2021/2022

LAW 451
Corporations Law

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CONDENSED ANNETATED NOTES (CAN)

UNIVERSITY OF ALBERTA
FACULTY OF LAW

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CHAPTER 1: CHOOSING THE FORM OF BUSINESS VEHICLES

Types of Business Vehicles

When starting a business, there are three (primary) types of business vehicles, and each have their own pros and cons. The three typical vehicles are:

1. Sole Proprietorships
2. Partnerships
3. Corporations

There are 6 criteria to consider when advising a client who is starting a new legal entity:

- (a) Creation & formal requirements
    - (a) What work needs to go into establishing this type of business venture
- (b) Liability
    - (a) Who bears the financial risk of the financial operations? This includes voluntary obligations (contracts with suppliers) and involuntary (torts)
    - (b) This is probably the largest factor when weighing which vehicle to pick because consequences can be very severe
- (c) Control
    - (a) Who has the power/authority to make decisions of the business enterprise (strategic, managerial, employment, etc)
    - (b) How does the choice of legal form affect the allocation of power of these decisions
- (d) Participation in Profits & Distribution of Assets
    - (a) Who has the legal rights to profits/assets of the business
    - (b) How does the choice of business form restrict flexibility and discretion on how the assets are distributed
- (e) Dissolution
    - (a) If, when and how a business vehicle ceases to exist for legal purposes (insolvency or bankruptcy for example), what legal requirements are there based on the vehicle
- (f) Tax Implications

(a) What taxes are to paid by who and what amount
(b) This is probably the second largest factor when considering which vehicle to chose.

A corporate lawyer will focus on the legal repercussions for their clients, and the way to manage risks from legal liability

- Tax lawyers, and sometimes corporate lawyers will advice their clients such that tax implications will drive the transaction

Sole Proprietorships

Sole Proprietorship: a business vehicle where there is no legal separate personality from the individual proprietor/owner and all obligations of the business are obligations of the individual owner

- This means all risks fall on the individual owner
- But all benefits also accrue directly to the individual owner
- The assets of the business are assets of the individual owner.
- There is no legal separation between the owner and the business they are running
    - Because of this, there are various knock-on consequences.

1. Creation
    a. Simplest and cheapest vehicle. There is nothing legally required in the formation of the proprietorship
    b. Typically, these are small mom and pop shops, but any size business can be run as a sole proprietorship. Most often they are just an individual who wants to run a business
    c. No documents need to be filed to constitute a sole proprietorship, but there is a formal requirement to register a trade name

Partnership Act, RSA 2000, c P-3
Section 110 (1) Each person who (a) is engaged in business for trading, manufacturing, contracting or mining purposes, (b) is not associated in partnership with any other person or persons, and (c) uses as the person's business name (i) some name or designation other than the person's own, or (ii) the person's own name with the addition of "and company" or some other word or phrase indicating a plurality of members in the firm, shall file with the Registrar, in a format acceptable to the Registrar, a declaration in writing of the fact. Section 111 If a person who has filed a declaration under section 110 ceases to carry on business under the business name referred to in the declaration, the person may file with the Registrar a declaration stating (a) the date the declaration under section 110 was signed, and (b) the date on which the person ceased to carry on business under that business name. Section 112 Every member of a partnership and every other person required to file a declaration under this Act who fails to comply with the provisions of this Act respecting filing is guilty of an offence and liable to a fine of not more than $500. Section 113 An action or other proceeding instituted in any court in Alberta (a) by an unregistered partnership, or

(b) by any other person who is required to register a declaration under this Act but has failed to comply with the requirements respecting registration,

may be stayed on application of the defendant or party opposite in interest until the partnership becomes registered or until the declaration is filed, as the case may be.

d. The *Partnership Act* provisions are more of an incentivization to register trade name more than a legal requirement
e. Penalties for non-compliance are under s112 and s113, but not particularly severe ($500 in s112 and the inability to bring legal action until registered under s113)
f. There needs to be some public record for means of transparency or accountability, so people know who they are dealing with.
    i. So, s110 requires the enumerated peoples in (a), (b), (c) to declare their name, address, business name within 6 months of opening
        1. This includes people who are not in partnership, and use a name that is not their own
    ii. If there is more than one person's business name, "& company/co"
g. But, section 110 only is triggered when certain kinds of businesses are engaged: trading, manufacturing, contracting or mining
    i. The language of these 4 are kind of cryptic, and there is very little case law as to the analysis of them
        1. Mining and manufacturing are kind of straightforward
        2. But what defines contracting and trading?
            a. Trading is usually the sale of goods
            b. But contracting is quite ambiguous. The general view is that it can't simply mean entering into a contract (if it were that, the entire provision would be reducnant since manufacturers and miners also contract). It is usually interpreted as contractors (those who are in the building of construction projects)
    ii. The language of the section seems to exclude service field professions (law, accounting, engineering). These would not be captured by s110, so they would not need to register a trade name
h. "John Doe's Pizza Pies"
    i. Is in business of trade, but it is just John's name, so (c)(i) is not satisfied
    ii. No requirement to register
i. "Amazing Pizza Pies"
    i. No naming at all, so it would have to be registered, so the public knows who it is dealing with
    ii. Requirement to register
j. "John Doe & Co's Amazing Pizza Pies"
    i. & Co means (c)(ii) is satisfied
    ii. Requirement to register
k. "John Doe & Co's Nail Salon"
    i. Does 'nail salon' fit into one of the four professions?
    ii. Likely a service industry and probably not sufficient to satisfy (a)
    iii. (likely) no requirement to register
l. There are other considerations as well, including municipal, provincial and federal licensing, regulatory, zoning requirements. These would apply to al business forms, regardless of the vehicle they use
    i. These are independent of legal requirements for formation.

        ii. If you want to run a pizza joint out of your garage, you probably can, but the City would probably not let you without valid permits and requirements.
2. Liability
    a. Unlimited Liability: the individual owner/proprietor is legally, personally responsible for all business debts and obligations
    b. All of the individual proprietor's assets are at risk (whether used for business or personal reasons) to satisfy the business's obligations
        i. This means their personal assets can also be seized
    c. This is for all voluntary obligations (loans or contracts) or involuntary obligations (torts)
        i. If you use old cheese while making pizza and it makes a customer sick, you could be liable for negligence and it could be drawn from your personal assets
        ii. Also applies for vicarious liability. If an employee commits a tort through negligence or other tort, the employer is vicariously liable as long as it is in the course of employment
3. Control
    a. All power is with the sole proprietor. They are not accountable to anyone else. No management structure is needed
4. Profits and Asset Distribution
    a. Proprietor has all rights to all profits of the business and to net assets (gross income minus expenses).
5. Dissolution
    a. Proprietor has sole discretion to determine the duration of business – it is as easy to dissolve as it is to create
    b. Death of proprietor results in dissolution of the business
        i. This means there is no capacity for perpetual existence for sole proprietorships
        ii. Sole proprietorship cannot exist forever
        iii. Partnerships and Corporations, in contrast, can exist forever
    c. Section 111 of the *Partnership Act* requires registered proprietorships under s110 to file a declaration when they cease to exist or cease to carry business under that name
6. Tax Considerations
    a. Proprietor is taxed directly for the incomes/losses of the business as an individual
    b. Losses from the business can be directly deducted from the income of other sources of the proprietor. This is often seen as a good thing for the first few years
        i. If the proprietor is generating losses, they can be deducted from other incomes (employment income)
7. Main points:
    a. Advantages: simple, cheap, no documents needed, potential tax benefits
    b. Disadvantages: no separate legal personality, so unlimited personal liability for business obligations (personal assets of the provider at risk)
        i. Unlimited personal liability means that appropriate insurance is critical
        ii. You would want to ensure the client is well aware of the risks before choosing to proceed

<u>Partnership</u>

There are three types of partnerships:

- Ordinary
    - Partners have unlimited personal liability
- Limited Liability Partnership (LLP):
    - partners have unlimited personal liability subject to section 12 of the *Partnership Act*
    - Statutory modification on top of ordinary partnerships

- Limited Partnership (LP): the general partner has unlimited liability, the limited partner has liability limited to the amount of its investment, subject to section 64 of the *Partnership Act*
    - Statutory modification on top of ordinary partnerships
    - Often with invested vehicles (general partner involved in management, and also passive limited partners that are not engaged but invested (they would lose partnership if they engaged)

Partnership: the relationship that subsists between persons carrying out on a business in common with a view to profit

- Partnerships, by definition require more than one person, and they are working in common to generate the profit (recall profit is gains over and above of expenditures)
    - Each partner has a reciprocal duty of loyalty and good faith toward their partners (*Hitchcock v Sykes*)
    - Partners are prohibited from competing with the firm under section 34 of the *Partnership Act*
- Partnerships are actually quite complex, they are ruled by the *Partnership Act*, but also under equity and common law
    - Section 105 says that common law and equity can still exist, except when inconsistent with the statute
- Partnerships are not distinct legal entities
- Partnerships are rather complex since it is heavily mixed in statutory, common law and equity, particularly with the area of agency (which is complicated in its own right)

<u>Ordinary Partnerships</u>

1. Creation and Formal Requirements
    a. Under section 106 of the *Partnership Act*, persons associated in trading, manufacturing, contracting or mining purposes shall file with the Registrar a declaration in writing signed by several members of the partnership
    b. Until a declaration is filed to cease being a partner, a partner will remain as a partner (section 115)
        i. This has important implications for liability of a partner
    c. Partnerships, in practice, should be accompanied by a partnership agreement. It should be tailored to the business venture in question and specifies the rights, intentions, roles and obligations and interests of the partners (it is bespoke)
        i. This makes it quite costly and complicated to draft
        ii. Waterfall clause: when does a particular type of partner get benefits
    d. Like a sole proprietorship, there is no legal requirement for a legal document to constitute an operation, but it is the best practice to do so
        i. But, partnerships are still governed by the law of contract, since not all contracts need to be said, they can be enforced through action
            1. Objective approach: what were the reasonable expectations of the parties
            2. So, it doesn't matter if partners say "we didn't intend to be partners"
            3. We look to their conduct and ask if it could be reasonably thought to constitute a partnership
            4. A legal determination of partnership can be made through the reasonable interpretation of their conduct
    e. Partnerships are not separate legal entities, so it is not always clear when and at what point in time the partnership exists
    f. Section 4 sets out factors that should be considered, including but not limited to

i. common ownership of property does not itself create a partnership (a)
ii. sharing of gross returns does not itself create partnership (b)
iii. receipt by a person of a share of profits is proof, in the absence of evidence to the contrary, that the person is a partner in the business but there are exceptions (c)

g. Why is share of returns enough, but gross returns are not?
  i. Gross returns only care about revenue, but profit is net revenue and expenses
  ii. So, if you have an interest in profits, you also have an interest in how the enterprise expenses (how revenue is made but also how expenses are incurred)
  iii. Indicates that there is an interest in the management of the business of the whole rather than just the bottom dollar that comes out of it like most employees care about

Volzke Construction v Westlock Foods, 1986 ABCA 136

Facts:

Mr. Shefsky was the main shareholder of Westlock Foods (defendant/respondent). Volzke Construction (plaintiff/appellant) undertook to build the Westlock Shopping Centre, which was 80% owned by Bonel Properties, and 20% owned by Westlock Foods.

- Volzke was not paid in full. It was accepted as fact that amounts went unpaid ($77,000) and a contract did exist
- Volzke brought action against Westlock, alleging that Westlock Foods is a partner of Bonel

Procedural History:

At the Alberta Court of Queen's Bench, the trial judge found they were not partners, just co-owners

Issue:

Are Westlock Foods and Bonel partners or merely co-owners?

Rule:

Section 1 of the *Partnership Act*

In this Act,

(d) 'partnership' means the relationship that subsists between persons carrying on a business in common with a view to profit;"

Section 4

In determining whether a partnership does or does not exist, regard shall be had to the following rules:

(c) the receipt by a person of a share of the profits of a business is prima facie proof that that person is a partner in the business"

Analysis:

If Westlock Foods and Bonel are partners, the defendant is liable for the obligations of the partnership, including the $77,000 to the plaintiff. Section 1(d) of the *Act* means partnerships are relationships between parties carrying on business with a view to profit. The trial judge opined that the lack of control of Westlock Foods over Bonel negated partnership, but control plays not role in the definition.

- Additionally, section 4(c) shows that receipt for share of *profits* is proof that they are in business.
- The parties agreed the costs and profits of the Centre were split 80-20, so this is *prima facie* proof of partnership and control is not required for the existence of a partnership

Activities of the parties are consistent with those of partners. Both parties pledged for a collateral for a loan.

Conclusion:

Partners – defendant liable for unpaid amounts.

Hold, Order:

Appeal allowed

Ratio:

Control is not germane to the determination of partnership; the domain of sharing profits and interest in how the enterprise is being managed

h. The *Volzke* decision is the leading case for interpretation of conduct constituting partnerships in Alberta. Most noteworthy was the control dynamic being totally irrelevant.
i. Even if one party was completely uninterested in executing company standards beyond profit, they would be *prima facie* partners as long as proof of splitting profits existed.
j. Once a partnership was found, Westlock Foods was liable for the unpaid contract with Volzke, so Volzke could enforce the agreement against Westlock Foods.

2. Liability
   a. Similar to sole proprietorships, partnerships are not distinct legal entities. Partners are responsible for the liabilities and obligations of the partnership and other partners in the relationship
   b. Joint Liability: a shared liability such that each defendant is liable for the full extent of the obligation in question. Section 11(2) of the *Partnership Act* confirms this
   c. Several Liability: a separate or distinct liability based on apportionment according to fault or responsibility (damages apportioned based on contribution to the wrong)
   d. Joint and Several Liability: a form of liability such that, the plaintiff can collect 100% of its judgements from any of the defendants but facilitates apportionment as between defendants according to fault or responsibility
      i. Section 13: firm is liable for wrongful acts or omissions of a partner acting in the ordinary court of business of the firm, or with the authority of the partner's co-partners
      ii. Section 14: liability of the firm when the partner, acting within the scope of the partner's apparent authority, misapplies money or property received from a third party
      iii. Section 15: partners of liable *jointly* with the partner's co partners and also *severally* for everything for which the firm while the partner is a partner in it becomes liable under sections 13 or 14
         1. Actual and apparent authority as in ss 13 and 14 are key, since *Volzke* found that 'control' is irrelevant.
   e. Section 20: A partner is only liable for wrongdoings that occurred when they were partner – not before or after. Section 20(2) also confirms that a partner cannot avoid liability for wrongdoings made during partnership by retiring as partner, but s20(3) allows this to be displaced through an agreement or contract.
3. Control
   a. Section 28 of the *Partnership Agreement* found that subject to section 12 (more to come) or an express or implied agreement between partners, the interest of partners in the partnership property and their rights and duties in relation to the partnership shall be determined by s28(e): each partner can contribute to management
   b. Section 6: each partner is an agent of the firm and of the partners other partners for the purpose of business of the partnership

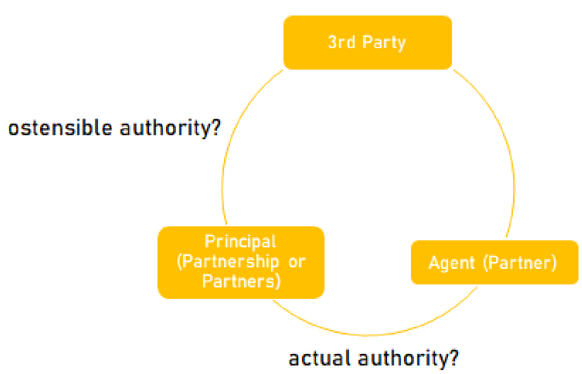
c. Section 7: the acts of each partner in carrying on in the *usual way* business of the kind carried on by the firm, of which the partner is member, bind the firm and the partner's partners. But there is an exception to this, with two criteria:
    i. 7(a): the partner has no authority to act for the firm in that capacity AND
    ii. 7(b): the person with whom the partner is dealing knows that the partner has no authority, or does not believe/know that person is a partner

d. Partner status as agent is critical for how it binds the partner and imposes liability on others in the partnership. It is thus always needed to determine if they are an agent or not

e. The scope of the agent's authority determines the power they have. The power of the agent has to affect the legal position of their principal
    i. If an agent enters into a contract on behalf of the principal (likely the whole company), the question is whether the principal is bound because the agent had the authority to do so. But, it can
    ii. Agency is the fiduciary relationships which exists between persons, one of whom *expressly or impliedly* consents ta the other should act on his behalf so as to affect his relations with third parties, and the other of whom similarly consents to doing that act. The one who is represented is called the 'principal'. The one who represents is the 'agent'. Any other party to the two are called a 'third party'.

Actual Authority: a legal relationship between a principal and an agent created by a consensual agreement to which they alone are parties. This agreement can be either:
- Express: authority granted expressly through oral or written agreement
- Implied: every agent has implied authority to do everything necessary or incidental to carrying out this express authority, unless expressly contradicted by the principal. This is by reasonable interpretation of what is required to carry out the object of thee express authority.
    - So, If the principal grants express authority to an agent to conduct a sale, the agent likely has implied authority to negotiate the sale, given that is necessary or incidental to the fulfilment of the object of the express authority

Ostensible (or Apparent) Authority: the impression of authority that the principal has created in a third party. This arises when a person is held out as an agent when the person is not, or being an agent is held to possess an extent of authority greater than that which they were actually given.
- If the conduct implies authority, even if not expressly or impliedly granted by the principal, this can create the impression apparent authority in that agent, a representation of the principal's actions



- To determine Actual Authority, since it is given within the business, it needs to be an internal analysis between the principal and agent

- To determine Ostensible Authority, since it is made by representations, needs to be an external analysis of the relationship made between the principle and third party.

McDonic Estate v Hetherington, [1997] 31 OR (3d) 577 (CA)

Facts:
Mr. Watt was a partner with at a legal firm. He was partners to Hetherington et al. (partner defendants) and was retained by Ms. McDonic and Ms. Cooper (plaintiffs) for an investment transaction. Watt made various investments for the plaintiffs.

- However, in doing so, some loans were insufficiently secured, others were completely unsecured
- Watt did not inform the plaintiffs as to the nature of the investments, not did he get their approval. He failed to protect their interests.
    - The plaintiffs eventually lost several hundred thousands of dollars, so they bring action against Watt and all other partners

Procedural History:
At trial, partners were not liable since Watt was just an advisor, outside a law firms authority

Issue:
Are the defendants, as Watt's partners, liable to the plaintiffs for their loss based on actual or apparent authority?

Rule:
Section 11 of the (Ontario) *Partnerships Act*
Where by any wrongful act or omission of a partner acting in the ordinary course of the business of the firm, or with the authority of his co-partners, loss or injury is caused to a person not being a partner in the firm, or any penalty is incurred the firm is liable therefor to the same extent as the partner so acting or omitting to act.
Section 12
In the following cases, namely,
(a) where one partner, acting within the scope of his apparent authority, receives the money or property of a third person and misapplies it
the firm is liable to make good the loss

Analysis:
Actual Authority
Section 13 of the *PA* [equivalent to s11 in Alberta] renders partners liable for the third party's loss by a partners conduct, if that partner was acting either with the partners authority, or in the ordinary course of business of that firm.

- This means liability can come from express or implied authority to act on behalf of the other parties
    - Express authority flows from the authorization of other partners
    - Implied authority flows from acts done in the ordinary course of the business of the firm

There was no evidence to support Watt had express authority to invest on behalf of the other partners. Was their implied?

- Watts was investing money for firm clients, using the law firm's trust account, clients and facilities.
    - There is evidence that this was normal work for that firm
    - So, even if investment advice is the ordinary course of business in law firms, it was done in the ordinary court of *this* particular law firm.
    - This grounds implied authority

The defendants argued that Watt did not comply with the protocols for transactions, so they should fall outside the ordinary course of business of that firm

- However, it is the nature of the activity, and not how it was performed, that will determine whether the activity falls in the scope of that firms ordinary business
    - Even if sloppily performed, partners are still liable for it.
- So, Watts was acting in the ordinary scope of business of this firm, so he had implied authority, so the defendants are liable for Watts actions

The losses suffered by the plaintiffs were the result of Watt's action under implied actual authority of the ordinary course of business of the firm.

Apparent Authority

Liability goes even further in s12 where liability can be extended without express, or implied authority, but apparent authority too [s14 of the Alberta Act]

- Apparent authority is determined by a consideration of whether the person dealing with the partnership would reasonably regard the partner as acting on behalf of a partnership
- In this case, there is strong evidence that Watt had apparent authority
    - Other partners acknowledged that plaintiffs were clients of the firm
    - Watt was a partner of the firm, and had an office in the firm
    - He corresponded to the plaintiffs with the firm letterhead
    - Correspondence identified plaintiffs as clients and authorized the firm to hold their money. Cheques received by plaintiffs came from the firm
    - All the records referable to the investments were kept by the firm and bookkeeping was done by firm employees.
- In short, Watt was acting in a capacity as a partner in that law firm and any reasonable person in the position of McDonic would have no doubt of this

He was acting in the scope of his apparent authority, so all partners are liable for the losses from Watt's misapplication.

Conclusion:

Partners liable for actions of Watt

Hold, Order:

Appeal allowed

Ratio:

Express authority can be cemented from the authorization of the other partners. Implied authority does not have to be grounded in the industry standard for ordinary business, but the ordinary business of that specific company.

- Representations to ground apparent authority don't need to be express, but the conduct being done on the partners behalf and therefore cloaked the agent in apparent authority

- It is often for plaintiffs to sue all partners, for greater avenues to get all their damages.
- This is why partners will always deny authority was given to the agent. In this case, the ONCA found that Watts had both implied actual authority but also apparent authority.
    - It was irrelevant if most firms do not conduct investment practices, only that *that* firm did. This was enough to submit implied authority (internal analysis for actual authority)
    - Watt also acted as a partner to the firm in all dealings with the plaintiffs, so a reasonable person would adduce that he was cloaked in that authority (external analysis for ostensible authority)
- The court confirmed what is needed for all authority:
    - Express authority flows from the authorization of other partners
    - Implied authority flows from acts done in the ordinary course of the business of the firm
    - Apparent authority is determined by a consideration of whether the person dealing with the partnership would reasonably regard the partner as acting on behalf of a partnership

4. Participation in Profits and Distribution of Assets
    a. The partners do not "own" the property of the partnership in the usual sense
    b. Property belongs to the partnership and the partners can't divide it between them like real property.
    c. A partner can assign their share of the profits of the partnership, but not their partnership interests (substituting a new partner in their place) without the agreement of all the partners.
        i. Again, good practice is to have written agreements that specify all the rights and interests of the partners, though this is not needed.
            1. Section 28 says that agreement is allowed to displace this consent
        ii. They could form a contract where a new partner does not have to require consent to assign their interests
    d. If a partner assigns their share to another, the assignee is entitled to the profits, though does not acquire the right to management of the partnership: section 35.

5. Dissolution
    a. Dissolution is governed by ss 36-48 of the *Partnership Agreement*
    b. These are the default rules, they are subject to other agreements between partners (which all good companies should have)
    c. Section 36(1)(c): a partnership is dissolved when a partner gives notice to the others to dissolve the partnership
    d. Section 37: if a partner dies or becomes bankrupt, the partnership is dissolved.
        i. This also occurs when the partner's property in trust is assigned for the benefit of the partner's creditors
    e. Section 39 gives the Court broad discretion to dissolve a partnership on the application of one of the parties
        i. Things like 'the soundness of the minds of the partner' in s39(1)(a) or 'just and equitable that the partnership be dissolved' in s39(1)(f) are quite broad and general.

6. Tax Implications
    a. Because the partnership is not a separate legal entity, profits from a partnership are taxed in the hands of the partners only.
    b. Flowthrough treatment can be beneficial treatment in some situations because it avoids double taxation
        i. Corporations are subject to taxation at two levels (corporate taxes and dividends/interests of the recipient)
    c. There are also complications because dividends often give credits
        i. Businesses can decide if flowthrough treatment is beneficial in a particular case

Partnership Act, RSA 2000, c P-3
Section 1 In this Act, (g) "partnership" means the relationship that subsists between persons carrying on a business in common with a view to profit Section 4

In determining whether a partnership does or does not exist, regard shall be had to the following rules:

(a) joint tenancy, tenancy in common, joint property, common property or part ownership does not of itself create a partnership as to anything so held or owned, whether the tenants or owners do or do not share profits made by the use of it;
(b) the sharing of gross returns does not of itself create a partnership, whether the persons sharing the returns have or have not a joint or common right or interest in property from which or from the use of which the returns are derived;
(c) the receipt by a person of a share of the profits of a business is proof, in the absence of evidence to the contrary, that that person is a partner in the business, but the receipt of the share, or of a payment contingent on or varying with the profits of the business, does not of itself make the person receiving the share or payment a partner in the business, and in particular:

Section 6
Each partner is an agent of the firm and of the partner's other partners for the purpose of the business of the partnership.

Section 7
The acts of each partner in carrying on in the usual way business of the kind carried on by the firm of which the partner is a member, bind the firm and the partner's partners, unless

(1) the partner so acting has in fact no authority to act for the firm in the particular matter, and
(2) the person with whom the partner is dealing knows that the partner has no authority, or does not know or believe the partner to be a partner.

Section 11

(1) This section is to be applied subject to Section 12
(2) Each partner in a firm is liable jointly with the other partners for debts and obligations of the firm incurred while that partner is a partner.
(3) When a partner dies, the partner's estate is severally liable, in the due course of administration, for any debts and obligations of the firm incurred while the deceased partner was a partner that remain unsatisfied.
(4) The payment of debts and obligations under subsection (2) is subject to the prior payment of the separate debts of the deceased partner.

Section 13
When, by a wrongful act or omission of a partner acting in the ordinary course of the business of the firm or with the authority of the partner's co-partners, loss or injury is caused to a person not being a partner in the firm, or a penalty is incurred, the firm is liable for it to the same extent as the partner so acting or omitting to act.

Section 14
The firm is liable to make good any loss when

(a) one partner acting within the scope of the partner's apparent authority receives the money or property of a third person and misapplies it, or
(b) a firm in the course of its business receives money or property of a third person, and the money or property so received is misapplied by one or more of the partners while it is in the custody of the firm.

Section 15
Except as provided in section 12, each partner is liable jointly with the partner's co-partners and also severally for everything for which the firm while the partner is a partner in it becomes liable under section 13 or 14.

Section 20

(1) A person who is admitted as a partner into an existing firm does not by that admission become liable to the creditors of the firm for anything done before the person became a partner.

(2) A partner who retires from a firm does not by reason of retirement cease to be liable for partnership debts or obligations incurred before the partner's retirement.

(3) A retiring partner may be discharged from any existing liabilities by an agreement to that effect between that partner and the members of the firm, as newly constituted, and the creditors.

(4) An agreement under subsection (3) may be either expressed or inferred as a fact from the course of dealing between the creditors and the firm as newly constituted.

Section 28

Subject to section 12 and subject to an agreement, express or implied, between the partners, the interest of partners in the partnership property and their rights and duties in relation to the partnership shall be determined by the following rules:

(a) all the partners are entitled to share equally in the capital and profits of the business and shall contribute equally toward the losses, whether of capital or otherwise, sustained by the firm, but a partner is not individually liable to contribute to losses arising from a liability for which the partner is not liable under section 12;

(b) the firm shall indemnify each partner in respect of payments made and personal liabilities incurred by the partner

  (i) in the ordinary and proper conduct of the business of the firm, or

  (ii) in or about anything necessarily done for the preservation of the business or property of the firm,

  but a partner is not required to indemnify or make contributions to other partners in respect of debts or obligations of the partnership for which the partner is not liable under section 12

(c) a partner who makes for the purpose of the partnership a payment or advance beyond the amount of capital that the partner has agreed to subscribe is entitled to interest from the date of the payment or advance;

(d) a partner is not entitled before the ascertainment of profits to interest on the capital subscribed by the partner;

(e) each partner may take part in the management of the partnership business;

(f) no partner is entitled to remuneration for acting in the partnership business;

(g) no person may be introduced into the firm as a partner without the consent of all existing partners;

(h) a difference arising as to ordinary matters connected with the partnership business may be decided by a majority of the partners;

(i) no change may be made in the nature of the partnership business without the consent of all existing partners;

(j) the partnership books are to be kept at the place of business of the partnership, or the principal place of business if there is more than one, and each partner may have access to and inspect and copy any of the books.

Section 34

If a partner without the consent of the other partners carries on a business of the same nature as and competing with that of the firm, the partner shall account for and pay over to the firm the profits made by the partner in that business.

Section 35

(1) An assignment by a partner of the partner's share in the partnership, either absolute or by way of mortgage, encumbrance or redeemable charge, does not as against the other partners entitle the assignee during the continuance of the partnership
    (a) to interfere in the management or administration of the partnership business or affairs

Section 36
(1) Subject to an agreement between the partners, a partnership is dissolved
    (a) if entered into for a fixed term, by the expiration of that term,
    (b) if entered into for a single adventure or undertaking, by the termination of that adventure or undertaking, or
    (c) if entered into for an undefined time, by a partner giving notice to the other partner or partners of that partner's intention to dissolve the partnership.
(2) In the case mentioned in subsection (1)(c), the partnership is dissolved as from the date mentioned in the notice as the date of dissolution, or if no date is mentioned in the notice, then as from the date of communication of the notice.

Section 37
(1) Subject to an agreement between the partners, a partnership is dissolved with regard to all the partners
    (a) by the death of a partner,
    (b) by the assignment of a partner's property in trust for the benefit of the partner's creditors, or
    (c) by the bankruptcy of a partner.
(2) A partnership may at the option of the other partners be dissolved if a partner permits the partner's share of the partnership property to be charged under this Act for the partner's separate debt.

Section 39
(1) On application by a partner, the Court may order a dissolution of the partnership in any of the following cases
    (a) when a partner is shown to the satisfaction of the Court to be of permanently unsound mind;
    (b) when a partner other than the partner suing becomes in any way, other than through permanent unsoundness of mind, permanently incapable of performing that partner's part of the partnership contract;
    (c) when a partner other than the partner suing has been guilty of conduct that in the opinion of the Court, regard being had to the nature of the business, is calculated to affect prejudicially the carrying on of the business;
    (d) when a partner other than the partner suing wilfully or persistently commits a breach of the partnership agreement or otherwise so behaves in matters relating to the partnership business that it is not reasonably practicable for the other partner or partners to carry on the business in partnership with that partner;
    (e) when the business of the partnership can only be carried on at a loss;
    (f) when circumstances have arisen that in the opinion of the Court render it just and equitable that the partnership be dissolved.

Section 105
The rules of equity and of common law applicable to partnership continue in force except where they are inconsistent with the express provisions of this Act

Section 106

Persons associated in partnership for trading, manufacturing, contracting or mining purposes in Alberta shall file with the Registrar a declaration in writing, signed by the several members of the partnership.

Section 115

(1) Until a new declaration is made and filed by a person, or by the person's partners, or any of them, the person who signed a declaration is deemed not to have ceased to be a partner.
(2) Nothing in this Act exempts from liability a person who, being a partner, fails to declare that fact, but that person may be sued jointly with the partners mentioned in the declaration, or they may be sued alone, and if judgment is recovered against them any other partner or partners may be sued jointly or severally in an action on the original cause of action on which judgment was rendered.
(3) Nothing in this Act affects the rights of partners with regard to each other, except that no declaration shall be controverted by a signatory to it.

Limited Liability Partnerships (LLP)

It is presumed that partnerships are ordinary partnerships, unless specified that they are an LLP or LP. So, in a fact pattern, it is prudent to do the full analysis as if they were a normal partnership, and then analyze how LLPs or LPs may come into play and what the would change

- Ordinary Partnerships are the baseline, with LLPs and LPs deviating from there.

LLPs are like ordinary partnerships in which partners benefit from a measure of limited liability in certain circumstances

- The benefit is that it provides flowthrough tax treatment like ordinary partnerships do, but it provides some liability limits as you would receive in a corporation.
- Only members of certain professions can carry on as LLP
  - These are dependant on the statutes that govern the profession (not the *Partnership Act*)
  - They are primarily available for professional services
    - Accounting, law firms are the most common
    - Professional services started lobbying that the risk of liability that arises in an ordinary partnership create unfair risks to other partners
      - LLPs are a legislative response to lobbying that went for law reform
- Section 12 modifies sections 11, 13, 14, 15 of the *Partnership Act* (all begin with "subject to s12")
  - Section 11: jointly liable for the debts of the firm
  - Section 15: jointly and severally liable for the liabilities of the firm from:
    - Section 13: wrongful act or omissions in ordinary course of action
    - Section 14: misapplication of money by partner in the scope of their authority
  - Section 12 does not negate liability, it just shields other partners if they were uninvolved in the wrongdoing
    - So, there is still some risk about partnership liability, but personal liability is shielded
- Section 12(1) shields personal liability for innocent parties
  - If a firm is LLP, uninvolved partners will not incur any personal liability for another partner's negligence/wrongful act/malpractice that might occur in the ordinary course
    - If s12(1) applies, a partner's liability is limited to their share or interest in the partnerships assets, and no liability for negligent/malignant conduct of another partner
    - Partners will always be liable for the management of the firm, but the negligent or wrongful partner will be liable for everything

    - This *only* applies when the wrongful act occurs in the *ordinary* course of action in an eligible profession
    - This shield is further limited by s12(2). If the partner had knowledge *or* supervised the employee who did the wrongful/negligent act, they are not shielded if they did not take reasonable steps or provide adequate and competent supervision
        - If they did not know = shield
        - If they knew and took reasonable steps to avoid = shield
        - Partner was directly responsible for supervision employee *and* they failed to make adequate supervision to benefit from the shield
            - Both have to be proven
        - Section 12 is meant to shield innocent or uninvolved partners
            - You are not innocent if you knew and did nothing
    - Section 12 won't applied unless it is in the ordinary course of business or an eligible profession. So, LLPs don't shield as much as they sound like
- Interestingly, section 12 applies in the conduct in the ordinary course of action of the profession, not the practice of that firm. This is the opposite of the *McDonic* finding
    - So in *McDonic*, if it was an LLP, the partners would have been shielded from personal liability because investment was not the ordinary course of action of law firms
        - Whether the partners took steps to avoid is pretty obsolete
- The shield is not available if the act/omissions did not occur in the ordinary course of carrying on a practice in an eligible profession as defined under s81
- Partners of an LLP remain personally liable for the ordinary contractual obligations of the firm under section 11 and the partner who is negligent/wrongdoer does not get the benefit of the section 12 shield.
- There are a lot of formal registration requirements between ss 81-104 that have more layers:
    - Apply to the Registrar of Corporations to be registered as an Alberta LLP or an extra-provincial LLP pursuant to ss82 or 94
        - Must first be able to register as a corporation
        - But then must also check the statute to see if LLPs are ever prohibited
    - The name of the partnership must include "LLP" in the name (or "limited liability partnership")
    - Can transition from ordinary partnership to LLP without dissolution, but must notify all clients of the change (ss 84-85)
- Basically, LLPs provide some liability protection of a corporation with the tax treatment of an ordinary partnership.

Partnership Act, RSA 2000, c P-3
Section 12 (1) Subject to subsections (2) and (4), a partner in an Alberta LLP is not individually liable, directly or indirectly by means of indemnification, contribution, assessment or otherwise, for debts, obligations or liabilities of the partnership or another partner that arise from the negligence, wrongful acts or omissions, malpractice or misconduct of (a) another partner, or (b) an employee, agent or representative of the partnership that occur in the ordinary course of carrying on practice in an eligible profession within the meaning of section 81 while the partnership is an Alberta LLP. (2) Subsection (1) does not operate to protect a partner from liability

(a) where the partner knew of the negligence, wrongful act or omission, malpractice or misconduct at the time it was committed and failed to take reasonable steps to prevent its commission, or
(b) Where
(i) the negligence, wrongful act or omission, malpractice or misconduct was committed by an employee, agent or representative of the partnership for whom the partner was directly responsible in a supervisory role, and
(ii) the partner failed to provide such adequate and competent supervision as would normally be expected of a partner in those circumstances.
(3) A partner in an Alberta LLP is not a proper party to a proceeding by or against the partnership that claims relief in respect of negligence, wrongful acts or omissions, malpractice or misconduct referred to in subsection (1).
(4) The protection from liability given to a partner under subsection (1) shall not be construed as offering any protection from claims against that partner's interest in the partnership property

Section 81
In this Part, "eligible profession" means a profession or discipline that is regulated by an Act of Alberta that specifically authorizes members of the profession or discipline to carry on business through a corporation that has the words "Professional Corporation" or the abbreviation "P.C." as part of its name.

Section 82
(1) A partnership consisting of partners carrying on practice in one or more eligible professions may apply to the Registrar to be registered as an Alberta LLP.
(2) Subsection (1) does not apply where the governing body of any of the eligible professions in which the partners in the partnership carry on practice has passed a rule or bylaw prohibiting persons who carry on practice in the eligible profession from doing so in a limited liability partnership under this Act.

Section 84
Subject to any agreement between the partners, the registration of a partnership as an Alberta LLP does not cause the dissolution of the partnership, and the Alberta LLP continues as the same partnership that existed before the registration.

Section 85
On being registered as an Alberta LLP, a partnership shall forthwith send to all of its existing clients a notice that advises of the registration and explains in general terms the potential changes in liability of the partners that are a result of the registration.

Section 94
(1) A partnership that
(a) has the status of a limited liability partnership under the laws of a jurisdiction outside Alberta, and
(b) consists of partners that carry on practice, whether through a professional corporation or not, in one or more professions or disciplines that are eligible professions in Alberta,

may apply to the Registrar to be registered as an extra-provincial LLP.
(2) Subsection (1) does not apply where the governing body of any of the eligible professions in which the partners in the partnership carry on practice has passed a rule or bylaw prohibiting persons who carry on practice in the eligible profession from doing so in a limited liability partnership under this Act

Limited Partnerships (LP)

LPs are totally different. Unlike LLPs, they do not apply to specific professions. LPs are defined by a general structure of some ordinary partnerships and some LPs: section 51 says they need one or more people as general partners, and one or more as limited partners

- LPs are sort of like shareholders in a corporation. All they stand to lose is their share – their liability is limited to their investment in the venture
    - But, where an LP engages in control of management or affairs of the business, they lose status of an LP, and open themselves up to liability the same as ordinary partnerships.
- Governed by sections 49-80.1 of the *Partnership Act*
- There are specific steps to form an LP: filing certificate with the registrar (s52)
- General partners (s56) are subject to all liabilities of a partner in an ordinary partnership
- Limited partners (s57) are not liable for the obligations of the LP except for property they contribute or agree to contribute to the partnership.
    - But, if an LP takes control of the business, they lose their LP status (s64)

Partnership Act, RSA 2000, c P-3
Section 51 (1) A limited partnership may, subject to this Part, be formed to carry on any business that a partnership without limited partners may carry on. (2) A limited partnership shall consist of (a) one or more persons who are general partners, and (b) one or more persons who are limited partners. (3) There may be any number of limited partners in a limited partnership. (4) Persons comprising a firm may enter into a limited partnership with other persons, including persons comprising one or more other firms. Section 52 (1) Subject to subsection (2), a limited partnership is formed when a certificate substantially complying with subsection (3) is filed with and recorded by the Registrar. Section 56 A general partner in a limited partnership has all the rights and powers and is subject to all the restrictions and liabilities of a partner in a partnership without limited partners except that, without the written consent to or ratification of the specific act by all the limited partners, a general partner has no authority to (a) do any act in contravention of the partnership agreement, (b) do any act that makes it impossible to carry on the ordinary business of the limited partnership, (c) consent to a judgment against the limited partnership, (d) possess limited partnership property, or assign any rights in specific partnership property, for other than a partnership purpose, (e) admit a person as a general partner, (f) admit a person as a limited partner, unless the right to do so is given in the partnership agreement, or (g) continue the business of the limited partnership on the death, retirement or mental incompetence of a general partner, unless the right to do so is given in the partnership agreement. Section 57

Subject to this Part, a limited partner is not liable for the obligations of the limited partnership except in respect of the amount of property the limited partner contributes or agrees to contribute to the capital of the limited partnership.

Section 64
A limited partner does not become liable as a general partner unless, in addition to exercising the limited partner's rights and powers as a limited partner, the limited partner takes part in the control of the business.

<u>Corporations</u>
There are three types of Corporations. This course focuses almost entirely on corporations.

