NOVA SCOTIA COURT OF APPEAL
Citation: *Courtney v. Bank of Montreal*, 2005 NSCA 153

Date: 20051129
Docket: CA 237229
Registry: Halifax

Between:

Holly Courtney

Appellant

v.

Bank of Montreal

Respondent

Judge(s): Saunders, Oland and Hamilton, JJ.A.

Appeal Heard: September 26, 2005, in Halifax, Nova Scotia

Held: Appeal dismissed with costs and disbursements as per reasons for judgment of Oland, J.A.; Saunders and Hamilton, JJ.A. concurring

Counsel: Tim Hill, for the appellant
William Chisholm, for the respondent

Reasons for judgment:

Introduction

[1] The Bank of Montreal claimed against Holly Courtney based on several promissory notes signed by her and by her husband, Raymond Courtney. Mrs. Courtney appeals the decision and order of McDougall, J. which found in favour of the Bank. Her appeal raises issues which concern undue influence in the context of a marital relationship and a lender's duty of inquiry to a borrower who is in such a relationship.

Background

[2] Holly Courtney married Raymond Courtney in 1996. Three years later, he sold his 50% interest in MicroNet Information Systems Limited to Knowledge House Inc. The purchase and sale was by way of a pure share swap; that is, Mr. Courtney received no cash for his shares. Mrs. Courtney had never been involved with MicroNet and learned of its sale and the share swap after it had happened.

[3] Knowledge House created a limited partnership to raise funds for research and development. Raymond Courtney, who had become a director and a senior vice-president of that company after the sale of Micronet, agreed to purchase a limited partnership unit. Each unit cost $150,000. His understanding was that he would potentially save $75,000 in income tax.

[4] Mr. Courtney needed to borrow $120,000 to purchase the limited partnership unit. It was through his broker, Eric Richards of the Financial Concept Group, that the Bank of Montreal agreed to lend him the money.

[5] Holly Courtney and Raymond Courtney met with Gary Cooper, a loans officer with that Bank, on October 17, 1999. They signed a promissory note for $120,000 as co-borrowers. No independent legal advice was provided. The monies were used to buy a unit, in Mr. Courtney's name, of the Knowledge House limited partnership. He ultimately redeemed it for Knowledge House shares.

[6] The Courtneys borrowed from the Bank on two further occasions: (a) a second loan of $300,000 on January 27, 2000; and (b) a third loan of $500,000 on

March 28, 2000. On both those occasions Gary Cooper, who had processed those loans, was unavailable to meet. Another loans officer, Barbara Covey, dealt with the Courtneys when they attended at the Bank. Holly Courtney signed promissory notes as principal borrower while her husband signed as guarantor, for each of those second and third loans. No independent legal advice was provided.

[7] The second loan was used to buy additional shares of Knowledge House which were placed in separate accounts in the names of Mr. and Mrs. Courtney with the Financial Concept Group. $300,000 of the $500,000 third loan was used to pay out the second loan. The remaining monies were used to purchase shares in a company known as ITI and more shares in Knowledge House, in the name of Raymond Courtney only. For each of the second and third loans, the Bank took as security a hypothecation of his shares in Knowledge House.

[8] Each of Mr. and Mrs. Courtney gave evidence as to their discussions surrounding the first loan from the Bank. He testified in part:

> A. I told her that I couldn't get the loan without having her signature on it, she seemed not really to understand why it couldn't be done without - - with - - why it had to be done with her signature, and I basically berated her into signing it. We had several arguments, I hollered at her, I told her she had to do it, I gave her all kinds of rationale about the company and that I had, you know, millions of dollars of stock, so big deal. I pressured her to sign it, is what I did.
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> Q. Did you give her any details about the particulars of [inaudible]?
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> A. I made reference to the tax vehicle, that I would likely receive some benefit from that as well. As part of my pitch to her to tell - - to ask her - - to get her signature or to obtain her signature for that, I told her that I had promised my partners that I would do this and that I had to do it and it was the nth hour . . .

[9] Asked what her husband had told her he needed in relation to the first loan, Holly Courtney testified:

> I think he told me I had to sign on it, I had to guarantee it in some way, and I again said, "Why me?", because I didn't work, I had no means of repaying it, and he assured me that the stock would secure the loan.

