustee" continue to be used in Quebec even though the article in question now uses the term *fondé de pouvoir*? It is to be noted that article 2692 addresses the form of the deed only. It prescribes that whenever a hypothec secures payment of bonds or other titles of indebtedness, the deed creating it must be granted by notarial act. Article 3060 and the amendments to the S.C.P.A.[179] also employ the phrase *fondé de pouvoir*. In such cases it is probable that the legislature contemplated a variety of structures: simple arrangements whereby various creditors agree that one of them alone will hold a hypothec on their behalf, but also more complex arrangements such as those found in the corporate trust deed. Thus the legislator may have chosen the term *fondé de pouvoir* as a generic term that avoids any restriction of the principles set out in the article to those of a trust deed and that accommodates both the trustee and the mandatary.[180]

As noted above, the minister of justice, in the *Commentaires*, has made it clear that reform in this area was not intended to change the law.[181] In the commentary on the law of hypothecs, expanded to include moveables, future property and the floating hypothec, as well as the hypothecary remedies, the *Commentaires* frequently make reference to the S.C.P.A. as one of the sources.[182] It is unreasonable to suggest that the concepts giving rise to the forms of security and practices that inspired much of this reform must now themselves change.

It is my opinion that the term *fondé de pouvoir* is at best descriptive and merely replaces the notion previously found in the S.C.P.A. that the trustee acts "for the benefit of the bondholders". It can refer to the "mandatary of the creditors" to mandate (2130).[183] It can also have a wider meaning, perhaps one that has different juridical characteristics. As is well argued by Louis Payette,[184] some French dictionaries define *fondé de pouvoir* in a way that is broader than "mandate". *Le Petit Robert* suggests a person "qui est chargée d'agir au nom d'une autre ou d'une société."[185] Mr. Payette notes that the C.C.Q. provides for many categories of representative, including the tutor (177), the curator (258), the trustee (1260), the administrator of property of another (1299), the mandatary (2130) and the hypothecary creditor who sells hypothecated property (2786). One can perhaps add the usufructuary as regards the interests of the owner (1142), she who has a right of use (1175), the institute under a

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[179] See *Implementation Act*, *supra* note 7, ss. 643-648.

[180] Note, however, that the Quebec *Companies Act* continues to employ the term "trust deed" (*actes de fidéicommis*) in the sections providing that a copy of the deed must be forwarded to every holder of any such debenture or other security at his request on payment of a fee (see *Companies Act*, R.S.Q. c. C-38, ss. 78 and 170).

[181] *Commentaires*, *supra* note 6, vol. 1 at 748 and 751; vol. 2 at 1686.

[182] *Ibid.*, vol. 2 at 1666, 1669, 1680, 1682, 1687, 1695, 1698, 1700, 1701, 1720, 1736.

[183] See Claxton, *Security on Property*, *supra* note 2 at 226ff.

[184] See L. Payette, *Les sûretés dans le Code civil du Québec* (Cowansville, Que.: Yvon Blais, 1994) at 166-68.

[185] A. Rey & J. Rey-Deboue, eds., *Le Petit Robert*, vol. 1, rev. ed. (Paris: Le Robert, 1990) at 802. See also *Le Robert Dictionnaire de la langue française*, t. 4, 2d ed. (Paris: Le Robert, 1987).

substitution as regards the substitute (1225), the liquidator of a succession (812), the designated person in the sale of an enterprise (1773), and the sequestrator (2305). I agree with Mr. Payette that had the codifiers intended to refer to mandate, they would have used the phrase "*mandataire des créanciers*". There is no doubt that the English expression in article 2692, "person holding the power of attorney of the creditors", appears to refer to a relationship which is usually one of mandate, but it seems to be merely an awkward translation. I would suggest that the term *fondé de pouvoir*, as used in article 2692, means "representative of the bondholder", the phrase used in the S.C.P.A. It must include a "trustee" for bondholders contemplated by article 1260.

In a close-held issue, perhaps where the debentures are held by a single bank or group of banks, the characterization of the trustee as strictly a mandatary could be appropriate. If so, the deed should be drafted accordingly and called something other than a trust deed.

In practice, however, I submit that little change is needed in terminology. A corporate trust deed may still be called a "trust deed", or perhaps a "deed of trust and hypothec" where an issue secured by hypothec is contemplated. It could readily be called a "trust indenture" if that is the wish of the draftsman or the issuer. This is the term usually used in the financial markets. Although the term "trust indenture" is of English origin and foreign to Quebec, so was the term "trust deed". As noted earlier, it is used in the *Canada Business Corporations Act*,[186] federal legislation which applies to companies in Quebec incorporated thereunder.

