**Biz Orgs** CAN

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**Chapter 1: Partnership Law Principles**

**Agency**

a relationship that exists between **two or more parties**

when one person is **agent**, who is considered at law **to represent the other, the principal**

in such a way that the **agent can affect the principal’s legal position** (making contracts, disposing of property)

***principal becomes bound by the contract (and agent is not a party)***

3 necessary ingredients:

1. **Consent** by the principal and the agent
2. **Action** by the agent on behalf of the principal
3. **Control** by the principal (determines what things the agent can do on their behalf)

* **Businesses are persons, but cannot do anything without agents acting on their behalf**
* Important that agent discloses to third party that they are acting on behalf of principal, so that the contract is not formed between rogue agent and third party

**Sole Proprietorships**

* least expensive form of business, money is important; no specific legislation
  + 2 sections in *Partnership Act* (88 and 89), must register name if you do not want it to be your own name
* income tax applies, but applies to everything so not really mentioned in course
  + do not need to share profits with anyone (unless you have borrowed)
  + no duties to consult with anyone, vote, etc.
  + when you die, your SP dissolves, does not continue on
    - people who rely on services like to have continuity
* unlimited personal liability – creditors can come over your personal assets
  + insurance becomes important
* really easy to change to a corporation from an SP (to save from tax, and other benefits)

**Partnerships**

* relationship between people, not a separate entity still
* Need two or more ‘persons’ (can be humans or corporations)
* **2+ persons must be carrying on business together with a goal to make a profit**
  + Do not actually have to make a profit, but must be for the purpose of making a profit
* Partnership can be implied, does not have to be written
  + Also, can alter the sections of legislation that apply through contract
* **3 kinds:** general partnerships, limited partnerships, and limited liability partnerships
  + most small business partnerships are GP – responsible for all debts
* biggest disadvantage is still the liability, joint liability – sections 11/12 of the Act

**[ADD condensed partnerships stuff]**

**Chapter 2: Evolution of Corporations Law / Corporate Personality**

**History**

***British Origins***

* Common law recognizes two principal forms of incorporation: (a) by exercise of **the royal prerogative** (letters patent/royal charter) and (b) by a **private or general act of the legislature**
* Until mid 1700s, letters patent was by far the most common
  + Main reason for incorporation Hudson Bay or East India Company was to give them monopoly over the territory, not for limited liability
* In 1720, *Bubble Act* was passed, restraining development of corporations law for 100 years; was devastating for business; finally repealed in 1825
* *Joint Stock Companies Act* was not adopted until 1844 – introducing incorporation by registration
  + In 1855, *Limited Liability Act* was past which finally allowed for limited liability, forced companies to have ‘limited’ after name to warn public about ‘dangerous’ new entity

***Canadian History***

* In 1849, acts passed in upper and lower Canada allowing for incorporation of joint stock companies for constructing roads/bridges; 1850 act then allowed for manufacturing and other purposes
  + 1860 and 1864 then allowed for incorporation by judicial decree and by letters patent; not abolished until 1970 when *Canada Business Corporations Act* occurred in 1975 (template for many provinces)
* In Ontario in 1970s, passed legislation that replaced letters patent with registration
  + Permitted one person companies, protected third parties dealing with a corporation, codified duties of directors/officers, regulated insider trading, improved minority shareholder protection, permitted derivative action, etc.
* In BC, passed Companies Act in 1973 which was very similar to federal act, but not the same (*sui generis*)
* ***Business Corporations Act* replaced it in 2002** 
  + Retains **‘contract plus registration’** model of incorporation (need both – incorporation agreement and registration with registrar)
* Businesses in BC can choose federal or provincial incorporation

***American History***

* In late 1800s, early 1900s, there was massive consolidation of businesses in monopolistic trusts – states were fighting this (because of potential for corruption), but there were major economic incentives to merge
* The Delaware Phenomenon – to generate more tax revenue, NJ changed its legislation to allow more business freedom – other states followed – a competition to see which state govs could be the most ‘hands off’ / race to the bottom
  + Delaware became the dominant US corporate jurisdiction
  + Pressure for federal government to intervene, but some argued that directors will do what is in the best interest of shareholders (accountability)
  + Push persisted for a while for federal corporate law, but faded away after WWI
* Canada – fairly flexible federal corporate law, so many companies incorporated federally and there was no ‘race to the bottom’ or Delaware phenomenon

**Differences between Canada and US**

1. US has far more publicly traded companies, absolute and per capita
2. Much more liquid market; only 5.3% widely traded in Canada
3. Concentration of share ownership is higher in Canada; only 14% of companies are widely held by investors as opposed to 63% in US
4. Highly interconnected corporate relationships in Canada
5. US does not have federal corporate law as Canada does, on top of provincial legislation
6. Canada does not have have a federal securities commission - we have provincial, US has national

**Securities regulation**

* Aim is to provide an informed, transparent and honest market in the publicly issued and traded securities of corporations
* Applies to all corporations regardless of where the issuer was incorporated
* Slowly through 60s-70s introduced more stringent requirements for disclosure, outlawed insider trading, etc.
* *Sarbanes Oxley* in US was echoed in Canada with even more stringent requirements

**Constitutional Issues**

* Federal corporations remain subject to provincial laws of general application; employment standards, consumer protection, and securities laws
  + **Paramountcy can apply if there is conflict between fed and prov laws**

**Salomon v Salomon & Co [1897]**

**F:** S incorporated his boot company by selling his personal business to the company at a price of 38,800; only shareholders were himself, wife and 5 children, each of whom had 5 shares; sale was made by issuing 20K shares to S, 1K in cash and 10K debenture

* company went into bankruptcy as a result of economic depression/lost gov contracts; S lent money to company, some of which were transferred to Broderip who paid cash
* Later in bankruptcy, liquidation could only pay out S’s debentures, not B and other creditors

**A:** liquidator claims company was a mere alias of S, and that S should indemnify the company for ordinary creditors before receiving any money – says this is fraud, wants to rescind loan contract, and says 20K shares not paid up

* S built up valuable business over 30 years, created a limited private company as family wanted part of the business, and to grow the business (good faith motive, no intended fraud/deceit)
  + Corporation was formed according/complying with legislation, no weird/abnormal internal rules (articles) for the company
  + Among reasons which induce people to form companies, is desire to avoid risk of bankruptcy, and increased facility afforded for borrowing money
  + Trades can be made without exposing persons interested in it in the event of failure to the harsh provisions of bankruptcy law; can also raise money on debentures
* **Price was fairly extravagant, over-valued by S as owner, but that has little bearing on decision**
* In almost every company that is formed, **subscribers are friends who sign their names without any intention to take further part or interest in the matter** – there is no requirement for balance or power, different minds and wills in the business; Act just requires 7 signatories
* **Any member of a company acting in good faith can take debenture as outside creditor**; every creditor is entitled to get and hold the best security the law allows him to take
* If shares are fully paid up, does not matter whether they are in hands of one or many

**C: Salomon not liable**

**R:** Company is a separate legal entity, not merely an alias of the owner

If a company is properly formed/incorporated, then:

A shareholder is **not liable to pay company debts**

A shareholder and the company are **two distinct entities**

A company may exist with **one shareholder** (or more)

A shareholder may **also be a creditor**, even in a one-person company

**Terminology**

* Corporation is separate legal entity from incorporator, directors/officers, shareholders, employees, etc.
* Can enter into contracts, be held liable; can own, buy and sell land / lease assets, can borrow/lend money, can be liable in tort
* Shareholder: provides money to corporation with hope of receiving dividends, increase in value of shares
* Share is not defined in *Act*, but is essentially a **bundle of rights** depending on class – that can be used against corporation or management of corporation
  + **Does not give you legal title to any assets of the company**

**Limited Liability vs Creditor Protection**

**Limited liability** is principal reason to incorporate – an investor will never be liable for more than their investment

* Shareholder’s assets are protected from liability (shareholder immunity) (s 87(1))
* **Other reasons:**
  + Can have separation between **ownership** and **control**
  + **Perpetual succession** – does not cease to exist when founder dies
  + **Transferability** – can sell/transfer shares to other persons
  + Reduces overall **income tax payable**

**Creditor protection -** Limited shareholder liability is at odds with lenders who want assurances of repayment

* Recommendations:
  + Register a security interest on the loan (mortgage on property)
  + Obtain a personal guarantee from the shareholder (in contract, loan agreement), increases liability
    - Subcontract with individual person (gets around Salomon)
  + Demand a higher interest rate if more risk
  + Advise it to refuse to lend to the corporation (if it does not make sense)
* ***BCA* has creditor protection built in**
  + **Corporate naming rules** (‘cautionary suffix’ – s 23,24) – Inc. / ltd. / corp. – must use when forming contracts, invoices, orders of goods/services, etc.
    - Duty as lawyer to tell newly incorporated company that they must use cautionary suffix
    - **Directors can have liability as well if not using suffix**
  + **Capital maintenance** – corporation must receive cash or true equivalent when issuing shares (s 64)
    - corporation must not pay dividends if insolvent or making payment would cause insolvency (s 70)
    - Ie. not able to pay its debts – creditors must get paid before profit sharing
  + **Publicity** – must be registered, gets published in Gazette; anyone can search registry, can find headquarters and has some rights to inspect it
    - Corporations must keep certain records; public companies have reporting standards/rules
  + **Officers’ and Directors’ liability** – remittances not paid to appropriate entity, employees not paid, environmental issues if affected (can give rise), torts (see below)
  + **Oppression remedy (see Chapter 10)**
  + **Duties in the vicinity of insolvency** (*People’s Dept Stores*) – shift towards creditor protection when approaching insolvency – eg. directors should not keep making deals when they ought to realize it is unlikely they will meet obligations
  + **Piercing the corporate veil (below)**

**Conflict of interest** – concerns/aims/goal of two or more different parties; goals are not compatible

* Lawyers are bound by different rules – 3.401 lawyer must not act or continue to act for a client where there is a conflict of interest, except as permitted under this code
* As a lawyer, must ask: what is the risk that my loyalty to a client would be materially/adversely affected by my own interest, duties to another client, a former client, etc.
  + To whom do I owe a duty of loyalty? Ie. If I receive several instructions, who do I listen to
* If the company is your client, even if you take instructions from an officer, employee, etc. **duty to act for the organization as a whole**
* **Can also take on a single director/shareholder as your client, but need to be explicit about to whom your loyalty is** – if you choose one person, recommend that the other people seek out independent legal advice
* can have joint retainer – can represent business and employee at same time as long as no conflict in goals

**Torts –** officers, directors are not shielded from personal liability in tort

* Examples: trespass, assault, libel, some negligence
* even if the person was acting in normal course of employment

*Said v Butt [1920]*

* Officer of a company could not be sued for procuring breach of contract between the company and other party
* Officers/directors could not be sued for committing **economic** torts if they are acting in normal scope of office
* This was modified by SCC in *ADGA*

**ADGA Systems Int’l Ltd v Valcom [1999]**

**F:** ADGA claimed that competitor Valcom raided its employees and caused economic damage – claiming against director and 2 employees who led the recruitment program

**I:** whether directors can be sued for actions as individuals when the actions were genuinely directed to the best interests of the company

**A: “The consistent line of authority in Canada holds simply that, in all events, officers, directors and employees of corporations are responsible for their tortious conduct even though that conduct was directed in a *bona fide* manner to the best interests of the company, always subject to the *Said v Butt* exception** (procuring breach of contract between your company and the other contracting party) – Valcom liable as they are not privy to contract

* *Lewis v Boutilier –* does not matter if the corporation might also be liable
* *Berger v Willowdale –* action against officer allowed despite action against company being barred by *Workmen’s Compensation Act*

**Baron Summary:** there will be situations where there will be cause of action against company and senior management, but never against a shareholder who is just a shareholder

* There **is independent cause of action against an officer/director for breach of fiduciary duty**, as well as a cause of action against the company

**Piercing the corporate veil**

* There are situations where we look through the company into the particular shareholders (‘disregarding the separate legal personality of the corporation’)
* Categories:
  + **If a company is created for fraudulent purposes** (*Lynch*), courts will pierce through company and extend liability to shareholders
  + **If there is conflict with other legislation, like *Income Tax Act***, courts can look in favour of CRA and extend liability
* Holding company – a company that buys shares of subsidiary companies – can own lots (wholly owned subsidiary, or not)
  + Does not have any operations, just set up for liability / income tax reasons
  + Parent company is similar but usually has its own operations

**De Salaberry Realties v MNR [1974]**

**F:** two wealthy families incorporated a variety of companies, and had a ‘grandparent’ company that owned shares of subsidiary (‘parent’) company, that owned shares of sub-subsidiary (‘sister’)

* Incorporated a new sister company for the purpose of buying land, to develop and purportedly build shopping malls; what they were actually doing was **buying and selling land to make a profit**
  + All policy/decision-making done at grandparent company level
* CRA did not agree with how they were filing their taxes, wanted to collect

**Court considerations:** at sister level, businesses were buying land for as much as $2M, but the share structure was valued at tiny amounts like $1000 – companies were just borrowing from the other companies (thin capitalization)

* + Thought it was a half-hearted attempt to look like they were actually doing business
  + They were careless about zoning bylaws so intention was clearly just to sell it at a profit
  + Minister was curious why they needed so many sister companies, why not just one?

**I:** Should the corporate veil be lifted and the collection of companies analyzed as one? (increases tax liability here)

**A:** The appellant company is a shield – its conduct must be ascertained by the course of conduct of **the whole group of companies** – the parent companies are in an intimate and immediate domination of the appellant company which has **no independent functioning on its own**

**R: 6 considerations** for determining whether a subsidiary was carrying on the business of a parent company

1. Were the profits **treated as profits of the parent company**?
2. Were the persons conducting the business **appointed by the parent company**?
3. Was the parent company the **head and brain of the trading venture**?
4. Did the parent company **govern the adventure**, decide what should be done and what capital should be embarked on the adventure?
5. Did the parent company **make the profits by its skill and direction**?
6. Was the parent company in **effectual and constant control**?