According to Mrs. Courtney, the couple had "many, many conversations" which were "very heated." At some point she agreed to sign. Asked why she eventually acquiesced, Holly Courtney responded:

> Because the fighting was escalating to the point that I really didn't think that the marriage would continue if we continued to fight like that and I - - Ray told me and pointed out to me on numerous occasions that he had many years of business experience, many more than me at high levels, and that he knew what he was doing.

She also testified that:

> It was very important to Ray, he told me he couldn't get it done without my signature, I felt that if I didn't do it that I would be responsible for him looking bad in the eyes of his co-workers, we were arguing about it constantly, in the end I just felt that I had to trust his judgment. I'd had no reason not to up to that point.

[10] As with the first loan, Mr. Courtney talked to his wife about the second loan only after he had everything all set up and ready to go. When he told her she was needed to sign on it, he described her response as follows:

> She freaked. She got very mad that I would propose this to her, just essentially tell her she had to sign for me again, and I continued to tell her what a great company Knowledge House was and I talked about Charles Keating coming in and buying significant amounts of stock and investing $6 million dollars and I talked about the prognosis of the company and, you know, it's a sound thing to do and it's the right thing to do. I told her I had given the commitment to help the company and to support the company in my best efforts and that's what I wanted to do.

According to Mr. Courtney, these arguments continued over a number of days and he "continued to harass" his wife to sign. In regard to the second and third loans, Mrs. Courtney's evidence was that her husband had told her that there was no risk because the loan was secured with stock.

[11] Each of Gary Cooper and Barbara Covey, the loans officers, had worked in lending for over 25 years. Neither had met Holly Courtney before she came with her husband to sign the promissory notes. Neither recalled her expressing any reluctance or concerns about signing them. Each formed the opinion from the

meetings with them that both Courtneys understood the nature and effect of the security documents and were signing willingly. Each decided that independent legal advice was not required.

[12] The value of Knowledge House shares was increasing at the time of each of the three loans. When Mr. Cooper sought authorization for the third, a senior employee of the Bank expressed concern about the risk, considering the high concentration of Knowledge House stock in Raymond Courtney's portfolio as well as its very short history trading at high prices. This concern was not communicated to Mr. Courtney or to Holly Courtney.

[13] After completing a year of university and obtaining her legal secretarial diploma, Holly Courtney had worked outside the home for some 15 years. Ten years as secretary to the president of Halifax-Dartmouth Industries ended in the summer of 1995. She worked as secretary to the president of Nautel Industries until the spring of 1997. Thereafter Mrs. Courtney was not employed outside the home. That was her status at the time the three Bank loans were obtained between October 1999 and March 2000.

[14] In 2001 the stock price of Knowledge House shares collapsed and the shares became worthless. Raymond Courtney subsequently made a proposal under the *Bankruptcy and Insolvency Act*, R.S. 1985, c. B-3, as amended.

Decision of the trial judge

[15] The Bank brought an action against the Courtneys to enforce repayment of their loans with the Bank. Among other things, Holly Courtney's defence alleged duress and undue influence, that the transactions were sufficiently divergent from ordinary standards of commercial morality to justify recision of the loan agreements, and that they were unenforceable in that she received no consideration.

[16] Following a three day trial, the trial judge gave judgment for the Bank. His decision is reported at 2004NSSC182. It noted at ¶ 12 that Holly Courtney never asked any questions or raised any concerns with anyone at the Bank about the pressure allegedly exercised upon her by her husband or about the documents she was asked to sign. His decision concluded:

> ¶ 26 In the final analysis, I do not find that there has been undue influence exerted upon Mrs. Courtney. Furthermore, I do not find that there was anything that should have put the BoM on notice to make inquiries before allowing Mrs. Courtney to sign the loan documents. The loans were for the purpose of investing and not to secure the existing indebtedness of Mr. Courtney's business or to prop up a faltering business. Mrs. Courtney stood to benefit from these investments. She received consideration. By co-signing the first loan the requirement for providing additional security was waived. Although the second and third loans required further security, the Courtneys were given a lower interest rate. Mrs. Courtney, along with her husband, benefited from this.
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> ¶ 27 It might have been more prudent for the BoM to recommend independent legal advice for Mrs. Courtney but, in the circumstances of this case, I do not think it was mandatory.

