


In the Privy Council.

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UNIVERSITY OF LONDON
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INSTITUTE OF ADVANCED
LEGAL STUDIES

No. 18 of 1951

ON APPEAL FROM THE COURT OF
APPEAL FOR ONTARIO

BETWEEN

JAMES JOSEPH GRAY ... (Defendant) APPELLANT

AND

NEW AUGARITA PORCUPINE MINES LIMITED
(Plaintiff) RESPONDENT.

CASE FOR THE APPELLANT

RECORD

1.—This is an appeal from an order of the Court of Appeal for Ontario (Laidlaw, Aylesworth and Bowlby, J.J.A.) dated the 3rd March, 1950, which varied a judgment of McFarland, J., dated the 15th October, 1949, in an action begun on the 29th January, 1946, in which the Respondent as plaintiff sought against the Appellant as defendant, relief which may be summarised as

pp. 333-335

pp. 327-329

p. 1, l. 9

p. 5, l. 33—p. 6,
l. 31

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(i) a declaration that certain transactions in December, 1941, did not constitute a final settlement between the parties, or alternatively setting aside any such settlement or agreement as having been entered into by the Respondent's directors on the basis of fraudulent misrepresentations of the Appellant, on false and incomplete information, and without independent legal advice or the shareholders' approval

(ii) an accounting of all transactions of the Appellant with the Respondent concerning money or shares from the 13th May, 1936, to January, 1942

(iii) the return of certain shares or their value

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(iv) judgment for the amount found owing by the Appellant to the Respondent by reason of wrongful misappropriations

(v) \$100,000 damages for fraud and breach of trust and fiduciary duty

(vi) \$2,500 paid out in investigations, as special damages

(vii) injunctions, costs and just and necessary further or other relief.

2.—From the Respondent's incorporation in May, 1936, until November, 1941, except for a short period from August to October, 1936, the Appellant was vice-president and a director of the Respondent. The secretary-treasurer, G. H. Bourne, was also a director. He was an employee of the Appellant, as was also Margaret Emma Lord, another director. During this period such accounts and records of the Respondent as were kept were kept in an untidy and incomplete manner and many transactions on behalf of the Respondent were informal. In November and early December, 1941, four independent persons became directors. The Appellant's employees resigned as directors and, though the Appellant remained a director he resigned as vice-president and Mr. Bourne resigned as secretary-treasurer. On the 9th December, 1941, an agreement (hereinafter called "the settlement agreement") was entered into between the Appellant and the Respondent upon which the Appellant relies as being the basis of settlement of all matters complained of in the action. On the 16th January, 1942, the Appellant formally resigned as a director of the Respondent.

Exhibit 3, p. 77,
l. 8
pp. 381-382

Exhibit 3, P. 86
l. 13

p. 327, l. 5
pp. 330-331

p. 346, l. 40-p. 347,
l. 1

p. 347, ll. 1-46

3.—The action was tried in October, 1947, by McFarland, J., who delivered judgment on the 15th October, 1949, for the Respondent declaring that the transaction of the 9th December, 1941, did not constitute a final settlement of the claims of the Respondent against the Appellant. Accordingly he directed a reference to the Master for an accounting. The Court of Appeal for Ontario held that the declaration granted by McFarland, J., was "inappropriate," and that the Court could not order rescission of the settlement agreement. The Court nevertheless held that the Respondent was entitled to damages incurred by reason of the fraud of the Appellant and, for the purpose of ascertaining the amount of such damages, directed that there be an accounting of the dealings between the Appellant and the Respondent covering the period during which the Appellant was a director of the Respondent.