**Need these considerations + some policy concern (eg tax avoidance)**

**Clarkson v Zhelka [1967]**

**F:** Selkirk incorporated several companies, was controlling shareholder; one of those many companies (Industrial) bought land 1959 – money came from other companies in loan

* In 1960, Selkirk, for Industrial, transfers land to sister Zhelka for promissory note worth $120,000
* In 1961, Zhelka mortgages the land to G; Z doesn’t pay, so G commences foreclosure action; part of the land was sold, and the cash was used to pay off mortgage and a province of ON tax lien
* Z receives interest adjustment and it ends up in another of S’s companies (Fidelity)
* S went personally bankrupt in 1960, Clarkson was appointed as trustee, trying to figure out who owns what
* Claims that the transfer to Z not real, should be able to pierce corporate veil and go after that land
  + They think he transferred it to escape his creditors

**A:** The companies in S’s corporate structure were interrelated in that there were transfers of assets from one to another, or advances of money between them, although none were subsidiaries

* Only person to benefit financially from their operation was S himself
* S was not called as a witness, and there are many gaps in evidence – too much has been left to unsafe conjecture
* His companies are all under his power – his nominees are all family members that he likely dominates in decision-making (all one-man companies)
* **Money that ended up in Fidelity was really the property of Industrial, and was relatively minor**
* **Industrial was not created for any fraudulent purpose**, when it was created in 1958 there **is no evidence that S was insolvent** – cannot trace any of S’s personal assets into the hands of industrial
  + this is not a case where a debtor has transferred his own assets to a corporation of his making for the purpose of avoiding existing personal liabilities or obligations, nor has he made secret profit
  + general rule is *Salomon*, and only exception is where it would be **flagrantly opposed to justice to not pierce the veil**
  + “if a company is formed for the express purpose of doing a wrongful act, or if when formed, those in control expressly direct a wrongful thing to be done, the individuals as well as the company are responsible to those to whom liability is legally owed”
* Therefore, not going to pierce the corporate veil here – they are two distinct entities, **no fraudulent purpose**

**Lee v Lee’s Air Farming [1961]**

**F:** Lee operated a business flying an airplane over farming land spraying fertilizer (was essentially a one-man company); was appointed governing director of the company for life, and was appointed chief pilot at a salary arranged by him;

* one article held that master servant relationship will exist between him and company in course of employment
* Lee died flying his plane – wife is claiming compensation from workers compensation board
* Board claims that **because he was governing director who had all control of the company, he cannot be a servant of the company**

**A:** **Lee died carrying out his duties as an employee, not as a director**

* He was **paid a salary** which was recorded – work that was being done was **at request of customers whose contractual rights were only against the company**
  + Cannot be said that when he died he was discharging duties as a governing director
* Just as the company and deceased were separate legal entities so as to permit of contractual relations being established between them, so also were they separate legal entities so as to enable the company to give an order to the deceased (contract was made between him and the company)

**R:** a person who is president/director of corporation can also be an employee of the corporation

**Lynch v Segal [2006]**

**F:** Marital breakdown, wife L applies for spousal/child support, husband S flees the jurisdiction

* L then seeks a court order against his corporations because S has no assets in his name
* When S set up companies, he set it up to distance himself from his wife and his creditors in every possible way - He was an expert at setting up these corporate screens, using aliases, etc.; incorporated by an Ontario solicitor D
* there were lots of blank spots in filings – incorporated on behalf of an unnamed beneficial owner, no recording letter (notes/summary), transfer forms/share forms were blank
  + D instructed to appoint himself as sole shareholder/director of company, to prepare and execute the blank forms providing that the land be held in trust for the beneficial owner
  + He was told to resign as director and send blank forms to S’s solicitor on obscure island country
* This was done allegedly because there was ‘mysterious high-end foreign investor’ operating through the trusts
* S had already done similar things to his mansion and other assets where money was transferred to untouchable foreign bank accounts after selling off assets

**A:** Mr. Siegel and his corporations can be treated as law as the same thing – he is beneficial owner of shares/land

* General rule is *Salomon* – that a corporation is unique legal personality
  + But, in *Wildman*, court addressed that it is **not an absolute principle** – courts will not enforce ‘separate entities’ notion where ‘it would yield a result too flagrantly opposed to justice, convenience or the interests of the Revenue’
* A more flexible approach is appropriate in the family law context, particularly where – as here – **the corporations in question are completely controlled by one spouse, for that spouse’s benefit, and no third parties are involved**
  + In *Wildman*, in similar circumstances, court ordered to put a charge on **companies as well as him personally**, to pay the spousal support payments
  + “The law must be vigilant to ensure that permissible corporate arrangements do not work an injustice in the realm of family law” – *Wildman*
* S was using the corporate structure for one sole purpose, to disguise his property so that his spouse and children would have no claim against him should he ever defend against a claim
* **Piercing the corporate veil is an essential mechanism for ensuring that a spouse and children of the marriage receive the financial support to which, by law, they are entitled**
* Would put vesting order on the lands

**R:** *Salomon* does not apply when separate personality is used for the purpose of avoiding financial obligations (fraudulent purpose), especially in the family law context (‘flagrantly opposed to justice’)

**Chapter 3: The Process of Incorporation**

**Differences between BC and Federal legislation**

* **BC**
  + **No residency requirement**
    - Federally – 25% of directors must be residents of Canada (not necessarily citizens)
  + **Directors** have a lot **less liability** – eg. if a company does not pay wages, director can be liable for 2 months of pay, federally can be up to 6 months
  + More difficult for **shareholders to remove a director** – must do a shareholder’s resolution (vote), need 2/3 (default) to throw them out (can be up’d to 3/4s in the articles)
    - Federally, must only be simple majority (50%+1)
  + Legislation does not dictate how **many years a term can be for directors** – is determined by the articles
    - Federally, directors **cannot exceed 3 years** (can only make shorter); but can stand for reelection
  + Easier for the company to pay dividends
    - Federally there are more stringent requirements for solvency (extra steps)
  + **Can waive AGM** if all shareholders agree (mainly for family businesses)
    - Federally, can delay meeting but must have it
  + **Company can own its own shares** – eg. small company, only a few shareholders and one wants to exit, if cannot sell them or do not want to bring anyone else in, the company can purchase them (not available federally)
* **Federal**
  + **Better protection for your corporate name** – highest name protection outside trademarking
    - Take priority, even if provincial name already registered
  + Have right to carry on business in all provinces
  + **More investors are familiar with CBCA**
  + Better protection for minority shareholders

**Carrying on a business**

* **It is an offence for a foreign company to carry on business in BC without registering**
  + But, offenders are rarely prosecuted, will generally be fined by BC government
* ON definition – deemed to carry on its business in ON if, *inter alia*, it has a ‘resident agent, representative, warehouse, office or place where it carries on its business in Ontario’
* **BC definition** – s 375 BCA – very broad definition compared to ON – not limited to statute (‘**it otherwise carries on business**’)
  + Also note ss 374-379 (foreign/extra-provincial registration section)
  + Exceptions – banks, railways, only because it has interest as limited partner in LP in BC, etc.
* **If BC company wants to carry on business elsewhere** (continuance) – need to (i) obtain **consent from shareholders (special resolution)**, (ii) **apply to** **registrar**, and then (iii) **meet requirements of foreign jurisdiction**
  + SK, BC and AB can register all at the same time (reciprocal agreement)
  + Continuance = move into extra-provincial jurisdiction and carry on business
  + **If moving into foreign jurisdiction – get external council from that jurisdiction**
  + If a foreign company wants to continue in BC – fill out continuation application (s 302-311)
* Unlicensed extra-provincial companies are usually incapable of bringing actions on contracts they have signed
* Amalgamations permitted: s 269; Amalgamations into foreign jurisdictions: s 284(1)

**Company is deemed to be ‘Public’ if:**

**(1)** If company has **any of its shares listed on stock exchange**

**(2)** If company has **filed a disclosure statement/prospectus with securities commission**

Note: If it is the result of an amalgamation/private arrangement, if it puts you in first two categories, you are public

**One-person corporations** – 1963 BC case claimed ‘meeting’ requires more than 1 person, rejected by legislation (s 172, 140) – meeting can be held by only one person

**C3 – bridge gap between corporation and non-profit society (***Societies Act***) –** under societies act, cannot pay dividends, so not a lot of personal benefit to invest unless its just a donation

* Corporations are opposite, can pay dividends
* C3 can still generate profit, and some profit can be paid to shareholders (even though most gets reinvested into business) – cap on dividend is 40% of profits
* Types of business you can have is quite broad – just need community purpose
* Easier to register C3 under Act than registering charity under Income Tax Act
* **Signals to community that business has legal obligation to have special social purpose;** higher degree of accountability, need to have 3 directors, extra annual disclosure requirements

Note sections BCA: 55.91-94, 51.97

**Corporate Names**

* To prevent members of public from being misled about what entity they are dealing with (tackles confusion)
* Identical or very similar names to one that already exists will be rejected by registrar
* Most corporate names have 3 distinct parts: (i) distinctive part (ii) descriptive part (iii) corporate element/cautionary suffix (inc. ltd. corp. corporation, or full words, or French equivalent)
  + 2 surnames is okay, or your own first/last name + suffix, can be numbered company
  + eg. Pinnacle Consulting vs Pinnacle Landscaping is okay, as long as not in same industry (confusing)
* Trademarks will take priority over any name registration

Note sections: BCA 21-29, 263

**Process of Incorporation**

* **Can reserve a name** for a period of time after it is approved (56 days) while other requirements are met (s 22(2))
* (1) **Incorporation agreement –** prepared by lawyer, statement of intention to incorporate under specific statute and buy certain shares, lists authorized share capital, signed by incorporator
  + Incorporation agreement + notice of articles = **memorandum**
  + **all 3 documents = corporate constitution**
* (2) **Create articles –** internal rules of the company – signed by incorporator (not on public registrar)
  + Can use standard form provided in regulations, or can customize with lawyer
* (3) **File online ‘incorporation application’**
  + **list records office** – can be regular office or law firm
  + **list directors names and addresses**, officers if applicable
  + **describe authorized share capital** – max, amount, class, if there are any rights/restrictions [yes/no]; whether shares have par value or not – fixed sale price for tax advantage in BC (not fed)
  + **share rights or restrictions available** – whether they are voting shares or not (not on all decisions, but at AGM), whether they can receive profit sharing/dividends, priority for profit sharing (preferred), and priority on dissolution, redemption/retraction – whether company can buy back (prov but not federal)/whether investor can leave when they want
  + dividends can be mandatory/fixed, or whether it is a management decision
  + **do not need:** to state the business’ purpose (different from C3)
    - articles can have restrictions on purposes that must be overruled by shareholder agreement
    - **Also do not include notice of articles or shareholder names**
* **Solicitors must create minute book** – contains cert of incorp, corporate constitution, resolutions, CSR, etc.
* **If the required forms are handed in properly, registrar must accept them and issue certificate**

**companies are allowed to change articles**

* needs a shareholder’s resolution with a simple majority, unless established otherwise
* changing or creating class of shares is changing the corporate constitution, need consent from shareholders (simple majority generally)
* altering the rights of preferred / unique shares can require the consent of shareholders holding those shares/rights
* common for legislation to hold that voters who disagree with alterations have right to be bought out at a valuation (appraisal remedy)
* majority cannot exercise its powers in fraud of, or to oppress, a minority that operates as a limitation on the power to alter the constitution

**Plan of arrangement**

* Where a company **wants to do something** (amalgamate, transfer assets for shares, exchange shares, etc.) but the **legislation does not have procedure**
* So **disclose to shareholders what you want to do, get special resolution** (more than simple majority)
* **then apply to courts -** will you permit us and supervise us?
  + Eg. public companies going private – court will look at unique facts, but if there is precedent procedure, they may follow it even though it hasn’t made it into the act yet
  + Allows corporation to do multi-step transaction all in ‘one go’

**Pre-incorporation contracts**

* The law does not recognize the existence of a corporation before the certificate of incorporation has been issued, or other conditions are met
  + Laypeople often **negotiate contracts before incorporation** which presents issues of **personal liability**

S 20 – BCA (modified common law)

**Definitions:**

* Facilitator (or promoter) – purports to enter into contract on behalf of company not yet incorporated
* New company – does not exist yet
* Other parties – makes contract with promoter

**Provisions:**

(3) if after pre-incorporation contract, company is incorporated, company may, **within reasonable time**, **adopt the pre-incorporation contract by any act or conduct signifying its intention to be bound by it**

(4) on adoption,

(a) the **new company is bound** **as if it was incorporated at time contract was made**

(b) **facilitator** **ceases to be liable** in respect to the contract

(2) if a facilitator purports to enter into pre-incorporation contract, **they are deemed to warrant** to other parties **that the company will**

(warrant – representation to induce entering into contract; if breached, facilitator is liable for damages)

(i) **come into existence within a reasonable time**

(ii) **adopt the contract within a reasonable time** after the company comes into existence

(5) if new **company does not adopt pre-incorporation contract within reasonable time** after incorporation, facilitator or any party **can apply to court to restore any benefit received by the new company** (company must have received benefit)

(8) facilitator is not liable under (2) if the parties to pre-incorporation contract have, in writing, expressly agreed

(can contract out of the statute)

**Previous Common Law (Baron not overly concerned with these cases)**

**Kelner v Baxter [1866]**

**Facts:** P was a wine merchant (had his own company); In Aug 1865, proposed that a hotel company be formed in the town; P and others were to be directors, and P was to be manager

* The company was to buy land from P for 5K, 3K cash and 2K in shares – this agreement was completed, with Baxter being the nominal purchaser on behalf of company
* In 1866, a memorandum of association was executed by P and Ds and others
* Pending the completion of sale, P carried on his wine business and purchased additional wine for sale
* P then sold the wine to the proposed company for 900, which was later ratified by formed company
* Company then collapsed and P brought action for unpaid 900

**A:** If the company had existed, D’s would have signed the agreements as agents of the hotel

* **However, as no company existed, the agreement would be inoperative unless it was personally binding on Ds** – they profess to be agents but there was no principal at the time of the contract
  + **A stranger by subsequent ratification cannot change this**
* When a company comes into existence, it creates rights and obligations, **but nothing retroactive**
* **Contract was not worded to include a contingency on the formation of the company**
* In the case at hand, ‘on behalf of the hotel’ is no different than someone buying corn ‘on behalf of my horses’

