

Personal Liability of Directors in Oppression Cases: The Supreme Court Clarifies the Applicable Criteria in *Wilson v Alhareyeri*

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By

In *Wilson v Alhareyeri*, 2017 SCC 39, released on July 13, 2017, the Supreme Court of Canada affirms the decisions of the lower courts holding two directors personally liable to pay compensation to a minority shareholder in an oppression case brought under section 241 of the *Canada Business Corporations Act (CBCA)*. The Supreme Court's unanimous decision clarifies the criteria governing the imposition of personal liability on corporate directors in oppression cases.

The facts in *Wilson* are as follows. The corporation issued a private placement, which had the effect of substantially diluting the proportion of common shares held by any shareholder who did not participate in it. Prior to issuing the private placement, the board of directors refused to convert into common shares the Class A and Class B Convertible Preferred Shares held by the Respondent, Mr. Alhareyeri, even though these shares were convertible based on the financial tests laid out in the articles of incorporation and the corporation's audited financial statements. In contrast, the board accelerated the conversion of Class C Convertible Preferred Shares held by the President and CEO, despite doubts expressed by the auditors as to whether the test to convert these shares into common shares had been met. As a result of the private placement, the Respondent's proportion of common shares and their value were significantly reduced.

The trial judge found that the President and CEO and the chairperson of the audit committee, who were the only two members of the audit committee, were personally liable for the board of directors' refusal to convert the Respondent's Class A and B shares into common shares, and the failure to ensure that the Respondent's rights as a shareholder were not prejudiced by the private placement. Both directors had used their influence, as the only audit committee members, to advocate against the conversion of the Respondent's shares.

The main issue before the Supreme Court was when personal liability for oppression may be imposed on corporate directors. The trial judge's finding of oppressive conduct was not in issue before the Supreme Court. The Supreme Court also summarily dismissed the Appellant's argument that the pleadings in the case were insufficient to ground the imposition of personal liability.

In Reasons written by Côté J., the Supreme Court confirms that the test set out in the Ontario Court of Appeal's decision in *Budd v Gentra Inc.* is the applicable test with respect to the imposition of personal liability on corporate directors in oppression cases. The Court also provides additional guidance on this issue in light of diverging views in the case law regarding the application of the *Budd* test.

Under the *Budd* test, personal liability can be imposed when: (1) the oppressive conduct is properly attributable to the director because he or she was implicated in the oppression; and (2) the imposition of personal liability is fit in all the circumstances.

The Supreme Court identifies the following four general principles that should guide courts in fashioning a “fit” order under section 241(3) of the *CBCA*, i.e. the oppression remedy provision:

1. *The oppression remedy request must in itself be a fair way of dealing with the situation.* The presence of the following factors provide indicia of fairness:

- (a) where directors obtain a personal benefit from their conduct;
- (b) where directors have increased their control of the corporation by the oppressive conduct;
- (c) where directors have breached a personal duty they have as directors;
- (d) where directors have misused a corporate power; and
- (e) where a remedy against the corporation would prejudice other security holders.

This is not a closed list of factors. In some cases, it may be fair to allocate responsibility partially to the corporation and partially to the directors personally.

2. *Any order under section 241(3) should go no further than necessary to rectify the oppression.* Section 241(3)'s remedial purpose is to correct the injustice or unfairness between the parties.

3. *Any order made under section 241(3) may serve only to vindicate the reasonable expectations of security holders, creditors, directors or officers in their capacity as corporate stakeholders.* Such orders cannot be used to vindicate expectations arising from family or personal relationships, or to serve purely tactical purposes, such as jumping the corporation's creditors' queue by seeking relief against a director personally.

4. *A court should consider the general corporate law context in exercising its remedial discretion under section 241(3).* This means that director liability should not be a surrogate for other forms of statutory or common law relief.

The Supreme Court rejected the Appellant's submissions seeking to narrow the *Budd* criteria. It held that the additional factors advocated by the Appellant – whether the director has control of the corporation, acts in bad faith, or has obtained a personal benefit at the expense of the oppressed party, while they may be important considerations, are not necessary criteria for the imposition of personal liability.

The guidance provided by the Supreme Court in *Wilson v Alharayeri* is very general. While helpful, the Court's elaboration on the *Budd* test consists in broad principles and non-exhaustive lists of non-mandatory factors or, in the Court's own words, “guideposts informing the flexible and discretionary approach the courts have adopted” under section 241(3). While this decision is unlikely to give corporate directors the specificity and clarity that they would like to have on the issue of personal liability, it is important to remember that, as pointed out by the Court, the oppression remedy is meant to be a discretionary, equitable remedy that looks to commercial realities. The appropriateness of an order turns on equitable considerations, and the courts have consistently held that “[i]t would be impossible, and wholly undesirable, to define the circumstances in which these considerations may arise.” Fashioning a fit remedy is a fact-dependent exercise. The best protection against personal liability is for directors to ensure that they do not participate in corporate conduct that is oppressive, unfairly prejudicial to or unfairly disregards the interests of any security holder, creditor, director or officer. Further, it is important for directors to “put their best foot forward” before the court of first instance:

given the importance of factual findings in oppression cases, it will be very difficult to have decisions in such cases overturned on appeal.

The information and comments herein are for the general information of the reader and are not intended as advice or opinion to be relied upon in relation to any particular circumstances. For particular application of the law to specific situations, the reader should seek professional advice.

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