1. Business Corporations
    a. governed by the *Alberta Business Corporations Act* ("ABCA") and the *Canada Business Corporations Act* ("CBCA")
2. Professional Corporations
    a. governed by the *Alberta Business Corporations Act* and relevant statutes which regulate certain professions (like the *Legal Professions Act*)
    b. Lawyers can operate their practice through a Professional Corporation
    c. Section 133(2) of the *LPA*: even if a professional corporation, the lawyer is still personally liability
        i. Lawyers will often still do a PC for tax reasons
        ii. All billings for the clients should be held by the corporation and not as a lawyer
3. Unlimited Liability Corporations
    a. governed by the *Alberta Business Corporations Act*
    b. Don't need to know for this course

1. Creation & Formal Requirements
    a. Articles of Incorporation (AoI) are needed for corporations. They must be in a prescribed form, and submitted to the Registrar of Corporations
        i. This is required by sections 5 and 7 of the *ABCA*
    b. Under section 6, AoI's need:
        i. name of corporation
        ii. classes and maximum number of shares corporation is authorized to issue
        iii. rights attaching to each class of shares
        iv. restrictions on transfers of shares
        v. the number of directors
        vi. restrictions on the business that the corporation may carry on
    c. Submission of articles must also include a NUANS search, notice of directors, and notice of address
        i. NUANS search runs a search on that specific name because no two corporations can have the same number
    d. A certificate of incorporation is issued by the appropriate government official (Registrar of Corporations under s8)
        i. The corporation comes into existence on the date shown on the certificate of incorporation, as per s9
    e. Ongoing reporting requirements are also needed
        i. Annual returns, preparing financial statements, filing corporate tax returns, notifications of changes of directors or their addresses
2. Liability

a. The corporation has a separate legal personality.
    i. This means that the corporation receives different obligations and benefits separate of its constituting directors or shareholders.
    ii. This also means they have different liability: if the corporation does something unlawful, only the corporation will be liable
        i. There are various exceptions to this rule
b. This means that shareholders have limited liability with respect to business activities of the corporations, with some exceptions
    i. Shareholders sign a personal guarantee for the corporation's debt
    ii. Shareholder has contracted personally without giving adequate notice to third party that they are acting as agent of the corporation
    iii. Loss occurs as a result of a shareholders personal act/negligence
        i. If you sign a lease or contract before the corporation is incorporated, there is a personal liability with that
    iv. Shareholder assumes the powers of a director under a unanimous shareholders agreement ("USA"), under section 146
        i. If a shareholder signs a USA, they are held to the same liability as the director is
    v. Court lifts of pierces the corporate veil
    vi. All of these will be covered later on
c. Directors, as managers of the corporation's business, do have exposure to some liability arising from the corporation's obligations under s119 of the *ABCA*

3. Control
    a. Shareholders elect the board of directors by exercising their voting rights.
    b. The Board of Directors then manage the affairs of a corporation (including hiring other executives, like CFO, CEO, COO, CLO)
    c. The AoI may specify that different voting rights attach to different classes of shares
        i. Different degrees of control to different degrees of shares
    d. Can accommodate many owners
        i. Doesn't become as unwieldly as a partnership with a lot of partners
4. Participation and Profits
    a. Very generally, rights of shareholders to profits and assets are determined by the AoI and the *ABCA*
        i. The statute has a default setting, the AoI can qualify the rights that are more flexible.
        ii. If the AoI exist, they are paramount to the statute
    b. Shareholders have a right to profits of corporation in the form of dividends declared and the residual net assets of the corporation on dissolution after creditors and bondholders have been paid
        i. Bondholders and creditors get first cut, then shareholders
5. Dissolution
    a. There is the possibility of perpetual existence of a corporation
    b. The corporation survives the death of shareholders
    c. Partnerships and proprietorships will end when the partner/proprietor dies
6. Tax Implications
    a. Since corporations are a separate legal entity, the corporation is taxed separately
    b. Taxed at the level of the corporate entity – requires separate tax returns for the corporation to be prepared
    c. Distributions from the corporation (dividends) are taxed again in the hands of shareholders

        i. No flowthrough treatment: taxed at the corporate level and then again at the shareholder level
    d. Canadian-controlled private corporations ("CCPCs") benefit from special tax treatments.
        i. They are controlled by citizens, built to promote business

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 5 One or more persons may incorporate a corporation by signing articles of incorporation and complying with section 7. Section 7 (1) An incorporator shall send to the Registrar (a) articles of incorporation, and (b) the documents required by sections 12(3), 20 and 106. (2) If the name of the corporation set out in the articles of incorporation contains the words "Professional Corporation", the incorporator shall also send to the Registrar evidence satisfactory to the Registrar of an approval of the articles that is less than 2 years old by or on behalf of the governing body of the appropriate profession or occupation. Section 8 On receipt of the documents and evidence required under section 7 and the prescribed fees, the Registrar shall issue a certificate of incorporation in accordance with section 267. Section 9 (1) A corporation comes into existence on the date shown in the certificate of incorporation. (2) A certificate of incorporation is conclusive proof for the purposes of this Act and for all other purposes (a) that the provisions of this Act in respect of incorporation and all requirements precedent and incidental to incorporation have been complied with, and (b) that the corporation has been incorporated under this Act as of the date shown in the certificate of incorporation.

A lot of corporate work is legal risk management. When choosing the form of a business vehicle, various things need to be considered:

- Nature of the business and associated risks
- Tax implications
- Formalities and cost of set-up and administration
    - This is more important for smaller ventures
- Degree of control
    - If the person wants to keep business in the family
- Who participates in the profits?
- Flexibility
    - Corporations are more flexible. For partnerships to be flexible, costs go up
- Transferability
    - If a family business, you may want it to be untransferable
    - Corporations have no restrictions on the transfer of shares
- Dissolution

Also important to keep in mind that there is a distinction between the legal form of the business organization/vehicle vs the arrangements pursuant to which business activities are carried out by two or more business organizations

- All vehicles can have arrangements, but these are separate
- Examples of business arrangements:
    - Franchise (between franchisor and franchisee)
        - Usually around a distinct product/service, but almost always under a tradename
        - McDonalds; a franchisee will benefit from the name of their restaurant being McDonalds
        - No separate statutes for these – purely contractual
            - Can be regulated by statute, but governed by contract
    - Joint Venture
    - Distributorship/Dealership
    - Sales Agency
    - Licensing
        - Holder of license gives right to someone else to sell those products in another jurisdiction

CHAPTER 2: BACKGROUDNER TO CORPORATIONS

Corporation as a Separate Legal Entity

The Alberta *Business Corporations Act* ("ABCA") and the *Canada Business Corporations Act* ("CBCA") are the very important legislations for corporate law. They provide a default stage for the common law to work around. They have also both been used to amend the common law as required.

The landmark case, for which is the starting point of basically every corporate law issue, is the *Salomon* case. It is the case that creates the principle that corporations and the people within it are separate legal entities in Canada. It stands that corporations can enter into debt/credit relationships with their shareholders, as if the corporation was a separate person.

Salomon v Salomon & Co Ltd, [1897] AC 22 (HL)

Facts:

Mr. Salomon (plaintiff) carried on a very successful boot/shoe manufacturing business. Though it started as a sole proprietorship, he later incorporated it to make Salomon & Co. Ltd ("Salomon Ltd"; defendant). Under the *Companies Act, 1862*, there is a requirement of 7 shareholders in order for the company to be officially a corporation.

- Shares were issued to different members of Mr. Salomon's family, giving one to each of his five children, 20,000 shares to himself, one share to his wife.
- Mr. Salomon maintained the complete authority to manage the affairs of the company

Mr. Salomon made an agreement with Salomon Ltd where the company will purchase the assets of the sole proprietorship. The company purchased it for $39,000 (20,000 shares at $1/share and a floating charge debenture of $10,000)

- The industry then nosedived and Salomon Ltd was struggling financially
- To avoid financial harm, Mr. and Mrs. Salomon lent Salomon Ltd money
    - He got his debentures cancelled and reissued to Mr. Broderip. Mr. Broderip advanced him $5,000 for the cancellation.
    - Mr. Salomon immediately gave the $5,000 to his company.

The company missed a payment/defaulted a debenture, so Mr. Broderip forced receivership to force the sale of corporate assets. The liquidator of the company filed various claims:

- On Mr. Broderip for the debenture

- On Mr. Salomon for the remainder of the debenture after Mr. Broderip was paid out
- On unsecured creditors for the remainder.

The forced sale of the company's assets had enough to cover Mr. Broderip's debenture, but not enough to pay off Mr. Salomon's. This meant the unsecured creditors were completely left out in the cold.

- The unsecured creditors saying the debentures were not legitimate so Broderip and Salomon should not be prioritised. The liquidator then brought a counter claim against Mr. Salomon personally, on the grounds that the debentures were fraudulent

Procedural History:
Trial judge found the company was just a fiction for Mr. Salomon's actions and found him liable

Issue:
Is Mr. Salomon a personally liable for the debts of Salomon Ltd? Is Mr. Salomon a genuine creditor?

Analysis:

Argument 1: Company was fiction, by which Mr. Salomon continued individual business

The argument was raised that nothing actually changed, the family members don't have a real interest and Mr. Salomon had as much power as he did with the sole proprietorship.

- The Act required seven members, all with a mind of their own, not mere puppets of the person under the solo proprietorship. But, the Act makes no requirement to the participation of the members – one share is enough. The Legislature could have limited shareholders to those independent and interested.
- There is no way that the member loses individuality just because the bulk of the capital is in one person.
- The company is, at law, a different person altogether from the constituting parties.
  - Even if the corporation is basically the same after incorporation, the company is not in law the agent of the managers.
  - The managers and members are not liable, other than the extent in the Act.
- Even if the company was only formed to allow Salomon to carry on the business as a corporation, this is not contrary to the *Act*. The whole point of incorporating in the *Act* is to give legal existence to a company with rights and liabilities of its own, whatever the scheme of the person running the company does.
  - He complied with strict requirements, and should thus be immune.

Even if members had to be *bona fide* members, where do we draw the line? Do all 7 people need to be actively participating every day? Is a meeting once a year enough? An 'interest' requirement is unworkable, uncertain and contrary to business efficacy.

Argument 2: Company acted as an agent for Mr. Salomon

They also raised the argument that the company was just acting as an agent on behalf of Mr. Salomon as a principal – meaning they entered into a contract with Mr. Salomon and he was bound (agents have authority to enter into legal relations with the principal).
However, either the limited company was a legal entity, or it was not.

- If it was, the company entered into contracts in it's own right
- If it was not, there was no thing to be an agent to at all
- It is not possible to say that there is a company, and Mr. Salomon was an agent for it at the same time, because that would require there to be a company, and to not be a company.

Argument 3: Shareholders and creditors of the company were defrauded

When all the shareholders are perfectly cognisant of the conditions under which the company is formed and the conditions of the purchase, it cannot be that they were defrauded. The shareholders knew in incorporation why Mr. Salomon was giving them shares and that he is controlling the company. They were fully informed on what was happening and the conditions, as well as the assets and rights of Salomon.

- There is thus no merit to the argument that the shareholders were defrauded.

The same can be said for the creditors: the memorandum of association gave notice that the main object for which the company was formed was to adopt and carry into affect the modifications of the debenture agreement and were given to Mr. Broderip for the part payment. This is allowed in their articles of association.

- The purposes and powers of the company were public: it was on the creditor to look up the credibleness of the account they were dealing with.
- They could have looked up what they needed to know, and the creditors apathy is no reason to assert fraud. The court won't make up for their mistakes in making the assessment of the credit worthiness.
- The law does not lay an obligation to warn members of the public who deal with them on credit that they run the risk of not being paid.
  - Any member of the company is as entitled to hold debentures as any outside creditor, and all creditors are all entitled to the security of the law
    - This includes Mr. Salomon

This is the whole purpose of the corporation being a separate legal entity

Conclusion:

Mr. Salomon is a genuine creditor and not personally liable.

Hold, Order:

Appeal allowed; no personal liability to Mr. Salomon

Ratio:

The corporation is a separate legal entity, meaning its officers and directors are not personally liable to creditors in the absence of fraud; lending money to your company is not fraudulent. Creditors have the choice on if they want to supply money or not, and must educate themselves with the agreement setup of the corporation.

- The terms laid on debenture deals are open to the parties setting them up, so long as they comply with appropriate legislation.
  - Purpose is to limit liability, and this is a valid reason to incorporate.

Mr. Salomon incorporated the company so he could bring the family in and provide limited liability, as allowed by the Act. When Salomon Ltd bought the assets, that's all they buy (ie, they don't buy the liability).

- Debentures are basically a debt (or an evidence of debt) and can be secured by certain assets
  - Fixed Debentures: loan is secured over a specifically tied property (this exact machine)
  - Floating Debentures: secures debt over a category of assets (inventory of the company, which fluctuates over time)
- By issuing a debenture to himself, Salomon became a secured creditor, so the company owed him money. The debt was secured on the floating assets, so if the company goes into liquidation, he has priority over unsecured creditors on liquidation.
  - Floating debentures provide security over assets of the company, so he is not only a creditor, but a secured one and thus has priority on liquidation.
  - Once the company pays the debenture off, it is gone and no debt exists anymore
- When Mr. and Mrs. Salomon cancelled the debenture and reissued it to Mr. Broderip (who advanced him $5,000 for cancellation), Mr. Broderip became the secured creditor who gets priority in the case of liquidation.
  - In liquidation, there was not enough assets to pay Broderip, Salomon and all unsecured creditors, only Broderip (all of his money owed) and a small portion to Salomon, with nothing to the unsecured creditors (they are out of luck)

- When the unsecured creditors argued that debentures were fraudulent, they are saying the debt is meaningless and they are going after Salomon personally to collect on their unsecured debt.

This case presents a lot of complicated facts and analysis, but the general takeaway is relatively simple: the corporation is a separate legal entity and the directors and officers will not be personally liable to the debts by creditors (absent fraud). This has been known as 'the corporate veil' where the individuals in the corporation are (ostensibly) insulated from liability because the corporation is itself a legal entity with the obligations.

The idea of the corporation as a separate legal entity is codified in Alberta statutes:

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 16 (1) A corporation has the capacity and, subject to this Act, the rights, powers and privileges of a natural person. Section 46 (1) The shareholders of a corporation are not, as shareholders, liable for any liability, act or default of the corporation except under section 38(4), 118(5)/(6), 146(7) or 227(4) or Part 2.1.

<u>Corporate Constitution</u>

Every company has a certain basic charter documentation that constitutes it's fundamental terms of the corporation concerned. Things within the documentation are how it exercises power and carries on business and organizes affairs. The company must stay within the bounds traced out by that constitution. The nature of the documents are dependent on the statute under which the company is incorporated.

- Could be form of letters patent, a special Act, articles of incorporation or a memorandum of incorporation.

All companies have stakeholders within the corporation: shareholders, creditors and officers. What power is allocated to each of them depends on the Constitution, and what it lays out for responsibilities of each. If there is a conflict between them, this should also be set out

- There may be some mention of how employees are treated, though this is more under labour and employment law
- Technically, there are more that three stakeholders in a corporation, since there are also employees, but this course focuses on these three.

In Alberta, the corporate constitution is comprised of:

1. Articles of Incorporation
    a. Name of corporation, classes of shares, restrictions on share transfers, number of directors, restrictions of business, names of people with signing authority
    b. Model used in most of provinces and in the *CBCA* for federal corporations
2. Bylaws
    a. Rules directed at internal maintenance of a corporation
    b. Not a requirement to have bylaws, but they are often done for efficiency sake
    c. Not filed with the Registrar – this is an internal document.
3. Unanimous Shareholder Agreement ("USA")
    a. Contracts, but are statutory since they are regulated by s146 of the *ABCA*

    b. The *ABCA* gives the contract particular significance for the constitution of the corporation, and is a means by which stakeholders can take for themselves managers that the directors would have.
        i. The Supreme Court has found that the USA has to be found in the constitution as it regulates the powers of the parties in a corporation.
4. Directors statements and common law elements (not discussed)

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 146 (1) A unanimous shareholder agreement may provide for any or all of the following: (a) the regulation of the rights and liabilities of the shareholders, as shareholders, among themselves or between themselves and any other party to the agreement; (b) the regulation of the election of directors; (c) the management of the business and affairs of the corporation, including the restriction or abrogation, in whole or in part, of the powers of the directors; (d) any other matter that may be contained in a unanimous shareholder agreement pursuant to any other provision of this Act.

Shareholders have rights associated with voting, any dividends declared, and net assets upon dissolution. The agreement will state who has these powers.
- Shareholders have limited liability and have indirect control of the corporation by electing the Board of Directors.
- The Board of Directors main function is to appoint officers (CEO, COO, CFO) who will make corporate policy and manage the affairs of the corporation and have a fiduciary duty to the corporation. Importantly, this duty is to the corporation, not the shareholders.

Officers (directors, managers, supervisors) are put in place by the Board, as well as evaluated by the Board, and the officers must report to the Board.
- Directors have a general oversight of the CEO; the CEO is often on the Board.

Corporate constitutions enumerate and govern the rights and obligations of shareholders. There are different methods of creating corporate constitutions:
- Special Acts of Incorporation
    - Used by federal and provincial governments (via statutes) to see what rights, powers or obligations the corporation has
    - The Constitution of the corporation is set out in the act
        - For example, Crown Corporations
    - Set out the purposes of the corporation, and the doctrine of *ultra vires* such that acts outside the scope cannot be done by the corporation
- General Acts of Incorporation
    - Generic for the purpose of the corporation (nature of the business does not matter)
        - Letters Patent: only in Prince Edwards Island
        - Memorandum of Association: Nova Scotia and British Columbia
        - Articles of Incorporation: Ontario, Quebec, Alberta, Saskatchewan, Manitoba, Newfoundland, New Brunswick
    - There are formal requirements for incorporation, and articles need to be filed with the appropriate Government Body.
        - In Alberta, this is the Registrar of Corporations

- They will give a certificate, the date of which is the moment the corporation came into existence

Canadian Jorex Ltd v 477749 Alberta Ltd, 1991 ABCA 330

Facts:

The Directors of Jorex (defendant, appellant) called a special meeting for Dec 10, but then cancel the special meeting by notice on Nov 27.

- Minority shareholders (plaintiff, respondent) would lose the right to examine the auditor of the corporation if the meeting is cancelled
- So, they applied for an order declaring the notice of cancellation was of no force and effect

Procedural History:

Trial judge found the Directors did not have the power to cancel the meeting

Issue:

Do the directors of the corporation have the power to cancel a special meeting called by them in advance of its advanced date?

Rule:

Section 101 of the (AB) *Business Corporations Act*

(1) Subject to any unanimous shareholder agreement, the directors shall manage or supervise the management of the business and affairs of a corporation.

Section 142

(1) The directors of a corporation

(a) May at any time call a special meeting of shareholders

Section 17

(1) It is not necessary for a bylaw to be passed in order to confer any particular power on the corporation or its directors.

Analysis:

Parties arguments:

- Jorex argues that unless the bylaws or the unanimous shareholder agreements prohibit specific action, s101 of the *ABCA* gives the power to the directors to do various things, including cancel the meeting.
- The minority shareholders argue that the *ABCA* does not expressly grant the directors power to cancel the meeting, so they cannot do it.

Jorex's arguments are stronger for a variety of reasons:

1. Section 101 was designed to give powers to directors, not restrict it
    a. This is basic statutory interpretation; what is the point of a basket clause if you have to specify what they can do?
    b. Unless there is explicit prohibition of something by the *ABCA* or bylaws, residual powers include the right to do so
        i. Section 17(1) shows a bylaw is not needed to give powers to directors
        ii. There is no bylaw saying directors can't cancel meetings, so they can
    c. Read together, unless prohibited by bylaw or USA, provisions grant directors the power to cancel meetings under residual powers of s101(1)
2. The case used by the respondent's to support their case was a UK case, which is based off a different statute and incomparable to the current situation.
    a. In the UK, directors only have powers that were not delegated to them
        i. Shareholders have the power, Directors only get what is given to them
    b. In Canada, directors have statutory powers to do affairs of the bylaws/USA
        i. Directors have powers, subject to bylaw/USA modifications
    c. The starting point is completely different
3. Reductio rationale; to accept shareholder argument would lead to unreasonable results

4. The shareholders right to requisition a meeting under s142 would not be affected
    a. Sections 101(1) and 142 can be read together where directors residual power to cancel a meeting would not extend to the unilateral cancellation of any meeting properly convened on the shareholders' request
        i. The Directors called the meeting they cancelled; s142 irrelevant
    b. To use s142 like the shareholders argument, would render s101 useless
5. The shareholder right to examine the auditor (under s168 of the *ABCA*) would not be violated by the Board's residual power to cancel meetings
    a. Shareholders have various other avenues to pursue (ss142, 242,143, 132, 109, 146, 102(5))

Conclusion:

Directors have power from statutory residual management powers

Hold, Order:

Appeal allowed

Ratio:

Courts will read a corporate constitution, in line with statutes, to not limit Directors residual power provisions, unless contrary to bylaws or unanimous shareholder agreements.
- Power is limited by the constitution, not by common law (like in the UK)

This case strikes at the core of the corporation's constitution. The shareholders were arguing about jurisdiction: the directors could not do what they did.
- There was no argument that the corporation had the power, but improperly used it
- This also serves a precautionary tale to only use case law that is applicable to you
    - The shareholders lawyer, in essence, made an argument that was no help to them because it was not applicable.
- The corporate constitution will always be read in line with statutes and will only limit powers based on internal bylaws or USAs, rather than explicitly granting directors powers (but this default is based on statute)

CHAPTER 3: PROCESS OF INCORPORATION

<u>Procedures</u>

The procedures on incorporation get very technical and best learned through practice. Statutes cover most of this, but not all of it, so common law is still needed.
- Where to incorporate?
    - Nova Scotia, British Columbia and Alberta are the only provinces to have unlimited liability (usually for tax purposes)
    - Incorporate federally or provincially?
- Who may incorporate?
    - Section 5 of the *ABCA* or section 5 of the *CBCA*
        - As long as AoI and other provisions are followed, a group of people are allowed to incorporate.
            - Individuals can incorporate as long as they are not a minor, incompetent or bankrupt
- How to incorporate?
    - Incorporation, nowadays at least, is done online on the Corporate Registries System ("CORES").
    - In Alberta, section 7 of the *BCA* requires the incorporator to send all the Articles of Interpretation to the Registrar
        - Section 12(3) requires all documents relating to the corporate names to prescribe to the regulations, including a NUANS search

        - Section 20 requires notice of address (registered office, records office and an address for service to mail)
        - Section 106 also requires sending to the Registrar a notice of Directors
    - Section 6 requires specific information to be in the Articles of Incorporation:
        - Name of the corporation
        - Shares of the company and the rights and privileges that come with them
        - How shares are to be transferred
        - How many directors and the maximum and minimum are permitted
            - If a USA is inconsistent with the # of directors, USA prevails
        - Any other restrictions of the company
    - Section 8: Registrar is to issue a certificate of incorporation when it receipts documents
    - Section 9: corporation comes into existence on the date shown on the certificate

Directors Organizational Meeting

Under section 104 of the *ABCA,* it is a requirement that directors have a meeting after incorporation. However, what they talk about is up to them ("*shall* have a meeting; "at which the directors *may*…:"

- Make bylaws
    - If they make bylaws, the shareholders must approve them (s102(2))
    - Bylaws are part of the corporate constitution so this is important
    - The more efficient approach would thus be to only make bylaws that are different than those under the Act
- Adopt securities or corporate records
- Appoint officers
- Appoint an auditor
- Arrange for banking system
- Transact other businesses (pre-incorporation contracts)

This can occur by a director's resolution instead of a meeting if they don't want to meet in person.

Shareholders' Organizational Meeting

- Section 102(2): all bylaws adopted by the directors at the organizational meeting *must* be confirmed by shareholders
- Directors can be elected under s106(2)(3)
    - They can also set the amount of directors, add any, or remove.
    - However, there are statutory exceptions to who can be a director (cannot be a minor, someone bankrupt, a corporation or someone who is incompetent)
- Auditors can be elected by the shareholders by a simple majority under ss162-163
    - Most people would want an auditor to oversee financials of the company
    - A special resolution must be passed if they don't want an auditor
        - Special resolutions need 2/3rds majority

Under s21(1), a corporation has to prepare and maintain all records of the meetings. These must include the articles and bylaws (and any amendments), USAs (and any amendments), minutes of them, copies of all notices, securities register, financial statements and disclosures (under s120, so people are aware if there are any conflicts)

- Under s23, directors, shareholders and their legal agents/representatives and creditors and their legal agents/representatives are allowed to access the corporate records

Professional Ethics and Code of Conduct

The Code of Conduct 3-4.5 relate to joint retainers. Most corporate law legal issues revolve around representation

- Before someone can act on behalf of multiple parties to an agreement, they must obtain consent and inform them of the advantages and disadvantages of the joint retainer
    - They must assure that joint representations is in their client's best interest
        - To do so, the lawyer must be sure there is no dispute when there is a conflict or potential conflict and consider all relevant factors
    - Identify any potential conflicts of interest ("COIs")
        - These arise when clients are aligned in interest and there is dispute among them in fact, but the relationship or circumstances are such that there is a possibility of differences developing
        - Tell they potential COIs may arise in the future
        - This is particularly germane for USAs
            - E.g, several shareholders want to retain you to enter into an LSA
    - Informed consent to joint representation
        - If a lawyer finds joint representation is permissible, consent of the parties must be obtained and it will only be valid if the lawyer has provided disclosure of certain things:
            - Advantages/disadvantages of retaining one lawyer and retaining independent counsel for each party
            - The fact that no material information received in connection with the matter from one party can be treated as confidential as against other parties
            - If a dispute arises, the lawyer will cease acting altogether, unless all parties consent to the lawyer representing them
            - Any relationships or interest of the parties in connection with the matter
        - The lawyer has the onus in establishing that disclosure was provided and consent was granted. So, it is strongly advisable to document all communication between them and to obtain *written* confirmation.
            - This isn't technically required, but if there is a paper trail, it will resolve any disputes on the part of the lawyer

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 1 (1) In this Act, (x) "person" includes an individual, partnership, association, body corporate, trustee, executor, administrator or legal representative Section 5 (1) One or more persons may incorporate a corporation by signing articles of incorporation and complying with section 7. Section 6 (1) Subject to section 15.3, articles of incorporation shall be in the form required by the Registrar and shall set out, in respect of the proposed corporation, (a) the name of the corporation, (b) the classes and any maximum number of shares that the corporation is authorized to issue, and (i) if there are 2 or more classes of shares, the special rights, privileges, restrictions and conditions attaching to each class of shares, and (ii) if a class of shares may be issued in series, the authority given to the directors to fix the number of shares in, and to determine the designation of

each series, and the rights, privileges, restrictions and conditions attaching to the shares of each series,

(c) if the right to transfer shares of the corporation is to be restricted, a statement that the right to transfer shares is restricted and either
   (i) a statement of the nature of the restrictions, or
   (ii) a statement that the nature of the restrictions appears in a unanimous shareholder agreement,

(d) the number of directors or, subject to section 107(a), the minimum and maximum number of directors of the corporation, and

(e) any restrictions on the businesses that the corporation may carry on.

(2) The articles may set out any provision permitted by this Act or by law to be set out in the bylaws of the corporation.

(3) Subject to subsection (4), if the articles or a unanimous shareholder agreement require a greater number of votes of directors or shareholders than that required by the Act to effect any action, the provisions of the articles or of the unanimous shareholder agreement prevail.

Section 7

(1) An incorporator shall send to the Registrar
   (a) articles of incorporation, and
   (b) the documents required by sections 12(3), 20 and 106.

(2) If the name of the corporation set out in the articles of incorporation contains the words "Professional Corporation", the incorporator shall also send to the Registrar evidence satisfactory to the Registrar of an approval of the articles that is less than 2 years old by or on behalf of the governing body of the appropriate profession or occupation.

Section 8

On receipt of the documents and evidence required under section 7 and the prescribed fees, the Registrar shall issue a certificate of incorporation in accordance with section 267.

Section 9

(1) A corporation comes into existence on the date shown in the certificate of incorporation.

(2) A certificate of incorporation is conclusive proof for the purposes of this Act and for all other purposes
   (a) that the provisions of this Act in respect of incorporation and all requirements precedent and incidental to incorporation have been complied with, and
   (b) that the corporation has been incorporated under this Act as of the date shown in the certificate of incorporation.

Section 12

(3) There shall be sent to the Registrar documents relating to corporate names that are prescribed by the regulations.

Section 20

(1) A corporation shall at all times have a registered office within Alberta.

(2) A notice of
   (a) the registered office,
   (b) a separate records office, if any, and
   (c) the post office box designated as the address for service by mail, if any,

must be sent to the Registrar in the form required by the Registrar together with the articles of incorporation.

Section 21

(1) A corporation shall prepare and maintain at its records office records containing
  (a) the articles and the bylaws, all amendments to the articles and bylaws, a copy of any unanimous shareholder agreement and any amendment to a unanimous shareholder agreement,
  (b) minutes of meetings and resolutions of shareholders,
  (c) copies of all notices required by section 106 or 113,
  (d) a securities register complying with section 49,
  (e) copies of the financial statements, reports and information referred to in section 155(1), and
  (f) a register of disclosures made pursuant to section 120.

Section 23

(1) The directors and shareholders of a corporation, their agents and legal representatives may examine the records referred to in section 21(1) during the usual business hours of the corporation free of charge.

(2) A shareholder of a corporation is entitled on request and without charge to one copy of the articles and bylaws and of any unanimous shareholder agreement, and amendments to them.

(3) Creditors of a corporation and their agents and legal representatives may examine the records referred to in section 21(1)(a), (c) and (d), other than a unanimous shareholder agreement or an amendment to a unanimous shareholder agreement, during the usual business hours of the corporation on payment of a reasonable fee and may make copies of those records.

Section 102

(1) Unless the articles, bylaws or a unanimous shareholder agreement otherwise provide, the directors may, by resolution, make, amend or repeal any bylaws that regulate the business or affairs of the corporation.

(2) The directors shall submit a bylaw, or an amendment or a repeal of a bylaw, made under subsection (1) to the shareholders at the next meeting of shareholders, and the shareholders may, by ordinary resolution, confirm, reject or amend the bylaw, amendment or repeal.

Section 104

(1) After issue of the certificate of incorporation, a meeting of the directors of the corporation shall be held at which the directors may
  (i) make bylaws,
  (ii) adopt forms of security certificates and corporate records,
  (iii) authorize the issue of securities,
  (iv) appoint officers,
  (v) appoint an auditor to hold office until the first annual meeting of shareholders,
  (vi) make banking arrangements, and
  (vii) transact any other business.

Section 106

(1) At the time of sending articles of incorporation, the incorporators shall send to the Registrar a notice of directors in the form required by the Registrar.

(2) Each director named in the notice referred to in subsection (1) holds office from the issue of the certificate of incorporation until the first meeting of shareholders.

(3) Subject to subsection (9)(a) and section 107, shareholders of a corporation shall, by ordinary resolution at the first meeting of shareholders and at each succeeding annual meeting at which an election of directors is required, elect directors to hold office for a term expiring not later than the close of the next annual meeting of shareholders following the election.

Section 162

(1) Subject to section 163, shareholders of a corporation shall, by ordinary resolution, at the first annual meeting of shareholders and at each succeeding annual meeting, appoint an auditor to hold office until the close of the next annual meeting.

Section 163

(1) The shareholders of a corporation other than a reporting issuer may by special resolution resolve not to appoint an auditor.
(2) A special resolution under subsection (1) is valid only until the following annual meeting of shareholders.

Canada Business Corporations Act, RSC 1985, c C-44
Section 5 (1) One or more individuals or bodies corporate may incorporate a corporation by signing articles of incorporation and complying with section 7. (2) An individual may incorporate a corporation only if that individual (a) is not less than 18 years of age; (b) is not incapable; or (c) does not have the status of bankrupt

Corporate Names

When companies incorporate, they receive a numerical name designated by the Registrar (e.g. 123456 Alberta Inc.).

- Holding companies: Companies established for the sole purpose of holding shares, so they don't conduct any business.
    - For these companies, the numbered name is all they need.
- Shelf companies: companies made by law firms (typically) who do all the paperwork and incorporation to establish a corporation that can be quickly accessed once a client is ready to establish a corporation on a time sensitive basis. They are kind of like a back up company with all the work done, that can be used once needed
    - They also only usually need a number until they are ready to operate

Newly Upgraded Automatic Name Search ("NUANS")

- A corporate name search report is required by the federal and most provincial/territorial governments when granting new corporate names for use. The report lists similar existing corporate names and trademarks
    - They are used to determine the availability of a new proposed name. Ensuring that the new corporate names do not create confusion others is intended to protect Canadian businesses and consumers

Corporations that are actively engaged in business will usually have an alphabetic/word name. The true name must be reserved.

- To get a name, a NUANS search is needed. The NUANS report must be reported to CORES
    - If the name is available, the name will be reserved for 90 days
    - If the company wants it, they incorporate and submit the name and the Registrar will approve the name.
    - There are other naming specificity requirements in statute as well
        - If the Registrar refuses a name, the applicant can appeal that to the courts under s247(1)(b).
- S10(8): The corporation must set out the chosen name in legible characters in all contracts, invoices, negotiable instruments and orders for goods or services, issued or made by or on behalf of the corporation
- The statute states criteria for when a corporation has to use their corporation name. This is important because if they are not followed, the corporate veil can be pierced (more to come). There are also statutory causes of action if the name is "confusing or misleading"
    - But, even if the Registrar approves the name, there could be liability under the common law for "passing off" a name
    - A NUANS Search only looks for the identical name to the search, so a name that is very similar, but not identical, could be approved.
        - Common law and statutory liability could still arise despite Registrar approval

Various naming criteria under statute:

- Distinctiveness
    - Section 12 of the *ABCA*: cannot be prohibited by regulations, identical to an existing ABCA or CBCA name, or be too similar such that it's use would be "confusing or misleading"
    - Section 5 of the *Business Corporations Regulations* (a) and (b): a name is too similar if it would lead to an inference that it is associated or affiliated with another corporation or would lead someone to mistakenly believe they are dealing with another corporation
    - Section 6 of the Reg: a corporation cannot have a name that is too general or only describes the quality, function, or other characteristics of the goods/services in which the corporation deals or intends to deal.
- Legal Element
    - Section 10(1) of *ABCA*: the words limited, limitee, incorporated, incorporee, corporation, ltd, ltee, inc or corp shall be the last word of every corporation.
- Descriptive
    - While not strictly a legal requirement, a descriptive element needs to give an indication to the business practice carried on by the company
        - The risk of the name being misleading still rests on the shoulders of the person who creates a corporation, even if the Registrar approved it

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 10 (1) Subject to section 15.4(1), the word "Limited", "Limitée", "Incorporated", "Incorporée" or "Corporation" or the abbreviation "Ltd.", "Ltée", "Inc." or "Corp." shall be the last word of the name of every corporation, and a corporation may use and may be legally designated by either the full or the abbreviated form.

(8) A corporation shall set out its name in legible characters in or on all contracts, invoices, negotiable instruments, and orders for goods or services, issued or made by or on behalf of the corporation.

Section 12

(1) A corporation shall not have a name

- (a) that is prohibited by the regulations or contains a word or expression prohibited by the regulations,
- (b) subject to the circumstances and conditions prescribed by the regulations, that is identical to the name of
  - (i) a body corporate incorporated under the laws of Alberta, unless the body corporate has been dissolved for a period of 6 years or more,
  - (ii) an extra-provincial corporation registered in Alberta, or
  - (iii) a Canada corporation,
- (c) subject to the circumstances and conditions prescribed by the regulations, that is similar to the name of
  - (i) a body corporate incorporated under the laws of Alberta,
  - (ii) an extra-provincial corporation registered in Alberta, or
  - (iii) a Canada corporation,

  if the use of that name is confusing or misleading, or
- (d) that does not meet the requirements prescribed by the regulations.

(2) Where a body corporate incorporated under the laws of Alberta gives an undertaking to dissolve or change its name and the undertaking is not carried out within the time specified, the Registrar may, by notice in writing, giving the Registrar's reasons, direct the body corporate to change its name to one that the Registrar approves within 60 days after the date of the notice.

(3) There shall be sent to the Registrar documents relating to corporate names that are prescribed by the regulations.

Section 247

(1) A person who feels aggrieved by a decision of the Registrar

- (b) to approve, change or revoke a name or to refuse to approve, change or revoke a name under this Act

(Alberta) *Business Corporations Regulation*, Alta Reg 118/2000

Section 5

(1) A corporation and an extra-provincial corporation registered in Alberta may not have a name where the only difference from the name of a corporate person or of a dissolved body corporate is

- (a) the addition or deletion of punctuation marks or spaces,
- (b) the insertion or removal of a year in the name

Section 6

No corporation may have a name that

- (a) is too general,
- (b) is only descriptive, in any language, of the quality, function or other characteristics of the goods or services in which the corporation deals or intends to deal

Paws Pet Food and Accessories Ltd v Paws and Shop Inc, 136 AR 176 (QB)

Facts:

Paws Pet Food and Accessories ("PPFA", appellant) was formed in 1987 under the ABCA. In 1991, Paws and Shop Inc ("PS Inc"; respondent) was formed under the ABCA.

- Both operated in Calgary as retail pet stores (names were descriptive of their business)

PPFA applied to the Registrar to order PS Inc to change its corporate name by removing the name "Paws". This was made pursuant to s13 of the ABCA

- The Registrar refused, finding the names were not similar as set out by the *Regulation* requirements. They found the applicant did not established customers were confused or misled

PPFA then brought application to the court (under s247) for judicial order requiring the Registrar to reverse its decision.

Issue:

Should the application be granted on the argument that the respondent's corporate name is so similar that it would be "confusing or misleading", contravening s12 of the *Act*?

Rule:

Section 12 of the *Business Corporations Act*

(1) A corporation shall not have a name
    (a) Subject to the circumstances prescribed by the regulations that is similar to the name of
        (i) body corporate incorporate under the laws of Alberta
    if the use of the name is confusing or misleading

Section 13

(1) If, through inadvertence or otherwise, a corporation comes into existence with or acquires a name that contravenes section 10 or 12, the Registrar may, by notice in writing, giving the Registrar's reasons, direct the corporation to change its name to one that the Registrar approves within 60 days after the date of the notice.

Analysis:

The applicant has established and acquired the good will in its name, particular the word "Paws", with which the PPFA is identified in its logo and trademark with its goods.

- There is evidence that shows some customers believed the respondent was a second store of the Applicant, indicating that some were mislead or confused by the PS Inc name.
    - This leads to a reasonable inference that PS Inc is associated or affiliated with PPFA
- Accordingly, the respondent was in breach of s12(1)(c) because it was confusingly or misleadingly similar under the regulations (s4(4))

Conclusion:

PS Inc contravenes section 12

Hold, Order:

Application approved

Ratio:

If there is a reasonable opportunity that a member of the public could be misled, such that they believe the corporations are affiliated even if they are not, the name contravenes s12(1)(c)

This case illustrates that even if the Regsitrar approves the name through a NUANS, the court can find on the evidence that the names are too similar and order them to change.

- However, these are highly contextual and need evidence of confusion in the public eye

- Quite significant impacts to PS Inc as they would have to change all their manufacturing, marketing and advertising

Stenner v ScotiaMcLeod, 2009 BCSC 1093

Facts:

Stenner (plaintiff) is a financial consultant and investment advisor of NBF. His team was compromised of his daughter (Vanessa Stenner-Campbell), son in law (Raymond Campbell), former administrative assistant (Laura O'Connell). The team are the defendants

- The defendants were paid by NBF but also received bonuses and other renumerations from Stenner

Stenner did marketing research, radio shows and published client newsletters.

- Vanessa was responsible for providing investment advice to clients
- As part of his retirement plan, he sold his book of business to Vanessa, but before he could, there was a falling out and kept the book

The defendants then all moved to ScotiaMcLeod (a competitor) without notice.

- The plaintiff brough an action against the defendants on several grounds, including "passing off"
- He claimed the defendants passed themselves off as being associated with him after their professional relationship terminated.

Stenner had registered the name "stennerteam" in 2000. Vanessa used the name 'Stenner-Campbell' for business purposes

- She used Stenner-Campbell to represent herself and husband and the hyphenated name was used in advertising ever after they were told to desist by ScotiaMcLeod's compliance department
    - She then started her own radio at the same time as her father and employer the name 'Stenner' in the broadcasts

Stenner's application to use 'Stenner' as a trademark in 1998, giving him a *de facto* monopoly on the name. Stenner then brough action and claimed passing off in 2003

- Since her divorce, Vanessa only used 'Stenner' since 2006
- It was found the defendants were aware about the potential for confusion from the significant association in the financial world with the name 'Stenner' and they therefore appreciate a benefit derived from his name.

Issue:

Are the defendants liable for passing themselves off as being part of the plaintiff's business?

Rule:

There are three elements to prove passing off:

1. Existence of goodwill
2. Deception of the public due to the misrepresentation
3. Actual or potential damage to the plaintiff

Analysis:

The tort of passing off is the representation of the defendants' goods as being those of the plaintiff. One way to do so is to use the name which resembles the plaintiffs or creates the impression they are involved in the business of the plaintiff.

