ONTARIO DIVISIONAL COURT DECISION CONFIRMS SHAREHOLDERS' RIGHT TO REQUISITION A MEETING

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Ontario Divisional Court Decision Confirms Shareholders' Right to Requisition a Meeting

On May 18, 2017, the Ontario Divisional Court, in a unanimous decision,[1] set aside the decision of Justice Wilton-Siegel of the Ontario Superior Court in *Koh v. Ellipsiz Communications Ltd.*[2] and ordered Ellipsiz Communications Ltd. ("**ECT**" or the "**Company"**) to call a shareholders' meeting, at the earliest convenient date, to consider the two resolutions put forward by Mr. Koh in his August 30, 2016 requisition. The Court also ordered that the record date for the requisitioned meeting be October 24, 2016, the date Mr. Koh had originally selected for a requisitioned meeting that the Company had failed to call.

The *Koh* case is the first decision directly dealing with the interpretation of what constitutes a "personal grievance" under Canadian corporate legislation. The case involves a tension between shareholder democracy and the right of directors to manage the business and affairs of the corporation. It clarifies that, on certain matters, shareholders retain their fundamental right to requisition a meeting of shareholders under the Ontario *Business Corporations Act* (the "**Act**") to remove the directors they have entrusted to run the corporation. The decision of the Divisional Court clarifies the meaning of "personal grievance" and offers useful guidance on the demarcation between a "personal grievance" and legitimate personal interests of shareholders in the business and affairs of a corporation. It emphasizes that shareholders, especially significant shareholders, may have personal interest in the business and affairs of a corporation, but that a board may only refuse to call a requisitioned meeting where it is clearly apparent that a shareholder is seeking to advance a "personal grievance".

Background to the dispute

Michael Koh is the largest shareholder of ECT, holding approximately 42% of the issued and outstanding shares. Serious disagreements arose between Mr. Koh, who is also a director of ECT, and four of the then six directors of the Company. The matters of disagreement included: Mr. Koh's role in negotiating a potential acquisition (one which he was potentially unwilling to approve as a shareholder); his removal without notice as chairman of the ECT board and his removal from the board of the Company's Taiwanese operating subsidiary,

Ellipsiz Communications Taiwan Ltd. ("**ECTW**"); and significant operational changes at ECTW. Faced with these and other issues, Mr. Koh demanded the resignation of three of the directors (the "**Canadian directors**"), failing which he would requisition a shareholders' meeting to remove the Canadian directors and replace them with his own nominees. The evidence of the Canadian directors was that they had no intention of resigning.

Mr. Koh requisitioned a shareholders' meeting under the Act to remove those directors. The Board refused to call the meeting based on a narrow exception under sections 105(3)(c) and 99(5)(b) of the Act because it claimed that the primary purpose of the meeting was clearly to redress Mr. Koh's "personal grievances" against ECT and its directors. Mr. Koh proceeded to call the meeting for November 28, 2016, as he was allowed to do under the Act. The Board, however, relying on s. 105(3) of the Act, stated that they would not recognize the results of such meeting.

Mr. Koh brought an application to require the Company to recognize the meeting. Justice Wilton-Siegel dismissed the application, finding that the directors had satisfied their onus of showing Mr. Koh's meeting was to redress a personal grievance and that sections 105(3)(c) and 99(5)(b) gave the directors the discretion to refuse to call or recognize the requisitioned meeting.

Faced with the decision, Mr. Koh cancelled the shareholders' meeting to be held on November 28, 2016 and appealed the decision. Shortly thereafter, the Company issued new share options which would have the effect of diluting Mr. Koh's shareholdings.

