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DIRECTORS' FIDUCIARY DUTIES TO SHAREHOLDERS

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*In fulfillment of part of the requirements
of the LL.M. degree.*



M. Lee Stratton, Ottawa, Canada, 1993



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ABSTRACT

Since the 1902 decision of Percival v. Wright¹, Canadian common law has provided that directors generally have no fiduciary duties to shareholders. Shareholders have continued to assert that directors have such duties, however, undoubtedly spurred on by the conviction that directors' exclusive access to corporate information and the protective roles they not infrequently assume on behalf of shareholders merit special superintendence by the courts. Moreover, shareholders have been attracted by the allure of the rigorously restitutionary remedies imposed on fiduciaries.

Cases brought to the courts by shareholders seeking the imposition of fiduciary duties on directors have yielded disparate results. The state of this area of the law is unsatisfactory. Some courts continue to display vestiges of the solicitude for directors and a disregard for shareholders' interests expressed long ago in Percival v. Wright. Even when the decision in Percival v. Wright is overcome, Canadian courts seem unclear about the appropriate rationale for imposing fiduciary obligations on directors in favour of shareholders. Most courts consider a specific type of personal relationship between the director and the shareholder a prerequisite to the recognition of such duties. For example, the relationship between an experienced director and an unsophisticated shareholder might be viewed as a fiduciary relationship. Other courts consider the materiality of the events in which a fiduciary duty is claimed to have been breached a prerequisite to the imposition of certain fiduciary duties such as the obligation to disclose such events and material facts. For example, the sale of all of the shares of a business may be viewed as a sufficiently important event for all parties that a high level of conduct can be expected of directors in favour of shareholders. To these rationales for imposing fiduciary duties on directors in favour of shareholders we would add the observation that directors have wide knowledge about the corporation, broad powers of inquiry within the corporation, and broad powers to implement their plans within the corporation. In the absence of an unanimous shareholder agreement, shareholders have no access to such knowledge and

¹ [1902] 2 Ch 421.

cannot control the exercise of such powers. Possession of such knowledge and powers should entail responsibility not only to the corporation but to the owners of the corporation in respect of their use.

The idea that directors have fiduciary duties to shareholders has not had much currency in Canada. It has been buffeted by the strongly held view, reflected in Percival v. Wright, that directors' duties are solely to the corporation. The idea has, however, been rekindled periodically by developments in the law. Such developments include the new securities laws of the 1960s, the decisions of the New Zealand courts in Coleman et al. v. Myers et al.² and, more recently, the Supreme Court of Canada decision in LAC Minerals Ltd. v. International Corona Resources Ltd.³ The idea of directors' fiduciary duties to shareholders is, however, now being assailed by the existence of the statutory oppression remedy in the *Canada Business Corporations Act* (hereinafter referred to as the "CBCA")⁴ and the CBCA cognate statutes of several provinces.

The state of the law of directors' duties to shareholders was of primary concern to the Committee on Securities Legislation, known as the Kimber Committee, appointed in 1963 by the Attorney General of Ontario. The Kimber Committee, charged with the responsibility to create the legal framework for a vibrant securities market, noted its dissatisfaction with the state of judge-made law and its concern that the courts could not escape from the precedential influence of Percival v. Wright. These observations, coupled with a concern for shareholder interests, were motivating factors for the Canadian securities law reforms of the 1960s. The crowning achievement of the Kimber Committee's work was the enactment of a new *Securities Act* in Ontario in 1966.⁵ These reforms were followed by

² [1977] 2 NZLR 225 (SC); [1977]2 NZLR 297 (CA).

³ (1989), 61 DLR (4th) 14 (SCC).

⁴ RSC 1985, c. C-44, s.241.

⁵ *Securities Act*, SO 1966, c.142.

corporate law reform in the 1960s and 1970s. Of particular importance in this process was the work of the federal Task Force on corporations law. The work of the Task Force led to the enactment of the CBCA in 1974.⁶ The CBCA was followed by the enactment of cognate statutes in several provinces and it shaped certain amendments to the *Business Corporations Act* in Ontario. Canadian securities and corporate law reform in the 1960s and 1970s resulted in the enactment of insider trading rules, take-over bid rules, the oppression remedy and other mechanisms for protecting shareholders.

The securities law reforms of the 1960s established an elaborate statutory regime of statutory directors' and insiders' fiduciary obligations to shareholders of certain corporations, particularly widely-held corporations. These reforms did not, however, provide all shareholders with protection from the actions of directors and other insiders. Perhaps the most notable limit to such protection is that insider trading and take-over bid activity relating to a "private company" is not governed by the take-over bid and insider trading rules. Directors and insiders of privately-held corporations are, therefore, free from any specific regulation in these situations. This disparity has been addressed in various ways. For example, all corporations, both widely-held and privately-held, are subject to the statutory oppression remedy introduced by the corporate law reforms of the 1970s as well as the remedy for trading on the basis of confidential information. Also, the 1985 British Columbia Court of Appeal decision in Dusik v. Newton⁷ demonstrated that some Canadian courts are willing to impose fiduciary obligations on directors to protect shareholder interests.

A review of recent cases in which fiduciary claims have been advanced by shareholders shows, however, that some Canadian courts are reluctant or unwilling to impose fiduciary duties on directors in favour of shareholders. The 1988 Ontario Court of Appeal decision in Bell et al. v. Source Data Control Ltd. et al. is a noteworthy example of this

⁶ *Canada Business Corporations Act*, SC 1974-75-76, c.33.

⁷ 62 BCLR 1.

approach.⁸ This judicial unwillingness to impose fiduciary standards on appropriate individuals in favour of minority shareholders is a strong feature of some of the Canadian extra-statutory corporate governance jurisprudence today.

Some American jurisprudence, the New Zealand case of Coleman v. Myers and its Canadian progeny, cases such as Dusik v. Newton, together with the recent Supreme Court of Canada decision in LAC Minerals Ltd. v. International Corona Resources Ltd. indicate that a re-examination of the Canadian law of directors' fiduciary duties to shareholders would be useful. This examination commences with a return to the origin of the debate concerning directors' fiduciary duties to shareholders, the case of Percival v. Wright. The manner in which the problems raised by Percival v. Wright have been addressed by securities and corporate law reformers, is then considered.

Cases in which shareholders have made claims of fiduciary duty against directors since the law reforms of the 1960s and 1970s are examined. The law reformers expected that the courts would develop the law of fiduciary relations within the corporation. Moreover, the nature of securities law reforms confronted the courts with the previously noted gulf between the statutory fiduciary obligations imposed on directors and insiders of widely-held corporations and the lack of such obligations in private companies. This review of judicial decisions begins with an examination of the compulsory acquisition cases which preceded the statutory take-over bid reforms. These cases arise from facts which would constitute take-over bids under the statutory reforms of the 1960s. In these cases, we see a very limited attempt by the judiciary to impose fiduciary obligations of good faith and candour in favour of minority shareholders. The courts' sense of commercial morality seems to have been stirred in these cases, a morality engendered by the arbitrary expropriation permitted by the statutory compulsory acquisition provisions. An examination of latter day cases involving claims of fiduciary duty shows that the decisions are sprinkled with references to commercial morality. Despite this moral impetus, the courts seem unwilling to venture beyond the perceived

⁸ 40 BLR 10, 66 OR (2d) 78.

constraints of the corporations statutes. This unwillingness, coupled with the courts' inability to articulate a uniform rationale for imposing fiduciary duties on directors in favour of shareholders contribute to the unsatisfactory state of the law.

CHAPTER 1

INTRODUCTION

The Canadian law of directors' fiduciary duties to shareholders is in an unsatisfactory state. Some of our courts continue to display vestiges of the solicitude for directors and disregard for shareholders' interests expressed long ago in Percival v. Wright¹, a decision which has been taken to stand for the proposition that directors are not in a fiduciary relationship with shareholders. Where Percival v. Wright is overcome, our courts seem unclear about the appropriate rationale for imposing fiduciary obligations on directors in favour of shareholders. Most courts consider a specific type of personal relationship between the director and the shareholder a prerequisite to the recognition of such duties. The particular features of such a relationship have not been definitively stated by the courts, although dependence and vulnerability on the part of the shareholder coupled with power and discretion on the part of the director are particularly significant. Other courts consider the materiality of the events in which a fiduciary duty is claimed to have been breached a prerequisite to the imposition of certain fiduciary duties such as the obligation to disclose such events and material facts. Thus, some courts consider the relationship between a particular director and shareholder while other courts consider factors external to that relationship. Even where the appropriate approach is not in issue, however, the cases do not yield fully predictable or satisfactory results.

The lack of a sound theoretical underpinning and of predictable results in the Canadian cases involving claims of directors' fiduciary duties to shareholders is not surprising. There have not been many reported Canadian cases involving such claims. The idea that directors have fiduciary duties to shareholders has not had much currency in Canada. It has

¹ [1902] 2 Ch 421. Percival v. Wright is discussed in Chapter 2.

been buffeted by the strongly held view, reflected in Percival v. Wright, that directors' duties are solely to the corporation. The idea has, therefore, sputtered along. Occasionally it has been rekindled by developments in the law such as the new securities laws of the 1960s, the decisions of the New Zealand courts in Coleman et al. v. Myers et al.² and, more recently, the Supreme Court of Canada decision in LAC Minerals Ltd. v. International Corona Resources Ltd.³ The idea of directors' fiduciary duties to shareholders is, however, now being assailed by the existence of the statutory oppression remedy in the *Canada Business Corporations Act* (hereinafter referred to as the "CBCA")⁴ and the CBCA cognate statutes of several provinces.

The Canadian law of directors' fiduciary duties to shareholders has been in an unsatisfactory state for many years. The state of the law was of primary concern to the Committee on Securities Legislation (hereinafter referred to as the "Kimber Committee") appointed in 1963 by the Attorney General of Ontario. The Kimber Committee, charged with the responsibility of creating the legal framework for a vibrant securities market, noted its dissatisfaction with the state of judge-made law and its concern that the courts could not escape from the precedential influence of Percival v. Wright. These observations, coupled with a concern for shareholder interests, were motivating factors for the Canadian securities law reforms of the 1960s. The crowning achievement of the Kimber Committee's work was the enactment of a new *Securities Act* in Ontario (hereinafter referred to as the "OSA") in 1966.⁵ These reforms were followed by corporate law reform in the 1960s and 1970s. Of particular importance in this process was the work of the federal Task Force on corporations law

² [1977] 2 NZLR 225 (SC); [1977]2 NZLR 297 (CA).

³ (1989), 61 DLR (4th) 14 (SCC).

⁴ RSC 1985, c. C-44, s.241.

⁵ Securities Act, SO 1966, c.142. Section references to the OSA are to the Securities Act, RSO 1990, c.S.5.

(hereinafter referred to as the "Task Force"). Its work led to the enactment of the CBCA in 1974.⁶ The CBCA was followed by the enactment of cognate statutes in several provinces and it shaped certain amendments to the *Business Corporations Act* in Ontario (hereinafter referred to as the "OBCA").⁷ The American securities lawyer, Louis Loss, captured the temper of this period of law reform when he told his English audience, "[T]he critical complex of problems today on both sides of the ocean is that conjured up by the phrases 'insider trading' and 'the fiduciary concept' as applied to management and controlling shareholders."⁸ The work of the Canadian law reformers led to the enactment of insider trading rules, take-over bid rules, the oppression remedy and other mechanisms for protecting shareholders.

An elaborate statutory regime of directors' and insiders' fiduciary obligations to shareholders of certain corporations, particularly widely-held corporations, was established by securities law reformers in the 1960s. There were and remain, however, limits to this regime which regulates insider trading and take-over bids. Perhaps the most notable of these limits is that insider trading and take-over bid activity relating to a "private company", as that term is defined in the OSA,⁹ is not governed by these rules. Directors and insiders of privately-held corporations are, therefore, free from any specific regulation in these situations. Thus, the securities law reforms of the 1960s created a two-fold approach to the law of directors' and insiders' fiduciary duties to shareholders. Essentially, a gulf was created between widely-held and closely-held corporations. This gulf has been made clearer by the bold initiatives of the

⁶ Canada Business Corporations Act, SC 1974-75-76, c.33. Section references to the CBCA are to the Canada Business Corporations Act, RSC 1985, c. C-44.

⁷ Business Corporations Act, SO 1982, c.4. Section references to the OBCA are to the Business Corporations Act, RSO 1990, c. B.16.

⁸ L.Loss, "The Fiduciary Concept as Applied to Trading by Corporate 'Insiders' in the United States", 33 Mod L Rev 34 at 34.

⁹ OSA, s.1(1) 32.

Ontario Securities Commission (hereinafter referred to as the "OSC") to implement fiduciary-based policies in the context of a wide variety of transactions in widely-held corporations.¹⁰

The gulf can be bridged. Both corporations where directors' conduct is heavily regulated by securities legislation and those where it is not are subject to the statutory oppression remedy introduced by the corporate law reforms of the 1970s as well as the remedy for trading on the basis of confidential information. Moreover, the 1985 British Columbia Court of Appeal decision in Dusik v. Newton¹¹ shows that some Canadian courts are willing to impose fiduciary obligations on directors to protect shareholder interests. This decision demonstrates the ability of the courts to overcome the paucity of regulation in situations analogous to take-over bids and to protect shareholder interests on a basis other than statutory shareholder remedies such as the oppression remedy.

As our review of recent cases in which fiduciary claims have been advanced by shareholders will show, however, some Canadian courts are reluctant or unwilling to impose fiduciary duties on directors in favour of shareholders. The 1988 Ontario Court of Appeal decision in Bell et al. v. Source Data Control Ltd. et al. is a noteworthy example of this approach.¹² There is a history to this judicial predilection. It was only twenty years ago that an English court accepted that directors had fiduciary duties to shareholders in take-over

¹⁰ See P. Anisman, "The Commission as Protector of Minority Shareholders" in Securities Law in the Modern Financial Marketplace: Special Lectures of the Law Society of Upper Canada-1989 (Don Mills: DeBoo, 1989), p.451, especially pp. 463-475 and pp. 492-493. J.G. MacIntosh, J. Holmes and S. Thompson have argued in "The Puzzle of Shareholder Fiduciary Duties" (1991), 19 CBLJ 86 at pp. 112-119 that the work of securities regulators has significantly retarded the development of shareholder fiduciary duties in the common law of corporations.

¹¹ 62 BCLR 1.

¹² 40 BLR 10, 66 OR (2d) 78.

situations in which the purchaser could avail itself of a statutory right to acquire a dissenting shareholder's shares.¹³ Close to forty years of Canadian jurisprudence under identical compulsory acquisition provisions yielded only a vague statement of fiduciary obligations in the reasons of Rand J. in the Supreme Court of Canada decision in Rathie v. Montreal Trust Co. and British Columbia Pulp & Paper Co.¹⁴ This judicial unwillingness to impose fiduciary standards on the appropriate individuals in favour of minority shareholders is a strong feature of some of the Canadian extra-statutory corporate governance jurisprudence today.

In contrast to the divergent approaches, uncertain principles and judicial antipathy which characterize the Canadian law of directors' fiduciary duties to shareholders, courts in the United States have formulated strong, bold principles in this area of the law. A notable recent example of the American jurisprudence is the Delaware case of Smith et al. v. Van Gorkom et al.¹⁵ The following passages from this decision illustrate the fiduciary duties that some American courts impose on directors in favour of shareholders:

In carrying out their managerial roles, directors are charged with an unyielding fiduciary duty to the corporation and its shareholders.... A director's duty to inform himself in preparation for a decision derives from the fiduciary capacity in which he serves the corporation and its stockholders.¹⁶

[Where stockholder ratification of a matter is sought,] directors owe to their stockholders a fiduciary duty to

¹³ Gething et al. v. Kilner et al., [1972] 1 All ER 1166, [1972] 1 WLR 337 (Ch).

¹⁴ [1953] 2 SCR 204, [1953] 4 DLR 289.

¹⁵ (1985), 488 A 2d 858 (Del Sup).

¹⁶ Ibid, 872.

disclose all facts germane to the transaction at issue in an atmosphere of complete candor.¹⁷

Similarly, but in the Anglo-Canadian tradition, the seminal decisions of the New Zealand Supreme Court and the New Zealand Court of Appeal in Coleman et al. v. Myers et al. boldly articulated and applied the law to impose fiduciary duties on two directors of a closely-held family corporation of the corporation's shareholders.¹⁸

Smith v. Van Gorkom and Coleman v. Myers indicate that a re-examination of directors' fiduciary duties to shareholders would be useful.¹⁹ The proposition that fiduciary duties to shareholders emanate from majority or dominant shareholders has already been considered by law reformers,²⁰ legal scholars,²¹ and the courts.²² Another approach to corporate governance matters has been taken by Bybelezer who has attempted to shift the focus of the debate by suggesting that the role of directors should be "to mediate objectively among the various inputs of the corporation", especially equity interests and management. Bybelezer

¹⁷ Ibid, 890.

¹⁸ Footnote 2. As is discussed in Chapter 5, the New Zealand courts, like the Canadian courts, are not clear about whether material facts or a particular type of director-shareholder relationship is a prerequisite to the imposition of fiduciary duties on directors.

¹⁹ The Smith v. Van Gorkom decision was instrumental in causing the Alberta Institute of Law Research and Reform to undertake its study entitled Corporate Directors' Liability (Edmonton: Institute of Law Research and Reform, 1989).

²⁰ See Canada, Proposals for a New Business Corporations Law for Canada (Ottawa: Information Canada, 1971) (hereinafter referred to as the "Dickerson Report"), paragraph 477 at pp.158-159, and paragraph 487 at pp.164-165.

²¹ See J.G. MacIntosh, "Corporations" in Fiduciary Duties: Special Lectures of the Law Society of Upper Canada - 1990 (Don Mills: De Boo, 1990) and J.G. MacIntosh et al., "The Puzzle of Shareholder Fiduciary Duties", footnote 8.

²² See Brant Investments Ltd. et al. v. KeepRite Inc. et al. (1991), 3 OR (3d) (Ont CA).

believes that rules extending greater protection to shareholders than to the corporation's management should be reconsidered.²³

In this paper, we return to the origin of the debate concerning directors' fiduciary duties to shareholders, the case of Percival v. Wright. We attempt to focus on the development of directors' fiduciary duties to shareholders rather than on the fiduciary duties owed by the broader array of corporate insiders to shareholders. There are limits to this approach since the triumvirate of corporate insiders - dominant shareholders, directors and officers - is linked. Directors are elected by shareholders, primarily dominant shareholders, and directors appoint officers. Moreover, a majority shareholder often serves as a director, perhaps the sole director of a private company, and as a senior officer. Once elected, however, directors are invested with statutory powers and obligations which distinguish directors from dominant shareholders and officers.

Our review takes us through the securities and corporate law reforms of the 1960s and 1970s. Those reforms both linked directors to and distinguished them from other corporate insiders. Corporate insiders were treated identically in respect of insider trading rules, for example, while directors alone were given special responsibilities to shareholders, such as the obligation to send a directors' circular to shareholders,²⁴ when their corporations became

²³ H.M. Bybelezer, "The 'Corporate Governance' Debate and Modern Theory of the Firm: Some Lessons" in L. Sazar, ed. Corporate Structure, Finance and Operations, 5th ed. (Toronto: Carswell, 1988), p.53 at p.78.

²⁴ CBCA, s. 201; OSA, s. 99. The seriousness of these responsibilities can be discerned from a review of the unsuccessful take-over bid by Campeau Corporation of Royal Trustco Ltd. in 1980 and the extensive litigation which surrounded that take-over bid. In respect to the directors' circular see Royal Trustco Ltd. et al., Re, (1981), 2 OSCB 322C (Ont Sec Comm); appealed sub nom Royal Trustco Ltd. et al. and Ontario Securities Commission, Re, (1983), 42 OR (2d) 147, 21 BLR 236 (Div Ct); and Sparling et al. v. Royal Trustco Ltd. et al. (1983), 143 DLR (3d) 112, 21 BLR 97, 32 CPC 291 (HCJ); (1984), 45 OR (2d) 484, 1 OAC 279, 6 DLR (4th) 682 (Ont CA); [1986]2 SCR 537 (SCC).

the target of a take-over bid. We examine the context in which the problem of shareholder rights was considered by securities law reformers and the extent to which the securities and corporate law reforms of the 1960s and 1970s resolved such problems through the imposition of statutory fiduciary duties on directors and other corporate insiders.