- Existence of Good Will
    - No doubt that the plaintiff has acquired a reputation and goodwill in his connection with financial services
    - Extensive use of name, publications and radio show
        - Evidenced by his successful application for trademark
        - Trademark requires goodwill in the first place
    - The defendants were certainly aware of this and that the name 'Stenner' brought advantage in their business name

- Deception of Public
  - Defendants represented in several, direct and implicit ways, there was a connection between them and the plaintiff
    - "Stenner/Campbell" implies there are two persons, one is Stenner
    - Letters sent to clients at NBF implied a link between Stenner Team ScotiaMcLeod
    - Receptionist answered the phone "Stenner Team"
  - Vanessa tried to argue that they had the same name and could not avoid that. However, that is not available since the defendant wasn't using her full name
- Actual or Potential damage to Stenner
  - Could be a loss of reputation in the name, or more concrete (profit removed from the plaintiff)
  - The effects of passing off diminishes over time
    - While passing off may have helped defendants acquire clients, the defendant creates business because of her own reputation and standing in the industry
  - It is true that the defendants benefited from the name, but it decreased over time. She had acquired her out clients

<u>Damages</u>

Given that Passing off is established, what damages?

- 10% of Defendants' gain up to trial, and apportionment of 10%-5% yearly for the further five years after
  - $1,000,000 for the plaintiff's loss of goodwill
- Permanent injunction from using the name 'stennerteam.ca'

Conclusion:

Passing off established; defendants liable

Hold, Order:

Application granted; damages and injunction ordered

Ratio:

Liability can exist beyond statutory provisions through the tort of passing off, even if both were incorporated with the Registrar

- Passing off diminished over time as the defendant acquires their own business.

The common law action of passing off is therefore possible, but it should be noted that the severity diminishes over time as the defendant gains their own business. The elements to goodwill are:

1. Existence of goodwill
2. Deception of the public due to the misrepresentation
3. Actual or potential damage to the plaintiff

The overall takeaways from incorporating are that corporations can accept a numeric one but also chose their alphabetic name. However, if they pick an alphabetic name, they are subject to certain statutory and common law criteria to not be similar to another corporation's name.

- The big requirements are a NUANS search and filing articles of incorporation
- Even if names are approved, other liability exists if too similar to another name
  - In a fact pattern, statutory liabilities should be discussed first, and common law second (like the tort of passing off)

<u>Unanimous Shareholder Agreements</u>

Corporate constitutions have bylaws, but also Unanimous Shareholder Agreements ("USA's"). The point of USAs is that closely held corporations should be guided by the interests of shareholders

- A USA is a tool that these closely held corporations govern the place similar to how partnerships do and organize the management as shareholders see fit.
    - In principle, these are possible for any corporation, but it is harder for wider held corporations, so USA's are needed for larger companies
- Before USAs were recognized by statute, there were only ordinary shareholder agreements and were governed by common law, like any other contract
- Now there are statutory requirements and guidelines for them.

USA's are governed by section 146 in both the *ABCA* and the *CBCA*.
- USA's under the ABCA are very broad. Under s146(1)(c), they can restrict powers of the directors. This could be a number of things:
    - Power of directors to manage, or supervise, the management of the business and affairs of the corporation (s101(1))
    - Power of directors to amend bylaws (s102(1))
    - Removal of any director from office (s109(1)).
- They can also establish methods of dispute resolution
    - Since Directors have the power to make bylaws, USAs are a way to vest powers in shareholders
- Common USA terms also include the right of first refusal ("ROFR"). If this is include, if a shareholder wants to sell their shares, they have to offer it to other shareholders first.
    - This way, the other shareholders get to refuse other sales and allow shareholders to limit the transfer of shares

As a whole, the *CBCA* is much narrower in terms of application to USA provisions.
- The *CBCA* is narrower: deals with any provision over the concerns of the powers of directors to manage the corporation
- The *ABCA* is more flexible: deals with any provision going to the internal affairs of a corporation

Comparing ordinary shareholder agreements vs USA's:
- USA is statutory and part of the constitution of the corporation
    - Can be enforced through two routes:
        - Seeking a compliance order under s248, or
        - Conventional claim for breach of contract
- It is difficult to amend a USA (section 146(8) of the *ABCA*). Amendments, by definition, require unanimous support by the shareholders
    - This is not the case for normal shareholder agreements
- Under a USA, shareholders incur all the liabilities of directors of the corporation to the extent that they have taken on the powers or duties of directors (section 146(7))

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 146 (1) A unanimous shareholder agreement may provide for any or all of the following: (a) the regulation of the rights and liabilities of the shareholders, as shareholders, among themselves or between themselves and any other party to the agreement; (b) the regulation of the election of directors; (c) the management of the business and affairs of the corporation, including the restriction or abrogation, in whole or in part, of the powers of the directors; (d) any other matter that may be contained in a unanimous shareholder agreement pursuant to any other provision of this Act.

(7) A shareholder who is a party or is deemed to be a party to a unanimous shareholder agreement has all the rights, powers and duties and incurs all the liabilities, subject to any defences available to a director of the corporation, of a director of the corporation to which the agreement relates to the extent that the agreement restricts the powers of the directors to manage the business and affairs of the corporation, and the directors are thereby relieved of their duties and liabilities, including any liabilities under section 119 or any other enactment, to the same extent.

(8) A unanimous shareholder agreement may not be amended without the written consent of all those who are shareholders at the effective date of the amendment.

Section 101

(3) Subject to any unanimous shareholder agreement, the directors shall manage or supervise the management of the business and affairs of a corporation.

Section 102

(1) Unless the articles, bylaws or a unanimous shareholder agreement otherwise provide, the directors may, by resolution, make, amend or repeal any bylaws that regulate the business or affairs of the corporation.

Section 109

(1) Subject to section 107(g) or a unanimous shareholder agreement, the shareholders of a corporation may by ordinary resolution at a special meeting remove any director or directors from office.

Section 248

If a corporation or any shareholder, director, officer, employee, agent, auditor, trustee, receiver, receiver-manager or liquidator of a corporation contravenes this Act, the regulations, the articles or bylaws or a unanimous shareholder agreement, a complainant or a creditor of the corporation may, in addition to any other right the complainant or creditor has, apply to the Court for an order directing that person to comply with, or restraining that person from contravening any of those things, and on the application the Court may so order and make any further order it thinks fit.

Canada Business Corporations Act, RSC 1985, c C-44

Section 146

(1) An otherwise lawful written agreement among all the shareholders of a corporation, or among all the shareholders and one or more persons who are not shareholders, that restricts, in whole or in part, the powers of the directors to manage, or supervise the management of, the business and affairs of the corporation is valid.

Cicco v 609940 Ontario Inc (Trustee of), (1985) 57 CBR (NS) 137 (Ont SC)

Facts:

609940 (“the Company”; defendant) carried on business as Five Star Auto, with Mr. Bertucci as the director and 50% shareholder, and Mr. Cicco (plaintiff) as other director and other 50% shareholder.

- Cicco and Bertucci enter into a USA. In the agreement, it says that decisions affecting the corporation shall be made only by consent of Cicco and Bertucci.

The two eventually have a falling out where Cicco resigns as director and Bertucci carries on business as the sole director.

- They enter into an agreement on how Cicco will leave. One term specifies that Bertucci will assume liabilities and assets of Cicco, who will be returned and receive indemnities
- Cicco has to transfer shares to Bertucci

Bertucci, without Cicco's consent, adopts a director's resolution to make an assignment in bankruptcy

- Cicco moves to annul Bertucci's assignment by basis that the USA requires Bertucci and Cicco to both consent to changes. Since Cicco did not, the assignment is void.
    - Cicco fulfilled his duties, but Bertucci did not fulfil his.

Issue:

Did Bertucci's directors resolution contravene the USA, thereby unauthorizing the resolution and assignment of bankruptcy? Can a USA negate the operation of the *Bankruptcy and Insolvency Act*?

Rule:

Section 151 of the *Bankruptcy Act*

(1) Where, in the opinion of the court, a receiving order ought not to have been made or an assignment ought not to have been filed, the court may by order annul the bankruptcy.

Analysis:

At the point of the assignment, Cicco was no longer a director, but was still a shareholder. The assignment of bankruptcy may be contrary to the USA and thereby contrary to the internal rules governing the corporation, in which case Cicco may bring a private action against Bertucci for breach of the USA.

- USA's bind the directors, but does it bind a third party dealing with a company who has no notice on the restrictive authority of its directors?
    - In the case of a trustee in bankruptcy, the answer is no.
- Test for annulment under s151 of the *Bankruptcy Act*: the court must conclude that the assignment ought not to have been made
    - Because the company was insolvent at the time of the assignment, the assignment was proper.
    - There was a deficiency of assets, creditors would go unpaid, which aligns with the assignment of bankruptcy.

The USA limited the authority of Bertucci, but the USA is entirely internal between directors and shareholders.

- If he fails to comply with the USA and statute, Bertucci can be accountable to other shareholders, but this will not render the assignment void
- The trustee is still entitled to rely on the assignment and supporting resolution
    - To accept Cicco's proposition would produce the effect that no trustee could safely act under a corporate assignment in bankruptcy without enquiring into the internal dealings of the directors
    - This could not have been the intention of the legislature.

As such, as sole director he could invoke the *Bankruptcy Act*, and the USA was the only thing preventing him from doing so. So, while he is liable for failing to follow the agreement (internal; between him and Cicco), his assignment (external; between company and trustee) is still valid

Conclusion:

Contravened USA, but did not invalidate assignment

Hold, Order:

Annulment application dismissed

Ratio:

Parties cannot, through a USA, encumber the operation of the *Bankruptcy and Insolvency Act*.

This case is actually quite limited in applicability since it is tailored to the facts. But, the court says that while Bertucci can be liable for violating the USA by not getting Cicco's consent before assignment for bankruptcy, the liability will not invalidate a separate agreement of bankruptcy with the trustee. Because all the requirements for bankruptcy under statute were satisfied (insolvent, inability to pay creditors, deficiency of assets), the assignment was perfectly fine.

- In other words, the USA cannot be used to push out statutory operation of bankruptcy. The failure to follow the USA did not outweigh the *Bankruptcy and Insolvency Act*
- If it were otherwise, the trustee would have to investigate into the internal functioning of the authority of the corporation, which is contrary to the aims of the statute

Share Capital

Share capital is beyond the scope of this course, but the elements are important building blocks for other concepts.

- Corporate share: a common, divided, participation interest in the corporation's business
  - Can be purchased from the corporation or from another shareholder
  - A new share of issuance is under securities legislation
  - A share in a corporation does not represent a proportionate share in the assets; it entitles to a proportionate share of the *net* assets after liabilities are removed.
    - This is what the corporate share gives you
- There is the presumption that shares of a corporation are equal in all respects, but this can be defeated by dividing shares into different 'classes'. Shares can belong to one class, and one only.
  - Where corporations have only one class of shares, the default rule is that the rights of holders are equal as to voting, dividends and remaining value of property on dissolution (ABCA s26(3))
  - It is common to see different classes with different rights/conditions attached to them
    - Articles of incorporation goes over all this
- Common/Equity Shares: shares that have full right of participation in the corporation through voting, including unrestricted rights in dividends and distributions of the value or remaining property upon dissolution
  - This is a riskier way to invest in a corporation than a debt holder (since debt holders have priority), but common share holders have potential for unlimited growth in profits or returns of those shares.
- Preferred Shares: special shares to which some special right is attached (voting, conversion rights) which makes it rank ahead of common shares in some ways (prior right to receive dividend, though usually at a fixed rate)
  - Get paid out before common shareholders
- Restricted Shares: special shares subject to limitations (non-voting)
  - Usually used to achieve a particular purpose (for example, they don't have voting access because you want to give those shares to foreign investors, but for specific reasons, you want to limit foreign control over those shares)
  - May have no right to dividends until after the common shareholders get their cut.

Pre-Incorporation Contracts

Directors will often adopt a pre-incorporation contract ("PIC") in their first meetings.

- Pre-incorporation contract: a contract entered into in the name of, on behalf of, or in trust for, a corporation that is not yet incorporated. Made between:
  - Promoter: the person who enters into the contract on behalf od the yet-to-be-incorporated corporation
  - Third Party: the counterparty to the contract (the company and the promoter are considered the first two parties)
- Parties will usually want to jump on a transaction before a corporation forms. If there is value in land or things they wish to purchase before incorporation, this becomes important.

    - In short order, they won't want personal liability for those contract. They purport to contract on behalf of a corporation that does not yet exist
- Obviously, the central issue thus becomes whether the promoter is liable under the contract

<u>Common Law Principles</u>

Common law has largely been displaced by statutes, but there are still areas where common law will apply

- The ABCA and CBCA only cover written contracts, not oral. So, if the PIC is oral, common law applies
- The ABCA and CBCA actually differ on the treatment of the PIC, so it is important to keep common law in mind.

At common law, there are two rules that govern PICs

1. The Promoter was personally liable for the contract
2. Once incorporated, the corporation could not ratify the contract and relieve the Promoter of personal liability under the contract.

These two are founded under three areas of common law principle:

1. Agency Law: agent contracting on behalf of non-existant principal is personally liable
2. Contract Law: contract can only be formed between two parties who were in existence at the time of formation
3. Corporate Law: creature of statute; only comes into existence on the date of incorporation (AoI acceptance).

Taking all three of these, the result is that the promoter has liability, and the rights/obligations under contract cannot be transferred to a corporation that did not exist at the time of incorporation.

- This had big impacts on corporate law and prompted a statutory response.

Two foundational principles:

- *Kelner v Baxter* (British case): under agency law, the Promoter has personal liability under the contract because he acted for a non-existent principal
    - The parties' intentions are irrelevant.
- *Black v Smallwood* (Australian case): interpreted *Kelner* as not necessarily imposing personal liability on promoters in all circumstances. Court directed us to look at the intentions of the parties: did they intend the Promoter to have personal liability?
    - Both parties mistakenly believed the corporation existed at formation of the contract, so the Court found neither had the intention of acquiring personal liability under it
    - This requires an interpretation of intentions (like in contract law)

Unfortunately, these two cases created a lot of uncertainty, and it was unclear how courts would respond to it. So, statutory responses ensued.

Section 14 of the *CBCA*

- 14(1) finds personal liability and entitlement of benefits of the Promoter
- 14(2) negates this liability if the corporation adopts the contract within a reasonable time after incorporation
- 14(4) allows the Promoter to contract out of personal liability
    - If the contract says the Promoter is not personally liable, in any case, they are not
        - Ie, the statute moves aside for the contract
    - However, if there is no mention of it, there is personal liability up until the corporation adopts the PIC (assuming it is within a reasonable time frame)

- From a business perspective, you would thus want to expressly include this in any PIC you are assigning, assuming you don't want personal liability

Canada Business Corporations Act, RSC 1985, c C-44
Section 14 (1) Subject to this section, a person who enters into, or purports to enter into, a written contract in the name of or on behalf of a corporation before it comes into existence is personally bound by the contract and is entitled to its benefits. (2) A corporation may, within a reasonable time after it comes into existence, by any action or conduct signifying its intention to be bound thereby, adopt a written contract made before it came into existence in its name or on its behalf, and on such adoption (a) the corporation is bound by the contract and is entitled to the benefits thereof as if the corporation had been in existence at the date of the contract and had been a party thereto; and (b) a person who purported to act in the name of or on behalf of the corporation ceases, except as provided in subsection (3), to be bound by or entitled to the benefits of the contract. (4) If expressly so provided in the written contract, a person who purported to act in the name of or on behalf of the corporation before it came into existence is not in any event bound by the contract or entitled to the benefits thereof.

Westcom Radio Group Ltd v MacIsaac, (1989) 70 OR 591 (ONCA)

Facts:

MacIsaac (defendant, promoter) contracts with Westcom Radio Corp (plaintiff, third party) on behalf of corporation *both* parties mistakenly believe to have existed

- MacIsaac signed the contracts as director and officer of the corporation and *not* in her personal capacity

Westcom was owed some money under the contract, so brought action against MacIsaac to get it.

Procedural History:

MacIsaac found not personally liable, Westcom application dismissed

Issue:

Is MacIsaac personally liable for the contractual obligations between Westcom and the non-existent corporation under s21 of the *OBCA*?

Rule:

Section 21 of the *Ontario Business Corporations Act*

(1) Except as provided in this section, a person who enters into an oral or written contract in the name of or on behalf of a corporation before it comes into existence, is personally bound by the contract and is entitled to the benefits thereof.

Analysis:

The starting point has to be to determine if the plaintiff intended to contract with the company (who did not exist) exclusively. Whether MacIsaac is personally liable under the OBCA will depend on the interpretation of the word 'contract' in s21(1).

- Taking the *Smallwood* logic, looking at the intentions of the parties, there was no intention of the promoter to have personal liability since both parties though the non-existent corporation existed (honest mistaken belief)

- But in applying the common law, there is a threshold question: was there a contract at all at common law? Was there a contract at all under s21(1) of the *OBCA*?

First, at common law, given the interpretation of the parties, there is no contract in existence for MacIsaac to be bound.

- Second, because there was no contract, s21(1) of the *OBCA* is not triggered
  - If it were, MacIsaac would be personally liable.

Conclusion:

MacIsaac not personally liable

Hold, Order:

Appeal dismissed

Ratio:

In order to trigger the use of statutory provisions relating to personal liability of PICs, it first must be determined whether a contract exists at all

- To find this requires analyzing the parties intentions and whether the Promoter intended to be personally bound.

Westcom is the leading case on the interpretation of statutory liability for PICs. The *OBCA* in this case is more similar to the *CBCA* and differs slightly from the *ABCA*

- While the statute was meant to displace the common law *Smallwood* (used) and *Kelner* (not used) logic, the Court here imposes the common law again by requiring the threshold question of asking whether a contract exists at common law. If it does not at common law, it cannot trigger the statute (which is exactly what they found here), calling it a failed attempt at contract
- So, the Court re-introduced the common law in interpreting the statute
  - The court even says the point of s21(1) is to avoid *Smallwood* rationale, but all the court can do is interpret the statute as it is written. Since it is only written to apply to real contracts, they need to use common law to determine what a real contract is.
  - In dissent, Estey called this ludicrous statutory interpretation that thwarts the legislative intent and imposes common law where the legislature wanted to avoid it.
    - Subsequent cases have eroded these findings.

Sherwood Design Services Inc v 872935 Ontario Ltd (1998) 39 OR 576 (ONCA)

Facts:

872935 ("the Company") is a shelf company at a law firm. Sherwood Design (plaintiff) entered into a contract with individual defendants of the Company for a $300,000 agreement to purchase Sherwood Design's assets "in trust for a corporation to be incorporated"

- Counsel for the individual defendants wrote to the counsel for the plaintiff stating:
  - "a corporation has been assigned from the law firm's shelf companies to complete the asset purchase"
  - They also included draft organizational documents and a draft, unsigned resolution of the directors adopting the pre-incorporation contract

The deal eventually fell through and the shelf company was returned to the shelf and assigned to another client at the firm.

- Sherwood then sued the individual defendants and the Company because it had the assets to answer any liability the earlier transaction may have attracted.

Issue:

Did the Company adopt a pre-incorporation contract within the meaning of s21(2)?

Rule:

Section 21 of the *Ontario Business Corporations Act*

(1) A corporation may, within a reasonable time after it comes into existence, by any action or conduct signifying its intention to be bound thereby, adopt an oral or written contract made before it came into existence in its name or on its behalf, and upon such adoption,
   (a) the corporation is bound by the contract and is entitled to the benefits thereof as if the corporation had been in existence at the date of the contract and had been a party thereto; and
   (b) a person who purported to act in the name of or on behalf of the corporation ceases, except as provided in subsection (3), to be bound by or entitled to the benefits of the contract.

Analysis:

To answer the question, one must ask if the conduct of the defendant counsel amounted to an adoption of the contract under the *Act* such that the Company became bound. In this case, the transaction went through, the corporation was incorporated, but the PIC was not adopted yet to the corporation.

- After the deal fell through, all that is left was a draft/unsigned document

Because s21(2) does not set out how a PIC can be adopted (no "manner of adoption"), there is no principled basis for imposing a stringent requirement of formality

- Actions of counsel, as agent for the Company, and on the instructions of the individual defendants, was sufficient evidence of an intention of the corporation to be bound by the agreement.
- So, the corporate defendant is now liable under the contract, notwithstanding the shelf company being assigned to another firm.

Conclusion:

Pre-incorporation contract adopted; no personal liability for individual defendants.

Hold, Order:

Appeal allowed; only corporate liability

Ratio:

Absent explicit instructions in the statute on pre-incorporation contract adoption, conduct can be used to "adopt" a pre-incorporation contract

- Assess whether the parties intended the corporation to be liable.

Notice that s21(2) is very similar to s14 of the *CBCA*, so this case is highly applicable for corporations incorporated under the CBCA. Abella interpreted this very broadly

- She found that parties should take at face value the correspondence that was received in good faith by opposing counsel.
- The standard commercial practice is that giving another party draft resolutions that go unsigned will not be sufficient to constitute adoption under the Act, so why is this any different?
  - The dissent really goes hard on this point and is quite persuasive
    - The purpose of s21 is to, again, override the common law interpretation of intentions, so courts are again infusing common law where the legislature intended to displace it.

In *Szecket v Huang*, where the plaintiff was promoter for a corporation that did not yet exist and contracted with the defendant and the corporation never incorporated, allowed a direct interpretation of the facts. Because the corporation never formed, Szecket sued Huang personally for failing to perform the contract. The court used a two step process from *Westcom*:

1. Whether there was a contract under common law principles
2. If so, is the defendant promoter personally liable under s21(1) of the *OBCA*

The trial judge found that (i) there was a contract on the basis of the parties intentions, and (ii) the defendant promoter was personally liable under s21 of *OBCA*.

- But, the ONCA rejects the two step analysis. They find that Huang's intention is irrelevant and his liability is all on s21. Ended up finding that the Promoter was liable under s21(1) of the *OBCA* and was not saved by s21(4).
- Their finding that statutes are used to avoid common law and confusion around them did not expressly overrule *Westcom*, but in effect it did.
  - They interpret s21(1) to include a "purported contract"

All this mess led Parliament to amend section 14 of the *CBCA* to include "a person who enters into, or purports to enter into, a written contract in the name of …". The rest is the same, for these people, there is personal liability until 1) the PIC was adopted within a reasonable timeframe after incorporation or 2) they contracted out of liability on the terms of the contract.
- This amendment overrode the *Westcom* logic

In comparing the CBCA and ABCA, there are a few key differences:
- CBCA says the promoter is personally bound
  - The ABCA includes the 'purports to' (negating Westcom rationale) but does not include 'personal liability'
- The ABCA characterises the parties as 'warrantors', whereas the CBCA characterises them as 'parties to the contract' (promoter).
  - So, the promoter in Alberta is not a party to the contract,
- If the ABCA applies, the promoter warrants that the 1) corporation will come into existence and 2) the PIC will be adopted
  - If neither of these happen, the promoter is liable for breach of *warranty*, not breach of *contract* (like they would be in the CBCA)
  - So, a promoter under the ABCA is not party to the contract, but a warrantor, and is liable for breach of *warranty* if s15(2)(a)(i) and s15(2)(a)(ii) are not satisfied.
- All of this doesn't come up much, since s15(6) of the ABCA says liability can be excluded if the contract expressly outlines that liability won't apply (like s14(4) of the CBCA).

The ABCA and CBCA are the same in the fact that they only apply to written contracts.
- So, if the PIC is written, then either the ABCA or CBCA would apply (depending on which it was incorporated under)
  - But, if it is oral, then it is by common law (*Kelner* and *Smallwood* logic).
    - Although outside the scope of this course, the *OBCA* also applies to written contracts.

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 15 (1) This section applies unless the person referred to in subsection (2) and all parties to the contract referred to in that subsection (a) believe that the body corporate exists and is incorporated under, or (b) intend that the body corporate is to be incorporated under the laws of a jurisdiction other than Alberta. (2) Except as provided in this section, if a person enters or purports to enter into a written contract in the name of or on behalf of a body corporate before it comes into existence, (a) that person is deemed to warrant to the other party to the contract

(i) that the body corporate will come into existence within a reasonable time, and

(ii) that the contract will be adopted within a reasonable time after the body corporate comes into existence,

(b) that person is liable to the other party to the contract for damages for a breach of that warranty, and

(c) the measure of damages for that breach of warranty shall be the same as if the body corporate existed when the contract was made, the person who made the contract on behalf of the body corporate had no authority to do so and the body corporate refused to ratify the contract.

(6) A person who enters or purports to enter into a written contract in the name of or on behalf of a body corporate before it comes into existence is not in any event liable for damages under subsection (2) if the contract expressly provides that the person is not to be so liable.

Damages

Wickberg v Shatsky et al. (1969) 4 DLR (3d) 540 (BCSC)

Facts:
Lawrence and Shatsky (individual defendants) became directors of Rapid Addressing Systems Ltd., which sold and serviced business machines and supplies. They planned to incorporate Rapid Data Ltd, but it never went through. They improperly carried on business under the name Rapid Data Ltd.

- Wickberg (plaintiff) was hired to be the new manager for the business

May 9, 1966: plaintiff received employment contract on Rapid Data letterhead

- It was signed by Lawrence Shatsky as President of Rapid Data. A few dates later, Lawrence told Wickberg they were dropping 'Ltd' from the name
- The business wasn't successful, and Wickberg was fired for refusing to work on a purely commission bases.

Aug 26, 1966: Termination letter sent to plaintiff, which referred to Rapid Addressing Systems as the employer of Wickberg

- Wickberg brought action against the individual defendants on various grounds.

Issue:
Is Lawrence personally liable as party to the contract, or for warranting the existence of Rapid Data?

Rule:
Black v Smallwood: parties intentions are required to determine whether personal liability for the promoter exists.

Analysis:
Breach of Contract
In line with the *Smallwood* logic, the parties never intended for the individual defendants to be party to the contract with the plaintiff. Even though both were mistaken about the existence of the corporation, the plaintiff knew Shatsky was not contracting in his personal capacity

- No intention to be personally bound; Lawrence has no liability in the contract

Breach of Warranty
While not liable for breach of contract, Shatsky did make warranties (representations) to Wickberg about the existence of the Rapid Data (letterhead, signed as Rapid Data) and that it was in contract with Wickberg.

- They warranted that Rapid Data was a legal entity and had the authority to bind it. Because this was false, Shatsky et al. are liable for breach of warranty.

Conclusion:

No personal liability under contract, but breach of warranty established.

Issue:

What damages are applicable?

Rule:

Damages can only be given if the warranty caused the plaintiff's loss

Analysis:

At the time of entering into the contract, Wickberg did not know that Rapid Data was not incorporated and the defendants did.

- However, there is no causal connection between the damages suffered by the plaintiff (termination) and the breach of warranty as to its existence.
- There was a breach, and there was a loss, but there was no connection
  - The loss was the unsuccessful business. This would have happened with or without Shatsky warranting Wickberg on the existence of Rapid Data

Conclusion:

Damages nominal in $10

Hold, Order:

Nominal damages awarded for breach of warranty

Ratio:

Damages will be nominal for breach of warranty if they cannot be causally linked to the loss

This case is older than ABCA or CBCA, so it is purely using common law principles. It can still be used when assessing damages for breach of warranty (but not contract)

- By using the intentions of the parties, the court uses *Smallwood* and found no intention to be personally bound existed and thus Shatsky was not personally liable for breach of contract
  - In this case, they only used *Smallwood*, but faced with a fact pattern, both *Smallwood* and *Kelner* should be analysed
- But he did warrant the existence of the company that did not exist, so he was liable for breach of warranty
  - However, damages can only be given if the breach of warranty was tied to the loss. Since it was not causally connected (the failure of the company was irrelevant to the representation that it was actually a different company), damages were only nominal.
- What if Shatsky made further warranties? On something like how the corporation would be capitalized (the assets)
  - Could then argue that the loss was made from the breach of warranty because they did business with the yet to be incorporated business on the basis that it was a fully funded entity, or whatever the warranty may be.
  - The third party is basically taking a chance when dealing with the promoter on whether or not the corporation will have the financial wherewithal
- Section 15(2)(b) of the ABCA also goes into damages as well

CHAPTER 4: CORPORATION AS A LEGAL PERSON

Liability Based on Lifting the Corporate Veil

In rare situations, the courts will lift the corporate veil to ground liability for the individual standing behind the corporation.

- Other areas of liability for directors or officers like regulatory statutes, tortious conduct are different than lifting the corporate veil, it is more in line with concurrent liability

The starting point with the corporate veil is always *Salomon* (see chapter 2).

- Corporate Veil: a corporation is a separate legal entity which exists by operation of the act under which it is incorporated. The purpose of a corporation is to shield the individuals standing behind it from personal liability; the corporation assumes its own obligations, enters into its own contracts and commits its own torts and crimes.
    - This begs the question, when will courts look behind the corporate veil?
        - Corporations are an artificial person, and since it is artificial, courts will decide when the corporation is liable, and when the individuals are liable.

Kosmopoulos was the first major deviation of the *Salomon* logic. In that case, the Supreme Court of Canada found that the principle can be disregarded (the corporate veil can be "lifted" or "pierced") and be treated as a mere 'agent' or 'puppet' of the controlling shareholder or parent corporation in rare cases.

- Lifting the veil can occur when not doing so would yield a result that is too "flagrantly opposed to justice, convenience or the interests of the revenue".

In Alberta, *Driving Force Inc v I Spy-Eagle Eyes Safety Inc* (2022 ABCA 25) found that *Kosmopoulos* is a background principle, not a background test.

- The "too flagrantly opposed" is not a test, it would be too unworkable. It is more of a policy objective to be balanced against the reluctance of the courts to undermine the concept of a separate legal personality.
    - They don't introduce a test themselves however
- In the absence of a unifying test, lifting the veil cases tend to be decided based on their own facts and circumstances
    - A highly relevant factor in determining whether the corporate veil should be lifted is whether the plaintiff voluntarily dealt with the limited liability corporation, knowing the consequences.
- In *Driving Force*, similar to *Salomon,* the Court found no liability since documents were all public anyway, and therefore there cannot be fraud.

Driving Force cites another important case: *Transamerica Life Insurance Co. of Canada v Canada Life Assurance Company* ("*Transamerica*"). In *Transamerica*, the court found that courts will disregard the separate legal personality of a corporate entity in a two part test:

1. Where the corporate entity is completely dominated and controlled by an individual/parent company, and
2. Where the corporate entity is being used as a shield for fraudulent or improper conduct

However, this entire test is again very fact specific. Courts are more likely to pierce the corporate veil to find a corporation liable for shareholder obligations, but less so where a shareholder would be liable for corporate obligations.

When faced with a fact scenario the analysis should look like:

- Step 1: General principle in *Salomon* that recognizes the separate legal entity of corporations
- Step 2: Cite *Kosmopoulos* that it is possible to life this "corporate veil", but will only be done so in cases where it would be "too flagrantly opposed to justice to not lift it"
    - *Driving Force* finds this is not a test, but a general principle where the facts of the specific case are highly determinative of if the veil will be lifted or not
- Step 3: Use *Transamerica* to analyse if the veil will be lifted, using the two-part test and rely on the facts:
    - Completely dominated by an individual
    - Used as a shield for improper conduct

The *Yaiguaje v Chevron Corporation* followed this framework exactly.

- Chevron (oil company) development damaged lands in Ecuador and caused health issues to citizens. The citizens couldn't sue the company in the States for technical reasons, so they brought action in Ecuador, even though Chevron was American.
- The litigants eventually tried to sue Chevron Canada, who was a subsidiary of Chevron US. In essence, they were trying to collect from the US, so they went through Canada to lift that veil to access the assets of Chevron US
    - In this case, it wasn't an individual who benefits from the separate legal entity, but the parent company. Either would be shielded from liability under *Salomon*
- Step 1: *Salomon* of corporate separateness
- Step 2: Corporate veil can be lifted under *Kosmopoulos*
- Step 3: Can be lifted if:
    - Completely dominated by parent company; Chevron Canada completely dominated by US
    - Used subsidiary for fraud
- In the end, the Court held that Chevron Canada's assets are not severable for that judgement because of the corporate separateness.

Big Bend Hotel Ltd v Security Mutual Casualty Company, (1980) 19 BCLR 102 (SC)

Facts:
Vincent Kumar was the president and sole shareholder of K&S Enterprises Limited which operated the Fort Hotel in Langley, BC.
- The Fort Hotel was destroyed by fire and Security Mutual Casualty Co (Defendant, insurer) paid out the insurance claim for the fire.

Kumar then purchased all the shares in Big Bend Hotel (plaintiff/insured), the sole asset of the plaintiff corporation in Golden. BC.
- Kumar, acting for Big Bend, sought to increase the insurance of the hotel. When applying for the insurance, Kumar never disclosed the previous insurance claim for a fire to Security or to Reed Shaw Stenhouse, the insurance agent. But he was also not directly asked.
    - The application form even had space for "loss records".
- The insurance policy was placed for Big Bend, and the hotel ended up also burning down.

Security denied coverage on two bases:
1. There was a failure to communicate circumstances material to the risk (insurance law)
2. There was failure to disclose previous losses (lifting corporate veil in corporate law)

Big Bend brought action to receive this insurance coverage

Issue:
Should the corporate veil be lifted when looking to Mr. Kumar's failure to disclose information to Security?

Rule:
Section 14 of the *Insurance Act*
(1) No contract is rendered void or voidable by reason of any misrepresentation, or any failure to disclose on the part of the insured in the application or proposal for the insurance or otherwise, unless the misrepresentation or failure to disclose is material to the contract.

Analysis:
<u>Insurance Law analysis</u>
The test for 'material fact' (as seen in s14(1)): whether the mind of a prudent insurer would be affected, either in deciding whether to take the risk at all or in fixing the premium, by knowledge of a particular fact if it had been disclosed.

- Kumar did fail to disclose a material fact. Because he controlled both companies, the previous fire loss of Fort Hotel was material and the failure to input this on the form led the insurers to believe he had no prior losses
- It was 'patently obvious' that Kumar didn't disclose the information since he knew (from experience) it would prevent him from obtaining insurance for the hotel. He was cognizant of the importance of the prior loss to make a full and frank disclosure thereof

Corporate Law analysis

Big Bend argues that Kumar filled out the form, on behalf of Big Bend, not his personal account; that it wasn't Kumar seeking insurance, it was Big Bend. So, Kumar's prior insurance claims were not asked for on the forms, only Big Bends.

- Security argues we should look beyond the corporate veil to the conduct of Mr. Kumar as he improperly used Big Bend.

While courts adhere to the corporate veil in *Salomon*, there are exceptions to ground liability for individuals, particularly in the case of improper conduct or fraud.

- Kumar, in this case, was using Big Bend to conceal the prior insurance claims, and thus for an improper purpose.
  - As such, the corporate veil is properly lifted to deny this claim.

Conclusion:

Corporate veil lifted

Hold, Order:

Action dismissed

Ratio:

Courts are more likely to pierce the corporate veil in cases of improper conduct or fraud.

This case was prior to *Transamerica* and the two-part test, but in a similar case today, it should be brought up. In terms of piercing the corporate veil being fact specific, one very large fact is if the conduct was improper or fraudulent. If it is, then the court is much more likely to lift the veil

Jin v Ren, 2015 ABQB 115, aff'd 2016 ABCA 80

Facts:

Ren (defendant) was the director of Hart Fibre Trade Company ("Hart"). Ren approached Jin (plaintiff) about investing in Hart, and Jin invested about $300,000 for a controlling interest in the company.

- Ren just took Jin's money and never provided proof of Jin's interest in the company and did not provide an account of his investment. Ren refused to return Jin's money
- Ren promised to return the money only if he agreed to a non-competition clause in relation to the hemp industry in Canada and China (ie, Jin won't compete with Ren)

Jin brought an action against Ren and Hart to recover his investment amount.

Issue:

Can Jin recover the $300,000 in Hart Fibre, or is Ren protected by the corporate veil?

Rule:

As per *Kosmopoulos*, can pierce the corporate veil from *Salomon*. *Transamerica* test:

1. Where the corporate entity is completely dominated and controlled by an individual/parent company, and
2. Where the corporate entity is being used as a shield for fraudulent or improper conduct

Analysis:

Ren tried to argue that the corporation could be sued, but not him personally. The test for lifting the veil is more stringent that the "just and fair standard" in *Kosmopoulos*; courts will disregard separate legal personality of a corporation when the *Transamerica* test is satisfied.

1. Ren was the sole director of Hart, he was the only one calling the shots. He directed Hart to retain the money against Jin.
2. Hart was not set up as a mere façade or shield to attract Jin's investment. However, Ren enticed Jin's investment and retained it for an improper purpose, as he did not give any accounting, coerced the investment and retained the money.
    a. By retaining Jin's money in his capacity as Director of Hart, which did not belong to him, he expressly directed a wrongful thing to be done.

Conclusion:
Ren and Hart are jointly and severally liable to the plaintiff

Hold, Order:
Application allowed

Ratio:
When examining the control examined in Stage 1, we can look at if the individual directed the corporation to engage in those wrongful acts.

This gives more context to the *Transamerica* test based on factual determinations. The court found that a corporation does not have to be established for the purpose of improper conduct to satisfy the second branch of the test. However, if the conduct done was to hide behind the shield, it can.
- And if the individual directed the corporation to conduct the improper conduct, that is sufficient to satisfy the first branch.

Aubin v Petrone, 2020 ABCA 13

Facts:
Ms. Aubin (plaintiff) and Mr. Petrone (defendant) married in 1993 and incorporated Quantiam Technologies ("Quantiam") in 1998, where Petrone was the majority shareholder, director and CEO and Aubin was the director and minority shareholder.
- To finance the purchase of their home, they incorporated another corporation where they were equal owners, 159 Corp. This corporation borrowed money from Quantiam.

Aubin then filed for divorce, and the divorce was very contentious. Whenever Aubin threatened to leave, Petrone threatened to liquidate the company and that she 'would never see a single dollar'. Petrone instructed Quantiam to demand repayment of loan and foreclose the house.
- In response, Aubin sold her shares back to Quantiam under a USA but Petrone refused to release her proceeds

Pursuant to the divorce proceedings, Petrone was ordered to pay $5,6M in equalization payments.
- Petrone did not have this money, so Aubin brings action to recover that money

Procedural History:
Trial judge secured the payment by placing charge on Petrone's shares and Quantiam's building.

Issue:
Is Quantiam liable for the equalization payment owed by the individual defendant, Petrone?

Rule:
Salomon, Kosmopoulos and *Transamerica* all apply for family law contexts. *Arsenault v Arsenault* amended the test for a family law context:
1. Individual exercises complete control of finances, policy, business of the company
2. Control was used to commit a fraud that unjustly deprives claimant of their rights
3. Misconduct must be the reason for the third party's injury or loss.

Analysis:
Petrone argues that Quantiam, as a separate legal entity, should have no liability for his actions. He claimed this was a way to partition assets to shield it from liability of the himself.

- Given the intersection between family law and corporate law, this is a difficult analysis. But, the proper focus on marital breakdown should be on the parties real assets after the separation and a fair distribution of them.
  - Piercing the veil of a company owned by one party can be appropriate, or perhaps essential, to ensure kids and ex-spouses receive financial entitlements
  - The law must be used to ensure permissible corporate arrangements don't work an injustice on the realm of family health.

This is not to say family law makes a relaxed test; the added factor recognizes that obligations of family law are on equal footing with other legal obligations and deserve balancing where interests compete.

- For family law, a spouse cannot chose to deal with a corporation always since the assets of the family are tied to the corporation.

Modified *Transamerica* test:

1. Complete control of finances/policy
   a. *De facto* control also counts; where a person has the right to change the directorship of the company or influence shareholders who could
   b. Obvious that Petrone controls Quantiam as he controlled his salary and used it to minimize exposure for spousal support (he could draw cash from Quantiam) and directed Quantiam to foreclose on the loan for the home.
2. Control used to commit a fraud that would unjustly deprive claimant of their rights
   a. Veil can be lifted to prevent conduct akin to fraud – it can be done as a responsive act and a preventative one (not just to be used when wrongful conduct has occurred, but in anticipation of it) like the seizure of assets here
   b. Pre-emptive in the sense that he won't pay this sum. If he fails to pay, the court will pierce the corporate veil, go in and take assets.
   c. Petrone tried to argue that each wrongful act he did was not sufficient to occasion a loss for Ms. Aubin. However, the acts cannot be read in isolation, they need to be assessed on the whole of the circumstances to see if there would be flagrant injustice.
      i. The injustice, in this case, is the deprivation of Ms. Aubin's family law rights (not those of shareholder, just family law)
   d. Remedy is dependant on the loss of rights in that area of law
      i. Oppression remedy doesn't work as that is corporate, whereas the loss is one of family law
3. Conduct must be the reason for the claimant's loss of rights
   a. Mr. Petrone committed, attempted to commit or threatened various wrongs against Ms. Aubin and used Quantiam as a weapon. He said and acted in ways to prevent Ms. Aubin from receiving additional payment
      i. He risks the family's wealth and placed it beyond her reach, and frustrates her family law rights
   b. "rights" connotes legal entitlements, including those under family law

Conclusion:

Quantiam is liable

Hold, Order:

Appeal dismissed.

