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RECENT DEVELOPMENTS & TRENDS IN CASE LAW

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When Can the Director of a Corporation Be Held Personally Liable for Oppression?

Oppression is a broad and equitable remedy. It allows Courts to rectify unfair or prejudicial behaviour on the part of corporate stakeholders. While most Canadian case law is devoted to the issue of what amounts to oppression, a new decision of the Supreme Court of Canada, *Wilson v. Alharayeri*, 2017 SCC 39, clarifies the circumstances in which a director can be held personally liable for oppressive conduct. *Wilson* emphasizes that the test for personal liability for oppression is fluid and contextual.

Facts

Wilson involved an oppression application by the minority shareholder and director (the "applicant") of a technology company incorporated under the *Canada Business Corporations Act*, R.S.C. 1985, c.C.-44 (the "CBCA"). As a result of the defendants' conduct, the value and proportion of the applicant's shares in the corporation were significantly reduced.

The story in *Wilson* begins when the applicant agreed to sell some of his common shares in the technology company to another corporation. He did so without advising the Board of the technology company. Ultimately, the applicant never sold his shares and when the Board discovered the applicant's conduct, he was reprimanded. The applicant eventually resigned as CEO and President of the corporation and the individual defendant, who was a member of the company's audit committee and Board, became the new President and CEO.

The company began experiencing financial troubles. In response, it issued a private placement of convertible secured notes to its existing common shareholders (the "Private Placement"). The Private Placement would dilute the proportion of common shares held by any shareholder who did not participate in it.

Before issuing the Private Placement, however, the Board accelerated the conversion of Class "C" Convertible Preferred Shares into common shares. The Board did so even though it was not clear that the financial test for Class C share conversion was satisfied.

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The applicant's Class A and B Convertible Preferred Shares were never converted into common shares, even though they met the applicable conversion tests. This occurred because the defendant President and CEO advocated against converting the applicant's Class A and B shares at a Board meeting, on the basis of the applicant's previous misconduct.

As a result, the applicant didn't participate in the Private Placement. The value and proportion of his common shares was reduced and he commenced an oppression application under section 241 of *CBCA*.

The application judge granted the application in part and held two directors personally liable for the oppression. The application judge found that, but for the oppressive conduct, the applicant's Class A and B shares would have been converted to 1,223,227 common shares, putting the applicant's loss at $648,310.00, for which the directors were to be held personally liable. The Quebec Court of Appeal affirmed the defendant directors' personal liability.

The defendant President and CEO appealed, arguing it was not appropriate to hold him personally liable for the oppression. The Supreme Court of Canada dismissed the appeal.

When Will a Director Be Held Personally Liable for Corporate Oppression?

Under section 241(3) of the *CBCA*, the Court has a broad remedial jurisdiction to craft a remedy once it determines that an act of oppression has taken place. In particular, the Court may make "any interim or final order it thinks fit", including an "order compensating an aggrieved person".

The Court in *Wilson* began its analysis by observing that the oppression remedy "seeks to apply a measure of corrective justice". That is, the purpose of the remedy is to correct any inequities between the parties.

Noting that the *CBCA* itself provided no guidance on how to craft an oppression remedy, the Court turned to the case law, relying primarily on the Ontario Court of Appeal decision in *Budd v. Gentra* (1998), 43 B.L.R. (2d) 27. In *Budd*, the Court of Appeal noted that a director will not be held personally liable for oppression unless: (i) the director or officer was implicated in the oppressive conduct; and (ii) the order is "fit in all the circumstances".

According to *Wilson*, these two requirements do not mean that a director can only be held personally liable where the director is a controlling shareholder or where there is evidence of the director's bad faith. Director liability for oppression can take place in the absence of bad faith conduct. Moreover, whether the director has reaped a personal benefit from her conduct is not a precondition to finding the director personally liable.

On the contrary, the Court in *Wilson* emphasized a "flexible and discretionary" approach to directors' liability. Accordingly, the Court adopted and clarified the two-pronged test from *Budd* as follows:

1. The first prong requires that the oppressive conduct be "properly attributable to the director because he or she is implicated in the oppression". That is, the director must have exercised, or failed to exercise, her powers so as to effect the oppressive conduct.

2. Once the first prong is established, the Court turns its mind to whether the imposition of personal liability would be "fit in all the circumstances". The Court in *Wilson* characterized fitness as an "amorphous concept". There are four general principles that should guide the Courts' analysis:

   a. The oppression remedy must "in itself be a fair way of dealing with the situation". For example, where the directors have derived a personal benefit from the oppressive conduct, an order finding the director personally liable will be "fit". The list of factors to determine whether personal liability is fair is not closed and should not be "slavishly applied". Bad faith and personal benefit are "but two factors" to be considered in the overall factual matrix;

   b. Any order for personal liability should "go no further than necessary to rectify the oppression";

   c. The order should serve only to vindicate the reasonable expectations of the corporate

stakeholders. For example, a complainant cannot seek to obtain an advantage over creditors of the corporation by seeking to hold a director personally liable for oppressive conduct; and

d. The Court should consider the "general corporate law context" in deciding whether to hold the director personally liable. In other words, director liability "cannot be a surrogate for other forms of statutory or common law relief, particularly where such other relief may be more fitting in the circumstances".

Applying the considerations above, the Supreme Court of Canada held that the trial judge made no error in imposing personal liability against the defendant President in *Wilson*.

First, the defendant was implicated in the oppression. As a member of the company's audit committee, he played a "lead role" in Board discussions resulting in the non-conversion of the applicant's Class A and B shares. While this conduct alone would not suffice to impose personal liability on the defendant, other factors tipped the balance towards finding liability.

That is, a finding of personal liability was "fit" in the circumstances because: (i) the defendant had accrued a personal benefit as a result of the oppression, i.e. he increased his control over the corporation; (ii) the remedy went no further than necessary to rectify the applicant's loss; and (iii) the remedy was appropriately fashioned to vindicate the reasonable expectations of the applicant as a Class A and B shareholder. The applicant reasonably expected his shares to be converted if the corporation met the applicable financial tests set out in the company's articles.

In all the circumstances, the trial judge did not err in holding the defendant director personally liable for the oppression.

Conclusion

Wilson represents less a radical transformation in the law of oppression than a refinement. The Court's emphasis is on a contextual approach to director liability for oppression.

In this way, *Wilson* affirms the broad and equitable nature of the oppression remedy. Rather than imposing personal liability on a director on the basis of rigid preconditions, *Wilson* invites a holistic approach to crafting an appropriate order.

The two key considerations, i.e. whether the director is implicated in the oppressive conduct and whether personal liability would be "fit in all the circumstances", are informed by the equities of the individual case.