From our examination of the problems raised by Percival v. Wright and the manner in which these problems were addressed by securities and corporate law reformers, we move to the courts. The law reformers expected that the courts would develop the law of fiduciary relations within the corporation. Moreover, the nature of securities law reforms confronted the courts with the previously noted gulf between the statutory fiduciary obligations imposed on directors and insiders of widely-held corporations and the lack of such obligations in private companies. Our review of judicial decisions begins with an examination of the compulsory acquisition cases which preceded the statutory take-over bid reforms. These cases arise from facts which would constitute take-over bids under the statutory reforms of the 1960s. In these cases, we see a very limited attempt by the judiciary to impose fiduciary obligations of good faith and candour in favour of minority shareholders. The courts' sense of commercial morality seems to have been stirred in these cases, a morality engendered by the arbitrary expropriation permitted by the compulsory acquisition provisions. While this does not appear to be one of the "guiding principles of corporate law morality" which Professor Cheffins urges students of corporate law "to ascertain with greater precision",²⁵ it is nonetheless a significant feature of the case law. As we shall see when we examine latter day cases involving claims of fiduciary duty, the decisions are sprinkled with references to commercial morality. This should not be surprising for, as John Howard has said, the fiduciary standard "is purely and simply a standard of moral duty based on conflicts of interest or duty that a director or officer can always

²⁵ B.R. Cheffins, "Law, Economics and Morality: Contracting Out of Corporate Law Fiduciary Duties" (1991), 19 CBLJ 28 at 47.

avoid."²⁶ As Professor Cheffins notes in his critique of Mr. Howard's views, "[Howard] asserts that all fiduciary cases, including those involving take-over bids, are resolved primarily on moral grounds."²⁷ Despite this moral impetus, the courts seem unwilling to venture beyond the perceived constraints of the corporations statutes.²⁸ This unwillingness, coupled with the courts' inability to articulate a uniform rationale for imposing fiduciary duties and fact situations in which the relevant actors frequently occupy the positions of director, majority shareholder and officer all at the same time, contribute to the unsatisfactory state of the law. In the Conclusion, we invoke the memory of the agenda set by Loss and other law reformers and consider afresh the extent to which fiduciary claims against directors may be successfully made by shareholders.

²⁶ J. Howard, "Fiduciary Relations in Corporate Law" (1991), 19 CBLJ 1, p.17.

²⁷ Cheffins, op. cit., p.45.

²⁸ I have particularly in mind the case of Brant Investments supra, footnote 21, in which McKinlay J.A. states that the existence of the statutory oppression remedy forecloses the need to consider claims of fiduciary duty in the corporate context. This constraint on the development of the law is noted by J.G. MacIntosh, J. Holmes and S. Thompson in "The Puzzle of Shareholder Fiduciary Duties", footnote 10, at pp. 130-134.

CHAPTER 2

DIRECTORS' FIDUCIARY DUTIES TO SHAREHOLDERS PRIOR TO LAW REFORM IN CANADA

Anglo-Canadian law governing directors' fiduciary duties to shareholders reached its nadir in 1902 with the decision in Percival v. Wright.¹ The decision has come to stand for the principle that directors are not in a fiduciary relationship with shareholders.² In this Chapter we review a few of the most significant Anglo-Canadian cases involving claims of fiduciary duty against directors prior to the Canadian securities and corporate law reforms of the 1960s and the 1970s. We also briefly review the development of this area of law in the United States because of the influence the American jurisprudence undoubtedly had on Canadian law reformers.

The three English cases reviewed show three different approaches to fiduciary claims made against directors. In Percival v. Wright, such a claim was made by shareholders and was rejected by the Court, in large part because of the directors' fiduciary duty to the corporation, but also probably because the shareholders did not seem to need protection. In Allen v. Hyatt³, the Privy Council considered a not uncommon fact situation in which directors assumed a role with shareholders, either as agents or trustees, which entailed fiduciary responsibilities. The Privy Council suggests in this decision that directors' powers are to be used in favour of both the corporation and its shareholders. In Regal (Hastings), Ltd. v.

¹ [1902] 2 Ch 421.

² An outline of the facts and a discussion of the case follows.

³ (1914), 17 DLR 7, 30 TLR 444 (PC).

Gulliver⁴ the directors were found to have breached their fiduciary duty to their corporation. Ironically, the shareholders at the time of the breach did not benefit from the imposition of fiduciary duties on the former directors as their shares had been sold and the new shareholders brought the action against the directors.

These cases show both the allure and the limitation of fiduciary claims. Breaches of relationships acknowledged to be fiduciary are rigorously dealt with by the courts by the imposition of stringent remedies, but only such relationships are so protected. Since Percival v. Wright, shareholders have sought such remedies when they have considered themselves injured by directors of their corporations. The courts have not, however, acknowledged shareholders to be a class of persons which is entitled to the benefit of fiduciary conduct from directors. At best, these early cases show that fiduciary claims could be made against directors in appropriate circumstances. Consideration of what constitutes such circumstances, at least in Anglo-Canadian jurisprudence, would only arise after the problems raised by Percival v. Wright were dealt with by securities and corporate law reformers in the 1960s and 1970s. Moreover, in cases like Regal (Hastings), Ltd., the law enriches uninjured persons, and, therefore, seems wrong. As we shall see, the American case law happily avoids these problems.

Percival v. Wright

This case, which helped to expose the poverty of minority shareholder rights, arose in the following circumstances.

⁴ [1942]1 All ER 378 (HL).

The Factual Background and Arguments

The plaintiffs sold their shares in a company to three of its directors. The plaintiffs subsequently sought to have the sale set aside on the basis that while they were negotiating for the sale of the shares, the directors did not disclose to the shareholders the fact that negotiations for the sale of the business were in progress. The shares of the company were held by few shareholders and were not traded on a stock exchange.

The judge formed the view that there had been no unfair dealing with the plaintiffs.⁵ This view was supported by plaintiffs' counsel's concession of the point.⁶ The court was also bolstered in this view, however, because the plaintiffs had "named the price" at which they were prepared to sell their shares and the chairman, on behalf of the purchasing directors, had agreed.⁷ The chairman did not participate in the valuation of the shares; nor did he seek to negotiate a lower price for the shares. The plaintiffs had set the price on the basis of a valuation which they had obtained from independent valuers some months before the sale. In fact, the plaintiffs "named the price" a second time when they had the valuation updated. They requested a marginally higher price per share on the basis of the updated valuation and the chairman agreed. The history of the negotiations on the matter of price prompted plaintiffs' counsel's further concession that there was no suggestion that the shares had been purchased at an undervalue.⁸ This concession precluded an award of common law damages and reinforced the judge's conclusion that there had been no unfair dealing.

⁵ Footnote 1, p. 426.

⁶ Ibid, p. 423.

⁷ Ibid, p. 427.

⁸ Ibid, p. 423.

Prior to and during the negotiations for the share purchase, the directors were negotiating with an individual to sell the company's business. Various prices were suggested by the prospective purchaser, all of which would have resulted in the company's holding liquid assets which, on a per share basis, were considerably higher than the price at which the plaintiffs sold their shares. These facts were not disclosed to the plaintiffs while they were negotiating the sale of their shares. No firm offer which the directors could place before the shareholders was made and, eventually, the negotiations were terminated without the sale of the company's business. The judge concluded that the directors never intended to sell.

Since a remedy for common law damages based on the value of the shares seemed unavailable, the plaintiffs suggested the remedy of rescission to the judge. In support of such a remedy, plaintiffs' counsel submitted that the directors had a fiduciary duty to the shareholders which had been breached. He argued that although directors purchasing shares do not have to disclose "information acquired in the ordinary course of management", they must disclose "special information acquired during their negotiations for the sale of the entire undertaking".⁹ Counsel argued that special information subject to disclosure included information acquired during negotiations for the sale of the entire undertaking. Information acquired in the ordinary course of management, and not subject to disclosure according to the argument, included such matters as a large casual profit, the discovery of a new vein in the company's coal mines and the prospect of a good dividend. Counsel's argument for disclosure was predicated on the view that at the commencement of negotiations the directors became trustees for the benefit of the company and the shareholders and could not purchase the interest of the shareholders, whom counsel viewed as the ultimate beneficiaries of the sale of the business, without disclosing the negotiations.¹⁰

⁹ Ibid, p. 423.

¹⁰ Ibid, p. 423.

Decision and Discussion

The court noted that directors occupy a position which encompasses their being trustees of the company's business and agents for its transactions. "They must act bona fide for the interests of the company," the judge observed, summarizing the unifying principle of directors' fiduciary duties to their corporations.¹¹ But, he noted, the plaintiffs' position went "far beyond" that. They argued that the directors owed fiduciary duties to the shareholders as well. The judge outlines the plaintiffs' position and his holdings as follows:

It is urged that the directors hold a fiduciary position as trustees for the individual shareholders, and that, where negotiations for sale of the undertaking are on foot, they are in the position of trustees for sale. The plaintiffs admitted that this fiduciary position did not stand in the way of any dealing between a director and a shareholder before the question of sale of the undertaking had arisen, but contended that as soon as that question arose the position was altered. No authority was cited for that proposition, and I am unable to adopt the view that any line should be drawn at that point. It is contended that a shareholder knows that the directors are managing the business of the company in the ordinary course of management, and impliedly releases them from any obligation to disclose any information so acquired. That is to say, a director purchasing shares need not disclose a large casual profit, the discovery of a new vein, or the prospect of a good dividend in the immediate future, and similarly a director selling shares need not disclose losses, these being merely incidents in the ordinary course of management. But it is urged that, as soon as negotiations for the sale of the undertaking are on foot, the position is altered. Why? The true rule is that a shareholder is fixed with knowledge of all the directors' powers, and has no more reason to assume that they are not negotiating a sale

¹¹ Ibid, p. 425.

of the undertaking than to assume that they are not exercising any other power. It was strenuously urged that, though incorporation affected the relations of the shareholders to the external world, the company thereby becoming a distinct entity, the position of the shareholders inter se was not affected, and was the same as that of partners or shareholders in an unincorporated company. I am unable to adopt that view. I am therefore of opinion that the purchasing directors were under no obligation to disclose to their vendor shareholders the negotiations which ultimately proved abortive. The contrary view would place directors in a most invidious position, as they could not buy or sell shares without disclosing negotiations, a premature disclosure of which might well be against the best interests of the company. I am of opinion that directors are not in that position.¹²

The court concluded that directors are not trustees for shareholders and that the relationship among shareholders is not one of partnership. Two sources of fiduciary obligations to shareholders were, thereby, rejected in this passage. In recognition of those who view fiduciary obligations within the corporation as emanating from the influence exercised by controlling or majority shareholders, it should be noted that the judge in Percival v. Wright did not separately consider the duties which such shareholders may owe to other shareholders.

While the judge's conclusions may seem based on sound legal reasoning, the extent to which they partake of judicial policy making should not be overlooked. As the judge noted, no authority was cited in support of the plaintiffs' position. Likewise, however, no authority against the plaintiffs' position was cited. Essentially, the judge held that since directors may exercise many powers which affect shareholders' interests, shareholders should be wary when dealing with directors. As a policy matter, he decided that shareholder wariness should be sufficient control over directorial conduct. Such control should not be supplemented or

¹² Ibid, pp. 425-426.

supplanted by the courts. The judge further recognized that conflicts could arise if directors were required to act both in the best interests of shareholders and in the best interests of the corporation. Such a requirement would "place directors in a most invidious position", he said. This judicial solicitude for directors continues to this day. In Brant Investments et al. v. KeepRite Inc. et al., McKinlay J.A. states the following:

To impose upon directors and officers a fiduciary duty to the corporation as well as to individual groups of shareholders of the corporation could place directors in a position of irreconcilable conflict.¹³

There are limits to the utility of analogies from other areas of law as the judge in Percival v. Wright demonstrated when he effectively stated that shareholders were not partners, a proposition we accept as obvious. Similarly, directors are not trustees as such, either for the corporation or its shareholders, unless they explicitly assume that additional office. Plaintiffs' counsel's use of analogies in his attempt to impose on directors fiduciary duties to shareholders is not without merit, however. The law of fiduciary relations has developed through the careful use of analogies from other areas of law as plaintiffs' counsel attempted to do. Although the courts increasingly view the law of fiduciary relations as an area of law sui generis, it certainly seems apt to describe shareholders as having some of the rights and responsibilities of partners and to describe directors as having some of the responsibilities of trustees for shareholders, particularly, in view of the statutory oppression remedy.

The arguments and reasons in Percival v. Wright demonstrate the careful consideration of the particular facts of the case which characterizes cases in which fiduciary claims are considered. As noted, plaintiffs' counsel sought to distinguish the usual situation in which directors are viewed as not having any fiduciary duty to shareholders, for example, the

¹³ (1991), 3 OR (3d) 289 at 301.

day-to-day operation of the business, from special situations which arise, for example, the prospective sale of the business. This approach to identifying situations in which a fiduciary duty may arise has been used by many subsequent judges. Thus, in determining whether fiduciary duties arise, one must carefully examine the particular circumstances; few fiduciary duties arise by virtue of the classification of the relationship between the parties alone. That fiduciary duties do not arise in all circumstances between directors and shareholders was made amply clear by the decision in Percival v. Wright.

Although Percival v. Wright was decided at a time when the law of fiduciary relations was still poorly developed, the decision cannot be dismissed on that basis. Even if the directors in Percival v. Wright were judged by standards which require directors to act in the interests of shareholders, the result may not have been different. Ultimately, the plaintiffs' proposition that the directors were in a fiduciary relationship to the shareholders and had a fiduciary duty to disclose the negotiations for sale of the corporation's business failed because the facts do not disclose such a relationship. The facts do not suggest that the plaintiffs were relying on the directors or in need of protection from the directors. To recapitulate, the plaintiffs had obtained an independent valuation of the shares and the directors agreed to the price requested by the plaintiffs. In fact, the directors agreed to pay a higher price when it appeared that the price the plaintiffs had initially set was too low. Thus, even if directors' conduct towards shareholders were set at a higher standard than that for which this case has become notorious, these facts may have been sufficient to save the directors from liability. Further, even without the intervention of the court, the shareholders could have done more to protect themselves. There is no evidence that the directors were so intent on acting in a self-interested manner that a special plea to the courts to rescind the contract of purchase and sale was justified. The plaintiffs could have sought representations from the directors that they knew of no negotiations for the sale of the company's shares or the company's business, for example. This they should have done because, as the judge notes, "a shareholder is fixed with knowledge of all the directors' powers", including the power to negotiate a sale of all the company's

undertaking and should not assume that such powers are not being used possibly to the shareholder's detriment. Should the law require the shareholder to be so vigilant in transactions with directors?

Unfair negotiating is not, however, the crux of the plaintiffs' complaint in Percival v. Wright. They do not appear to have had a relationship of dependence on or vulnerability to the directors which made them needy of the protection of the courts. The plaintiffs' complaint was that they were not privy to information which they subsequently discovered and considered material, information which was available to the directors, by virtue of their office, and which would enable them to act to their benefit. There is no suggestion that this lack of information caused the shareholders to act to their detriment or that the directors, in fact, acted for their own benefit on the basis of their special knowledge. But, the corporate structure which excludes shareholders from information merited special attention in this case. Surely, beyond their proper compensation for discharging their responsibilities, directors should not be permitted to benefit from their knowledge of the corporation's business and affairs which they acquire in discharging their office particularly when shareholders are excluded from such specially acquired information. Nonetheless, the trial judge refused to impose fiduciary duties on directors in favour of shareholders. The fact of the negotiations for the sale of the business was qualitatively different from the type of personal relationship which courts in the English law tradition have come to consider as an appropriate basis for imposing fiduciary duties.

Although the judge did not seem to appreciate that directors' special access to information may justify special claims by shareholders where material facts are not disclosed, it should be noted that plaintiffs' counsel's argument on this matter is not entirely convincing. Plaintiffs' counsel's argument that "special" information should be disclosed to shareholders in the position of the plaintiffs while "ordinary" information need not be disclosed is unsatisfactory because the distinction between "ordinary" and "special" information is confused and unclear. From the perspective of a shareholder wishing to sell his shares and maximize the price to be

paid for them, it is difficult to distinguish between the types of information discussed by counsel. To recapitulate, he argued that special information subject to disclosure included information acquired during negotiations for sale of the entire undertaking while information such as a large casual profit, the discovery of a new vein of coal or the prospect of a good dividend, acquired in the ordinary course of management, was not subject to disclosure. Both the information counsel called "special" and the information he called "ordinary" are likely to have a material impact on the value of the shares. Therefore, disclosure of all of the types of information discussed by plaintiffs' counsel would assist shareholders in valuing the shares they wish to sell. Eventually, courts and law reformers would recognize that materiality to the shareholder or prospective shareholder should be the relevant test for disclosure of information in securities matters.¹⁴

The unwillingness of the court to formulate any protection for shareholders demonstrated the dangers to shareholders who are not directly involved in the operation of a corporation's business or who do not control the corporation. Unwary shareholders were now exposed to the dangers of unscrupulous directors since such directors could be insulated from shareholder complaints. This was a judicially created risk to shareholders which was added to the business risk which shareholders assumed by investing in corporations. This additional risk threatened shareholders' investments and, hence, the viability of the corporation as a vehicle for capital formation and the conduct of business activity.

¹⁴ This realization has led to the so-called continuous disclosure rules in securities statutes including the rules requiring reporting of a material change pursuant to OSA, s. 75, on the occurrence of some of the types of events discussed by plaintiffs' counsel in Percival v. Wright. This is not to suggest that the identification of a "material change" is a matter free from difficulty.

The threat posed by Percival v. Wright to shareholders and, thereby, to corporations has caused the case to be the subject of much attention from legal scholars, judges and law reformers. As Louis Loss quipped, Percival v. Wright "has had a remarkable career for a lower court decision."¹⁵ Referring to the trial judge's unyielding fidelity to the proposition that directors have fiduciary obligations only to their corporation and not to shareholders, Loss observed that the judgement stands as "a monument to the ability of lawyers to hypnouze themselves with their own creations".¹⁶

As Loss indicates, the development of a fair and balanced law of directors' duties to shareholders has been made difficult by the decision in Percival v. Wright. The rule in Percival v. Wright is understood in various ways by various commentators. Loss, for example, summarized the case as stating that "a director has no fiduciary obligation of affirmative disclosure when he deals with shareholders individually rather than with his company."¹⁷ A somewhat broader view of the principle of the case was taken by the Task Force.¹⁸ They considered the decision to have declared that "ordinarily a director is not in a fiduciary relationship with individual shareholders...".¹⁹ Broader still was the view of Percival v. Wright taken by the Kimber Committee. In its Report (hereinafter referred to as the "Kimber Report"), the Kimber Committee stated that derived from Percival v. Wright was the principle

¹⁵ L. Loss, "The Fiduciary Concept as Applied to Trading by Corporate 'Insiders' in the United States", 33 Mod L Rev 34, p. 40.

¹⁶ Ibid, pp. 40-41.

¹⁷ Ibid, p. 40.

¹⁸ Canada, Proposals for a New Business Corporations Law for Canada (Ottawa: Information Canada, 1971).

¹⁹ Ibid, v.I, paragraph 262, p. 90.

that "no fiduciary relationship exists between a director of a company and its shareholders."²⁰

Few commentators would quarrel with the following passage in the Dickerson Report:

Under existing rules of common law and equity, the outsider is almost totally unprotected. This is largely the result of the decision in Percival v. Wright.²¹

From these views of the law of directors' fiduciary duties to shareholders, law reformers would attempt to move in the 1960s and 1970s.

Allen v. Hyatt

In Allen v. Hyatt²², the Judicial Committee of the Privy Council made clear that the protection of directors reflected in Percival v. Wright should not be expanded. In this case, the directors became trustees²³ or agents²⁴ for shareholders when they acquired options over shareholders' shares in order to effect a proposed amalgamation. By their conduct, these directors placed themselves in a traditional fiduciary relationship with the shareholders. Accordingly, they were barred from profiting from this relationship by exercising the options and reselling the shares at a higher price. Thus, Allen v. Hyatt exemplifies an important limitation to the rule in Percival v. Wright, namely, that although directors generally are not

²⁰ Ontario, Report of the Attorney General's Committee on Securities Legislation in Ontario (no publication information, 1965), p. 14.

²¹ Dickerson Report, v.I, paragraph 262, p. 90.

²² Footnote 3, above.

²³ Ibid, DLR, p. 11.

²⁴ Ibid, p. 12.

in a fiduciary relationship with shareholders, they may place themselves in such a relationship through their conduct. Moreover, Haldane L.C. stated the following:

The appellants [directors] appear to have been under the impression that the directors of a company are entitled under all circumstances to act as though they owed no duty to individual shareholders. No doubt the duty of the directors is primarily one to the company itself. It may be that in circumstances such as those of Percival v. Wright...they can deal at arm's length with a shareholder. But the facts as found in the present case are widely different from those in Percival v. Wright, and their Lordships think that the directors must here be taken to have held themselves out to the individual shareholders as acting for them on the same footing as they were acting for the company itself, that is as agents.²⁵

(Emphasis added.)

In this passage, Lord Haldane indicates that directors have a general duty to shareholders although he acknowledges that their primary duty is to the company. Thus, directors are acknowledged to owe duties to shareholders by virtue of their office and, in circumstances such as these, by their conduct.

Regal (Hastings), Ltd. v. Gulliver

While the Anglo-Canadian law governing directors' fiduciary duties to shareholders remained frozen in its 1902 formulation in Percival v. Wright, subject to the possibilities of a thaw in judicial thinking which appeared in Allen v. Hyatt, the law governing directors' fiduciary duties to corporations continued to develop. The leading decision in this

²⁵ Ibid, pp. 11-12.

area of the law is the House of Lords 1942 decision in Regal (Hastings), Ltd. v. Gulliver.²⁶ This decision represents a synthesis and summary of the Anglo-Canadian law of fiduciary relations to 1942. The Law Lords' discussions of fiduciary situations and the principles of law applicable therein form the foundation upon which certain reforms of the OSA and the Canada Corporations Act, the predecessor of the CBCA, would be built. In particular, the rules relating to disclosure of trading by corporate insiders and the rules regulating take-over bids emanate from the Law Lords' views concerning who may benefit from the use of corporate information and corporate opportunity.