Issues

[17] The issues raised on appeal can be divided into two categories: those which pertain to undue influence, and those which pertain to a duty of inquiry on the Bank. Under the first category fall the following:

(a) Did the learned trial judge commit palpable and overriding error:

  (i) in finding that Holly Courtney stood to benefit from the loans advanced by the Bank?

  (ii) in ignoring or misunderstanding evidence of undue influence exerted by Raymond Courtney over his wife?

(b) Did he err in law in failing to apply or consider the presumption of undue influence insofar as the relationship between the Mr. and Mrs. Courtney was concerned?

[18] The issues which pertain to a duty of inquiry on the Bank are as follows:

(a) Did the trial judge err in finding that:

(i) the Bank owed no duty to advise Holy Courtney of dangers associated with the transactions and no obligation to explain her liability in relation to the loans?

(ii) the Bank had met its obligations to her where it failed to advise her to seek independent legal advice prior to entering into the transactions?

(iii) the Bank was not required to make reasonable inquiries to ensure no undue influence existed where the loans in question were made for the sole purpose of Raymond Courtney and not Holly Courtney, and also given the potential for influence within the husband and wife relationship?

(b) Did the trial judge err in failing to find that the Bank had constructive notice of undue influence exerted by Raymond Courtney over his wife?

Standard of Review

[19] In *Flynn v. Halifax (Regional Municipality)*, 2005 NSCA 81, this court stated:

> 13 An appeal is not a re-trial. The powers of an appellate court are strictly limited. A trial judge's factual findings and inferences from facts are insulated from review unless demonstrating palpable and overriding error. On questions of law the trial judge must be correct. A question of mixed fact and law involves the application of a legal standard to a set of facts and is subject to a standard of palpable and overriding error unless it is clear that the trial judge made some extricable error in principle with respect to the characterization of the standard or its application, in which case the error may amount to an error of law and, therefore, be subject to a standard of correctness (**Housen v. Nikolaisen** [2002] 2 S.C.R. 235).

It accepted the description of palpable errors and overriding errors as set out in *Waxman v. Waxman* (2004), 186 O.A.C. 201 (Ont. C.A.).

Analysis

Undue Influence

[20] The trial judge's decision disposed of the issue of undue influence as follows:

> ¶ 15 Mr. Courtney opted to proceed, with Mrs. Courtney's agreement, to negotiate the first loan in both names. Although I accept that Mrs. Courtney was reluctant at least at first to act as a co-borrower, I do not accept that she was the victim of undue influence by her husband. There might have been some tension between them but it was not enough to constitute undue influence. I find that she knew what she was doing and she did it willingly without undue influence from her husband.
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> ¶ 16 I also do not accept that Mr. Courtney was acting as an agent of the BoM in convincing Mrs. Courtney to co-sign the loan documents. The BoM provided Mr. Courtney with an option. There were certain advantages to having the loan signed by both parties. By proceeding as they did, both Mr. and Mrs. Courtney benefited from these advantages. Even though the limited partnership was put in Mr. Courtney's name only, Mrs. Courtney also stood to benefit if it helped to reduce her husband's income tax liability. This would increase the couple's after-tax household income. What is more, the loan was not intended to secure existing business indebtedness of Mr. Courtney nor to bail out a failing business. It was an investment. The value of KHI shares was increasing at the time. Mrs. Courtney stood to benefit from these investments along with her husband.
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> . . .
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> ¶ 18 Like the first loan, the funds from the second loan were used for investment purposes. And since Mr. and Mrs. Courtney did not have a marriage contract that would preclude her from making a claim to a share of these investments in the event of a separation or divorce she stood to potentially benefit. Likewise if they remained together as husband and wife then they would both potentially benefit from the investment.

[21] In my view, none of the grounds of appeal pertaining to undue influence have merit.