4.—It is not contended in this appeal that the Appellant was not responsible for what happened during the period from the incorporation of the Respondent to November, 1941. The Appellant's contention is that in the uncertain state of affairs which then existed the settlement agreement settled all such matters. It is further contended that whatever

may be said as to what had gone before there was no fraud or other improper conduct on the part of the Appellant in the making of the settlement agreement and if anything were said by the Appellant in regard to past dealings the Respondent in no way relied thereon. By reason of delay and change of position the Respondent could not ask that the settlement agreement be rescinded, and the Court of Appeal has so held. If there was fraud or other improper conduct on the part of the Appellant relating to entering into the settlement agreement, no damages were proved; and the reference directed by the Court of Appeal, it is submitted, ignores the settlement agreement and is on an improper basis. The Appellant further contends that the effect of the order of the Court of Appeal is to allow the Respondent (contrary to what is just and equitable) now to take advantage of purchases of stocks said to have been made by the Appellant on behalf of the Respondent, although at the time of the settlement agreement the Respondent deliberately elected to repudiate these purchases and only changed its attitude years afterwards when there had been a spectacular rise in the price of the stocks.

5.—In 1941 the Respondent was in a precarious financial position. Shareholders were anxious and complaints were made to the Ontario Securities Commission, which is empowered to make an investigation where it appears probable that any person has violated the provisions of the Securities Act or regulations, or committed an offence under the Criminal Code in connection with a trade in securities.

p. 261, l. 35—p. 262, l. 36

6.—On the 19th November, 1941, the employees of the Appellant on the board of directors resigned and three persons, G. E. Buchanan, J. W. Tovell and A. H. Seguin, who were in no way under the control of the Appellant, were elected to the board of directors.

Exhibit 3, p. 77

7.—The Ontario Securities Commission commenced an investigation on or about the 18th November, 1941. It seized all the books and records of the Respondent and conducted an examination of them. The Ontario Securities Commission obtained from the Appellant and his employees the minute book and all other papers and documents belonging to the Respondent which the Appellant or his employees had in their possession. The Ontario Securities Commission then made a report based upon a complete examination of these records.

p. 121, l. 35—p. 122, l. 9
p. 86, ll. 15–25;
p. 132, ll. 1–12;
p. 158, l. 40—p. 159, l. 20

8. Mr. W. H. Bouck was a solicitor for Preston East Dome Mines Limited. This company was one of the Respondent's principal creditors. Mr. Bouck became a director of the Respondent on the 9th December, 1941. Prior to his election as a director of the Respondent he was instructed to investigate the Respondent's affairs. Mr. Bouck saw and examined the minute book and all documents, cheques, receipts, bank statements and other papers now relied upon by the Respondent in this action. Mr. Bouck

p. 243, l. 7; p. 262, l. 38
Exhibit 3, p. 81, ll. 13–16
p. 307, ll. 18–22
p. 243, l. 55—p. 244, l. 8; p. 261, ll. 18–27
p. 258, ll. 44–46

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visited the office of the Ontario Securities Commission on three occasions. He saw, and for a time had in his possession, the statement made by the auditor of the Securities Commission. He also spent a number of evenings going over the accounts, and then he worked out a draft statement which in his view fairly represented the position of the Respondent.

p. 244, l. 8-p. 246,
l. 11

9.—On the 2nd December, 1949, Mr. Seguin, Mr. Buchanan and Mr. Tovell went over the statement which Mr. Bouck had drafted and then all four went up to the office of the Securities Commission where they saw the Deputy Registrar and the Accountant for the Commission and discussed the affairs of the Respondent. They were all at that time shown the report prepared by the Commission. The evidence is that the Appellant was not present at any of these discussions between the other directors and the officers of the Securities Commission, although he was questioned by the officers of the Commission and was interviewed by Mr. Bouck. 10

p. 246, l. 9-p. 247,
l. 46

pp. 381-2

p. 247, ll. 39-46 ;
p. 250, ll. 19-33 ;
p. 268, ll. 32-35

10.—On the 4th December, 1941, after having studied the report of the Securities Commission and the minute books and other documents, Mr. Bouck prepared a statement to form the basis whereby all dealings between the Respondent and the Appellant could be settled. The Appellant had nothing to do with the preparation of the statement and when it was shown to him he objected to it as being unduly harsh, although he later 20 reluctantly agreed to it.