The Factual Background

Regal (Hastings), Ltd. ("Regal") owned and managed a cinema at Hastings. In the summer of 1935, the directors of Regal began looking for further cinemas to acquire. Two were found. A new corporation ("Amalgamated") was incorporated to hold the leases. Regal or its nominees were to hold Amalgamated's 5,000 £1 shares so that Amalgamated would be a wholly owned subsidiary of Regal. The result of this arrangement would be that "[t]he whole beneficial interest in the lease would... enure solely to the benefit of Regal."²⁷ The directors of Regal determined that Regal could only pay for 2,000 £1 shares at that time. The remainder of the shares were to be issued to Regal's nominees as fully paid for services rendered.

The owners of the two cinemas wanted the rent guaranteed. The directors thought that the assurance sought by the landlords could be provided in either of two ways. The directors of Amalgamated, who were also the directors of Regal, could personally guarantee the rent.

²⁶ Footnote 4, above.

²⁷ Ibid, p. 383.

Alternatively, the 3,000 £1 shares which were to have been issued to Regal's nominees for past services rendered could instead be issued for cash, thereby significantly increasing Amalgamated's paid up capital. One of the directors, Gulliver, objected to guaranteeing the rent. Therefore, the directors of Regal and Amalgamated decided to arrange for the subscription for the Amalgamated shares. Four of the Regal/Amalgamated directors each subscribed for 500 shares. As to these shares, Lord Russell of Killowen states, "[T]hese shares, when acquired by the directors, were acquired by reason, and only by reason of the fact that they were directors of Regal, and in the course of execution of that office."²⁸ Gulliver did not invest in Amalgamated. Rather, he found three outside investors who cumulatively acquired 500 shares. Garton, the solicitor to both corporations, was requested by the directors to subscribe for 500 shares and did so. With these arrangements in place, the leases were obtained.

Subsequently, all of the Regal and Amalgamated shares were sold. Regal, the directors, the three outside investors and Garton sold their Amalgamated shares for a significant profit. Sometime thereafter, Regal, at the behest of its new shareholders, sued its former directors and Garton to recover the profit made on the sale of their Amalgamated shares. The suits against the four directors who held the Amalgamated shares succeeded. The suit against Gulliver failed because he had placed the shares with outside investors. He had not made any profit for which he was accountable. The case against Garton also failed because his profit was made with the knowledge and consent, indeed, at the invitation of, Regal. Thus, though the directors and Garton were found to have acted throughout in good faith and without fraud, the four directors were ordered to pay their profits to Regal. None of Regal's former shareholders obtained any portion of that benefit.

²⁸ *Ibid*, p. 387.

The "Fiduciary Position":
The Basis of a Fiduciary Relationship

In the course of argument, it was accepted that directors are in a fiduciary relationship to their corporations. This principle which governs directors' conduct towards their corporations is sufficient to support the decision in the case. The foundation of a fiduciary relationship was a "fiduciary position", an idea referred to by several of the Law Lords.²⁹ It is apparent that the Law Lords believed that fiduciary relationships were not limited to those categories of relationships which had traditionally been identified as such and that fiduciary obligations could be imposed in contexts yet to be considered. Thus, the Law Lords opened the door to the possibility, as a matter of law, that a director could be in a fiduciary position to a shareholder. The Regal (Hastings) decision raised the possibility that the rule in Percival v. Wright could be changed, but an appropriate set of facts would be required before the courts might consider modifying the rule. Director-shareholder relations therefore, remained in the unsatisfactory state which led to the statutory reforms to be discussed in Chapter 3.

The Rule Requiring Disclosure and Assent

As various Law Lords point out, the directors of Regal could have taken for themselves the advantage and opportunity presented to them by virtue of their office had they obtained the assent of the shareholders.³⁰ Obviously, assent is preceded by disclosure. Disclosure and assent insulate directors from subsequent action because the making of disclosure and the seeking of consent enables the shareholders to act in their own best interests by extending or withholding their consent based on their assessment of whether the proposed action

²⁹ See, for example, ibid, pp. 381, 382, 387, 392 and 395.

³⁰ See, for example, the speech of Lord Wright at ibid, p. 394.

will benefit or prejudice them. The requirement of disclosure and assent discussed in Regal (Hastings) suggests that, under English common law governing directors, directors are ultimately obliged to act in the interests of and to protect the corporation's shareholders.

Remedy

Although the Law Lords only obliquely approach the view that directors stand in a fiduciary relationship to shareholders, they make clear the rigour of the divestiture rule which results when a fiduciary breaches his duty. For example, Viscount Sankey cites the following passage from Ex p. James:

The doctrine as to purchase by trustees, assignees, and persons having a confidential character, stands much more upon general principle than upon the circumstances of any individual case. It rests upon this; that the purchase is not permitted in any case, however honest the circumstances; the general interests of justice requiring it to be destroyed in every instance; as no court is equal to the examination and ascertainment of the truth in much the greater number of cases.³¹

Lord Russell of Killowen quotes from the case of Parker v. McKenna as follows:

...[I]t appears to me very important that we should concur in laying down again and again the general principle that in this court no agent in the course of his agency, in the matter of his agency, can be allowed to make any profit without the knowledge of his principal; that the rule is an inflexible rule, and must be applied inexorably by this court, which is not entitled, in my judgement, to receive evidence, or suggestion, or argument, as to whether the principal did or did not suffer any injury in fact, by

³¹ Ibid, p. 381.

reason of the dealing of the agent; for the safety of mankind requires that no agent shall be able to put his principal to the danger of such an inquiry as that.³²

Finally, Lord Wright states the following:

[B]oth in law and equity, it has been held that, if a person in a fiduciary relationship makes a secret profit out of the relationship, the court will not inquire whether the other person is damnified or has lost a profit which otherwise he would have got. The fact is in itself a fundamental breach of the fiduciary relationship. Nor can the court adequately investigate the matter in most cases. The facts are generally difficult to ascertain or are solely in the knowledge of the person who is being charged. They are matters of surmise; they are hypothetical because the inquiry is as to what would have been the position if that party had not acted as he did, or what he might have done if there had not been the temptation to seek his own advantage, if, in short, interest had not conflicted with duty.³³

These quotations from authority and observations of the Law Lords themselves convey the following points:

1. The principles of fiduciary obligations are analogous, in part, to the law of trusts, confidences and agency. Indeed, the Law Lords used principles from proximate areas of law to illuminate the law of fiduciary relations. Nonetheless, the law of fiduciary relations was treated as an area of law sui generis. Gone was the awkward

³² Ibid, p. 388.

³³ Ibid, p. 392.

straining of analogies to other areas of law which characterized the arguments in Percival v. Wright;

2. The good faith and honesty of a fiduciary does not immunize his conduct from review and rectification by the courts;
3. Evidence of absence of damage to the beneficiary of the fiduciary obligation will not be considered by the courts; and
4. In order to obtain relief from the courts, the beneficiary of the fiduciary obligation must simply prove the fact of the fiduciary relationship and the fiduciary's making of a profit without either the knowledge or the assent of the beneficiary.

Implications for Law Reform

The Regal (Hastings) decision articulated the judiciary's view of the appropriate morality which should operate within the corporation. This view was extremely influential in the work of Canadian securities and corporate law reformers although the law applied in respect of the directors' conduct in Regal (Hastings) did not address all of the Canadian law reformers' concerns. For example, the strong interest which Canadian securities law reformers had in economic development was probably of little immediate interest to the Law Lords. Consequently, the Law Lords may have expected a higher level of economic disinterestedness from directors than securities reformers would require. Similarly, securities law reformers would want shareholders injured by corporate insiders to have a remedy while the Law Lords were content to leave the corporation as the sole entity entitled to a remedy for the acts of errant directors. Nonetheless, the Regal (Hastings) decision expresses the hallmarks of

statutory reform; such hallmarks did not have to be created by the reformers. These hallmarks include the requirements that:

1. A director's appropriation of corporate information or a corporate opportunity for his own use must be disclosed; and
2. A director's appropriation of corporate profit-making opportunity must be approved.

The core of the decision is that directors must disclose corporate information and opportunities which they wish to use and that in the absence of a proper sanction permitting them to do so, directors are accountable to the corporation for their use of such information and opportunities. These rules recognize the position which directors occupy and the preferential, exclusive, often unscrutinized, access to corporate information and opportunities which directors have. They are intended as a protection against, and a corrective of, directorial abuse of position. This rationale forms a sound basis for imposing fiduciary duties on directors in favour of shareholders as well.

United States

Just as Anglo-Canadian jurisprudence would influence Canadian securities and corporate law reformers in the 1960s and 1970s, so would American jurisprudence. In fact, it seems likely that the decisions of several American courts on the issues of directors' and insiders' fiduciary duties to shareholders prompted the Kimber Committee and the Task Force to place considerable faith in the Canadian courts to develop this area of the law. Of particular note, and in contrast to the Anglo-Canadian courts' refusal to impose fiduciary duties on directors in favour of shareholders, some courts in the United States simply "abandoned"

Percival v. Wright.³⁴ Other courts "achieved much the same result by paying lip service to it but finding 'special circumstances'".³⁵ This approach was approved by the Supreme Court of the United States which ruled in the 1909 decision of Strong v. Repide that where a director was aware of an impending sale of the company's one valuable asset, the director could not purchase a shareholder's shares without disclosing that fact.³⁶ Such facts altered the ordinary relationship between directors and shareholders in which fiduciary duties were not imposed and came to be known as the "special circumstances" exception to the general rule that there was no fiduciary relationship between directors and shareholders. Subsequently, American courts found a pending merger, a consolidation, a take-over, a pending sale of corporate assets and a pending liquidation to constitute such special circumstances. Unlike Anglo-Canadian courts, American courts considered the factors facing corporations rather than the personal relationship between directors and shareholders in determining whether the imposition of fiduciary duties on directors in favour of shareholders was appropriate. This approach amounted to considering whether facts were material to an investor. If the facts were material, they should be disclosed.

Strong v. Repide was followed by securities legislation in 1933 and 1934 with the enactment of the *Securities Act of 1933*³⁷ and the *Securities Exchange Act of 1934*.³⁸ Under s.10 of the 1934 legislation, the well-known Rule 10b-5 was adopted. This Rule came to provide injured security holders with a private right of action where a fact which might reasonably be expected to affect the value of a security, for example, a material fact, was not disclosed in a purchase or sale transaction.

³⁴ Loss, *op. cit.*, p. 41.

³⁵ *Ibid*, p. 41.

³⁶ 213 US 419.

³⁷ Chapter 38, title I, § 1, 48 Stat 74.

³⁸ Chapter 404, title I, § 1, 48 Stat 881.

In the United States, the courts, not the legislators developed directors' and insiders' fiduciary duties to shareholders. As Loss notes, "The SEC statutes (more specifically the *Securities Exchange Act of 1934*) say very little about insider trading and nothing at all about the fiduciary position of directors and controlling shareholders."³⁹ An effective law concerning directors' and insiders' fiduciary duties to shareholders dates from 1946 when the United States District Court in Philadelphia ruled in respect of a four shareholder company that a violation of Rule 10b-5, promulgated by the Securities and Exchange Commission under the *Securities Act of 1933*, creates a private right of action as a matter of U.S. federal law.⁴⁰ The judicial decisions under Rule 10b-5 led to a new "new federal common law" governing corporations. Loss summarizes this new judge-made law as follows:

When we come to examine the content of this new federal common law that has been developed by the lower federal courts under Rule 10b-5, we find that they have enthusiastically abandoned Percival v. Wright in favour of an affirmative obligation on the part of the directors and other insiders to disclose material facts in buying shares of their company.⁴¹

Loss adds the following observations:

To say this much, one need hardly add, is to begin the discourse, not to end it. Once an insider is considered to have substantially a fiduciary's affirmative disclosure

³⁹ Loss, op. cit., p. 37.

⁴⁰ Ibid, p. 42.

⁴¹ Ibid, p. 45.

obligation when dealing with outsiders, a considerable bevy of problems emerges...⁴²

Loss notes that, by 1970, of the "considerable bevy of problems" he refers to, "most have already been the subject of litigation."⁴³ Hence, American corporate law has benefitted from the cumulative wisdom of many lawyers and judges collected in the judgements of these cases. As we shall see in Chapter 3, Canadian securities and corporate law reformers anticipated a similarly rich jurisprudence to be developed by Canadian courts.

⁴² Ibid, p. 46.

⁴³ Loc cit.

CHAPTER 3

DIRECTORS' AND INSIDERS' STATUTORY FIDUCIARY DUTIES TO SHAREHOLDERS

The proclamation in force of the CBCA on December 15, 1975 completed twelve years of far-reaching securities and corporate law reform in Canada. The reform process began in October 1963 when the Attorney General of Ontario appointed a Committee on Securities Legislation, known as the "Kimber Committee" in recognition of its Chairman J. R. Kimber, Q.C., to review Ontario's securities legislation. The Kimber Report was released in early 1965.¹ In late 1967, the federal government established a Task Force under the leadership of Dr. R.W.V. Dickerson to review corporations law in Canada. The Dickerson Report, properly entitled Proposals for a New Business Corporations Law for Canada, was published in 1971 and led to the enactment of the CBCA.²

Both the Kimber Committee and the Task Force were concerned about the state of the law protecting shareholders. One area of concern was the lack of directors' duties to shareholders which would be upheld by the courts. The Kimber Committee's salutary recommendations concerning this issue were implemented by the enactment of the insider trading and take-over bid provisions in the OSA. Ancillary regulatory power was given to the OSC, in part, under s. 127 of the OSA which permits the OSC to order the cessation of trading of securities of an issuer where such an order is in the public interest. This regulatory power has

¹ Ontario, Report of the Attorney General's Committee on Securities Legislation in Ontario (no publication information, 1965).

² Canada, Proposals for a New Business Corporations Law for Canada (Ottawa: Information Canada, 1971).

been confidently assumed by the OSC and it has been used sensibly.³ This assumption and discharge of jurisdiction is in sharp contrast to the conduct of the courts in this area of the law.

Although the Kimber Committee wished to regulate directors' and insiders' conduct in public company take-over bids and insider trading, the Committee did not seek to regulate either private company affairs or public company affairs which lay outside of these parameters. Thus, a range of directors' and insiders' conduct towards shareholders remains unregulated by statute. The Kimber Committee specifically anticipated that the judiciary would develop and apply the law in these areas.⁴ Moreover, general corporate law reform was the purview of others: the Lawrence Committee in Ontario and the federal Task Force. The Task Force largely adopted the Kimber Committee's recommendations concerning insider trading and take-over bids. These recommendations were supplemented by the introduction of the oppression remedy. The Director appointed under the CBCA and shareholders were given powers to uphold the provisions of the statute and to enforce their rights, respectively. These powers were employed by the Director in cases such as Sparling et al. v. Royal Trustco Ltd. et al.⁵ and by shareholders in cases such as Whitehorse Copper Mines Ltd. v. Luecke.⁶ Nonetheless, the Task Force also contemplated that the courts would retain significant jurisdiction for developing shareholder rights.⁷

³ See P. Anisman, "The Commission as Protector of Minority Shareholders" in Securities Law in the Modern Financial Marketplace Special Lectures of the Law Society of Upper Canada - 1989 (Don Mills: DeBoo, 1989), p.451.

⁴ Kimber Report, p. 23.

⁵ (1983), 143 DLR (3d) 112, 21 BLR 97, 32 CPC 291 (Ont HC); (1984), 45 OR(2d) 484, 1 OAC 279, 6 DLR (4th) 682 (Ont CA); [1986]2 SCR 537.

⁶ (1980), 10 BLR 113 (BCSC).

⁷ See, for example, Dickerson Report, vol. I, paragraph 477, p. 159.

The Kimber Report

The Kimber Committee was given a broad mandate to "review and report upon, in the light of modern business conditions and practices, the provisions and working of securities legislation in Ontario".⁸ The first two items the Committee was particularly directed to consider were "the problems of take-over bids and of 'insider' trading".⁹ Other matters such as shareholder disclosure, proxy solicitation and the procedures for the primary distribution of securities were included in the Committee's mandate, but the "problems of take-over bids and 'insider' trading" were at the forefront of the Committee's deliberations and the Kimber Report.

Before embarking on its discussion of insider trading and take-over bids, the Kimber Committee outlined some of the objectives which Committee members considered securities law reform should achieve. These objectives should be borne in mind by readers of the Kimber Report because they propelled securities law reform in a direction which has left problems akin to the "problems of take-over bids and 'insider' trading" in closely-held corporations largely unaddressed by legislation to this day.

The Committee noted that "the underlying purpose of legislation governing the practices and operation of the securities market must be the protection of the investing public".¹⁰ The concept of the "investing public" was not explored in the Kimber Report. It is clear, however, that the Kimber Committee did not have in mind all shareholders of privately-held as well as publicly-traded corporations. For example, in its recommendations concerning insider trading, the Committee said:

⁸ Kimber Report, p. 6.

⁹ Loc cit.

¹⁰ Ibid, p. 7.

The reporting of insider trading should, in principle, be made applicable to all companies whose securities are traded among members of the public. Thus, private companies will be excluded.¹¹

Insider trading reports were part of a "principled" response to the problem of insider trading because they were expected to discourage "improper trading" and, hence, boost "investor confidence in the securities market".¹² The concepts of "trading", "investors" and the "securities market" show that the Kimber Committee was not directing its attention to the problems associated with errant directors in all corporations including privately-held corporations. Similarly, the Committee's recommendations concerning take-over bids did not extend to private company transactions.¹³

In addition to protecting the "investing public", or the holders of publicly-traded securities, the Kimber Committee noted that "securities legislation will affect the development of financial institutions and their efficiency in performing certain economic functions."¹⁴ The Committee clearly had the big economic picture in mind. Economic development was a significant factor in the Committee's deliberations. Hence, the following passage:

While Canada enjoys one of the highest standards of living in the world, it is not yet one of the leading industrial nations. However, Canada is at that stage of economic growth where the importance of the development of mature secondary industry is now

¹¹ Ibid, p. 14.

¹² Ibid, p. 10.

¹³ Ibid, p. 23.

¹⁴ Ibid, p. 7.

surpassing in importance the development of natural resources. A prime requirement to accelerate our movement along this road is for our capital markets to be unquestionable in their efficiency and respectability. Such is the interest of all who are concerned for the economic future of the country and the province; such is the responsibility of those who are charged with considering securities legislation in the Province of Ontario.¹⁵

(Emphasis added.)

Fortunately, the Committee noted, protecting the investing public and nurturing the economy are closely linked: "Establishment of conditions and practices in the capital market which best serve the investing public will normally be consistent with the best interests of the whole economy".¹⁶

The Committee consolidated its thoughts on the task at hand in the following passage:

The Committee believes that changes in securities legislation in the Province of Ontario should be devised in recognition of two basic propositions. To the extent that securities legislation is improved in the interest of investors, the securities industry will benefit from increased public confidence. To the extent that the industry becomes a more effective and efficient part of the economy, the general public will benefit.¹⁷

¹⁵ Ibid, pp. 8-9.

¹⁶ Ibid, p. 7.

¹⁷ Ibid, p.9.

These passages show that the Committee sought to protect the investing public and to nurture the economy thereby. The investing public would be protected by implementing various measures to ensure the integrity of the securities market. The integrity of the securities market was, thus, the focus of the Kimber Committee's research and recommendations. The recommended reforms, chief among them being various forms of "disclosure of information to investors", were subsumed by the Committee's chief objective of developing and maintaining "public confidence" in the securities market.¹⁸ Private corporations and their shareholders were, thus, outside of the Committee's purview.

Insider Trading

The Kimber Committee defined insider trading as "purchases or sales of securities of a company effected by or on behalf of a person whose relationship to the company is such that he is likely to have access to relevant material information concerning the company not known to the general public."¹⁹ It was clear to the Committee that directors were not the only persons who could work abuse of the stock market and investors. The Committee observed at the outset that it is not improper for an insider to purchase or sell securities of his own company.²⁰ In fact, it was observed that the acquisition of a "direct financial interest in the welfare of the company" by its officers and directors is often considered desirable by investors.²¹ What is improper, however, is the use by an insider of "confidential information acquired by him by virtue of his position as an insider to make profits by trading in the

¹⁸ Loc cit.

¹⁹ Ibid, p. 10.

²⁰ Loc cit.

