Court File No.: 01-CV-221646 CM
Date: July 22, 2005.

ONTARIO
SUPERIOR COURT OF JUSTICE

BETWEEN:

JOHN STONEMAN, SARAH STONEMAN and
MAKO FILMS LTD.

Plaintiffs

and

J. GARY GLADMAN, FRANK MONTELEONE, A FARBER & PARTNERS INC. and MAXIMA FILM CORPORATION

Defendants

COUNSEL:
Anthony J. O'Brien for the defendants J. Gary Gladman and Maxima Film Corporation
James C. Morton, for the plaintiffs
Alan B. Merskey, for the defendant Frank Monteleone

HEARING DATE: July 18, 2005

REASONS FOR JUDGMENT

PERELL, J.

[1] This is a motion by Maxima Film Corporation ("Maxima") and J. Gary Gladman, who are two of the defendants in an action brought by John Stoneman, Sarah Stoneman, and Mako Films Ltd., to have the action dismissed or indefinitely stayed on a combination of grounds, none of which standing alone would be sufficient to stop the plaintiffs' action.

[2] To be more precise, these defendants submit that that claims of the plaintiffs to recover compensation for a valuable library of approximately 2.1 million feet of film footage should be stayed on the grounds that the plaintiffs do not have the legal capacity to pursue the claims. In seeking a stay of these claims, the defendants

Gladman and Maxima rely on rule 21.01 (3)(b) of the *Rules of Civil Procedure*, under which a defendant may move before a judge to have an action stayed or dismissed on the ground that the plaintiff is without legal capacity to commence or continue the action. They also are relying on rule 21.03 (d), under which a defendant may move before a judge to have an action dismissed on the ground that the action is frivolous or vexatious or is otherwise an abuse of the process of the court.

[3] Then, these defendants submit that the claim for damages by Mr. Stoneman for wrongful dismissal should be dismissed under rule 20.01 (3), under which a defendant may move for summary judgment dismissing all or part of the claims in the statement of claim. The defendants concede that Mr. Stoneman has the legal capacity to advance this claim, but the defendants argue that there is no genuine issue for trial and the claim is without merit and should be dismissed.

[4] Thus, the optimum goal of the defendants Maxima and Gladman is to rely on the combination of Rules 20 and 21 to have the plaintiffs' action totally dismissed. Their fallback position is that if the claims challenged under rule 21.01 (3)(b) and (d) are allowed to proceed, then the plaintiffs should be obliged to post security for costs for these claims.

[5] The obvious opposing goal of the plaintiffs is to have the two-pronged attack on their pleading dismissed, and in aid of that goal they argue that there are genuine issues for trial and it would be inappropriate for the court to stay part of their claims on the ground that they want for legal capacity.

[6] Understanding the nature of the motion brought by Maxima and Gladman and the problems it presents becomes clearer by summarizing the allegations contained in the statement of claim.

[7] The background to the action is that John and Sarah Stoneman are a married couple in their sixties, and Mr. Stoneman is a cinematographer in underwater photography. The Stonemans owned the plaintiff Mako Films Ltd, which, in turn,

owned a film library of approximately 1.1 million feet of underwater and general nature film footage.

[8] The Stoneman's allege that in the early 1990's, they faced significant financial difficulties, and to help them find a way out of these difficulties, their bank manager introduced them to the defendant Gladman, a business person in the City of Toronto. Gladman made various proposals, but ultimately one scheme, which the plaintiffs acknowledge was dishonourable and of highly questionable legality was implemented.