**C:** defendants are **personally liable**

**Black v Smallwood [1966]**

**F:** Blacks purported to enter into a contract to sell land to Western, but the company was not incorporated at time

* However, **both parties believed it was at the time**, and that Smallwood was director of the company

**A:** Rule from *Kelner* would say that the agent would be personally liable when the principal does not exist

* But, that was in a circumstance where based on the contract, and the **imputed intentions of the parties**, **knowing there was no company in existence**, that the defendants should be bound personally
  + Here defendants thought the company existed, so they cannot have intended to incur personal liability
* The reason for creating the company may have been to avoid personal liability
* In *Kelner*, the defendants were not substituted as principals, **they were principals**
* **It would be wrong to enforce contract when there was no intention here to be personally bound, based on construction in light of what the parties took to be the facts**

**C:** Contract is a nullity, as the proposed purchaser did not exist when it was made

**Wickberg v Shatsky & Shatsky [1969]**

**F:** In 1965, S purchased an interest and became directors of Rapid Addressing Systems Ltd, which was carrying on business in Vancouver selling/servicing business machines and supplies

* S decided to carry on business under the name Rapid Date (Western) Ltd **even though no company was ever incorporated under that name**
* S hired W to be manager of the corporation, and executed a contract under the fake letterhead, signed by S as president to hire W for 15K/year “to be reviewed 6 months from this date”
* S then told W that they should drop ‘ltd’ from name and continue as Rapid Data (Western)
* Business was unsuccessful and in 1966, W, after refusing to work on straight commission, was given notice of termination
* W now brings claim that **S is liable as a party to contract as it was signed by him for non-existent principal**

**A:** Rule from *Kelner* does not apply because it **is clear that the defendant did not intend to be personally bound**, as was found in *Smallwood*

* However, **as S knew the company was not incorporated, they may be liable for breach of warranty or fraud**
  + **S represented that it was a company, but there is no causal connection between its non-existence and the plaintiff’s loss**
* W should have also known that as it dropped ‘Ltd’ it was a firm rather than a corporation
* Loss resulted from failed business, not from breach of warranty

**C:** P is only entitled to nominal damages for breach of warranty

**Chapter 4: Management and Control of the Corporation**

**Management, Control and Ownership**

* Corporations, since inception, have become dramatically more publicly owned, with dispersed shareholder ownership (no controlling shareholder)
  + This caused the ‘owners’ / shareholders of corporations to be more passive principals
  + Separation of ownership and control
* **Agency conflicts** – arise naturally from delegation of authority – shareholders delegate power to directors and officers who also have personal interests as well as duties to the corporation

**Contractarian model of the corporation** – corporation is simply a nexus for different contracts between different parties; and if that is the case, managers and shareholders will agree on contracts that maximize value and minimize agency costs

* Markets work to align the interests of managers and shareholders
* **This suggests that corporate law is not really needed and it can be dealt with under contract law** – however, corporate law outlines rules that allow these markets to operate – they outline voting rules, how investors realize returns, incorporating saves transaction costs, etc.
  + **corporate law helps facilitate** (standard form contract and legal personality), but that people should be able to choose what they agree to and contract out of a particular term if they want – **should avoid mandatory corporate rules**
* **Critiques** – markets cannot effectively control agency costs – examples like Enron – regulators need to step in to fill the corporate governance void
  + 2008 crisis was brought about partly by failure of managers to manage risks and compensation

**Relevant BCA sections**

1(3) – **director –**  an individual is appointed as a director of a company if

Appointed as a director in accordance with this act, or the memorandum/articles of the company

(c) **declared by the court to be a director of the company** (court has power is person is avoiding being a director to avoid liability)

2 (3) – **control –** a person has control of a corporation if shares of the corporation are held by the person, or a corporation controlled by the person, and the votes carried are sufficient to elect or appoint a majority of the directors of the corporation

128 (3) – **removal of director –** a company may remove a director before expiration of their term (a) by a special resolution or (b) if memo or articles say differently, that threshold can be lowered

(lawyer can override government here - Baron)

CBCA 6(4) – *cannot change threshold* for removing directors

135(1)(a) – **no directors in office –** an individual (anybody) may be empowered by the shareholders to call a meeting of the shareholders for the election of directors; and appoint directors by simple majority

appointment under (1)(b) may be effected by a unanimous resolution

**136(1) – directors of a company must manage or supervise the management of the business and affairs of the company (subject to exceptions)**

**Bushell v Faith [1970]**

**F:** Conflict between external rules and internal rules – family business in England with 3 shareholders (siblings with 100 shares each)

* One brother is a director, and the other two siblings are trying to remove that director from office
* However, the internal articles stipulate that in that situation, the shares of the director who is to be ousted give 3 votes per share in the resolution (this inevitably results in a 300 to 200 vote, so the brother stays in office)
* Sister argues that the article that allows this is frustrating the whole object and purpose of the Act, so that a director can become irremovable
* S 184 says that notwithstanding anything in its articles, ordinary resolution can remove a director

**A:** an ordinary resolution means a bare majority of votes, but this depends on the voting rights that are attached to different classes of shares

* **Parliament has never sought to fetter the right of a company to issue a share with different rights or restrictions in different circumstances**
  + Provision does not say that in this ordinary resolution, all special voting rights are removed

**C: finding for the brother** (baron disagrees with decision; dissenting opinion says so too)

* Baron – how can a solicitor prevent *Bushell* situation? – state in articles that attached to one class of shares, each shareholder is entitled to elect one director

**Some sections of BCA/CBCA cannot be modified by articles or shareholder agreement**

**Polls:** In a meeting, voting is usually done by show of hands – but after the result of vote, if someone disagrees, **they can demand a poll** with written ballot and one vote per share

* Doesn’t change threshold required, but can change outcome

**Sale of the undertaking** (sell off everything the company owns)

* s 301 contains procedure – generally requires special resolution
  + protection for *bona fide* purchaser in good faith
* But what if the majority controlling shareholder wants to vote one way, but directors disagree (clash between owners and management)

**Automatic Self-Cleansing Filter Syndicate v Cuninghame [1906]**

**F:** Articles of association stipulated that the management of the business is vested in the directors, unless there is 75% shareholder votes (extraordinary resolution)

* one major shareholder wants to sell company’s assets, and the resolution passed by simple majority
* management disagreed and refused to sell the assets because they felt it was not in the best interests of the company

**A:** Majority shareholder cannot impose that obligation on the director (s 136)

* **The directors are not agents of the shareholders, they are agents of the corporation**, so they do not have to be bound by the resolution
* The only thing that can change this is **an extraordinary resolution affecting the powers of the directors**, and not a simple majority approving the sale

**Unanimous Shareholder Agreements** (only federal) – alters relation between directors and shareholders – purpose to restrict, either completely or partially, the director’s powers

* **Historically, directors cannot fetter their discretion** (contract into how they will act in future), but shareholders are allowed to; In 1970, this changed with USAs
* **USA makes shareholders liable as directors** (not very common), but can be **demanded by owners if they want more control**
* CBCA 146 – **directors have a duty to comply with them**; therefore, breaching USA is like breaching the articles
* Examples of things you can do in a USA – change voting thresholds, make directors disclose more information at AGM, limit authority to issue shares, borrow money, appoint officers, set remuneration (traditionally decisions that directors would make)
* Note BCA 137 – powers of directors may be transferred (but BC **does not** have USAs)
  + this takes place in the articles – not a contract; may be added to articles after special resolution
  + transfer recipient can be **any person**, not just shareholders – the transferee takes on rights, powers, duties and liabilities of the Directors, to the extent of the transfer (and director is relieved similarly)

**Bury v Bell [1984]**

**F:** Bury was employee and shareholder at Bell, company had USA that said that if he left employment at Bell, he would have to sell shares at price determined by Bell, bought within 6 months, but could be extended to 12 months

* No one was contesting validity of the agreement
* Bury left employment at Bell, and got job at new brokerage where shares were part of compensation package
* But legislation held that you could only have shares at one brokerage house at one time – prohibiting him from taking new shares, so is trying to compel Bell to purchase the shares

**A:** **this is an unjustified delay, an act of penalizing Bury for leaving** – the deprivation gives a *prima facie* case of oppression/unfairness, **so the onus is on Bell to justify the deprivation** (no justification advanced)

* So, court forced them to buy back the shares at the six month mark (court empowered to disregard articles)
* CBCA 241(2)(c) and (3) noted – **powers of the court – 241(3)(c)** brought up in *Bury* as court can regulate a corporations affairs by amending the articles / USA / etc.

**Ultra Vires Doctrine** – old rule that says corporation **can only act if it is specifically authorized to in articles** if the company was made by memorandum (did not apply to letters patent companies)

* In BC, enacted s 30 BCA – **“rights,** **powers, and privileges of an individual of full capacity”**
  + BCA s 33 – **restrictions** – company must not carry on any business or exercise any power that **is restricted by its articles**
* BCA 154 – **directors’ liability** – directors who vote/consent to resolution that authorizes a company to do any of the following are jointly/severally liable to restore the company to its position
  + **(a) do any act contrary to section 33 (against the articles)** that results in company paying person
  + (c) to pay a divided contrary to section 70
* BCA 259 – **procedure to alter articles** (if want to change restriction)
  + BCA 260 allows for shareholder dissent, and sell-off of shares

**Protecting 3rd party reliance** – Indoor Management Rule

* BCA 146 – persons may rely on authority of companies and their directors, officers and agents
  + Unless they ought to have known by virtue of their relationship to the company (different than CBCA)
* CBCA s 17 – no constructive notice (a person should have known, as RP, of an event or fact, whether they actually had notice or not)
  + s 18 – **information in notice of articles can be taken at face value**

**Shelf company** – in the past, documents submitted to registrar would take several weeks to be approved, so lawyer would become director of a ‘shelf company’ and then give the company to a client who wants it immediately

* Basically a pre-packaged corporation ready to go, transfer shares, title of director to client
* Company is supposed to have never done anything before (should be fresh for client)

**Sherwood Design Services v Ontario [1998]**

**F:** Pre-incorporation contract made by a group of people to buy Sherwood, so lawyer sold shelf company to client which was supposed to secure contract

* lawyer sent a letter to Sherwood’s lawyer stating the numbered company was incorporated and the asset purchase will be completed; attached unsigned copies of a certified copy of the director’s resolution adopting purchase agreement and other documents – but transaction never went through as buyers never showed up
* The lawyer later transferred the shell company to another party for a different real estate transaction
* Sherwood then sued the numbered company alleging the numbered company’s assets were liable for the earlier transaction (they had lost money as they were forced to sell for a lower amount to another purchaser)

**I:** is numbered company liable for the breach?

**C:** Majority: yes; dissent: no

**Majority**: upheld protecting third party reliance – people involved in a corporation cannot rely on something that the other party did not know (third party does not have to do as much due diligence – can assume it is set up properly and people named as directors have authority to act, take articles at face value)

* Lawyer had full authority of the law firm – he held authority to speak on behalf of the corporation and the clients
* The company therefore cannot dispute the authority of the solicitor in his letter that made such representations

**Dissent:** unsigned draft resolution was sufficient to give notice that the corporation had not adopted to contract – the documents made it clear that the corporation had not been formed, and not had the opportunity to turn its mind to the pre-incorporation contract

**Corporate Goals and CSR**

**contractarian view** – corporation can do whatever its directors decide it should do, but once decision is made, no singly person should have power to change (usually focuses on a profit-seeking motive as most investors want that)

* Eg: if a shareholder invests in a for-profit corporation in order to receive a share of profits, if that corp donates those profits to charity instead, we have an agency problem (but if it was a C3 – it would make sense)

**second view:** businesses are connected to the rest of the world – rejects contractarian model, profit maximization is too narrow, must also consider employees, consumers, communities (other stakeholders)

**Dodge v Ford [1919]**

*Background:* big merger movement in this period, much discussion about government intervention

* extremely profitable company – so dividends were contentious

**F:** Henry Ford had control over directors of company, decided goal was to produce more cars at lower price, wanted to reinvest in facilities/improvements, increasing employment, instead of dividends

* Short term will be less profitable but arguably will be better long term
  + Immediate effect will diminish value of shares, reduce dividends
* One shareholder (Dodge brothers) rejected this, brought claim to court – said this is like giving to charity rather than maximizing profits (reinvesting in workers, company)
* Baron adds facts: Ford’s motive was actually that he did not want to pay dividends to Dodge brothers as it would allow them to compete with rival car company (they owned 10%)
  + Shareholders have no duty to the corporation, they just want the most money as possible, starting competing businesses (different if a director did this)

**I:** are the directors (director) working in the best interests of the corporation?

**A:** goal is to maximize value for shareholders – **the directors have discretion over how to achieve that goal, but they cannot change the goal and devote profits for other goals**

* **Directors do not have discretion to conduct affairs for the mere incidental benefit of shareholders, and for the primary purpose of benefiting others**
* But, it is tough to tell if the expansion is or is not in the best interests of the corporation - we are not business experts, we are not satisfied that the alleged motives of the directors menace the interests of the shareholders
* Still the dividend should have been paid – the shareholders have a just grievance

**C:** Ford, as director, does not have discretion to change profit seeking goal to lower consumer prices and raise employee salaries

**Parke v Daily News [1962]**

**F:** 2 subsidiary newspapers make up a large part of Daily News’ business, employing ~3000 people

* the newspapers were not profitable, so they wanted to sell the companies and focus on other things
* before the sale completed, directors decided that money left over from sale will be used towards benefit of staff/pensioners – vacation pay, severance, etc. (for employees in this massive sale as jobs are affected)
* directors let shareholders know that the vote is coming up – shareholders did not like this plan at all so they applied to courts, spearheaded by majority shareholder Parke (seeking resolution that the vote is ultra vires)