²¹ Loc cit.

securities of his company."²² The Committee observed that to the extent that insider trading jeopardizes a free and open securities market, it "lessens the confidence of the investing public in the market place and is, therefore, a matter of public concern."²³

The Kimber Committee noted that the existing law recognized that "in certain circumstances a director is not entitled to profit personally as the result of the use of inside information", however, it believed that the existing law was not "adequate to prevent or discourage all the potential abuses inherent to the position of special advantage enjoyed by the insider".²⁴ In addition to being too narrow in certain respects, the existing common law was also too broad in other respects. For example, the directors in Regal (Hastings) were required to account to the company for their gains in circumstances where the shareholders undoubtedly would have wanted them to invest so that the valuable leases of the two cinemas could be acquired by Amalgamated. Equity's divestiture rule did not take account of such shareholder views; it discouraged directors from committing their own resources and linking their own financial rewards to the success of the company. The Committee, on the other hand, viewed such behaviour as strengthening investor confidence.

While the Kimber Committee welcomed insider investment, it also concluded that "the law should clearly provide that the use by insiders, for their own profit or advantage, of particular information known to them but not available to the general public is wrong and that the law should give appropriate remedies to those aggrieved by such misuse."²⁵ To achieve these objectives, the Committee recommended that insiders, meaning primarily directors, officers

²² Loc cit.

²³ Loc cit.

²⁴ Loc cit.

²⁵ Loc cit.

and substantial shareholders, be required to report to the OSC their transactions in securities of their own companies within ten days following the month in which the transaction occurred. Moreover, the companies or other shareholders were to be permitted to recover any benefits obtained from improper insider trading.²⁶

In order to permit the recovery of benefits improperly obtained by insiders, the Kimber Committee had to confront the rule, derived from Percival v. Wright, that "no fiduciary relationship exists between a director of a company and its shareholders."²⁷ As the Committee noted, this rule had been qualified by the Privy Council in Allan v. Hyatt such that "in certain special circumstances there is a fiduciary relationship."²⁸ The extent to which Allen v. Hyatt had qualified Percival v. Wright was, however, viewed as "uncertain".²⁹ In a passage which foreshadows the New Zealand Court of Appeal's 1977 decision in Coleman v. Myers, the Committee observed that a director - shareholder fiduciary relationship was "probably limited to a very narrow class of case in which the shareholder and the director meet virtually face-to-face and the director is put in a fiduciary relationship by the conduct of the parties."³⁰ That is to say, in the view of the Committee, fiduciary obligations are most likely to exist in closely held corporations where the director and the shareholder have a close relationship. Thus, the common law of fiduciary relations was not a satisfactory basis for regulating the often faceless transactions in the securities of large enterprises. Moreover, as the Committee observed, even if judicial inroads on the rule in Percival v. Wright were made, transactions by insiders other than directors would remain unregulated. Accordingly, the Committee recommended that "the

²⁶ Ibid, pp. 10-13.

²⁷ Ibid, p. 14.

²⁸ Loc cit.

²⁹ Loc cit.

³⁰ Loc cit.

so-called doctrine of Percival v. Wright be abolished by statutory enactment, to be replaced by legislative rules... governing the legal relationship between insiders of a company and persons with whom they trade in the company's securities."³¹

The provision advocated by the Kimber Committee regarding recovery against insiders who violated the insider trading rules was to be available either to aggrieved shareholders or to the companies in whose securities the insiders improperly dealt. The Committee considered the view that on the basis of the House of Lords decision in Regal (Hastings), Ltd. v. Gulliver and the Supreme Court of Canada decision in Zwicker v. Stanbury³², a company had a right of recovery for improper insider trading. The Committee believed that this view also was sufficiently "uncertain" that statutory revision of the law was required.³³ Accordingly, the Committee recommended the imposition of statutory liability for insider trading in the following terms:

An insider of a company who, in any transaction relating to the securities of that company or of any company of which the first mentioned company is an insider, makes improper use of specific confidential information which might be expected materially to affect the value of those securities, shall be liable to compensate any person who directly suffers from his action in so doing unless that information was known or ought to have been known to such person, and shall also be accountable to the company for any direct benefit, received or receivable by him, resulting from any such transaction.³⁴

³¹ Loc cit.

³² [1953]2 SCR 438.

³³ Kimber Report, p. 16.

³⁴ Loc cit.

In the event that a shareholder or the company did not pursue the matter against the offending insider, the OSC was empowered to do so.³⁵

The Kimber Committee emphasised the requirement of directorial disclosure particularly by way of insider trading reports and take-over bid circulars. But directorial disclosure may not be adequate to protect shareholders. Disclosure of insider trading is made through the Bulletin published by the OSC which is not widely circulated. Even when circulated, the information disclosed relates to historical actions. It does not enable shareholders to preempt undesired directorial behaviour. It seems, however, that assent, as discussed in Regal (Hastings), was considered by the Kimber Committee to be too great an impediment to entrepreneurial insiders. Therefore, the Committee recommended enactment of a remedy which would permit shareholders or the corporation to be compensated for an insider's improper use of "specific confidential information". This was done in the OBCA and the CBCA.³⁶ By extending this remedy to shareholders, securities law reformers overcame one of the unfortunate features of the Regal (Hastings) case, viz., that although the former shareholders of Regal may have been injured by the directors' wrongdoing, the subsequent shareholders, through the corporation, benefitted by the decision in favour of the corporation.

Take-over Bids

Closely linked to the problem of insider trading profits, according to "allegations made in the press and elsewhere", was the take-over bid transaction.³⁷ Criticism

³⁵ Ibid, p. 17.

³⁶ OBCA, s. 138, CBCA, s. 131, cf. OSA, s. 76.

³⁷ Ibid, p. 22.

"by the general public, the financial community and the press concerning both the form and the effect"³⁸ of take-over bids had apparently not been abated by a voluntary Code developed by various trust companies, the Investment Dealers Association of Canada and the Canadian stock exchanges to regulate such transactions. It was apparent that the Code was not being followed in many cases. Therefore, "to achieve full disclosure on an equitable basis, the Committee... [recommended] that... [the Code] be supplanted by legislative measures".³⁹

The Committee's recommendations concerning take-over bids were based on a special set of shareholder-oriented objectives. The Committee outlined these objectives in the following passage:

The Committee has concluded that the primary objective of any recommendations for legislation with respect to the take-over bid transaction should be the protection of the bona fide interests of the shareholders of the offeree company. Shareholders should have made available to them, as a matter of law, sufficient up-to-date relevant information to permit them to come to a reasoned decision as to the desirability of accepting a bid for their shares.⁴⁰

Although the Committee viewed its primary objective in the regulation of take-over bids as "the protection of the bona fide interests of the shareholders of the offeree company", it was also aware of the larger economic issues associated with take-over bids. The Committee recognized that "take-over bids can, in many cases, have positive advantage to the companies

³⁸ Ibid, p. 20.

³⁹ Ibid, p. 21.

⁴⁰ Ibid, p. 22.

involved, to their shareholders and to the economy generally".⁴¹ In order to promote these positive economic effects, the Committee stated that it "attempted to ensure that its recommendations would not unduly impede potential bidders or put them in a commercially disadvantageous position vis-a-vis an entrenched and possibly hostile board of directors of an offeree company".⁴²

The Committee's objectives led to the conclusion that any attempt to acquire effective control of a target company should result in statutory regulation. The Committee determined that, as a general rule, effective control could be achieved with little more than twenty per cent of a company's securities. Accordingly, the Committee defined a take-over bid as "an offer (other than by way of private agreement or by way of purchase on a stock exchange or in the over-the-counter market) made to any number of the holders of any class of outstanding voting shares of a company, other than a private company, to purchase a number of such shares which, together with the number of such shares beneficially owned, directly or indirectly, by the offeror and any person or company associated with the offeror at the time of making such offer, will amount in the aggregate to more than 20 per cent of the outstanding voting shares of such class".⁴³ The shares of private companies were excluded from the definition of a "take-over bid". While this exclusion was appropriate given the Committee's objective of ensuring the integrity of the securities market, it meant that shareholders of private companies would not benefit from the rules and procedures devised by the Committee. In addition to the exclusion for private company shares, private agreement transactions, stock exchange and over-the-counter market purchases were excluded from the take-over bid rules and the Committee also

⁴¹ *Ibid*, p. 20.

⁴² *Ibid*, p. 11.

⁴³ *Ibid*, p. 23.

recommended that a provision for obtaining a judicial exemption from the statutory regulation of take-over bids be included in the legislation.

The Committee discussed the private agreement exemption and the possibility of differing treatment of shareholders which it provided. In particular, the Committee acknowledged that this exemption would permit the sale of control blocks at a premium to the price paid to minority shareholders. The Committee was, however, "of the opinion that the evolution of a legal doctrine which may impose upon directors or other insiders of a company who constitute a control group a fiduciary duty toward other shareholders of such company in cases of change of control is, apart from insider trading aspects, a matter to be left to development by the judicial process".⁴⁴ The development of a unified principle of directors' and insiders' fiduciary duties to shareholders was, therefore, left to the courts.

The Committee outlined several of the take-over bid provisions which it recommended for inclusion in an amended *Securities Act*. For example, in order to provide management of the offeree company an "ample opportunity" to give shareholders the benefit of its "analysis" of a take-over bid, the Committee recommended that any shares deposited could not be taken up and paid for until seven days following the making of the bid.⁴⁵ During that time, shareholders could withdraw their deposited shares. In order to ensure that shareholders had "reasonable time" to assess information received during the course of the bid, the Committee recommended that offers to purchase remain open for fourteen days following the initial seven day period.⁴⁶ Further, in the event that a bid was for less than all of the outstanding shares of a class and shares deposited pursuant to the bid exceeded the number which the offeror had

⁴⁴ Loc cit.

⁴⁵ Ibid, p. 24.

⁴⁶ Ibid, p. 14.

agreed and was prepared to purchase, acceptance of deposited shares was to be on a "pro-rata rather than a first-come first-served basis".⁴⁷ The recommended time frame was intended to ensure that shareholders had an adequate opportunity to consider the bid, but the Committee, aware of the greater economic good which could be achieved through take-over bids, also felt that the recommended time frame should not work "a hardship on bidders by unreasonably exposing them to counter bids whether from management or others".⁴⁸ Along the same lines of ensuring that an uncooperative management would not be able to thwart a bid, the Committee also recommended that bidders be furnished with lists of shareholders.⁴⁹ The Committee recommended that in the case of cash bids, the arrangements for financing be disclosed. It also recommended that amendments to the bid to increase the price paid be applicable to both shares to be deposited as well as those already deposited. Finally, the Committee recommended that extensive disclosure be made in offerors' take-over bid circulars as well as in the circulars of directors of offeree companies if the directors recommended acceptance or rejection of the bid. Sanctions and penalties for breach of the take-over bid regime were to be "sufficiently onerous to serve as an adequate substitute for prior review of circulars by a governmental agency".⁵⁰ In short, the Kimber Committee codified a fair and open procedure for the transfer of substantial blocks of shares or all of the shares of publicly traded corporations. The contents of take-over bid circulars outlined by the Kimber Committee are set forth in the Appendix to this paper. Those lists of information to be provided form the core of take-over bid disclosure yet today.

⁴⁷ Ibid, p. 24.

⁴⁸ Loc cit.

⁴⁹ Ibid, p. 26.

⁵⁰ Ibid, p. 73.

The Dickerson Report

The Dickerson Report is noteworthy for its lack of a declaration of directors' duties to shareholders. The federal Task Force certainly appreciated the poor position occupied by shareholders. In the Introduction to the Dickerson Report, the Task Force states, "The position of the minority shareholder has always been an exceptionally unenviable one".⁵¹ More specifically, in Part 10.00 which deals with insider trading, the Task Force states the following:

Under existing rules of common law and equity, the outsider is almost totally unprotected. This is largely the result of the decision in Percival v. Wright [1902] 2 Ch. 421, which declared that ordinarily a director is not in a fiduciary relationship with individual shareholders, and is therefore not bound to make any disclosure of information in his possession that affects the value of any shares that are the subject of a transaction between them.⁵²

In response to these concerns, the Task Force, "overruling Percival v. Wright",⁵³ recommended that the Kimber Committee's insider trading rules be largely carried forward into the CBCA. Parliament had already incorporated these rules into federal corporations law in the 1970 amendments to the *Canada Corporations Act*.⁵⁴ Parliament had also amended the *Canada Corporations Act* in 1970 to incorporate the Kimber Committee's take-over bid rules.⁵⁵ Again, the Task Force advocated carrying forward most of the take-over bid

⁵¹ Dickerson Report, vol. I, paragraph 23, p. 7.

⁵² Ibid, paragraph 262, p. 90.

⁵³ Loc cit.

⁵⁴ SC 1969-70, c.70, ss.98-98F.

⁵⁵ SC 1969-70, c.70, ss. 127-127L.

provisions which were in place. The Task Force recommended three minor changes to the Kimber Committee's take-over bid rules. First, transactions involving no more than fifteen private agreements were to be exempted from the take-over bid rules.⁵⁶ Parliament modified this recommendation so that an "exempt offer" includes separate agreements with fewer than fifteen shareholders.⁵⁷ A broader definition of "shares" subject to the take-over bid rules was sought by the Task Force and implemented by Parliament. Finally, the Task Force agreed with the threshold for the "take-over bid" rules in the *Canada Corporations Act*. Any offer for more than ten per cent of a corporation's shares constitutes a "take-over bid" unless the offer is otherwise exempt. This contrasts with the Kimber Report recommendations and the OSA provisions which are triggered when there is an offer for at least twenty per cent of a corporation's shares.⁵⁸

The Dickerson Report does not deal with the compulsory acquisition provisions of the *Canada Corporations Act*.⁵⁹ Undoubtedly this omission follows from the Task Force's careful following of the Kimber Report. At the time of the Kimber Report, Ontario's corporate and securities statutes contained no compulsory acquisition procedures. These were introduced in Ontario in the OBCA in 1982.⁶⁰ Although the Dickerson Report and the Task Force's draft *Canada Business Corporations Act* did not contain a compulsory acquisition provision, Parliament added such a provision to the draft legislation prepared by the Task Force, though in a form substantially revised from the *Canada Corporations Act*. The compulsory acquisition provision is now found in CBCA, s.206.

⁵⁶ Dickerson Report, vol. I, paragraph 428, p.144.

⁵⁷ CBCA, s.194.

⁵⁸ OSA, s.89(1) "take-over bid".

⁵⁹ RSC 1970 c. C-32, s.136.

⁶⁰ Now OBCA, ss.187-190.

Directors' duties to shareholders are rarely stated explicitly in the Dickerson Report. For example, section 16.07 of the *Draft Act* requires the directors of an offeree corporation to send a directors' circular to shareholders and others if the directors recommend acceptance or rejection of a take-over bid. This provision was modified by Parliament so that directors must send a circular when a take-over bid is made, irrespective of whether a recommendation is made.⁶¹ The Dickerson Report does not state the purpose of the directors circular, although it is obviously intended to assist shareholders in responding to a take-over bid. The Regulation issued pursuant to the CBCA outlines the extensive contents of the directors' circular.⁶² This disclosure permits shareholders to assess the merits of the bid as well as the interests of the directors of the offeree corporation who make a recommendation concerning whether or not to accept the bid. In short, as with take-over bids regulated by the OSA, directors have a significant statutory duty of disclosure to shareholders in take-over bids which are regulated by the CBCA.

As noted, the Dickerson Report does not codify the duties owed by directors to shareholders. Certainly, the provision designed to prevent the dilution of shareholdings,⁶³ which provision Parliament altered to become predicated on specific provisions in the articles of incorporation,⁶⁴ was an attempt to contain the abuse to which shareholders may be subjected by directors. Similarly, the rules fashioned in respect of disclosure of a director's interest in contracts to be entered into with the corporation⁶⁵ were intended to protect the corporation and,

⁶¹ CBCA, s.201.

⁶² Canada Business Corporations Regulations, SOR/79-316, PC 1979-1195, as amended, s.68.

⁶³ Dickerson Report, vol. I, paragraphs 114-116, pp. 40-41.

⁶⁴ CBCA, s. 28.

⁶⁵ Dickerson Report, vol. I, paragraphs 226-233, pp. 78-80.

indirectly, its shareholders. These rules were augmented by Parliament and govern material contracts between the corporation and its officers as well as its directors.⁶⁶ Throughout the Dickerson Report and the CBCA there is, however, no explicit statement of directors' duties to shareholders. Perhaps this omission can be traced to the fact that there was little case law to support such a principle.

By contrast, the Dickerson Report contains a statement of the directors' fiduciary relationship to the corporation. This statement represents the Task Force's "attempt to distil the effect of a mass of case law illustrating the fiduciary principles governing the position of directors".⁶⁷ Accordingly, subsection 122(1) of the CBCA states:

122.(1) Every director and officer of a corporation in exercising his powers and discharging his duties shall
(a) act honestly and in good faith with a view to the best interests of the corporation; and
(b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

A similar provision may be found in various CBCA - cognate statutes.⁶⁸ As we shall see when we consider the directors' responsibility to manage the affairs of the corporation, however, the statute and some case law contemplate that it is the duty of directors to act in the best interests of shareholders, not only in the best interests of the corporation.

⁶⁶ CBCA, s.120.

⁶⁷ Dickerson Report, vol. I, paragraph 236, p. 81.

⁶⁸ See, for example, OBCA, s. 134.

The Task Force's "general statutory formulation of the principles underlying the fiduciary relationship between corporations and their directors"⁶⁹ is not free from uncertainty. For example, it is not always clear that the "best interests" of a legal construct, the corporation, can be readily ascertained. This very difficulty forms a sound basis for requiring that directors and officers act "honestly and in good faith" when discharging their duties.⁷⁰ The Task Force recognized that it would be difficult "to give precision to the notion of 'the best interest of the corporation'".⁷¹ Accordingly, they left the law "to develop in the hands of the

⁶⁹ Dickerson Report, vol. I, paragraph 236, p. 81.

⁷⁰ The best interests of a corporation may include taking active steps to block a take-over of the corporation. Berger J., in Teck Corporation Ltd. v. Millar et al. (1972), 33 DLR (3d) 288 at p.315, said "the directors ought to be allowed to consider who is seeking control and why. If they believe that there will be substantial damage to the company's interests if the company is taken over, then the exercise of their powers to defeat those seeking a majority will not necessarily be categorized as improper.... [In forming this belief, the] directors must act in good faith. Then there must be reasonable grounds for their belief." Such powers may be used by the directors to preserve an ephemeral commodity, the corporation's "identity", in a hostile take-over bid situation. For an interesting discussion of the attempts by the directors of Time Incorporated to preserve the "Time Culture" and the Delaware Courts' acknowledgement of the legitimacy of this objective, see Paramount Communications Inc. et al. v. Time Inc. et al. (1989), 47 BLR 252 (Del Ch); appealed sub nom Re Time Incorporated Shareholders Litigation (1989), 47 BLR 223 (Del Sup Ct). Generally, if the courts are satisfied that directors have exercised their powers in good faith based on reasonably formed opinions, the courts will not set aside their actions. This rule, often referred to as the business judgement rule, has been considered extensively by the Delaware courts in the take-over cases. See J. Howard "Takeover Battles and The Business Judgment Rule: Recent American Case Law Development" (1985), 11 CBLJ 445 and R. Franklin Balotti and Jesse A. Finkelstein, The Delaware Law of Corporations and Business Enterprises (Clifton, N.J.: Prentice Hall, 1988), p.70.1 ff. In the case of Palmer v. Carling O'Keefe Breweries of Canada Ltd. et al. (1989), 41 BLR 128 (Ont HC), counsel for the corporation unsuccessfully invoked the business judgement rule to insulate from review the conduct of directors at pp. 136-137. A like result met counsel for the dissenting shareholders in Brant Investments Ltd. v. KeepRite Inc. (1991), 3 OR (3d) 289 at pp.319-321.

⁷¹ Dickerson Report, vol. I, paragraph 241, p. 82.

judges".⁷² This approach to the development of the law would be adopted in respect of shareholders rights also.

Although the Dickerson Report lacked an explicit statement of directors' duties to shareholders, it recommended the continuation of the recently implemented rules regarding insider trading and take-over bids, rules which were intended, in part, to protect shareholders from directors' misconduct. Additionally, the Task Force recommended the implementation of a new shareholder remedy which came to be known as the "oppression remedy". The Task Force called the draft provisions which outlined the oppression remedy their "most significant and far-reaching proposals".⁷³ This remedy, like the remedy for use of "specific confidential information...that, if generally known, might reasonably be expected to affect materially the value of the security...",⁷⁴ may be used by shareholders in closely held corporations. These remedies help overcome the gap between the highly regulated statutory fiduciary obligations in "take-over bid" and insider trading situations and the unregulated world of private company transactions.

Although a review of statutory shareholder remedies is beyond the scope of this paper, the Task Force's views about shareholder remedies are central to evaluating the development of a Canadian common law of directors' fiduciary duties to shareholders. The Task Force believed that it was the role of the courts to develop this area of the law as can be seen in the following passage:

[T]he remedies provided in the *Draft Act* recognize that corporation law --and particularly the duties of officers,

⁷² Loc cit. The Task Force was here quoting with approval Professor L.C.B. Gower.

⁷³ Ibid, paragraph 23, p. 7.