p. 248, l. 1-p. 251,
l. 5

p. 381, l. 14

11.—The statement was prepared on the following basis: There was no money in the Respondent's account. It was quite impossible to tell how much money the Respondent had in fact received. The only source from which the Respondent could have obtained money legally was from the sale of shares and 1,963,181 shares had been issued. The new directors by this statement held the Appellant responsible to the Respondent for what the directors considered should have been obtained for those shares, thus making the Appellant (irrespective of what the Appellant had obtained for them) pay an adequate price for the shares. The Appellant was therefore 30 held accountable for a price fixed at about 20 cents a share for all shares which had been issued, except those which had been transferred for the purchase of mining properties. On the other hand, the Appellant by this statement was credited only with such expenses as he could strictly prove. His word was not accepted for anything. All his expenses had to be verified or they were disallowed. Expenses which the directors considered properly payable by the Respondent were shown as credits on the statement, whether the Appellant or the Respondent had in fact paid them. For the use of his office, for all his work, for his legal fees, the Appellant was allowed a lump sum. The directors did not, and probably could not, prepare a 40 statement showing what the Appellant had actually received for the Respondent and what he had actually done with the money he had received for the Respondent; rather, they held the Appellant responsible for all money which they considered that the Appellant should have obtained

p. 381, ll. 21-39

p. 382, ll. 1-3

for the Respondent and allowed him a credit for any money they considered had been spent properly. Any purchases or expenditures purported to have been made on behalf of the Respondent which the directors considered not to be proper, they repudiated by not allowing the Appellant a credit for the expenditure or purchase.

12.—One of the chief complaints against the Appellant at this time was that he had been speculating on the stock market in the Respondent's name. The new directors considered that this speculation was improper and therefore they would not recognise and refuse to adopt the transactions
 10 on behalf of the Respondent. They would thus not allow the Appellant to charge the Respondent for shares which he had bought on its behalf and which they did not consider worth the money which the Appellant appeared to have paid for them. At the time of the settlement the Respondent had in its possession, as a result of the speculation, 56,300 shares of Bear Exploration and Radium Limited, 25,000 shares of Giant Yellowknife Gold Mines Limited, 2,500 shares of Hugh-Pam Porcupine Mines Limited, and 7,700 shares of New Augarita Porcupine Mines Limited. The directors would not adopt these purchases as the Appellant had bought
 20 some of the shares of Bear Exploration and Radium Limited and the shares of Giant Yellowknife Gold Mines Limited for the Respondent from himself, and the Appellant was interested in all of these companies as a director and a shareholder. The shares were considered to be of little value, were held on margin, and were not at that time worth what the Appellant charged the Respondent for them. The directors, therefore, insisted on treating these share transactions as not having been made on the Respondent's account. These shares were accordingly handed over to the Appellant and he was not in the settlement allowed to charge the Respondent the price paid for them. One purchase of shares by the Appellant had, however, proved advantageous to the Respondent. That
 30 was the purchase of 3,400 shares of Preston East Dome Mines Limited still on hand in December, 1941. The price of these shares had risen on the market and the shares had been used by the Respondent as security. This purchase alone was ratified. All other purchases of stock the directors elected to disaffirm.

13.—Under the statement the Appellant owed the Respondent \$18,765.29, but the directors realised that the Appellant had no ready money although they knew he could obtain shares of the Respondent from his sisters. The directors therefore asked the Appellant to deposit 93,816 shares of the capital stock of the Respondent with the Premier Trust
 40 Company (the transfer agent of the Respondent) and to agree that the Respondent should sell these shares as and when and at such price as the Respondent saw fit, in order to liquidate the Appellant's indebtedness to the Respondent.

p. 249, ll. 1-40 ;
 p. 277, ll. 9-45 ;
 p. 307, l. 36-p. 308,
 l. 12

p. 382, l. 6

p. 382, ll. 4-5

p. 253, ll. 27-30

14.—It is clear from the evidence that the directors agreed to the settlement; that the Appellant deposited certificates for 93,816 shares of the Respondent with the Premier Trust Company pursuant to the settlement agreement; and that these shares were sold under the direction of the Respondent. The Respondent received payment in full of the \$18,765.29.

p. 256, ll. 15-18

15.—The Appellant respectfully submits that an agreement was entered into and that there was no fraud or other improper conduct on the part of the Appellant in the making of the settlement agreement.

