

DIRECTOR LIABILITY FOR EMPLOYEE REMUNERATION: SIGNIFICANT CHANGES LIKELY IN STORE IN ONTARIO

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All employers operating in Ontario will want to pay close attention to a number of proposed changes to the director liability regime with respect to unpaid wages and vacation pay. In their Final Report on Ontario's Changing Workplaces Review issued on May 23, 2017, the government's special advisors have recommended changes to the *Employment Standards Act, 2000* ("ESA") and the *Business Corporations Act (Ontario)* ("OBCA"). If these recommendations are accepted and passed into law, the enforcement process for employee remuneration claims will become more streamlined, and the amount and likelihood of potential director liability will likely increase.

Current Director Liability Rules

Both the ESA and the OBCA currently impose personal liability on the directors of business corporations for unpaid wages and vacation pay in certain circumstances, but not severance or termination pay. However, any such liability is not absolute, and both the ESA and OBCA contain detailed conditions which must be satisfied. In practice, the complexity of these conditions often deters individuals from pursuing claims against directors.

In the case of the ESA, there is a separate enforcement regime through the Ministry of Labour. However, an employee seeking a claim against directors for unpaid remuneration must choose between proceeding with an administrative claim under the ESA's enforcement mechanism or going to court. They do not have the option to do both. In many cases, the fact that the Ministry and the courts operate in parallel puts claimants in a difficult position, especially when there are related court proceedings or a severance claim on top of the ESA claim.

To further complicate the matter, formal insolvency or liquidation proceedings against the employer (or, in the case of the OBCA, a judgment against the employer) are a prerequisite to an employee's ability to seek a direct remedy against the directors. In addition, the current regime under both the ESA and the OBCA does not allow for one representative employee to act on behalf of all employees with unpaid remuneration claims.

Stated Barriers to Effective Enforcement

In their Final Report, the special advisors note that the current legal regime in Ontario is often not the “relatively streamlined process” which would be preferred. Instead, the following barriers to a direct remedy for employees against directors are currently observed in the existing ESA and OBCA provisions:

1. There is a requirement for a formal court-based insolvency proceeding involving the employer or, under the OBCA, a judgment against the employer, before employees can pursue directors;
2. There is no ability for one employee representative to act for all employees in an action against directors for unpaid remuneration;
3. Under the ESA, employees must file a proof of claim and wait to see if there will be a distribution in any insolvency proceedings before they can pursue the directors; and
4. The list of insolvency proceedings that will “trigger” director liability under the OBCA is incomplete.

These provisions, taken together, mean that employees are often essentially forced to either initiate bankruptcy proceedings or wait for another party (i.e. creditors) to initiate them. The special advisors note that it can be months, or even years, before employees and other unsecured creditors will know about whether or not there will be distributions.

The Final Report emphasizes the rationale for imposing personal liability, which is to ensure that employees are paid. The special advisors comment that existing provisions result in unnecessary, time consuming and expensive barriers to effective enforcement.

Recommended Changes

The special advisors have recommended that the personal liability remedies provided by the ESA and OBCA be harmonized and enhanced, all without altering the scope or extent of director liability. In the summary of their recommendations, the Final Report says the new enforcements rules “simply takes the existing purpose of the law and seeks to make important changes to make it effective”.

The Final Report makes the following specific recommendations regarding director liability for employee remuneration:

1. The ESA and OBCA should be amended to provide that up to six months’ wages and up to 12 months’ accrued vacation pay are to be the responsibility of directors. The only condition that must be met in order for an employee to receive these amounts is that they have not been paid by the corporation. (This means that the previous requirements to initiate proceedings against the employer would be eliminated.)
2. The ESA and OBCA should be consistent. (The enforcement rules are currently different.)
3. An employee representative should be able to bring proceedings or make a claim against directors on

behalf of all employees. (No such representative proceedings are currently contemplated or permitted.)

4. The Ontario Ministry of Labour should ensure that adequate resources are allocated, or continue to be allocated, and used to recover from directors any unpaid amounts owing by a corporation to an employee. (The Final Report emphasizes increased enforcement across the province for numerous workplace issues.)

Takeaways for Corporations and Directors

In response to the Final Report, the Ontario government announced proposed changes to employment and labour legislation and issued a press release which summarized the proposed changes. While most indications continue to be that the recommendations of the special advisors will be accepted, the specific revisions to the relevant legislation are not yet available. Our expectation, however, is that changes to numerous workplace and corporate rules, including those relating to director liability, will be implemented with effect on January 1, 2018. The impact of the changes to the enforcement regime for employee remuneration claims is potentially quite profound. We intend to continue to provide updates as future developments warrant.

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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