The extent of the beneficiary's rights must, of course, be determined from the language of the contract. This principle has been repeatedly noted in the jurisprudence.[187] In some cases, particularly issues of debentures with a single debentureholder, the contract may provide the debentureholder with such rights of direction, even of interference with the trustee's rights, to engage the debentureholder's responsibility as a mandator. Should, for example, the trust deed (or some collateral agreement) provide that the trustee will not act except upon instruction and indemnification by the debentureholder, the rules of mandate should apply, either instead of, or in addition to, those of trust.

On the other hand, where the contract is silent as to the powers of the beneficiary to direct the trustee, it must be assumed that the trustee has very broad and independent powers limited only by the express provisions of the deed, the fulfilment of the general objectives of the trust and the powers of full administration (1306, 1307). Neither the exculpatory provisions of the trust deed, which limit the trustee's responsibility, nor the power to convene the debentureholders to obtain their "consent" to a course of action, should engage the debentureholders' responsibility as mandators. Each case, in other words, will have to be considered upon its own merits.

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[186] *Supra* note 11.

[187] See cases cited *supra* note 129.

4. Form

Article 2692 provides that where a hypothec is to constitute part of the security for bonds or debentures, on pain of absolute nullity (of the hypothec), the deed must be granted by notarial act *en minute*. This is the only express text of law respecting its form.

If the proposed issue of bonds or debentures is not to be secured by a hypothec, there is no requirement that the constating deed be in notarial form. No such form is required to evidence a trust *per se*. Moreover, if the trustee, in addition to having administrative functions respecting the debentures, is obliged to hold security other than hypothecs, there is no requirement as to form. Such other security could include, for example, conditional sales contracts or finance leases, including one or more *credit bail* that are held by the trustee as transferee. It could include a deposit of cash, a guarantee or a letter of credit. It could also include a deposit of cash with instructions to the trustee to invest in the name of the trustee in government bonds, treasury bills and other comparable forms of short term securities. It can, of course, also include any covenants or provisions for default and enforcement that the parties may agree upon.

5. Responsibility of the Trustee

This review would be incomplete without some reference to the responsibility of a trustee towards the debentureholder.[188] A comprehensive study is beyond the scope of this paper, but some brief observations should be made.

Today, subject to the terms of each contract, the duty of care of a trustee and that of a mandatary are substantially the same. The principle that one must act towards others "in good faith" is now expressly stated (6, 7, 1375). The administrator of the property of another (including a trustee) has the duty to act with "prudence and diligence".[189] The administrator has the additional duty to act "honestly and faithfully in the best interest of the beneficiary or the object pursued" (1309). The mandatary must also act with "prudence and diligence" and "honestly and faithfully in the best interest of the mandator" (2138). Both must avoid being in a conflict of interest (1310, 2138) and must disclose any such conflict (1311, 2139, 2143). Furthermore jurisprudence has established that a professional or *commerçant* who holds himself out as having certain technical skills must perform such skills to a reasonable professional standard (2100). This last principle could result in the law imposing different duties of care on

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[188] For a review of the position before reform, see Lévesque, *supra* note 142.

[189] Reform has generally replaced the duty of care of a "prudent administrator" (*bon père de famille*) found in the former law, with that of "prudence and diligence". These terms are found in a host of articles, including 322 (company director), 1128 (usufructuary), 1225 (substitute), 1309 (administrator of property of another), 1855 (lessee), 2088 (employee), 2100 (entrepreneur), 2138 (mandatary), 2283 (depositary). Many other articles defining special capacities adopt the principles and standard of the administrator of property of another. These include 208 & 286 (the tutor), 262 (the Public Curator), 802 (the executor-liquidator), 1085 (the manager of a co-ownership syndicate) and 1278 (the trustee).

trustees and on mandataries, according to the circumstances, but such study is beyond the scope of this paper. There are other incidental duties, but these are the essential ones. There are also slight, but essentially immaterial, differences in the wording of the codal provisions relating to mandatary and those relating to a trustee.