[22] The trial judge's finding that Mrs. Courtney stood to benefit from the loans with the Bank was supported by the evidence. Holly Courtney did not sign notes

in support of her husband's own business. Rather, the Knowledge House limited partnership unit and the Knowledge House and ITI shares were purchased as investments. It was expected or at least hoped that they would increase in value. There was no marriage or other contract between these spouses which would disentitle the wife from an interest in them. Some of the Knowledge House shares were placed in an account in Mrs. Courtney's own name. A reduction in her husband's income tax liability, which Mr. Courtney testified he expected, would increase their household income. The trial judge did not make any palpable or overriding error in finding that Mrs. Courtney stood to benefit from the loans.

[23] Nor, in my view, did he make any such error by ignoring or misunderstanding the evidence of undue influence allegedly exerted by Mr. Courtney on Mrs. Courtney. Holly Courtney's submissions relied heavily on the uncontradicted evidence of her reluctance to sign and Mr. Courtney's persuasion, and made much of her reliance on her husband's judgment. The evidence did establish that there had been strong disagreement between the Courtneys. However, here the spouse alleging undue influence was not herself unfamiliar with loans and financial terms.

[24] While, at the time she signed for the loans Mrs. Courtney was not employed outside the home, she had had considerable work experience over 15 years until 1997. Moreover, Holly Courtney has a good educational background and an appreciation of financial and business matters. She testified she was critical of her husband when he received no cash as part of the MicroNet sale as she felt MicroNet was an amazingly profitable company. She knew she was signing loan documents and understood the obligation to repay the amount borrowed plus interest. She was sophisticated enough to understand the concept of liquidity in terms of business dealings and stocks. On one occasion Mrs. Courtney had advised Raymond Courtney to reconsider purchasing shares of a certain company as she was concerned about their liquidity, and he accepted her advice.

[25] According to the evidence, it was Mr. Courtney who attended to the couple's financial affairs. He did the trading on his wife's account at Financial Concept Group. However, nothing prevented Mrs. Courtney opening statements from that firm, from speaking with or contacting Eric Richards, or from directing her own account. She chose to refer his messages and correspondence to her husband.

[26] The trial judge found that never during the three loan transactions did Holly Courtney ask any questions or express any concerns whatsoever to anyone at the Bank. Nothing about her behaviour or demeanour during three meetings gave the Bank's loan officers any cause for unease about her understanding of the loan documents or as to her willingness to sign them.

[27] The trial judge found that based on her education and experience, Holly Courtney was well aware of her legal obligations regarding these loans and that whatever influence was exerted upon her husband, it was not sufficient to constitute undue influence. I see no palpable or overriding error in his refusal, based on the evidence before him, to accept that Mrs. Courtney was the victim of undue influence by her husband.

[28] I also reject the argument that the trial judge erred in law by failing to address the presumption of undue influence. Mrs. Courtney submits that instead of asking whether there was sufficient evidence to support the presumption, he went into another debate entirely, namely whether there had been evidence of undue influence.

[29] In *Geffen v. Goodman Estate*, [1991] 2 S.C.R. 353, [1991] S.C.J. No. 53 (QL version), Wilson, J. (Cory, J. concurring) addressed what a plaintiff had to establish in order to trigger a presumption of undue influence:

> 43. . . . In my view, the inquiry should begin with an examination of the relationship between the parties. The first question to be addressed in all cases is whether the potential for domination inheres in the nature of the relationship itself. . . .
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> 44. Having established the requisite type of relationship to support the presumption, the next phase of the inquiry involves an examination of the nature of the transaction. When dealing with commercial transactions, I believe that the plaintiff should be obliged to show, in addition to the required relationship between the parties, that the contract worked unfairness either in the sense that he or she was unduly disadvantaged by it or that the defendant was unduly benefited by it. ..."

Once this two-part test is satisfied and the presumption raised, then the onus moves to the defendant to rebut it.