[9] The scheme is described in paragraph 20 of the statement of claim, which states:

> 20. In the subsequent proposal, Gladman suggested that a better solution for the on-going financial difficulties of Mr. and Mrs. Stoneman was that they go bankrupt personally. Prior to the bankruptcy, Mr. and Mrs. Stoneman would cause Mako Films to transfer all its assets to a new company to be controlled by Gladman. The transfer would be accomplished by the exercise of security formerly held by Mr. and Mrs. Stoneman's bank and acquired by Gladman through Maxima Film Corporation. The proposal was reduced to writing by letter of Gladman to Frank Monteleone [the Stonemans' lawyer and another defendant to this action] dated March 6, 1995. The bankruptcy would wipe out any personal debts of Mr. and Mrs. Stoneman and following the bankruptcy discharge, Gladman would gift 50% of the new company to Mr. Stoneman or as Mr. Stoneman directed.

[10] The Stonemans allege that the scheme was implemented to the extent that Maxima became the owner of the assets of Mako Films and in so far as the Stonemans, one after the other, made summary assignments into bankruptcy through A. Farber & Partners Inc., a trustee in bankruptcy and another defendant to this action. In the bankruptcy proceedings, the Stonemans did not disclose that assets were being held in trust for them or that assets would be returned to them after the bankruptcy.

[11] The dates of the transfer of Mako Film's assets and the dates of the bankruptcy proceeding are significant. The transfer of assets to Maxima occurred on or about March 16, 1995. Two years later, on March 4, 1997, Mr. Stoneman made an assignment into bankruptcy, and he was discharged from bankruptcy on December 4,

1997. Mrs. Stoneman made an assignment into bankruptcy on March 9, 1998, and she was discharged from bankruptcy on December 10, 1998.

[12] The Stonemans alleged that the balance of the scheme was not implemented, but rather Mr. Stoneman became an employee of the defendant Maxima. Paragraph 25 of their Statement of Claim states:

> 25. Following the transfer of assets, Mr. Stoneman called upon Gladman for the transfer of half of the business back to Mr. and Mrs. Stoneman. Gladman refused to honour the terms of his agreement with Mr. and Mrs. Stoneman and instead, offered to employ Mr. Stoneman at a salary of about $48,000 per year. Nevertheless, until mid 1999, Gladman referred to Stoneman as "partner".

[13] The Stonemans allege that Mr. Stoneman's employment continued until about February 28, 2002 when he was dismissed.

[14] The Stonemans allege that the termination from employment was a wrongful dismissal and that the refusal to transfer the business as agreed was a breach of contract, or oppressive conduct within the meaning of s. 245 of the *Ontario Business Corporations Act*. They seek to set aside the initial transfer of Mako Film's assets as void for no consideration, or void for being an illegal transaction. As a further alternative, they say Gladman is liable for misrepresentation in stating that he and the Stonemans would be partners and in claiming he was holding assets for them.

[15] The Stonemans add claims against their former lawyer for professional negligence. And tellingly of the problems just under the surface of these claims, they state in paragraph 2 of their pleading that A. Farber & Partners has been made a party, because it "may be a party necessary for the proper adjudication of the matters set out herein."

[16] The Stonemans' Statement of Claim makes three major claims: (a) general damages of $2,500,000; (b) a declaration that the plaintiffs are entitled to 50% of the defendant, Maxima Film Corporation and half the profits distributed therefrom since March 16, 1995 together with such tracing and ancilliary orders as necessary or just;

and (c) as against J. Gary Gladman only, punitive, aggrevated and exemplary damages of $250,000.

[17] The defendants move for a stay or a dismissal of all these claims, but the Stonemans argue that the claims arising from Gladman's failure to transfer the business and from Mr. Stoneman's wrongful dismissal are closely intertwined and that the defendants have not met the high test that the law of civil procedure sets for the dismissal of actions either under Rules 20 or Rule 21. Further, they submit that if there is some doubt about the legal capacity of the Stoneman's to prosecute part of their claim, the impugned part of the claim should nevertheless be allowed to proceed because of the intertwined nature of all the claims.