16.—The judgment of the Court of Appeal appears to overlook the fact that the statement presented to the meeting of the directors on the 9th December, 1941, did not purport to be a financial statement showing the exact position between the Appellant and the Respondent, but was the statement prepared by Mr. Bouck as the basis of settlement, with knowledge of the position after seeing the report of the Ontario Securities Commission. 10

p. 244, l. 19-p. 245, l. 36

17.—What was in the minds of the directors at the time was, in the Appellant's submission, clearly relevant to the issues. The Appellant accordingly sought to lead evidence about the information obtained from the Ontario Securities Commission. The Respondent, however, objected, and McFarland, J., ruled that the evidence was inadmissible. It is clear, however, that on the 9th December, 1941, the directors knew that actions of the Appellant had been illegal. The purpose of the settlement agreement was to make the Appellant settle for these illegal actions. 20

p. 248, ll. 1-22 ;
p. 280, ll. 5-26 ;
Exhibit 3, pp. 80-81

18.—The Appellant submits that the settlement was fair and reasonable. The directors knew and were in a position to know the sale prices of the Respondent's shares between 1936 and 1941. One of the directors was a transfer agent of the Respondent. Two of the directors were stock brokers who had sold the Respondent's shares, and the fourth director was a solicitor. The directors did not wish to go into the question of the price the Appellant had obtained by selling the Respondent's shares. The basis of making the Appellant pay 20 cents a share was fair. Twenty cents was a high price for the Respondent to receive for all shares sold from its incorporation. The mining property was merely a prospect. The Respondent has never since been able to obtain any price comparable with the price obtained from the Appellant for these shares. The Appellant sold some shares for substantially more than 20 cents per share, but the cost of selling was high. In the settlement the Appellant was not allowed to charge any selling expenses. The Respondent had commitments from one P. W. Bishop to purchase shares at 20 cents a share. This was one of the reasons for valuing the shares at 20 cents in the settlement with the Appellant. Moreover, the settlement brought ready money into the Respondent's treasury. It was a well-known fact that the Appellant had no money. By the settlement the Respondent obtained shares from the Appellant's sisters. If the directors had preferred an accounting, the Respondent might have obtained a 30 40

judgment for a larger amount, but they could not have obtained immediate money without the co-operation of the Appellant's sisters. Had the Respondent asked the Appellant to account for his profit from the sale of these shares, the Respondent would have adopted the Appellant's sales and there was good reason for the Respondent not wishing to do so.

- 19.—The directors were willing to recognise that, even though the records and documents of the Respondent had not been kept in a proper manner, the Appellant had done valuable and constructive work on behalf of the Respondent. The Appellant had incorporated the Respondent.
- 10 The head office of the Respondent had been in his office. He had looked after all the Respondent's correspondence. He had negotiated the purchase of all the Respondent's mining claims. He had supervised the operations at the mining property. He had negotiated all agreements entered into by the Respondent. In particular, he had negotiated a very valuable agreement with Preston East Dome Mines Limited, whereby the latter company agreed to cross-cut its shaft at a depth of 1,050 feet into the properties of the Respondent. The Appellant had looked after the Respondent's legal affairs. For all his work, for the use of his office, his stenographer, for his legal fees (including the defence of three actions, and an appeal to the Court of Appeal), for his expenses (including travelling and payments made to the secretary), the Appellant was allowed a lump sum arrived at by paying him at the rate of approximately \$225.00 a month. There is not the slightest suggestion that the Appellant claimed to have done work which he had not done. Even if the Appellant erred in claiming too high a price for his services, his doing so would not be misrepresentation.
- 20.—Laidlaw, J.A., in finding fraud relies upon an agreement whereby the Appellant and his two sisters agreed to cast all their voting power in favour of certain directors for a period of two years. It is respectfully submitted that the learned judge has misconceived the object of this agreement. Its purpose was to ensure that the Appellant could not, by influence exerted on his sisters, get control of the Respondent again after the settlement was completed. Even after the settlement the Appellant's sisters still had enough shares to control the Respondent. Also it was important to the Respondent that the Appellant and his sisters should not be in a position to compete with the Respondent by sale on the market of a large number of the Respondent's shares while the Respondent was holding shares for sale to liquidate the Appellant's debt. The new directors therefore insisted that the Appellant and his two sisters sign a voting trust agreement covering their shares and providing that for a period of two years
- 49 the voting rights in respect of the shares of the Appellant and his sisters could only be exercised in accordance with the wishes of the majority of the board of directors of the Respondent in office at the time, and that the share certificates should be deposited subject to the agreement and should not be transferred or realized without the consent of the majority of the board. Such an agreement, which tied up all the Appellant's shares and

