SCC CONFIRMS DIRECTORS CAN BE PERSONALLY LIABLE IN CASES OF OPPRESSION

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In the recent and much anticipated decision of *Wilson v Alharayeri*[1], the Supreme Court of Canada ("**SCC**") confirmed that corporate directors can be held personally liable in cases of oppression.

Facts

The respondent, Mr. Alaharayeri ("**Mr. A**"), was a significant minority shareholder and director in a technology company (the **"Company")** incorporated under the *Canada Business Corporations Act* ("**CBCA**").[2] The Company was experiencing cash flow issues and began merger negotiations. During the course of these negotiations, Mr. A secretly entered into discussions and signed a share purchase agreement with the same business with whom the Company was negotiating. The Company's board of directors (the "**Board**") learned of Mr. A's failure to disclose this conflict of interest and Mr. A ultimately resigned his position as President, CEO and director.[3]

Shortly thereafter, the Company issued a private placement to certain of its existing common shareholders. The private placement had the effect of substantially diluting the shareholdings of any shareholder who did not participate in it.[4]

Importantly – before issuing the private placement, the Board accelerated the conversion of the Class C preferred shares owned by the appellant Mr. Wilson ("**Mr. W**"), who was the Company's new President and CEO. This meant that Mr. W could participate in the private placement. The conversion was done notwithstanding doubts expressed by the auditors as to whether or not the test for conversion of the Class C shares had been met.[5] Meanwhile, the Board refused to convert Mr. A's Class A and B Convertible Preferred Shares into common shares, despite the fact that those shares did meet the relevant conversion tests.[6] As a result, Mr. A could not participate in the placement and his shareholdings were diluted.

At the time these decisions were being made, the Board was comprised of seven directors. The audit committee was only comprised of two directors: Mr. W, and Mr. Black ("**Mr. B**").

As a result of the private placement and the dilution of his shareholdings, Mr. A brought an application for

oppression against several of the Company's directors.[7]

The trial judge found that there was oppressive conduct and held that Mr. W and Mr. B had used their influence, as the only members of the audit committee, to advocate against the conversion of Mr. A's shares during Board meetings. Mr. W and Mr. B were found personally liable for the Board's refusal to convert Mr. A's shares and the failure to ensure that Mr. A's rights as a shareholder were not prejudiced by the private placement.[8]

Issue

The question the SCC was required to answer in this case was: when can personal liability for oppression be imposed on corporate directors?

Reasons

The SCC upheld the decision of the trial judge and found that the imposition of personal liability against Mr. W and Mr. B was a fair way of rectifying the oppression Mr. A had suffered.[9]

The SCC confirmed that the two-pronged test articulated by the Ontario Court of Appeal in *Budd v Gentra Inc.*[10] ("**Budd**") remains good law and should be used when determining personal liability of directors under the oppression remedy.[11]

Under *Budd*, a director may be found personally liable if: (1) the director or officer is implicated in the oppressive conduct, and (2) the order is fit in all of the circumstances. [12]

Notably, the SCC highlighted several examples of situations in which personal orders against directors may be appropriate,[13] including:

- where directors obtain a personal benefit from their conduct;
- where directors have increased their control of the corporation through their oppressive conduct;
- where directors have breached personal duty that they have as directors;
- where directors have misused a corporate power; and
- where a remedy against the corporation would prejudice other securityholders.

In the *Wilson* case, Mr. W and Mr. B were very much implicated in the oppressive conduct. They took a "lead role" at Board meetings where the conversion of shares was dealt with (which on its own would not be sufficient), and they accrued a personal benefit as a result of the oppressive conduct.[14]

In terms of the *Budd* test itself, the first prong indicates that a director will be implicated in the oppression if that director exercised (or failed to exercise) his or her powers so as to effect the oppressive conduct.

With respect to the second prong, the SCC identified four general principles to guide courts in determining whether it is appropriate to assign personal liability:

1. The oppression remedy itself must be a "fair" way of dealing with the situation. While the fairness assessment is "unamenable to formulaic exposition", personal benefit and bad faith remain "hallmarks" of conduct properly attracting personal liability.[15]
2. An order assigning personal liability should only go as far as necessary to rectify the oppression; this is an acknowledgement that the remedial purpose of the oppression provision is to correct the injustice between the parties.[16]
3. Similarly, a finding of personal liability should only serve to vindicate the reasonable expectations of the corporate stakeholder.[17]
4. Director liability cannot be a surrogate for other forms of relief, where such other relief may be more fitting in the circumstances.[18]

Takeaways

This case confirms that corporate directors can be personally liable in oppression actions, so long as the imposition of liability is "fit in all the circumstances" and the director is personally implicated in the oppressive conduct.[19] The court's assessment in any given case will be highly fact-dependent.

Directors are more likely to face exposure to personal liability in situations where they have personally benefited or increased their control of the company through their oppressive conduct, or where they have otherwise acted in bad faith or in breach of their duties.

Accordingly, directors should take heed of this decision and should scrupulously avoid any conduct that is oppressive, unfairly prejudicial or that unfairly disregards the interests of any stakeholder. The SCC was clear that courts retain broad, equitable jurisdiction to enforce "not just what is legal but what is fair."[20]

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[1] 2017 SCC 39 [Wilson].[ps2id id='1' target='/]
[2] R.S.C., 1985 c. C-44, s. 241; Wilson at para 4.[ps2id id='2' target='/]
[3] Wilson at para 6.[ps2id id='3' target='/]
[4] Wilson at para 9.[ps2id id='4' target='/]
[5] Wilson at para 10.[ps2id id='5' target='/]
[6] Wilson at paras 11-12.[ps2id id='6' target='/]
[7] Wilson at para 13.[ps2id id='7' target='/]
[8] Wilson at para 14.[ps2id id='8' target='/]

[9] Wilson at para 21.[ps2id id='9' target='/]
[10] (1998), 43 BLR (2d) 27 (ONCA)[ps2id id='10' target='/]
[11] Wilson at para 30.[ps2id id='11' target='/]
[12] Wilson at para 31.[ps2id id='12' target='/]
[13] Wilson at para 37, citing to Budd and “Oppression and Related Remedies” by Markus Koehnen (now Mr. Justice Koehnen), Toronto: Thomson/Carswell, 2004.[ps2id id='13' target='/]
[14] Wilson at paras 11, 61 and 62[ps2id id='14' target='/]
[15] Wilson at paras 50 and 53.[ps2id id='15' target='/]
[16] Wilson at para 53.[ps2id id='16' target='/]
[17] Wilson at para 54.[ps2id id='17' target='/]
[18] Wilson at para 55.[ps2id id='18' target='/]
[19] Wilson at para 31.[ps2id id='19' target='/]
[20] Wilson at para 23.[ps2id id='20' target='/]

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.