[18] Turning then to the grounds advanced by the defendants Gladman and Maxima to have the action stayed or dismissed, it is convenient to begin with Rule 20, the summary judgment rule. Here it may quickly be concluded that part of the plaintiffs' argument is correct. Before granting summary judgment, it must be clear that a trial is unnecessary: *Aguonie v Galion Solid Waste Material Inc.* (1998), 38 O.R. (3d) 161 (C.A.); *Irving Ungerman Ltd. v. Galanis* (1991), 4 O.R. (3d) 545. The court's function on a motion for a summary judgment is not to resolve any issue of fact but to determine whether a genuine issue of fact exists: *Aguonie v Galion Solid Waste Material Inc.* (1998), 38 O.R. (3d) 161 (C.A.); *Irving Ungerman Ltd. v. Galanis* (1991), 4 O.R. (3d) 545. On a motion for summary judgment, the court does not assess credibility, weigh evidence, or find facts, and the court's role is limited to assessing whether a trial is necessary to determine the material facts, that is, the facts upon which the existence of the claim or defence depend.

[19] A review of the evidentiary record on this motion establishes that there are genuine issues for trial about the circumstances of the alleged agreement to transfer the business and film library assets and about the nature of Mr. Stoneman's relationship with Maxima, be it as an employee who was wrongfully dismissed, as he alleges, or as an independent contractor who decided to withdraw his services, as Mr. Gladman alleges.

[20] Turning next to Rule 21, it also has a high threshold. Generally speaking, to succeed under this rule, the moving party must show that it is plain, obvious, and beyond doubt that the plaintiff cannot succeed: *Hunt v. Carey Canada Inc.*, [1990] 1 S.C.R. 959. It is not the function of a motion to strike a pleading to weed out cases where the claim or defence is legally sound but factually unprovable; that is a function of a motion for a summary judgment: *Dawson v. Rexcraft Storage & Warehouse Inc.* (1998), 164 D.L.R. (4th) 257 (Ont. C.A.); *Goudie v. Ottawa (City)*, [2003] 1 S.C.R. 141. Although evidence is permissible on the motion, the facts must be uncontroverted or easily ascertainable and the motion may not be used to resolve a factual dispute or to circumvent the requirements of the summary judgment rules that address whether there is a genuine issue for trial of the facts: *Goudie v. Ottawa (City)*, [2003] 1 S.C.R. 141; *Dawson v. Rexcraft Storage & Warehouse Inc.* (1998), 164 D.L.R. (4th) 257 (Ont. C.A.).

[21] The thrust of the defendants' argument under Rule 21 is that it is beyond doubt that the plaintiffs' claim based on the alleged failure to transfer the business assets cannot succeed because the plaintiffs are without legal capacity to commence or continue that claim and the claim is also an abuse of the process of the court.

[22] In making this argument, the defendants, however, are confronted with the problem that Mr. Stoneman does not want for legal capacity to advance his wrongful dismissal claim and they are confronted with the plaintiff's argument that the claims are too closely intertwined to be separated. The plaintiffs assert - and I agree with them - that there is no basis to challenge the wrongful dismissal claim other than as a factual matter after a trial.

[23] The defendants assert nevertheless that at least the part of the claim based on the defendants' failure to transfer the business assets should be stayed or dismissed.

[24] For the reasons that follow, it is my conclusion that the defendants are correct in asserting that the claim based on the defendants' failure to transfer the business assets should be dismissed now. It is further my conclusion that rather than dismiss part of the action, it should be dismissed in its entirety without prejudice to the plaintiff John

Stoneman commencing a new action to claim damages solely for his wrongful dismissal from employment.

[25] To explain these conclusions, it is necessary to discuss certain principles of the law of bankruptcy because these principles establish beyond doubt that the plaintiffs do not have the legal capacity to commence or continue their claim for compensation for the alleged failure to transfer the business assets.

[26] Under s. 71 (1) of the *Bankrupcty and Insolvency Act,* R.S.C. 1985, c. B-3, on an assignment in bankruptcy, a bankrupt ceases to have any capacity to dispose of or otherwise deal with his or her property, which passes to and vests in the trustee in bankruptcy. The property vested in the trustee does not revert back to the bankrupt upon his or her discharge: *Carriere v. Carriere (Trustee of),* [1994] M.J. No. 332 (C.A.). There, however, are some exceptions and some property rights remain vested in a bankrupt.