p. 249, l. 43-p. 250,
l. 17

p. 43, ll. 20-23
p. 46, ll. 29-34
p. 161, l. 25-p. 162,
l. 12

pp. 424-428

p. 344, l. 4-p. 345,
l. 11; p. 346, ll. 23-
31

p. 273, l. 26-p. 274,
ll. 5, pp 464-465

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all the shares of the Appellant's sisters so that they could not be sold, could have a very serious effect on the interest of the Appellant and his sisters in the Respondent. As a safeguard to them it was provided that the directors would not enter into any agreement for the sale of more than 200,000 shares of the capital stock of the Respondent during the two-year period, except to Preston East Dome Mines Limited, without the consent of the Appellant. The exception to Preston East Dome Mines Limited was necessary in view of a previous contract arrangement with Preston East Dome Mines Limited. This agreement with the Appellant and his sisters was not challenged by the Respondent in the pleadings and the good faith 10 of the directors in entering into the agreement has never been questioned. The fact that the agreement was omitted from the minutes cannot be attributable to the Appellant. A copy of the agreement was put with the Respondent's papers.

p. 264, l. 45-p. 265, 21.—It is further submitted that if there was any misrepresentation by the Appellant, no statements made by him were in any way relied upon by the directors, who took the position that they would not accept his word unless it was substantiated.

22.—So far as non-disclosure is concerned, it is respectfully submitted that at the time of the settlement the parties dealt with each other 20 at arm's length and the settlement was pressed upon the Appellant by the other directors. Far from the Appellant being in any position of domination or influence, he was being sorely pressed by the Ontario Securities Commission; the directors had possession of the books and statements of the Respondent and the report of the Ontario Securities Commission; and the Appellant knew that the other directors had studied these documents. The very settlement itself amounts to a waiver on the part of the Respondent of the right to full disclosure of the details of his wrongdoing which an accounting would disclose, and which the Appellant could not give after he had been deprived of access to the records. 30 It is further submitted that the Appellant did all he was required to do under Section 94 of the Ontario Companies Act, as he disclosed his interest and refrained from voting. The nature of his interest as party to the settlement was, of course, obvious. Section 94 thus affords the Appellant a complete answer unless the Respondent proves fraud.

Exhibit 3, p. 82,
l. 32

23.—It is also submitted that the only remedy for non-disclosure is an equitable remedy and that there can be no damages awarded therefor unless the non-disclosure has the effect of rendering false a representation already made.

24.—Even if fraudulent misrepresentation were established or there 40 was some culpable non-disclosure (and it is submitted that there has not been) rescission cannot be granted as the Respondent had been guilty of a very great delay in bringing action, the parties cannot be restored to the

position which they were in before the agreement was entered into, and the rights of third parties (the Appellant's sisters) are affected.