**I:** are the directors acting in best interest of the corporation?

**A:** Court looks at 2 cases

* 1st: on winding up, directors wanted to pay money to people who lost their jobs but had no legal claim to compensation – court said the company was no longer a going concern and sole purpose was winding up
* 2nd: company granted a pension to a widow of a former managing director
  + When granting money such as this, which involves expenditure of company funds, it can only be spent for purposes reasonably incidental to the carrying on of the company’s business; must ask 3 questions:
    - is the transaction **reasonably incidental** to the carrying on of the company’s business;
    - is it a ***bona fide*** transaction;
    - is it done **for the benefit and to promote the prosperity of the company**?
* Conclusions from cases – companies funds cannot be applied to do charitable things; court will inquire into the motives / objectives of the use of funds; **court will uphold the validity of gratuitous payments if the test is satisfied; onus of upholding validity of payments lies on people asserting it (directors)**
* Directors argued they must take into account employees interests – rejected by court, they say you must only look at profits, what is best for the corporation as a whole
* Court says it was noble what they were trying to do, but there was no legal basis for the application of funds

**Re Peoples Department Stores [1992]**

**F:** Marks and Spencer Department Store was department store, but also owned other businesses including Peoples

* Spencer sells Peoples to Wise Stores in a leveraged buyout – instead of paying cash, borrow money from seller
* Wise is the purchaser, integrating the companies did not go well though, recording inventory was a mess
* One of the directors (Wise brothers) consults with everyone, says they are going to do a joint inventory procurement, Peoples will buy from US suppliers, Wise will buy from overseas, and then transfer inventory to each other, and record it on financial statements as the companies owing money to each other
  + Within a year, both companies are bankrupt
  + Trustee says Wise brothers favoured their own old store over the Peoples to the detriment of People’s creditors in breach of duties of directors under s 122 (142 BCA)
  + TJ found they owe FD to creditors in the vicinity of insolvency, and it was breached

**A:** Although shareholders are commonly said to own a corporation, in absence of USA, it is directors appointed by shareholders that supervise the management of the corporation

* + Considerable power vested in directors under s 136, and vested in officers by delegation from directors
  + They have fiduciary duty, must respect trust and confidence vested in them, must avoid conflicts of interests, avoid using the position for personal benefit, maintain confidentiality of information they see in their position, etc.
* **Best interests of corporation is not simply best interests of shareholders – just means maximization of the value of the corporation**
* But courts have recognized that other factors are relevant in managing a corporation
* When in vicinity of insolvency, shareholders may prefer directors to pursue high-risk alternatives with high potential payoff to maximize prospective claim; creditors may prefer in the same circumstances that directors steer a safer course as to maximize value of their claim against assets of corporation (2 different pressures from different groups)
  + **Duties of directors do not change when they are in this zone (insolvency)**
  + **Directors owe a duty of care to creditors, but not a fiduciary duty**
  + **Any honest, good faith attempt to turn the business around, if unsuccessful, will not qualify as breach of fiduciary duty**

**Re BCE [2008]**

**F:** Corporation made plan of arrangement to sell off shares of company in leveraged buyout

* Three offers contemplated a substantial amount of debt which would be held by subsidiary company Bell CAN
* Plan was approved by basically everyone except for some banks that said no, they had debentures and were worried about value of them (when complete, the short term trading value of their bonds will decline by 20%)
* Seek relief under oppression remedy, and they say it is not fair and reasonable
* TJ says its fair, CoA disagrees

**SCC:** an essential component of corporation is capital stock, which is divided into fractional parts: shares

* **Shares do not confer right to underlying assets while it is running**
  + **A share is not an isolated piece of property, it is a bundle of interrelated rights and liabilities**
    - Rights to assets on insolvency, right to oversee management of company
* Directors are subject to two duties: fiduciary and duty of care of reasonably prudent person (this case is only FD)
* **If interests between shareholders and stakeholders conflict, the directors duty is to the corporation** (*Peoples*)
* Fiduciary duty is not confined to short-term profit or share value, must look to long term interests of corporations
  + Although directors must consider best interests of corporation, may also be appropriate (but not mandatory) to consider impact of corporate decisions on all stakeholders (shareholders, employees, creditors, consumers, governments and the environment to inform their decisions)
* Courts should give deference to the judgements of directors who take into account these ancillary interests (BJR)
* Directors are not making any decisions that are not in the best interests of corp, **even if** the decisions reduce the value of some debentures

**Chapter 5: Duty of Care owed by Managers & Directors**

**Common law around duties of directors was historically relaxed:**

**Re City Equitable Fire Insurance [1925]**

**F:** Order made to wind-up/liquidate insurance company that was once very profitable

* Investigation showed deficit of 1.2M pounds at the time there were large trading profits
* The losses resulted from failed investments and diversion of funds by managing director into another company
* Managing director was jailed for fraud – liquidator brought action against directors and auditors alleging negligence and breach of duty

**A:** Directors are trustees, but merely in the sense of a fiduciary relationship to the company – little resemblance to a trustee of a will or marriage settlement

* **The duty is impossible to describe in general terms** – it changes based on the size of the company, the nature of the company, and the matters left to the officers and directors
* If a director acts **honestly**, he **cannot be liable unless guilty of gross or culpable negligence** in a business sense
* He **does not need to take all possible care**, he is only bound to take “reasonable care” measured by the care an ordinary man might be expected to take in the circumstances
  + If a director exercises reasonable care, having regard to knowledge and experience, and acted honestly, they have discharged both their equitable and legal duties to the company
  + Directors are not liable for mere errors in judgement
  + Not bound to give continuous attention to the affairs of his company
    - The duty is intermittent – to be performed at periodical board meetings and committees that he is reasonably able to attend
* **Exclusion clause** - Article 150 holds that directors are not to be answerable for any loss that may happen in the execution of their respective offices unless it occurs through “wilful neglect or default”
  + Directors and auditors are guilty of negligence but are protected by this article

**R:** Standard was quite low at common law – as long as there was no wilful neglect or deceit and you were honest, you were pretty much okay

Directors were not required to give full time attention – just intermittent attention at meetings

Common law failed to establish professional standard for a director

**Legislature responded:**

BCA 142(1) (CBCA 122) **director**, **when exercising powers**/functions of director (not as a shareholder eg. AGM) **must**

(a) **act honestly and in good faith** with a view to the **best interests** (duty of loyalty/fiduciary) of the company

(b) **exercise the care**, diligence and skill **that a reasonably prudent individual** would exercise in **comparable circumstances** (duty of care / standard of care)

(c) act in accordance with this act and regulations

(d) subject to a-c, act in accordance with memorandum (NoA) and articles of the company

**Liability of Directors**

BCA 154(1) – directors are **liable if money is paid and not recovered as a result of a resolution when**:

(a) company does something contrary to s 33 (articles of the company), or

(c) votes to pay a dividend contrary to s 70(2)

(5) – director who is present at a meeting of directors is **deemed to have consented to the resolution** in (1) unless the dissent is recorded in minutes, is put in writing and it provided to the secretary, or sent promptly to mailing address to company after the meeting (8 – if not at meeting, deemed to consent unless dissent within 7 days)

* email is not good enough – must be in writing physically

(6) a director who votes in favour is not entitled to dissent in section (5)

157(1) – **limitations on liability – not liable If the director relied in good faith on:**

1. **financial statements** represented by **officer**, or a **written report of auditor**;
2. a **written report** by a **professional that lends credibility** (lawyer, accountant, engineer, etc.);
3. statement of **fact represented to the director** by an **officer**;
4. **any record that the court considers provides reasonable grounds for the actions of the director**, whether the record was forged/etc. (judges have much discretion here)

158 – **liability if the company’s name is not displayed**

(1) **director who knowingly permits** the company to contravene s 27 (naming rules) is **personally liable to indemnify the following persons** who suffer damages by being misled: **(a) purchaser, (b) supplier, (c) person holding a security of the company**

**Peoples Department Stores [1992]**

**F:** 3 brothers are owners of Wise; Marks and Spencer sold chain to Wise Stores

* contract forbade Wise from merging with Peoples until purchase price paid; so used strange inventory maneuver
* Had to run Peoples as a subsidiary corporation (so that if it was given back to seller, had to keep it separate)
* **David Clement, VP admin and finance** suggested weird inventory maneuver to directors
* Trustee alleges Wise brothers breached fiduciary duty and duty of care

**A: The standard of care is objective** – factual aspects of the **circumstances surrounding** the decisions of the director are relevant here

* Subjective motivations of the director or officer are only relevant to the statutory fiduciary duty (duty of loyalty)
* **The brothers accepted the suggestion without studying the indirect impact it could have** – Clement was **not qualified** to have Wise brothers **rely on his representation as a bar to a suit under the duty of care** (Does not absolve directors of duty of care)
  + The named professional groups that absolve are named in provision as lawyers, accountants, engineers, etc. – **Clement was only a BComm with 15 years experience**
  + Although he may be better equipped to find a solution than the wise brothers, this is not enough

**C: Wise brothers cannot invoke the defence under s 123(4)(b) of CBCA**

**R v Bata Industries [1992]**

**F:** In the yard of Bata’s shoe factory, there was large chemical waste storage site that stored known carcinogens in rusting and uncovered containers – court found that the containers had been a matter of concern for years

**A:** Directors are **responsible for reviewing** the environmental compliance reports provided by officers of the corporation, but are **justified in placing reasonable reliance on reports provided to them** by informed parties

* **Directors should substantiate that the officers are promptly addressing environmental concerns brought to their attention by gov agencies or other concerned parties** (s 136-1 of BCA)
  + Directors should be aware of the standards of their industry and other industries which deal with similar environmental risks
* **Directors should immediately and personally react when they have notice the system has failed**
* Of the 3 directors in question, one was exculpated because he **had little operational impact on activities**, and acted appropriately in response to being alerted of violations (likely semi-retired)
* **The other two were guilty:**
  + **one had knowledge 6 months before any action was taken** (not a timely OR appropriate manner)
  + The other was **on-site manager and failed to discharge duty to ‘walk-about’ on a regular basis** to ensure no violations occurred

**Business Judgement Rule**

* Courts reluctant to look retrospectively based on **results/outcome** to determine what the directors should have done (“hindsight is 20/20”)
* **directors are not expected to be judges** – when there is no evidence of fraud, illegality, or conflict of interest in relation to business judgement, directors are presumed to have acted in good faith and due care (fuses FD/DoC)

**UPM-Kymmene Corp [2002]**

**F:** Forestry company that was bogged down by debt

* Company hired chairman that wasn’t needed but whose compensation package put the company on verge of bankruptcy – claimed breach of fiduciary duties by directors

**A:** Only get benefit of business judgement rule if you have used your best judgement – not in this case, they basically just made a silly decision without any thought

* The court looks to see that the directors made a reasonable decision, not a perfect decision
  + However, only protected to the extent that their actions **actually evidence their business judgement**
* **Courts are entitled to consider the directors decision, what they relied on, what facts were available to the directors at the time that they made their decision**
  + In the space of 30 minutes, made decision to recruit someone they did not know, with a massive compensation package with bonuses and other rights that will bankrupt them
    - Stock options amounting to 13.4% of the company
    - Change of control protection, lengthy employment term

**C: Decision was not an informed decision, nor a reasoned one – therefore, the business judgement rule cannot be applied in the circumstances to protect them from judicial intervention**

**Indemnification and insurance**

* Directors are often held liable for decisions that are not made personally – made often by officers/others
  + *Policy:* is the goal of lawmakers to punish, or deter?
* **A corporation may indemnify a director for**: any expense reasonably incurred in defending/settling/satisfying a judgement for any action against director
  + BUT, director **must have fulfilled their fiduciary duty**
* **A modern corporation may also purchase insurance for the benefit of a director (or the corporation)**; but director must still uphold fiduciary duty
  + Can insure for **wider amount of situations** that indemnification though (some are insurable but not indemnifiable – beyond scope of course though)
* **Potential agency problem** – costly insurance expense may reduce amount of money available to pay dividends – valid and justifiable business expense that the shareholders do not like

**Re BCE [2008]**

“**The fiduciary duty of the directors to the corporation is a broad contextual concept**; it is **not confined to short-term profit or share value.** Where the corporation is a going concern, it looks to the **long-term interests of the corporation.** The **content of this duty varies with the situation at hand**. At a **minimum, it requires directors to ensure that the corporation meets its statutory obligations**. But, depending on context, **may also be other requirements**. The fiduciary duty is **mandatory** – directors must look to what is in the best interests of the corp”

* Directors did what they thought was reasonable, their duty is to the corporation, no breach of fiduciary duty

**RECAP: Duty of Care**

* A Director must exercise the care, diligence and skill that a reasonably prudent individual would exercise in comparable circumstances
* Directors are making decisions for the future, and judges do not expect Directors to be able to see, with certainty, the future results of those decisions (BJR)
* Directors must make reasonable decisions, but do not need to make perfect decisions
* Directors must do what a reasonably prudent person would do in similar circumstances

**Examples of breach of duty of care:**

* Relying on a report written by a person whose profession is not found in s 157(1) or equivalent (*People’s*)
* Quickly reading then barely discussing an important contract, then voting on it right away (*UPM*)
* Director had knowledge of environmental violations for 6 mos before acting, then didn’t act appropriately (*Bata*)
* A factory manager who fails to walk around the site, and fails to fix broken carcinogen storage containers (*Bata*)
* **Examples of NOT breaching duty of care:**
* Creating a business plan in hopes of saving two failing businesses (*People’s*)
* Creating competitive bidding process, then choosing one of 3 bids, where all three bids were not perfect (*BCE*)
* A director who has little operational impact, who acted appropriately and promptly when alerted to environmental violations (*Bata*)

**Chapter 6: Fiduciary Duty owed by Managers & Directors**

**When acting as a director, a director must:**

* Act honestly
* In good faith
* With a view to the best interests of the company
  + Means the director must place the company’s interests **above** his/her interests
  + Avoid conflicts of interest

*3 different relevant fact patterns*

1. **Self-dealing:** a director selling an asset to the company at too high a price (or buys something too low)
2. **Corporate Opportunities:** director learns about opportunity at a meeting, decides to pursue it individually
3. **Competition:** director has an interest in two competing businesses