Ratio:

Three-part *Transamerica* test for family law context:

1. Individual exercises complete control of finances, policy, business of the company
2. Control was used to commit a fraud that unjustly deprives claimant of their rights
3. Misconduct must be the reason for the third party's injury or loss.

The test can be reformulated to better meet the requirements of different areas of law

De facto control of the corporation is sufficient to ground the first branch of the test – a 51% shareholder can dominate the corporation is they have *de facto* control.

Lifting corporate veil can be preventative or reactive; not just to be used when wrongful conduct has occurred, but in anticipation of it.

This case is important for a lot of reasons. First, while it confirms the *Transamerica* multi-part test, it adds another factor. This is because the test is fact dependent, and this is a family law case, which prompts different considerations. What may otherwise be permissible may not be passable in family law. Creditors can chose if they want to deal with a corporation if they want – family law removes this choice. Piercing the corporate veil may well be needed to ensure children are protected and ex-spouses receive their financial entitlements.

- As such, it is more accurate to view *Transamerica* as a baseline test, one which can be deviated or additional elements added depending on the field of law the case is in. In this case, family law interests justified adding the third element. The test can be reformulated
- This case was cited in *Driving Force*, saying that in the absence of a unifying test, lifting the veil can be decided based on their own facts, and analysed in a way relevant to the context at hand.
    - Decisions outside corporate law can be coloured by considerations of corporate oppression

The other important takeaway is that *de facto* control of a company is enough to establish the first branch of the test if *de jure* control is not established. In this case, even if someone isn't the sole shareholder/director, but exhibit sole discretion over the directing of the company, the corporate veil may still be lifted.

Lastly, the lifting of the corporate veil can be preventative or reactive. Courts don't have to wait until an injustice has occurred to pierce the veil. In this case, Petrone was unlikely to pay, so the Court could pierce the veil and collect the assets before he refuses to pay.

Rockwell Developments Ltd v Newtonbrook Plaza Ltd, [1972] 3 OR 199 (CA)

Facts:
Rockwell Developments ("Rockwell"; plaintiff) entered into an agreement to purchase real estate from Newtonbrook Plaza Ltd ("Newtonbrook"; defendant). Litigation arose over the transaction.

- Newtonbrook won the litigation and costs were awarded against Rockwell ($4800)
    - Newtonbrook sought to collect costs, but Rockwell only had $31.85 in assets.

Newtonbrook brought application to collect costs from, Kelner, the Director or Rockwell

Procedural History:
Trial judge allowed costs to be collected from Kelner (ie, corporate veil pierced)

Issue:
Can Newtonbrook collect costs from Kelner (ie, pierce the corporate veil)?

Rule:
As per *Kosmopoulos*, can pierce the corporate veil from *Salomon*. *Transamerica* test:

1. Where the corporate entity is completely dominated and controlled by an individual/parent company, and
2. Where the corporate entity is being used as a shield for fraudulent or improper conduct

Analysis:
There are indeed a number of facts that suggest Kelner was acting in a personal capacity:

- No directors resolution authorized Kelner to enter into purchase on Rockwell's behalf
- Deposit was advanced to Kelner from their own funds directly to Newtonbrook (it wasn't entered on Rockwell's books)
- No resolution of directors authorizing Rockwell's action against Newtonbrook
- No resolution relating to the retention of counsel for litigation.

It is obvious the Kelner was poor in handling the corporate records and conducting his business. However, no one connected to Rockwell was in a position to complain except Kelner himself. There are also no serious allegations of misconduct or fraud

- The use of a 'one man company' for carrying out business transactions is permitted and the property of the corporation need be properly distinguished from the member.
- This contract was between Newtonbrook and Rockwell; Kelner was not the actual contracting party even if he benefited from the contract
  - He could not have sued on it, or himself been sued.

Internal formalities not being conducted properly is not sufficient to pierce the veil in a separate matter.

- The parties having issues with the internal issues would only be those in the company (ie, Kelner himself)

Conclusion:

Veil not pierced.

Hold, Order:

Appeal allowed; trial judge order set aside and substitute order to dismiss application

Ratio:

Internal formalities not being conducted properly is not sufficient to pierce the veil of a separate matter.

What Kelner did is common in real estate; agents will incorporate a separate corporation for each real estate transaction they do to manage risks and isolate the risks of each project within that one corporation, rather than the whole agency.

- Kelner was the legal and beneficial owner of the shares in the company

While it may seem antithetical, the issues of Kelner acting in a personal capacity were actually not on issue for Newtonbrook-Rockwell; the only people who could take issue with the internal functioning were the internal members, not Rockwell.

- What could Newtonbrook have done to protect themselves?
  - Get Kelner to sign a personal guarantee of performance
  - If Newtonbrook insisted on this, the transaction may not have gone through given Rockwell's finances. But, these are legal risks associated with negotiating agreements.

This is the first case we have seen where the Court did not pierce the corporate veil. But, it should be noted that this is by far the most common outcome in requests to lift the veil. Courts are generally hesitant to pierce the veil since it exists for a reason – if the rules to lift it are too loose, the principle is redundant.

It is not uncommon for a client, who a lawyer represents, is a shareholder in a company asks to bill to the corporation rather than them personally. This is a big risk – a lawyer who represents a client, and not their company for that matter, cannot accept the companies money.

- Even if that person was the only shareholder/director/officer, there is no legal justification to bill the corporation since the veil still exists
  - Doing so would violate the Lawyers' Code of Conduct to not follow instructions prior to professional ethics and don't assist a client in committing a crime/fraud.

- They may be asking the lawyer to deduct the amount from the company, and then the lawyer could be potentially assisting tax avoidance/fraud.
- Clients and their corporations should never be treated as the same person. There could be other factors, like the government or stakeholders in their corporation

Liability Based on Thin Capitalization

Thin Capitalization: when shareholders have invested a small amount of money and usually in an amount that is inadequate to cover the reasonably foreseeable obligations of the corporation's business

- Even worse, if the corporation is liable for something, and the capital is inadequate to make good of the liability, can the defendant sue the shareholders to get that money if there is in thin capital?
  - This is not a large component of Canadian corporate jurisprudence, but is in the USA
    - American courts will often pierce the corporate veil in the USA, but they will not often do so in Canada, if at all.

Henry Browne & Sons Ltd v Smith, [1964] 2 Lloyd's Rep 476

Facts:

A contract was negotiated between Smith (defendant) on behalf of Ocean Charters Ltd (defendant corporation wholly owned by Smith/purchaser) between Henry Browne (plaintiff, manufacturer) and Ocean Charters.

- Ocean Charter fails to pay for a steerage device and therefore breached the contract. Ocean Charter was also thinly capitalized (only had a $2 share capital)

Henry Browne brought an action against Smith for breach of contract on basis of thin capitalization.

Issue:

Does thin capitalization change contractual liability such that Mr. Smith is personally liable?

Rule:

As per *Salomon*, corporations are separate legal entities

Analysis:

Thin capitalization does not mean the corporation is a mere façade; there is nothing fraudulent about running a business through a corporation.

- Henry Browne could have inquired into Ocean Charter and assess the risk of contracting with the corporation directly before contracting with them.

Conclusion:

Mr. Smith not personally liable.

Hold, Order:

Action dismissed

Ratio:

The corporate veil won't be lifted to save a plaintiff from a bad deal

The corporate veil cannot be lifted simply because two parties entered into a bad deal that ended up being detrimental to the plaintiff – particularly when it is available to research the company they interact with. But what about involuntary actions, like torts?

Walkovszky v Carlton (1966) 18 NY 414 (CA)

Facts:

Walkovszky (plaintiff) was severely injured in New York City when he was run over by a taxi owned by the defendant Seon Cabs, and negligently driven by another defendant, Marchese.

- Carlton (individual defendant) was a stockholder of 10 corporations, Seon being one of them. All 10 have two cabs in their name, and each only has the minimum insurance ($10,000).
- Although separate corporations on paper, these 10 operated as a 'single entity, unit and enterprise' for financing, repairs, employees and garaging.

The plaintiff brings action for his injuries and alleges that he is entitled to hold all stockholders of the 10 corporations personally liable because the multiple corporations constitute an unlawful attempt to defraud members of the public who may be injured by cabs.

Issue:

Does Carlton have personal liability for the injuries suffered by Walkovszky?

Rule:

Salomon: corporations are separate legal entities.

Kosmopoulos: can sever the corporate veil if unjust not to do so

Analysis:

Plaintiff Argument 1: Group Liability Argument

Plaintiff argues that the group of companies should be treated as a single entity, so the liabilities of one attach to the others.

- Even if carrying on one larger business (rather than 10 separate ones), there is no group liability. There is separateness of corporate liability
- It is one thing to say that a corporation is a fragment of a larger entity which actually conducts the business, but that does not make the corporation a dummy for it's individual stockholders who are carrying out business in their personal capacities rather than corporate.

Plaintiff Argument 2: Fraud Argument

Plaintiff argues that corporations were used to defraud the members of the public by separating the corporations and their resulting liability

- Thin capitalization does not amount to fraud – if we accept that it does, we could attach liability to many shareholders
- The corporate structure here cannot defraud the public, since there is no fraud. The defendant merely incorporated as he was to capitalize on liability for his company
  - If this was a single company, the individual would still not be liable, so why would the multiple corporations change anything?

Plaintiff Argument 3: Thin Capitalization Argument

Plaintiff argues that corporations were undercapitalized (not enough insurance, and not enough capital to make good claims of injuries that are reasonably foreseeable in their business.

- The corporations have complied with the law – each company held the statutory minimum for insurance
  - There was no obligation for him to have done more. So there is no basis for any wrongdoing
- There is nothing wrong with thin capitalization, as long as the formal elements of the law are complied with

Conclusion:

No personal liability.

Hold, Order:

Individual liability denied.

Ratio:

Thin capitalization does not amount to fraud. There is nothing wrong with thin capitalization, as long as the formal elements of the law are complied with.

Dissent (Keating):
These corporations are intentionally separated for the purpose of avoiding responsibility of a large fleet. To permit this privilege, no matter how irresponsible or to what cost to the public, is not in the Policy of the State. The shareholders should all be held individually liable. The law decides if and when the corporation has a separate legal personality or not, and there are situations that amount to abuse and irresponsibility where the law should intervene.

- There is a line to be drawn between irresponsible conduct and responsible conduct
  - Where finances are insufficient to cover the costs of insurance premiums, the shareholder should not be liable.
- Should form a test: due to thin capitalization, and the corporation is unable to pay for liabilities, when liabilities are certain to arise, the shareholder will be personally liable.

The idea that thin capitalization does not amount to fraud is sound in Canada. As this case found, there is nothing wrong with thin capitalization, so long as formal requirements are respected.

- Part of this makes sense; the point of corporations is to shield the shareholders from liability. To prevent individuals from doing this because they did it pervasively throughout their business would render the notion of corporate veil redundant.
  - Where do you draw the line? How many is too many? Why is incorporating one time ok, but multiple is not?

Nonetheless, the dissent does bring in a fairness perspective. That a company with little assets can avoid paying (arguably) what they should by having many smaller corporations.

- The problem with the test proposed by Keating is that it is likely untenable.
  - When do finances dwindle too much?
  - In terms of division of labour, institutionally speaking, who should address this problem?
    - Majority says the courts should not be imposing liability, that is a problem for the legislatures to decide
    - Dissent has good points by considering the policy considerations behind corporate law and when insulations should apply
      - But should it be the courts, or the legislatures?

In Alberta, thin capitalization alone is not enough to lift the corporate veil, unlike in the USA. It has to be adjusted to fit into the *Transamerica* framework of lifting it. In Canada, you can include it as part of a broader argument, but it won't do all the work itself.

Liability Based on Disregard of Formality

It is possible to ground personal liability, notwithstanding the corporate veil, even when the context of the case would not support lifting of the corporate veil otherwise (not "flagrant injustice" as *Kosmopoulos* puts it)

Wolfe v Moir, [1969] 69 WWR 70 (AB SC)

Facts:
Gordon Moir (defendant) carried on business as an individual under the names "Fort Whoop-Up and "Moir's Sportsland". Moir was also the secretary of Chinook Sport Shop Ltd.

- Wolfe (plaintiff) was injured while roller skating at Fort Whoop-Up in Lethbridge at the age of 14, which was owned by Chinook
  - Wolfe brought action against Chinook and Wolfe.

Issue:
Is Moir personally liable to Wolfe for the injuries at the skating-rink or is it sole liability of Chinook?

Rule:
Section 84 of the *Companies Act* (Section 10(8) of the *ABCA*)
(1) Every company,
    (c) shall have its name set forth in legible characters in all notices, advertisements, and other official publications of the company, and in all bills of exchange, promissory notes, endorsements, cheques, and orders for money or goods purporting to be signed by or on behalf of the company, and in all bills of parcels, invoices, receipts, and letters of credit of the company.

Analysis:
Fort Whoop-Up became involved with another company, Chinook, who operated the rink and was created to operate it. The corporation, Chinook, exists and it owns the skating rink in question. The defendant argues that, based on *Salomon*, he does not own the rink, Chinook did, so Chinook should be the one liable.

- However, as *Salomon* found, requirements of the relevant Act must be complied with to benefit from limited liability resulting from separate legal personality
    - In this case, there was a failure to comply with the requirements of s84(1)(c) of the *Companies Act* [s10(8) of the *ABCA* today] by advertising without the name Chinook involved

The way Moir conducted his business, there was no indication that the rink was owned and operated by Chinook.

- There was no advertising or signage included in the name of the corporation
- No indication the customers were dealing with Chinook
- Appeared only operated by Fort Whoop Up
- He referred to himself personally as manager
    - Also no indication of the involvement of an LLP

The effect is that if a person choses to hold themselves out to the company without association, he holds himself liable. There is no indication when he is acting personally, or when he is acting as part of the corporation.

- It does not matter whether the customer relied on the representations, it is not incumbent on the plaintiff to think about how the corporation works
    - It is an obligation for the corporation to be clear in how they operate.
- For a person to rely on the protection from liability by a corporation, they must prescribe to all the formalities laid out in statute – which Moir did not do.
- Further, for a manager to hold himself in advertising, but not the company, he runs the risk of personally liable.

Conclusion:
Moir personally liable.

Hold, Order:
Action allowed

Ratio:
For a person to rely on the protection from liability by a corporation, they must prescribe to all the formalities laid out in statute

This case illustrates how the 'holding out principle' requires some strict adherence to legislation. Moir was holding out being personally liable for this business, and not the corporation.

- While this would normally be fine, by failing to comply with the legislation around formalities of the corporation, the defendant cannot claim limited liability from the separate legal entity

Vallis v Prairie Alternative Energy Solutions Ltd, 2013 SKPC 124

Facts:

Prairie Alternative Energy Solutions ("PAES", defendant) is a corporation, where Mr. Karras is president, secretary, shareholder, and sole director.

- Vallis (plaintiff) contracted with PAES to instal a geothermal heating system. Mr. Karras was the only person the plaintiff dealt with.
  - Karris did not represent that his business was incorporated in email correspondence or invoices.
  - Karras did the installation, had no business cards, the truck did not have a business name. Karras stated he didn't have 'ltd', 'corp', or 'inc' in his name because he did not think it was relevant.

PAES ended up being liable for breach of contract, in the amount of $4,176.00

Issue:

Is Mr. Karras personally liable for breach of contract?

Rule:

Section 299 of the (Saskatchewan) *Business Corporation Act*

(2) Subject to subsection 10(2), no person shall carry on business under a name that does not include "Limited", "Limitée", "Incorporated", "Incorporée" or "Corporation", "Ltd.", "Ltée", "Inc." or "Corp.", if the name is the name of a corporation, unless:
  - (a) the name is on the register; or
  - (b) the name is the name of a corporation that is exempted from registration pursuant to this Act.

Analysis:

Was Mr. Karras holding out PAES as the entity doing business, or is he holding himself out as the individual doing it?

- Karras did not use 'ltd' in his business because he did not think it was relevant.
  - This contravenes s299 of the *SBCA*.
- Nothing to suggest this was not a sole proprietorship
- No names on vehicle, business cards, emails, cheques that identified PAES

Though Karras was using PAES as a way to carry out business, he did not hold himself out this way, and he did not submit any formal requirements of the name. It does not matter if the mistake was not dishonest, the Act is clear on this regard

- Karras failed to accurately represent the corporate status of his business, and is thus personally liable.

Conclusion:

Karras personally liable.

Hold, Order:

Action allowed

Ratio:

Even negligent failure to comply with formal requirements can ground personal liability

This case is almost the exact same as *Wolfe v Moir*. However, Moir was a little more intentional in his dealings and not advertising his involvement with Chinook, whereas Karras was just negligent.

- However, both were as liable as the other. So, it does not matter whether the failure to comply with the formalities was negligent or intentional, personal liability can be found in both cases.

It has also been found that a solicitor who gave oral advice to a client, was liable for an ensuing breach. Even though he had a memo to file about the advice, it was not a letter sent to the client, and thus the lack of written advice was a violation of formalities of corporate law

- Any kind of communication with a client is usually done on a memo to memorialize the advice on an evidentiary basis anyway. This may be why.

Liability Based in the Area of Trust Law

In situations where a corporation is a trustee (holding funds on behalf of someone else) and the corporation breaches that trust by using the funds for something else, personal liability can arise to the individual who directed this.

- For example, travel agencies hold money for Air Canada, and if they breach that trust by using it for their own operating expenses, the director can also be personally liable.
- Liability for Knowing Assistance: Director knowingly assisted a corporation in breaching it's trust obligations by improperly using those funds for some other purpose.

Caja Paraguaya de Jubilaciones y Pensiones del Personal de Itaipu Binacional v Garcia, 2020 ONCA 412

Facts:

Caja ("the Pension Fund") attempted to invest more than $34,000,000 in Canadian investments, as suggested by Mr. Garcia (defendant). The investments were on unfavourable terms and at risk of the elaborate fraudulent documentation disclosed. Union was one of the Canadian enterprises. Mr. Garcia controlled the flow of money between Union and Caja. He fudged the transfers through a shelf corporation

Ms. Duscio was the sole officer and director of Catan Canada; this was incorporated for a business vehicle for office rental income and a dance studio, operated by herself.

- Her husband was actually the *de facto* brains behind Catan and made all financial decisions in relation to Catan, controlled its banking and arranged for the books and records to be kept.
    - He incorporated Columbus Capital, which was used to transfer $3M through Catan as part of the fraud

Mr. Garcia perpetrated a multi-million dollar fraud against the Pension Fund. Mr. Duscio "filtered" $3M through Catan as part of the fraud.

- Mr. Garcia who was holding the money in trust for the Pension Fund, transferred it to Catan to hold as trustee for the Pension Fund
    - In sum, Mr. Garcia, with the help of Mr. Duscio, routed $3M of funds that have been invested with Union through a bank account of Catan, a corporation owned by Ms. Duscio. Some funds were paid to Ms. Duscio.
        - Money was diverted to pay Caja insiders and enrich Mr. and Mrs. Garcia.

Procedural History:

Trial judge found Mr. Garcia liable, as well as Caja was entitled to judgement against the Duscio's and Catan. Mr. Duscio personally liable since he was the effective controlling one.

Issue:

Is Ms. Duscio personally liable for knowing assistance?

Rule:

Knowing assistance is a mechanism for imposing liability to a fiduciary relationship when there is a breach of trust. Liability is from a 'meaning lack of honesty'. Four elements:

1. Fiduciary Duty
2. Fraudulent and Dishonest Breach of Duty by Fiduciary
3. Actual Knowledge by the stranger to the Fiduciary of the relationship and conduct
    a. Suspicion that fiduciary was up to no good is not sufficient
4. Participation by/Assistance of stranger in the dishonest conduct

Analysis:

Knowing assistance is a mechanism to impose liability on strangers of a fiduciary relationship who participate in a breach of trust by the fiduciary. Strangers to these relationships are made liable for their "want of probity" or "meaning lack of honesty". In this case, Ms. Duscio was the stranger and the fiduciary relationship is between Catan and Pension fund.

1. Fiduciary Relationship
    a. Trustee relationship cements fiduciary
    b. Catan was holding funds in trust for Pensionfund – fiduciary
2. Fraudulent Conduct
    a. Trustee must be acting fraudulently
    b. Catan dissipated the funds fraudulently
3. Actual knowledge by the stranger of the fiduciary
    a. Needs *actual* knowledge of the fiduciary relationship and the fraudulent conduct
    b. Wouldn't be enough if Ms. Duscio suspected was something suspicious was going on. Instead, she must know Catan held funds as a trustee and that she was participating Catan in fraudulent conduct with those funds.
    c. Actual knowledge also satisfied if reckless or wilfully blind.
    d. Wilful blindness is subjective and thus depend on the strangers state of mind
        i. Objective standards better suited for negligence
    e. The trial judge mistook wilful blindness for constructive knowledge – she knew of things going on, but he did not make any finding if she suspected the trust money was being employed in a fraudulent way. He applied an objective standard, and in this regard he erred.
        i. No evidence that Ms. Duscio knew of the frauds occurring
4. Participation or assistance of the stranger in the fiduciary's fraudulent conduct
    a. She did not know and thus could not participate

Conclusion:

No liability in knowing assistance

Issue:

Is Mrs. Duscio personally liable for knowing receipt?

Rule:

Test for knowing receipt:

1. Stranger receives trust money
2. For his/her benefit or in his/her personal capacity
3. With actual or constructive knowledge it was being misapplied

Analysis:

Liability rests in restitution, not wrongdoing. So, even if knowing assistance is not made out, knowing receipt can be, and it requires a lower level of knowledge. Constructive knowledge based on knowledge of the facts by a reasonable person may ground restitutionary liability.

1. Stranger receives trust property
    a. Ms. Duscio received trust property from Catan
2. Received for his/her benefit or in their personal capacity
    a. Easily established
3. With actual *or* constructive knowledge the trust fund is misapplied
    a. Again, wilful blindness or recklessness will also satisfy this, but this time applied objectively
    b. If the recipient, having knowledge of the facts which would put a reasonable person on inquiry, actually fails to inquire as to the possible misapplication of the trust property.
    c. Ought Ms. Duscio to have known that she had received the funds from the Pensionfund from Catan?
    d. The trial judge found that Ms. Duscio continued to sign cheques for very large quantities of money as proof of assistance. The finding of liability would require Ms. Duscio to do so between the Pensionfund and Catan accounts, but there is no proof she did this after the funds were deposited

i. There is no evidence Ms. Duscio had any knowledge in transfers
ii. Her signing authority was not linked to the trust money

Conclusion:
Insufficient factual findings – new trial ordered.

Hold, Order:
Appeal allowed for knowing assistance; new trial ordered for knowing receipt.

Ratio:
Teste for knowing assistance:
1. Fiduciary Duty
2. Fraudulent and Dishonest Breach of Duty by Fiduciary
3. Actual Knowledge by the stranger to the Fiduciary of the relationship and conduct
    a. Subjective; wilful blindness and recklessness count
4. Participation by/Assistance of stranger in the dishonest conduct

Test for knowing receipt:
1. Stranger receives trust money
2. For his/her benefit or in his/her personal capacity
3. With actual or constructive knowledge it was being misapplied
    a. Objective; wilful blindness and recklessness count

This is a long and complex factual scenario, and thus the application gets tricky. For our purposes, Ms. Duscio analysis is the only informative one – the other people involved were obviously involved in fraudulent conduct

- For Knowing Assistance, it is a higher standard. Need four criteria to be met:
    (a) Fiduciary Duty
    (b) Fraudulent and Dishonest Breach of Duty by Fiduciary
    (c) Actual Knowledge by the stranger to the Fiduciary of the relationship and conduct
        i. Subjective; wilful blindness and recklessness count
        ii. Not trying to attribute constructive knowledge to a stranger. Underlying assistance is fraud, which needs subjective intentions to ground liability
        iii. Was the stranger assisting the corporation in a fraudulent or dishonest way?
        iv. This includes "deliberate ignorance" where the subject suspects relevant facts but deliberately chooses not to inquire
        v. "Did the accused shut his eyes because he knew or strongly suspected that looking would fix him with knowledge?"
    (d) Participation by/Assistance of stranger in the dishonest conduct

- For Knowing Receipt, it is a more relaxed mental standard. Needs three criteria to be met:
    (a) Stranger receives trust money
    (b) For his/her benefit or in his/her personal capacity
    (c) With actual or constructive knowledge it was being misapplied
        i. Objective; wilful blindness and recklessness count
        ii. Can include recklessness and wilful blindness, but also knowledge that a reasonable person would have inquired (but this person didn't)

Overview of how to "pierce the corporate veil"
(1) *Salomon*: Corporation is a separate legal entity
(2) *Kosmopoulos*: veil will not be recognized when it is too flagrantly opposed to justice
    (a) This is a background principle, not a workable test (*Driving Force*)
(3) *Transamerica*: workable test. Courts will disregard the separation where the corporation is

(a) Being controlled by a specific entity (other corporation or director/officer) and
(b) Being used as a shield for fraudulent behaviour

(4) The *Transamerica* test is not concrete, it can be amended to accommodate different cases
    (a) Parent company (*Chevron*)
    (b) Family law (*Aubin*)
    (c) Used to perpetuate fraud (*Big Bend*)
    (d) Corporation directed to do the wrong thing (*Ren*)
    (e) Disregard of formality (*Wolfe*)
    (f) Thin capitalization (not in Canada)
    (g) Liability under trust law (*Garcia*)
        (i) Knowing receipt
        (ii) Knowing assistance

(5) It should be remembered that courts will resist piercing the veil. All the above cases are very much the exception(s) not the rule(s).

CHAPTER 5: TORTIOUS, CRIMINAL, REGULATORY & CONTRACTUAL LIABILITY OF THE CORPORATION

This chapter deals with situations where the corporate entity, as a separate legal entity, has primary liability under either tort, criminal law, regulatory law, or contract

- When will the corporation have liability when an individual acts tortiously or criminally?
- When is the employee sufficiently attached such that their liability is also the liability of the corporation?

This is kind of like the opposite of piercing the corporate veil.

- Piercing the corporate veil was to find individual liability in a person beyond the liability of the corporation
- This is about finding corporate liability from individual wrongful behaviour

	Individual Liability	Corporate Liability
Contract Law	Bob enters contract Bob has primary, personal liability	N/A
Tort Law	John commits tort John has primary, personal liability	ABC Inc commits a tort ABC Inc has primary liability established by the directing mind doctrine
Criminal Law	Bill commits crime Bill has primary, personal liability	XYZ Inc commits a crime XYZ has primary liability established through the directing mind doctrine as modified by the *Criminal Code*

A corporation can't enter into a contract on it's own, so that is why it is N/A. Corporate entities can only enter into contract via an agent. But agency makes everything more complicated…

	Individual Liability via Agency	Corporate Liability via Agency
Contract Law	Bob's agent, at Bob's request, enters contract Bob has primary, consensual liability if the agent has actual/ostensible authority	ABC Inc's agent enters into a contract ABC Inc is bound if the agent has actual or ostensible authority
Tort Law	John's agent/employee commits a tort in the ordinary scope of their employment John has non-consensual, vicarious liability	XYZ Inc's agent/employee commits a tort in the ordinary course of employment. XYZ Inc has non-consensual, vicarious liability

Criminal Law	Bill's agent commits crime (not at Bill's request/direction) Bill has no liability	N/A

Attributing Liability to a Corporate Body

The "Rhone" v The "Peter AB Widener", [1993] 1 SCR 497

Facts:
North Central (plaintiff) owned the ship, the Rhone. The Rhone was struck by a barge, the Widener which was a 'dead ship (without motor) and being towed by 4 tugboats, all owned and operated by Great Lakes (corporate defendant)

- Captain Kelch (individual defendant) was employed by Great Lakes and was the master of the 4 tugs. The negligence of the Kelch caused the collision.

North Central brings action against Great Lakes and Kelch

- Section 647 of the *Canada Shipping Act* awards limited liability for acts/omissions of the ship operator where injury occurred without their actual fault

Procedural History:
Trial judge found the defendant personally liable, not allowing the statutory defence of s647

- Federal Court of Appeal upheld this finding.

Issue:
Is Captain Kelch a directing mind of the corporation, such that his acts should be attributed to the corporation?

Rule:
Section 647 of the *Canada Shipping Act*
(2) The owner of a ship, whether registered in Canada or not, is not, where any of the following events occur without his actual fault or privity, namely,
(d) where any loss or damage is caused to any property, other than property described in paragraph (b), or any rights are infringed through
(ii) any other act or omission of any person on board that ship
liable for damages beyond the following amounts

Analysis:
The owner of the tugs was Great Lakes – did the accident happen without the corporation's actual fault or privity. How do we know the state of mind of a corporation?

- Identifying individuals within a corporate structure as a directing mind is a question of mixed law and fact.
  - Legal issue: which functions/offices ground corporate identification?
  - Factual issue: who carries out these functions or fills these offices?
- In *Canadian Dredge*, "identification theory" was used – the employee who physically committed the offence must be the 'ego' of the corporate personality, the 'vital organ' of the body corporate. There can be multiple directing minds

In this case, the focus must be whether the impugned individual has delegated the 'governing executive authority' within the scope of their authority. If discretion conferred on an employee amounts to express/implied delegation of executive authority to design and supervise the implementation of corporate policy rather than simply carrying out such policy.

- Negligence of a shipmaster for navigation does not amount to actual fault for the corporate shipowner.
  - The shipmaster was clearly negligent
- Court has to consider whether the corporation breached duty to supervise or manage vessels properly, or whether the shipmaster's faults are the faults of the corporation because of his spot in the hierarchy.

- Kelch had important duties, and some decision-making (navigating) but the evidence does not show that he held 'governing executive authority'
- The key factor that distinguishes employees and directing minds is the capacity to exercise decision-making authority on matters of corporate policy, rather than merely to give effect to such a policy on an operational basis, whether at head office or elsewhere.
  - His responsibilities were more of port captain subject to supervision responsibilities. He had 25 years experience so this makes sense
  - However, these are not so much to give him executive authority over management of the fleet – this remained with the corporation.

The collision did not occur with the actual fault of the corporation.

Conclusion:

Not directing mind of Great Lakes; not fault of Great Lakes under s647(2)

Hold, Order:

Appeal allowed

Ratio:

The key factor that distinguishes employees and directing minds is the capacity to exercise decision-making authority on matters of corporate policy, rather than merely to give effect to such a policy on an operational basis

How are you supposed to judge what is going on in the mind of a corporation to ground an objective liability, like negligence? In this case, the legislation limited liability, and Great Lakes wanted to benefit from it, so they argued Kelch was not a directing mind of Great Lakes

- If Kelch was a directing mind, then Great Lakes and Kelch are at fault
- If Kelch was not a directing mind, then Kelch is the only one liable

Canadian Dredge is no longer the test for liability, but pieces or it are useful.

- Directing minds need to be found through governing, executive authority
- Authority in the corporation to set high level policy, design it and supervise implementation of it
  - Simply carrying out policy is a task of normal employees and cannot ground liabilty on the corporation
- While Kelch obviously had important responsibilities, his decisions were not making policy, but executing it.

The key factor to distinguish normal employees and directing minds is the capacity to exercise a certain amount of authority rather than implement it.

Deloitte & Touche v Livent Inc (Receiver of), 2017 SCC 63

Facts:

Deloitte was retained by Livent to conduct statutory audits. Deloitte did so negligently, failing to detect that Livent's two directors (Drabinsky and Gottlieb) fraudulently manipulated their financial records (they recorded "imaginary revenue" and "cooked the books" as assets to defraud Livent)

- After the audits, Livent appointed new managers who discovered the fraud.

Livent became insolvent and sued Deloitte for their negligent audits, arguing the incompetent audit meant its management was not properly supervised and Livent's liquidation deficit was larger than it otherwise would have been

Issue:

Was Deloitte liable for their negligent audits of Livent?

Rule:

Illegality Defence

1. Wrongdoer must be directing mind

2. Wrongful actions must have been done in the scope of their authority

Analysis:

Deloitte's Argument:

The defence of illegality bars an otherwise valid action in tort on the basis that the plaintiff engaged in illegal/immoral conduct and should not recover. The Manager's illegal conduct should be attributed to Livent, based on identification theory and provide a full defence of negligence.

Livent's Argument

Deloitte was hired as an auditor for the very purpose of discovering issues with the finances of the corporation including, wrongful and illegal conduct.

Defence: Illegality

To ground this defence, the fraudulent directors need to be attributable to Livent (basically establish corporation liability). The test for corporate identification (to attribute fraudulent acts of an employee to its corporate employer):

1. Wrongdoer must be the directing mind of the corporation
2. Wrongful actions of the directing mind must have been done within the scope of his/her authority. His/her actions must be performed within the sector of the corporate operation assigned to him

The individual will be considered a directing mind unless the action (1) was totally in fraud of the corporation and (2) was not by design or result partly for the benefit of the corporation.

- The two wrongdoers were directors and their actions were within the scope of their authority
- While the acts were fraudulent, they were genuinely designed to assist Livent by trying to prolong its life by saying it had more financial resources than it actually did

Technically, public policy can sometimes favour imputing the corporation with the actions of it's directing minds in certain criminal prosecutions. But this may not always be the case for a civil suit of an auditor's negligent preparation of a statutory audit.

- The point of a statutory audit is to provide a means to find fraud and wrongdoing. Denying liability on the basis that an individual within the corporation has engaged in the action the auditor was enlisted to protect would render the statutory audit meaningless.
- *Dredge* finds a sufficient basis to find actions of the directing mind attributable to the corporation, but not a necessary one.
- Courts retain discretion to refrain from applying it where it would not be in the public interest to do so. If applying the directing mind would, as is this case, render the duty of care meaningless, it would not be in the public interest.
  - If a professional undertakings a service to detect wrongdoing, the existence of the wrongdoing should not bar the civil liability of negligence through corporate identification.

Technically, if we applied the directing minds test in certain criminal prosecutions, it would undermine the whole policy of statutory audits (they would become meaningless). There are public policy considerations to consider

Defence 2:

Conclusion:

Defence made out but will not apply.

Hold, Order:

Application allowed.

Ratio:

While directing mind can be used to identify corporate liability, it does not have to if contrary to public policy, even if the corporate identification would otherwise be made out.

This case can be used to combat the idea of directing mind. So, even if the directing mind is made out, and corporate liabilty can be made out, it should not if it is contrary to public policy considerations. In this case, while the directors fulfilled the directing mind test, to hold the corporation liable while they are hired Deloitte to find the fraudulent activity would not make any sense. What would be the point of having the audit at all, especially if statutorily mandated, if they could be liable for the fraud they are trying to find?

- As such, corporate identification theory is premised on the idea that we are trying to fix corporate acts to the person, and out came the Directing Mind test.
- Which individuals exercise governing executive authority, the authority of design and supervision of policy, not the implementation.
- Directing mind can be with more than one person, but there are situations where courts have the discretion to refrain from using the test when it is against public interest.

Criminal vs Tortious Liability
Criminal liability for corporations has recently changed with amendments to the *Criminal Code* in 2018. There has been little litigation since to expand on the amendments.

Historically, criminal liability was with *Canadian Dredge* (directing mind test). This led to a lot of difficulty prosecuting corporations since both actus reus and mens rea would have to be identified with one individual in particular. This became unworkable.

- Corporations have a distribution of decision-making authority
- One individual in the corporation may know the requisite information, but another individual could have done the criminal act.
    - Directing mind had to commit the crime (actus reus) but also have the mens rea for it.

As a result of these difficulties, and a huge mining disaster with many worker deaths, the *Criminal Code* was amended to find more responsibility that could not have been established by the old test.

Criminal Code, RSC 1985, c C-46
Section 22.1 In respect of an offence that requires the prosecution to prove negligence, an organization is a party to the offence if (a) acting within the scope of their authority (i) one of its representatives is a party to the offence, or (ii) two or more of its representatives engage in conduct, whether by act or omission, such that, if it had been the conduct of only one representative, that representative would have been a party to the offence; and (b) the senior officer who is responsible for the aspect of the organization’s activities that is relevant to the offence departs — or the senior officers, collectively, depart — markedly from the standard of care that, in the circumstances, could reasonably be expected to prevent a representative of the organization from being a party to the offence Section 22.2 In respect of an offence that requires the prosecution to prove fault — other than negligence — an organization is a party to the offence if, with the intent at least in part to benefit the organization, one of its senior officers (a) acting within the scope of their authority, is a party to the offence;

(b) having the mental state required to be a party to the offence and acting within the scope of their authority, directs the work of other representatives of the organization so that they do the act or make the omission specified in the offence; or
(c) knowing that a representative of the organization is or is about to be a party to the offence, does not take all reasonable measures to stop them from being a party to the offence.

Section 2
In this Act,

representative, in respect of an organization, means a director, partner, employee, member, agent or contractor of the organization;

senior officer means a representative who plays an important role in the establishment of an organization's policies or is responsible for managing an important aspect of the organization's activities and, in the case of a body corporate, includes a director, its chief executive officer and its chief financial officer

Section 22.1 ground negligence claims. What s22.1(a)(ii) means is that the mens rea and actus reus could be identified in separate individuals and still ground liability.

- The 'senior officer' of (b) is broader than the common law understanding of 'governing executive authority'. As long as they depart from the standard of care, can look to a representative
  - For the standard of care, can look to the officer's conduct, even if the representative conducted the actus reus
- The act can be performed by the representative and not only the governing executive authority and still ground liability in the corporation.

Section 22.2 finds fault other than in cases of negligence. Have to show that the senior officer is party (ie, acting in their authority) and had the mental state required for it. They also need to direct the representative to do the act or omission or fails to take steps to prevent them from doing to.

The *Code* defines representative and senior officer. Senior officer is broader than the 'governing, executive authority' from the directing mind test.

- Unclear how far down the corporate letter we go until someone is no longer a senior officer.

The *Metron* case is notable because the Crown's burden of proof under the revised test for corporate criminal negligence outline was collapsed into the conduct one person. The site supervisor was the representative and the senior officer, so it doesn't really clarify the law a ton.

- In that case, Metron was contracted to restore balconies in high rises, and hired a manager and site supervisor. The platforms made weren't properly constructed (it was only safe for 2 people but there were 6 people on it)
  - As a result, the platform collapsed and many people died.
- The prosecution proceeded on the basis that the supervisor conduct had the actus reus and the mens rea for the prosecution, as he was the representative and a senior officer
  - But Metron plead guilty so there isn't a lot of judicial guidance
  - The senior officer likely wouldn't have been captured under the common law officer test

Deferred Prosecution Agreement ("DPA"): voluntary agreements that are negotiated between an accused and the Crown to resolve corporate wrongdoing as an alternative to long and costly prosecutions. The effort of a DPA is that the outstanding investigation or prosecution is suspended, in exchange for certain undertakings that the corporation must fulfill in order to have the charges dropped.

DPAs often require full co-operation with the relevant law enforcement authority and an admission of guilt, fines and governance reform.

Regulatory Offences

Statutory offences can be described as quasi-criminal. They prohibit action or conduct that is contrary to the public interest. Most of these, in the corporate world, are related to pollution or environmental degradation. Often, you can impose liability to the corporation, but also the officer.

- However, liability always depends on the statute. The statute should always be looked at first.

There are three types of offences:

- Absolute Liability: Liability arises instantly on the breach of statutory prohibition and no particular state of mind is a prerequisite to guilt (no mens rea required)
    - Corporations and individual officers stand on the same footing so there is no need to establish any rules of corporate liability
- Strict Liability: Liability arises on the establishment of the actus reus, subject to the defence of due diligence.
    - The offence is primary (corporation can be held directly liable) so the corporation and individual are in the same position.
- Mens res Offences: traditional criminal offences for which the accused may be convicted only if the requisite mens rea demonstrated by the prosecution.
    - Look to the *Criminal Code* for these offences.

The Crown always has the burden of proof to establish that the actus reus occurred (the statute was violated), but in strict liability, the burden then shifts to the defendant to establish due diligence defence.

R v Bata Industries, (1995), 25 OR (3d) 321 (CA)

Facts:

Thomas Bata, Douglas Marchant and Keith Weston (individual defendants) were directors and officers of Bata Industries (corporate defendant), a shoe manufacturing company

- Government officials conducted an inspection of the factory, and found chemical waste that was not stored in accordance with environmental regulations
- Bata and the individual defendants were charged with 4 offences under the *Environmental Protection Act* and 2 offences under the *Ontario Water Resources Act*

Issue:

Can Bata or any of the individual defendants establish due diligence?

Rule:

Strict Liabilty offence: Crown has burden BARD to prove *actus reus* and once they do this, they are presumptively relieved of proving anything further.

