MINDEN GROSS LLP

Fall 2015

TOPICS:

the Role of the Chair

Introduction

Every corporation is operated differently and each may take on a life of its own. However, there are several elements all corporations have in common; these include the need to have officers, directors, shareholders or members and a chair for the meetings of its shareholders/members and directors. Corporations must all take positive action to comply with corporate governance in order to remain legally compliant.

Who is Entitled to Chair Meetings and Role of Chair

For meetings of directors and shareholders/members to be considered properly constituted, a corporation must appoint a chairperson. The courts have heeded this need and in one Australian case in particular, the judge started as follows:

> It is an indispensable part of any meeting that a chairman should be appointed and should occupy the chair. In the absence of some person (by whatever title he or she may be described) exercising procedural control over a meeting, the meeting is unable to proceed to business.[1]

Most by-laws provide that the chair of the board, if present and willing, will preside at meetings of the board. In the absence or refusal of the chair to preside, or to continue presiding, the president shall preside, unless the constitution provides otherwise. If no such provision exists, a remaining quorum of the board may elect a new chair from among the directors.[2]

The Chair Need Not be a Lawyer

In the B.C. case of *Hastman v. St. Elias Mines Ltd.*,[3] the applicants sought to set aside a shareholders meeting. They alleged the chair was not a lawyer and essentially was not qualified to rule on the validity of proxies. The Court rejected this argument and stated:

> …from a policy point of view, it would not be desirable to restrict the group of people who could be chairs of a corporation to lawyers. The authorities are replete with situations where chairs of companies are not lawyers and I was

1 *Colorade Construction Pry. Ltd. v Platus* (1966), 2 N.S.W.R. 598 at 600.
2 *Klein v. James* (1986), 36 B.L.R. 42 (B.C.S.C.) affirmed (1987), 37 B.L.R. (XXV1) (B.C.C.A.).
3 2013 B.C.S.C. 1069.

> not given any authorities to contradict that history.[4]

The chair should, however, consider engaging counsel to advise on issues, especially if those issues may become contentious at the meeting or afterwards.

Authority of the Chair

The chair must not act to frustrate the expression of the wishes of the meeting by leaving the chair, refusing to put proper motions to a vote, acting in an oppressive manner to end the discussion or refusing to have votes counted. In *American Aberdeen-Angus Breeders' Ass'n v. Fullerton*,[5] it was stated:

> The right of the majority of the members to control the action of the meeting cannot be questioned. A presiding officer cannot arbitrarily defeat the will of the majority by refusing to entertain or put motions, by wrongfully declaring the result of a vote or by refusing to permit the expression by the majority of its will. He is the representative of the body over which he presides. His will is not binding on it, but its will, legally expressed by a majority of its members is binding.

A Court may set aside a meeting because a chair did not preside at the meeting in a proper manner and allow questions to be put or to allow questions to be answered and if the conduct was such as to affect the outcome of the meeting itself.[6]

The Delaware decision in *Portnoy v. Cryo-Cell International, Inc.*[7] is an example where the Court ordered a new election with a new chair at the expense of the management due to the improper behavior of the Chair in trying to maintain control of the board at a shareholders

4 *Ibid* at para 139.
5 (1927), 156 N.E. 314 (Ill. Sup. Ct).
6 *See Re: Canadian Pacific Ltd.* (1997), 30 B.L.R. (2d) 297 (Ont. Ct. Gen. Div.).
7 (2008), 940 A.2d 43 (Del.Ch.).

meeting. The Chair (Mercedes Walton) and the management groups devised a plan to buy up stock and bolster their position in a proxy contest. Going into the annual meeting, the Chair sensed defeat. Walton did not want to close the polls and count the vote when the scheduled presentations were over, so she had members of her management team make long, unscheduled presentations to give her side more time to gather votes and ensure that they had locked in two key blocks. She overruled motions to close the polls. Even after filibusters, Walton still had doubt that the Management Slate would prevail if the vote was counted and the meeting was concluded.

At around 2:00 p.m., Walton declared a very late lunch break, supposedly in response to a request made much earlier. In fact, Walton called the break so that she would have more time to seek votes and so that she could confirm that the major blockholders had switched their votes. Only after confirming the switches did Walton resume the meeting at approximately 4:45 p.m., declare the polls closed, and have the vote counted.

The judge had harsh words to say about the Chair's behavior and found a serious breach of fiduciary duty that tainted the election of directors. The Court ordered a new meeting with a new Chair at management's cost.