**Self Dealing**

* Always involves a contract/transaction
* Could be between **director and corporation**, *or* between **some other entity he has an interest**, and corporation
* Potential for director to divert corporate wealth to himself, potential for divided loyalties (conflicts of interest)
  + As a shareholder, a director is motivated to generate wealth for the company; however, the increase in wealth from the transaction could be greater than the loss to the share value
* **Price difference between fair market value and sale/purchase price is incurred by the company** (agency cost)

**Historically,** rules against self-dealing were far stricter, now most commonwealth allow it, but heavily regulate it

* legislation for self-dealing came before fiduciary duty provisions (so there are some discrepancies)
* Provisions use the word ‘material’ in provisions, but don’t include definitions
  + For our purposes, material = ‘important and relevant’, when disclosure is required
* The main point of self dealing is that the director must ‘account’ for his profits (ie. pay back $ to corporation)

S 147 – (1) **a director has a disclosable interest** in a contract/transaction if:

(a) the contract/transaction is **material** to the company;

(b) company **has entered** or **proposes to enter** into the contract/transaction; **and**

(c) **either**  (i) **director has material interest** in contract/transaction, or

(ii) **director is a director/senior officer of or has a material interest in a person** (company) **that has material interest** in the contract/transaction

s 148 – director is **liable to account** to the company for **any profit that accrues as a result of contract/transaction** if director holds a **disclosable interest**

s 149 – contract/transaction where disclosure has been made, in accordance with 148, **can be approved by directors or by special resolution** (more in legislation book)

**Corporate Opportunities**

* Completing governed by **common law**; highly fact dependent, and generally unresolved/unclear
* Baron: probably not codified because disputes are generally settled outside court – no one wants codification
* CL does not completely block the area of corporate opportunities; **there are circumstances where it is okay**

**Main issue in COs**: did the director usurp the authority granted to him by the shareholder in order to acquire an “un-bargained for” personal benefit? (this is another example of an agency problem)

**Regal (Hastings) v Gulliver [1942]**(prior to statute – does not conflate duty of good faith / fiduciary duty like Laskin)

**F:** Regal owned cinema in Hastings; company wanted to buy two more theaters as it was struggling

* Regal formed a subsidiary company, and offered to lease 2 cinemas, but the landlord required guarantee of the rent by the directors unless the paid-up capital of the subsidiary was 5,000 pounds
  + Parent company was unable to provide more than 2,000 pounds
  + So, directors of company and solicitor put up 3,000 and the company put up 2,000
* The entire business, parent and subsidiary were sold to buyers; but, the directors who owned 3K shares made a profit of ~2 pounds per share – new directors of Regal are suing for breach of fiduciary duty as they gained profit

**A:** **company must satisfy two things:** (i) that what the directors did could be said to have been done in the course of their management and in utilization of their opportunities and special knowledge as directors; and (ii) that what they did resulted in a profit to themselves

* An agent must account for net profits acquired by him in the course of his agency, it does not depend on fraud or corruption
  + Even if they did not intend to make a profit, if they did make a profit, it is enough
  + Doesn’t matter if the company does not actually lose money
* The rule is stringent and absolute because ‘the safety of mankind’ requires it to be absolutely observed in the fiduciary relationship

**C:** 4 directors bound to pay back because they are directors who made a profit in course of positions (other facts are irrelevant)

**Peso Silver Mines v Cropper [1966]**

**F:** C was director of company that took over several silver mine claims, was instrumental in incorporating *Peso*

* Company went public for financing the purchase of the claims, but later became financially strained
* Peso was offered 3 groups of claims to more land– one was turned down by 6-man BoD because of financial constraints, and because it felt that Peso had enough land currently under control
  + Later, a few directors and a geologist for Peso created a company and took on the project as Cross Bow
  + Peso is fine with this at the time
* Wrote letter to BC Brokers explaining transaction – main interest lies with Peso, but it was unable to buy, wanted to get land because other people are interested in acquiring it
* Charter Oil bought Peso, demanded that Cross Bow turn over the interest in the claim

**I:** Did Cropper breach his fiduciary duty?

**C:** Finding for Cropper – can keep interest, does not have to pay back to Peso

* even though he was a director and learned about it on the board, Peso declined the opportunity when raised
  + Baron: if C was negotiating on the side before Peso turned it down – would have been problematic

**A:** impossible to say that C obtained the interests he held in Cross Bow and Mayo **by reason of the fact that he was a director of Peso** **and in the course of the execution of that office**

* **When C was offered the claim, it was his duty to take part in the decision of the board as to whether that offer should be accepted or rejected; at that point he stood in a fiduciary relationship with Peso** 
  + he and his co-directors acted in good faith, solely in the interests of Peso and with sound business reasons in rejecting the offer
  + the offer to C was not accompanied by any confidential information unavailable to any prospective purchaser, and he did not have access to any of this information by reason of his office
* When the later proposal with respect to Dickson's claims was made to C, it was not in his capacity as a director of the appellant but as an individual member of the public

**Canadian Aero Services v O’Malley [1973]**

**F:** Main business of Canaero was topographical mapping and geographical exploration – Ds were assigned to map the country of Guyana

* Ds then resigned from Canaero and incorporated Terra, to perform identical work; their proposal was competing with the proposal from Canaero
* Canaero suing for breach of fiduciary duty

**4 issues:** (i) determination of relationship of defendants to company;

(ii) duties, if any, owed by them to the company;

(iii) whether there was a breach of this duty;

(iv) if there was a breach, consider liability

**A:** Does not matter whether the two people were properly appointed as directors of Canaero**, they, in practice, acted as president and executive VP** of Canaero for 2 years - Top management and not mere employees,

* (Court considers them to be officer even though not technically on paper)
* **So then they have fiduciary relationship with company** – betokens loyalty, good faith, avoidance of conflict of duty and self-interest – a director is precluded from obtaining for himself any property or business advantage either belonging to the company or for which it has been negotiating without approval from the company
  + Especially when the director has been participating in negotiations on behalf of the company
* None of the rigid rules in *Regal* should be applied rigidly; as in this and other new branches of the law, **new fact situations** **may require a reformulation** of existing principles
  + “particular facts may determine the shape of the principle of decision without setting fixed limits to it”
* Even though the project slightly changed, would be absurd to let them off on a technicality – they are close in enough that **the projects can be considered the same thing**
* Distinguished from *Peso* – Canaero **maintained significant interest** in the project; no good faith on behalf of D
  + Officers first negotiated parts of the deal as part of the company, then left and scooped it up
* **Non-exhaustive list of factors to consider in each case:** position held by D; nature of the CO - its ripeness specificness and the director’s relation to it, the amount of knowledge possessed, the circumstances in which it was obtained and whether it was special or private; timing with termination of relationship with other company, and the circumstances under which the relationship was terminated (retirement or firing)

**Competition**

In Law 459 the term competition refers to:

* A Director **serving on the boards of two competing corporations**
* A Director (or officer) **operating a business that competes with the corp**; or
* A Director (or officer) having a **material interest in an entity that competes with the corp**
  + Each could involve a conflict of interest
  + Competition is **competing against** the corp, whereas self-dealing is **making a deal** **with** the corp

**Historically,** judges looked at this as a conflict of interest in the sense of breach of fiduciary duty

* Then, obscure motion from 1891 made its way into case in 1932 and changed the rules
* **London v Mashonaland [1891]**– a person can be a director for both – nothing in articles that prohibits, no NCA
  + nothing prohibits him from acting as a director of this other company; no sufficient damage was shown
* **changed common law** – allowed to sit on board of two competing companies, depending on facts and behavior – **NCA or articles prohibiting competition would overrule this though**
* S 153 applies if nothing in articles, or no agreement (**director must simply disclose other interest**)
  + Director still must maintain fiduciary duty though

**Competition and corporate opportunities can have significant overlap** – stealing the opportunity is essentially competing against the other corp – *Slate* shows interplay

* distinction is fairly artificial, but we have s 153 for competition and common law for COs

**Slate Ventures v Hurley [1996]**

**F:** Hurley a director of Slate, purchased a slate quarry for himself without disclosing this to his company

**I:** Was a breach of fiduciary duty?

**Current law on fiduciaries’ liability in Canada:**

* Where there is **an actual conflict of interest** and the information/opportunity is **acquired by virtue of the fiduciary’s position**, they are **liable to account** for any profit
* Where there is a **potential conflict of interest** and **info by virtue of position**, they are **accountable** for any profit
* Where there is a **potential conflict**, but information/opportunity was **acquired independently**, fiduciary is **not accountable**
* Where there is an **actual conflict**, but information was **acquired independently**, fiduciary **is accountable**
* Where there is **no conflict**, but the information was **acquired by virtue of position**, fiduciary **is accountable**

**A:** Hurley **did not acquire the information by virtue of his position as a fiduciary**, but the quarry was important to the corporation because it would add slate reserves, provide different colours to meet consumer needs, and prevent competitors from entering market in NFLD

* therefore because they had general interest in acquiring quarries and could purchase the properties
* **actual conflict of interest even though independently acquired knowledge – Hurley accountable** – **breach of FD**

*Note:* **Slate [1997]** *–* disagrees with finding that **potential conflict** of interest would **not be enough**

**Cranewood Financial Corp v Norisawa [2001]**

**F:** Competition scenario similar to Slate case – embraces appellate level decision

**A: Potential conflict of interest is enough, doesn’t have to be actual conflict of interest**

* Breach of fiduciary duty comes down to two questions:
  + (i) Was there either an **actual or potential conflict** of interest by virtue of fiduciary creating new company to pursue an opportunity?; OR
  + (ii) Were the opportunities **acquired by virtue of their position** with the companies as director/officer of the first company?
    - If either are satisfied, **the fiduciary is liable to account**

**Scholarly theories on the fiduciary duty**

* **law and economics theory** – purpose is shareholder wealth maximization; so directors must perform the function of generating effectively and efficiently (primary purpose)
  + if the director focuses on something other than that goal, they are breaching their fiduciary duty
    - Baron: very narrow and perhaps short-cited
  + **duty to all stakeholders is not practical** – lots of conflicts of interest, a duty to all will denigrate into a duty to none
* **Shareholder point of view** – shareholders have a residual claim – if a corporation tries to maximize this claim (grow the value of shares) it will help most stakeholders (good for shareholders, creditors, etc.)
  + avoid taking risks, manage conservatively, etc.
  + **this is at odds with the entrepreneurial spirit** – taking risks, exploring new markets, innovation/failure
  + directors must balance this against conservative management
* **Shareholder primacy view**
* Shareholders choose to invest in corporations – in public corporations it is easy for them to exit
* they are **not protected by contract law like creditors and employees** (no statutes other than BCA/CBCA)
* **shareholder primacy view** – fiduciary duty should fill this gap by protecting the shareholders
* simplistic though because duty is not actually owed to shareholders
* **Negotiating agency view –** what would the perfect FD look like? A bargain – investors and agents are able to negotiate with each other at no cost
  + shareholder delegates authority to director (exchange liability for not having to make mgmt decisions)
  + FD rules **preserve the gains** resulting from the delegation of authority and the division of labour **while limiting the ability of agents to further their own interests** at the **expense of investors** (but duty to corp)

**the traditional common law concept reflected shareholder primacy rule**,

* but SCC rejects this rule in two decisions
* corporation does not just mean the shareholders, or other stakeholders
  + they should only be focused on making the corporation a better corporation without regard to any particular group
* “Thus in a short period of time, we have moved from one end of the normative spectrum to the other. It is up to you to decide which you prefer”
* **fair treatment** – corporation and shareholders are entitled to maximize their share value, but cannot go so far to treat **other stakeholders unfairly** – what stakeholders are entitled to ‘reasonably expect’ (oppression remedy)

**To whom is FD owed?**

* *Peoples* – **owed to corporation**, **not** owed to **each and every constituency** like shareholders or creditors
* *Peoples and BCE* treat the corporation as an **abstract entity** (eg. what is best for the bus analogy)
  + A decision could be good for the corporation but not ideal for any specific group of stakeholders
* *People’s* – not mandatory to consider various constituencies, but then:
  + *BCE*: directors have a duty to *consider* the best interests of the debenture holders
* What can directors do to discharge their fiduciary duties?
  + Form committees
  + Get advice from outside experts
  + Engage in consultation
  + Use BJR to decide how much $ to spend on those reports vs benefits of those reports
* Many times, consultations are just a box to check, they file it in minute book and do what they want anyways
* BJR can be used with FD or duty of care, or both – directors can rely on it
  + **If directors follow procedure found in BCA, directors will tend to avoid liability**
* part of the reason for duty to corporation is because there are actually major divergences between different groups of shareholders and their interests

**Old Conflict and Profit Rules**

* **The Conflict Rule –** any conflict of interest was not tolerated
  + Directors could not sit on two boards
  + Eg. Blaikie is a **partner a firm that sells railway chairs to a corp, of which he is a Director**
    - As a Director he has an interest in getting the lowest price (for the buyer) but as a Partner, he has an interest in getting the highest price (for the seller)
    - This is a conflict of interest: divided loyalties
    - HL decides the transaction is voidable at the option of the corp
* **The Profit Rule –** a fiduciary cannot earn a profit from his office
  + Historically, where there is a conflict, it usually follows that the Director will make a profit from it
  + Conflict and Profit went hand in hand
  + **The conflict and profit rules were strictly enforced** (*Regal)*
* **Now** this has changed though, old rule is far to strict
  + courts apply different standards in different situations – no strict rules
  + *Canaero* - Laskin J. seems to create a different duty for corporate opportunity cases
  + SCC found that the 2 people appropriated a CO and ordered them to hand over the profit they made
  + Laskin J. took the old C&P rules and mixed them with the modern “good faith” standard (FD)
    - You could say then, that we still have these rules to some degree
* Judges will still use old common law if it fits with the legislation, that has room for interpretation – if old common law conflicts though, legislation will be the rule

**Self-dealing/Competition Shareholder Protection**

* There are exceptions to self-dealing and competition that involve disclosure to and approval by the Board, and **shareholders may view these documents in the minute book**
* An interested, diligent shareholder m**ay view minute book, see lots of self dealing and then choose to vote for a different director** (protection here, unless shareholder is very passive / does not care)