[27] Property includes causes of action, and thus where a person has been adjudged bankrupt it is necessary to consider whether the person has lost the capacity to prosecute the cause of action. This matter is discussed in Williston and Rolls, *The Law of Civil Procedure*, (Toronto: Butterworths, 1970) at pp. 173-174, where the authors state [citations omitted]:

> Where a person or corporation has been adjudged a bankrupt, it is necessary to consider if a cause of action can be asserted by his trustee in bankruptcy and whether an action may be brought against the trustee in bankruptcy with leave.
>
> Not all causes of action vest in the trustee, but only those which belong to the bankrupt's estate and which may be applied for the purpose of distribution amongst his creditors. Consequently, the right of action does not vest in the trustee where the damages claimed are to be "estimated by immediate reference to pain felt by the bankrupt in respect of his body, mind or character, and without immediate reference to his rights or property. The following rules may be stated:
>
> 1. A right of action in respect of a tort or a breach of contract resulting in injuries wholly to the person or feeling of the bankrupt does not pass to the trustee.

> 2. A right of action in respect of a tort or of a breach of contract resulting in injuries wholly to the estate of the bankrupt passes to the trustee.
>
> 3. A right of action, whether in respect of a tort or of a breach of contract, resulting in injuries both to the estate and also to the person or feelings of a bankrupt, will be split and will pass so far as relates to the estate, to the trustee and will remain so far as relates to the person or feelings of the bankrupt, in him.
>
> Applying these rules, it has been held that an undischarged bankrupt cannot himself sue a defendant for damages for having fraudulently and without reasonable cause procured his bankruptcy, or for damages for wrongful and illegal conspiracy to put the bankrupt into bankruptcy. Such causes of action, if they exist, pass to and are vested in the trustee.

[28] In the immediate case, it is my opinion that the plaintiffs' claims for compensation for the alleged failure to transfer the business assets is a claim for injuries to the estate in bankruptcy and not a claim personal to Mr. or Mrs. Stoneman. The claim for the alleged failure to transfer the business assets is a claim vested in the trustee in bankruptcy. This claim should be split from the wrongful dismissal claim, which is a claim that relates to the person or feelings of John Stoneman. In this regard, see: *Cherry v. Ivey* (1982), 37 O.R. (2d) 361 (H.C.J.); *Wilson et al. v. United Countries Bank Limited*, [1920] A.C. 102, [1918-19] All E.R. Rep 1035 (H.L.); *Egan v. Grayson* (1956), 8 D.L.R. (2d) 125 (Alta. S.C.).

[29] Notwithstanding the plaintiffs' argument to the contrary, *Re Holley* (1986), 54 O.R. (2d) 225 (C.A.) is not inconsistent with my conclusion that the claim about the transfer of business assets should be stayed. In *Re Holley*, the Court of Appeal reversed a decision that a bankrupt did not have the legal capacity to prosecute a wrongful dismissal action. The only claim asserted in *Re Holley* was a wrongful dismissal claim, and as I read the judgment and *Cherry v. Ivey, supra*, which was relied upon the Court of Appeal, *Re Holley* is authority that where the cause of action is clearly a personal one but a head of damage might turn out to be property vested in the trustee in bankruptcy, then this should be left to be determined after a trial. The immediate case is different. The plaintiffs are not advancing a claim that is clearly a

personal one; rather, they have threaded a personal claim into the fabric of a cloth of a claim that belongs to the estate in bankruptcy.