The chair must enforce designated rules of order, must preserve and maintain order, and do all things necessary for the proper conduct of the meeting. The chair may call the speakers, regulate the length of the speeches, deal with points of order, and control the arrangements for any vote that may be taken. He or she may judiciously attempt to regulate interruptions from the floor. The chair must combine fairness with tact.

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Casting Vote of the Chair

At common law, the chair does not have a second or casting vote[8] if directors are equally divided on a question. There is no provision for a casting vote in the corporate statutes and if the chair is to have a casting vote, it is to be provided for in the by-laws. If there is provision for the Chair to have a casting vote it is meant to be used to remedy occasional tie votes,[9] not

8 *Nell v. Longbottom*, [1894] 1 Q.B. 767 (Q.B.D.).
9 *Re: Citizen's Coal v. Forwarding Co.*, [1927] 4 D.L.R. 275 (Ont. Co. Ct.).

to deal with a continuous and settled deadlock condition.[10] Some people think the chair only has a vote if the chair has a **casting** vote. This assertion is wrong. A chair must act in good faith in casting a tie-breaking vote, but is not compelled to cast the tie-breaking vote.

If it is intended that consensus be achieved among the directors, the occurrence of a tie vote shows that obviously consensus has not been achieved. Those who are of the consensus view would argue that the chair should not have a casting vote or exercise a casting vote in order to break a deadlock.

Appeals of a Chair's Rulings

The rulings of the chair related to procedural matters may be appealed to the meeting. The best practice is for the person acting as chair of the meeting to vacate the chair while a vote is taken and the appeal of such procedural rulings by the Chair should not involve speeches. A majority vote is required to vary or reverse the Chair's ruling.

There is a presumption that the Chair's decision is a correct one. There have been several pronouncements in cases to this effect. For example, in the *Re Indian Zoedone Co.* case in the English Court of Appeal, Cotton L.J. stated:

> Whether the objection depends on the form of the document or on the general point of law, the Court can decide, and is bound to decide, when the question comes before it, whether the decision of the chairman was right or wrong; but until the contrary is shown his decision must be held to be right, that is to say, the Court must decide the questions between the parties, but not until those who object to his decision satisfy the Court before whom the question comes that his decision was wrong.

Removal of the Chair

A chair appointed by the meeting can be replaced by the meeting. If the by-law provides who is to chair, a resolution cannot be passed to remove that person and appoint another as chair. All one can do is to bring a motion in Court to order a new meeting.

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10 Re: *Daniels and Fielder* (1988), 65. O.R. (2d) 629 (Ont. H.C.).

THE DE FACTO DIRECTOR

Introduction

No matter what a person may call himself or herself, if he or she acts as a director, the person may be deemed to be a director and is called a *de facto* director. As such, the person may be on the hook together with the other directors for any liability that may arise from their role.

By definition in both the *Canada Business Corporations Act* ("CBCA") and the *Ontario Business Corporations Act* ("OBCA") (ss. 2(1) and 1(1), respectively), a director includes any person occupying or acting in the position of director, by whatever name it is called.

What is a *De Facto* Director?

De facto directors typically fall into one of the following three categories: (i) persons who are properly elected but lack some qualification under the relevant company law that disqualifies them from legally being directors; (ii) former directors whose term of office has expired but who have continued to act as directors; or (iii) those who simply assume the role of director without any pretense of legal qualification. It is the latter situation that this article addresses.

In determining whether an officer or an employee is a *de facto* director, the courts have considered, among other factors, whether outsiders would assume the person was a director, whether representations were made by the person, and whether the person participated in directorial acts, such as signing documents as a director or sitting on the board of directors.

One of the most often-cited definitions of a *de facto* director is in the case of *Re Hydrodam (Corby) Ltd.*, [1994] 2 B.C.L.C. 180, where Millet J stated that:

> A *de facto* director is a person who assumes to act as a director. He is held out as a director by the company, and claims and purports to be a director, although never actually or validly appointed as such. To establish that a person was a *de facto* director of a company it is necessary to plead and prove that he undertook functions in relation to the company which could properly be discharged only by a director.

The person must have assumed the status and functions of a company director and exercised real influence in the corporate governance of the company. More specifically, the person must have participated in directing the affairs of the company on an equal footing with the other director(s) as part of the board and not in a subordinate role.