- Defence of due diligence available

Analysis:

<u>Establishment of Offence</u>

Actus Reus

- Actus reus of these charges is engaging in an activity that may or does discharge – obviously established

<u>Defence of Due Diligence for Corporation Culpability</u>

The defence requires Bata to exercise all reasonable care. Bata did not establish a proper system to prevent the leakage, nor take reasonable steps to repair the defective system they had. They permitted the barrels to sit, rust and disintegrate.

- In terms of the corporation, Bata did not establish that it took all reasonable care. It did not have a proper system to prevent spilling, nor did they take reasonable steps to ensure the operation of whatever system they had worked.
- Liability for the corporation is maintained

Liabilty of the individual defendants - Legal Standard

The statute puts individual liability on directors as well as the corporation. The minimum profile developed against which I find the directors' liability should be measured. It is ok for the directors to delegate responsibility (they don't have to be there all day long), but the directors have to ensure adequate oversight and supervision. This requires reporting system to them. So, delegating responsibility does not negate responsibility of the directors.

1. Did the board of directors establish a pollution prevention system
    a. Supervision, inspection, improvement in business methods
2. Did each director ensure the corporate officers have been instructed to set up a system sufficient with the industry to ensure compliance of environmental laws
3. The directors are responsible for reviewing environmental reports
4. The directors should be aware of industry standards
5. The directors should immediately *and personally* react when they see the system fails
    - Mr. Bata was more corporate and rarely came in
        - When the chemical problem occurred, Bata directed the money to minimize the impacts. He reviewed it and was not wilfully blind.
        - He was entitled to believe the site manager would keep going and report any further difficulties.
        - To the extent of his responsibilities, he took reasonable steps
        - He has established due diligence
    - Mr. Marchant was at the facility more frequently, about once a month
        - An employee brought the issue to his *personal* attention. He knew of this for 6 months and took no steps to view the site and assess the problem.
        - The system was made no safer or steps taken to contain it
        - He had a responsibility to give orders but also ensure they were executed to minimize damages. His delay was inadequate
        - He has not established due diligence – conviction
    - Mr. Weston was the onsite manager
        - He was aware of toxic chemicals and environmental responsibilities.
        - As on-site director, he had the responsibility to personally inspect the site regularly, as is industry standard.
        - He had an obligation, if he chose to delegate responsibility, to ensure the delegate received necessary training on inspection and reporting
        - He has not established due diligence – conviction

Conclusion:

Due diligence only made out for Thomas Bata

Hold, Order:

Bata, Marchand and Weston guilty

Ratio:

Responsibility can be delegated to site employees, but the directors are responsible for the delegation, supervision and reporting being adequate.

This case established the burden sharing of strict liability offences; Crown to prove actus reus, Defence to prove the defence. It also establishes that due diligence requires more than 'reasonable steps to take all reasonable care'. The standard is slightly higher:

(1) Was there a proper, reasonable standard set up?
(2) Was there all reasonable care to ensure the system was carried out in an effective way?

(a) This involves timely reporting, timely oversight, in cases with delegation urging the employees to act
(b) Industry practices will be considered when considering the defence

The ONCA also allows responsibilities needed in the execution of reasonable care to be delegated to other employees, but the directors still have a responsibility to ensure the delegation and reporting is adequate.

- The onsite manager tried to argue that the managers were incentivized to cut costs, so that could explain Weston's response to the quote to solve the contamination.
    - However, this incentive structure makes it very hard to establish due diligence.
    - If you say "I was worried about my bonus", that won't negate or lower the need for due diligence, nor its requirements.

R v Syncrude Canada Ltd, 2010 ABPC 229

Facts:
Syncrude discharged bitumen tailings into ponds in it's oilsands operations. An investigation revealed that 1600 migrating ducks were trapped in the bitumen on the surface of one of their basins and died.

- Syncrude was charged with failing to store a hazardous substance in a manner that did not come into contact with animals against s 155 of the *Environmental Protection and Enhancement Act*
- They were also charged with depositing a substance harmful to migratory birds, contrary to s 5.1 of the *Migratory Birds Convention Act*.

Issue:
Is Syncrude liable for violating the legislation?
Did Syncrude establish due diligence for deterring birds from landing on tailings ponds?

Rule:
Section 5.1 of the *Migratory Birds Convention Act*
(1) No person or vessel shall deposit a substance that is harmful to migratory birds, or permit such a substance to be deposited, in waters or an area frequented by migratory birds or in a place from which the substance may enter such waters or such an area.

Analysis:
<u>Actus Reus</u>
The birds came into contact (area frequented by birds) with the bitumen in Syncrude's tailings ponds. Actus reus made out.
<u>Due Diligence</u>
If Syncrude can establish that it could not have reasonably foreseen the contravention of the statute, the defence can be establish. Syncrude's actions must be judged on the basis of the information available to it at the time of the offence.

- In the case of an individual's liability, if the act took place without the director's direction, wilful involvement is negated. The director must also exercise all reasonable care by establishing a proper system to prevent an offence and by taking reasonable steps to ensure the system is operating properly.
- In the case of the corporation's liability, the defence will depend on if the due diligence was taken by those who are the directing mind and will of the corporation, and their acts are, in law, the acts of the corporation itself.

Complexity of the issue:

- Volume of tailings is massive and there are a large number of birds in the migration.
- Given the complexity, Syncrude asked the Bird and Environmental Team to look into it. But they did not have sufficient expertise or training in the area.

Prevention system:

- Have to show reasonable steps were taken to see this system through.
- Syncrude had documents to set out procedures for bird deterrence
- But the documents were not comprehensive and inadequate to reflect the complexity of bird deterrence
    - There was no schedule to implement the system
    - They did not have enough noise cannons to satisfy their own documents
    - Budget cuts to the deterrence team meant many of the employees were cut
    - The program was started too late and inadequately

Alternative Solutions:
- There is no real industry standard for these tailings ponds, but Shell and Suncor were available to deploy adequate deterrence in early April
- They had more comprehensive procedures, oversight, training and planning
    - Syncrude need not implement these systems, but it does show that clearly better alternatives existed.

Foreseeability:
- Due diligence does not require clairvoyance of the possible failures
- But, Syncude's management should have foreseen that a spring storm in April is not out of the norm
- There is a reasonable understanding the birds would be there in April, and land on the ponds, particularly during a storm
- A reasonable person in Syncrude's position would have foreseen the failure to deploy the mechanisms created an unacceptable hazard for the waterfowl

De minimis argument:
- Syncrude's argument that 1600 dead birds is negligible because many more are hunted every year is egregrious
- The conduct was not minimal; birds die in the oil sands, but the deterrence was insufficient and the amount of dead birds was much larger

Conclusion:
Due Diligence not established; Syncrude liable

Hold, Order:
Fined under both provincial and federal acts
- Additional $1.3 million to UofA bird conservation; $900,000 to Alberta Conservation Agency and $250,000 to College to establish a diploma in environmental agency

The de minimis argument was greeted very poorly in the public light. It is a possible argument, but a pretty bad reading of the room, and likely part of the steep charges ordered by the Court. The Prevention System is the biggest weakness however. Even if Syncrude had a stellar system in pace, did the Board of Directors have effective oversight to ensure the system is carried out properly
- Normally in a case like this, the directing mind would have to be identified, but in a company as large as Syncrude, they undoubtedly had a Board.
- The Board could delegate responsibilities, but they needed the oversight to ensure it was properly executed.

Regulatory offences aren't considered piercing the corporate veil in the common law sense, since it is statutory. So, these directors are liable, not through piercing the corporate veil, but through statute, which is another way to find individuals in the corporations as liable.

Contractual Liability: Doctrine of *Ultra Vires*
Under contract law, a corporation's contractual liability is tied to:

- Doctrine of *ultra vires*: describes a class of acts of a body that are beyond its powers or jurisdiction. The corporation cannot act outside the scope of its powers as stated in the original acts of the constituting documents
- Doctrine of constructive notice: is knowledge of a fact that is presumed/imputed by law. At common law, a person who is dealt with a corporate body was deemed to have notice of the contents of all documents that the corporation was required to file with, and did file with, a public office that were open to public inspection (including constituting documents)
    - This was more relevant when constituting documents used to actually state the objectives of the corporation, and the scope of the corporation's power

Both of these doctrines have been heavily modified by statute, but they still have some grounding.

Re Jon Beauforte (London) Ltd [1953] 1 CH 131

Facts:

Jon Beauforte's memorandum of association (equivalent to constituting documents) were to "carry on business of costumers, gown-makers and related activities". The company then started making veneered panels without amending this clause

- They entered into various contracts for the veneer business including a fuel supplied
- The company then went into liquidation and its creditors, including the fuel company, sought to collect on its debts

Issue:

Are the creditors of the company entitled to be paid under the contracts?

Analysis:

The company tried to argue that the contract was outside the memorandum of association, so the corporation never had the power to enter into this contract. The creditors argued that the contract was used in a legitimate business so it should not matter if outside the contract.

- However, the fuel supplied had constructive notice of the memorandum of association and thus had notice that the transaction was ultra vires of the company.

Conclusion:

Defendant corporation not liable.

Hold, Order:

Action dismissed

Ratio:

Parties to a contract are deemed to know the contents of publicly filed documents at the company registry, whether or not they actually did this or not.

The public reaction to this was not particularly favourable, as it was seen as quite harsh. In response, the *ABCA* was amended to effectively eliminate the doctrine of *ultra vires* in Alberta.

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 16 (1) A corporation has the capacity and, subject to this Act, the rights, powers and privileges of a natural person. (2) A corporation has the capacity to carry on its business, conduct its affairs and exercise its powers in any jurisdiction outside Alberta to the extent that the laws of that jurisdiction permit. Section 17

(1) It is not necessary for a bylaw to be passed in order to confer any particular power on the corporation or its directors.
(2) A corporation shall not carry on any business or exercise any power that it is restricted by its articles from carrying on or exercising, nor shall the corporation exercise any of its powers in a manner contrary to its articles.
(3) No act of a corporation, including any transfer of property to or by a corporation, is invalid by reason only that the act or transfer is contrary to its articles or this Act.

Section 18
No person is affected by or is deemed to have notice or knowledge of the contents of a document concerning a corporation by reason only that the document has been filed by the Registrar or is available for inspection at an office of the corporation.

Section 18 is a statutory repeal of constructive knowledge, and s 17(3) is basically a repeal of the doctrine of *ultra vires*. However, these doctrines are only repealed for corporations under corporations acts (like the *ABCA* , *CBCA*). These doctrines still apply to those incorporated under special acts (through statutory instruments like public bodies).

Communities Economic Development Fund v Canadian Pickles Corp. [1991] 3 SCR 388

Facts:
The Communities Economic Development Fund ("CEDF", plaintiff) was created by statute. The statute provided that the CEDF was made to encourage the economic development of "remote and isolated communities".
- CEDF loans money to the Canadian Pickles Corporation (corporate defendant). Mr. and Mrs. O'Donnell (individual defendants) guaranteed the loan.
- However, the corporation operates 20km outside Winnipeg, so is not really remote.

Issue:
Is the loan to the corporate defendant *ultra vires*? Are the individual defendants liable as guarantors?

Rule:
Section 9 of *The Communities Economic Development Fund Act*:
(7) No loan shall be made under this Act, or financial assistance given under this Act if the making or giving thereof contravenes any provision of this Act

Analysis:
The doctrine of *ultra vires* has been repealed by statute since it did not protect investors and a trap to the unwary. However, some aspects of the doctrine may be kept for corporations created by special act for public purposes.
- It protects public interest because a company created for a specific purpose of a legislature ought not to have the power to do things in furtherance of that purpose. *Ultra vires* applies in a case like this.
- The loan contravened s9(7) since it did not go to a remote or isolated community. As such, it is *ultra vires* of the CEDF to make

Conclusion:
Loan is *ultra vires*

Issue:
Are the individual defendants liable as guarantors?

Rule:
Liability can be grounded by guarantors

Analysis:

The loan was *ultra vires* by virtue of contravening s9(7). Since the loan was *ultra vires*, so to is the guarantee. As such, it has no effect and the individual defendants cannot be liable.

Conclusion:

Not liable to repay because the principal debt is *ultra vires*

Hold, Order:

Loan of no effect.

Ratio:

Doctrine of *ultra vires* is maintained in public bodies created by a special act of legislature fulfilling a public purpose, unless provisions otherwise state.

Though this case confirms that *ultra vires* still exists from statute, the *ABCA* otherwise repealed it. It confirms that the first step is to always look at the corporation.

<u>Indoor Management Rule</u>

Even when *ultra vires* was the common law, courts were be loath to require third parties who contract with a corporation to enquire into compliance by a corporation of its directors and officers, or the other internal rules of management that governs the conduct of the business or affairs of the corporation.

- These rules might govern the directors or officers and may entitle a corporation or its shareholders to restrain them from acting in contravention or to seek damages should those rules be broken, but they were not a matter which the general public had need to concern itself.

Basically, because the corporation did not comply with it's own internal requirements does not mean that contracts with third parties are void.

- There is no requirement that the third party has to inquire into these requirements prior to contracting.
- However, at common law, if they had knowledge of the internal rules and contracted anyway, they cannot rely on the Indoor Management Rule.

The Indoor Management Rule has now been captured in statute:

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 19 A corporation, a guarantor of an obligation of the corporation or a person claiming through the corporation may not assert against a person dealing with the corporation or dealing with any person who has acquired rights from the corporation (a) that the articles, bylaws or any unanimous shareholder agreement have not been complied with, (b) that the persons named in the most recent notice filed by the Registrar under section 106 or 113 are not the directors of the corporation, (e) that a person held out by the corporation as a director, an officer or an agent of the corporation (i) has not been duly appointed, or (ii) has no authority to exercise a power or perform a duty that the director, officer or agent might reasonably be expected to exercise or perform, (f) that a document issued by any director, officer or agent of the corporation with actual or usual authority to issue the document is not valid or not genuine, or unless the person has, or by virtue of the person's position with or relationship to the corporation ought to have, knowledge of those facts at the relevant time.

Section 19 ensures that the enforceability of a contract cannot be denied because of non-compliance with internal bylaws, unless they knew or ought to have known the requirements were in place and not met. Aka, a codification of the Indoor Management Rule.

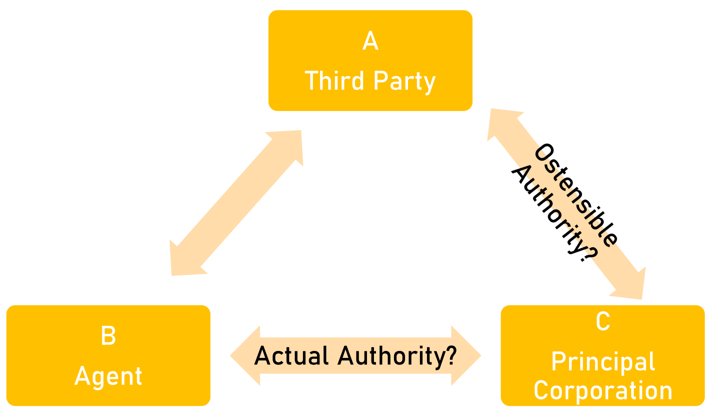
Contracting with Agents of the Corporation

Treating corporations as a natural person is not totally accurate, because corporations, on their own, cannot contract themselves. They must do so via an agent.

- Principals have an authority relationship with an agent, such that the agent can enter a contract with a third part which binds the principal.

Authority can be either apparent or actual.

- Actual Authority:
  - Express: authority given orally or in writing
  - Implied: what is necessarily or normally incidental to the activity expressly authorized
- Ostensible/Apparent Authority: a representation made by the Principal to the 3rd part about the agent's authority



If the Agent has actual or ostensible authority, they can enter into a contract on behalf of the Principal Corporation and bind the corporation contractually.

- Internal: Corporation grants actual authority to the Agent either expressly or impliedly
- External: Corporation holds out to the 3rd party that the Agent has ostensible authority to act on the corporation's behalf

Questions from this inevitably arise:

- When can a Principal Corporation avoid being contractually bound by claiming that its Agent didn't have actual or ostensible authority?
- How can the Principal Corporation make representations about the agent having ostensible authority?
  - Has the Principal clothed the agent with authority through representations made to the third party?
  - Representations need to be traced back to someone who has actual authority such that they clothe the agent with apparent authority

We really only care about the corporation-agent-third party relationship in these questions.

Panorama Developments (Guildford) Ltd v Fidelis Furnishing Fabrics Ltd, (1971) 3 A11 ER 16 (CA)

Facts:
Panorama (plaintiff) runs a car hire business called 'Belgravia Car Hire'. They have a flight of high-end cars and let them out on hire as a 'self drive' hire.

- Fidelis (defendant) are a company of excellent credit. Mr. Mavrogordata is the managing director. Fidelis appointed Bayne as a secretary.

Bayne contracted with Belgravia to drive the cars and paid them with his own private account. This was fine and gave a list of dates they wanted the cars in the future. He asked them to charge the Fidelis account. They sent the cars on the dates. Bayne would always sign the contract.

- But Fidelis never paid for them. This was all done when Mr. Mavrogordata was gone

When Mr. Mavrogordata returned, he discovered the frauds, that Bayne was using the cars on his own and involved the company in the debts. Bayne was prosecuted and imprisoned.

- Belgravia now sues Fidelis for the hire due. Fidelis argued Bayne had no authority to hire them.

Procedural History:
Trial judge sided with Panorama. Fidelis appealed.

Issue:
Is Fidelis a party to the contract with Panorama, and thus liable for the frauds perpetrated by Bayne? Did Bayne have authority to bind Fidelis under the contract with Panorama?

Analysis:
The parties intended for the contract to be between Fidelis and Panorama. Fidelis would thus only be obligated to pay under the contract if Bayne had actual or ostensible authority; does a "corporate security" have the authority to bind the corporation?

- A corporate security has extensive duties and responsibilities.
- He would be entitled to sign contracts connected with administrative duties, like hiring, ordering and so forth.
- Given this, he has the ostensible authority to enter into contracts for the cars

Bayne performed tasks in the power of the company's secretary. He had been clothed with ostensible authority by Fidelis to enter into the hire contracts on their behalf, and the company must thus pay for them. Panorama surely would have assumed he had authority. Fidelis thus represented to Panorama that Bayne had the authority to the contracts.

- Bayne did the fraud, but the company put him in the position in which he was able to do them, as company secretary.

Conclusion:
Company liable for employee fraud; Bayne had ostensible authority to bind Fidelis

Hold, Order:
Appeal dismissed

Normally, the analysis should look like:

1. Does Bayne have actual authority?
    a. Secretary would usually have actual authority
    b. Would need to know if the authority was express or implied
        i. If a contract expressly said the scope of his authority, there can also be authority that is necessarily implied in exercising the authority
            1. A salesperson is agent for the corporation with certain responsibilities. What if the contract is silent on whether the salesperson can make representations on a certain project? You could infer that the person has implied authority to do so as normal functioning of their job.

2. If not, does Bayne have ostensible authority?
    a. He has been granted a position that has extensive authority typical of these agreements.
    b. By granting this title, the corporation is representing to everyone that Baynes has the apparent authority, even if he does not.

Freeman and Lockyer v Buckhurst Properties (Mangal) Ltd, (1964) 1 A11 ER 630 (CA)

Facts:
Kapoor (agent) was a property developer and entered into a contract to purchase an estate. He obtained financial assistance from Hoon and formed a limited liability company, Buckhurst (principal and defendant corporation) with $70,000 equity. The estate was to be bought to sell for development.
- Kapoor and Hoon were the Board of Directors.

There were powers for the Board to hire a managing direct, but the Board did not do so. Kapoor, to the knowledge (and thus consent) of the Board, acted as if he were the managing director of the company in relation to finding a purchaser of the estate.
- Kapoor employed a firm of architects, Freeman & Lockyer (3rd party, plaintiffs) for submission of an application for development. He did so without express authority of the Board
    - The firm did the work and now requests the expenses

Procedural History:
Trial judge found that the company was liable. Company appealed.

Issue:
Was Buckhurst bound by the contract entered into by Kapoor? Did Kapoor have the necessary authority to enter contracts on behalf of Buckhurst?

Rule:
Actual authority is a legal relationship between principal and agent created by a consensual agreement. The contractor is a total stranger, and may be completely unaware of the existence of any authority on the agent. But, if the agent enters into a contract from this "actual authority", it cements contractual rights and liabilities

Ostensible authority is a legal relationship between the principal and contractor mad by representations, intended to be acted on by the contractor. The agent has authority to enter into contracts on behalf of the principal within the scope of their authority and renders the principal liable to perform any obligations imposed on him by such a contract. The agent does not have to be aware of the existence of the representations.

Analysis:
<u>Did Kapoor have actual authority?</u>
Actual authority requires more than silent acquiescence, there needs to be some oral or written statements on to the authority.
- There was nothing on the facts that can relied on to the conferral of actual authority in this case.
- But the directors knew that Kapoor was acting as if he had actual authority, or that he was expressly authorized.

<u>Did Kapoor have apparent authority?</u>
The firm intended to contract with Kapoor as agent of the company, and not Kapoor personally. The board of the company intended that Kapoor would do what he could to get the best price. Kapoor, though never appointed as managing director, was acting as such and the board knew this.
- The actual authority could have been transferred from the Board to Kapoor without it being formal. Actual authority need be more than acquiescence but communication. It appears that Hoon acquiesced.

- Actual authority and apparent authority are very separate
  - Actual authority is by consensual agreement
  - Apparent authority is by representation
    - The representation acts as estoppel, preventing the principal from claiming he is not bound.

Apparent authority represents to anyone that the agent is acting with authority.

- No representation can estop the corporation from denying the authority of the agent to do on behalf of the corporation at act which the corporation cannot do
- Conferring of actual authority is an act of the corporation, the corporation is estopped from denying it has conferred the agent.

Conclusion:

Buckhurst liable; Kapoor had apparent authority to enter the contracts

Hold, Order:

Appeal dismissed

Ratio:

Acquiescence is not enough to create actual authority.

This is the leading case in agent law when it comes to ostensible authority. The most common representations made by the principal to the agent is by permitting the agent to act in a certain way to carry out the business practice. This effectively represents to third parties that the agent is acting with authority to enter into contract on behalf of the authority of the corporation or acting in the authority of what the agent would normally have.

- This allows the agent to act in a way that would give the impression to third parties that they have the authority to contract as they have.

When the principal is a corporation, things gets more complicated.

- The capacity of corporations are limited by its constitution (doctrine of *ultra vires*)
- Unlike a natural person, a corporation can only make representations through an agent
  - So, the representation as to the authority of the agent which creates his ostensible authority must be made by some person(s) who have actual authority from the corporation to make the representation.

In this case, the Board permitted Kapoor to act in the way he did, and since they have actual authority, they permitted Kapoor's conduct. This was in effect a representation made by the Board, to the agent, that clothed him with apparent authority.

- It didn't have to be the Board, anyone who had actual authority to make the representation could have clothed him with authority. This does not mean they are the managing director though.

Four conditions are needed to entitle a contractor to enforce against a company a contract entered on behalf of the company by an agent who had no actual authority to do so:

(1) A representation that the agent had authority to contract on behalf of the company was made to the contractor
(2) The representation was made by a person(s) who had actual authority to manage the business of the company, either generally or in respect of those matters to which the contract relates
(3) That the contractor was induced by such representations to enter the contract (ie, that he in fact relied on it, and)
(4) That under its articles of association, the company was not deprived of the capacity either to enter the contract of the kind sought to be enforced or to delegate authority to enter a contract of that kind to the agent.
    a. This is usually not an issue in Canada because *ultra vires* is now gone, unless it is a special Act corporation.

Doiron v Manufacturers Life Insurance Co (Cob Manulife Financial) 2002 ABQB 664, aff'd ABCA 336

Facts:
Manulife was a principal corporation. Demmers was a high-up employee on Manulife, but on various companies as well. He could sell Manulife products, but products of other investment firms as well.

- Doiron couple (third parties) sold their home in Calgary and wanted to invest, so they consulted with Demers. Through the meetings, they invested $60,000
    - They wanted a low risk investment, but Demmers suggested one that the Doiron's did not like since the returns were too low.
- Demmers then advises them to invest in Devon Capital, who he was involved with. The investment was actually a fraud, and completely independent of Manulife.
    - The Doiron's then lost all their money

Doiron's brought action against Demmers & Manulife, arguing Demers was acting as Manulife's agent

Issue:
Is Demmers an agent of Manulife, such that Manulife is liable for the plaintiff's losses from the Devon investment?

Rule:
As per *Freeman & Lockyer*, for an agent with ostensible authority to bind the principal:

a. Representation that the agent had authority to contract was made to the contractor
b. The representation was made by a person(s) who had actual authority
c. That the contractor was induced by such representations to enter the contract
d. No *ultra vires* preventing 1-3

Analysis:
<u>Demmers was an independent contractor, not an employee of Manulife</u>
Demmers was performing services in a business on his own account, as reflected by his contract with Manulife. It was a non-exclusive relationship, since payment was by commission, he paid his own office/staff. Manulife had no corporation of his day-to-day operations.

- The investment was not a product of Manulife, though the Doiron's thought it was.
- Was Demmers was acting as an agent of Manulife for the Devon investment?

<u>Did Demmers have actual authority?</u>
He is not an employee of Manulife, and thus Manulife cannot be vicariously liable. Clause 3(b) of his Agreement specifically prohibited Demmers from entering Manulife into any contractual relationships. Demmers could do no more than solicit insurance applications; he couldn't even approve them.

- Demmers was not an agent of Manulife, and had no actual authority to bind it

<u>Did Demmers have ostensible authority?</u>
Even if he had no actual authority to bind Manulife, the Doiron's had every right to believe that he did. When they invested in Devon, they reasonably believed they were investing in a Manulife product.

- Demmers had Manulife business cards; they had to call Manulife first to reach him
- Demmers office was located on the same floor as Manulife
- Correspondence with Demmers was printed on Manulife letterhead

All these factors indicate that Demmers had ostensible authority. While the interactions were between Demmers and the Doiron's, Manulife stood idly by and permitted Demmers to create this impression.

- Manulife used promotional pictures of agents in their ads, and it was through this that the Doiron's sought out Demmers/relied on his advice, which led directly to their loss.

Conclusion:
Manulife liable.

Hold, Order:

Action allowed [appeal to ABCA dismissed]

Ratio:
The law of ostensible authority does not require explicit representations of authority; where the principal created a situation where it is reasonable to infer and rely upon the apparent authority of the person, that is sufficient.

The conduct that established the ostensible authority was, again, Manulife permitting Demmers to keep acting the way he was. This created the impression to Doiron's and other third parties that he had the ability to do so.

The ABCA largely affirmed the ABQB judgement.

- Manulife tried to argue that the Doiron's mistakenly believed they were contracting with Manulife, which is insufficient to bind Manulife.
- The ABCA reject this. They agree that a mere belief on the third party that they are contracting, absent other representations, cannot support ostensible authority to bind the corporation.
    - But, Demmers did represent to contract on behalf of Manulife.
- The ABCA confirmed the *Freeman* test, that ostensible authority does not have to be explicitly given, and it is reasonable to rely on a person's representation of authority.
    - Because of the impressions created by Manulife with respect to Demmers, the risk was on Demmers and Manulife, not the Doirons
    - Even if the Doirons had insufficient knowledge to avoid the situation, Demmers did not void the situation, and the representation grounded liability.
- At the time the Doiron's received a letter from Devon, they should have known Demmers had no authority. But, since they made the investment at a time they thought Demmers was with Manulife, Manulife is still liable.

Canadian Laboratory Supplies Ltd. v Engelhard Industries of Canada Ltd. [1979] 2 SCR 787

Facts:
Canadian Laboratory Supplies ("Canlab", plaintiff and principal corporation) employed Cook (agent) in their sales department, and then supervisor of inside sales. Canlab regularly bough platinum from Engelhard Indusries (defendant, 3rd party) was a refiner of precious metal, including platinum. Canlab would then sell the unused scraps back to Engelhard.

- Cook contacted Engelhard and told them Canlab had a customer, "Giles" who conducted secret experiments, and needed platinum.
- Engelhard agreed to ship platinum ordered by Canlab and to buy back the scraps directly from Giles, as well as make payment for the scraps directly to Giles (shipment would be directly to and between Giles and Engelhard.
    - This occurred for a long time and Giles stole over a million dollars worth of platinum

Oct 1966: Engelhard called Canlab to make inquiries about their account and spoke with Canlab's purchasing agent, Snook.

- Oct 1968: Engelhard president, Scott inquires about Giles, and Canlab's VP Operations says they are unaware of the transactions
- The scraps technically belonged to Canlab, whereas Engelhard is paying Giles to purchase the scraps and Canlab's therefore lost the scraps and the money for them

Issue:
Is Engelhard liable to Canlab in conversion of Canlab's platinum?

Rule:
As per *Freeman & Lockyer*, for an agent with ostensible authority to bind the principal:

a. Representation that the agent had authority to contract was made to the contractor

b. The representation was made by a person(s) who had actual authority
c. That the contractor was induced by such representations to enter the contract
d. No *ultra vires* preventing 1-3

Analysis:

The question, since Cook defrauded both Canlab and Engelhard, is if the loss should be born by Canlab or Engelhard. There were certain representations made by Canlab over the years. The initial purchases were proper, but the issue is the legality of the agreement to sell the scraps back to Giles. If Canlab made representations that clothed Cook with ostensible authority, Engelhard can rely on them. When the fraud begins, there is no evidence to show that Canlab, as principal, placed Cook in a position to hold himself as having authority to do the transactions in question.

- Cook was a sales agent and not a purchasing agent, he had neither actual nor ostensible authority to make this kind of agreement.
- There was no representation made by Canlab to Engelhard that Cook had the authority to enter into this kind of agreement.
    - So, Engelhard bears the risk of loss from the agreement

The question thus becomes, did Canlab make such representations in 1966 or 1968? If they did, and Cook had ostensible or actual authority, Engelhard has a right to rely on those expectations.

- Canlab did make the representations in 1966: Snook occupied a position with Canlab that held Cook out as having the authority to deal with Engelhard for the platinum purchases.
    - Snook said to Engelhard that Cook was the person to consult with on this matter. Since Snook had the requisite authority, the representations by Canlab clothed Cook with ostensible authority for the purchase and repurchase of the platinum.

Conclusion:

Engelhard is liable

Hold, Order:

Engelhard must recover damages until Oct 1966

Ratio:

Person who grants the agent with ostensible authority must have requisite actual authority to do so.

Dissent (Laskin):

The Snook representations by Canlab was merely a purchase agent dealing and he did not have the authority to hold Cook out as having the power to settle the accounts.

- As per *Freeman,* for ostensible authority to be made, the representation has to be from someone who had actual authority, which Snook did not have enough of to do so.

The 1968 conversation by VP Operations was the proper representation that clothed Cook with ostensible authority to continue dealing with Engelhard.

- Any losses suffered by Canlab by the continued deception of Cook

In this case, the dissent is generally accepted as more convincing, since it seems unlikely that Snook had the actual authority to clothe the Cook with ostensible authority. However, the end conclusion is the same, that Engelhard is liable for the damages, the only thing that changes is when they had to recover up to, since Cook eventually did have the authority in Oct 1968.

Recap of Chapter 5:

- Primary Tortious Liability:
    - Directing Mind doctrine, governing executive authority (*Rhone*)
    - Courts will limit operation of the directing mind doctrine (*Livent*)
- Criminal Liability:

- No longer the directing mind test, see *Criminal Code* ss 22.1, 22.2

- Statutory Liabilty:
  - Strict liability offences allow due diligence defences
  - Creating systems of compliance and policies and procedures to ensure efficacy of the system are necessary in due diligence (*Bata, Syncrude*)
- Contractual Liabilty:
  - *Ultra vires* and constructive notice no longer strong in Canada, ss 16, 17(3), 18 and 19, but still hold for public corporations under a special Act (*Jon Beauforte, Canadian Pickles Corp*)
  - Indoor Management Rule
  - Agency: actual and ostensible authority (*Panorama, Freeman, Doiron, Canlab*)

CHAPTER 6: CORPORATE GOVERNANCE

Governance Basics

The purpose of a corporation should be directed as a broader interest of stakeholders (customers, suppliers, the community) and the idea of shareholder should be different – it should be long term and not wedded to a short-term way of thinking.

- Some are skeptical about this, what should we take or how firm are corporate commitments?

Role of Directors

Any Board that is adequately fulfilling its responsibilities are doing so through 5 basic tasks:

1. Appointing and Supervising CEO and other officers
   a. Hiring, supervising, compensating, succession planning
2. Directing and evaluating Strategy
   a. Major changes to improve corporate performance with broad supervision
3. Representing shareholders and maintaining shareholder relations
   a. Reflecting concerns to management, maintaining shareholder relationships though communications like public disclosures of financial statements and keeping them apprised of internal business developments
4. Protecting and enhancing the company's assets
   a. Including potential acquisition or amalgamation and risk of solvency
5. Fulfilling fiduciary and other legal requirements
   a. Responsible for corporations adherence to laws and regulatory requirements, the preparation and maintenance of systems, documentation, maintenance of practices to ensure compliance with the law
   b. Fiduciary duties differ a lot if the corporation is private vs public
   c. Duties may be the same by performance will be different
      i. Private corporations usually have the shareholder and management as the same people and usually few in number, so closer shareholder-director relationships
      ii. Funds allocated differently and shareholder control is governed indirectly through governing the directors, who have the obligations.

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 101 (1) Subject to any unanimous shareholder agreement, the directors shall manage or supervise the management of the business and affairs of a corporation.

Section 105

- (a) The following persons are disqualified from being a director of a corporation:
  - (f) anyone who is less than 18 years of age;
  - (g) anyone who
    - (i) is a represented adult as defined in the *Adult Guardianship and Trusteeship Act* or is the subject of a certificate of incapacity that is in effect under the *Public Trustee Act*,
    - (ii) is a formal patient as defined in the *Mental Health Act*, or
    - (iv) has been found to be a person of unsound mind by a court elsewhere than in Alberta;
  - (h) a person who is not an individual;
  - (i) a person who has the status of bankrupt.

Section 106

- (1) At the time of sending articles of incorporation, the incorporators shall send to the Registrar a notice of directors in the form required by the Registrar.
- (3) Subject to subsection (9)(a) and section 107, shareholders of a corporation shall, by ordinary resolution at the first meeting of shareholders and at each succeeding annual meeting at which an election of directors is required, elect directors to hold office for a term expiring not later than the close of the next annual meeting of shareholders following the election.

Section 107

If the articles provide for cumulative voting,

- (b) each shareholder entitled to vote at an election of directors has the right to cast a number of votes equal to the number of votes attached to the shares held by the shareholder multiplied by the number of directors to be elected, and the shareholder may cast all those votes in favour of one candidate or distribute them among the candidates in any manner

Section 109

- (1) Subject to section 107(g) or a unanimous shareholder agreement, the shareholders of a corporation may by ordinary resolution at a special meeting remove any director or directors from office.

Section 241

In connection with an action brought or intervened in under section 240 or 242(3)(q), the Court may at any time make any order it thinks fit including, without limiting the generality of the foregoing, any or all of the following

Section 242

- (3) In connection with an action brought or intervened in under section 240 or 242(3)(q), the Court may at any time make any order it thinks fit including, without limiting the generality of the foregoing, any or all of the following:

an order appointing directors in place of or in addition to all or any of the directors then in office;

Canada Business Corporations Act, RSC 1985, c C-44

Section 101

- (1) Subject to any unanimous shareholder agreement, the directors shall manage, or supervise the management of, the business and affairs of a corporation.

Both federally and provincially, the role of directors are the exact same in the *CBCA* and *ABCA*. There are legal requirements to who can be a director: must not be a minor, without capacity, another corporation or bankrupt.

- Section 105(3) made it a requirement to have citizenship, but this was repealed to make Alberta a more competitive jurisdiction for corporate investment, as it broadens the scope of the availability of Alberta corporations.
    - This adds a whole bunch of knock on effects, so there needs to be more provisions soon

Section 106 requires that at the first shareholder meeting, the directors have to be elected pursuant to an ordinary resolution. They also need to elect directors at each successive annual meeting as well

- An ordinary resolution is a simple majority, 50% + 1

If articles for incorporation allow cumulative voting (cumulative voting is not allowed without it), each shareholder can vote in a director election and their votes are equal to the number of shares multiplied by the number of directors to be elected.

- If shareholder has 100 shares, and they're electing 7 directors, that shareholder gets 700 votes.
- The votes can be distributed at will
    - This gives minority shareholders a better chance at having influence over elections.

Section 109 allows directors to be removed by a simple majority (ordinary resolution). But, s 242 and 241 allow other avenues to remove a director.

- Section 241 allows the shareholders to seek a court order to remove directors by derivative action
- Section 242(3)(f) allows the shareholders to seek a court order to remove directors by oppression action
    - We will explore these both later.

More recently, the *CBCA* has legislated on disclosure requirements to designated groups to ensure equity, diversity and inclusivity.

- Corporations are required to report on the composition of the group, ensure shareholders that there is a policy to nominate certain groups of people for election, and what the details are.
- If there is no policy, they need to explain why they do not have one
    - Designated groups include Aboriginal peoples, persons with disabilities, members of visible minorities and women (as defined by the *Employment Equity Act*)
    - The idea is that diversity promotes business efficacy since diversity is a more efficient business management style and reflects values of social justice
    - Corporations are not just accountable to shareholders, but also socially accountable and thus their composition should reflect the broader society
- This is only for the *CBCA*, not for the *ABCA.*

<u>Statutory Duties of Directors and Officers</u>

Canada Business Corporations Act, RSC 1985, c C-44
Section 122 (1) Every director and officer of a corporation in exercising the director's or officer's powers and discharging the director's or officer's duties to the corporation shall (a) act honestly and in good faith with a view to the best interests of the corporation, and (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

Section 122(a) grounds a fiduciary duty and provisions to consider what the best interests of the corporation are. But what is the substance of the duty to act honestly and in good faith?

- (b) cements a duty of care: the care and diligence of a competent and reasonable person
    - This statutory duty of care is higher than what is required at common law
    - It is designed to remedy what was a problem of common law at the time, where there was precedents of appalling actions by directors who did not breach their duty of care, and the public wanted more accountability
        - So, the statute elevated the standard at common law

Peoples Department Stores Inc (Trustee of) v Wise, 2004 SCC 68

Facts:

The Wise Bros (individual defendants) were the directors of Wise Stores, which was incorporated under the *CBCA* in 1992. Peoples is acquired by Wise Stores pursuant to a transaction structured as an amalgamation so the Wise brothers become the directors of Peoples.

- Due to financial conditions of the amalgamation, Peoples could not amalgamate with Wise Stores until a parent company of Peoples had been paid in full
- Upon consultation with management of both companies, the Wise Bros instituted a new joint-inventory procurement policy system to achieve greater efficiencies:
    - Wise Stores: to purchase overseas inventory and bill Peoples for its share (since less inventory is sourced overseas, Wise takes on relatively less debt)
    - Peoples: to purchase North American inventory and bill Wise for its share (since more inventory is sourced in America, Peoples takes on relatively more debt)
        - As a result of this, Peoples is owed $4.4 million by Wise

In 1995, both Wise and Peoples file for bankruptcy. The trustee for Peoples brought an action against the Wise Bros, as directors of Peoples, alleging a breach of fiduciary duty, and breach of duty of care under s122 of the *CBCA*.

- They argue that the Wise Bros favoured the interests of Wise over the interests of Peoples to the detriment of Peoples' creditors under the new policy

Procedural History:

Quebec Court of Appeal dismissed the action

Issue:

Did the individual defendants breach s122 by implementing the policy that favours Wise over Peoples?

Rule:

Section 122 of the *Canada Business Corporations Act*

(1) Every director and officer of a corporation in exercising their powers and discharging their duties shall

(a) act honestly and in good faith with a view to the best interests of the corporation; and

(b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

Analysis:

<u>Statutory Fiduciary Duty (s 122(1)(a))</u>

Directors do now owe a fiduciary duty to creditors under s122(1)(a), the statute specifies that the fiduciary duty is owed to the corporation only

- The debtors (directors) may owe a fiduciary duty to creditors based on circumstances of any given case under the common law, but they do not by operation of s122(1)(a).
- The statute requires directors and officers to act honestly and in good faith to the corporation. This requires avoiding conflicts of interest in the corporation for the

proper management of assets, and cannot abuse their position to gain benefits. They must serve the corporation selflessly, honestly and loyally.

- There is no evidence of personal interest or improper purpose since they were just trying to solve inventory costs problems
  - The attempt was honest and in good faith, even if it was unsuccessful
  - As such, they did not breach their fiduciary duty under s122(1)(a)
- Nonetheless, "best interests of the corporation" does not mean the "best interests of the shareholders". Various other factors are relevant in determining what directors should consider in soundly managing with a view the best interests of the corporation.
  - It is more accurate that the vest interests of the corporation, given all the circumstances of a given case, for the directors to consider interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment.