**Hostile Takeover Bids** – offer made by person or corporation (acquirer – specific entity does not matter) to shareholders to purchase all of the shares of the target corporation

* acquirer is seeking to buy enough shares that they can take control of the target
* why hostile? Done without approval of directors of the target – they will probably lose jobs by being voted out
* being human beings who want jobs (self interest) – they do what they can to block this from happening
  + sometimes will issue shares, sell to themselves or people who are friendly to them
  + under the old law, if acquirer challenged this, the court would side with them (improper purpose rule)
* Now, if a corporation **genuinely needed to raise money**, that was a *bona fide* reason and the issuance of shares could stand (if you can show that you needed to build a factory, you’re probably okay)
* other times, the bid would actually be in the best interest of the company – director has divided loyalties / CoI

**Teck Corp v Millar [1972]**

**F:** junior mining company needs help getting to the next step – need major investment or ‘ultimate deal’

* an issuance of a controlling block of shares to the major company sufficient to allow for full development of the junior’s mining properties – Afton needed this investment
  + Two different companies wanted ultimate deal with Afton – Teck and Canex
* Director of Afton (Millar) felt Canex would do a better job, and they needed operating funds
  + sold non-controlling block to Canex because they needed cash but were not ready for ultimate deal
* Teck sees this and starts buying Afton’s shares in market; M knows they are getting closer to acquiring control
* Millar proposes 70% Afton, 30% Placer (subsidiary of Canex)
* Teck is worried that Millar will make ultimate deal with someone else, calls a meeting of shareholders of Afton
  + Says do not sign this deal without consulting us – hear us out on our deal
  + Teck then bought enough shares that they control the board
* Afton’s lawyer says ignore it, no meeting yet, so just sign the deal you want to do
* Millar signs deal, and then Teck sues them for breach of fiduciary duty

**A:** Old common law says a director cannot block a hostile takeover

* **But court asks why issuing shares to block a bid is segregated from other steps directors can take if they believe it is in the best interests of the corporation** – court inquiries into the **reason for the blocking**
* General rule: directors must act in good faith – **there must be reasonable grounds (objective for their belief**; if they say the company’s interests will be substantially damaged, there must be reasonable grounds for that belief; **if not, justifies a finding of improper purpose**
* **Directors should be entitled to use their powers to protect the company, if it is in the company’s interests**
* Defendants were elected to exercise their best judgement – **they were not agents bound to accede to the directions of the majority of the shareholders, their mandate continued as long as they were in office**
* They acted in what they conceived to be the best interests of the shareholders, and signed a contract which they knew the majority shareholder did not want them to sign – **they had a right in law to do that**

*Note:* In Canada, in change of control situation, if the board wants to get protection under BJR, they should set up committee; the courts want to see that the director made a decision that was reasonable – court will not substitute its own opinion if its reasonable at the time (even if since it has gone very wrong)

**Pente Investment Management v Schneider [1998]**

**F:** Schneider corp was 108 year old family business, went public in the 1960s

* Company had different classes of shares – when it went public, family kept full control of one class
* In the 1980s, family altered the articles to allow for a coat-tail provision
  + In a takeover bid, we assume acquirer is getting voting shares – coat-tail provision says that if a takeover bid happens, the family have right to convert their class A shares into voting shares
  + This is in effect diluting the shares such that acquirer must buy more; can veto a takeover bid
* Maple Leaf wants to take over the company without negotiating with Schneider’s board – triggers coat-tail
* Board then establishes special committee of the board, independent from the family
  + Committee looks at offer in great detail, and consider other alternatives
* Family tells committee that they will consider Smithfield’s deal (better company values, decent offer 25/share)
  + Maple Leaf responds with 29/share offer
  + Smithfield’s deal would save the family tax money – offers after tax were basically equal same
* Five class A shareholders felt that the committee was taking way too long – “the actions or inaction of the Committee, together with those of the Schneider family have in effect, contaminated the value maximization process outlined by BoD in its circular and public statements”

**I:** did the directors act in the best interest of the corporation?

**A:** If there are no reasonable grounds to support an assertion by the directors that they acted in the best interests of the company, a court will be justified in finding that the directors acted for an improper purpose (*Teck*)

* How do we learn if they acted in the best interests of the company?
* One way is “to ask what was uppermost in the directors’ minds after a reasonable analysis of the situation”
  + Acting in the best interests of the corporation does not mean that the directors must choose one of the stakeholder groups and act in that group’s best interest
  + However, if the directors have unfairly disregarded the rights of a group of shareholders, then the directors will not have acted reasonably in the best interest of the corp, and the court will intervene
* **The fact that alternative transactions were rejected is irrelevant unless it can be shown that a particular alternative was definitely available and clearly more beneficial to the corp than the chosen transaction**
* The real question is whether the directors of the target successfully took steps to avoid a conflict of interest
  + Here, they created an independent committee – Should they have done that? Yes
  + Was the committee independent from the board and the family? Yes
  + Did the members of the committee act in good faith in the sense that they acted honestly? Yes
  + Were the members of the committee well-informed? Yes
* reason to appoint special committee is to make sure that no stakeholders are unfairly disregarded or prejudiced
* To ensure the best interests of the corporation are met, it is appropriate to explore alternatives to unsolicited (not asked for) takeover bids – this **does not mean the family was obligated to accept a bid**

**C:** both the board and the committee fulfilled their duties – so request by 10% of shareholders was not successful

**Sanction of breach of FD by shareholders**

* Old common law: *Foss* v. *Harbottle [1843]*
  + **if the majority votes to ratify a breach, the minority has no standing to complain** (the majority votes on basically anything, minority is out of luck)
* if the company suffers harm, the company is the only the claimant, not the minority shareholders

**North-West Transportation Company v Beatty [1887] (follows *Foss*)**

**F:** Director sold his steamship to his company, which was approved by ratification at meeting because he was also a significant shareholder of the company

* **Price was reasonable, and boat was actually used in course of business – not a frivolous purchase**
* Minority shareholder arguing that this director’s fiduciary position was so strong that he should not have under any circumstance entered into this contract

**A:** the majority of votes must prevail, unless the adoption was brought about by unfair or improper means (or fraudulent or oppressive to minority) – only unfairness here is that Beatty had so many shares to vote on this

* **The constitution of the company enabled the director to acquire his voting power, no limits in articles**
  + So articles do not change the default common law here
  + **Just because someone is a director, does not mean that they cannot vote as a shareholder**
* **Summary of 4 levels of court:**
* **Chancery** = set aside the sale; James was in a conflict between duty and interest (director, shareholder and vendor all at the same time)
* **CoA** = reverses; the resolution to purchase the steamer was a pure question of internal management, and shareholders had a perfect right, either to ratify it [or, treat the matter as an original offer to themselves, and to agree to it and complete the purchase]
* **SCC** = affirms the Chancellor; this case turns entirely on FD character of James as director: he should have been impartial and neutral (We can read into this that he should have **abstained from voting as shareholder**]
* **PC** = one one hand, they do not want to relax the rules against self-dealing, but, on the other hand, voting is voting, and just because someone is a director does not mean he can’t vote as a shareholder, if he is also a shareholder (**affirms CoA** – it is okay) *Baron:* court was too deferential to majority – now law is different

**Dickerson report suggested that the minority shareholders should be protected more**

* Current Law – BCA s 142(3) no provision in a contract, memorandum or articles relieves a director from the duty to act, or from liability (eg. breach of any duty)
* **Some breaches of duty by Directors may be ratified** by a shareholders resolution
* **Some breaches cannot be ratified** (e.g. unlawful dividends, fraud on minority shareholders)
* Procedures are spread out throughout the *BCA*
* S 157 directors are relieved of liability under s 142(1) if they relied in good faith on documents listed in s 157(1)

**Chapter 8: Shareholders’ Rights**

**Shareholder control**

* ***De jure* control** – 50% +1 shares – can secure an ordinary resolution alone (majority shareholder)
* ***De facto* control** – in public companies in Canada, only votes actually cast count towards a resolution; many shareholders do not actually vote, so a company can be a controlling shareholder with only ~20% of the votes, even though they are not a majority
* **Negative control** – can be *de jure* or *de facto –* power to block a resolution from passing – may be 34% in the case of a special resolution
* Always count how many votes are cast, do not assume 100%

**Shares and voting**

* **Share is not defined in BCA – unit of capital**
* voting rights can allow shareholders to elect directors – ensures directors do not act in their own self interest
* **voting rights are key distinction between creditors and shareholders**
* unless articles say otherwise, **1 share has 1 vote**
* at least one class must have voting rights
* **preferred (non-voting) shares** often have preferential dividend, priority on insolvency, but no voting rights
* within a class of shares – rights are the same but # of rights depend on amount of shares
* Shareholders are entitled to vote on a small number of items that may be considered management issues
  + Because they are fundamental changes, the shareholders may vote on:
    - Amalgamation
    - Sale (or lease or exchange) of all or substantially all of the undertaking (the assets of the corp)
    - Continuing into another jurisdiction
    - Changes to the corp’s Articles
* Owners of non-voting share may vote on a very small number of items (generally info from directors/mgmt)
  + Each year they are entitled to vote in favour of, or against, waiving the:
  + obligation of directors to produce financial statements (usually small closely-held companies)
  + requirement to have financial statements prepared to the form of GAAP
  + appointment of an auditor
* Also, owners of shares of any class (voting or not) may vote (within their class) for or against the creation of a new class of shares that could interfere with that class’ special rights (eg. priority to receive dividends s 61)
  + New preferential-treatment class of shares can be made for new angel investor, and allowed by existing shareholders because they know the investment is going to make the corp more valuable
* Any person can ask a company for a list of shareholders and their last known addresses (s 49 BCA)

**Jacobsen v United Canso Oil & Gas [1980]**

**F:** Company incorporated under Alberta, old federal and new federal legislation

* Issue with respect to rights of shareholders
* Company articles said that no matter how many shares are owned, maximum vote is 1000 shares
* Company had only one class of shares
* Plaintiff Jacobsen brings claim asking whether this provision contravenes any of those 3 acts

**A:** Court looks at 3 different pieces of legislation, and different rules on what applies with different classes of shares

* BCA 59(3) – **if only one class – that class all has same voting rights**
* **article violates each of the three acts** – Jacobsen will get to vote with all of his shares (1000 share max invalid)
* **whatever number of shares you have, that’s the number of rights you have** – if you put a cap on this it would be the same as putting a cap on $ of dividends you receive
  + **if clauses in articles contrary to act, particularly with respect to shareholders rights, act prevails**
  + **if company has different classes of shares, then you can add different details**

**Other rights that may be attached to shares**

Rights (and restrictions) must be included in the Articles, except for voting: if the Articles are silent on voting, we presume that voting is a right attached to all shares

1. **Pre-emptive rights** 
   * Directors must offer existing shareholders opportunity to buy more shares, in proportion to current holdings (the number that would allow them to keep the same overall % of the company)
   * eg. on a takeover bid, directors may be tempted to issue more shares to defeat the bid
   * Prevents dilution – e.g. can be found on page 581, final paragraph
2. **Dividends** (company pays $ to shareholders, at a fixed amount per share)
   * **Shares that receive dividends are called “participating”**
   * Articles must say whether Dividends are:
   * declared at the directors’ discretion, or according to a set schedule (annually/quarterly, and/or fixed rate)
   * declared on one class independently of others, or on all classes
   * paid to one class in priority over another class
   * cumulative (catch up) or non cumulative (skip over if not given one year – no double dividends next year)
3. **Priority Dissolution**
   * When the company dissolves, who gets their $ first? In what order do classes receive their $ back, if there is anything left? The Articles must say, otherwise all shares rank equally
4. **Conversion** (converting shares to a different kind e.g. non-voting to voting eg. *Pente*)
5. **Redemption / Retraction**
   * Redemption = corp. can demand to buy back shares from you
   * Retraction = shareholder can demand the corp. buy back shares from shareholder
   * Retraction may put a corp. out of business if cash is not available

**Shareholder meetings**

* It is the Directors who call (or “convene”) the meetings of shareholders
* Two types of shareholder meetings
  1. **Annual** = AGM
     + Rules are set out in s 182 *BCA*
     + Elect Directors
     + Appoint or waive the appointment of auditors
     + Present financial statements and auditor’s report (if any) to the shareholders
     + Other business
  2. **Special (s 167)**
     + Deals with business that arises between annual meetings
     + eg. Directors are contemplating a fundamental change that requires shareholder approval

**Definitions related to shareholders’ meetings:**

* **Consent resolution** – actual meeting need not take place if:
  + Ordinary resolution – special majority consented to in writing
  + Any other – unanimous resolution in writing
  + S 180 – **deemed to be a proceeding at a meeting** of those shareholders
* **Unanimous resolution** – resolution consented to **in writing by all shareholders** **entitled to vote on it**

**Eisenberg v Bank of NS [1965]**

**F:** Bank gave loan to George Rideout for secured on assets of his company Rideout Real Estate

* George was director/president and sole shareholder of the company

**I:** can a unanimous resolution happen if there is only 1 shareholder?

**C:** Court says yes you can

**A:** Documents delivered to bank by employee; supervisor was familiar with people and recognized signatures

* **Whether an actual formal, duly convened meeting took place or not does not matter – it is the signature on the page (consent resolution)**
* **it is true that no meeting was ever held to approve; all shareholders were mere nominees of George – so even if it did happen the result is a foregone conclusion; if he signed its all good**

Basic process for **one person trying to incorporate**

The Record Book would show the Company’s Constitution:

1. NOA:
   * Class A Shares, No Maximum Number of Shares, No Par Value, No Special R&R
2. Articles are silent
   * Perhaps the incorporator chose the default Table 1 Articles
3. Incorporation Agreement
   * Incorporator agrees to buy 1 share for $1.00
4. The Central Securities Register would state:
   * Certificate number
   * Date of issue (or transfer)
   * Shareholder’s Full name and address
   * # of shares
   * Allotment (or transferred from whom?)
   * Issue price per share
   * Consideration received (money or other)
5. There would also be an Incorporator's Resolution appointing himself as Director and waiving the requirement of an auditor, and a Director’s Resolution issuing the shares to himself