The Test for a *De Facto* Director

The test for *de facto* directors is one established by jurisprudence. While it is not statutorily mandated, this does not take away from the importance of understanding one's roles and responsibilities when the person is acting in such a manner that may deem the person to be a director of a corporation.

The test used to establish whether a person acted as a *de facto* director looks at whether the individual in question had influence and control over the management of the affairs of the corporation.

The Courts have recently had the opportunity to address the test for *de facto* directors. In the English case of *Elsworth Ethanol v. Ensus*, [2014] EWHC 99, the Court confirmed that there is no single test, but listed some of the non-exhaustive factors that should be considered in order to determine if an individual is a *de facto* director:

1. Whether an individual (the putative *de facto* director) was acting with one or more "true directors" on an equal footing in directing the affairs of the corporation;
2. Whether there was a holding out by the company of the individual as a director;
3. Whether the individual used the title of director; and
4. Whether the individual was part of the corporate governing structure, being the system by which the company is directed and controlled.

The Court emphasized in this case that the first factor is particularly important, that is, whether the individual acted on equal footing to manage the affairs of the corporation. However, the Court also found that if it is unclear whether the person is a *de facto* director, the benefit of the doubt should be given. It was held that directorship should not be inferred unless there is clear evidence that the individual had assumed the role.

Deeming Statutory Provision

As noted above, corporate statutes define a director as "a person occupying the position of director of a corporation by whatever name called." While there is no statutory provision that dictates when an individual will be held to be a *de facto* director, it is evident from this definition that no matter what name an individual may give to his or her position within a corporation, if he or she acts as a director, he or she will be deemed to be one.

There is one other provision that deems an individual to have assumed that role. This provision can be found in s. 115(4) of the OBCA and s. 109(4) of the CBCA. These provisions provide that if all the directors of a corporation have resigned or have been removed from office, the law will infer that "any person who manages or supervises the management of the business and affairs of the corporation shall be deemed to be a director."

For example, in the case of *Gerald Grupp v. R.*, 2014 TCC 184, the Tax Court of Canada found that the appellant remained a *de facto* director until the business closed in 2010, even

though he had resigned from the role in 1995. There were no other directors in the corporation and no one was appointed to replace the appellant after his resignation. Furthermore, he remained active in the business, managed the affairs of the corporation, and did not inform third parties that he was no longer a director. Interestingly, the term "director" is not defined as such in the taxation statutes but, as noted, the Courts find a way to make a *de facto* director liable.

Liabilities of a *De Facto* Director

If an individual is found to be a *de facto* director, he or she will be jointly and individually liable with the other directors for any liability that may arise while the *de facto* director acted in such a role. However, liabilities of *de facto* directors can also extend to more than one corporation such as the parent companies and their subsidiaries. In this context, the Courts will look to examine whether corporate formalities between the parent and subsidiary have been properly observed and whether the chain of actual decision-making matches the legal decision-making chain in the corporate structure. Where corporate formalities are not properly observed, a director or *de facto* director could be liable for both the parent's and subsidiary's liabilities.

The impact of *de facto* directors' liability is widespread and one could be held personally liable for matters such as employee

wages, withholding taxes that were not remitted to the government, improperly paid dividends, environmental liability facing the corporation, product liability and outstanding fines.

Conclusion

Individuals that get involved in the management and affairs of a corporation should be very cautious about the level of their involvement if they do not wish to assume the possible liability connected with being a director of the corporation. While in most situations there may not be any liability that arises from acting as a director, or being deemed to act as such, it is important to keep in mind that an individual's actions may result in them being deemed a *de facto* director. As such, all individuals that act in a manner which may deem them to be directors should ensure that they get adequately informed about the affairs of the corporation so as to properly protect themselves against possible liability.

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Firm News

Minden Gross welcomes **Risa Sokoloff** and **Melissa Muskat** to the firm to practice in the areas of municipal, property assessment and taxation law.

Welcome to **Jane Yoo** as an Associate in our Litigation Group. Jane articled with Minden Gross LLP from 2014 to 2015.

Minden Gross LLP is again ranked in the **Top 10 Ontario Regional Law Firms** by *Canadian Lawyer* magazine. Lawyers, in-house counsel, and clients from across Canada vote on their top full-service, regional firms in Ontario.

Professional Notes

Minden Gross LLP is pleased to announce that **Howard Black** (Trusts and Estates); **Michael Horowitz** (Commercial Leasing); **Stephen Messinger** (Commercial Leasing); **Adam Perzow** (Commercial Leasing); **Stephen Posen** (Commercial Leasing); **Reuben Rosenblatt**, QC, LSM (Real Estate) have been recognized by their peers in the 2016 edition of *The Best Lawyers in Canada*.