[30] It should be noted that, strictly speaking, the bankruptcy has no significance to the wrongful dismissal claim. Mr. Stoneman was long discharged from bankruptcy when he was dismissed from employment. The cause of action for the failure to transfer the business assets, however, is property that is in respect of a breach of contract or a tortuous misrepresentation resulting in injuries to the estate of the bankrupt, and these claims and any associated claims passed to the trustee in bankruptcy. The plaintiffs do not have the legal capacity to commence or continue the claim for the business assets.

[31] As already noted, the plaintiffs say that their claim for compensation for the alleged failure to transfer the business assets should go forward because it is closely intertwined with the claim for wrongful dismissal. I disagree. The plaintiff John Stoneman can start again and assert his wrongful dismissal claim. What, however, he cannot do is assert a claim for compensation for the failure to transfer the business assets.

[32] There is an alternative ground to stay the plaintiffs' claims for compensation for the alleged failure to transfer the business assets. Brought by these plaintiffs, this claim is, in my view, an abuse of the process of the court. The legal maxims *ex turpi causa non oritur actio* and *ex dolo malo non oritur actio* express the principle that the court will not aid a litigant who founds his or her claim upon an illegal or immoral act. A classic expression of the principle is by Lord Mansfield in *Holman v. Johnson* (1775), 98 E.R. 1120 (K.B.) at p. 1121 where he states:

> The principle of public policy is this: *ex dolo malo non oritur actio*. No court will lend its aid to a man who founds his cause of action upon an immoral or illegal act. If, from the plaintiff's own stating or otherwise, the cause of action appears to arise *ex turpi causa*, or the transgression of a positive law of this country, there the Court says he has no right to be assisted. It is upon that ground the Court goes; not for the sake of the defendant but because they will not lend their aid to such a plaintiff.

[33] In *Pupiec v. Dereniowski*, (1998), 39 O.R. (3d) 150 (C.A.), the vendor participated in a fraudulent scheme to deceive the mortgagee who was providing first

mortgage financing. The vendor was disentitled from enforcing her own mortgages that were received as part payment of the falsely stated purchase price. The court stated that a plaintiff who is a willing participant in an illegal or immoral act may not have the assistance of the court if damages flow from the illegal or immoral act.

[34] In asserting that they should be allowed to advance the claim for compensation for the alleged failure to transfer the business assets, the plaintiffs attempt to take some comfort from the fact that the trustee in bankruptcy has, so far, shown no interest in taking over the claim. I do not see how this assists the plaintiffs. The trustee's disinterest does not confer legal capacity on the plaintiffs, and unlike the trustee, they remain tainted by their professed acknowledgment that the scheme that they seek to have enforced is dishonourable and illegal.

[35] Because I have ruled that the whole action should be dismissed, it is not necessary to address the defendants' request that the plaintiffs post security for costs.

[36] Because I have ruled that the whole action should be dismissed, two additional matters need to be addressed. First, this result ends the main action as against all defendants, and they all have a claim for costs against the plaintiffs for the main action. This is a matter that I can deal with. Unless the parties can come to an agreement, I require their submissions in writing about costs of the action and of the motion, not to exceed 10 pages in length within 10 days of the release of these reasons.

[37] Second, there is the matter of a counterclaim by Gladman and Maxima and a crossclaim by Frank Montelone, which are not matters before me. These significant loose ends may be resolved by the parties, although it may be necessary for some of them to bring additional motions. If they are prepared to file consents or minutes of settlement with respect to the counterclaim and the crossclaim within 10 days of the release of these reasons, then I will deal with these matters too.

Perell, J.

Perell, J.

Released: July 22, 2005

Court File No.: 01-CV-221646 CN
Date: July 22, 2005.

ONTARIO
SUPERIOR COURT OF JUSTICE

BETWEEN:

JOHN STONEMAN,
SARAH STONEMAN and
MAKO FILMS LTD.

Plaintiffs

and

J. GARY GLADMAN, FRANK MONTELEONE, A FARBER & PARTNERS INC. and MAXIMA FILM CORPORATION

Defendants

REASONS FOR JUDGMENT

Perell, J.

Released: July 22, 2005