**Block takeover bid by making company less attractive: poison pill**

* **Flip-in:** permits existing target shareholders (not the acquirer) **to purchase additional shares at a discount**
  + This right must already be stated in the Articles
  + This is attractive to existing shareholders (if they have the means to purchase more shares) because they get to buy cheaper shares of a lucrative company (can assume lucrative because acquirer wants it)
  + This could increase the existing shareholders’ % ownership
  + **From acquirer’s point of view,** the shares become diluted, and the acquirer’s bid becomes more expensive because they have make offers on more shares and they cannot decrease their offer price (because no one would accept a lower price than they had previously been offered)
  + Many reasons for hostile takeover – patents, property, change in management, etc.
* **Are PPs good/bad?** It depends on your point of view. It is arguable whether:

1. PP are not good for shareholders, because it allows the current Directors to stay in power, and perhaps it is time that those Directors are replaced; or
2. In PP situation, the Directors are “sabotaging” corp’s value; or
3. PP are good for everyone involved: target shareholders receive more shares at a discounted price, the acquirer (if they eventually succeed) gets a corp with more capital, and shareholders who did not tender (buy shares) go along for the ride

* **What can the acquirer do?**
  + acquirer could offer a **“flip out” aka “flip over”** which permits **shareholders of the target to buy the acquirer’s shares, after the takeover, at a better rate than any one else**
  + Acquirers hope that this will be attractive to shareholders of target, so they will happily sell to acquirer
  + This is something that has to be in the Acquirer’s Articles ahead of time, and the triggering event is the successful takeover bid

**Wall v London and Northern Assets Corp [1898]**

**F:** Majority wants to make resolution to sell assets of the company

* Wall does not want this to happen, but is in a tiny minority
  + Voiced his opinion for a while at the meeting – demanded a poll but not enough people supported it
  + Wall is fighting this to the bone – Baron: almost a situation where minority is tyrannizing the majority

**A:** Procedures have been followed – majority cannot be tyrannical, should listen to the minority for a reasonable time, but are not bound to listen until everybody is tired of talking and has sat down

* **As long as majority is acting in a *bona fide* manner, there comes a time when the minority must stop, and majority rule is what goes forward**

**Shareholder meetings:**

* Normally, Directors set the agenda for shareholder meetings
  + However, a shareholder may make a proposal to add items to the agenda of a shareholder meeting
  + If criteria are met, the corp must allow the submitter to present the proposal at the shareholder meeting
  + S 188 – **requirements for proposals**
* **Shareholders may requisition a meeting for the purpose of transacting any business** that may be transacted at a general meeting (directors calling a meeting = calling, convening; shareholders = requisitioning) s 167 BCA

**Varity Corp v Jesuit Father of Upper Canada [1987]**

**F:** Varity making application to court that they should not be compelled to include items in proposal for AGM

* Proposal was for Varity to end its investments in South Africa
* *Note:* BCA s.189(5)(d,e) = different from the statute in the case; If this was today in a BC company, shareholders may have had more success (Baron)

**A:** Court does not say it is a bad proposal, the court is just saying the company does not have to print/mail it out/put it on their agenda (that Act allowed refusal if general purpose was to promote political/social/etc. causes)

**C: Varity has the power to refuse to circulate the proposal**

**Airline Industry Revitalization Co v Air Canada [1999]**

**F:** 2 American companies are trying to use a subsidiary to buyout Air Canada and merge them with another airline

* To this end, they want to change articles of the company, so they submit requisition for a shareholder meeting
* But, the day before, Air Canada declared that they already have a meeting on record for January – so they claim they are not required to respond to the requisition for a meeting in November

**I:** is Air Canada required to hold a special meeting? Should the court compel them to?

**A:** The meeting on record does not fit in to the criteria for an exemption

* The record date needs there to be **a reasonable chance of the matter being heard there**
  + The requisition was done properly according to the act
  + This is not a situation of a date already chosen to hear the matter – the ‘record date’ was completely unrelated and should not fit into the exemption
  + Record date = meeting already fixed prior to receipt of requisition but at which the requisitioners’ business **may nonetheless be considered**
* DIY – instead of going to court here:
  + Government, by enacting legislation, has given you a procedure
  + Directors should have called a meeting – so instead of going to court, shareholders should have done ‘step 2’ when directors did not act appropriately (**requisitioners call a meeting themselves**) s 167(8)
  + “where there is a corporate remedy still open to a shareholder under the legislative scheme […] the court should be reluctant to step into the fray and impose its own solution

**The Audit Committee**

* s 223 – this Division does not apply to a company unless it is a public company (or a financial institution)
* For private companies, the shareholders may waive the requirement of an auditor
  + But for publics/banks, must have auditor
* Remember how the Directors wisely decided to create a special independent committee in *Pente*?
  + Here, the Audit Committee is an example of how Directors of a public company must set up a committee
  + The purpose is to review the company’s financial statements before the Directors sign them and present them to the shareholders (at the AGM)

**Chapter 9: Closely Held (Private) Organizations**

In a private company, the **shareholders, directors, officers and employees are often all the same people**

* From their point of view, **distinctions** amongst these roles are **blurred**, and for most of the year, **don’t matter**
* In a public company, a **change in ownership** does not directly affect the **day to day operations** of the business
  + In a private company, a change in ownership **can fundamentally change the operations of the business**
* If a controlling shareholder sold his or her shares to someone new, it is as if they are retiring
  + Does the new shareholder have the business skills, honesty, energy and interest the ‘exiter’ had?
  + A new shareholder could bring a surplus of cash, to be used to grow the business, or, lead to disaster if they control the board but do not fit with the company’s mission statement / business plan
* Small businesses start up because the founders work well together and have complementary skills and talents
* Consider whether the new shareholder is just investing money, or wants to actively participate in the business

For a start-up business, **the founders need to agree on:**

(1) Control

(2) Sharing of profits

* **A solicitor’s goal is to pro-actively prepare appropriate** 1) articles, and 2) a shareholders agreement, so that any transition from shareholder to shareholder can be managed effectively

**Restrictions on transfer**

When we discuss the “rights and restrictions attached to a class of shares”, RoT are an example of a restriction

We place RoT in the Articles at the beginning (when incorporating) in order to:

(1) prevent the **intrusion of undesirable business associates**,

(2) preserve the **relative interests amongst the owners** (fractions),

(3) resolve **deadlock** (tie-breaker)

* Alternatively, or in combination, we can create a shareholders agreement that governs the rights and restrictions for shareholders

**Sample provision:** Consent required for Transfer of Shares

No share may be sold, transferred or otherwise disposed of without the consent of the Directors and the Directors are not required to give any reason for refusing to consent to any such sale, transfer or other disposition

**Types of restrictions on transfer:**

1. **Absolute restrictions** = not valid if lasting **indefinitely**
   * Could be valid for a set period of time (if reasonable and necessary in the circumstances ~5 year max)
   * Found in shareholders agreements
2. **Consent restrictions**
   * No transfer is valid unless **approved** by directors, or shareholders, or proportion of both
   * Used **almost universally** in private companies; appears in default Table 1 Articles (in BCA regulations)
   * Refusal is generally assumed to be *bona fide* +in interests of corp, but have been rejected by courts
   * Binding on executors, trustees in bankruptcy (if someone wants to give shares in a will – overridden)
3. **First Option restrictions** (Baron: equitable and practical)
   * If a shareholder wants to sell his share, he must first offer them to the other shareholders
   * Price and procedure set by shareholders agreement (valuation formula, method they need to take)
   * May be triggered by a specific event (eg. retirement)
4. **Buy-out Arrangements**
   * Similar to First Option restrictions, but mandatory (must buy-out shares when someone leaves)
5. **Buy-sell Arrangement**
   * Upon the death of a shareholder, that deceased shareholder’s estate will sell those shares to the remaining shareholders at a specified price (generally when shareholders are also heavily involved)
   * Company will already have purchased life insurance polices on each of the shareholders, so that the company will have the funds available to pay the deceased’s estate for the shares

Note: classifications/titles are less important than the actual wording of the restrictions in the Articles or in a SA

**Re Smith & Fawcett Ltd [1942]**

**F:** articles of S&F provided that directors can refuse to register any transfer of shares in ‘absolute and uncontrolled discretion’; son, as executor for his dead father, claimed to have 4,001 shares; directors refused to register his shares unless he would sell 2,000 to a director at a certain price, and only then would they register remainder to him

**A:** there is nothing in principle or in authority to make it impossible to draft such a wide and comprehensive power to directors to refuse to transfer

* **The question is simply whether, on the true construction of the particular article, the director are limited by anything except their *bona fide* view as to the interests of the company**
  + - The article is drafted in the widest possible terms, and I decline to write into that clear language any limitation other than one that is implicit in law’, that they must maintain their fiduciary duty
    - if there is no *mala fide* behaviour and are following rules of articles – no breach of fiduciary duty

**C:** the refusal of transfer could stand

**Case v Edmonton Country Club [1974]**

**F:** Articles of public company were altered to give directors of club unfettered power to restrict transfer on shares

* another alteration required shareholders of the club to pay annual club fees whether they were playing or not

**SCC:** **mandatory fees** for shareholders **offends the basic principle of limited liability** and is *ultra vires*

Dickson **(majority):** Directors are allowed to refuse a transfer if that power comes from clearly stated articles

* it is a very common restriction on shares, **and although the right to transfer shares is one of the incidents of share ownership, the right is not absolute** – a restriction is not repugnant to ownership of shares, but is one of the original incidents attached to them by the contract contained in the articles (also no evidence of *mala fide*)

Laskin **(dissent):** the company has effectively turned itself into a private club despite its incorporation as a public co

* **if a company is unwilling to establish criteria upon which to enable a measure of *reasonable exercise of discretion***, it ought not to be permitted to have the cover of incorporation as a **public company**
* *Act* does not expressly confer power to restrict shares – just says they are transferable as provided in articles
  + Need to have some standard accepted to make it amenable to judicial control

**Shareholder agreements** (pooling agreements - section 175)

* Agreements amongst shareholders as to the manner in which they will vote their shares are lawful (*Ringuet*)
* In small businesses, shareholders are typically also directors, or have other roles in the business
* Must be for a lawful purpose:
  + **Directors cannot contract how they will vote as Directors**
  + if Directors are also shareholders, they may sign a shareholders agreement and use their rights under that agreement as shareholders, but the agreements cannot be used to fetter discretion of directors
  + Shareholder Agreements are often planned in phases; we modify and replace them when new shareholders invest or old shareholders retire
* Sometimes a **corporation is party to a shareholders agreement**
* **What else is in a shareholders agreement:**

1. **Parties:** who are the shareholders? (people/partnerships/etc.)
   * What classes/rights, # or % of shares, purchase price (shares/loan)
2. **Transfers**
   * Restrictions? Are there any types of transfers that are permitted?
   * Buy-sell provisions, triggering events (retirement/death/going public), Valuation formula
3. **Management** – who will be Directors?
   * Self-appointment, or, right to appoint a certain # of board members
4. **Finance/budget** – plans to borrow money? Who will guarantee the loan?
5. **Confidentiality**
6. **Non-compete and non-solicit**
7. **Dispute Resolution**

**Ringuet v Bergeron [1960]**

**F:** group of people made shareholders agreement that they would acquire 50 shares of a company (which would give them control of it), and then that they would vote themselves into BoD in different capacities, and agreed to vote unanimously in all meetings, providing a penalty for breach of contract

**I:** is this agreement contrary to public order or legality?

**A: there is nothing illegal or contrary to public order in an agreement to unite upon a course of policy or action and upon whom the directors they will elect**

* The fact that an agreement **may potentially involve a detriment to minority shareholders** does not render it illegal and contrary to public order
* Courts are hands-off with contracts between shareholders - they can pool their votes if they wish to
* Just because someone is a director, does not mean they cannot have an SA if they are a shareholder

**Common share structure:**

* **Class A voting**, participating without par value
* **Class B non-voting**, participating without par value
* **Class C voting with $1 par value** – 100 maximum outstanding – good way to allocate voting rights without affecting any other rights (depending on how much someone has invested)

**Chapter 10: Shareholder Remedies**

* Ownership of a share means that shareholder has a “bundle of rights” attached to that share
  + **Remedies are the means by which shareholders can enforce some of those rights**
* shareholders can assert some rights **without starting an action in court**:
  + Voting, Proposing an item for the AGM agenda, Requisitioning a meeting, Removing directors

**Derivative Action**

* What happens when a wrong is done to the corp but the directors don’t do anything about it?
* *It seems like, based on the common law, a* shareholder would not have standing to bring an action to remedy the wrong, and/or receive the benefit if the action is successful

**Foss v Harbottle [1843]**

**F:** directors sold property to the company at an inflated price, but was approved by majority of shareholders (self-dealing); a few minority shareholders attempted to bring an action on behalf of the company

**A:** corporation is a separate legal entity, so it is the proper plaintiff in these scenarios if a wrong has been done to it

* Majority rule will speak for the company – these issues are not for the courts, but for meetings
* **If the majority ratified this wrong, that majority speaks for the company, so individual shareholder has no standing to bring an action on behalf of the company**
  + **No common law derivative action**

**Statute says the opposite:**

* **A shareholder may bring an action on behalf of the corporation**
  + The cause of action *derives* from the corporation’s cause of action (ie. derivative action)
  + The action is rectify a wrong committed against the corp in situations where the mgmt is not trying to
  + Often, 1+ of **the management was the alleged wrongdoer** (so obviously they won’t bring action)
* **Statute is giving the shareholder standing if certain criteria are met (to prosecute, or defend on behalf)**
* Two step process: complainant must apply for leave first, then commence legal proceeding on behalf of corp
  + 232(1) – Rights are granted to a shareholder (broad definition) *or* a director
  + 233(1) – criteria for leave to commence the action
  + 233(4) – court may make any order it deems appropriate (a lot of flexibility here)
  + 233(5) – legal proceeding (step 2) cannot be settled outside of court without approval
  + 233(6) – ratification of shareholders does not immediately dismiss action, but can be used as evidence
* **Pro:** Enhance management’s accountability
* **Con:** Potential for frivolous or nuisance suits (this is a reason why complainants must apply for leave first)