Statutory Duty of Care (s 122(1)(b)

Just because a fiduciary duty wasn't broken, doesn't mean the duty of care wasn't. Section 122(1)(b) requires more of directors and officers than the traditional common law duty of care

- It is an objective standard where directors and officers won't breach the duty if they act "prudently and on a reasonably informed basis".
- The decisions must be reasonable business decisions in light of all the circumstances about which the directors or officers knew or ought to have known.
  - Perfection is not needed; courts are ill-suited to determine if the application of business expertise in corporate decisions are appropriate.
    - They can determine in an appropriate amount of prudence was brought to bear when making the decision
  - This is called the Business Judgement Rule

Tribunals should refrain from finding directors liable for "bad" business decisions where two conditions are met:

1. Decision making process was followed prudently on a reasonably informed basis
2. Reasonableness of the decision considering all the circumstances about which the directors knew, or ought to have known

Under s122(1)(b), directors can owe a duty of care to creditors under s122(1)(b) because (b) does not only refer to the corporation

- The identity of the beneficiary of the duty is much more open-ended, and it appears obvious that it must include creditors.
- But, the directors did not breach the standard of care; the policy was a reasonable decision with a view to addressing their business problem.

Section 122(1)(b) also does not ground it's own independent cause of action. It only provides a standard of care. The plaintiff must first establish that, at common law, a duty was owed and only then look to the statute for the standard of care.

Good Faith

Bros argued they were relying in good faith on the judgement of a person whose profession lent credibility to his statement, in line with the defence in s123(4)(b)

- The QCCA accepted that argument, which was an error.
- The good faith reliance had to be from a lawyer, accountant, engineer, appraiser or other professional who lends credibility to a statement made by him
- This must be a profession, and the employee in this case was VP of Finance, which is not a professional.

Conclusion:

No breach of s122

Hold, Order:

Appeal dismissed

Ratio:

Creditors are not owed fiduciary duty under the *CBCA* because it's owed by directors to a corporation. But they must serve the corporation selflessly, honestly and loyally.

- The duty is broader than the coextensive interest of shareholders and can include government, environment and shareholder interests

Directors/officers won't breach duty if act prudently and on reasonably informed basis (objective)

The standard of care analysis has been critiqued to say it is not obvious that creditors are owed a duty of care. Isn't the section as whole related to the relationship between the directors and the corporation as a whole?

- The *ABCA* was amended to reflect this, so that both the fiduciary duty and standard of care are owed to the corporation.

The biggest thing is that the Courts will give deference to businesses when they make business decisions, so long as they were prudent in the way they did so, and it was reasonable in light of all the circumstances.

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 123 (3) A director is not liable under section 118, and has complied with the director's duties under section 122, if the director exercises the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances, including reliance in good faith on (a) financial statements or interim financial statements of the corporation represented to the director by an officer of the corporation or in a written report of the auditor of the corporation to reflect fairly the financial condition of the corporation, o (b) an opinion or report of a person, including a lawyer, accountant, engineer, appraiser or employee of the corporation, whose profession or expertise lends credibility to a statement made by that person.

Canada Business Corporations Act, RSC 1985, c C-44
Section 122 (1.1) When acting with a view to the best interests of the corporation under paragraph (1)(a), the directors and officers of the corporation may consider, but are not limited to, the following factors: (a) the interests of (i) shareholders, (ii) employees, (iii) retirees and pensioners, (iv) creditors, (v) consumers, and (vi) governments; (b) the environment; and (c) the long-term interests of the corporation

Section 123 was amended to provide a broader scope to individuals on whom directors and officers can rely on. It does not apply only to professionals

- But, what counts as sufficient expertise such that reliance on those is enough to discharge their statutory duties?

Section 122(1) was also amended after *Peoples* to state that the director's and officer's duties are to the corporation.

- This does not mean that directors will never owe a duty to a third party, that is always a possibility, but need to look to other sources of law or the common law

Also after *Peoples*, the *CBCA* was amended to include 122(1.1) which codifies that *Peoples* findings that the best interests of the corporation is broader than the shareholders interests.

- This reflects a legislative intent to codify a broader understanding of what the purpose of a corporation is

Peoples was only interpreting the *CBCA* and the Quebec *Civil Code*, but the principles articulated have been confirmed in Alberta, under the *ABCA* in *Transportation Lease Systems Inc v Weaver*.

- Statutory duty of care does not ground a way of liability, but a way to judge directors and officers; plaintiff must establish there is a duty of care at common law before moving to the *ABCA* for the standard of care, which is a stricter standard apply than otherwise would at common law

BCE Inc v 1976 Debentureholders, 2008 SCC 69

Facts:

BCE is a very large telecommunications company of Bell Canada. A group of purchasers proposed a leveraged buyout of all BCE shares. Under the transaction, BCE would incur $30 billion of debt to support the purchase. Bell, as a wholly owned subsidiary of BCE, would guarantee the debt.

- Bell's existing debenture holders argued that Bell's increased liability under the guarantee had the effect of downgrading their debenture values (by about 20%) while conferring a benefit only on the shareholders of BCE from the premiums on market price of BCE shares

The Debenture holders then brought an oppression action under the *CBCA* s 241 and challenged the approval of the plan of arrangement under s192 as not being "fair and reasonable".

Procedural History:

At trial, board decision of selecting this offer was consistent with Director duties

- Quebec Court of Appeal reversed the decision on the *Peoples* logic.

Issue:

Are the directors of BCE liable for oppression?

Rule:

Section 241 of the *Canada Business Corporations Act*

(2) If, on an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates

(a) any act or omission of the corporation or any of its affiliates effects a result,
(b) the business or affairs of the corporation or any of its affiliates are or have been carried on or conducted in a manner, or
(c) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner

that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer, the court may make an order to rectify the matters complained of.

Analysis:

Often the interests of shareholders and stakeholders are co-extensive with the interests of the corporation. But, if they conflict, the directors duty is to the corporation.

- Although directors must consider the best interests of the corporation, it may consider the best interests of the corporation, it may also be appropriate, although not mandatory, to consider the impact of corporate decisions on shareholders or a particular group of stakeholders.
    - This weighing of decisions is a directors role, and courts should give deference to the business judgement of the directors who take the ancillary interests into consideration, as reflected by the business judgement rule, so long as it is in the range of reasonable alternatives.
        - This applies to decisions on stakeholders' interests, as much as other directional decisions.

Normally, only the beneficiary of a fiduciary duty can enforce the duty. This isn't particularly helpful for corporate law. Directors have that duty, but are also the ones who control the corporation, and they are unlikely to bring an action against themselves for breach of their own fiduciary duty

- As such, several special remedies in common law and statute protect shareholders and stakeholders' interests of the corporation.
    - Derivative actions under s239 of the *CBCA*
    - Civil action for breach of duty of care under s122(1)(b) of the *CBCA*,
    - Oppression under s241 of the *CBCA*, as used in this case
        - Was there a reasonable expectation that the Directors would consider the shareholders when making decisions, but failed to do so when making the leveraged buyout
        - In oppression remedies, the claimant has to prove that some reasonable expectation was frustrated through oppressive conduct of the directors.

In this case, the trial judge recognized that directors had a fiduciary duty to act in the best interests of the corporation and the content of this duty was affected by various interests at stale in the process that BCE was doing.

- Directors, when faced with these conflicting interests, may have no choice to approve transactions that would benefit some groups at the expense of others, in the name of being in the best interest of the corporation.
- Shareholders benefiting from the transaction and the Debentureholders prejudiced does not ground the conclusion that the directors breached their fiduciary duty
- All bids required Bell to take some debt, and there was no evidence that bidders were prepared to accept less leveraged debt
    - As long as the directors made decisions in good faith and in the performance of functions they were given by the shareholders, the business judgement rule will protect their decision from judicial interference

Conclusion:
Oppression not established

Hold, Order:
Appeal allowed

Ratio:
Directors making a choice that would best benefit the corporation, but prejudicially hurt another stakeholder will not be a violation of their fiduciary duty on the basis of the business judgement rule, so long as the decision was reasonable.

This case gives a nice summary of legal avenues available to stakeholder since the s122(1)(b) duty of care does not ground an independent cause of action:

- Derivative actions under s239 of *CBCA* which allows stakeholders, with leave, to enforce the directors' duty to the corporation when the directors are themselves unwilling to do so

- Civil action for breach of duty of care under s122(1)(b) of the *CBCA*, where the duty is not owed solely to the corporation, and thus may be the basis for liability to other stakeholders in accordance with tort law and extra-contractual liability
- Oppression under s241 of the *CBCA*. Unlike derivative actions, the oppression remedy is focused on the harm to the legal/equitable interests of shareholders affected by oppressive acts on a corporation or its directors. Available to a range of stakeholders, security holders, creditors, directors and officers
    - Claimants will often bring oppression when they should have brought derivative actions, since derivative actions are more complicated

This case also reinforces the idea that just because a director decision hurts a particular group of stakeholders, does not mean they breached any fiduciary duty.

- This will come back to the Business Judgement Rule that grants discretion to the directors so long as their decision was reasonable. This is because directors often have to make decisions that balance various interests of various stakeholders.
    - In any decision that would be inconsistent with shareholder and stakeholder interests, the decisions must be one that benefits the corporation

Smith v Van Corkum (1985) 488 A2d 858 (Del Sup Ct)

Facts:

Van Corkum (defendant) is chair and CEO of Trans Union (corporate defendant). Trans Union held significant investment tax credits it couldn't offset. Van Corkum met with Pritzker, a takeover specialist to discuss the acquisition of Trans Union.

- Under the proposed deal, "New T Company" was formed by acquiring the corporation to carry out a "cash our merger" with the defendant corporation at $55/share

As a result of the deal, Smith (plaintiff) and other minority shareholders bring a class action against Trans Union and the individuals on the Board of Directors, including Van Corkum.

- Under the deal, the shareholders would have no future opportunity to participate in the growth or profits of the business, they would just leave with the cash in hand.

Issue:

Did Van Corkum breach their duty of care to the corporation by approving the cash out merger?

Rule:

Delaware law:

The business judgement rule exists to protect and promote the full exercise of managerial power granted to directors; it presumes that in making a business decision, the directors acted on an informed business, in good faith that the action was the best interest of the company.

Analysis:

The presumption of the Business Judgement Rule must be rebutted by the party attacking the Board decision as uninformed. Did the directors reach an informed business judgement in agreeing to sell the company on the terms of the deal? The Board met to approve the deal.

- Van Corkum held a presentation, but did not explain why $55/share
- Board never sought a fairness opinion or made a report for the value of the company
- Written agreements weren't available for the Board review
- Corporate lawyer informed the Board that if the deal wasn't approved, they could be sued. However, they are being sued anyway after approving
    - The deal was brought up roughly; van Corkum was pushing it through

Need some fairness opinion (one provided by an investment firm that would give some market opinion as to the "fair value" of the corporation. The Board did not do this. The overall indication was that the process was bad

1. Directors didn't adequately inform themselves of Van Corkum's role in forcing the sale

2. Directors were uninformed as to the intrinsic value of the Company
3. Directors were grossly negligent in approving the sale after 2 hours consideration, without notice and without exigency of a crisis/emergency

Conclusion:
Van Corkum personally liable

Hold, Order:
Motion allowed; fair value of plaintiffs' sharers in the corporation ordered

Dissent:
Board was not negligent. Directors were "highly qualified and well informed" and made an informed business judgement which was buttressed by their test of the market

Because this is a Delaware case, there are many things that are different from Canadian law. The Delaware court found that there was a breach of duty because the Directors didn't follow a good process when coming to their business judgement.

- In Canada, there are two requirements: establish a good process, and the decision was substantively a reasonable one (in the range of reasonable alternatives)
- In America, the analysis is purely the first one, the process being good. The second limb is given almost complete deference to the directors under the business judgement rule.
    - Here the deal was so egregious that the directors couldn't even benefit from the rule

Another difference is that, in Canada, the business judgement rule is not a presumption, whereas it is in Delaware.

- In Canada, the plaintiff would bring action for statutory duty (fiduciary duty, or duty of care)
    - Once they established the duty on a balance of probabilities, the defendant directors try to establish a defence by relying on the business judgement rule.
    - This is likely to show that a good process was used, and the decision was reasonable (in the range of reasonable alternatives)
        - If they do this, the court will defer the directors and officers judgement
    - So it is not really a presumption that needs to be rebutted, more of a defence that needs to be established by the officers
- In Delaware, the plaintiff would bring action to rebut the presumption that the officers and directors used business judgement in their decision.
    - This will only be an analysis of the process, not the reasonableness of the outcome

One way to think about these kinds of questions is to take a step back and ask how this current decision may look with the benefit of hindsight.

- In this case, there was a lot of emphases on a negligent process. A lot of it turns on how the $55/share was arrived at.
- In the Canadian process, should ask if the decision was reasonable (in the realm of alternatives)

<u>Duty of Directors and Officers: Fiduciary Duty</u>

Directors and officers have a duty to put the corporations interest ahead of their own personal interests. They must avoid a situation where there is a conflict between the corporation and their personal interests. Generally, there are multiple issues a director will face in their fiduciary duty

- Taking of Corporate Opportunities
    - Where an officer breached their fiduciary duty by taking a business opportunity that belongs to the corporation that they are serving
- Self Dealing

- Where a direct conflict of interest ("COI") because the director has a self-interest stake in a contract to which the corporation is a party
  - If the Board of Directors ratifies a contract of the corporation where that Director is a counterparty, the Director has their own self interest in the corporation and it is at odds with the corporation; an inherent COI
- Competing Directors
  - To some degree, a director has an obligation to avoid engaging with or directing a competing corporation or enterprise
- Business Judgement Rule ("BJR")
  - Relevant for analyzing the fiduciary duty, but depends on the facts
    - If there is potential claim, presumably the Director has made some judgement as to whether that is a corporate opportunity relating to them
    - Involves some business judgement. Still deference from the Court

<u>Taking Corporate Opportunities</u>

Cook v Deeks, [1916] AC 554 (PC)

Facts:

Toronto Construction Company ("TCC") are contractors for railway construction. Mr. GM Deeks, Mr. GS Deeks and Mr. Hinds (individual defendants) are all Directors of the TCC, each are 25% shareholders.

- Mr. Cook (plaintiff), was a director of the remaining 25%

The defendants considered Cook "unsatisfactory from a business standpoint" and wanted to exclude him from benefiting from contracts. They negotiated and executed with the Canadian Pacific Railway Company under the name of a different corporation, without Cook.

- The new corporation is granted the CPR contract
- The defendants passed a shareholders resolution (as owners of ¾ of the outstanding shares of the TCC) declaring that the company had no interest in the contract

Cook brought action as shareholder and on behalf of the TCC, claiming the defendants breached their fiduciary duty

Issue:

Did the individual defendants breach their fiduciary duty by appropriating a corporate opportunity from the TCC?

Analysis:

The defendants intentionally concealed all circumstances to their negotiations until the arrangement had been concluded in their favour and the contract could not be interfered with. While entrusted with the conduct of the company affairs, they deliberately designed to exclude the company who they had a first duty to protect.

- Those who assume control of a business must remember they are not at liberty to sacrifice the interests which they are bound to protect and divert business in their own favour which properly belongs to the company they represent

The defendants secured the contract and cannot retain the benefit of the contract for themselves but must be regarded as holding it on behalf of the company.

- Guilty of a distinct breach of duty since the contract belonged in equity to the company and ought to have been dealt with as an asset of the company

Can the shareholder resolution absolve this?

- The majority cannot appropriate to themselves money or other advantages that belong to the company or where all shareholders should participate
- This would be a fraud on the minority; majority cannot use their power to oppress the minority shareholder by giving a gift to themselves.

Conclusion:

Fiduciary Duty breached

Hold, Order:

Action granted

Ratio:

It is a breach of fiduciary duty to sacrifice the interests of their company and divert business in their own favour that rightly belonged to that company

- The resulting agreement would properly belong to the corporation

This is an old case, but drives the general point home that it is a breach of fiduciary duty for directors to take an opportunity that belonged to the company they owe the duty to and vest it in themselves. This was the first case of Taking of a Corporate Opportunity which is now a pillar of fiduciary breaches.

Canadian Aero Service v O'Malley, [1974] SCR 592

Facts:

O'Malley and Zazyski (defendants) were the President/CEO and Vice President of Canadian Aero Services ("CanAero"; plaintiff) respectively. CanAero was a surveyor and mapping company. The defendants devoted efforts to secure a contract for the mapping/surveying of Guyana after its independence.

- When the project goes out to tender, the defendants incorporate Terra Surveys Ltd with Nominal directors appointed and the defendants are majority shareholders and officers
- CanAero and Terra both bid for the tender, the defendants resign from CanAero and Terra ultimately wins

Procedural History:

Ontario Court of Appeal dismissed the action, labelling defendants mere employees owing no duty

Issue:

Did the individual defendants breach their fiduciary duty to CanAero by taking it's corporate opportunity?

Rule:

A director/senior officer precluded from obtaining for themselves, either secretly or without approval of their company (which need to be granted full disclosure) any property or business advantage that belongs to the company or for which the company was negotiating.

Analysis:

<u>Was there a duty?</u>

While the defendants were subject to supervision of the officers of CanAero, their positions were seniors of a working organization and granted them with responsibilities far removed from the role of obedient servants.

- Defendants stood in a fiduciary relationship to CanAero which requires loyalty, good faith and the avoidance of a conflict of duty and self interest.

<u>Was the duty breached?</u>

O'Malley and Zazyski are precluded from obtaining for themselves a business advantage that belongs to the company they are officers of.

- This is especially true where they are a participant in the negotiations on behalf of the company.

The defendants raised three defences:

1. They had resigned from CanAero when the bid was won
    a. If this was a defence, any director could take what was otherwise a corporate opportunity and then resign last minute to avoid liabilty
    b. This can't be all that is needed to get away with it and avoid liability

c. At what point is there no longer a fiduciary opportunity? How much time must pass before the defendants can take the opportunity?
   i. Contextual and factual interpretation is needed
   ii. If the opportunity or property properly belonged to the company that the director was fiduciary in, the time passed might not matter much
d. This is not accepted

2. The bid wasn't an opportunity because it hadn't fully "ripened"
   a. Fiduciaries cannot pursue maturing business opportunities
   b. The defendants entered into the project at the heat of maturation
      i. The bid doesn't have to be fully ripened or matured opportunity
   c. This is not accepted
3. Terra's bid added work from CanAero's bid rather than being a copy
   a. Simply changing some details of the proposal cannot be a defence
   b. Liability could always be avoided by simply changing one detail

Conclusion:
Fiduciary duty breached

Hold, Order:
Appeal allowed

Ratio:
Fiduciary duty requires standards of loyalty, good faith and avoidance of a conflict of duty and self-interest. This is a contextual analysis based on the circumstances around the taking of opportunity
- The plaintiff does not need to prove that they would have won the opportunity, merely that they were reasonably likely to pursue it and had not abandoned it.

Laskin here rejects a stricter approach that was previously used in *Regal Hastings*. It is thus not followed in Canada. Instead, he favours a contextual approach when it comes to standards of loyalty, good faith and avoidance of conflict of duty or self interest. The conduct of the director or officer accused of a taking of corporate opportunity must be tested on a case-by-case basis, considering multiple factors:
- Position or Office held
  - Was it more like a director/officer, or more like a general employee?
- Nature of the corporate opportunity
  - Was it truly an opportunity for the corporation?
- Ripeness of the opportunity
  - Was it something opened for years, or a time sensitive sought-after bid?
- Specificity of the opportunity
  - Was it open to many people or industries, or likely only a handful
- The director/officer's relation to the opportunity
  - Did they work with it closely with their principal organization?
- Amount of knowledge possessed by the directors
  - Was it reasonable for them to know their corporation could reasonably get it?
- Circumstances in which it obtained the opportunity
  - Whether it was special, or private to certain organizations
- Timeline in the continuation of the fiduciary duty
  - Were they in a fiduciary role temporally close to the taking?
- How the fiduciary ended, by retirement, resignation of discharge

However, this is not an exhaustive list. There are other factors, and not all factors need be considered.

Importantly, CanAero did not need to prove that they would have won the bid without the misconduct. At the time of misconduct, it was clear CanAero was pursuing the bid, and they had not abandoned it. There is no indication that when the defendants resigned, they were not going to get it.

- In other words, there is no need to prove the profit would have been won by the plaintiff to ground this breach of fiduciary relationship

Think of this as an equitable remedy; damages could be loss of profits by CanAero, or the gain or profit by the other corporation/defendants as a result of the breach of fiduciary duty

- It is not expectation damages awarded, it is a measure of damages for a breach of fiduciary duty (loss incurred or the benefit gained)
- CanAero is entitled to compel the faithless fiduciaries to answer for their default according to their gains. Similar to unjust enrichment.

In any case, the proper remedy for a taking of corporate opportunity is to disgorge the defendants of their benefits/profits under the contract they faithlessly won.

In *Matic et al. v Waldner et al.* 2016 MBCA 60, the Court summarizes the process for taking of corporate opportunity very well. In essence, use this when approaching one of these situations.

(1) Begin with the statute
  - Section 122 of the *ABCA:*
    (1) Every director and officer of a corporation in exercising the director's or officer's powers and discharging the director's or officer's duties shall
      (a) Act honestly and in goof faith with a view to the best interests of the corporation

(2) Next, go over the common law content of the duty as found in *Peoples*:
  (a) They must avoid conflicts of interest with the corporation and avoid abusing their position to gain personal benefit.
    (1) This includes conflicts with directors personal interests and those of any other corporation in which the director is interested

(3) Next, go over the Corporate Opportunity doctrine from *CanAero*
  (a) Use Laskin's approach in *CanAero*
    (1) The doctrine precludes a fiduciary from obtaining for himself, either secretly or without the approval of the company (would require full disclosure), any property or business advantage either belonging to the company or for which it has been negotiating
  (b) It is not a "right mind" test (as in America), but a "imprecise ethical standard" which prohibits directors and officers from "appropriating a business opportunity to the company which in fairness should belong to the corporation"
    (1) This includes a "maturing business opportunity which his company is actively pursuing"
  (c) *Matic* also gives more interpretive guidance:
    (1) What counts as a maturing business opportunity?
      (a) Is the duty only limited to opportunities that are "immediately available" or is it more expansive to include potential opportunities as well as maturing ones?
      (b) A broader approach is usually taken, so potential likely count but there must be a "real sensible possibility and more than a theoretical conflict"
      (c) Would a reasonable man, looking at the circumstances think that there is a real and sensible chance for conflict?
      (d) Need potential for active conflict, not just one that is possible under certain circumstances
    (2) Does the plaintiff corporation have to be in "active pursuit" of the opportunity?

        (a) It is not necessary for the plaintiff to be in active pursuit
        (b) It is a factor to consider, but a case would not be dismissed because the corporation was not "actively" pursuing the opportunity
(4) Then, go over the circumstances in which the opportunity was obtained (*Matic*)
    (a) The manner in which the opportunity came to knowledge of the director is not determinative, but a fact to be considered as part of the contextual analysis
    (b) If they take the opportunity while acting as director/officer, it is more indicative that it was a breach, but that is not the only thing to consider.
    (c) If they became aware of the opportunity, or took the opportunity
        (1) Was their special or private knowledge that the defendant is privy to because of their position, even if that position is not as director/officer
        (2) The further removed they are, it becomes less clear if the breach will be established
    (d) The factual matrix is more of a subtle way of analyzing, it may create some uncertainty for officers. If there is any potential for conflict, then it should be fully disclosed
    (e) Elaborates on the factors brought up in *CanAero*
        (1) Maturity of the opportunity
        (2) Whether the corporation was actively pursuing it
        (3) Whether the opportunity was in line with the corporation's line of business or a related business
        (4) How the opportunity arose or came to the director's attention
        (5) Whether the other directors had knowledge of the director's pursuit of it
        (6) Whether the directors gave fully informed consent to the director's pursuit
    (f) The overall goal of the analysis is to determine whether the opportunity fairly belonged to the corporation in the circumstances
(5) Limits on liability of Directors or Officers
    (a) If the directors/officers fully disclose the opportunity to the corporation and get informed consent, liability will not attach
        (1) If uncertainty, there should be full disclosure and consent

There have been recent amendments to the *ABCA*:

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 16.1 (1) Subject to the regulations, a corporation may waive any interest or expectancy of the corporation in or to, or in being offered an opportunity to participate in, a specified business opportunity or specified classes or categories of business opportunities that are offered or presented to the corporation or one or more of its officers, directors or shareholders. (2) Subject to the regulations, a waiver referred to in subsection (1) may only be made if the corporation's articles of incorporation or a unanimous shareholder agreement enables the ability to so waive, or in any other manner set out in the regulations. (3) Subject to the regulations, a waiver may be modified or revoked.

Section 16.1 allows the corporation to submit an advanced waiver of opportunity. This allows a corporation to weigh certain corporate opportunities in advance.

- This must be specified in advance to avoid a director taking of corporate opportunity and may only be made if the corporation's AoI or USA enables the ability to do so (s 16.1(2))
- This requires certainty in advance such that directors and officers cannot run afoul with their fiduciary duty

Self-Dealing Transactions

This is the second breach of fiduciary duty. Where there is a contract between the director/officer ether directly (with them as an individual) or indirectly (with the corporation they have an interest in) and the corporation they are director to, this breach may arise.

- If someone is on either side of the transaction, they have an influence over the corporation's decision, but also an interest in the other side of the transaction or deal.
- This is purely a common law treatment, there are no statutory provisions dealing with this.

Aberdeen Railway Co v Blaikie Bros [1843] All ER Rep 249 Facts: Aberdeen Railway (plaintiff) contracted with Blaikie Bros (defendant partnership) to purchase chairs. Blaikie is a director for Aberdeen and also a partner at Blaikie. Issue: Is the contract voidable at the option of Aberdeen because it is self dealing? Rule: A corporate body can only act through agents, and it is the duty of those agents to act as best to promote the interests of the corporation whose affairs they are conducting. Analysis: The director has a duty to discharge their fiduciary duty towards his principal, and this is a rule of universal application: someone who has director fiduciary duties shall not enter into engagements in which he has or could have a personal interest conflicting (or which could conflict) with the interests of the corporation he is bound to protect. - This principle is so strict, that no question shall be raised as to the fairness of the contract. - Mr. Blaikie was a director, and chairman of directors. He had the burden to bargain for the benefit of the company. He entered into contract with his firm for the sale of chairs ○ His duty was to obtain these chairs at the lowest possible price ○ His personal interest would lead him in the exact opposite direction – to have them as high as possible. He had to give his co-directors the full knowledge and assist them in getting the contract at the cheapest possible price. ○ He had to put his interest in conflict with his duty, and whether he was the sole director, or only one of many, can make no difference in principle. Conclusion: Yes, contract voidable Hold, Order: Contract voided at Aberdeen's request Ratio: Involvement by a Director on both sides of a contract make it voidable since the director would have competing interests. No question is allowed to be raised as to the quality of the deal

This was a fairly clearcut illustration of this breach. It should be set aside because Blaikie's involvement with either side. However, it is not automatically void, but voidable, only at request of the plaintiff.

- This was universal application; serving on the board of another corporation automatically allowed the contract to be void.
- This became problematic over the years as it was seen as unnecessarily strict
    - There are times when the contract is beneficial for both parties

- The *Aberdeen* was not one of those times, since Blaikie would want the cheapest chairs from one corporation but to sell them for the most expensive possible for the other.

- Eventually, the common law evolved over time to allow directors to sit on both board if the AoI had them, so long as they were not oppressive or fraud on the minority
- *Northwest* refined this ever more

North-West Transportation Company Ltd v Beatty, (1887) AC 589 (PC)

Facts:
Beatty (plaintiff) is a shareholder and shareholder of North-West Transportation Company ("Northwest", defendant). Northwest enters into a contract for the purchase and sale of a steamship from Beatty in his personal capacity.

- At the date of purchase, the acquisition of another steam was considered an "essential" purchase to the efficient conduct of the company's business and the ship was in good shape, and the best bargain for the company (the price was reasonable)
- The shareholders ratified the purchase of the ship, including Beatty who voted in favour.
- Henry Beatty, another shareholder, sues on behalf of North West to have the contract void

Issue:
Is the contract for the purchase of the ship a self-dealing transaction and voidable? Does the shareholder ratification insulate the validity of the contract?

Rule:
Aberdeen: a self dealing transaction with conflicting elements can be void without exception.

Analysis:
Directors have a duty to not deal on behalf of the company with himself or from contracting in engagements where he has a personal interest conflicting. However, the only unfairness/impropriety that could have arisen out of the facts is that Beatty, possessing high voting power, had many shares which enabled him to adopt the by-law and ratify the voidable contract into which he, and other co-directors entered.

- Every shareholder has the right to vote, even if they have an interest in the subject matter. There is no limit upon the number of shares a shareholder may hold and each entitled him to a vote.
- The conduct may have given rise to a potential conflict of interest and may breach his fiduciary duty
- But, the dealing can be affirmed or adopted by the company, provided it is consistent with the articles of incorporation, and it is not oppressive.

Acquisition of the ship was a pure policy question, where there are differing opinions but the majority must prevail. To void the contract would give effect to the minority and void the majority opinions.

- Any kind of impropriety would be open to the shareholders to vote it down by shareholder resolution.
- The only exception is if it violated the articles of incorporation (it did not) or if it was oppressive or a fraud on the minority (it was not).

Conclusion:
Contract ratified in accordance with AoI and enforceable.

Hold, Order:
Action dismissed

Ratio:
A self dealing transaction will be enforceable if ratified by shareholder resolution in accordance with the articles of incorporation. The only way to void this is if it is oppressive or a fraud on the minority.

This was a walk back of the *Aberdeen* logic which was very strict on this topic. Generally speaking, a self dealing contract is enforceable if it is ratified by shareholders in a general meeting, premised on agency law principles

- Principal can ratify the unauthorized acts of their agents, applied in the context of a corporation, so long as it is not oppressive or a fraud on the minority

However, this is the common law approach. There have since been statutory amendments to this rule:

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 120 (1) A director or officer of a corporation who (a) is a party to a material contract or material transaction or proposed material contract or proposed material transaction with the corporation, or (b) is a director or an officer of or has a material interest in any person who is a party to a material contract or material transaction or proposed material contract or proposed material transaction with the corporation, shall disclose in writing to the corporation or request to have entered in the minutes of meetings of directors the nature and extent of the director's or officer's interest. (2) Subject to subsection (3), the disclosure required by subsection (1) shall be made, in the case of a director, (a) at the meeting at which a proposed contract or transaction is first considered, (b) if the director was not interested in a proposed contract or transaction at the time of the meeting referred to in clause (a), at the first meeting after the director becomes so interested, (c) if the director becomes interested after a contract or transaction is made, at the first meeting after the director becomes so interested, or (d) if a person who is interested in a contract or transaction later becomes a director, at the first meeting after the director becomes a director. (3) Where a proposed contract or transaction is dealt with by resolution under section 117 instead of at a meeting, the disclosure that would otherwise be required to be made in accordance with subsection (2)(a) or (b) shall be made (a) forthwith on receipt of the resolution, or (b) if the director was not interested in the proposed contract or transaction at the time of receipt of the resolution, at the first meeting after the director becomes so interested. (4) The disclosure required by subsection (1) shall be made, in the case of an officer who is not a director, (a) forthwith after the officer becomes aware that the contract or transaction or proposed contract or transaction is to be considered or has been considered at a meeting of directors, (b) if the officer becomes interested after a contract or transaction is made, forthwith after the officer becomes so interested, or (c) if a person who is interested in a contract or transaction later becomes an officer, forthwith after the officer becomes an officer. (5) If a material contract or material transaction or proposed material contract or proposed material transaction is one that, in the ordinary course of the corporation's business, would not require approval by the directors or shareholders, a director or officer shall disclose in writing to the corporation, or request to have entered in the minutes of meetings of directors, the nature and extent of the director's or officer's interest forthwith after the director or officer becomes aware of the contract or transaction or proposed contract transaction. (6) A director referred to in subsection (1) shall not vote on any resolution to approve the contract or transaction unless the contract or transaction is

(a) a contract or transaction in which, but only to the extent that, the director undertakes an obligation or obligations for the benefit of the corporation,
(b) a contract or transaction relating primarily to the director's remuneration as a director, officer, employee or agent of the corporation or an affiliate,
(c) a contract or transaction for indemnity or insurance under section 124, or
(d) a contract or transaction with an affiliate.

(8) If a material contract or material transaction is made between a corporation and one or more of its directors or officers, or between a corporation and another person of which a director or officer of the corporation is a director or officer or in which the director or officer has a material interest,
(a) the contract or transaction is neither void nor voidable by reason only of that relationship, or by reason only that a director with an interest in the contract or transaction is present at or is counted to determine the presence of a quorum at a meeting of directors or committee of directors that authorized the contract or transaction, and
(b) a director or officer or former director or officer of the corporation to whom a profit accrues as a result of the making of the contract or transaction is not liable to account to the corporation for that profit by reason only of holding office as a director or officer,

if the director or officer disclosed the director's or officer's interest in accordance with subsection (2), (3), (4), (5) or (7), as the case may be, and the contract or transaction was approved by the directors or the shareholders and it was reasonable and fair to the corporation at the time it was approved.

(9) If a director or an officer of a corporation fails to comply with this section, a Court may, on application of the corporation or any of its shareholders, set aside the material contract or material transaction on any terms that it thinks fit, or require the director or officer to account to the corporation for any profit or gain realized on it, or both.

The provision is pretty long and bulky, but the gist is this:

- Step 1: Disclosure
  - 120(1) requires disclosure
  - Director who is a party, or has an interest in a party to the material contract to the corporation they serve must disclose their interest
    - Can be a direct or indirect interest
    - Can also have material interest with any person who is a party to the contract (if it is their family or friends for example)
  - 120(2) and (3) have rules about when the director has to disclose
    - Must be in writing or entered into the meeting minutes
  - 120(4) is made when the person in conflict is an officer

- Step 2: Approval
  - 120(6): If the contract requires Board approval, the director with the material interest cannot vote on any resolution to approve the contract/transaction
    - But what if the contract needs shareholder resolution?
    - Can the director who has a material interest in the new agreement, if they are also a shareholder vote as part of the shareholder ratification to approve the deal? The statute says nothing on this
      - The better view is that they can vote in their capacity as a self interest shareholder (absent oppression and fraud on the minority)
      - Would have to do a *Beatty* analysis rather than look at the statute

  - 120(5): If the contract does not require Board approval, the director/officer must disclose their interest in the contract
  - Approval requirements are set out in the Articles of Incorporation
- Step 3: Contract/transaction is "reasonable and fair to the corporation"
  - 120(8): if the requirements of s120 are complied with, then the material agreement is not void/voidable only by reason of the material interest if the agreement was approved by the directors/shareholders and it was reasonable and fair
    - Would require some assessment as to the substance of the contract and whether it was reasonable/fair to the corporation
- Step 4: Failure to comply
  - 120(8.1): if there is failure to comply, a director/officer acting honestly and in good faith will not be accountable to the corporation and the contract is not void if
    - It is ratified by special resolution of shareholders (2/3 vote)
    - Interest was disclosed prior to shareholder approval, and
    - The contract was reasonable and fair to the corporation
  - 120(9): if there is a failure to comply, the courts have the power to set aside the contract on any terms that it thinks fit or require an accounting or both
    - The typical remedy will be to void the contract

The 'material interest' is not defined in the act, so what does it take for a director/officer to have a material interest?
- Generally accepted that financial interests count.
- But what about emotional or relationship interests?
  - Is it self dealing contract if a husband has his corporation enter into a contract with his wife's corporation for which she is director?
    - If the husband has shares, obviously material interest because there is financial interest
    - If he doesn't, no one knows
    - What are the underlying dynamics? If the director was acting in the best interest of the corporation, shouldn't be an issue
  - There is no reason why this should only be limited to financial interests; there are other interests that compromise a parties ability to best serve their corporation in the dealings of the contract

Dimo Holdings Ltd v H Jager Development Inc, (1998), 43 BLR (2d) 123 (Alta QB)

Facts:

Dimo Holdings (plaintiff) has Dianne as sole director, officer and shareholder. H Jager Developments ("HJD", defendant) has Dianne's husband, Herb, as the director.
- Dimo lends $50,000 to HJD with an interest of 50% per annum. Herb did not disclose his wife being the sole director and officer of Dimo when it took the loan.

Dimo then brings actions to collect $30,619 of the loan which remains unpaid
- HJD argues that the loan contract be set aside because Herb did not disclose his material interest in the contract as required by the ABCA

Issue:

Does s120 of the *ABCA* apply to the loan between Dimo and HJD?

Rule:

Section 120 of the *Business Corporations Act*

(1) A director or officer of a corporation who

(b) is a director or an officer of or has a material interest in any person who is a party to a material contract or material transaction or proposed material contract or proposed material transaction with the corporation

shall disclose in writing to the corporation or request to have entered in the minutes of meetings of directors the nature and extent of the director's or officer's interest.

Analysis:

Herb is not a director, officer or shareholder of Dimo. But, does he still have a "material interest" as capture in s120(1)(b)? Presumably it is a broad concept

- It requires a financial interest, but if it is material it needs to be more than insignificant. It is a question of fact.
- It could include an interest where the person could exercise discretion or control over sufficient shares so as to affect the financial outcome of a company

In this case, Herb does not have a material interest, so section 120 would not apply.

- Even if s120 applied, the remedy is permissive of the court's discretion under s120(9)
- The court would not exercise its discretion to set aside the contract here
- The interest was not reasonable, but the loan was, and the court should defer
- Even if the contract was not enforceable, plaintiff would have an unjust enrichment claim.

Conclusion:

Herb did not have material interest; s120 does not apply

Hold, Order:

Application denied

Ratio:

S 120 requires a "material interest", which does not have to be financial, but not insignificant. It can include a person having sufficient control over shares to affect the financial outcome of the company

- Court's power to issue award is flexible, and they may not intervene even if a breach is found

This finding is a little questionable. Herb's ability to contract was likely affected by the fact that his wife was on the other side of the deal.

- Also, wouldn't he have an indirect financial interest because his wife will get the money
- So, it could very well compromise his ability to deal properly

But the court said even if it applied, they would not apply their discretion to impose a remedy because the loan was fair and reasonable.

Zysko v Thorarinson (2003) ABQB 911 also tried exploring if a fiduciary's ability to bargain effectively has been compromised

- Where there is an emotional involvement rather than financial (like family or friends), the directors and officers actions ought to be suspect
- The purpose is not where the director gets a gain, but where their ability to bargain effectively on behalf of the corporation may be inhibited by some interest it has in the other side.
    - A personal relationship may be said to be inhibiting and thus a material interest if the disclosure of the relationship may be relevant to the corporate decision.
- Rule of thumb: there should be disclosure whenever the director/officer's involvement might be relevant to the corporation's decision making process. If the corporation would undertake more due diligence or assign another director to negotiate, then the contract is material and must be disclosed.
- This logic appears more compelling than the *Dimo* holding

Competing Director

This is the third source of fiduciary breach. If a director of a corporation sits on another board of directors of a competing corporation, it could be a breach of fiduciary duty. They can be either a director or officer in the competitor, so long as it is a fiduciary role.

- In *London and Mashonaland Exploration Co Ltd v New Mashonaland Exploration Co Ltd*, Lord Mayo sat on board of directors of both corporations, and the plaintiff corporation wanted to restrain Mayo from being director on the other.
  - The court did not accept this. They found than him sitting on the board of the other was not, in itself a breach of fiduciary duty. Something more is needed. If he disclosed confidential information in his role as chairman, that would ground the claim

This is the general proposition that it is not an issue to sit on a Board of a competing company, but logically speaking this cannot be the case. If there are two companies, in the same business, and the fiduciary of the plaintiff has information and uses it for the benefit of the competitor, that must breach fiduciary duty.

Sports Villas Resort, Inc (Re), 2000 NFCA 11

Facts:

Sports Villas was incorporated in 1992 to acquire and operate a golf course, hotel and resort outside of St. John's. Richard and Bruce Pardy (plaintiffs) were the directors of Sports Villas. Mr. and Mrs. Dobbin (defendants) owned Clovelly Golf course in St. John's.

- Mr. Dobbin is a director and shareholder of Sports Villas.

The plaintiffs seek an order under an oppression remedy to disqualify the defendants as directors of Sports Villas because of Mr. Dobbin's interest in Clovelly Golf Course Inc, which they allege is competing with Sports Villas.

- Also claimed that Mr. Dobbin appropriated corporate information and opportunity of Sports Villas for his own benefit.

Procedural History:

Trial judge rejected the application as they did not believe they could not carry out director roles as there was no competition between them

Issue:

Did the Dobbins' breach their fiduciary duty to Sports Villas by (i) their interest in Clovelly, and/or (ii) by appropriating a corporate opportunity/proprietary information of Sports Villas?