[30] In *Barclay's Bank plc v. O'Brien*, [1994] 1 A.C. 180, [1993] 4 All E.R. 417 (H.L.), at § 16 and 17 Lord Browne-Wilkinson first noted two classes of undue influence (actual and presumed). Then at § 18 and 19, he further divided presumed influence into two parts: Class 2A which encompasses those relationships which, as a matter of law, raise the presumption of undue influence; and Class 2B where the existence of a relationship under which the complainant generally reposed trust and confidence in the wrongdoer, raises that presumption. He continued at § 21:

> Although there is no class 2A presumption of undue influence as between husband and wife, it should be emphasized that in any particular case a wife may well be able to demonstrate that de facto she did leave decisions on financial affairs to her husband thereby bringing herself within class 2B ie that the relationship between husband and wife in the particular case was such that the wife reposed confidence and trust in her husband in relation to their financial affairs and therefore undue influence is to be presumed. Thus, in those cases which still occur where the wife relies in all financial matters on her husband and simply does what he suggests, a presumption of undue influence within class 2B can be established solely from the proof of such trust and confidence without proof of actual undue influence.

[31] The categorization of undue influence set out in *O'Brien* was accepted by the Supreme Court of Canada in *Gold v. Rosenberg* [1997] 3 S.C.R. 767, [1997] S.C.J. No. 93 (QL version) at § 60 and § 78-79.

[32] In his decision the trial judge did not make explicit reference to the presumption of undue influence, how that presumption might be triggered, or if the evidence before him raised that presumption. While it would have been preferable had he done so, I am satisfied from my review of the trial judge's decision that he directed his mind to the requirements that give rise to that presumption, and the evidence in support of the presumption and of its rebuttal. This is apparent from his review of the facts pertaining to the relationship between Mr. and Mrs. Courtney in regard to financial matters and in particular these loans, and his description of the "tension" between husband and wife regarding. The trial judge was clearly focussed on the potential for domination within this marital relationship and the extent to which Mrs. Courtney reposed trust and confidence in her husband in relation to their financial affairs. He also considered the nature of

these transactions. In finding that Mrs. Courtney stood to benefit, he implicitly decided that the loan arrangement did not work an unfairness. Moreover, his familiarity with *O'Brien*, *supra* is reflected in his reference to that decision. Finally, he considered those factors which might rebut the presumption. In these circumstances I am unable to agree that the trial judge erred by failing to consider the presumption of undue influence.

Duty of Inquiry

[33] In § 25 of his decision, the trial judge noted that Mrs. Courtney had urged him to apply *Royal Bank of Scotland plc v. Etridge* (No. 2) (HL (E)), [2002] 2 A.C. 773 and then continued:

> . . . This House of Lords decision makes it clear that their earlier decision in **Barclays Bank plc v. O'Brien**, [1993] 1 All E.R. 417; [1993] 3 W.L.R. 786; [1994] 1 A.C. 180 (U.K.H.C.) is still good law. There are also a number of Supreme Court of Canada decisions that consider the **O'Brien** authority and which were decided prior to **Etridge**. **Etridge** does not overturn the decision in **O'Brien**; rather, it only serves to better explain it. I am not persuaded that the law has changed substantially if at all. Even if it had, I am not bound by a decision of the House of Lords.

In the following paragraph, he concluded: "I do not find that there was anything that should have put the BoM on notice to make inquiries before allowing Mrs. Courtney to sign the loan documents" and stated at § 27:

> It might have been more prudent for the BoM to recommend independent legal advice for Mrs. Courtney but, in the circumstances of this case, I do not think it was mandatory.

[34] The grounds of appeal allege that the trial judge erred in law in finding that the Bank had met its obligations to Holly Courtney although it had not advised her to seek independent legal advice, or of the risk involved with these transactions. I am not persuaded that he so erred.

[35] I address as a preliminary matter, the argument that the Bank breached its own policy regarding the provision of independent legal advice. That submission is without foundation. The Bank's operating procedure regarding such advice reads in part:

Introduction	Where a loan transaction involves a third party, lack of consideration (benefit) could prejudice the validity of the guarantee or covenant. A court may dismiss a claim for recovery by the Bank from a third party who co-signed, endorsed, guaranteed or pledged security on behalf of a primary debtor if the court feels that the third party was subjected to pressure from: - the primary debtor, - the Bank, or - any other person. Accordingly, determine, under the Lending process, whether the Bank should insist on the third party obtaining independent legal advice (ILA) as to the legal effect and consequences of providing support.
Independent legal advice ILA	. . . ILA is often obtained when the third party is an individual and: - is the spouse of the primary debtor Also applies . . . for the benefit of a business owned or controlled by the other spouse or of which the other spouse is a principal officer.