Catherine Francis, with Shelley Babin from Ontario Power Generation, presented to the Association of Corporate Counsel on "Everything In-House Counsel Needs to Know About Privilege and Confidentiality" on October 6.

Matt Maurer spoke to REP TV on the law of buying and selling tenanted property on October 14 and published "How to protect yourself against provincial offences" in Canadian Real Estate Wealth on October 7. He talked about home inspections on Canadian Real Estate Wealth's CREW TV on October 6. He also published his blog on Slaw.ca, including "Claims for Damage Caused by Tenants Fall Under Exclusive Jurisdiction of Landlord Board."

Joan Jung presented "Creating and Maintaining or Retaining CCPC Status" on October 27 at the Ontario Tax Conference. Minden Gross LLP was a sponsor for the event. She published "Proposed Review of Ontario Business Legislation" in the October edition of *STEP Inside*. Joan was also part of a panel on "Drafting Fundamentals (Including Drafting for the Changing Management Issues of Modern Partnerships)" at The Annotated Partnership Agreement 2015 seminar on September 29.

Irvin Schein published "When Can an Employment Agreement be Voided for Duress?" and "When Can A Ski Resort Be Liable For A Skier's Injuries?" at irvinschein.com.

The **Commercial Leasing Group** participated in the ICSC Canadian Convention on October 6-7, where **Stephen Messinger** was on the Program Committee and presented a workshop on "Special Interest Groups". They also attended RealLeasing 2015 where **Stephen Posen** moderated a panel on "Good Faith and Other Recent Case Law: Implications for Asset Management Strategies and Lease Negotiation" and Stephen Messinger moderated a panel on "Negotiating Strategies for Today's Market: How to Understand the Deal, Resolve Key Issues, and Close the Transaction" on September 30. The two were also listed in the *Lexpert Special Edition on Infrastructure*.

Reuben Rosenblatt, QC, LSM, and **Stephen Messinger** have been recommended by their peers in *Who's Who Legal - Real Estate 2015*.

Stephen Messinger co-presented "Whose Money Is It Anyway? Tenant Improvement Allowance Payment Conditions and Securing Payment" at the ICSC US Shopping Center Law Conference on October 29 and taught "The Law and Its Application: Working with Your Attorney" at the John T. Riordan School in Miami, FL on September 28.

Samantha Prasad was a panelist at the Every Family's Business event with RBC and Richter and our **Tax Group** on October 5. She also spoke on Attribution Rules with TD Bank on September 30. She published three articles on *The Fund Library*, including "Family transfers can have tax effects" on September 22 and three articles in *The TaxLetter* including August's "Tax traps for shareholders of family-owned businesses".

David Ullmann was quoted in "Some creditors find cold comfort in Yukon Zinc's payback plan" in *Yukon News* on September 4.

Michael Goldberg was a co-presenter on "21-Year Trust Unwinds: Strategies and Related Issues" on September 18 at the CIDEL Provence Conference in Seillans, France. He also hosted the first session of Tax Talk: Year 3 on September 16.

Brian Temins was mentioned in the article "Grassroots M&A: Lawn care not just a PE summer pastime" in *The Deal* on August 5.

Eric Hoffstein published "Recent Decisions Add Pieces to the Puzzle of Joint Ownership" in October's *STEP Connection*. His co-presentation "The Use and Abuse of Exculpatory Clauses" was rebroadcast at an American Bar Association webinar on October 20. Eric co-presented "Practice Skill Challenges" at the CBA Will, Estate and Trust Fundamentals for Estate Practitioners program on October 17. He presented "The Role of the Estate Trustee

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During Litigation" at the 18th Annual LSUC Estates and Trusts Summit on October 7-8. He co-chaired the OBA's The Family Business: Administration and Litigation of Trusts and Estates Holding Business Assets program where he presented "How to Navigate Disputes Involving Trust-Controlled Businesses" on September 29. He also presented "Construction Lien Act 101" at the Association of Architectural Technologists of Ontario's Lecture Series on September 28.

Congratulations to **Christopher Grisdale**, student-at-law, who accepted an award at the 15th Annual UFCW Canada - AWA Awards Dinner on October 27 for his work on the *2015 National Report on the Status of Migrant Workers in Canada*.