⁷⁴ CBCA, s. 131(4), OBCA, s. 138(5), cf. OSA, s.76.

directors and dominating shareholders of corporations --is in a very fluid state, reflecting the uncertain role or identity of the business corporation in contemporary society. For this reason we have frequently established only very broad quality standards of conduct (e.g., s. 9.19 referring to duties of directors and officers and s. 19.04 relating to "oppressive or unfairly prejudicial" conduct of management or dominant shareholders), permitting the courts to determine whether there has been failure to comply with those standards, that is, to continue to develop the common law of responsibility of corporate management unhampered by the legal fetters created at a time when courts were preoccupied with enforcing "democratic" structures --particularly voting power --as the one real object of the law.⁷⁵

(Emphasis added.)

Much of this development, the Task Force believed, would be instigated by shareholders if they were permitted to seek redress for their complaints. In this regard, the Task Force stated the following:

The major premise of this Part is that a corporations Act should be largely self-enforcing by civil action initiated by the aggrieved party, not by severe penal sanctions or sweeping investigatory powers. If this policy is not adopted, it is our opinion, given the state of the common law, that we must continue to rely on ever broader powers of investigation as a means to remedy corporate ills, which become increasingly complex as businesses become more and more sophisticated.⁷⁶

(Emphasis added.)

⁷⁵ Dickerson Report, vol. I, paragraph 477, pp. 158-159.

⁷⁶ Ibid, paragraph 479, p. 160.

Although the Task Force was apparently disappointed with "the state of the common law" regarding minority shareholder rights, they also believed that if the courts were given the opportunity to develop the law of directors' and insiders' fiduciary duties to shareholders, the law would so develop. Accordingly, they stated the following:

By giving the court wide discretion to consider the pertinent facts [in respect of the effect of shareholder ratification of a matter] and by barring the court from following a simplistic path such as applying the shareholder ratification rule, we in effect compel the court to adjudge the issue on its merits. Implicit in this policy is the premise that dominant shareholders, who are in a position to control management, owe a fiduciary duty to minority shareholders comparable to the duty that directors and officers owe to the corporation. This policy constitutes a major divergence from the English common law, but it is clearly a corollary of the U.K. Companies Act, s. 210 and of the Draft Act, s. 19.04. Moreover, this approach has long been commonplace in U.S. courts, both state and federal.⁷⁷

(Emphasis added.)

Was the Task Force's reliance on the courts "to develop the common law of responsibility of corporate management" well placed? Could the courts develop a unified set of principles governing directors' and insiders' duties to shareholders? Could they jettison the rule in Percival v. Wright and consistently apply a set of fiduciary principles? Unfortunately, the development of this area of the common law has been slow and inconsistent as we shall see in Chapter 5.

⁷⁷ Ibid, paragraph 487, pp. 164-165.

Directors' Responsibility to Manage

The fundamental duty of directors is expressed in s. 102(1) for the CBCA which states, "Subject to any unanimous shareholder agreement, the directors shall manage the business and affairs of a corporation".⁷⁸ Subsection 86(1) of the *Canada Corporations Act*,⁷⁹ which governed federally incorporated business corporations prior to the proclamation of the CBCA, required the board of directors to manage the company's "affairs". To this responsibility the Task Force added the requirement that the directors also manage "the business" of the corporation.⁸⁰ When Parliament considered the Task Force's draft legislation, the concept of "affairs" was changed from the broad meaning it had under the *Canada Corporations Act*. Although the directors' responsibility to manage the "affairs" of the corporation does not appear to have been specifically considered by the Task Force, Parliament significantly narrowed the meaning of the word "affairs" and defined it in s 2(1) of the CBCA as follows:

"affairs" means the relationships among a corporation, its affiliates and the shareholders, directors and officers of such bodies corporate but does not include the business carried on by such bodies corporate.⁸¹

By interpolation of the term "affairs" into s.102(1) of the CBCA, directors are given the responsibility of managing the relationship between the corporation and its shareholders in addition to their responsibility to manage the corporation's business.

⁷⁸ The comparable provision in the OBCA is s. 115(1).

⁷⁹ RSC 1970, c. C-32.

⁸⁰ Dickerson Report, v.II, s. 9.01.

⁸¹ The identical provision is found in the OECA, s.1(1).

The only Canadian case in which the term "affairs" has been considered is the 1984 Ontario Court of Appeal decision in Sparling et al. v. Royal Trustco Ltd. et al.⁸² The case arose from the unsuccessful take-over bid by Campeau Corporation for Royal Trustco Ltd. The directors of Royal Trustco Ltd. sent a circular to the corporation's shareholders as required by the CBCA.⁸³ It was alleged by the Director appointed under the CBCA that the directors of Royal Trustco Ltd. had omitted material facts from their circular to shareholders. The shares of Royal Trustco Ltd. increased in price on the stock market while the bid was on-going and decreased in price when the bid was eventually withdrawn. The Director alleged that some shareholders of Royal Trustco Ltd. would have sold their shares at high prices in the stock market if the directors had not issued a deficient circular. The Director sought a remedy for these unnamed shareholders pursuant to ss. 205(3) and 241 of the CBCA. In considering whether the facts of the case fell within the ambit of the statutory oppression remedy, Cory J.A., as he then was, said:

In my view, a takeover bid comes within the concept of "affairs" of the corporation as referred to in s. 234(2)(b) [now s. 241 (2)(b)]. Such a bid is concerned with the control of the corporation which must be considered a vital affair of that corporation.⁸⁴

The failure of the directors to disclosure "all other material facts known to the directors or officers of the offeree corporation" in the directors' circular to shareholders, as required by s.68(s) of the Canada Business Corporations Regulations was, therefore, contemplated by s.241(2)(b) of the CBCA, which states, in the relevant parts, the following:

⁸² See Footnote 5.

⁸³ CBCA, s. 201(1).

⁸⁴ Footnote 5, OAC 279, p. 286.

241.(2) If, on an application under subsection (1), the court is satisfied that in respect of a corporation...
(b) the business or affairs of the corporation...have been carried on or conducted in a manner...that is oppressive or unfairly prejudicial to or that unfairly disregards the interest of any security holder..., the court may make an order to rectify the matters complained of.

(Emphasis added.)

It should be noted that the decision of the Ontario Court of Appeal was appealed to the Supreme Court of Canada. The Supreme Court affirmed the decision of the Ontario Court of Appeal, saying, "[A]ll the issues raised in this appeal were fully and correctly dealt with by the Court of Appeal, speaking through Cory J.A."⁸⁵

The responsibility of the directors to supervise the affairs of the corporation has been extensively considered by Delaware courts.⁸⁶ As in Sparling, the Delaware cases arose from directors' response to takeover activity. Balotti and Finkelstein state, "These cases read the words 'and affairs' in Section 141(a) [of the Delaware General Corporation Law] as giving a board of directors additional power to act in areas which are beyond the scope of the directors' duties in guiding the corporation's everyday business."⁸⁷ Where the legitimate interests of shareholders require protection, as in take-over bids, Parliament has enacted specific obligations on directors such as the obligation to issue a directors' circular and a general obligation to supervise the affairs of the corporation. These duties should be viewed as statutorily imposed fiduciary duties in favour of shareholders since, pursuant to s. 122(1)(a) of the CBCA, "[e]very director...in exercising his powers and discharging his duties shall (a) act

⁸⁵ Sparling v. Royal Trustco Ltd., [1986]2 SCR 537, at p. 538.

⁸⁶ See Balotti and Finkelstein, op cit., p.45 ff.

⁸⁷ Ibid, p. 46.

honestly and in good faith..."⁸⁸ These powers are to be exercised and duties discharged "with a view to the best interests of the corporation".⁸⁹ This responsibility does not preclude the directors' responsibility for acting in the interest of shareholders. Rather, the words "with a view to the best interests of the corporation" diminish the extent to which the directors must act in the best interests of the corporation. By use of this phrase, Parliament has indirectly delineated the role which directors must assume with respect to the shareholders of their corporations.

The courts, in various decisions, have long recognized that directors have a general duty to act in the interests of shareholders. Haldane L.C. in Allen v. Hyatt⁹⁰ noted that a director's duty was primarily to the corporation. He made clear, however, that a director is expected to act in the interests of shareholders. This general, though secondary, duty to shareholders may be subject to some exceptions, since as the Lord Chancellor equivocally stated, "It may be that in circumstances such as those of Percival v. Wright...[a director] can deal at arm's length with a shareholder."⁹¹ More recently, in the British Columbia Supreme Court case of Teck Corporation Ltd. v. Millar et al., Berger J. stated, "The classical theory is that the directors' duty is to the company. The company's shareholders are the company".⁹² In this case the directors of Afton Mines Ltd. (N.P.L.) had used their powers to allot and issue shares to dilute the shareholdings of the majority shareholder, an unwanted corporate suitor. There was weighty authority for the proposition that the directors had exercised their powers for an improper purpose and that the share allotment and any resulting issuance should be set aside.

⁸⁸ The comparable OBCA provision is s. 134(1)(a).

⁸⁹ CBCA, s. 122(1)(a); OBCA, s. 134(1)(a).

⁹⁰ (1914), 17 DLR 7, 30 TLR 444 (JCPC) at DLR, p.11

⁹¹ Ibid, p.12.

⁹² [1973]2 WWR 385, 33 DLR (3d) 288 at p.313.

Berger J. concluded that the directors had good reasons for acting as they did and that their actions would enure even to the benefit of the majority shareholder whose shareholdings would be diluted. In reaching this conclusion, Berger J. expressed the following caution about directorial action against shareholders:

I do not think it is sound to limit the directors' exercise of their powers to the extent required by Hogg v. Cramphorn Ltd., [1967] Ch.254, [1966] 3 W.L.R. 995, [1966] 3 All E.R. 420. But the limits of their authority must be clearly defined. It would be altogether a mistake if the law, in seeking to adapt itself to the reality of corporate struggles, were to allow the directors any opportunity of achieving an advantage for themselves at the expense of the shareholders. The thrust of companies legislation has brought us a long way since Percival v. Wright, [1902] 2 Ch.421.⁹³

This view that directors must act in the interest of "the company as a whole" which means in the interest of "all of the shareholders, taking no one sectional interest to prevail over the others" was recently adopted by the Ontario Supreme Court, as it was then, in Palmer v. Carling O'Keefe Breweries of Canada Ltd. et al.⁹⁴ That this view has survived from the pre-CBCA time of Teck v. Millar is somewhat surprising; the corporation is, after all, an entity entirely separate from its shareholders. In Palmer the directors of Carling O'Keefe Limited acted solely in the interest of the sole common shareholder and to the detriment of the holders of two other classes of shares by authorizing the amalgamation of their corporation with the

⁹³ Ibid, p.315.

⁹⁴ (1989), 41 BLR 128 at p.138. For a discussion of the case law on the phrase "bona fide for the benefit of the company as a whole" in the context of shareholder voting rights, see B. Welling, Corporate Law in Canada: The Governing Principles, 2nd ed. (Toronto: Butterworths, 1991), pp.627 ff. Welling argues that the case law in this area is "rather confused and contradictory".

common shareholder, thereby making a "gratuitous assumption" of the shareholder's \$400 million debt.⁹⁵ The reference to all shareholders in the judgement seems superfluous since the directors' conduct in authorizing the amalgamation could be attacked on the basis that it was not in the best interests of the corporation itself. The detriment to the preference shareholders was further reason for objecting to the amalgamation. The reference to all of the shareholders is a testament, however, to the intensity with which some members of the judiciary view the core duty of directors, that is to act in the best interests of all shareholders as well as in the best interests of the corporation.

⁹⁵ Ibid, p.134.

CHAPTER 4

THE COMPULSORY ACQUISITION CASES: JUDICIAL RESPONSE TO CORPORATE GOVERNANCE LEGISLATION

In 1934, the Canadian Parliament enacted a compulsory acquisition provision in the federal corporations statute.¹ Several provinces enacted similar provisions in their *Companies Acts*.² As the Honourable C.H. Cahan, Secretary of State, noted in the debates preceding the enactment of the federal provision, "We followed...[the English] act in the first place and we are now endeavouring to maintain conformity in order that the English decisions may provide guidance to our legal fraternity."³ The English decisions were, in fact, influential in determining the Canadian cases which arose under the various compulsory acquisition provisions.

The compulsory acquisition provisions allowed a company to acquire the shares of any dissenting shareholder of a target company where the holders of not less than nine-tenths of the shares of the target company agreed to transfer their shares to the purchasing company. The dissenting shareholder's shares were to be acquired on the same terms as those on which the other shareholders had transferred their shares. This right to acquire a dissenting shareholder's shares was subject to the court's jurisdiction to "order otherwise" upon an application by the dissenting shareholder.

¹ The Companies Act, 1934, 24-25 Geo V, c. 33, s. 124.

² Select Committee on Company Law: 1973 Report on Mergers, Amalgamations and Certain Related Matters (Toronto: Legislative Assembly, 1973) p.43.

³ Dominion of Canada Official Report of Debates - House of Commons, 1934 (Ottawa: King's Printer, 1934, p.3465.

The compulsory acquisition cases cast considerable doubt on the Canadian securities and corporate law reformers' faith in the courts to develop the law of fiduciary relations within corporations. These cases demonstrate a very limited willingness by Canadian judges to venture beyond the confines of corporations statutes. The law reformers should have taken particular notice of this jurisprudence because the compulsory acquisition of untendered securities is often the last step of a successful take-over bid. While these cases show the limitations of English and Canadian judges, they also show another source of the law, commercial morality. Although the judges seem inclined to resist the compulsory acquisition of private property, they are powerless to do so. As a substitute for the values and rectitude which they would have preferred but considered themselves powerless to impose, Canadian courts imposed requirements for the punctilious observance of the statutory provisions, an approach which betokens stronger views of commercial morality which have been voiced in recent fiduciary duty cases.

Rathie v. Montreal Trust Co. and British Columbia Pulp & Paper Co.

The first significant Canadian decision under the compulsory acquisition provisions was the 1953 decision of the Supreme Court of Canada in Rathie v. Montreal Trust Co. and British Columbia Pulp & Paper Co.⁴ This decision yielded both a mundane application of the statute and a lofty, if unclear, statement of principle. In this case, Montreal Trust Co. had made an offer to purchase all shares of British Columbia Pulp & Paper Company, Limited. The offer was dated December 1, 1950. The offer was conditional on acceptance on or before December 15, 1950, by the holders of not less than ninety per cent of the shares. The holders of more than 90% of the shares accepted the offer on or before December 15, 1950. The offeror then sought to acquire the shares of the other shareholders.

⁴ [1953]2 SCR 204, [1953]4 DLR 289.

The approval of an offer by the holders of nine-tenths of the shares of a company contemplated by subsection 124(1) of the *Companies Act, 1934* was to be received "within four months after the making of the offer". The Supreme Court of Canada unanimously, though in two separate opinions, determined that the subsection "contemplates that the offer shall be open for acceptance for a period of 4 months by those to whom it has been made."⁵ Locke J. concluded, "As, in my opinion, the offer made did not comply with the terms of the subsection, the respondents were not entitled to invoke the assistance of the Court to compel the dissentients to transfer their shares."⁶ Locke J. observed that "[i]n a matter involving what amounts to a forced sale of the shares of the dissentients, there must clearly be strict compliance with the terms of the section."⁷

Rand J., in separate concurring reasons, looked outside of the four corners of the statute. Like his brother judges, Rand J. appreciated the strong power which section 124 of the *Companies Act, 1934* bestowed on those who were dealing with shareholders of the target corporation. His appreciation of this power led him to conclude, "This comparatively new power by which a majority may coerce a minority is one to be exercised in good faith and with the controlling facts available to shareholders to enable them to come to a decision one way or the other."⁸ He, therefore, charged the "majority" with the general obligation to act in good faith and with the specific obligation to disclose "the controlling facts". Both of these obligations are characteristic of duties imposed on fiduciaries. Rand J.'s reading of the compulsory acquisition provision impressed that provision with a fiduciary gloss. But, who did he have in mind when he referred to "a majority"? Was he referring to the other shareholders

⁵ Per Locke J at DLR, p. 295.

⁶ Ibid, p. 296.

⁷ Ibid, p. 294.

⁸ Ibid, p. 298.

of the target corporation or did he have in mind other actors such as the directors of the offeror or target corporations? Unfortunately, his reasons are not clear on this point although in this particular case the directors of the target corporation had been by-passed as the offer had been sent directly to the shareholders. Nonetheless, Rathie stands as an example of the courts' willingness both to construe strictly corporate governance legislation and to impose fiduciary-like obligations on those corporate actors whose powers over minority shareholders are derived from statute.

Esso Standard (Inter-America) Inc. v. J.W. Enterprises Inc.

By the time the Supreme Court of Canada considered the federal compulsory acquisition provision for the second time, courts on both sides of the Atlantic had largely retreated from the lofty fiduciary principles articulated by Rand J. in Rathie. Judson J. dispassionately summarizes the development of the case law in the following passage from Esso Standard (Inter-America) Inc. v. J.W. Enterprises Inc. et al. and Morrisroe:

The reported cases on the sections, both in England and Canada, have been comparatively few. There was little guidance to be found in the legislation itself on the principles to be applied in considering a dissenting shareholder's application for an "order otherwise" under the section. These were first formulated by Maugham, J., in Re Hoare & Co. (1933), 150 L.T. 374, and followed - it seems to me with increasing emphasis on the difficulties in the way of a dissenting shareholder - in three other cases. These were Re Evertite Locknuts Ltd., [1945] 1 Ch. 220; Re Press Caps Ltd., [1949] 1 Ch. 434; and Re Sussex Brick Co., [1961] 1 Ch. at p.289n (decided in 1959 but reported in 1961). The matter is summarized in Palmer's Company Law, 20th ed., p.691:

When an application is made to the court by a shareholder who alleges that the terms are not fair, the onus is upon the applicant to establish his allegation. The court will

attach considerable weight to the fact that the large body of shareholders have accepted the offer. An application by a shareholder must allege unfairness: it is not sufficient merely to say that insufficient information was given: discovery will not be allowed, upon such an application, to enable the shareholder to establish his case.⁹

The Supreme Court of Canada in Esso Standard did not retard the general retreat from the principles articulated by Rand J. in Rathie. It did, however, close one abuse of the compulsory acquisition procedure. Esso Standard (Inter-America) Inc. ("Esso Standard") had sought all of the shares of International Petroleum Company Limited ("International"). Close to ninety-seven per cent of International's shares were held by Standard Oil Co. ("Standard"). Standard also owned all of the shares in Esso Standard. When Esso Standard offered to buy the shares of International at \$45.00 (U.S.) per share, Standard and certain other shareholders accepted. The holders of less than ninety per cent of the "free shares",¹⁰ however, accepted the offer within the time frame stipulated by the statute. Judson J, for the Court, concluded, "I would reject the appeal and hold that the section contemplates the acquisition of 90% of the total issued shares of the class affected and that this 90% must be independently held."¹¹

As in Rathie, the Supreme Court of Canada in Esso Standard stood as a guardian for minority shareholders in compulsory acquisition cases. As Judson J. notes, if the acceptance of an offer by shareholders related to the offeror is counted in determining the level

⁹ [1963] SCR 144, 37 DLR (2d) 598, pp. 601-602.

¹⁰ DLR, p. 600.

¹¹ Ibid, p. 604.

of shareholder acceptance of the offer, "the whole proceeding...is a sham with a foregone conclusion, for the purpose of expropriating a minority interest on terms set by the majority."¹² The courts, therefore, would not approve a compulsory acquisition transaction where the required level of acceptance is based on the acceptance of a shareholder who is related to the offeror.¹³ This principle shows that the courts view the procedures of corporate governance created by the legislatures as being imbued with and to be used with probity. Unfortunately, such a view stands as a rather diffuse guide to conduct for corporate actors. In the absence of good faith, however, the courts required little of the majority in compulsory acquisition matters and, in most cases, placed a heavy onus on the dissenting shareholder.

Re Hoare & Co.

It is unclear to what extent the "difficulties" confronting dissenting shareholders to which Judson J. referred in Esso Standard are attributable to legislators and to what extent they are attributable to the courts. Certainly, the judicial gloss on the compulsory acquisition provisions restricted the ambit of the courts' inquiry into the merits of the matter and set a high evidentiary standard for shareholders who sought relief. These observations may be discerned from the following passage taken from the first reported compulsory acquisition case, Re Hoare & Co., Ltd.:

I have some hesitation in expressing my view as to when the court should think fit to order otherwise. I think, however, the view of the legislature is that where not less than nine-tenths of the shareholders in the transferor company approve the scheme or accept the offer, prima facie, at any rate, the offer must be taken to be a proper one...Accordingly, I think it is manifest that the reasons

¹² Ibid, p. 603.

¹³ Ibid, p. 604.

for inducing the court to "order otherwise" are reasons which must be supplied by the dissentients who take the step of making an application to the court, and that the onus is on them of giving a reason why their shares should not be acquired by the transferee company....[P]rima facie the court ought to regard the scheme as a fair one inasmuch as it seems to me impossible to suppose that the court, in the absence of very strong grounds, is to be entitled to set up its own view of the fairness of the scheme in opposition to so very large a majority of the shareholders who are concerned. Accordingly, without expressing a final opinion on the matter, because there may be special circumstances in special cases, I am unable to see that I have any right to order otherwise in such a case as I have before me, unless it is affirmatively established that, notwithstanding the views of a very large majority of shareholders, the scheme is unfair.¹⁴

It is interesting to note that although Re Hoare was decided before Rathie, the Supreme Court did not refer to the decision in Rathie, but did refer to it in the Esso Standard decision.