25.—In any event it is submitted that whether or not there is any binding settlement, the Respondent cannot be allowed at this stage to alter its decision to repudiate the purchase of the 56,300 shares of Bear Exploration and Radium Limited, the 25,000 shares of Giant Yellowknife Gold Mines Limited, and the 7,700 shares of stock of the Respondent and the transfer thereof to the Appellant consequent on such repudiation. The settlement takes into consideration that such sales had been repudiated
10 by the Respondent but the repudiation is entirely distinct from the question of the Appellant accounting for his wrongdoing.

26.—It is respectfully submitted that if there was any fraud on the part of the Appellant in making the settlement agreement, the Court of Appeal was right in holding that the only remedy was damages, but that the Court of Appeal erred in the method by which it ordered the damages to be computed.

27.—The only possible basis for making the Appellant account for the price that the 56,000 shares of Bear Exploration and Radium Limited, the 25,000 shares of Giant Yellowknife Gold Mines Limited, and the 7,700 shares
20 of stock of the Respondent rose to after the 9th December, 1941, would be on the basis that there had been a conversion of the shares by the Appellant, and there are no grounds upon which it can be held that the Appellant converted these shares.

28.—If the Respondent is entitled to damages for fraud in the making of the settlement agreement, the measure of damages (it is submitted) must be the difference between the amount the Appellant paid to the Respondent under the settlement agreement and the amount that the Respondent's claim against the Appellant was worth on the date of the settlement. No account should be taken of subsequent values.

30 29.—The Appellant respectfully submits that it is entirely inconsistent to say on the one hand that the settlement cannot be set aside (so that the Appellant can keep the shares he got under the settlement) and on the other hand that the Appellant must account for the value which the shares subsequently attained. Such an accounting would be based on the premise that the Respondent and not the Appellant was entitled to the shares. The remedy of damages is based on the hypothesis that the Respondent had elected, or is compelled, to adhere to the agreement which gave the Appellant the complete ownership of the shares and thus the benefit of all perquisites of ownership. In other words, to hold that the Appellant
40 must account for subsequent profit, is to hold him to be a constructive trustee of the shares which the Court in the same judgment by saying the settlement agreement cannot be set aside, acknowledges to be his property.

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p. 3, ll. 26-38

p. 19, ll. 11-28

30.—It is respectfully submitted that the Court of Appeal also erred in making the Appellant account for the actual value as of times of issue of all the stock of the Respondent received by all persons on the requisition or authority of the Appellant and G. H. Bourne. Such accounting is much more than is asked for in the statement of claim. Paragraphs 16 and 17 of the statement of claim allege that 252,850 shares were improperly issued (see also particulars of the statement of claim) on the 9th December, 1941. In fact, 1,963,181 had been issued. The allotment of shares for certain mining claims was never questioned. It is submitted that the Respondent is bound by its pleadings, and that the Court of Appeal is not entitled to give relief in respect of the issue of other shares. 10

31.—The Appellant therefore humbly submits that this appeal should be allowed with costs for the following amongst other

REASONS

1. BECAUSE on the 9th December, 1941, the Respondent and the Appellant settled all matters between them on terms with which the Appellant duly complied.
2. BECAUSE the settlement agreement was not procured by the fraud or any other improper conduct of the Appellant.
3. BECAUSE the settlement agreement was made in circumstances which made it fully binding upon the Respondent, and the agreement debars the Respondent from the present claims against the Appellant. 20
4. BECAUSE evidence was wrongly excluded of the information which the Respondent's directors had obtained from the Ontario Securities Commission prior to the settlement agreement.
5. BECAUSE the Court of Appeal's findings of fact adverse to the Appellant are not justified by the evidence.
6. BECAUSE the Court of Appeal granted relief to which in any event the Respondent is not entitled. 30

FRANK GAHAN.

W. B. WILLISTON.

In the Privy Council.

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BETWEEN
JAMES JOSEPH GRAY
(Defendant) APPELLANT
AND
NEW AUGARITA PORCUPINE
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(Plaintiff) RESPONDENT

CASE FOR THE APPELLANT

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