The *Canada Business Corporations Act* obliges an indenture trustee (i) to act "honestly and in good faith with a view to the best interests of the ... debentureholders", and (ii) to "exercise the care, diligence and skill of a reasonably prudent trustee."[190] The first test is identical to the requirement of Quebec's reformed law. The "reasonably prudent trustee" requirement is merely an application of the "reasonably prudent man" test of the common law[191] in the context of a qualified corporate trustee in Canada. A professional level of competence must be inferred. For all practical purposes, it is the same test as that of a *bon père de famille*.[192]

Both the law of trusts and the law of mandate are subordinate to the constituting act in each case. The law of trusts is expressly so (1280, 1299, 1308). The rules on mandate are essentially suppletive to the mandate conferred (2135). With one exception, the duty of care of the debenture trustee will be determined by the trust deed (this reflects the past jurisprudence and authority).[193] The exception is for rules found to be of public order. In the case of trust, for example, it is likely that the power of supervision and control given to the settlor and the beneficiary (1287) are of public order. This power is to ensure that the objects of the trust are fulfilled but, as discussed earlier,[194] ought not to be construed to give either party extensive rights to interfere and direct the trustee in the exercise of his or her discretion.

It is likely that the courts will find that the trustee has some basic duty of care as a matter of public order. Exculpatory measures found in the corporate trust deed (often entitled "protection of the trustee") can and will be enforceable to mitigate, or perhaps more properly to channel, the trustee's duty of care, but will not free him from all responsibility. Thus, according to the parameters of most protective clauses, if the trustee: acts only on the advice of experts who are ostensibly competent; selects agents or depositaries or advisers with reasonable diligence; attempts to call in assets with reasonable diligence; refuses to advance his own funds; fails to give notice before the security is enforceable; or fails to enforce covenants of the issuer where the deed so permits, as the case may be, the court should find that the trustee has discharged the duty imposed upon him, and that he is not further responsible. It is true that under the civil law, contractual exculpatory clauses are enforceable, but it is also true that in most representational situations a minimum standard of reasonable care is imposed.[195] The normal corporate-trust-deed clauses afford the trustee a large measure of protec-

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[190] *Supra* note 11, s. 91.

[191] See *Learoyd* v. *Whiteley*, [1887] 12 A.C. 727, 3 T.L.R. 813 (H.L.), Lord Watson; Waters, *supra* note 149 at 750.

[192] Fabien, *Les règles du mandat*, *supra* note 173 at 138.

[193] See cases cited *supra* note 129.

[194] See comments on article 1290 C.C.Q. in Part II.D above.

[195] See *Van Horne* v. *The Montreal Trust Company*, [1924] 62 C.S. 436 at 441, Rinfret, J.; *Pagé* v. *Cie Montréal Trust*, [1981] C.S. 217, aff'd [1986] R.J.Q. 2890 (C.A.).

tion, but should not relieve him of all responsibility. The provisions of law respecting enforcement of such exculpatory clauses and the basic responsibility of the trustee are similar in the common-law jurisdictions.[196]

Conclusion

Financing through the issue of bonds or debentures under the corporate trust deed developed as a practice in Quebec in largely the same era as it evolved in England and elsewhere in North America. It proved essential to the raising of capital on the international markets for the large public and industrial undertakings sought by every western society from 1840 on. The development of the corporate trust deed was accommodated under Quebec law initially by private bill, and ultimately through the adoption of the S.C.P.A. This enabling legislation sanctioned the device and the related charges and remedies, but did not define them in terms of Quebec's unique legal concepts. This process was left to the courts, which had to reconcile the mechanisms of the S.C.P.A. with the traditional principles of civil law. In the process of doing so, the courts successfully resolved a number of issues in terms which should provide continuing guidance for the future. The courts never satisfactorily explained, however, the relationship of the trustee to the debtor, on the one hand, and to the debentureholder, on the other. The trustee was characterized, according to the circumstances, as the veritable creditor, the mandatary of the issuer and the mandatary of the debentureholder, or some undefined combination of these concepts.

The reforms brought in by the C.C.Q. in 1994 introduced a form of trust broad enough to encompass the structures used in the corporate trust deed. In substance, the principles apply to a corporate trust deed because the corporate trust deed achieves all of the conditions necessary for a trust to result; that is to say, a settlor (the company) transfers property (the bundle of rights which are the fundamental element of the corporate trust deed, which may or may not include a security interest) to a trustee and appropriates it for a particular purpose (the protection of the debentureholder's interests in a manner consistent with the company's interests, including ultimately the debentureholders' right to be repaid). Fundamental to this analysis is the notion that "property" is defined very broadly under the C.C.Q., and includes contractual and patrimonial rights. Because the trust is now a device that permits a new way to hold property, and that "results" when certain conditions are met, this new institution achieves a rational and logically consistent explanation for the relationship of the debentureholder, the trustee and the company, both for trust deeds which pre-dated the 1994 reform and for those entered after reform.