Maugham J. in Re Hoare takes the legislature to have determined that once nine-tenths of the shareholders have accepted the offer, the offer is "proper". It follows from this reading of the statute, that the courts must exercise restraint in reviewing the offer; a restriction to the ambit of the courts' review which Maugham J. adopts without criticism. In addition to developing the view that courts are not to subject offers to their normative standards of review, however, Maugham J. sets a high evidentiary standard for interference by the courts by declaring that dissenting shareholders have the onus to show the courts why "the scheme is unfair".

¹⁴ [1933] All ER Rep 105, p. 107, 150 LT 374 (Ch).

Maugham J.'s views are completely at odds with the fiduciary-like standards which Rand J. held to be appropriate in compulsory acquisition cases in Rathie. A fiduciary is always accountable for his conduct. Thus, by analogy, a representative of the "majority" should show the probity of the process and the fairness of the result. The beneficiary of a fiduciary duty is not required to show how he has been mistreated or the extent of any mistreatment. Thus, arguably, there should be no onus on the dissenting shareholder. Finally, the courts should not be reluctant to exercise their jurisdiction to review the conduct of fiduciaries; neither should they restrict their jurisdiction. Nonetheless, Maugham J.'s views, tacitly approved by the Supreme Court of Canada in Esso Standard, have been followed in several Canadian compulsory acquisition cases. In Re Shoppers City Ltd. and M. Loeb, Ltd., the dissenting shareholder failed in his application because he did not show that the price offered was unfair.¹⁵ Similarly, in Re Dad's Cookie Co. (B.C.) Ltd. et al., the dissenting shareholder failed to "affirmatively establish that the price is unfair".¹⁶ To like effect was Re Canadian Allied Property Investments Limited.¹⁷

Gething v. Kilner

In 1971, the English Chancery Court in Gething et al. v. Kilner et al., echoed the Supreme Court of Canada's early concerns about the fairness of the compulsory acquisition procedure.¹⁸ The Court imposed common law fiduciary duties on directors of an offeree corporation to make disclosure and not to mislead shareholders in a take-over situation. Brightman J. reasoned that, particularly in view of the fact that dissenting shareholders' shares

¹⁵ [1969] 1 OR 449, 3 DLR (3d) 35, p. 39 (Ont HC).

¹⁶ (1969), 7 DLR (3d) 243, p. 255 (BCSC).

¹⁷ (1977), 3 BCLR 366, 78 DLR (3d) 132 (BCSC).

¹⁸ [1972] 1 All ER 1166, [1972] 1 WLR 337.

could be compulsorily acquired, shareholders in a take-over situation were in a position of vulnerability which required the imposition of fiduciary duties on the directors of the offeree corporation. He said:

I accept that the directors of an offeree company have a duty towards their own shareholders, which in my view clearly includes a duty to be honest and a duty not to mislead. I also accept that a shareholder in an offeree corporation may be prejudiced if his co-shareholders are misled into accepting the offer. I express this view because as soon as the appropriate percentage of shareholders have been misled and have assented, the minority become subject under s 209 of the Companies Act 1948 to statutory powers of compulsory purchase. It therefore seems to me that a minority could complain if they were being wrongfully subjected to that power of compulsory purchase as a result of a breach of duty on the part of the board of the offeree company.¹⁹

Gething v. Kilner shows that fiduciary principles have some utility in protecting shareholders, but it also demonstrates the tardiness with which the common law deals with pressing corporate law issues. Only in 1971 do we have some particularity to the fiduciary principles which Rand J. articulated in Rathie. The common law expressed in Gething v. Kilner is, like Rand J.'s reasons in Rathie, deficient when considered in the light of the needs of shareholders. Gething v. Kilner contains a fine expression of principle, but little detail about the obligations of directors. For example, the decision is silent concerning the specific information which should be disclosed as well as the appropriate form and time for disclosure. The statutory and regulatory take-over bid rules discussed in Chapter 3 give effect to the

¹⁹ Ibid, All ER, p. 1170.

fiduciary duties expressed in Gething v. Kilner by adding clarity, detail and, hence, enforceability, to those duties.

The compulsory acquisition cases may be subjected to two criticisms. First, although they reflect a concern for the integrity of the process, they were a poor guide to conduct for those who were expected to conduct themselves in good faith. Until Gething v. Kilner, the case law was not even clear as to the identity of those who were to so conduct themselves. Secondly, the courts completely resiled from any substantive review of the transactions. Though the courts were willing to impose fiduciary-like standards on the "majority" or on directors, they did not hold these fiduciaries to account. Thus, the cases yielded disparate results. They show the gulf which may be created between corporate governance legislation and fiduciary principles. Finally, they illustrate the difficulty of grafting evolving judge-made law on to corporate law.

CHAPTER 5

RECENT DEVELOPMENT OF DIRECTORS' AND INSIDERS' FIDUCIARY DUTIES TO SHAREHOLDERS

As we have seen, the proposition associated with Percival v. Wright,¹ that directors are not in a fiduciary relationship with shareholders, was unacceptable to securities and corporate law reformers. Although the law relating to fiduciaries had developed in a manner which provided guidance to law reformers in cases such as Regal (Hastings), Ltd. v. Gulliver,² a regulatory structure for ensuring that directors and insiders maintained a proper regard for the interests of shareholders was considered necessary. Therefore, reformers developed regulatory codes relating to take-over bid transactions and insider trading transactions. These codes required disclosure of a wide variety of information which could be used by shareholders in determining whether or not to tender to a take-over bid and whether or not to take action in respect of an insider trade.

Despite the existence of elaborate statutory protection for shareholders selling their shares in these regulated transactions, the purchase and sale of shares in closely-held corporations and directorial conduct outside of the take-over bid and insider trading contexts remain free from such regulation. As Cory J.A., as he then was, was moved to remark in Beji et al. v. Source Data Control Ltd. et al., a case involving the private sale of shares of a closely held corporation, "It would seem anomalous that there should be complete protection of minority shareholders of a publicly held corporation, and no protection in a private corporation."³

¹ [1902] 2 Ch 421.

² [1942] 1 All ER 378 (HL).

³ (1988), 40 BLR 10 at p.25, 66 OR (2d) 78.

Anomalous from a corporate law perspective, yes, but not from the perspective of securities law which focuses on protecting the integrity of the capital markets. To recapitulate the discussion in Chapter 3, the take-over bid provisions of the OBCA and the OSA apply only to the securities of public companies.⁴ The provisions of the CBCA, OBCA and the OSA do not apply unless a specified percentage of a corporation's securities are sought.⁵ Another significant limitation on the ambit of take-over bid legislation is the exempt offer.⁶ Similarly, insider trading need only be reported in limited situations. Under the CBCA only transactions involving securities of "distributing corporations"⁷ must be reported while the OSA insider trading and self-dealing provisions apply primarily to "reporting issuers".

In this Chapter, we examine several recent cases in which shareholders have asserted that fiduciary duties are owed to them by directors and insiders of the corporation. The cases in which such claims have been successful involve the purchase and sale of shares between a shareholder and a director or insider. Attempts have been made by shareholders to extend the claim that directors are in a fiduciary relationship to shareholders beyond the context of a

⁴ Pursuant to s.186(1) of the OBCA, the take-over provisions only apply to "offering corporations" which are defined in OBCA, s.1 as corporations which have filed a prospectus or similar document under the OSA and the securities described therein are still outstanding, and corporations whose securities are listed on the Toronto Stock Exchange. The "private company" exemption from the take-over bid provisions of the OSA is found in s. 92(1)(d).

⁵ A "take-over bid" is defined under s.194 of the CBCA to occur only when an offeror seeks or holds and seeks shares which will cumulatively exceed ten percent of any class of issued shares of a corporation. Under s.187(2)(g) of the OBCA, a "take-over bid" occurs when ten per cent or more of the "voting securities" are sought or held and sought. Under s.88(1) of the OSA, a "take-over bid" occurs when an offeror seeks "voting securities" or "equity securities" which, together with the offeror's securities, aggregate twenty percent or more of the class of securities sought.

⁶ See CBCA, s.194 "exempt offer"; OSA, s.92.

⁷ CBCA, s.126(1).

purchase and sale of shares. Such attempts have failed to date. We shall see that Percival v. Wright has come to be disclaimed by the courts, although its vestiges remain. Some courts have imposed fiduciary duties on directors in share purchase and sale transactions. Although some generalizations can be made about the types of situations in which fiduciary duties will be imposed, judicial discretion seems to be a major factor in these decisions. The application of the law in this field, subject to the perceptions and value judgments of judges, is, therefore, uncertain.

Another element of uncertainty is the scope and effect of certain securities and corporate law reforms on common law relationships. It appears to be the view of the Ontario Court of Appeal that the enactment of statutory oppression remedies has arrested the development of the law of fiduciary obligations "in the corporate context".⁸ Provisions governing insider trading based on specific confidential information may have decreased the need to assert that insiders are subject to common law fiduciary duties in favour of shareholders.⁹ But the case law does not yet make these matters clear. For example, in Roberts et al. v. Pelling et al., Berger J. states that even where a director and controlling shareholder negotiates the redemption of a minority shareholder's shares for a price which is less per share than the undisclosed price for which the director had agreed to sell and, following the redemption, sold his shares, at common law, "there is no fiduciary obligation as between shareholders, and no general fiduciary obligation owed by a director to shareholders."¹⁰ The plaintiff shareholder recovered modest damages in that case on the basis of the director's/majority shareholder's

⁸ Brant Investments Ltd. et al. v. KeepRite Inc. et al. (1991), 3 OR (3d) 289 at p.301.

⁹ The plaintiff shareholder was granted a modest remedy on this basis in Roberts et al. v. Pelling et al. (1981), 16 BLR 150 (BCSC) while his claim for relief on the basis that the offending director breached his fiduciary duty to the shareholder was rejected.

¹⁰ Ibid, p.153.

trading using specific confidential information. Paradoxically, Berger J. seems unable or unwilling to consolidate his thoughts about the rights of shareholders, for approximately a decade earlier in Teck Corporation Ltd. v. Millar et al., he had declared, "The thrust of companies legislation has brought us a long way since Percival v. Wright, [1902]2 Ch.421."¹¹

The cases indicate that there are fact situations where commercial morality demands a remedy for injured shareholders but where the statutory oppression remedy and the remedy for insider trading based on specific confidential information may not be available. A typical situation is where a director sells his shares to a third party for a higher price than other shareholders obtain for their shares.¹² Is the fact that shareholders could contract with each other to disclose such sales before they occur relevant to determining whether fiduciary duties should be imposed on the shareholder/director who sells for a higher price? In the absence of an agreement, should such a shareholder/director be required to share the benefit of his commercial insights, contacts and action? Can such insights, contacts and action be separated from the information about the corporation and its opportunities which the director must not appropriate and which a shareholder, unaided by someone with access to such information, cannot appropriate? Numerous issues such as these remain to be satisfactorily dealt with by the courts.

Coleman v. Myers

Coleman et al. v. Myers et al.¹³ represents the marriage of the articulation of a principle of law that directors can owe fiduciary duties to shareholders in appropriate

¹¹ [1973]2 WWR 385, 33 DLR(3d) 288 at p. 313.

¹² See the discussion of Dusik v. Newton and Bell v. Source Data Control Ltd. below

¹³ [1977] 2 NZLR 225 (SC); [1977] 2 NZLR 297 (CA).

circumstances to facts which constituted one set of such circumstances. In 1976 the New Zealand Supreme Court considered the fiduciary relationship between directors and shareholders in a take-over situation. The trial judge held, as a matter of law, that directors owe fiduciary duties to shareholders when they are purchasing shares directly from shareholders. He found, however, no factual basis for holding the directors liable in the case. The decision was reversed on appeal to the New Zealand Court of Appeal. The appeal court was of the view that directors' common law fiduciary duties to shareholders may be based on the circumstances of the case and the relationship between the director and shareholders. Such duties were not absolute, however, even in a situation where a director purchases shares directly from a shareholder. The appeal court nevertheless reversed the trial judge based on its assessment of the facts of the case.

The Factual Background

Michael Peirs Coleman and Anthony Clive Coleman (the "plaintiffs") acquired the beneficial interest in slightly more than one percent of the issued and outstanding shares of Campbell and Erenfried Co. Ltd. ("C & E") in early 1972. C & E was "an old established private company in which, like the plaintiffs, many of the other shareholders, individually or through trusts, were relatives".¹⁴ The plaintiffs sued two of these relatives, Arthur Douglas Myers and Kenneth Ben Myers for an alleged breach of fiduciary duties owed to them in connection with a take-over bid for all of the shares of C & E which was made by Paddington Holdings Ltd. ("Paddington"), A.D. Myers' holding company. How might this have happened?

C & E was incorporated in 1897 as a hotel owner and wine merchant. Very early in the history of the corporation, the administration of the corporation was taken over by Arthur Myers. He was the father of the second defendant, K.B. Myers, and grandfather of the

¹⁴ [1977] 2 NZLR, p.229.

first defendant, A.D. Myers. K.B. Myers became chairman and managing director of C & E in 1933. At the time of the take-over bid, K. B. Myers had restricted his activities to being the Chairman of C & E and A. D. Myers had become its managing director.

By 1960, most of the corporation's shareholders were third generation descendants of Sir Arthur Myers. Many of these shareholders relied on their dividend income from the C & E shares. At about this time, C & E came under pressure from the Licensing Control Commission to renovate and improve many of its hotels. The C & E shareholders were unable to provide the capital required to complete this work. Moreover, it appears that debt financing would have impaired the dividend income upon which several C & E shareholders relied. Therefore, it was decided to sell several of C & E's hotels to New Zealand Breweries Ltd. Further, C & E merged its wine and spirits business with New Zealand Breweries Ltd. to form New Zealand Wines and Spirits Ltd. ("NZWSL"). Some properties were retained by C & E, the most valuable being the Strand-Coburg property in Auckland, a business centre and hotel which stood side by side.

Once the arrangements for restructuring the business of C & E were completed in 1970, C & E had considerable "free assets" and, as Mahon J., the trial judge, notes, "[t]he question arose as to what should be done with the capital reserves of the company."¹⁵ Various plans for making distributions to shareholders were considered. While the two directors had the interests of the shareholders in mind, they were also interested in the situation of A.D. Myers. He was a young man who had recently returned to New Zealand from studies in the United States. He was already active in the management of C & E as its managing director and was also managing the NZWSL business. He would eventually become the holder of a block of C & E shares since he was the residuary beneficiary of more than one of the family trusts, however, he wanted to accelerate the process of acquiring shares of the company. K.B. Myers

¹⁵ Ibid, p.232.

wanted to assist his son in acquiring an interest in C & E sooner than he would under the trust arrangements. On this matter, Mahon J. makes the following observations:

As I read the relevant correspondence, it seems to have been in the mind of Mr KB Myers early in 1971 that a capital dividend of either \$2 or \$3 per share would not only benefit his sisters' trusts by making available cash which could [be] utilized for the benefit of their children, but would also enable funds to be provided to Mr KB Myers from which Mr AD Myers could be assisted to acquire a beneficial interest in C & E.¹⁶

Because of tax implications for a major shareholder in England, it was determined that C & E would not make a capital dividend. "Thus," Mahon J. states, "the situation now resolved itself into a question whether the main shareholders would sell and if so at what price."¹⁷ The directors had retained E.D. Wilkinson, a chartered accountant, whom Mahon J. described as "the doyen of share valuation experts in New Zealand"¹⁸ to value the shares of C & E. He reported in May 1971 that "assuming the proposed cash distribution of \$2 per share in C & E then in contemplation the value of each share should be assessed at \$4.17, and without the proposed cash distribution, the sum of \$2.78."¹⁹ Wilkinson's report was circulated to representatives of major shareholders. Subsequently, steps were taken to sell certain of the C & E properties. Therefore, Mr. Wilkinson was requested to make a further valuation of the C & E shares in November 1971, which valuation was to take into account the value of the sale of these properties rather than their revenue earning value.

¹⁶ Ibid, p.233.

¹⁷ Ibid, p.237.

¹⁸ Loc cit.

¹⁹ Loc cit.

As the trial judge notes, "By this stage it was clear enough that the KB Myers Trust, together with the trusts of his two sisters, were prepared to sell their respective holdings and it was equally clear that Mr AD Myers had decided to acquire a controlling interest in the company if he could."²⁰ To effect this result, A.D. Myers offered to buy the shares of his aunts' trusts in March 1972. In his letter to them, "he adverted to the possibility of reduced dividends from C & E having regard to the commitment of that company in New Zealand Wines and Spirits Ltd" and the possible introduction of a capital gains tax into New Zealand in the near future.²¹ He indicated that "he wanted to have a substantial stake in the business as its managing director" but did not disclose an intention to acquire all of the shares of C & E.²² In support of A.D. Myers' attempt to purchase the C & E shares held by his aunts' trusts were letters from his father, K.B. Myers, to the aunts. By the end of March 1972, agreements had been concluded whereby A.D. Myers had obtained a three-month option to purchase the C & E shares held by his father's and his aunts' trusts as well as the shares of a related holding corporation which also held shares in C & E. These shares represented 68.3 percent of the share capital of C & E. A.D. Myers then wrote to the trustees of the Logan Campbell Trust which held 17.84 percent of the C & E shares. By the end of April, 1972, the Trust had accepted A.D. Myers' offer and granted him an option for the C & E shares it held at \$4.80 per share. The Trust had retained a chartered accountant to appraise the C & E shares. The appraiser noted that the "asset-backing" of the shares was \$6.44 and that if the goodwill associated with NZWSL were taken into account, the asset-backing of the shares would be \$7.50. On an "earnings-yield basis", however, he considered that \$4.80 was a fair price per share and he recommended that the Trust sell at that price.²³

²⁰ Ibid, p.238.

²¹ Ibid, p.240.

²² Loc cit.

²³ Ibid, p.243.

All did not go so smoothly with certain minority shareholders. Mr. G.E. Myers was the holder of a small number of C & E shares and was the third director of C & E. He and the plaintiffs, through their counsel, retained a further share valuation expert to prepare a valuation of the C & E shares. A separate valuation of the Strand-Coburg block and the Victoria Hotel was obtained. This valuation showed that the market value of these properties exceeded their book value by \$205,489.00. This information was utilized in the share valuation report which was prepared with "particular attention to the asset-backing of the shares."²⁴ The report indicated that C & E shares had an asset-backing of \$7.31 per share under certain assumptions and of \$7.75 per share under certain other assumptions. The author of the report agreed with the other appraisers, however, that the market value of the shares on an "earnings-basis" was \$4.80. Perhaps this share valuation fortified G.E. Myers' opposition to the bid. In any event, he made "some observations adverse to Mr. K.B. Myers" and this feuding between the directors lead the majority of shareholders, acting through K. B. Myers, to remove G. E. Myers from the board.²⁵

On June 22, 1972, Paddington delivered written notice of a take-over scheme to C & E. C & E in turn wrote to Mr. Wilkinson to advise him about the statutory notice and to request that he update his valuation of the C & E shares for the board of directors. Mr. Wilkinson was advised of the valuations completed on behalf of the Logan Campbell Trust and G.E. Myers and the plaintiffs. On July 8, 1972, Paddington made its formal offer to the shareholders to purchase all of the C & E shares for \$4.80 per share. Included with the offer document was "the required statutory statement of the directors and also... a copy of Mr. Wilkinson's report of 27 June, 1972."²⁶ In that report, Mr. Wilkinson had observed that "the asset-backing value was not

²⁴ Ibid, p.245.

²⁵ Ibid, p.250.

²⁶ Ibid, p.251.

relevant to the market value in a case where the liquidation of the entire company was not in contemplation"²⁷ He also stated, "I do not think the directors of the company would be holding these cash resources without a good reason"²⁸ The holders of more than 90 percent of the C & E shares accepted Paddington's offer, and on August 4, 1972, a compulsory acquisition notice pursuant to the *Companies Act 1955*, s. 208 was served on the remaining shareholders. Upon receiving that notice, the remaining shareholders agreed to sell their shares.

The total purchase of the C & E shares cost \$5,647,996.00, most of which money had been borrowed. In order to repay the loans, A.D. Myers caused C & E to sell "surplus assets" and these sales attracted "advantageous prices".²⁹ In particular, the Strand-Coburg property was sold shortly after the completion of the take-over bid for \$3,500,000.00, well in excess of its book value. These sales permitted C & E to pay dividends totalling \$6,725,971.00 which was sufficient to repay the loans and to leave A.D. Myers, through Paddington, with a cash profit. C & E, all of the shares of which Mr. Myers held through Paddington, owned a half interest in NZWSL which, some months after the take-over, was valued at \$5,154,364.00. These figures suggested that A.D. Myers had made a profit of \$6,232,339.00 and confirmed the plaintiff's belief that the shares had been acquired "at a gross under-value".³⁰

In the Court of Appeal certain facts which changed the result of the case were highlighted. For example, E.D. Wilkinson's statement that the directors would not be holding cash resources without a good reason was found to be entirely misleading. The statement was

²⁷ *Ibid*, p.250.