Rule:

Section 371/203 of the *Corporations Act*

London and Mashonaland: sitting on a competitor's board does not breach fiduciary duty if there is no material damages.

Analysis:

Question 1: Does Mr. Dobbin owe a fiduciary duty to Sports Villas?

Fiduciary duty exacts a strict ethic to honesty and good faith in the corporations best interests. This requires avoiding actual conflict of duty, but also potential conflict too.

- He obviously owes a duty to both companies as he is on the Board of both
- If there was a potential conflict, as there is no proof of actual conflict, and his role on the Clovelly Board cements it, this could breach the duty.

Question 2: Did Mr. Dobbin breach the duty by sitting on the competitors Board?

1. Competition Argument
   a. This fiduciary does not preclude multiple membership on board of different companies. Any assessment of claim of infringement of fiduciary corporate duty

based on a director's involvement in another business will invariably engage balancing interests within the circumstances presented by the case at hand.

        i. This is a balancing act of societal interests with fiduciary duties
        ii. People who have an aptitude for business ought be able to do so; to require other people could have a chilling effect on business efficacy

    b. The validity of the complaint needs two determinations:
        i. Whether there was actual competition between the two, and not simply Dobbin's dual directorship
            1. The golf courses were over 200km apart, which really begs how strong competition will really be
            2. The potential of competition from Clovelly on Sports Villa is quite low as the two have different markets.
            3. Unless the plaintiffs can establish that Clovelly actually competed with Sports Villas, there can be no basis for which Mr. Dobbin did not hold himself in a conflicting position through his ownership in Clovelly.
        ii. The balancing of public interests within the context of the claim

2. Proprietary Interest Argument
    a. The plaintiffs argued that there was an agreement that "all future golf course developments within the province would be acquired or operated" through Sports Villas. This would make Mr. Dobbin's involvement in Clovelly an appropriation of a corporate opportunity belonging to Sports Villas
        i. Must rely on trial judge findings since he heard the most information
        ii. There is no evidence to support the notion that an agreement was reached
        iii. It appears one of the plaintiffs also developed another golf course
    b. The plaintiffs also argued that Mr. Dobbin used confidential proprietary information of Sports Villas like marketing programs, operational procedures and management systems.
        i. There is also no evidence that Dobbins did this.
        ii. The management systems disclosed were ones that any reasonable managed golf course would use – that information was not unique to Sports Villas
            1. If he didn't get this information from Sports Villas, he could have got it from literally anywhere else.
            2. No evidence that he even had access to confidential information

Conclusion:

No basis for disqualification

Hold, Order:

Appeal dismissed.

Ratio:

There needs to be a contextual analysis to see if there was an actual competition that would favour liability for breach of fiduciary duty over the societal interests of allowing dual directorship

While this case was unsuccessful, it was nonetheless a departure from the *London* rationale that says run free and be on as many competing boards as you want. The court really stresses how much of a balancing act there is.

(1) Is there a fiduciary duty owed?

(2) Was the duty breached?

- a. Was there *actual* competition between the two corporations?
- b. Does balancing of societal interest with corporate interests support liability?

This is all highly factual and context dependant on the case at hand.

- The typical remedy for these breaches would be to remove them from the board of the other company

<u>Take Over Bids</u>

Why is there a potential fiduciary duty breach in a takeover bid situation?

- Hostile or unsolicited takeover bids
  - Imagine there is a perspective buyer (that is also a director) and is making an offer that was not sought out by the company
  - The Board of Directors is under obligation to act in the best interest of the corporation, but if they are taken over, the existing Board is at risk of losing their position
    - New companies will often do a clean state
  - Possibility that the board would lose their position if the acquisition goes through creates a potential conflict of interest
  - The Board must meet their standard of care, diligence and skill
    - Cannot oppress minority shareholders
  - A solution to this is the Board of Directors can insulate themselves against conflict of interest breaches by setting up a special committee of independent members of the Board that don't hold an executive position if the new company goes clean house.
    - They can advise the directors with respect to a hostile takeover bid
  - Look at the composition of the committee and see if there are any directors on it that would have a competing conflict of interest
    - Their decisions would be expected to conform to the standard of care of directors
    - Advice was one made pursuant to a good process and reasonable

<u>Other Sources of Fiduciary Obligations</u>

Directors have statutory duties

- Their fiduciary duty is owed to the corporation. *BCE* goes through what goes into the best interests of the corporation. Recall that it is not merely shareholder financial gain that needs to be considered, but a look at all internal factors as well
  - There may be a fiduciary duty that is not grounded in this statutory duty (arises outside the statutory framework)
- Do Directors owe a fiduciary duty to minority shareholders?
  - Not a question of whether the Board breached there duty to the corporation. We ask if
    1. The Board has a fiduciary duty that is not in statute, but on the facts of the case, and
    2. When do they have this duty and
    3. What does it consist of

Tongue v Vencap Equities Alberta Ltd, (1994) 148 AR 321 (QB) aff'd (1996), 184 AR 368 (CA)

Facts:

Tongue and Harrap (plaintiffs) were minority shareholders in Synerlogic. Negrin et al. (defendants) were also shareholders and directors of Synerlogic.

- Slator and McDougald (defendants) were directors (but not shareholders) of Synerlogic.

The defendants negotiated to sell the plaintiffs shares at $0.6/share to Vencap Equities (defendant corporation). The plaintiffs sold the shares and signed a release discharging any existing right of action and prohibiting a future action.

- The defendants did not disclose that a buyer was negotiating to buy them for $1.97/share. After Tongue sold their shares, Vencap sold them to the buyer for $2.16/share.

Tongue sued the defendants claiming damages for insider trading, contrary to s131 of the *Canada Business Corporations Act* and breach of fiduciary duty.

- They sued the corporation, the directors, both shareholding and non-shareholding.
- Defendants argued they don't have a fiduciary duty to minority shareholders, and also relied on the signed release.

Issue:

Do the defendants owe a fiduciary duty to minority shareholders?

Analysis:

Was there a Fiduciary Duty

There is no general duty that arises between a director and shareholders simply because that relationship brings them in proximity to eachother. But one can still exist.

- Fiduciary duties arise when directors act outside their normal duties.
  - It is clear that Mr. Negin was orchestrating the deal with Synerlogic, with Vencap as the intermediary. This cemented a different relationship between him and Synerlogic since it was outside the scope of his duties as a normal director.
    - Breach to not disclose that there is a potential buyer willing to pay more
- Fiduciary duties arise when directors purchases shares from shareholders
  - When a director buys shares from a minority shareholder, a fiduciary duty arises. The directors benefited from the transaction of the minority shareholders since they profited from the subsequent sale to the eventual buyer
  - The directors/shareholders purchased shares from the plaintiffs, meaning they each owed a fiduciary duty to disclose to them the fact of the eventual buyers interest
  - The individual directors were also shareholders indirectly through Vencap purchasing the shares of the minority shareholders
    - They breached this duty by causing the plaintiffs damage when they sold their shares at a price below their value.
- Fiduciary duties from other grounds
  - The defendants had information which the plaintiffs required to make an informed sale, but they did not disclose.
  - They used their positions for personal advantage at the expense of the plaintiffs.

The releases signed by the plaintiffs did not contemplate a loss of profit on the transaction in which they were immediately involved. They did not contemplate the defendants breach for s131 or fiduciary duty, and the defendants duty was not discharged and they are still liable.

- Each defendant is jointly and severally liable for the entirety of the plaintiffs losses

Conclusion:

Duty existed and duty breached

Issue:

Did the release negate liability?

Rule:

A release operates to cover what the parties had in contemplation: "a dispute that has not yet emerged, or a question which had not at all arisen, cannot be considered as bound and concluded by the anticipatory words of a general release"

Analysis:

The parties did not contemplate a release from liability for a breach of fiduciary duty in respect of the immediate transaction. The plaintiffs were not given knowledge of all the relevant circumstances.

- They are releasing their rights to subsequent purchase of the shares, but not contemplating a loss of profits in the transaction they were immediately involved in.

The release cannot operate to prevent a claim for insider trading under the scheme. No contract can release a duty they owe under statute.

Conclusion:

Duty existed and duty breached

Hold, Order:

Action allowed

Ratio:

Fiduciary duty between directors and shareholders is not given, but can be created in many cases:

- Fiduciary duties arise when directors act outside their normal duties
- Fiduciary duties arise when directors purchases shares from shareholders
- Other cases (not a closed list)

It is important to realize that while there is no statutory fiduciary duty from directors to shareholders (only the duty to the corporation is statutory), it could arise. The court here finds two specific instances where it could, but leaves the door open for more:

(1) Directors act outside the scope of their powers
(2) Directors purchase shares from shareholders
    (a) Look at the substance of the arrangement; in this case, the economic substance was such that the directors (who are also shareholders) enter into an arrangement with Vencap, pursuant to which they can make a large profit
    (b) Because they purchased the shares, they owed a fiduciary duty to the minority shareholders to disclose the price that the eventual player would want to pay
        (i) They breaches this duty and caused the plaintiffs damage by selling far below the purchaser's price
        (ii) The directors who are *not* shareholders would have no liabilty on this ground since they had no directness in purchasing shares.
(3) Other general grounds
    (a) This was more of a chance to look at the broad circumstances and ask if the nature of the relationship anchors a fiduciary duty

In this case, it was also established that insider trading, from s130 of the *ABCA,* was established. The gist of this is that insiders cannot purchase shares to the corporation on the basis of information that is not publicly disclosed.

- Insider trading provisions do not provide for joint and several liability because it imposes liability for the direct loss suffered by the plaintiff. Therefore, liability under this provision would be in proportion to the shares of the plaintiff which each director purchased.
- However, individual defendants are jointly and severally liable for the amount of the plaintiffs loss for their breach of fiduciary duty
    - Each defendant is responsible in full, and the plaintiffs may collect from one, or two, or more jointly, or all of them

Technically, if the defendants sought legal advice, they could have discharged their duty

- But legal advice is only as good as the information they have. Independent legal counsel would have no knowledge of the next purchase so it wouldn't help much
- The advice would be compromised because it wouldn't be based on the relevant information

<u>Shareholder Ratification</u>

Does a shareholder ratification cure a breach of fiduciary duty?

- Both the *ABCA* and *CBCA* have greatly reduced the effect of shareholder approval for curing breaches of duties
- Section 122(3) of the ABCA says that no provision in a contract, articles or bylaws relieve a director or officer from the duty to act, nor the liability for the breach thereof
  - This is subject to s146(7), which goes over when shareholders take on duties of the directors
- Section 243(1) of the ABCA also states that an action shall not be stayed/dismissed if only that the alleged breach of a right/duty to the corporation has been approved by the shareholders of the corporation.
  - But, this approval may be taken into account by the court when deciding whether or not to bring a derivative action on behalf of a corporation
  - Ratification is not a get out of jail free card, but it can be adduced.

<u>Dissenting Director</u>
There are important differences between the *ABCA* and *CBCA* provisions on this front.
- *CBCA* s123:
  - (1) A director who is present at a meeting of directors is deemed to have consented to any resolution passed or action taken at the meeting unless
    - They request a dissent to be entered in the meeting
    - They send a written dissent to the secretary before it is adjourned
    - They send a dissent in mail or delivers it to the office immediately
  - (3) A director who is not present at a meeting at which a resolution was passed or action taken is deemed to have consented thereto unless, within 7 days of becoming aware of a resolution, the director
    - Causes a dissent to be placed in the minutes
    - Sends a dissent by registered mail or delivers it
- *ABCA* s123:
  - (1) A director who is present at a meeting of directors is deemed to have consented to any resolution passed unless
    - Same three criteria as s123(1) of *CBCA*, or
    - Director otherwise proves that the director did not consent to the resolution
  - There are no provisions presuming consent if they did not attend the meeting.
  - This is important for potential liability
    - This only arises when an individual director is in attendance of the meetings
    - But, does that just mean that all directors need to do is not show up to avoid liability?
      - Maybe not, since not attending is not the requisite care and diligence of a director by failing to attend the meetings, so avoiding could also be a breach of fiduciary duty
      - Would also not be acting in the best interests of the corporation

Zwierschke v Minister of National Revenue also found that directors have a statutory duty to remit amounts withheld by the corporation as source deductions under the *Income Tax Act*.
- The *Act* provides that amounts withheld are deemed to be held in trust for the Crown. Whereas in this case, they used the funds held in trust to finance its business operations.
  - They did not exercise any degree of care, diligence or skill to prevent the failure to remit the amounts withheld by the Company
- This proved that other statutes can ground a duty, other than a fiduciary duty or statutory fiduciary duty

- Similarly, s119 of the *ABCA* imposes personal liability on directors for wages of employees of the corporation.

<u>Directors' and Officers' Liability in Tort to Third Parties</u>

This is a very difficult question of policy. On one hand, there is a principle that an incorporated company is separate and distinct in law from its shareholders, directors and officers, and it is in the interests of the commercial purposes served by the incorporated enterprise that they should as a general rule enjoy the benefit of the limited liability afford by the incorporation. On the other hand, there is the principle that everyone should answer for his tortious acts.

- Directors and officers, can, outside of statute have liability at common law.
- We know that corporations can have liability in tort, from the directing mind test, but can directors and officers have personal liability in tort, and not under statute

It is settled law that directors and officers can be personally liable for negligence causing death, injury or damage to property as well as nuisance (loss of amenity)

- Courts have always weighed the corporate interests that would shield them, but often found that the corporate entity do not have a mitigative effect from liability when serious injury or property damage occurs. In these cases, corporate law principles do not outweigh foundational principles of tort law
  - It is a tad different when the loss is purely pecuniary

Pure Economic Loss

(1) Directors and officers can be personally liable for fraudulent misrepresentation
  - (a) Corporate interests < Tort interests
  - (b) Even if the corporate veil is considered, which it is not in these cases, *Jin v Ren* found that fraudulent conduct was enough to pierce it

(2) Directors and officers can be personally liable for the intentional tort of inducing breach of contract, subject to the defence in *Said v Butt*
  - (a) Inducing breach of contract is a tort
  - (b) Liable unless defence can be established
  - (c) Salient because directors and officers often cause agreements and deals of corporations, so they are in a position to induce the breach of contract
    - (i) This is most often brought up when directors/officers direct a corporation to terminate an employment contract

(3) But, can directors and officers be liable for negligence causing pure economic loss?

<u>Inducing Breach of Contract</u>

McFadden v 481782 Ontario Ltd, (1984), 47 OR 134 (H Ct J)

Facts:

McFadden (plaintiff) was employed by PMAI for a fixed term and signed a contract of employment.

- PMAI was purchased by PMAC (corporate defendant). Mr. and Mrs. Taylor (defendants) were the directors of PMAC . PMAC thus became McFadden's employer.

Mr. and Mrs. Taylor caused PMAC to improperly transfer $32,000 to them, leaving P<AC with not money (established as a fraudulent preference). PMAC's financial situation worsened and had no more assets to pay McFadden's salary.

- He was immediately terminated. He brought action for wrongful dismissal against PMAC, but also inducing breach of contract against the Taylors

Issue:
Are the Taylors, as directors of the corporation, personally liable in tort for inducing breach of contract?

Rule:

369413 Alberta Ltd v Pocklington 7-part test for tort of inducing breach of contract

Analysis:

1. Existence of a contract
    a. Employment contract
2. Knowledge or awareness by the defendant of the contract
    a. Taylors had to have known about the McFadden-PMAC contract
3. A breach of the contract by a contracting party
    a. PMAC breached it by wrongful dismissal
4. The defendant induced the breach
    a. Corporations cannot act on their own, so the director *has* to induce it
5. The defendant, by his conduct, intended to cause the breach
    a. Taylors intended to cause this
6. The defendant acted without justification
    a. The *Said v Butt* defence goes here
    b. This defence says that if the employees were acting within the scope of their authority, and causes the breach of the contract between their employer and a third party, they do not become liable in tort
    c. This means that for them to be relieved of liability, it is not because they are the company's alter ego. It is because in so acting they act under the compulsion of a duty to the corporation and the action is thus justified
        i. If they are not acting under this duty, the act is no longer qualified and they become liable
        ii. The corporation is insulated from liability inasmuch as the director/officer acted outside the scope of their authority
        i. By procuring the termination, they were not acting in the corporations best interest, but securing the transfer of the greatest possible amount to themselves; "feathering their own nest". They were trying to extract money from the fraudulent preference and the ultimate aim of inducing PMAC to breach the contract was not for PMACs benefit, but the Taylors benefit
        iii. Defence not made out, not justified.
7. The plaintiff suffered damages
    a. McFadden was fired

Conclusion:

Individuals personally liable

Hold, Order:
Action to plaintiff

Ratio:
Inducing breach of contract can be saved by the *Said* defence: that the person acting in their bona fide authority, as per their duty to the company, can be shielded by liability. Acting in their best interests, rather than that of the company will vitiate the applicability of his defence

Fraudulent preference is when you deal with a debtor's property in a way that favours one creditors (in this case, the Taylors) over the other creditors of the company. The *Said* defence will come up many times, so this is an important example of applying it.

Negligence Causing Pure Economic Loss

The law respecting liability of directors and officers for torts committed while conducting corporate business is not entirely consistent. Some cases approach the problem from the perspective of the "duty of care', whereas others approach it from the perspective of "piercing the corporate veil". Some exceptions to general liability for tort have been recognized, and others have been rejected, without any clear principle emerging.

- Courts tend to come at it from a policy perspective, either on the corporate side or the tort side. This has made the category kind of ambiguous

There are three distinct lines of authority on this matter

1. *ScotiaMcLeod v Peoples Jewelers Ltd*
    a. Appears to support the conclusion that directors and officers are not liable for simple negligence causing pure economic loss
    b. ONCA 1995 case
    c. In this case, Montreal Trust purchased debentures (debt security) of People's Jewellers through ScotiaMcLeod, who was an investment bank who acts as an intermediary to sell securities to investors
    d. ScotiaMcLeod put together the offering documents with disclosures about the company (so investors can know if they want to invest or not). This is common practice, where the investment bank takes all the risk, so they purchase securities for the issuer, then put it on the market. In sum, Montreal Trust bought debentures and ScotiaMcLeod oversaw it
    e. Montreal Trust then brought an action against ScotiaMcLeod for producing fraudulent documents that did not disclose the financial position of Peoples
        i. This is crucial because investors who buy debt need to know the liabilities
    f. ScotiaMcLeod then brought an action to third party Peoples, saying that the individual directors of Peoples made negligent misrepresentations about their liabilities
    g. ONCA: in the absence of fraud, deceit, dishonesty or want of authority on the part of the directors/officers, liability will rarely attach
        i. Unless the directors/officers tortious acts are acting in a separate capacity from that of the company (such that their conduct was their own), their actions are attributed to the corporation and is shielded from liability
        ii. To hold them accountable, their activity must be outside their roles of directing minds and no identity between the corporation and the conduct
        iii. Directing mind theory states that directors/officers are acting in good faith of their authority and their actions are those of the corporation.
    h. Simple negligence causing economic loss would be pretty difficult to establish
    i. This case has been critiqued by saying that technically, negligence can be found, but it is practically impossible. It drastically limits personal liability
    j. In essence, it elevates policy considerations of corporate law above those of tort law, and negates most personal accountability – so long as they are acting on behalf of a corporation, they cannot be personally liable.
        i. Fraud/deceit would still be liable, but that is not simple negligence
2. *ADGA Systems International Ltd v Valcom Ltd*
    a. Appears to support the conclusion that directors and officers are responsible for the torts they commit – whether as directing mind or outside the scope.
        i. This is subject only to the defence raised in *Said v Butt*, which only applies to inducing breach of contract, so the defence is very limited
    b. In this case, Valcom directors persuaded all employees of ADGA to leave ADGA and join them, so ADGA brought action against the raid
    c. They argued that Valcom was inducing breach of the ADGA employment contracts.

    d. The court said that, in all events, the directors and officers are responsible for their tortious conduct, even if acting in their authority, subject to the *Said* defence
        i. But since it was the ADGA contract in question, which Valcom directors were not part of, the *Said* defence cannot apply
    e. Court really opens the door to liability; if plead correctly, liability can be grounded for directors acting in the course of their duties, even if they are acting in their authority, saying that the fraud/deceit from *ScotiaMcLeod* are not the only cases to anchor liability.
    f. This line of thinking has also been criticized saying the balance is too far the other way. Under this rationale, it is too easy to find directors/officers liable for their actions
        i. Would create a chilling effect on directors/officer since they would be acting with undue caution and likely not in the best interests of the company
    g. The balance is too heavily weighted on the tort law principles over corporate principles (what is the point of a separate legal entity if it does not protect them)
3. *Hogarth v Rocky Mountain Slate Inc*
    a. A contextualized approach which balances the policies and principles of tort law with those of corporate law.
    b. At each stage of the analysis, consider policy objective of corporate and tort law

Hogarth v Rocky Mountain Slate Inc, 2013 ABCA 57

Facts:
Suhan, Simonson and Powell (defendants) incorporated Rocky Mountain Slate ("RMS", corporate defendant) to develop a slate deposit project in BC. They established a limited partnership (LP) as a vehicle to invest in the project where RMS was the general partner (limited liability, do not conduct partnership affairs – passive investors). Simonson was director of RMS and president of the LP
- Hogarth (plaintiff) invests in the LP based on the misrepresentations of RMS in its capacity as general partner and those by Simonson
- Hogarth brings against RMS and Simonson as director of RMS

Procedural History:
Trial judge found the defendants liable for negligent misrepresentation as there was a duty of care from sufficient proximity and reasonable reliance

Issue:
Are the defendants personally liable for negligent misrepresentation?

Rule:

Morrow/ScotiaMcLeod: There are cases where the director/officer will ground personal liability in tort even if in the act of their duties.
- The tortious actions must be from a separate identity or interest from that of the corporation so the make the act/conduct their own

Analysis:

The precedent requires the analysis on if the person was acting on their own or not
- Here, Simonson did not exhibit a separate identity from RMS; they were acting as director at the time.
- The trial judge made no finding of their conduct in making the representations that were separate from his capacity as a corporate officer
    - The statements were made to raise funds for the corporation, so acting on behalf of them at the time of negligent statements

Conclusion:

Not personally liable

Hold, Order:

Appeal allowed

Concurring (Slater):
Personal liability of directors can be grounded in ordinary negligence, but here the individual defendants did not owe the plaintiff a duty of care. The test for negligent misrepresentation, as articulated in *Cooper v Hobart* should be used, but throughout the analysis, there should be emphasis and consideration of corporate and tort policy in establishing if a duty exists

- First, does the defendant owe the plaintiff a duty of care?
  - Stage 1: Is there a *prima facie* duty of care?
    - Is the harm that occurred a reasonably foreseeable consequence of the defendants acts?
      - Ought defendant reasonably had foreseen that the plaintiff would rely on any representation
      - Was the plaintiffs reliance on the representation reasonable in the context of the case?
      - The main issue: was it reasonable for the plaintiff to rely on the individual directors personal involvement so as to create a personal duty of care? This means they relied on the defendant in their *personal* capacity, not on behalf of the corporation, to ground the individual duty.
      - There are a number of factors to consider if plaintiff believed the defendants made comments in their personal capacity
      - In this case, it was reasonable for Hogarth to rely on the representations of the promotional documents
      - But, was it reasonable to believe Simonson made them in a personal capacity?
        - No, the investors knew they were dealing with an LP and readily took their advice, so they should be taken to know the legal consequences of that such that the only reasonable expectation was that they were dealing with a corporate entity
    - Is there a relationship of sufficient proximity between the parties such that it would be just and fair to impose a duty of care to the defendant
      - Were the parties relationship such that the defendant is obligated to be mindful of the plaintiffs legitimate interests?
      - It wasn't even certain which director made the statements, so sufficient proximity is not met
  - Stage 2: Are there residual policy considerations outside the relationship of the parties that may negate the imposition of a duty of care?
    - There is lots of overlap with the factors in Stage 1 to be considered.
    - A crucial policy consideration is the importance of the LP corporation
    - There is nothing illegitimate about using a limited liability business structure and imposing a duty would undermine the viability of that structure. This is a legitimate policy concern.
    - Need to directly weigh tort law vs corporate law interests
    - If plaintiffs knew they were getting involved with an LP, they themselves have a duty to know what they are involving themselves with
    - Finding personal liabilty is not piercing the veil, since it is not a corporate tort, but a personal tort.
      - Holding individual liable for a tort committed directly in pursuit of the company's business goals is the same as requiring the director to grant a personal guarantee for the tort liabilities of the company.

- In sum, a personal duty of care for Simonson should not be found; the tort is not sufficiently independent to engage him personally

Ratio:
(concurring) infuse tort and corporate policy consideration in the entire duty of care analysis

Slatter's concurring opinion is more germane to our purposes since it has since been embraced more than the majority's approach. Basically, you do a normal duty of care analysis as you would for tort law, but incorporate policy considerations of corporate law throughout the assessment. In his assessment of if there is a prima facie duty, Slatter referred to multiple factors that influenced his decision making:

- If the plaintiff chose to deal with the corporation (tilts away from a duty)
- Had the corporate relationship been imposed (tilts towards a duty)
- Was the tort independent (tilts towards a duty)
- Was the tort a closely related corporate activity (tilts away from a duty)
- Was the loss economic (tilts away from a duty)
- Was the loss physical (tilts towards a duty)
- Was negligent act committed while engaging in the business of the corporation (tilts away)
- Was the individual pursuing any personal interest beyond the corporate interest (tilts away)

He was concerned with the concern about individual liability on corporate structure and efficacy. Another consideration was if it was reasonable for Simonson to believe they were protected from personal liability by the corporate structure. This necessarily asks if it was reasonable for the plaintiffs to think a duty was owed outside the corporate structure

- In *Cooper v Hobart*, it needs to be "just and fair having regard to that relationship to impose a duty of care in law". With intentional torts like fraud, physical damage, or misconduct, a duty of care would be appropriate, but not in a case like this

In sum, there is only a personal liability for pure economic loss if the defendant guaranteed the results in a personal capacity

- Asking objectively, from a reasonable perspective, was it reasonable for the defendant to believe that they had the benefit of the LP?
- Was it reasonable for the plaintiff to rely on the statements made in an individual capacity rather than the corporate capacity?

In cases where there is physical and economic losses, they would need to be analysed separately

- When approaching these fact patterns, you should be aware of all three approaches, but *Hogarth* is the Alberta decision, so that line of thinking likely wins out
- However, even if Slatter was in concurrence, his approach has been more embraced. The Alberta court of appeal took his view in *Abt Estate v Cold Lake Industrial Part GP Ltd* (2019 ABCA 16), where they used a duty of care analysis to balance corporate vs tort law policy to conclude that the defendant was taking a personal responsibility
    - As such, Slatter's opinion is likely what the court would use
- *Hogarth,* when compared to *ScotiaMcLeod* or *ABGA,* is more consistent with the *Peoples* case, because directors and officers have duties to people outside the corporation and can be liable for negligence.
    - But this analysis is also more polished to determine whether liabilty will be found.

We saw the *Deloitte & Touche v Livent Inc,* 2017 SCC 63 case, which analysed if the corporation has liabilty in tort. This case summarizes the steps taken quite well:

1. Is there a prima facie duty of care?

a. Proximity: whether the parties are in such a 'close and direct' relationship that it would be just and affair having regard to that relationship to impose a duty of care in law
b. Reasonable Foreseeability: whether an inquiry to the plaintiff was a reasonable foreseeable consequence of the defendant's negligence
    i. The defendant should have reasonably foreseen that the plaintiff would rely on his/her representations, and
    ii. Such reliance would, in the particular circumstances of the case, be reasonable
2. Are there residual policy considerations outside the relationship of the parties that may negate the imposition of a duty of care.

Overview of Directors and Officers Liability

1. Statutory liability of directors/officers under s122, subject to the business judgement rule (*Peoples, BCE*)
    a. Section 122(1)(b): duty of care (*Van Corkum*)
    b. Section 122(1)(a): fiduciary duty
        i. Taking of corporate opportunity (*Cook, CanAero, Matic*)
        ii. Self dealing (*Aberdeen, Northwest,* s120, *Dimo*, *Zysko*)
        iii. Competing director (*Sports Villas*)
        iv. Shareholder ratification (s122) and dissenting director
2. Other sources of fiduciary duty (*Tongue*)
3. Other sources of statutory duty (*Zwierschke*)
4. Liability in tort to third persons
    a. Inducing breach of contract (*McFadden, Pocklington*)
    b. Negligence (*ScotiaMcLeod, ABGA, Hogarth, Abt Estate*)
5. Liability under derivative or oppression action (chapter 8)

CHAPTER 7: CORPORATE SOCIAL RESPONSIBILITY

There is a contemporary debate as to whether corporations have corporate social responsibility ("CSR") that go beyond their responsibility to shareholders.

- Shareholder proposals are a tool to achieve the social aims to direct the corporation to pursue certain social aims.
- Shareholder activism: shareholders can, under corporate law, make proposals that directors have an obligation to circulate as a general manner

There are two models of seeing the shareholders responsibility.

1. *Dodge v Ford Motor Company*
    a. Considered the "shareholder primacy model"
    b. This was a 1919 US decision which articulates the view of a corporation at law
    c. Ford was very wealthy in cash and bonds, and he was basically the Board of his car company. He decided to not pay out a dividend out of a cash surplus, and instead chose to reinvest it into the company to increase employment, sell cars for less and make them available to employers (called "Fordism)
    d. Two minority shareholders, the Dodge brothers (who went on to found Dodge) owned 1/10 of the stock in Ford and they brought action to compel Ford to pay out the dividend
        i. The court ordered the payout, so Ford appealed
        ii. Company argued that although a manufacturing company cannot engage in humanitarian business as its primary focus, that does not men they cannot conduct affairs in a way that promotes charitable purposes that are incidental to the broad aims of the company and be justified

    iii. The immediate effect was to diminish the value of the shares and returns to the shareholder, and certain decisions, altruistic and philanthropic can do this
  e. The Court said that a business corporation is organized and carries on primarily for the profit of stockholders. The powers of the directors must be consistent to that end.
  f. The discretion of directors does not extend to a change in the end itself, to the reduction of profits or the non distribution of profits among stockholders in order to devote them for other purposes.
  g. The court does say they are not business experts and should thus not interfere with Ford's business decisions, but that the duty was not met to the shareholders, and ordered the payment of the dividends.
  h. There was talk that Ford did this to punish the Dodge brothers since Dodge had already been started, and if this was true, they could have brought an oppression remedy
  i. Directors are supposed to always work for the benefit of the company and the shareholders, if they pursue other means the law can step in
  j. Milton Friedman coined the "Shareholder Primacy Model of the Corporation" where he finds pursuits of non shareholder goals antithetical to corporate profits.
  k. This is almost a "property view" of the corporation; if directors and officers decide to expend company resources to increase environmental standard above and beyond what is required at law, they are effectively appropriating funds that belong to the shareholders for an "improper purpose"
    i. Directors and officers don't have expertise in this area, so without the requisite competency, it wouldn't be right.
    ii. There are other institutions who can take on these goals, like environmental regulation, so within the bounds of the law, all directors and officers need to focus on is maximizing of shareholder value of their business.
2. Corporate Social Responsibility
  a. Contrary to the Shareholder Primacy model, CSR understands that the corporation has a social, and not strictly private purpose (the "social entity view" of the corporation)
  b. There is a movement away from the shareholder primacy model
  c. *Peoples*: "We accept as an accurate statement of law that in determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, inter alia, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment."
  d. *BCE*: "Directors, acting in the best interests of the corporation, may be obliged to consider the impact of their decisions on corporate stakeholders…. This is what we mean when we speak of a director being required to act in the best interest of the corporation viewed as a good corporate citizen." (BCE)
  e. CSR is the idea that a certain social accountability is expected on business stakeholders other than to the shareholders.
    i. One way to think of it is that the corporation exists through the exercise of public power of the state, so it is acceptable to engage in questions of what public power should be directed towards
  f. One criticism in Critical Legal Theory, and common in feminist theory, is the elimination of public-private division. Treat everything in a public light, so why can a corporation only care about profits.

In reality, corporations tend to follow a more Social Entity View. *Peoples* found there was a duty to the corporation but more than that, and *BCE* reinforced this. There are international standards that CSR should be reflected in domestic law

- These are not legal standards, but normative/aspirational commitments
- But recall that s122 of the *CBCA* codifies the *Peoples* holding that directors have to consider interests of other groups

There was a "Statement on the Purpose of a Corporation" from the Business Roundtable 2019
- This echoed the fundamental commitment to shareholders while still
  - Delivering value to customers, investing in employees, dealing fairly and ethically with supplies, supporting communities and generating long term value for shareholders

<u>Shareholder Proposals</u>
One-way shareholders can bring concerns to the management of the corporation. Some see it as a tool for shareholder activism to influence the board of directors over the business of the corporation
- It allows shareholders to challenge management and is a tool to forcing management to justify its decisions on issues and reflects CSR

Re Varity Corp and Jesuit Fathers of Upper Canada et al
- Shareholders of Jesuit request a proposal that the company end its investments in South Africa (during Apartheid) and be included in the annual general meeting
- They used section 131 of the *CBCA* which applies and provides that shareholders may require the company to circulate proposals and supporting statements with exceptions based on shareholder status, timing and content
- Varity brought an application for a court order permitting the company not to include the proposal under s131(5)(b) of the *CBCA*:
  - (b) it clearly appears that the proposal is submitted by the shareholder primarily for the purpose of enforcing a personal claim or redressing a personal grievance against the corporation or its directors, officers or security holders, or <u>primarily for the purpose of promoting general economic, political, racial, religious, social or similar causes,"</u>
- Varity argued that the corporation is not compelled to comply with a shareholder proposal like the one of Jesuit Fathers if it is clear they are doing so for personal causes or the underlined section above.
  - If the primary purpose of the proposal of all these things it can be blocked
- The proposal was framed that Varity's investments are at risk resulting from the political conditions in South Africa, not just that Apartheid is bad
- The court agreed with the corporation that it was very specific and is directly related to business interests of Varity, but the court goes on to say the primary purpose is abolition of Apartheid
  - Since it was primarily aimed at blocking social/political things, the application is allowed and the proposal does not need to be circulated
- This case has been (rightfully) criticized

As a result of this case, the *CBCA* was amended:

Canada Business Corporations Act, RSC 1985, c C-44
Section 137 (5) Subject to subsections (1.1) and (1.2), a registered holder or beneficial owner of shares that are entitled to be voted at an annual meeting of shareholders may (a) submit to the corporation notice of any matter that the person proposes to raise at the meeting (a "proposal"); and (b) discuss at the meeting any matter in respect of which the person would have been entitled to submit a proposal.

(6) (2) A corporation that solicits proxies shall set out the proposal in the management proxy circular required by section 150 or attach the proposal thereto.
(7) If so requested by the person who submits a proposal, the corporation shall include in the management proxy circular or attach to it a statement in support of the proposal by the person and the name and address of the person. The statement and the proposal must together not exceed the prescribed maximum number of words.
(5) A corporation is not required to comply with subsections (2) and (3) if
  (a) the proposal is not submitted to the corporation within the prescribed period;
  (b) it clearly appears that the primary purpose of the proposal is to enforce a personal claim or redress a personal grievance against the corporation or its directors, officers or security holders;
  (b.1) it clearly appears that the proposal does not relate in a significant way to the business or affairs of the corporation

The CBCA now just says it clearly appears that the proposal does not relate in a significant way to the business or affairs of the corporation, so it removes the list that used to be in (b) that was the basis to stop the proposal from circulation in *Varity*

- However, the *ABCA* has not been amended and still includes a similar provision:

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 136 (5) A corporation is not required to comply with subsections (2) and (3) if (a) the proposal is not submitted to the corporation at least 90 days before the anniversary date of the previous annual meeting of shareholders, (b) it clearly appears that the proposal has been submitted by the registered holder or beneficial owner of shares primarily for the purpose of enforcing a personal claim or redressing a personal grievance against the corporation, its directors, officers or security holders or any of them, or primarily for the purpose of promoting general economic, political, racial, religious, social or similar causes

CHAPTER 8: SHAREHOLDER RIGHTS & REMEDIES

Rights and Remedies

Shareholders have rights to vote, participate in profits, proposals (CSR). And Part 19 Shareholder remedies in the *ABCA*

- Special rights in event to fundamental changes under part 14 of the *ABCA*
  - The basic ides is that some changes to the corporate constitution/structure may be so fundamental that the *ABCA* puts procedures into place that shareholders have certain rights in terms of procedure
- Amendment to Articles of Incorporation need a special resolution (2/3 shareholders)
  - Changes to class or series of shares, and share cancellation requires 2/3
- Section 176: specify situations in which members of a class of shares are entitled to vote separately as a class
  - Requires a special resolution
- Section 189: continuance; corporations incorporated under the *ABCA* can continue in another jurisdiction if the Board wants it
  - But since this is a fundamental change, 189(4) requires a special resolution
  - 189(3) says all shareholders vote whether or not they have a right to vote
- Section 191: shareholders rights to dissent to amendment/amalgamation

- Shareholders are entitled toa right of appraisal
- If consenting to a change, s191(3) says that shareholders are to be paid for by the corporation for the share value of their shares.

The most common other remedies are oppression and derivative actions, but Part 19 remedies.

- Oppression Remedy: The right to action belongs to an individual of the corporation who is wronged; they can bring an action on their own right against the corporation or the Board of Directors
  - Section 242 of the ABCA
- Derivative Action: an action that can be brought on behalf of a corporation by an employee of the company
  - Since a corporation cannot bring an action itself, and requires someone to do it for them, there needs to be a mechanism for the corporation to bring an action that does not rely on the Board of Directors – what if the Board is the party doing the wrong?
  - It isn't a remedy, just a way to bring action
  - Section 240 of the ABCA

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Commencing Derivative Action Section 240 (1) Subject to subsection (2), a complainant may apply to the Court for permission to (a) bring an action in the name and on behalf of a corporation or any of its subsidiaries, or (b) intervene in an action to which a corporation or any of its subsidiaries is a party, for the purpose of prosecuting, defending or discontinuing the action on behalf of the corporation or subsidiary. (2) No permission may be granted under subsection (1) unless the Court is satisfied that (a) the complainant has given reasonable notice to the directors of the corporation or its subsidiary of the complainant's intention to apply to the Court under subsection (1) if the directors of the corporation or its subsidiary do not bring, diligently prosecute, defend or discontinue the action, (b) the complainant is acting in good faith, and (c) it appears to be in the interests of the corporation or its subsidiary that the action be brought, prosecuted, defended or discontinued. Relief by Court on the ground of oppression or unfairness Section 242 (1) A complainant may apply to the Court for an order under this section. (2) If, on an application under subsection (1), the Court is satisfied that in respect of a corporation or any of its affiliates (a) any act or omission of the corporation or any of its affiliates effects a result, (b) the business or affairs of the corporation or any of its affiliates are or have been carried on or conducted in a manner, or (c) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer, the Court may make an order to rectify the matters complained of. Section 239 In this Part,

(a) "action" means an action under this Act or any other law;
(b) "complainant" means
  (i) a registered holder or beneficial owner, or a former registered holder or beneficial owner, of a security of a corporation or any of its affiliates,
  (ii) a director or an officer or a former director or officer of a corporation or of any of its affiliates,
  (iii) a creditor
    (A) in respect of an application under section 240, or
    (B) in respect of an application under section 242, if the Court exercises its discretion under subclause (iv),

  or
  (iv) any other person who, in the discretion of the Court, is a proper person to make an application under this Part.

Step 1 is that you always need to fall in the range of "complainant" in order to bring an oppression remedy.

- For Oppression Remedies, the "oppressive, unfairly prejudicial" part is key
  - It is a broad and equitable remedy
  - Courts have made tests on how to determine whether there is conduct that meets this such that a court will grant remedies
  - Personal Action: complainant gets a right of action against the corporation or individual officers of the corporation
- For Derivative Actions, applications must be made to even bring the action
  - This is not like oppression remedies, which can be brought on their own.
  - The application for a derivative action must be approved first (s 240(1))
    - 240(1) "complainant may apply to the Court for permission to…"
  - The Court won't grant permission unless: (s 240(2)):
    - The complainant gave reasonable notice to directors of the intention to bring this action
    - The complainant is acting in good faith (not a personal vendetta), and
    - It is in the interests of the corporation for the action to be brought

Pathak v Moloo, 2008 ABQB 389

Facts:
Pathak (plaintiff) and Moloo (defendant) were directors and shareholders of Tech Steal, each owned 50% shares

- Pathak alleged that Moloo breached his fiduciary duty to Tech Steal through various means:
  - Appropriation of corporate opportunity (by a company owned by Moloo's wife where Moloo gave Tech Steal's confidential information causing unfair competition between TS and Conquest)
  - Failure to pay debts
  - Drawing salary without providing any real services to the corporation

Issue:
Can Pathak bring the derivative action on behalf of Tech Steal?