Thus the corporate trust deed should now be characterized as creating a "trust", to be governed by the principles of "trust" found in article 1260 and following of the C.C.Q. Reform has achieved a satisfactory, indeed a complete, basis upon which the adaptation of our law to the device of the corporate trust deed may be characterized. In effect, reform has enabled a complete synthesis between this security device — developed by the necessities of commerce in the nineteenth century — and our civil law.

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[196] See Waters, *supra* note 149 at 449-50 and 755-58.

The provisions of reform are broad enough to permit the continuance of financing through the use of the corporate trust deed, with very little modification to the practices that developed before reform. The remedies for the enforcement of the security that may be contained in the corporate trust deed are no longer the creature of the corporate trust deed as a contract, but, essentially, have become the universal remedies provided by the C.C.Q. for the enforcement of hypothecs. This has resulted in significant changes in procedure and some changes in substantive rights, but has not in any way detracted from or modified the fundamental validity or the effectiveness of the structure of the corporate trust deed.

This analysis is justified not only by the functional benefits that the trust provides, but also by both the language of the C.C.Q. and the *Commentaires*, although both could have been more explicit. Indeed, the use of the new provisions on trust in this context reflects a natural, albeit slow, evolution — a continuum of commercial borrowing practices in Quebec since 1840.

APPENDIX

Extract from the Special Corporate Powers Act *as it appeared prior to reform, R.S.Q. 1977 c. P-16, ss. 27-31*

27. Notwithstanding any existing law, any joint stock company incorporated under an act of the Legislature of Québec or by letters patent, or any company so incorporated outside Québec if empowered thereto by its charter or its letters patent, may by authentic deed — for the purpose of securing any bonds, debentures or debenture-stock which it is by law entitled to issue — hypothecate, mortgage or pledge any property, moveable or immoveable, present or future, which it may own in Québec.

28. Such hypothecation, mortgaging or pledging may be by trust deed to any trustee, and such security shall be good and valid, notwithstanding that the mortgagor or pledgor may be permitted by the trustee to remain in the possession and use of the property so mortgaged or pledged.

29. The rights which such hypothec and mortgage give upon immoveables, and the manner in which they must be registered, shall be governed by the provisions of the Civil Code [C.C.L.C.] in the title of *Privileges and Hypothecs* and that of *Registration of Real Rights*, and they shall be subject thereto where not derogated from by the provisions of this section.

The mortgaging and pledge of moveables shall confer a privilege upon moveables present and future, ranking immediately after the other privileges on moveables, enumerated in articles 1994, 1994*a*, 1994*b* and 1994*c* of the Civil Code.

Such hypothec, such privilege, such mortgage and such pledge, whether affecting moveables or immoveables, shall take effect only from the date of the registration, in the manner hereinafter provided, of the deed by which they are constituted, *(a)* in the case of immoveable property being affected, in the registry office of the registration division in which such property is situated; and *(b)* in the case of moveable property, in the registry office of the registration division in which the company has its head office in Québec, and also in every other division in which it has a place of business.

This registration is effected by deposit.

30. It is and always has been lawful for a company falling under the provisions of this division, besides hypothecating, mortgaging and pledging for the purposes therein set forth, to cede and transfer, for the same purposes, the said properties to the trustee, with power, in the event of the failure of the company to fulfil the conditions of the trust deed, to take possession of the properties ceded and transferred and to administer and sell them for the benefit of the bondholders.

The cession and transfer referred to by this section shall be subject to registration in accordance with the rules contained in section 29.

31. Notwithstanding the provisions of article 1571 of the Civil Code, no signification or acceptance shall be necessary for any purpose in respect of debts, rights or claims in favour of the company which may be hypothecated, mortgaged, pledged, ceded or transferred to the trustee by the trust deed, provided that the trust deed be registered as to moveables in the manner provided by section 29 of this act, and that two notices of the fact that the security created by the trust deed has become enforceable be published in the manner hereinafter set forth; but, in the absence of signification and acceptance in cases in which signification or acceptance is required by article 1571 of the Civil Code, the trustees shall not enjoy the benefit of this section 31 in respect of any debts, rights or claims paid or otherwise discharged before the publication of such notice. The said notices shall be given by two publications in French in a newspaper published in that language in the judicial district in which the company has its chief place of business in Québec, but if there be no such newspaper in that district, then in the nearest judicial district in which there is such a newspaper, and by two publications in English in a newspaper published in that language in the judicial district in which the company has its chief place of business in Québec, but if there be no such newspaper in that district, then in the nearest judicial district in which there is such a newspaper.

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