²⁸ *Ibid*, p.307.

²⁹ *Ibid*, p.229.

³⁰ *Ibid*, p.230.

rooted in the failure of the directors to disclose their intentions to Mr. Wilkinson. Once made by this respected share valuer, the directors adopted the statement without comment or correction in their circular to shareholders in which they recommended acceptance of the take-over bid. Of these matters, Woodhouse J. states the following:

The statement by Mr. Wilkinson that liquidation was not contemplated was true in the technical sense; but wrong if it could be read to embrace the sort of partial liquidation which might be considered to result from the return to shareholders of a large percentage of the funds standing to their credit. I say that because the intention to make a cash distribution of \$2 per share that was expressed by Sir Kenneth Myers in the letters to his sisters dated 24 May 1971 had been replaced by a subsequent intention to make a larger cash distribution - although only after new shareholders had been substituted for the contemporary shareholders. The directors' intention to distribute does not seem at any stage to have been abandoned: the action upon it was merely to be delayed...

I cannot imagine that the various valuers would have ignored the advice, if they had been given it, that in the present case a large amount of surplus capital (even larger in amount than [sic] the accounts suggested) was not needed within C & E for company reasons; that it had been retained in the interests of one of the two directors as an essential means of making his take-over bid possible; and that decisions had already been taken that the sums involved ought at the convenient moment to be disbursed.³¹

In addition to the directors failure to disclose material facts so as to mislead the shareholders of C & E, A.D. Myers actively misled the plaintiffs and other shareholders

³¹ *Id.*, pp.308-309.

regarding the plans for various C & E assets, particularly the Strand-Coburg property, and the necessity for retaining cash resources when there was "no good reason" to do so and when it had been decided that the cash resources would be distributed once A.D. Myers had obtained all of the C & E shares.³² For example, C & E was not obliged to fund the operations of NZWSL as A.D. Myers had advised shareholders. On the contrary, the company was actually expected to make distributions from profits.³³ Woodhouse J. summarizes much of his view of the evidence on this matter when he observes, "What...[A.D. Myers] said to the Colemans was said for the deliberate purpose of gaining their acceptance of the take-over proposals and in order to avoid confrontation and possible delay".³⁴ A.D. Myers lied to the plaintiffs in order to achieve his objectives.

Cooke J. summarized the evidence of interest to the Court as follows:

I think the evidence shows that there were express oral misrepresentations that Strand-Coburg was going to be kept for the company's head office and that liquid assets were committed; implied written misrepresentations on the latter point in the circulation of the Wilkinson report; non-disclosure of the plan to finance the take-over virtually exclusively from the company's own assets and without the injection of any capital or assets by the first respondent; and non-disclosure of the engagement of property consultants with a view to selling the main free assets and of advice received from them having an important bearing on the value of Strand-Coburg. These

³² Ibid, p.315.

³³ Ibid, p.317.

³⁴ Ibid, p.320,

misrepresentations and non-disclosures are largely interrelated.³⁵

Casey J. notes the effect that the fraud and non-disclosure had on the plaintiffs:

The combined effect of the fraud and non-disclosure left the appellants believing that major assets were not going to be available for distribution under Mr. Myers' control, and they would have no way of reaching them as minority shareholders. Without information about his plans or his ability to use these assets, they had no basis for seeking any substantial increase on the price of \$4.80, based as it was on earnings, and not on partial liquidation. Mr. Ross thought this a fair price on that basis, and he was their advisor.³⁶

Accordingly, they sold their shares in C & E and they did so for prices lower than they otherwise would have accepted.³⁷ The Court held that their injury was caused by a "clear breach of fiduciary duty in the circumstances of this case".³⁸ Furthermore, the directors could not escape liability on the basis that the plaintiffs had been independently advised because "the misrepresentations and non-disclosures meant that neither the shareholders nor their advisers were properly informed".³⁹

³⁵ Ibid, p.351.

³⁶ Ibid, p.337.

³⁷ Ibid, p.377.

³⁸ Ibid, p.351.

³⁹ Loc cit.

Coleman v. Myers illustrates the importance of the fact-finding process in cases in which fiduciary relations are alleged to exist. While the trial judge found that as a matter of law directors have fiduciary obligations to shareholders when they seek to purchase their shares directly, he found that the directors in this case had discharged their fiduciary duties to the plaintiff shareholders. On appeal to the New Zealand Court of Appeal, each of the three judges took a less categorical, more contextual, view of fiduciary relations between directors and shareholders, but found that by acting without the appropriate candour, indeed, by misleading shareholders in a fraudulent manner, the directors had breached their fiduciary duties to shareholders.

The Courts' Discussion of Directors' Fiduciary Duty to Shareholders

(i) Supreme Court

Percival v. Wright

The plaintiffs pleaded that by recommending acceptance of the take-over offer and by making various statements to the plaintiffs concerning the affairs of C & E, the first and second defendants breached their fiduciary duty not to mislead the shareholders and to make disclosure of all material facts to the shareholders.⁴⁰ The decision of Percival v. Wright was viewed as an "obstacle" to that argument since the decision was "directly in conflict with the proposition advanced."⁴¹ Mahon J. in his richly researched judgement, notes that Percival v. Wright has been criticized because it conflicts with "commercial morality" and because it is "inconsistent ... with the fiduciary duty of directors not to use the property or confidential

⁴⁰ Ibid, p.266.

⁴¹ Ibid, p.268.

information of the company for personal profit".⁴² He observes, apparently without regard to the Canadian securities and corporate law developments of the 1960s and 1970s, "[D]espite all these strictures no Commonwealth country has so far enacted legislation effectively abrogating the decision."⁴³ Mahon J. attributes the "general reluctance on the part of legislatures to intervene in the matter" to "the difficulty in constructing the appropriate statutory formula."⁴⁴ In this regard, Mahon J. observes that it is "essential that the directors be the fiduciary agents of the company alone" as a general matter. A "general rule that the directors were also the fiduciary agents of the shareholders" would cause the "concept of corporate management" to "collapse".⁴⁵ Despite the absence of legislative inroads on the rule in Percival v. Wright, Mahon J. concludes that the case, "directly opposed as it is to prevailing notions of correct commercial practice, and being in my view wrongly decided, ought no longer to be followed in an impeached transaction where a director dealt with identified shareholders."⁴⁶

A Per Se Rule of Directors' Fiduciary Duties to Shareholders

Having disposed of the "obstacle of Percival v. Wright", Mahon J. is free to consider from first principles the questions of whether directors have fiduciary duties to shareholders and, if so, the basis of such duties. On these issues, Mahon J. states the following:

The essential basis of breach of fiduciary duty is the improper advantage taken by the defendant of a confidence reposed in him either by, or for the benefit of,

⁴² Loc cit.

⁴³ Ibid, p.270.

⁴⁴ Ibid, p.273.

⁴⁵ Loc cit.

⁴⁶ Ibid, p.280.

the plaintiff. When one considers the legal relationship between the shareholder in a limited liability company and the directors entrusted with the management of that company, it appears to me that in any transaction involving sale of shares between director and shareholder, the director is the repository of confidence and trust necessarily vested in him by the shareholder, or by his legal status, in relation to the existence of information affecting the true value of those shares. I say this because a shareholder who is not a director has not, in the absence of any special provision in the articles of association, any right to intervene in the management of the company. It is the exclusive responsibility and privilege of the directors to manage the company's affairs in accordance with the jurisdiction provided by the memorandum and articles of association and subject to the supervision of the Companies Act.... The only way in which the general body of shareholders can control the exercise of powers vested in the directors is by altering the articles or by refusing to re-elect the directors of whose actions they disapprove: John Shaw & Sons (Salford) Ltd v Shaw [1935] 2 KB 113 [, [1935] All ER Rep 456]. A shareholder has no power to examine the books of the company, to appoint auditors or other experts to investigate the affairs of the company, to inspect the minutes of director's meetings, or legally to compel a continuing disclosure of the information or opinions of directors in the course of company administration. The effective management of companies, and especially of large enterprises, would be destroyed if any such powers existed. So when a director enters into a negotiation with a shareholder of his company for the purchase or sale of shares, and when that director has, by reason of his office, knowledge of an impending advantage to the company which would appreciate the value of the shares, or knowledge of some impending disaster which will depreciate that value, he is in possession of information which the shareholder is legally precluded from acquiring in the absence of the consent of the board.... It is a case where the director, as a negotiating party, makes an offer founded upon corporate information as to the value of

shares which, by law, is placed outside the knowledge of the owner [sic] of that same parcel of shares. The shareholder is, of course, entitled to make specific inquiries as to the existence of any special factor which may influence either his decision to sell or the price at which he will buy or sell, and the director will be liable on ordinary principles for a misleading reply. Within the situation which I have been contemplating there is, in my opinion, by reason of the statutory disability of the shareholder to compel disclosure of the relevant facts, a necessary confidence reposed in the director, by virtue of his status, in relation to his advantageous possession of material information known to that director and not known to the shareholder....In my opinion, therefore, there is inherent in the process of negotiation for sale a fiduciary duty owing by the director to disclose to the purchaser any fact, of which he knows the shareholder to be ignorant, which might reasonably and objectively control or influence the judgment of the shareholder in forming his decision in relation to the offer. The application of the rule so assumed to exist must necessarily be confined to private companies and to such transactions in public company shares, listed or otherwise, where the identity of the shareholder is known to the director at the time of the sale.⁴⁷

(Emphasis added.)

Mahon J. articulates a limited, but absolute, rule of directorial fiduciary duty to shareholders. He says that a director negotiating with a shareholder of his corporation for the purchase of the shareholder's shares is per se in a fiduciary relationship with the shareholder. This holding is comparable to the "special facts" fiduciary relationship between directors and shareholders which developed in U.S. case law following Strong v. Repide. Mahon J.'s rule is objective; if there are facts which a director knows because of his office, and which a

⁴⁷ Ibid, pp. 277-278.

shareholder does not know, a confidence recognized by law arises in favour of a shareholder when the director deals with the shareholder and makes use of his special knowledge.

Mahon J.'s recitation of the powers of a director within the corporation and the corresponding disability of the shareholders is largely applicable to Canadian corporations. Although shareholders of CBCA and CBCA - cognate corporations can assume the powers of directors by way of unanimous shareholder agreement and although these statutes contain provisions for the making of investigations, in the absence of such an agreement or such an investigation, shareholders in Canadian corporations occupy a position similar to that described by Mahon J. To withhold relief to shareholders who do not know of the existence of these Canadian statutory provisions or who have not utilized them either because the shareholders made an incorrect assessment of their need to use such procedures or because the shareholders could not use such procedures, i.e., because they were minority shareholders, would not be a laudable development in Canadian jurisprudence.

It should also be noted that while Mahon J. limits his holding to directors of private companies, his reasoning may readily be extended to corporate officers and, in some cases, majority shareholders. They, too, will have the advantage of corporate information which lies beyond the grasp of most shareholders

Mahon J. does not indicate whether a director in the situation outlined is required to make inquiries to determine the state of knowledge of the shareholder with whom he is dealing. In situations where material facts are known only by the directors or management and directors, a shareholder outside of the management group would have to be informed of relevant material facts according to Mahon J.'s reasoning. Mahon J. explains that the qualification in the last sentence is based on his view that anonymous stock exchange transactions involving directors should be regulated by insider trading statutes.

Applying his legal analysis to the facts of the case, Mahon J. concludes that "where the director of a private company made an offer to shareholders to purchase their shares, he had a duty to disclose to such shareholders any material fact of which to his knowledge they were unaware, and which reasonably might, from an objective viewpoint, materially affect the decision of those shareholders as to whether they would sell or as to the terms of sale."⁴⁸ He concluded that the evidence showed that A.D. Myers had not "suppressed" any material fact.⁴⁹ While this finding is not consonant with a finding that A.D. Myers disclosed those material facts of which he knew shareholders were unaware, Mahon J. dismisses the claim of breach of fiduciary duty against Myers. The reasons do not contain an explicit conclusion concerning K.B. Myers, but since the plaintiffs' main complaint was against A.D. Myers, the finding in favour of A.D. Myers implicitly contains a finding in favour of K.B. Myers.

Six features of a director's fiduciary duty to shareholders, as formulated by Mahon J., should be noted. First, the case involved a director, through a corporation he controlled, purchasing shares from shareholders. Arguably, Mahon J.'s reasoning that the statutory disability of a shareholder to compel disclosure of relevant facts results in a relationship of confidence with a director in a purchase and sale transaction with shareholders by virtue of the director's status and his "advantageous possession of material information" can be applied to other factual situations. For example, it may apply to situations in which a director is negotiating for a sale of his or her shares to a third party on terms which are preferential to those offered to other shareholders or in circumstances which take advantage of the difficulties being experienced by other shareholders.⁵⁰

⁴⁸ Ibid, p.280.

⁴⁹ Loc cit.

⁵⁰ See the discussions of Bell v. Source Data Control Ltd. and Dusik v. Newton, respectively, below.

Second, the fiduciary duty as formulated by Mahon J. does not impose a duty on directors to be fully forthcoming about the affairs of the corporation and the value of the shares. A director is obliged to disclose any material fact "of which he knows the shareholder to be ignorant". As noted above, however, Mahon J. did not impose any duty on directors to make inquiries concerning the state of the shareholder's knowledge.

Third, it appears that Mahon J. is of the view that common law fiduciary duties ought not to regulate all insider trading activities. He was apparently of the view that, from a legal policy perspective, it was preferable that stock market regulation be effected by legislation rather than by judicial decisions. The fiduciary principles he articulated, however, do not contain any such inherent restriction.

Fourth, it is not all information about the affairs of the corporation and the value of the shares which the director must disclose to a shareholder with whom he is dealing, but only that information which Mahon J. variously calls "relevant facts", "material information" or "material facts". In this regard, Mahon J. merges a discussion of the case law on the "materiality" test which has developed under Rule 10b-5 adopted by the U.S. Securities and Exchange Commission and the Anglo-New Zealand law of actionable non-disclosure. He states the following:

It was held in the well-known case Securities and Exchange Commission v. Texas Gulf Sulphur Co. 401 F 2d 833 (1968), as in previous cases, that the test of materiality of disclosure is objective in that the relevant question always is whether there has been non-disclosure of any fact which in reasonable and objective contemplation might affect the value of a security, this being the same type of objective test as expounded by Spencer Bower in *The Law Relating to Actionable Non-Disclosure* (1915) para 30. It is not a question of the plaintiff having to prove that he was in fact induced by a

representation, as in a cause of action based on actionable misrepresentation. In a non-disclosure case the reasonable possibility of inducement will suffice, and this has developed as the statutory test under Rule 10b-5.... The test of materiality thus established by American federal courts in relation to stock exchange transactions is no different, in essence, from the common law test as applied in cases of actionable non-disclosure, but it is clear enough that whereas the stock exchange investor must be regarded for those purposes as merely an unknown member of a class, transactions in shares between directors and shareholders of private or family companies will involve as the test of materiality the question whether the undisclosed information would reasonably and objectively influence the decision of that identified shareholder having regard to such matters, for example, as the known extent of his shareholding. A fact reasonably certain to influence a minority shareholder will not necessarily influence a controlling shareholder. The assumption of inducement, nevertheless, is objective. If the fact is not a material fact, then the plaintiff cannot be heard to say that he was induced in his course of action by its non-disclosure: cf *Spencer Bower* op cit para 33.⁵¹

(Emphasis added.)

In this passage, Mahon J. strays from the objective test articulated earlier and would consider particular shareholders and the effect non-disclosure would have on them. This approach looks to the relationship between particular directors and shareholders rather than being restricted to an inquiry as to whether a director failed to make disclosure and the materiality of such non-disclosure.

Fifth, Mahon J.'s references to the law of constructive fraud should be noted. Mahon J. notes that "[t]he creation of a fiduciary obligation is not conditioned by the existence

⁵¹ Coleman v. Myers, footnote 13, pp. 271-272.

of settled categories of circumstances".⁵² He outlines the development of the law of fiduciary relations as a distinct branch of the law of equity. This development has resulted in the identification of several relationships which are per se fiduciary in nature. Not all categories of fiduciary relationships have yet been identified, however. In the process of identifying further fiduciary relations one may look to the law of constructive fraud as Mahon J. observes in the following passage:

[T]here are several settled categories of fiduciary relationships, such as principal and agent, promoter and company, and the like, and in most cases where a plaintiff seeks to enforce breach of a fiduciary obligation towards him he will need to establish either the relationship of trustee and beneficiary or else one of the other accepted fiduciary relationships, and the general consequence of a plaintiff failing to bring himself within one of the settled categories will be that he stands revealed as merely the victim of a hard bargain from which the law will not release him. But the categories of constructive fraud are not closed: Snell on Equity (27th ed) 454. The moving pageant of human affairs displays new varieties of personal and business transactions of which most, as they occur, may be seen to be covered by existing remedies either at law or equity. But in the area of constructive fraud, where relief is sought for abuse of a confidence reposed, the same originating principle will apply, no matter what the transaction may be, and the principle of constructive fraud will intervene to grant relief against the bargain thus impeached.⁵³

Finally, statements made by directors who are in the type of fiduciary relationship Mahon J. analyzes in the case must not be made negligently. Mahon J. expresses this observation in the following passage:

⁵² Ibid, p.275.

⁵³ Ibid, p.276.

[A] duty of care in relation to statements made by directors in this situation is established by the conclusion which I have reached (assuming it to be correct) that directors who negotiate a purchase of shares from shareholders of their own company are under a fiduciary duty towards those shareholders restricted to the elements of that transaction.⁵⁴

(ii) Court of Appeal

Percival v. Wright

Unlike Mahon J., the Court of Appeal saw no need to hold that Percival v. Wright was incorrectly decided. Each of the Appeal Court judges noted the concessions made by counsel in that case. The decision was, therefore, restricted to the "very limited point" of whether "fortuitous negotiations for the sale of the undertaking altered the whole position" between directors and shareholders.⁵⁵ As Woodhouse J. states, "That, in my view, could not possibly be the test and, with respect, the decision of the judge in that particular case, restricted as I think it was to that one point, was inevitable".⁵⁶ As Cooke J. notes, "While the result of Percival v. Wright may have been correct on its facts, the judgement can carry little authority for any general proposition in this country; and, with respect, I do not find it of much help in the present case".⁵⁷

⁵⁴ Ibid, p.282.

⁵⁵ Ibid, p.324.

⁵⁶ Loc cit.

⁵⁷ Ibid, p.320.

A Contextual Rule of Directors' Fiduciary Duties to Shareholders

Having thus disposed of Percival v. Wright, the Court of Appeal was also able to approach the case at hand from first principles. Woodhouse J. articulated a view of fiduciary duties which may arise in a particular context or in particular circumstances which he found present in this case. He stated the following:

[The] standard of conduct required from a director in relation to dealings with a shareholder will differ depending upon all the surrounding circumstances and the nature of the responsibility which in a real and practical sense the director has assumed towards the shareholder. In the one case there may be a need to provide an explicit warning and a great deal of information concerning the proposed transaction. In another there may be no need to speak at all. There will be intermediate situations. It is, however, an area of the law where the courts can and should find some practical means of giving effect to sensible and fair principles of commercial morality in the cases that come before them; and while it may not be possible to lay down any general test as to when the fiduciary duty will arise for a company director or to prescribe the exact conduct which will always discharge it when it does, there are nevertheless some factors that will usually have an influence upon a decision one way or the other. They include, I think, dependence upon information and advice, the existence of a relationship of confidence, the significance of some particular transaction for the parties and, of course, the extent of any positive action taken by or on behalf of the director or directors to promote it. In the present case each one of those matters had more than ordinary significance and when they are taken together they leave me in no doubt that each of the two directors did owe a fiduciary duty to the individual shareholders.⁵⁸

⁵⁸ Ibid, pp. 324-325.

In this passage, Woodhouse J. raises several factors to be considered including the "surrounding circumstances", the relationship between the director and the shareholder and "commercial morality". This is an interesting mixture of objective and subjective factors. It does not set forth an easily applied test. Another interesting feature is the listing of the "existence of a relationship of confidence" as a factor to be considered. Mahon J. was of the view that such a relationship always existed between directors and shareholders because of directors' access to corporate information. This view seems well founded in law. In a case when the shareholder has access to the same corporate information that a director has, no confidence will, however, arise.

Casey J. would look to the relationship between the parties. Casey J. applies this principle to the case at hand in the following passage:

I have no doubt that in this tightly-held family company, both directors owed a fiduciary duty to the appellants and to the other shareholders. It must have been clear to Mr. AD Myers particularly that they were reposing trust and confidence in him, from their discussions and the inquiries they made. I have no doubt Sir Kenneth Myers was in everyone's eyes the head of the family group and its associated shareholders, whom they respected and trusted to look after their personal interests in the management of the company. Typical of this concern are the letters he wrote to his sisters about the earlier proposals for a distribution, and his separate discussions with the appellants, when they sought his advice on Mr AD Myers' bid. In such a family situation the latter, as managing director, would inevitably have been expected to continue the care and prudence displayed by his father for the welfare of family and associates, notwithstanding the fact that he was bidding for their shares. The evidence points to his recognition of this in the discussions he willingly held with the appellants about the reasons for his take-over and his plans, and a letter among the exhibits suggests a similar discussion with Mr GE Myers.