[36] A careful reading of this document indicates that, in every case, it is for the loans officer to determine whether such advice should be obtained; the operating procedure does not make it mandatory. These loans were not for the benefit of a business which was a customer of the Bank and in which Mr. Courtney had an ownership interest. Moreover Holly Courtney was not a third party. She co-signed the first loan and it was she, not Raymond Courtney, who was the primary debtor on the second and third.

[37] I turn then to the argument regarding independent legal advice. The absence of such advice does not automatically preclude recovery under a security document. In *Gold v. Rosenberg, supra* Sopinka, J. for the majority stated at p.803:

> Whether or not someone requires independent legal advice will depend on two principal concerns: whether they understand what is proposed to them and whether they are free to decide according to their own will. The first is a function

> of information and intellect, while the second will depend, among other things, on whether there is undue influence. . . .

[38] Holly Courtney argues that her interaction with the Bank was limited and that she did not have the information and intellect to fully understand the nature of the loan transactions and her financial exposure. According to her submissions, independent legal advice would have afforded her the opportunity to understand her rights and obligations regarding the loans, and to properly understand the risk she was undertaking.

[39] Earlier in this decision, I determined that the trial judge had not made a palpable and overriding error in finding that Mrs. Courtney fully understood the obligation she was entering into and was doing so freely and voluntarily. As a consequence, independent legal advice would not have made a difference – she would have been told what she already knew and appreciated. The absence of such advice in such circumstances cannot be the basis of impeaching the loan transactions.

[40] Mrs. Courtney then submits that the Bank was fully aware of the risks and dangers associated with the loans. She points to the internal memorandum which urged caution in regard to the third loan because of the high ratio of Knowledge House stock in Mr. Courtney's stock portfolio, and says that the Bank should have drawn its concerns to her attention. She urges as well that where the loans were negotiated by her husband, the Bank should have been "put on inquiry" and that it should have arranged a private meeting with her to advise her of the risks and to assure itself that she understood her obligations.

[41] Her argument relies on *Etridge (No 2)*, *supra*. There the House of Lords held that whenever a wife stands as surety for her husband's debts, the bank is put on inquiry and it should insist upon the wife attending a private meeting where she is advised of the risks of the transaction and her potential liability and should also be urged to seek out independent legal advice. According to that decision, if these steps are taken, the bank is protected from a claim of undue influence.

[42] *Etridge (No 2)* has been referred to in several Canadian decisions. See, for example, *Faris v. Eftimovski*, [2004] O.J. No. 3407 (S.C.J.) and *Bank of Montreal v. Collum,* [2004] B.C.J. No. 1314 (C.A.), application for leave to appeal dismissed [2004] S.C.C.A. No. 412, where it was referred to as *Barclays Bank plc*

v. Coleman, [2001] 4 All E.R. 449. However, here the wife did not serve as surety for her husband's debts and no Canadian case has followed *Etridge (No 2)* and stipulated that a bank must take such steps to avoid a claim of undue influence was identified. I am not satisfied that in deciding not to follow that decision the trial judge erred such that this court should interfere.

[43] Finally, Mrs. Courtney argued that the trial judge had erred in failing to find that the Bank had constructive notice of undue influence exerted by Mr. Courtney over her. I am not persuaded that he so erred. There was nothing about Mrs. Courtney's conduct with respect to these loan transactions that alerted the Bank's loans officers to the possibility of undue influence. At their meetings, she gave no indication that she was not acting freely and voluntarily. She did not call them to express any concern. She admitted that she knew the legal effect of the documents she signed. In light of the evidence it cannot be seriously suggested that because Ms. Courtney was no longer in the workforce or that she was married to Mr. Courtney in whose name most of the investments purchased with the money they borrowed were registered, fixes the Bank with constructive notice of his undue influence over her.

[44] I would dismiss the appeal and would award the Bank costs of $4,000. plus disbursements as agreed or taxed.

Oland, J.A.

Concurred in:

Saunders, J.A.

Hamilton, J.A.