Rule:
Section 240 of the *Business Corporation Act*:
(2) No permission may be granted under subsection (1) unless the Court is satisfied that
  (a) the complainant has given reasonable notice to the directors of the corporation or its subsidiary of the complainant's intention to apply to the Court under subsection (1) if

the directors of the corporation or its subsidiary do not bring, diligently prosecute, defend or discontinue the action,

(b) the complainant is acting in good faith, and

(c) it appears to be in the interests of the corporation or its subsidiary that the action be brought, prosecuted, defended or discontinued.

Analysis:

(a) Reasonable Notice
  a. The application was filed before notice was given
    i. However, the requirement is only that the notice be reasonable
  b. So, the application is not precluded. It is not necessary to give notice prior to the application; the application was heard more than 4 months after notice was provided, which was sufficient time
  c. The particulars of the notice were clear, specific and no indication it was a fishing expedition

(b) Good Faith
  a. It is understandable that both parties are quite angry
  b. Courts do not see the anger/threats of legal actions as actions of bad faith
    i. If negotiations fail, legal action contentions are not unreasonable
  c. Good faith must be in commencing the action, not generally in all past or future conduct
  d. Bringing a derivative action is one option to resolve conflict, so presumably some degree of conflict must exist

(c) Interest of the Corporation
  a. *Prima facie* onus is on the applicant
  b. All that is needed is that the issues are arguable, not determinative. If there is possibility that issues are present, that is sufficient.
  c. Works even with contradictory evidence.

Conclusion:

Yes - can bring derivative action

Hold, Order:

Application granted.

Ratio:

Derivative action is not really an action, there needs to be some underlying action to bring it. As per s240, and the requirements to bring a derivative action:

- Reasonable notice does not have to be before filing; if it is given without enough time before it is heard, that will be reasonable
- Good faith conduct is in commencing the action, not the whole process
- Interests of the company is just as long as it is arguable.

Relief from Oppression or Unfairness

Deluce Holdings Inc v Air Canada (1992), 12 OR (3d) 131 (Ct J (Gen Div))

Facts:

Air Canada (defendant) and Deluce (plaintiff) owned Air Ontario Inc.

- Air Canada owned 75% of the shares, and appointed 7 directors
- Deluce owned 25% of the shares, and appointed 3 directors

The two parties had a USA, which allowed Air Canada to acquire Deluce shares on the termination of employment of both Stanley Deluce and William Deluce

- There was also an arbitration clause: any dispute over the values of the shares would be pursued through arbitration rather than litigation.

February 1989: Stanley Deluce's contract as chairman expired and it was not renewed
October 1991: employment of William Deluce was terminated

- Deluce alleged that Air Canada improperly exercised its majority control of the Board of Air Ontario to terminate Willian's employment for the sole purpose of enabling their buyout of Deluce's minority interest in Air Ontario.
    - Deluce argues it was "oppressive" within the meaning of the CBCA and the arbitration clause is of no force.
    - Air Canada brought application to stay the remedy on the grounds that it should be through arbitration

Issue:
Was the exercise of Air Canada's majority position on Air Ontario to acquire the interests of Deluce's shares "oppressive" on the minority?

Rule:
Section 241 of the *Canada Business Corporations Act*
(2) If, on an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates
    (c) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner

that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer, the court may make an order to rectify the matters complained of.

Analysis:
The USA didn't specify any details of the terminations needed to prompt the buyout, and any disagreements should be through arbitration. It appears that the decision by Air Canada's directors to fire William was unfairly prejudicial on the minority shareholder interests.

- While the conduct was not "oppressive" in the classic sense – not "lacking in probity, burdensome, harsh or wrongful", it is unfairly prejudicial since it unfairly disregards the interests of Deluce as a minority shareholder
    - This is contrary to s241 of the *CBCA*
- The decision to fire Deluce was clearly to acquire the minority interest
    - That may be a perfectly legitimate course for Air Canada under the USA, but the focus is not in if they can do it, but if it was prejudicial

Interests should not be mistaken with legal rights.

- A thwarted shareholder expectation (ie, an interest) is what the oppression remedy is all about. Shareholders buy their shares with expectations, some are reasonable in the circumstances.
- Acts which, by all means are valid exercises of the powers granted to the directors, may be outside the contemplations of the shareholders when they became members of the company and violate those reasonable expectations.

The USA bound the parties to act in good faith and for the best interest of Air Ontario. It was not the intention to allow Air Canada to trigger the buyout at will by causing the Air Canada nominated directors on Air Ontario to terminate William for that purpose

- Deluce had a reasonable expectation as shareholder of the management relationship with Air Canada as long as the Deluce's remained envisaged in the agreement.
- The termination of William was to acquire the minority shares, it was not in the best interests of Air Ontario.

Conclusion:
Air Canada's conduct was unfairly prejudicial

Ratio:
Oppression may require conduct that is harsh and egregious but can also include conduct that is unfairly prejudicial or disregards other interests.

Oppression Remedies are equitable, to protect the reasonable expectations of the complainant

Pursuant to the Act, and the *CBCA* and *ABCA* can be treated the same on this issue, there is a distinction between oppressive action (wrong or harmful), and prejudicial oppression (unduly fair on the minority).

- In these cases, either oppression or unfairly prejudicial will meet the standard for oppression remedies.

It is also important to realize that Air Canada did not really do anything wrong, legally speaking. They exercised their rights in the USA. However, the whole point of the oppression remedy is to protect the reasonable expectations of the complainant.

- Reasonable expectations are fact specific
  - A widely held corporation may ground different expectations than a small company with few shareholders
- The oppression remedy is equitable in nature, and thus it does not matter that Air Canada may have exercised it's legal rights, since it unfairly violated Deluce's reasonable expectations.

Air Canada tried to argue that the action should have only been a derivative action. Court rejects this.

- Oppression is conduct that may harm the corporation, and technically allow derivative actions, but that does not preclude the individual plaintiffs from using their personal action rights.
  - It is possible to bring both concurrently, but not always
  - If oppression fails, it is likely too late to bring a derivative action, so they are almost always brought at the same time.
- If directors wrong someone, is it the shareholders or the corporation that was wronged?
  - Again, fact specific. A wrong will often affect shareholders (like a drop in the value of their shares), but if the basis for the oppression was solely based on drop in share value, that is an indication that it should be a derivative action instead since it is usually something done to the corporation
  - Deluce was more than the shares dropping, it was a closely held corporation, there was a USA, an inappropriate termination

Recall the *BCE* case, where there was a leveraged buyout of all shares of BCE, which would require Bell Canada to take on massive debt and caused a loss in the value of the debentures

- We talked about this when considering the Business Judgement Rule, but we should *always* ask if the BJR can save the defendants in an oppression remedy.

The SCC sets out various principles, and is the leading oppression case. It also summarizes a good framework to use on these matters. They find that oppression is an equitable remedy (not just enforcing what is legal, but what is fair) and is fact-specific (looks to the business realities)

- What is fair/just/equitable depends on the reasonable expectations of the parties, and what those are depend on context and their relationship
- Conduct that is oppressive in one circumstance may not be in another.

Were the Debentureholders oppressed by the guarantee of the debt, within the meaning of the statute?

- Step 1: are Debentureholders "complainants" within the act (s239(b) of the *ABCA*)
  - Debenture holders are security holders in the company so satisfied
- Step 2: Go through the Oppression Test:
  - First, does the evidence support the reasonable expectation asserted by the claimant?
    - Factors to consider:
      - General commercial practice
      - Nature of the corporation

        - Relationship between parties
        - Past practice
        - Steps claimant could have taken to protect themselves
        - Representations and agreements
        - Fair resolution of conflicting interests between corporate shareholders
    - Second, does the evidence establish that the reasonable expectation was violated by conduct, falling in the terms "oppression", "unfair prejudice" or "unfair disregard" of a "relevant interest"
      - Oppression: conduct that is "burdensome, harsh and wrongful". A visible departure from standards of fair dealing, and an "abuse of power" going to the probity of how the corporations affairs are conducted.
        - Most serious wrong
      - Unfair prejudice: includes "squeezing out of a minority shareholder", failing to disclose related party transactions, changing corporate structure to drastically alter debt ratios, adopting a "poison pill" to prevent takeover, paying dividends without formal declaration, preferring some shareholders with management fees and paying directors fees' higher than industry norm.
        - Less offensive that oppression
      - Unfair disregard: favouring a director by failing to properly prosecute claims, improperly reducing a shareholders dividend, or failing to deliver property belonging to the claimant.
        - Least serious of the three
      - A pattern of distinct harms that harms a shareholder can satisfy one of these

On the facts, the Debentureholders did not show they had a reasonable expectation that the directors would protect their economic interests by maintaining investment grade rating of their securities. Offering documents (of which debentures are issued) had warnings that precluded and but the Debentureholders no notice that they may not retain them. This is used to prevent investors from reasonably expecting specific outcomes.
- In all competing bids, the treatments of the Debentureholders would have been the exact same

It is also a weak claim to say the Debentureholders had a reasonable expectation that the Directors would consider their interests
- Facts and process showed that the directors have to weigh the best interest of the corporation with different stakeholder interests.
- The Board met with Debentureholders and confirmed the contract would be honoured.
  - So, they did take their interests into consideration, meaning it is hard to say the conduct amounted to oppression
  - The Debentureholders could have refused to invest or tried to negotiate protections in context of a leveraged buyout
- The BJR was used here: they acted in the best interest of the corporation and that involves exercising judgement that is adverse to some stakeholders, so long as it was reasonable
  - Both the process and decision were reasonable

Re Ferguson and Imax Systems Corp (1983), 43 OR (2d) 128 (CA)

Facts:
IMAX was made by three married couples. The Husbands, Mr. Ferguson, Mr. Kerr and Mr. Kroiter all held common shares in IMAX (with the right to dividends and to vote). The Wives, Mrs. Ferguson, Mrs. Kerr and Mrs. Kroiter held class B shares (priority right to the dividend, non-voting and non-

redeemable). Non-redeemable mean that cannot be forced to sell shares back to the company if they leave, but they can be obtained pursuant to liquidation.

- Mrs. Ferguson was a film editor and significantly contributed to IMAX without getting adequately paid for the work she did
- All the men had day jobs with separate incomes

Mr. and Mrs. Ferguson divorce and Mrs. Ferguson is discharged by the company

- Although Class B shares have a priority right to common shares for cash dividends, the company did not pay them for two years.

A special meeting is called and a special resolution passed to amend the AoI and reorganize capital which would, in effect, result in redemption of Class B shares non-redeemable shares.

- Mrs. Ferguson would thus have no interest in the growth of IMAX. So, she sought relief under s 242, arguing the directors were oppressive with respect to her shareholder interests with the amendment to IMAX's articles

Procedural History:
Trial dismissed the remedy saying oppression was not made out.

Issue:
Did the conduct of the shareholders constitute oppression to ground the remedy under s242?

Rule:
Section 242 of the *Canada Business Corporations Act*
(2) If, on an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates
(c) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner
that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer, the court may make an order to rectify the matters complained of.

Analysis:
Step 1: Is Mrs. Ferguson a complainant as per s239?
- Yes, as a shareholder

Step 2: Did Mrs. Ferguson have reasonable expectations?
- This was a closely held corporation, which forces the court to consider the relationship which goes beyond the legal rights.
- Mrs. Ferguson's role in the company was important
- She had a reasonable expectation that her shares would remain nonredeemable, notwithstanding the divorce.

Step 3: Was the conduct oppressive, unfairly prejudicial or unfair disregard?
- There was an attempt by her ex-husband in concert with the other shareholders to squeeze her out. All actions that happened were to the main goal of squeezing her out; their intention was to deny her future participation in the growth of the company by force the sale of her shares through non-payment of dividends, violating her reasonable expectations.
  - She is the only one deprived since the other women got to continue participating in the profits.
  - The resolution was a culmination of a lengthy course of oppressive and unfairly prejudicial conduct towards Mrs. Ferguson.

It is important to note that technically the resolution was legally passed, since Mr. Ferguson convinced the other women to vote against Mrs. Ferguson to anchor the 2/3 majority. However, since oppression is an equitable remedy, what is otherwise completely legal, the nature of the relationships grounds the court to find a reasonable expectation was violated through oppressive conduct.

Conclusion:

Oppression made out

Hold, Order:
Appeal allowed

Ratio:
A closely held corporation, particularly one with close family relations, will likely ground reasonable expectations and must be considered when considering expectations and oppression.

The trial judge did not consider a factual matrix like the ONCA did in this case, which is why they came to a different conclusion. Again, the shareholders followed the law with all the conduct they did, but since oppression is an equitable remedy, the fact that their conduct created the resolution, which was unfair, it was still sufficient to ground this remedy

- Squeezing out is almost always unfairly prejudicial, and quite common. So if the fact pattern reflect this, the third step is likely easily established.

This case was confirmed in Alberta in the *Shefsky v California Gold Mining Inc*, 2016 ABCA 103. This case also confirmed *BCE* as the leading case on oppression remedies. The ABCA really contrasts it with derivative actions as well. A court's broad equitable jurisdiction under the oppression remedy is subject to the following governing principles:

(1) Not every expectation, even if reasonably held, will give rise to a remedy because there must be some wrongful conduct, causation and compensable injury in the claim for oppression
    a. Shareholder expectations are not determinative, need expectation and wrongful conduct
(2) Not every interest is protected by the statutory oppression remedy. Although other personal interests may be connected to a particular transaction, the oppression remedy cannot be used to protect or advance, directly or indirectly other personal interests
    a. Only interests as shareholder/officer/director which are protected.
    b. They are not intended to be a substitute for an action in contract, tort or misrep.
        i. The oppressive remedy is usually better for the complainant since it is equitable, so it is more attractive to pursue an oppression remedy rather than a breach of contract or tortious activity
        ii. But you must not dress up an action that should be something else
(3) The Courts can defer to the business judgement rule. The court must decide whether the directors made decisions that were reasonable in the circumstances and not whether, with the benefit of hindsight, the directors made perfect decisions.
    a. Recall that the Business Judgement Rule has two elements, a good process and a reasonable decision
    b. So long as the directors worked honestly and reasonably, and made a decision in the range of reasonableness, the court must not substitute their view and award deference
(4) Stakeholders' actual expectations are not conclusive. Reasonableness implies that the analysis is objective and contextual. In the context of whether it would be "just and equitable" to grant a remedy the question is whether the expectation is reasonable with regards to the context
    a. Even if there are reasonable expectations, and oppressive conduct, it will not ground oppression remedy. The impugned conduct must be oppressive to the interests of the complainant
    b. This is consistent with the rule in *Foss v Harbottle*
    c. The legislative response to this case was to make two different remedies, the derivative action and the oppression remedy. These two have two separate rationales, two separate statutory foundations
        i. Derivative action is a corporate remedy, oppression remedy is personal

Oppression or Derivative?

Personal actions (tort, contract or oppression remedy) are contrasted with derivative actions

- Oppression is better for a closely held corporation where minority shareholders are being oppressed
- Derivative action is a statutory means by which to bring action on behalf of a corporation
  - The distinction matters, and in terms of litigation, problems can arise if there is an improper claim being made for oppression. The litigation will be drawn out and it could be struck down for being improper when it should have been a derivative action
  - If this is the case, the limitation period may run out
    - Pursuing an improper oppression remedy claim may close the window to bring a derivative action.

Hercules Managements v Ernst & Young [1997] 2 SCR 165

Facts:

Guardian (plaintiff) was the sole shareholder of NGH company. He is also a non-voting shareholder of NGA. Hercules Managements (plaintiff) are also shareholders.

- Ernst & Young (defendants) were hired by NGH and NGA to audit financial statements.
- Both NGH and NGA then went into receivership because Ernst & Young negligently prepared the audits

Guardian and Hercules both bring action against Ernst & Young. Their claim for damages in tort was the loss they suffered for the values of their shares and claimed the defendants were in a contract with them to protect their interests.

- Defendants then brought a motion for summary judgement to dismiss the plaintiff's actions on three grounds:
  1. No contract existed
  2. Defendants did not owe them a duty of care in tort, and
  3. Claims can only be brough on behalf of NGH and NGA and not by the plaintiffs as shareholders.

Issue:

Did the accounting firm have a duty of care to shareholders?

Rule:

Foss v Harbottle: individual shareholders have no cause of action for wrongs done to the corporation and that if an action is to be brought in respect of such losses, it must be brought either by the corporation itself (through management) or by way of derivative action. Company's are liable in torts and contracts, but not the shareholder and no cause of action vests in the shareholder.

Analysis:

The plaintiff claim that if they had an accurate financial audit, they would have monitored the corporation closer and address shortcomings. But also, at least one of the plaintiffs claimed they made further investments in the company as a result of the audit, and wouldn't have without the audit. So the question becomes, did the auditors owe a duty to the individual shareholders for either 1) the ability to manage the company or 2) the investments.

- Was it reasonable that the individual shareholders would rely on the audits for their individual investment decisions or the management of the company

Company's are liable in torts and contracts, but not the shareholder and no cause of action vests in the shareholder.

- When a shareholder acquires a share he accepts the fact that the value of his investment follows the fortunes of he company and that he can only exercise his influence over the fortunes of the company by the exercise of his voting right
- In other words, shareholders have personal interests, but the audits were corporate.

The shareholders fail to acknowledge that they have two roles, one with a personal interest and one with collective shareholder interests. When exercising oversight and management, they do this for the corporation's benefits, not theirs. The audits were prepared for the shareholders for the best interests of the corporation.

- Audits were not made for shareholder investors sake.
- As such, any duty created would be owed to all the shareholders as a group, acting in the best interests of the company
  - Any wrongs based on the reports would be for the corporation, not the shareholders to recover.

Conclusion:

No duty established

Issue:

Can the claims be brought by plaintiffs as shareholders or on behalf of the corporation through derivative action?

Rule:

Oppression remedies are better as personal claims. Derivative actions are to be brought for the company.

Analysis:

The claim that there were losses stemming from an inability to oversee or supervise management are really derivative and not personal in nature. The corporation could have brought numerous causes of action, negligence, breach of contract.

- The corporation, who went into receivership, could have brought an action on behalf of the corporations against the auditors.
- Since it is the shareholders bringing action against auditors on their behalf, the question is whether they can do so

Conclusion:

Oppression remedy inappropriate.

Hold, Order:

Application dismissed

Ratio:

Need to distinguish when the claim is brought in the shareholders individual interest, or when it is a wrong committed against the corporation.

Even if there was a prima facie duty of care to the shareholders, there would be plenty of policy considerations to negate it as it would create indeterminate liability (anyone could rely on these and go after auditors for a number of reasons). It is thus crucial that the counsel file the right causes of action. Was the investment, and thus the duty, made for the company or the shareholders?

- It would be possible to make out a claim for individual negligence, but that would require going through a full individual duty of care analysis
- Personal investment decisions grounding a duty was not reasonably foreseeable; even if it was, the policy considerations would negate it.

There could have been a derivative action if the directors failed to bring actions against the auditors (which would require us to look at the *Moloo* factors.

Brunette v Legault Joly Thiffault S.E.N.C.R.L was a case where shareholders wanted to sue accountants for giving bad tax advice, which wound up the corporation.

- Would the corporation have a cause of action? Presumably yes
- Would the shareholders?
  - If they can demonstrate 1) a breach of distinct obligations and 2) a direct injury that is distinct from that suffered by the corporation

- Otherwise, it should be brought by a derivative action and shareholders don't have the right upon bankruptcy.
- You cannot shoehorn what is appropriately a derivative action into an individual claim in tort/contract or oppression remedy

It is possible, in principle, that the same pattern of conduct would amount to a wrong against a corporation, and if properly plead, a wrong against the individual personally
- Drawing these lines is not always clear
- SCC noted a "higher than usual management fees" to the management
  - If Directors/officers were paying themselves too much, that is a wrong against the corporation (misappropriation of corporations funds) so a derivative action
  - But if the corporation is closely held, salary may be a way to squeeze out a minority shareholder
    - This could form a pattern that is oppressive and could ground an Oppression remedy.

Remedy for both are different
- In derivative actions, directors/officer would have to pay the corporation back
  - Section 241: The court may make "any order it thinks fit"
- In oppression remedy, broader scope for addressing the wrong for the minority
  - Section 242(3): the court may make "any interim or final order it thinks fit"
- The statute provides broad discretion to the remedies in s241 and 242

Wilson v Alharayeri, 2017 SCC 39

Facts:
Alharayeri (plaintiff) held class A and B convertible shares. Wilson (defendant) held class C convertible shares. Wilson converted their C shares to common shares.
- He also played a key role in the Audit committee events which resulted in the Audit committee not letting the plaintiff convert their A and B shares into common shares.
- This resulted in a substantial dilution of the plaintiff's interest in the company

Procedural History:
Trial judge found the audit committee members were personally liable refusal to convert shares
- The Quebec Court of Appeal found the personal liability was appropriate

Issue:
Is Wilson personally liable for oppressive conduct against Alharayeri?

Rule:
Section 241 of the *Canadian Business Corporation Act*
(3) In connection with an application under this section, the court may make any interim or final order it thinks fit including, without limiting the generality of the foregoing,

Analysis:
Oppression is an equitably remedy that seeks to ensure fairness and what is just and equitable. Courts have broad, equitable jurisdiction to enforce what is legal and what is fair. Courts considering oppression are instructed to engage in fact-specific, contextual inquiries looking at business realities, not merely narrow legalities. The Act gives "broad discretion" to make "any interim or final order it thinks fit" but the discretion is not limitless. Have to look at what the plaintiff has a legal right to, but also a contextual inquiry as to the reasonably expectations that were violated through oppressive conduct. Two prong test from *Budd*:

1. Oppressive conduct must be properly attributable to the director because they were implicated in the oppression
    a. Must identify the individual officer/director as being implicated in the oppression
2. Requirement that the imposition of personal liability be fit in all circumstances. Once #1 is established, look to the four principles to the "fit" of this prong:
    I. Oppression must be fair a way of dealing with the situation
        a. There are 5 situations which are indicia of fairness, where directors:
            i. Obtain a personal benefit,
            ii. Increase their control of the corporation
            iii. Breached a personal duty as director
            iv. Misused a corporate power
            v. Remedy against corporation would prejudice other security holders
        b. Personal benefit and bad faith are hallmarks of conducting attracting personal liability in oppression, but not strictly necessary
            i. If they acted in good faith and did not get a benefit, it would be hard to attach personal liability
                1. If they obtained benefit but good faith
                2. If they didn't obtain benefit but bad faith
                    a. These are more unclear
        c. Decision is not binary, it can partially allocate responsibility to the corporation and partially to the director personally
    II. Order shouldn't go any further than necessary to rectify the oppression
        a. Not going into punishment, only to recover
    III. Any order may serve only to vindicate the reasonable expectations of the security holders, creditors, directors or officers in their capacity as corporate stakeholders
        a. Oppression protects reasonable expectations of the person in their capacity with the corporation, not for familial/personal relationships
    IV. Courts should consider general corporate law contract
        a. Basic idea that if other relief is more fitting, oppression should not be used, or another action at common law exists

In this case, the trial judge's remedy was appropriate since it went no further than necessary.
- Wilson played a major role I the decision that was oppressive conduct
- Personal liability was fit because Wilson obtained benefit (he converted shares and thus has a greater interest in the equity of the company)
- It was reasonable given the reasonable expectations in the constitution which allowed conversion of shares (that was then robbed)

Conclusion:
Personal liability is fit

Hold, Order:
Appeal dismissed

Ratio:
Attaching personal liability is possible in oppression remedies through a contextual analysis

While personal liability can attach in oppression remedies, they should not be used frequently given the contextual approach the courts will use, following the *Budd* logic. The likelihood of another remedy being better fit is often high.

Naneff v Concrete Holdings Ltd (1993) 23 OR (3d) 481 (CA)

Facts:
Nick Naneff establishes a company and built it into a very successful business. Both sons, Boris and Alex were intimately involved. Alex devoted his work life to the business (officer and director within

the corporate group and full time employee of the company). Alex and Boris were 50/50 owners in equity. Both brothers were supposed to take over the company after their dad.

- Eventually, Boris started excluding Alex from the business, dismissed and fired him.
- Alex claimed it was because Nick did not approve of his wife and lifestyle
    - So, Alex brought an oppression remedy

Issue:

Is Nick personally liable for the oppression remedy?

Rule:

Section 242 of the *Canada Business Corporations Act*

(3) If, on an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates

(d) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner

Analysis:

1. As former officer/director, does Alex count as "complainant" under the Act?
    a. Yes easily established.
2. Does the evidence support a reasonable expectation by Alex?
    a. Alex had the expectation that he and Boris would take over the corporation after the retirement/death of the father as was always the plan
    b. They were responsible for certain divisions in the companies and they gradually assumed more responsibilities over the years
    c. This underlies the entire corporate relationship of the Naneff family
    d. It was a reasonable expectation of both brothers that the would eventually take over the business.
3. Does the evidence establish that the reasonable expectation was violated through oppressive, unfairly prejudicial or unfair disregard conduct?
    a. The removal of Alex from his positions as officer, exclusion from day to day operations and from participation as director in any meaningful way constitutes "oppression" under the Act
    b. The powers of the family in particular was using corporate law as a way to discipline the son for his choices and to voice disapproval
        i. This is not a reason to ignore duties and obligations of the families corporate capacities. Corporate law interests must outweigh family desires
    c. He was treated the same as a nameless employee, not a family member

Conclusion:

Liability established

Issue:

What is the appropriate remedy?

Rule:

Section 242 of the *Canada Business Corporations Act*

(3) In connection with an application under this section, the court may make any interim or final order it thinks fit including

Analysis:

The remedy can be appropriately be broken into 2 pieces:

1. Dismissal from the company
    a. Two years compensation which was $200,000
2. Interest in the family company. Counsel suggested three remedies:
    a. An order restoring Alex to the positions that he previously held and remove Mr. Naneff from voting

i. This cannot be fair, this is essentially a punishment for the father, putting Alex in a better position that had the oppressive conduct actually occurred. Too punitive since Mr. Naneff still made the company
ii. Alex never had the reasonable expectation to take over the company while his dad was still alive

b. An order that the company be placed on the market for sale to the highest bidder, through the courts, to give both brothers equal chance
   i. Gives Alex an opportunity to continue participation in the company, but does not arbitrarily export fathers control
c. An order requiring that Mr. Naneff and Boris acquire Alex's shares at fair market value and considering that Alex owns, on his fathers death, a 50% chunk
   i. This would enable the parents and Boris to accomplish the very objective of their oppressive conduct; it would force Alex to chose between his lifestyle and the company
   ii. Not adequate

Family member situations do not justify oppression actions, but the dynamics of the relationship between the parties is very different from those of a normal commercial business, and this must be considered when fashioning a remedy. The broad discretion of courts to make an order it thinks 'fit' is subject to two limitations:

1. They must rectify the oppressive conduct only (not beyond undoing)
2. They may protect only the person's interests in their corporate capacity
   a. Can only take corporate law into account, not the familial relations
   b. Other factors are at play, but it goes beyond the practical utility of the remedy

What were Alex's reasonable expectations here?

- That he would ultimately be an equal co-owner of the business
- But only after the dad died/retired.
  - He could not be given ownership before this time, or it would be too punitive
  - Sale of the company would also be unfairly punitive to Mr. Naneff
    - This would advance his interests as a son, not as a shareholder

Requiring the defendants to purchase Alex's market shares is just an equitable, since it does not allow the family to get away with their conduct but goes no farther and does not impede the dads ability to retain control of the business and gives Alex his reasonable expectation

Conclusion:

Proposal #2 is the best option

Hold, Order:

Action allowed.

Ratio:

Remedies decided on a contextual analysis and only solve the oppressive conduct and no further

Cases like this are actually common where family law businesses are considered. When there is a falling out, corporate law is used to punish. In these cases, it is common that oppression remedies will be used by the courts.

Statutory Remedies

The *ABCA* does grant additional remedies that can be pursued other than oppression remedies.

I. Compliance and Restraining Orders
   a. Section 248
   b. If a member of the corporation fails to comply with a bylaw, AoI, USA, *ABCA* or regulations, then a complainant can submit an application to the court to order that the person comply with, or restrain from contravening any of those things

        i. If a meeting violates a bylaw, the complainant can apply to have the decisions made in the meeting void

c. A procedure is provided but the matter is usually pretty discrete, the bylaw was either contravened or it was not.
    i. This allows someone to bring an application in short order.
    ii. Court has broad discretion
d. When there are complex issues, like fiduciary breaches, this won't be used.

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 248 If a corporation or any shareholder, director, officer, employee, agent, auditor, trustee, receiver, receiver-manager or liquidator of a corporation contravenes this Act, the regulations, the articles or bylaws or a unanimous shareholder agreement, a complainant or a creditor of the corporation may, in addition to any other right the complainant or creditor has, apply to the Court for an order directing that person to comply with, or restraining that person from contravening any of those things, and on the application the Court may so order and make any further order it thinks fit

Caleron Properties Ltd v 510207 Alberta Ltd, 2000 ABQB 720

Facts:

Ron Slater is the owner of Caleron (plaintiff corporation), and in doing so he has indirect ownership of Class B shares of the numbered corporation (defendant).

- Class A Shareholders entitled to elect 4 directors
- Class B Shareholders entitled to elect 1 director

Shareholders resolution was passed amending the bylaws with respect to the Board of Director meetings that requires in person attendance at a registered officer, quorum requirements requiring Slater to be there and give Slater signing authority.

- Two Board meetings are held after without Slater there, not enough notice and not held in person.
    - A number of important matters were decided as well
- Slater was not happy, so he brought action under s248 for an order directing the directors to comply with the bylaws as amended by the shareholders and declaring the directors resolutions passed in the 2 meetings invalid.

Issue:

Does the court have jurisdiction to rule on the validity of the bylaw and to order compliance?

Rule:

Section 248 of the *Business Corporations Act*

If a corporation or any shareholder, director, officer, employee… of a corporation contravenes …bylaws … a complainant or a creditor of the corporation may… apply to the Court for an order directing that person to comply with, or restraining that person from contravening any of those things, and on the application the Court may so order and make any further order it thinks fit

Analysis:

Section 248 gives broad discretion to order compliance with the bylaws and specifically enumerates that corporations and directors as persons who may be subject to such orders. But, there is no justification for restricting its application based on that person having another standing – someone is not precluded from s248 merely because they can use another provision of the ABCA

- No justification for restricting application to the rectification of simple mechanical omissions.
- Difficult questions of fact and law can be treated under s 248

- However, the more complex an issue it is, the more it should be pursued using another avenue for the complaint.
- Discretion should not be confused with jurisdiction.

It is ultimately within the courts discretion to determine if there is sufficient evidence to grant summary relief. Inquiry into the legality/validity of by-laws may be necessary as part of the exercise of court's discretion under s 248.

Conclusion:

Court has jurisdiction

Issue:

Where the bylaw amendments passed by a majority of shareholders valid and binding?

Rule:

Section 122 of the *Business Corporations Act*

(2) Every director and officer of a corporation shall comply with this Act, the regulations, articles, bylaws and any unanimous shareholder agreement

Analysis:

Shareholders have the power to amend the bylaws under s102, and directors and officers have a statutory obligation to comply with the by laws under s122. However, bylaws derive their authority from the articles and are thus subordinate to them (they can't confer powers that are not excluded by or not conferred under the articles)

- Any inconsistency between the articles and bylaws, and the articles will prevail
- Altering the articles by a bylaw is void to the extent of the inconsistency

Amendments about quorum and signing authority (Slater had to be in attendance and had signing authority) confer powers that were not conferred in the AoI and alter the rights and privileges allocated to the classes of shareholders

- These are void and of no effect

By-law amendments going to notice of meetings and attendance in person at registered office are not inconsistent with the AoI

- These stand

Where there is partial inconsistency between a by-law and applicable statutes, it may be possible to sever the offending by law and let the rest operate

- To do this, the offending portion must be capable of being eliminated in a single stroke, while leaving the rest of the text intelligible
    - This is the case for the offending provisions can simply be struck
- If this is not possible, the court will have to analyze how they were drafted and try to determine if there is a way to sever it and not undermine the whole bylaw

Conclusion:

Business transaction at meeting invalid because it violated bylaw.

Hold, Order:

Application granted.

II. Dissolution
    a. Section 215
    b. The court can liquidate any corporation on shareholder application

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 215 (1) The Court may order the liquidation and dissolution of a corporation or any of its affiliated corporations on the application of a shareholder" (b) if the Court is satisfied that

i. a unanimous shareholder agreement entitles a complaining shareholder to demand dissolution of the corporation after the occurrence of a specified event and that event has occurred, or
ii. it is just and equitable that the corporation should be liquidated and dissolved.

Scozzafava v Prosperi, 2003 ABQB 248

Facts:
Henri Ltd had four directors: two Scozzafava members (couple) and two Prosperi brothers. The Scozzafava owned 50%, and the Prosperi owned 50%. Ms. Gardella (Scozzafava wife) was managing director of Henri. Henri operated under a license agreement which was granted and subsequently terminated by the Prosperi brothers.
- The Prosperi brothers then apply for dissolution under s215(1)(b)(ii)

Issue:
Can the dissolution be issued under s215?

Rule:
Section 215 of the *Business Corporations Act*
(1) The Court may order the liquidation and dissolution of a corporation or any of its affiliated corporations on the application of a shareholder"
(b) if the Court is satisfied that
(ii) it is just and equitable that the corporation should be liquidated and dissolved.

Analysis:
Section 215(1)(b)(ii) provides that the court may order the dissolution of the corporation if the Court is satisfied that it is just and equitable that the corporation should be liquidated and dissolved. *Noble v Keho Holdings* found 4 grounds on which it would be fair and equitable to order the liquidation of the corporation, only one needs to be established to ground the claim
- Deadlock in Management
  - Needs more than a stalemate
  - It needs to be so bad, that the parties can't even call a meeting
  - Two equal parties who are at complete odds with no way to resolve the deadlock (often USAs provide ways to resolve the deadlock)
    - Shotgun clauses to force the other to buy or sell shares (can't refuse the consequences once triggered)
    - Usually only with closely held corporations
      - Not in this case
  - This is compelling to order dissolution
- Business is akin to a Partnership
  - Something more than a purely commercial relationship exists
  - Is it more like a partnership than a corporation?
  - Association formed or continued on personal relationship with confidence
    - Refer to eachother as partners
  - In this case there was more than a commercial relationship, more like a personal endeavour
- Loss of Substratum
  - If, considering the circumstances under which the company came into being, and the main object of the company is determined, if it has failed, it may treat the substratum of the company as gone and the company cannot carry the real business for which it was formed, so a winding up order may be issued.
  - The license agreement rendered the corporation incapable of doing the objectives it set out to do
- Loss of confidence in management

- If the conduct of the directors (not in their private affairs) with regard to the company's business shows a lack of confidence from a lack of probity in the conduct of companies affairs, it is justified
  - Needs to be more than dissatisfaction at being outvoted on the business affairs

Because Henri is deadlocked with no means for it to end, and it is akin to a partnership and the substratum is lost, an order for the windup is justified

Conclusion:

Dissolution issued

Hold, Order:

Application granted.

The language of the provision is quite broad. "Just and equitable" is open to interpretation, so you kind of just have to get used to the kinds of situations where it would be appropriate.

III. Appraisal Remedy
   a. Section 191
   b. Shareholders can dissent and are entitled to be paid values of their shares
   c. Application can be made to fix the fair value, either by the corporation of the shareholders

(Alberta) *Business Corporations Act*, RSA 2000, c B-9

Section 191

(1) Subject to sections 192 and 242, a holder of shares of any class of a corporation may dissent if the corporation resolves to
   (a) amend its articles under section 173 or 174 to add, change or remove any provisions restricting or constraining the issue or transfer of shares of that class,
   (b) amend its articles under section 173 to add, change or remove any restrictions on the business or businesses that the corporation may carry on,
   (b.1) amend its articles under section 173 to add or remove an express statement establishing the unlimited liability of shareholders as set out in section 15.2(1),
   (c) amalgamate with another corporation, otherwise than under section 184 or 187,
   (d) be continued under the laws of another jurisdiction under section 189, or
   (e) sell, lease or exchange all or substantially all its property under section 190.

(3) In addition to any other right the shareholder may have, but subject to subsection (20), a shareholder entitled to dissent under this section and who complies with this section is entitled to be paid by the corporation the fair value of the shares held by the shareholder in respect of which the shareholder dissents, determined as of the close of business on the last business day before the day on which the resolution from which the shareholder dissents was adopted.

(6) An application may be made to the Court after the adoption of a resolution referred to in subsection (1) or (2),
   (a) by the corporation, or
   (b) by a shareholder if the shareholder has sent an objection to the corporation under subsection (5),

to fix the fair value in accordance with subsection (3) of the shares of a shareholder who dissents under this section, or to fix the time at which a shareholder of an unlimited liability corporation who dissents under this section ceases to become liable for any new liability, act or default of the unlimited liability corporation.

The purpose is for shareholders to receive the fair value of their shares. The valuation will depend on the facts and circumstances and appellate courts are reluctant to substitute trial valuation findings unless manifest error occurred.

- Expectation that the best value will be found and shareholder would only accept a reasonable offer

Available when AoI are amended and results in a fundamental change to the corporation. In the event of the dispute, the court can fix the value of the shares.

IV. Class Veto

a. Section 176
b. Also with fundamental changes
c. Holders of shares vote separately as a class. If they are restricted from voting from the fundamental change, they will have the right to vote still
d. Needs special resolution to approve the amendment
e. It is considered a veto, because if there is a fundamental change that changes a certain class of shareholders, they can vote for special resolution. If not, they are effectively given a veto to that change

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 176 (1) The holders of shares of a class or, subject to subsection (2), of a series are entitled to vote separately as a class or series on a proposal to amend the articles to (a) increase or decrease the maximum number of authorized shares of that class, (b) increase the maximum number of authorized shares of a class having rights or privileges equal or superior to the rights or privileges attached to the shares of that class, (c) effect an exchange, reclassification or cancellation of all or part of the shares of that class, (d) add, change or remove the rights, privileges, restrictions or conditions attached to the shares of that class and, without limiting the generality of the foregoing, (i) remove or change prejudicially rights to accrued dividends or rights to cumulative dividends, (ii) add, remove or change prejudicially redemption rights, (iii) reduce or remove a dividend preference or a liquidation preference, or (iv) add, remove or change prejudicially conversion privileges, options, voting, transfer or pre-emptive rights, rights to acquire securities of a corporation or sinking fund provisions (e) increase the rights or privileges of any class of shares having rights or privileges equal or superior to the rights or privileges attached to the shares of that class, (f) create a new class of shares having rights or privileges equal or superior to the rights or privileges attached to the shares of that class, (g) make the rights or privileges of any class of shares having rights or privileges inferior to the rights or privileges of the shares of that class equal or superior to the rights or privileges of the shares of that class, (h) effect an exchange or create a right of exchange of all or part of the shares of another class into the shares of that class, or (i) constrain the issue or transfer of the shares of that class or extend or remove that constraint.

(2) The holders of a series of shares of a class are entitled to vote separately as a series under subsection (1) only if the series is affected by an amendment in a manner different from other shares of the same class.

(3) Subsection (1) applies whether or not shares of a class or series otherwise carry the right to vote.

(4) A proposed amendment to the articles referred to in subsection (1) is adopted when the holders of the shares of each class or series entitled to vote separately on the amendment as a class or series have approved the amendment by a special resolution.

V. Investigations
   a. Section 231
   b. An investigation can be made on the corporation in enumerated circumstances.
   c. Sometimes it is really difficult to pursue an action for oppression because all the information will be within the corporation (someone claiming oppression likely won't have the information necessary to pursue the claim)
   d. These applications are made on camera but are private, not public
   e. Documents kept are confidential, and applicant not required to give security costs
      i. All to provide security holders oversight of the mismanagement to the internal matters of the corporation, which the security holder may not otherwise have access to.

(Alberta) *Business Corporations Act*, RSA 2000, c B-9
Section 231 (1) A security holder may apply to the Court, ex parte or on any notice that the Court may require, for an order directing an investigation to be made of the corporation and any of its affiliated corporations. (2) If, on an application under subsection (1), it appears to the Court that there are sufficient grounds to conduct an investigation to determine whether (a) the business of the corporation or any of its affiliates is or has been carried on with intent to defraud any person, (b) the business or affairs of the corporation or any of its affiliates are or have been carried on or conducted, or the powers of the directors are or have been exercised, in a manner that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of a security holder, (c) the corporation or any of its affiliates was formed for a fraudulent or unlawful purpose or is to be dissolved for a fraudulent or unlawful purpose, or (d) persons concerned with the formation, business or affairs of the corporation or any of its affiliates have in that connection acted fraudulently or dishonestly, the Court may order an investigation to be made of the corporation and any of its affiliated corporations.