The Application Decision

Mr. Justice Wilton-Siegel set out the following principles for determining when a board may refuse to call a requisitioned meeting under sections 105(3) and 99(5) of the Act:

- A board's determination of whether a requisition can be refused on the grounds in s. 105(3) is a "right or wrong" decision. Accordingly, the business judgment rule does not apply to the determination of whether it is clear that the requisitioned meeting is being sought for the primary purpose of enforcing a personal claim or redressing a personal grievance.
- The onus is on the board to defend its determination that it is not required to call a requisitioned meeting.
- Where the requisitioned meeting is for the purpose of removing directors between annual meetings, this determination is not to be made solely on the basis of the resolutions to be put to shareholders, but requires a determination of the shareholder's intent, based on objective evidence of the shareholder's actions that was before the board at the time.
- Relevant considerations to determine whether it is "clearly apparent" that the requisition is to advance a personal claim or redress a personal grievance (which should not be read as being separate or

disjunctive) could be, but are not, limited to the following:

- The nature of the dispute;
- The extent to which the dispute is properly the subject of a shareholders' meeting or lies within the domain of the directors; and
- The extent to which the shareholder acted alone or with the support of other like-minded individuals.

The Decision of the Divisional Court

The Divisional Court did not disagree with any of these principles. It concluded, however, that the application judge erred in his application of some of the principles and in his interpretation of s. 99(5)(b) and the meaning of "personal grievance". The Divisional Court further concluded that the application judge reversed the onus that was properly on the Board, and erred when he focused only on Mr. Koh's personal interests and possible motivation. As a result, the application judge erred in improperly requiring Mr. Koh to prove that he was not pursuing a personal grievance and by not examining the possible motives of the Canadian directors with the same level of scrutiny.

The decision of the Divisional Court clarified the following:

- The court must look at the root of the shareholder's complaints and whether these complaints are linked to the "business and affairs" of the corporation. The test articulated by the application judge, namely whether Mr. Koh's complaints related to (i) issues of corporate policy or operations or (ii) "primarily pertained to the personal interests" of the shareholder was incorrect and not consistent with the language of the Act.
- A shareholder, and in particular, a significant shareholder, will have a personal interest in the corporation that may be difficult to distinguish from the business interests of the corporation.
- A personal interest, however, does not trigger the exception in s. 99(5)(b) of the Act. Only a personal grievance does.
- Only a shareholder's personal interests with no real or direct relationship to the corporation, or which are not otherwise integral to the business and affairs of the corporation or to the applicant's role as a shareholder, can be called "personal grievances".
- The court's role is not to determine whether the board or the shareholder is right in the circumstances, only whether the matter should be put to the shareholders at a meeting of shareholders.
- Any doubt on an application regarding whether an exception to the general requirement that a board presented with a valid requisition *shall* call a meeting of shareholders should be resolved in favour of the meeting being held.

The Divisional Court decision clarifies and provides boards and courts with significant guidance in determining when the rare exception to a board's general obligation to call a requisitioned meeting arises. In general, a board is obliged under s. 105(3) to call a validly requisitioned meeting. Before refusing to call the requisitioned meeting based on sections 105(3)(c) and 99(5)(b) of the Act, a board must carefully consider whether a shareholder, particularly a significant shareholder, is motivated by matters or concerns that are collateral to the business and affairs of the corporation or whether the heart of the shareholder's concerns is a disagreement over the direction and management of the business and affairs of the corporation. Professional directors and sophisticated boards can easily lose sight of the fact that shareholders remain the owners of the corporation. An attitude of "the board and management know best" can lead boards to discount shareholder concerns. Boards need to make the correct determination of whether a shareholder is clearly acting to redress a personal grievance or personal claim and any doubt must be resolved in favour of the shareholder. In close cases, the collective body of shareholders, and not the board, must be entrusted with determining whether they agree with the dissident shareholder.

Koh v. Ellipsiz Communications Ltd. is potentially of broader significance. The *Canada Business Corporations Act*, other provincial corporate legislation, not-for-profit corporations or companies acts, and the *Bank Act*, all contain similar, if not identical provisions relating to the board's ability to refuse to call a requisitioned meeting or include a shareholder proposal. The guidance offered by the Divisional Court will no doubt find broader application.

by Charlotte Conlin, Geoff Moysa and Paul Davis

[1] 2017 ONSC 3083, McMillan LLP represented the appellant[ps2id id='1' target=''/]
[2] 2016 ONSC 7345. McMillan LLP represents the applicant.[ps2id id='2' target=''/]

A Cautionary Note