Note: there is significant overlap with Director’s breach of DoC or FD with DAs, PAs and oppression remedy

**Re Northwest Forest Products [1975]**

**F:** Northwest owned 51% of pulp company Forest Valley; FV then sold assets to another company at apparent undervaluation;shareholders asked directors of NW to vote to set sale aside; sought leave for derivative action

**I:** do they meet criteria under statute for step 1?

**A:** most criteria are satisfied – but is it in the interest of the corporation that the action be brought?

* **Do not have to prove their case – just show *prima facie* in the interest of the company (low threshold step 1)**
  + **minority shareholders are usually on the outside with limited information available at this step**
  + not held to the same standard as the Crown would be in a criminal *prima facie* case
* Court has discretion to allow minority shareholders to commence action on behalf of the company
* May be concerning matters to individual shareholders of FV, but that does not detract from or preclude this DA
* Sale was so 90K below the market value; failed to seek out other bids – so was *prima facie* in the interest
  + Director was negligent, not reasonable, corporation suffered a loss (and director Clarke appears to gain)
  + **Granted leave** – move to second stage of action (we don’t look at that)

**Re Bellman and Western Approaches [1981]**

**F:** Split amongst directors (5-3): Bellman group appointed 3, Duke appointed 5 – Duke then got loan which allowed them to purchase shares to control all directors; but loan required Duke to disclose confidential information to the bank, and a requirement that Duke use their powers to cause Western to go public; Complainants seek leave for DA

**A:** directors claim they were not given notice because one of the grounds in the petition was not in the notice letter

* **Notice does not have to specify each and every cause of action** – just requires ‘reasonable notice’ of intention to apply to commence a derivative action
* Court does not have to satisfy that it is in the interest of the corporation – only have to show that **it appears to be** in the best interests of the company
  + Presumably it was the intention of the drafters to remove the common law barriers to this action (*Foss*)
    - Ratification procedure by majority is also clearly eliminated
  + Quantifiable loss was not proven, but there was still evidence of potential loss
  + Loan agreement would require borrowers to pay a fee based on gross revenue if they did not go public, which might place directors in **conflict of interest** – keep revenues down to reduce fee, or maximize revenue in the interest of all shareholders

*Baron:* two-step process has lower threshold, but allows courts to shut down actions quickly to not bog down court,

**Turner v Mailhot [1985]**

**F:** P and wife had 30% of shares; the rest held by D and his wife; after disagreement, P and wife were fired, locked out of building; P sought and obtained leave to bring DA, seeking return of lost income diverted to the defendant

**A:** *Wallersteiner* – person bringing DA had exhausted all of their money, but still sought to bring action; would derive very little personal benefit from victory in litigation, and was therefore indemnified

* Here, Turner, as a 30% shareholder, would stand for great personal benefit out of litigation, not so much for company (**not a ‘lone altruist’**) – he also has not exhausted his financial means at all
  + **Financial ability is an important consideration, but it is not mandatory**, as that would be contrary to the idea that the plaintiff is the agent of the company for the purposes of the action
  + The benefit being sought purely for the plaintiff is certainly also a factor
  + Turner should accordingly get ½ indemnity
* **Mailhot simply paid for his costs at his discretion and only for his benefit** – should have to pay back 40K which will be used to indemnify Turner for future costs (Baron – very unique order here, shows flexibility)

**R:**  using company funds to defend an action for the sole benefit of the shareholder – D will have to pay back

**Re BCE vs Peoples Department Stores**

*Peoples and BCE* made a really big mess and we need more cases to go to trial about breach of duty, etc.

“to the extent that People’s and BCE are indeed followed by lower court judges, they are likely to lead to different and contradictory readings in different courts, at different times, and by different judges” – *Jeffrey MacIntosh*

**Baron thinks it is very unclear**

* Directors must consider the best interests of the corp.
* It may also be appropriate (not mandatory) to consider the impact of a corp. decision on shareholders or particular groups of stakeholders (Directors need to take a look around)
  + When they are considering what is in “the best interests of the corp.”, directors may look at the interests of: shareholders, employees, creditors, consumers, gov’t, and the environment
* Always comes back to the best interest of the corporation, not any particular group

**Access to justice versus frivolous litigation**

* 232(1)(c) complainant [must be] acting in good faith; But, we need to ensure that everyone has access to justice
* But, we need to balance this need with our Barristers’ & Solicitors’ Oath, that we will not promote suits on frivolous pretenses, etc. (more so in US, where many people use courts as a time/resource waster)
* *BCA* s.232 strikes a balance: **a complainant with a legitimate cause of action is permitted to proceed, but a complainant acting not in good faith is not**

**Personal Action:** some causes of action are personal to the individual shareholder(s) (ie. plain old litigation)

* **a civil cause of action** against a Director for breach of duty of care
  + E.g. alleged negligence, as in the facts in *Peoples, UPM, Bata*
  + s.142(1)(b) does not name a beneficiary – duty of care is owed to a broad range of beneficiaries
* **a personal action alleging that the Directors acted in bad faith** 
  + *E.g. Smith v. Fawcett* – an example where the individual plaintiff had standing to challenge the directors’ actions (right person to bring the claim – they are allowed to make that challenge)

**Personal actions for shareholders**

* Look for “interference by the company with the rights of **certain** shareholders”
* For example:

1. changing the rights attached to one class of shares
2. depriving a shareholder of rights conferred to him by the Articles
3. altering the structure of the corp. in a manner that amounts to fraud on the minority
4. depriving a shareholder of her right to vote (pretty common, clear example of where rights are affected, and the deprived person has standing to bring an action against directors)

* examples may have been done by one group of shareholders (majority) to another (minority), depriving rights
* or, examples could be caused by directors acting for a collateral purpose and causing the corp. to act in a manner that deprives a group of shareholders of their rights
  + i.e. the “bad guys” could be the majority shareholders, or, the directors

If the directors perform an *ultra vires* act (i.e. they do something forbidden by the Articles) or do something illegal

* **It is likely there would be both a personal action and a corporate action (derivative action)**
  + Causing damage to the whole company, and the shareholders at the same time
  + “the fact that the second alternative is a possible one is no reason for refusing to allow a member [shareholder] to sue the company if he has an independent right to do so”

**Goldex Mines v Revill [1975]**

**F:** Goldex was a shareholder of Probe Mines; dispute among Probe directors over proposed purchase of gypsum claims from a company controlled by a former Probe director – Goldex alleged breaches of duties by directors and defendant shareholders, but did not specify whether duties were owed to Probe or to its shareholders

**A: If you want to sue for both (derivative and personal), must separate them clearly**

* For derivative actions, you must do the two step process and apply for leave beforehand; this has not been done so the derivative action cannot be judged
* There is also an element of personal action here – if wrongs were committed against an individual, **‘the company cannot sue for my injury, it can only sue for its own’**
* However, claims are not properly pleaded – personal elements are inextricably woven into the derivative claims
* Could give leave to amend, but will just strike out the writ – no limitation period, so the writ can be remade
  + Also, P could apply for leave for derivative action, and add the derivative claims to the personal claims

**Hercules Management v E&Y [1997]**

**F:** H went into insolvency; Shareholders brought personal action against E&Y saying reports from 1980-1982 were negligently prepared, and as a result they lost money on their investments

**A:** But, the shareholders **were not harmed in two different ways here** – **they were harmed as one member of a collective group that was all harmed in the same way** – must bring action as a derivative and not a personal action

* In **supervising management** (through looking at resolutions adopted at meetings), **the shareholders are acting as a body in respect of the corporation’s interests** rather than as **individuals in respect of their own ends**
* Interest of shareholders in proper management is indistinguishable from the interest of the company itself
  + Any loss suffered by shareholders will be recouped in a claim brought on behalf of the company

**Oppression remedy –** does the majority still rule?

A basic principle of corporate law is Majority Rule:

1. The majority voting shareholders decide who the directors will be, and then those directors run the corp
2. The majority voting shareholders also determine the outcome of shareholder resolutions;
3. But, there is potential for directors and/or majority shareholders to act in a way that is oppressive or unfairly prejudicial to the minority shareholders

* the Oppression Remedy was created to give minority shareholders a remedy in those situations
* It allows judges to use the statute (s.227) to change the nature of majority-minority relationships in corp law
* Historically, *majority rule* prevailed, but now:
  + **The majority rule still prevails except when it is oppressive or unfairly prejudicial to the minority** [*CBCA* adds a 3rd category – unfair disregard, but not in BC]
  + we still look at both common law and statute
* this remedy is available to a wide range of stakeholders, if harm has been done to them (**must have been actually harm done**): security holders, creditors, directors, officers, etc.
  + very broad: “and any other person whom the court considers to be an appropriate person to make an application under this section”
* What is the **difference between breach of fiduciary duty and the oppression remedy**?
  + Breach of FD is one kind of mischief; the OR is a remedy that can be used to fix it (cause and effect)
  + There is significant overlap, but not 100% overlap
* **Oppressive conduct** is broad (e.g. majority use their powers in a way that is unfairly prejudicial to the minority)
  + **Breach of Fiduciary Duty is narrower class within oppressive conduct** (e.g. unfair self-dealing)
* Canadian courts have allowed **derivative actions to proceed under the oppression remedy** (p801)
  + An **oppression remedy can also be used in some personal actions**
  + If you are dealing with a corporation in some stakeholder role, and the corporation is harmed or you are harmed personally, there are two paths you can take, but you can use the oppression remedy for either

**Re BCE [2008]**

**F:** directors chose 1 out of 3 choices to sell BCE; the debenture holders (banks) allege directors were oppressive

**TJ:** banks have standing to bring an action, asking for this remedy, but they were not successful

**SCC:** did the trial judge err in dismissing the claim?

* There are two possible approaches involved with the statutory oppression remedy

1. A strict reading of the statute (oppression or unfair prejudice), as stated in some case law?

* No. “A categorical approach to oppression is problematic because the terms cannot be put into watertight compartments or conclusively defined”
  + - * + “The statutory components of oppression are really adjectives that try to describe inappropriate conduct; the difficulty with adjectives is they provide no assistance in formulating principles that underline court intervention” – SCC needs to come up with an effective way for lower courts to follow

1. What about broader principles that underlie and unite the various aspects of oppression?

* “In our view, the best approach…is one that combines the two approaches – it is fact specific”
* First, we should look at the broader principles underlying the remedy, in particular, what were the **reasonable expectations** of the person alleging they were harmed?
* Then, **if the complainant can establish a breach of reasonable expectations**, the court will **move forward and look at whether the conduct** was **actually oppressive or unfairly prejudicial**

**First Edmonton Place v 315888 Alberta [1988]**

**F:** complainant seeking leave under oppression remedy; FE contends that a **lease** is a security of the corporation that brings them within the definition of ‘complainant’ under the act

**A:** security: debt obligation of a corporation, and a certificate evidencing that obligation

* Creditor can be a ‘complainant’ if they **hold security** that is **capable of being registered in the registrar or corps**
* Under ‘proper person’ (BCA = ‘appropriate person’) category could be broader; two circumstances where creditor would be entitled to standing as proper person:
  + - * + **(1) act by directors constitutes using the corporation as a vehicle for committing fraud on applicant**
        + (2) act by directors constitutes a breach of underlying expectation of applicant

did circumstances that gave rise to lending include an element which prevented creditor from taking adequate steps to protect their own interests?

**Ebrahimi v Westbourne Galleries [1972]**

**F:** partners with lucrative business, who bought/sold expensive rugs – decided to incorporate, were sole shareholders and took directors salaries – one of their sons grew up, and each partner transferred 100/500 shares, entered board – father and son had fight with other partner; passed resolution to remove him

* Ebrahimi brought action to have the company winded up

**A:** After reviewing long line of cases, **common thread is distilled in the words “just and equitable**”: the words are a recognition that a limited company is more than a mere judicial entity, with a personality in law of its own; connected to it are individuals with rights, expectations and obligations

* Oppression remedy is available to minority shareholders is available **if 1+ of the 3 elements is satisfied:**
  + - * + (i) the **association formed on basis of personal relationship** involving mutual confidence
        + (ii) understanding that all, or most, of the shareholders **shall participate in the conduct of the business**
        + (iii) **restriction on transfer of shares among management** (so someone can’t pick up and leave)
* **it was in Ebrahimi’s reasonable expectations that he would continue to manage as a director**
* **E was oppressed** because he was trapped as shareholder, no longer on BoD (wont let him sell his shares)
  + - * + Money is all tied up in the corporation
* Category of applicants for OR is very broad – used to seek fairness/justice/equity – very fact specific, and courts have broad discretion to come up with a remedy

**C: Just and equitable to have the company wound up and Ebrahimi paid his capital**

**Ferguson v Imax Systems Corp [1983]**

**F:**Imax systems corp had founding shareholders of 3 couples – one couple divorced and they tried to squeeze the wife out by passing resolutions – changing her shares to limited, non-voting shares that did not receive dividends; F said it was unfairly prejudicial

**A:** here we have a small, closely held corporation controlled by small number of individuals

* F’s work and role with the company is important; the fact that the group intends to deny her any participation in the growth of the company
  + - * + The resolution authorizing the change is culminating event in a lengthy course of oppressive and unfairly prejudicial conduct
        + She is the only shareholder that is affected, and was not a small investor who came on at a later date

**C:** Set resolution aside

**Naneff v Con-Crete Holdings [1995]**

**F:** father built family business, gave shares to two sons; parents did not like one of their sons lifestyles and wanted him out – removed him from the company, do not let him participate in management anymore

**TJ** – gave OR that the family business can be sold to anyone that wants to buy it

**On appeal:** TJ remedy went too far – **OR cannot be punitive, only used to rectify the situation (restore fairness – put things back in the middle)**

* N senior was going to keep control for life, was not about to hand over control to his sons
* What were the reasonable expectations of the son?
* Having family business sold to anyone in public market was not one of those expectations
* **TJ gave an inappropriate remedy** – appeal proposed different remedy where shares are purchased at fair market value (buying him out would have been fair)