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Corporate Attribution and Knowing Assistance: Active Participation Required

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The Supreme Court of Canada recently weighed in on the doctrines of knowing assistance and corporate attribution when it overturned the majority decision of the Ontario Court of Appeal in *Christine DeJong Medicine Professional Corp v DBDC Spadina Ltd* ("***DeJong***"), 2019 SCC 30, adopting the minority decision in its entirety.

Often in cases of fraud, claimants rely on the equitable doctrine of knowing assistance to catch "strangers" to the fraud who had actual knowledge of it and hold assets that can be traced to the fraudulent scheme. However, complications arise when victims of the same fraud are pitted against each other in the quest to recover assets. This was the case in *DeJong*, where both the appellants and respondents were victims of the same fraudulent scheme.

In overturning the Court of Appeal's decision, the Supreme Court of Canada held that when an officer of a corporation defrauds that corporation as part of a larger fraudulent scheme, the officer's fraud is not attributed to the company.

The Fraudulent Scheme

The fraudulent scheme in *DeJong* was as follows: Norma and Ronauld Walton (the "**Waltons**") convinced both the appellants and respondents to invest equally with them in project-specific corporations that would acquire and improve commercial properties. However, instead of investing any funds of their own, the Waltons moved the investors' money in and out of the various corporations for their own purposes and used the rest of the money to further their own personal interests.

The appellant, Christine DeJong Medicine Professional Corporation ("**DeJong**"), invested approximately $4 million with the Waltons' "Schedule C Companies". The respondents, DBDC Spadina Ltd. and other related companies (collectively " **DBDC**"), invested approximately $111 million with the Waltons' "Schedule B Companies". As part of the fraud, the Waltons moved large sums of money from the Schedule B Companies through their own clearing house, Rose & Thistle Group Ltd., and into the Schedule C Companies.

DBDC was the first to discover the fraud. In addition to seeking recovery against the Waltons directly, DBDC also sought to collect $22.6 million against 10 project-specific companies, including the Schedule C Companies, alleging that these companies knowingly assisted in the fraud because they were used in the Waltons' overall fraudulent scheme.

A receiver was appointed by the court over the Schedule C Companies, who liquidated the assets of these companies. DeJong sought to recover some of its investments from these proceeds. DBDC's claim for knowing assistance targeted the same funds and would have left DeJong with nothing left to recover, if the claim was successful.

Lower Court Decisions

In 2016, Justice Newbould awarded DBDC $66 million against the Waltons personally for fraudulent misrepresentation, deceit and

breach of fiduciary duty. Justice Newbould dismissed DBDC's claim for knowing receipt and knowing assistance against the Schedule C Companies.[1]

In 2018, the majority of the Court of Appeal overturned Justice Newbould's decision, finding that while Ms. Walton was only a 50% shareholder of the companies, in reality she was the *de facto* controlling mind of the Schedule C Companies, thereby making these companies liable for knowing assistance in the fraudulent scheme.[2]

Knowing Assistance and Corporate Attribution

Under the knowing assistance doctrine, a stranger to a fiduciary relationship is liable where it, with actual knowledge (not constructive knowledge), participates in or assists a fiduciary in a fraudulent and dishonest scheme.

The elements of knowing assistance in a breach of fiduciary duty are: (1) a fiduciary duty; (2) a fraudulent and dishonest breach of the duty by the fiduciary; (3) actual knowledge by the stranger to the fiduciary relationship of both the fiduciary relationship and the fiduciary's fraudulent and dishonest conduct; and (4) participation by or assistance of the stranger in the fiduciary's fraudulent and dishonest conduct.[3]

The corporate attribution doctrine may be used to attribute knowledge and deceitful actions of an employee to their corporate employer. In 1985, the Supreme Court of Canada articulated the test for corporate attribution in *Canadian Dredge & Dock Co v The Queen*: the corporate attribution doctrine operates where the action taken by the directing mind (a) was within the field of operation assigned to him or her; (b) was not totally in fraud of the corporation; and (c) was by design or result partly for the benefit of the corporation.[4]

In *Deloitte & Touche v Livent Inc. (Receiver of)*, the Supreme Court added an additional element to the corporate attribution doctrine, holding that a court may decline to attribute the knowledge of a directing mind to a corporation if it would not be in the public interest to hold the corporation liable.[5]

In *DeJong*, the Court of Appeal held that the holding in *Livent* meant that the corporate attribution test could be applied in a "less demanding fashion", meaning that the knowledge of a directing mind could be attributed to a corporation even if all elements of the test were not met.[6]

The Court of Appeal found that "participation" required no significant act or omission on the part of the stranger. There was no evidence that the Schedule C Companies had actively engaged in assisting in diverting the funds fraudulently taken from the Schedule B Companies. However, because Ms. Walton was the controlling mind of the Schedule C Companies, her actions could be attributed to them. Therefore, the Schedule C Companies could be held liable for knowing assistance.[7]

The Supreme Court of Canada disagreed. It held that *Canadian Dredge* sets out the minimum requirements for the corporate attribution doctrine to apply, and confirmed that all elements of the corporate attribution doctrine must be met to attribute the mental state of a directing mind to the company. The Supreme Court adopted the minority decision of Justice van Rensburg of the Ontario Court of Appeal in its entirety and, as a result, affirmed that:

- the knowledge of the directing mind of a company will not be attributed to a company where the controlling mind was acting outside the scope of her authority, in fraud of the company, or only for her own benefit;
- where a company is sued for knowing assistance, the plaintiff must demonstrate through evidence that the corporation committed specific acts that helped the fraudster. Being "used" by the fraudster is not sufficient to find the corporation liable; and
- each individual company must be shown to have participated in the fraud – liability cannot be imposed on a corporate group

as a whole without evidence implicating each individual company.

Justice van Rensburg further held that courts should not grant remedies for knowing assistance where "one group of defrauded investors" seeks damages "against another group that has been defrauded in a similar manner."[8]

This decision provides some clarity and certainty to the law of knowing assistance and corporate attribution. Moreover, it should provide comfort and protection to shareholders in that they should not be held liable for the fraud of a rogue directing mind where they had no knowledge of and did not actively participate in the fraud.

[1] *DBDC Spadina Ltd v Walton*, 2016 ONSC 6018.

[2] *DBDC Spadina Ltd v Walton*, 2018 ONCA 60.

[3] *Ibid* at para 211.

[4] *Canadian Dredge & Dock Co v The Queen*, [1985] 1 SCR 662 at para 66.

[5] *Deloitte & Touche v Livent Inc (Receiver of)*, 2017 SCC 63 at paras 100, 104.

[6] *DBDC Spadina Ltd v Walton*, 2018 ONCA 60 at para 70.

[7] *Ibid* at paras 68, 113.

[8] *Ibid* at para 248.

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