Add to this special relationship their exclusive knowledge of facts and intentions affecting the shareholders in relation to the offer and there can be only one conclusion. These two directors clearly owed a fiduciary duty not to make deliberately or carelessly misleading statements on material matters and to make proper disclosure.⁵⁹

As Casey J. states, the existence of a fiduciary obligation "depends upon a consideration of all the circumstances establishing that one party was known to be reposing trust and confidence in the other in the particular transaction and justifying the intervention of the court".⁶⁰

Cooke J. indicates that the particular fiduciary obligations which apply in a particular situation will be articulated by the court:

With regard to the moulding of the precise scope of the obligation here, it must be important to remember that directors are free to profit from their position, in the sense that there is no reason why they should not make a profit from dealings with shareholders. The obligation has to be worked out in terms of representations and disclosures.⁶¹

The requirements to avoid misleading statements and ensure that the shareholder is adequately informed apply to "matters material to the proposed dealing"⁶² between the director and shareholder. Material matters are defined by Cooke J. as "those considerations which can

⁵⁹ Ibid, p.371.

⁶⁰ Ibid, p.370.

⁶¹ Ibid, p.333.

⁶² Loc cit.

reasonably be said, in the particular case, to be likely materially to affect the mind of a vendor or of a purchaser".⁶³

Remedy

Although Woodhouse J. would have granted rescission of the contract, the other two judges were of the view that damages were the appropriate remedy. As Cooke J. states, it would not be "practically just to grant rescission here".⁶⁴ Casey J. elaborates in the following passage:

[It] would be flying in the face of commercial reality to suggest that returning shares to these appellants now (with the capital dividends accrued) would be putting them back in the same position as before they sold. Restitution means what it says - a restoration of each party to the position which each occupied before the transaction. Both appellants then realised that their situation as minority shareholders would be very difficult with Mr AD Myers in control and they can be fairly described as shareholders who had accepted that their only realistic course was to sell. With proper disclosure I think it probable that once Mr AD Myers had obtained over 90 percent acceptance they would have sold at a price their advisors recommended, having regard to the take-over situation they were dealing with. Had matters then reached the stage of a s 208 notice, there was every prospect of a compromise along those lines, or of the court fixing a price that would take into account the substantial liquidation the directors had in mind. Accordingly, it is not unfair to the appellants to compensate them on the basis of the price difference, rather than putting them back

⁶³ Ibid, p.334.

⁶⁴ Ibid, p.361.

into the company as a tiny minority owning shares no longer subject to s 208.⁶⁵

Damages were assessed at \$7.00 per share. It is submitted that where, as here, there has been a breach of a relationship which is characterized as fiduciary in nature because of the personal relationship, a stronger remedy for the person who has suffered the breach of trust would be appropriate. This would be more in keeping with the remedial approach adopted by the House of Lords in Regal (Hastings), Ltd. v. Gulliver. Damages seem more appropriate to a situation analyzed by the courts in terms of material facts and objective relationships. The Court of Appeal, unlike the New Zealand Supreme Court, did not explicitly base its decision on such factors.

Dusik v. Newton

Coleman v. Myers has been considered and adopted in several reported Canadian cases, the earliest of which is Dusik v. Newton et al.⁶⁶ This decision of the British Columbia Court of Appeal represents the Canadian high-water mark for the imposition of common law fiduciary duties on a corporate insider, here a director and majority shareholder, in favour of shareholders.

In this case, John F. Newton ("Newton") was a director of Fletcher's Limited ("Fletcher's"), a British Columbia non-reporting company engaged in the meat processing business. J.F. Newton Limited, a company controlled by Newton, held all of the issued shares of Fletcher's until November 15, 1978 when Ervin L. Dusik ("Dusik") purchased 10 per cent of the Fletcher's shares for \$30,000. The report does not indicate that there was

⁶⁵ Ibid, p.379.

⁶⁶ (1985), 62 BCLR 1 (BCCA).

a shareholders agreement between Dusik and Newton's company or a unanimous shareholders agreement binding on Fletcher's. The Court of Appeal outlines further background as follows:

Fletcher's was a company of two shareholders. There was a special relationship between the two [Newton and Dusik]. In 1968, upon acquiring 90 per cent of the shares of Fletcher's, Newton hired Dusik as general manager. He was looking for the best available salesman and induced Dusik to leave his employment with Pacific Meats, in part, by the option to purchase Fletcher's shares. The two men worked together to build up the company.⁶⁷

In July, 1979, Dusik left Fletcher's and purchased a slaughter business. He financed this venture by borrowing from the Bank of British Columbia (the "Bank"). The Bank's security for Dusik's borrowings included a pledge of his Fletcher's shares. The new business was unsuccessful. Less than a year after he purchased it, the Bank demanded repayment and appointed a receiver.

One of the business's creditors was the Alberta Hog Trading Company, the selling agency of the Alberta Pork Producers Marketing Board (the "Board"). In an effort to refinance his business, Dusik met with officials of the Board and the selling agency on June 27, 1980 and agreed that he would pledge his shares in Fletcher's to the Board and eventually sell them to the Board for \$450,000 less the amount owed to the selling agency. The agreement was subject to the written approval of the Bank and its receiver which was never given. On that same day, an officer of the Board, Garry MacMillan, told Newton about the proposed acquisition of Dusik's shares in Fletcher's. Prior to his meeting with the Board on June 27th, Dusik had received Fletcher's 1979 financial statements. At the meeting he telephoned V.H.

⁶⁷ Ibid, p.23.

Bradley, Fletcher's Vice-President of Finance and Administration, to ask for a set of the 1980 financial statements. Bradley told him that the statements were not ready. In fact, the statements had been released by Fletcher's auditors on May 2, 1980 but Newton had instructed Bradley to withhold them. As the Court of Appeal noted, "Newton's evidence was that he deliberately withheld the statements from everybody because of the tax audit, although he knew that Dusik was endeavouring to sell his shares in the summer of 1980 and that the financial results would be critical to him".⁶⁸ Not only did Newton withhold Fletcher's 1980 financial statements, but he also called an employee of the Bank on the morning of June 27 to advise the Bank that he knew of Dusik's financial difficulties and to inquire as to whether the Bank would be disposing of Dusik's shares in Fletcher's.

On October 21, 1980, MacMillan met with Newton to discuss the Board's interest in purchasing all of Fletcher's for \$15,000,000. On November 26, MacMillan contacted Dusik and Dusik confirmed his readiness to sell his shares for the price of \$450,000 agreed to the previous June. The transaction was put into the hands of the Board's solicitors. On December 4, 1980, the parties, except Dusik, and their representatives, met to discuss the proposed transaction. The purchase price of \$15,000,000 for 100% of Fletcher's was reiterated, and it was agreed that the Board would pay J.F. Newton Ltd. \$13,500,000 for its 90% interest and would purchase the remaining 10% directly from Dusik. The Board planned to announce the acquisition of Fletcher's on December 15 and 16.

In the interim, the Board's solicitors attempted to enter into an agreement of purchase and sale with Dusik. Dusik was reluctant to sell before 1981 because he wanted the gain on the sale of his shares to be taxed as capital gain rather than as business income. His concern was addressed by the Board's solicitors who restructured the agreement of purchase and sale as the acquisition of an option to purchase Dusik's shares on January 2, 1981. Dusik did

⁶⁸ Ibid, p.24.

not engage his own solicitor until a few days before the Board's solicitor wanted the option agreement executed and, it would appear that he did not have sufficient time to conduct any investigations or formulate meaningful legal advice. During the few days leading to Dusik's execution of the option agreement, the Board's solicitors put Dusik and his recently retained solicitor under pressure to sign the documents. The Board's solicitor made it clear that if the agreement was not executed by Dusik, the Board would deal directly with the Bank to acquire the shares. Dusik executed the agreement on December 16 and delivered it to the Board's solicitor. He learned about the sale of Fletcher's to the Board that evening and was shocked. Newton had not discussed the transaction with him prior to that time. They first discussed the matter on January 7, 1981.⁶⁹ The trial judge observed that both Newton and the Board bore some enmity towards Dusik. He noted that they rejected the possibility that Dusik share proportionately in the proposed purchase price of \$15 million, because "neither Newton nor the marketing board wanted Willowbank [Dusik's business] revived from the proceeds of the sale".⁷⁰ He also observed that "Newton was well aware of what the board proposed to do, lent his assent, and at least tacitly agreed that as a director of Fletcher's he would approve the registration of the shares in the name of the board if the board were successful in buying from Dusik".⁷¹ Newton's counsel argued that throughout his negotiation with the Board, Newton believed that the Board had an effective agreement with Dusik to purchase Dusik's shares in Fletcher's and that as "Dusik had already made his bargain with the board, there was no need for Newton to disclose to him the details of his own negotiations".⁷² Neither the trial judge nor the Court of Appeal accepted that submission.

⁶⁹ Ibid, p.14.

⁷⁰ Ibid, p.12.

⁷¹ Loc cit.

⁷² Ibid, p.13

The Court of Appeal reviewed the law concerning directors' fiduciary duties to shareholders.⁷³ They extensively canvassed the reasons of the New Zealand Court of Appeal in Coleman v. Myers as well as the Ontario Court of Appeal decisions in Goldex Mines Ltd. v. Revill⁷⁴ and Francis v. Dingman.⁷⁵ The Court dealt with the issue of Dusik's loss incurred on the sale of his Fletcher's shares for an undervalue on the basis of common law fiduciary principles in the following passage:

Counsel for Newton says that the general rule is that laid down in Percival v. Wright, that a director does not owe a fiduciary duty to minority shareholders and only three exceptions have emerged. They are where a director acts as an agent of a minority shareholder; where a director buys shares from a minority shareholder; and where a director has been dishonest with or has misled a minority shareholder. In our view the law is no longer that restrictive. The correct approach is stated in the passages we have quoted from Coleman v. Myers and the Ontario cases.⁷⁶

(Emphasis added.)

The Court rejected the proposition that directors do not owe fiduciary duties to shareholders and, by implication, it rejected Percival v. Wright as authority for any general proposition as the New Zealand Court of Appeal had also done. By adopting the approach of the New Zealand Court of Appeal in Coleman v. Myers, the B.C. Court of Appeal accepted the proposition that an

⁷³ Ibid, pp.20-23.

⁷⁴ (1975) 7 OR (2d) 216, 54 DLR (3d) 672.

⁷⁵ (1983), 43 OR (2d) 641, 23 BLR 234, 2 DLR (4th) 244.

⁷⁶ Footnote 66, p.23.

individual director may owe fiduciary duties to shareholders and that the existence of any such duty or duties would depend on all of the facts of the particular case.

The Court then applied the law to the facts of the case. In the course of so doing, the Court commented on the third recognized exception to the rule in Percival v. Wright and stated that "there can be misleading in a negative way by failing to inform".⁷⁷ In the result, the Court concluded that "Newton as director owed Dusik the duty of disclosing to him that the board was proposing to acquire all of Fletcher's shares for the price of \$15 million....Newton deliberately kept Dusik in the dark thus making himself liable for the consequent loss".⁷⁸ It is unclear whether the court based its judgement on its assessment of Newton's personal relationship to Dusik. There was no longer a close, dependent relationship between these two individuals which could form a basis for imposing fiduciary duties. That was historical. Because of Newton's position as a director of Fletcher's, however, Dusik was vulnerable to Newton's actions. This vulnerability was particularly acute because Newton was activated by enmity towards Dusik. It was also acute because Dusik had lost touch with the Fletcher's business. In short, his vulnerability was a function of his exclusion from knowledge of the business, which exclusion was the result of his own action, the statutory disability facing all shareholders and Newton's ill will. The law of fiduciary relationships should be adequate to overcome Dusik's statutory disability when that disability is used to his detriment by a malicious director. As Professor MacIntosh, Ms. Holmes and Mr. Thompson have noted, "the dispute was really between Newton qua shareholder and Dusik qua shareholder."⁷⁹ While this observation is correct, it is important to keep in mind the manner in which Newton acted to Dusik's detriment, viz. the abuse of his directorial power.

⁷⁷ Ibid, p.24.

⁷⁸ Ibid, pp. 24-25.

⁷⁹ J.G. MacIntosh, J. Holmes and S. Thompson, "The Puzzle of Shareholder Fiduciary Duties" (1991), 19 CBLJ 86 at p.102.

It should be noted that the Court of Appeal imposed additional liability on Newton and J.F. Newton Limited on the basis of the breaches of the insider trading provisions of the B.C. *Company Act*.⁸⁰ This liability was imposed in respect of the disposition of one of Fletcher's assets, a piece of land in Red Deer, Alberta, and the payment for J.F. Newton Limited's shares in Fletcher's from Fletcher's retained earnings in the form of a tax-free dividend. Dusik's counsel also argued that an additional basis for the imposition of liability on Newton was the B.C. *Company Act* s. 224 oppression remedy. The Court of Appeal apparently was of the view that it was not necessary to decide this issue. The Court did not examine the inter-relationship of directors' common law fiduciary relationship to shareholders and the statutory oppression remedy.

Bell v. Source Data Control Ltd.

Coleman v. Myers has also been referred to with approval in the dissenting reasons of Cory J.A., as he then was, in the Ontario Court of Appeal decision in Bell et al. v. Source Data Control Ltd. et al.⁸¹

The Factual Background

This case involved a sale of the control block of shares of Source Data Control Ltd. ("SDC") by Hood for a premium which was neither disclosed to nor made available to two minority shareholders, Bell and Stewart. All three shareholders were also directors of SDC. The company was formed in 1968. Hood put up the majority of the capital and he had the original idea for the business. Accordingly, sixty per cent of the shares of SDC were issued to him. Stewart also put in funds and worked in the business from the outset. He received ten

⁸⁰ Ibid, pp. 25-27.

⁸¹ (1988), 40 BLR 10.

per cent of the SDC shares. Bell, who also held ten per cent of the company's shares, joined the company in the early period.

The company did not perform well initially, but through the hard work of all the parties, the company eventually prospered. It continued to perform well until some time in 1979. At this time, Hood became embroiled in marital problems. At about the same time, the relationship between Hood and the minority shareholders significantly deteriorated. By the financial year end in the fall of 1980, SDC had sustained a loss. The company had cash flow problems and its bank was considering the appointment of a "soft" receiver.

From some time in the early 1970s, McLean-Hunter Limited ("McLean-Hunter") had been interested in acquiring SDC. In the fall of 1980, one of the minority shareholders contacted McLean-Hunter to discuss a sale of three minority shareholders' shares. Thirty per cent of the SDC shares would be sold and each shareholder, who would be selling ten per cent of the SDC shares, would be paid \$200,000.00. McLean-Hunter indicated that it would only be interested in acquiring a control position in SDC.

At about the same time, Hood contacted McLean-Hunter. Originally, Hood proposed a sale price of \$3.5 million with each ten per cent block of shares being paid \$350,000.00. But, McLean-Hunter reviewed SDC's financial results and was prepared to pay no more than \$2.7 million for ninety per cent of the SDC shares. Hood still wanted \$350,000.00 for each ten per cent block of shares which he held. In order to accommodate this objective, McLean-Hunter proposed that Hood be paid this price for a total of \$2.1 million for his sixty per cent interest and that the other shareholders be paid \$200,000.00 for each ten per cent interest in the company as they had originally proposed.

The trial judge found that the minority shareholders wanted to get out of the company, to get away from Hood. They advised Hood of the price they sought for their shares.

Hood did not suggest this or any other amount for their shares. Hood did not influence or put pressure on the minority shareholders in respect of the sale of the shares or the price at which they were to be sold. He simply did not disclose the fact that he intended to sell his shares or the price at which he intended to sell even when the solicitors for the minority shareholders requested information from Hood and his solicitor. The trial judge concluded that on the basis of agreements in circulation prior to the closing of the purchase and sale of shares coupled with their knowledge of McLean-Hunter's desire to acquire a control position, the minority shareholders had to know that some of Hood's shares were being sold.

Fiduciary Duties of Directors and Majority Shareholders to the Minority

In his dissenting reasons, Cory J.A. reviewed the law relating to what he calls "the common law rule as to fiduciary duty owed by directors and majority shareholders to their corporation and the minority shareholders".⁸² He concludes by acknowledging that Percival v. Wright has been overruled and that the New Zealand Court of Appeal's approach is correct as follows:

[T]he original rule that individual shareholders are not owed a fiduciary duty by other directors or majority shareholders has been altered.... [T]he issue as to whether fiduciary obligations are owed will depend upon the facts of the particular case and will not be dependent solely upon the formal classification of the parties as majority and minority shareholders or director and shareholder.⁸³

⁸² Ibid, p.19.

⁸³ Ibid, pp. 24-25.

The "facts of the particular case" is an indeterminate phrase which would permit the courts to consider personal relationships as well as more clearly objective factors.

Although they were of the view that certain facts led to a result from which Cory J.A. dissented, the other judges took no exception to this statement of the law. It is unfortunate that the other judges did not highlight their reasons for refusing to impose fiduciary duties. Brooke J.A. (McKinlay J.A. concurring) simply said:

Having regard to the findings of fact made by the trial Judge, I think that this case must be distinguished from cases in which the principle relied upon by my brother Cory is to be applied. In these circumstances I agree with the reasons of Mr. Justice Eberle. Therefore the appeal should be dismissed.⁸⁴

The paucity of the majority's reasons leads the editor of the report of the Court of Appeal's decision to state the following:

The findings of fact referred to by Brooke J.A. appear to be: a) that the appellants were aware that at least some of the shares of H must have been included in the total price; b) that the appellants had obtained their price and had not asked H whether he was selling his shares or whether the sale of their shares was in any way tied to the sale of H's shares; and c) that the appellant's had not placed any reliance on H for guidance in making their decision either about selling their shares or about the price at which they were to be sold.⁸⁵

⁸⁴ Ibid, p.27. The author has been unable to locate a report of the trial judge's reasons. A summary of the trial judge's decision is available at 39 ACWS (2d) 62.

⁸⁵ Ibid, p.11.

One of the most striking features of factors (b) and (c) , assumed to be of importance to the majority, is their similarity to the reasoning of the court in Percival v. Wright.⁸⁶ One would assume, however, that these factors could only be strongly relevant in an atmosphere of candid and unrestricted communications. The majority, in placing considerable weight on factors (b) and (c) seem to have disregarded the fact that reasonable communications between the shareholders of SDC had completely broken down, ostensibly as a result of marital difficulties experienced by the majority shareholder, Hood. After working closely and diligently together for many years to build the business, the economic well-being of shareholders should not turn on a requirement that they communicate with one of their number who has either made impossible or become incapable of straightforward communication. The majority also seem to indicate that they will not assist shareholders who fail to extract representations and warranties even from persons with whom the shareholders are not contracting, namely, the majority shareholder. Shareholders who sell their shares without some rudimentary representations and warranties should not be left unassisted by the court, however. Such an approach punishes the unwary because they are unwary.

Cory J.A. analyzes the facts of the case in the following passage:

Applying that principle to the facts of this case I have concluded that a fiduciary duty was indeed owed by Hood to the minority shareholders. This was a small, very closely held corporation. The parties had worked together very hard and in close association for a number of years. They had all dedicated themselves to the success of the company. They had, until 1978 or 1980, enjoyed a special relationship arising from their long and close association in S.D.C. In all probability they would have continued their association had it not been for the marital difficulties experienced by Hood. The fact that as a result

⁸⁶ Discussed in Chapter 2.

of his personal problems he was difficult to deal with and the minority shareholders no longer trusted him nor wished to continue their association with him does not relieve him from his obligation. Where, as here, parties have worked together in a close association for some years, equitable fairness requires the majority shareholder at least to disclose the fact of the takeover.

The sale of a majority interest in a company is fundamental to its operations. If ever there is to be a duty to disclose it should arise in the circumstances of a takeover. It may well have been sufficient for Hood to disclose that he was selling his shares at a price greater than that of the minority shareholders. In a private corporation the majority interest may be entitled to receive a premium from the sale of the majority shares.... In circumstances where a small, closely held corporation has existed for a number of years and has been the source of livelihood for all the shareholders, common decency and elementary fairness dictate that a fiduciary obligation rests upon the majority shareholder to disclose the sale of the majority interest and at least whether there is to be a premium for the majority shares.⁸⁷

(Emphasis added.)

Cory J.A. supports the imposition of fiduciary duties on Hood on the basis of the "special relationship" among the shareholders, the fact of a take-over and on "common decency and elementary fairness". In doing so he would impose fiduciary duties on both a contextual and on a limited per se or absolute basis, for example, in take-over situations.

Although Cory J.A. states that his analysis proceeds from what he calls "that principle", his analysis is based on at least four points:

⁸⁷ Footnote 80, p.25.

1. Percival v. Wright need no longer be strictly followed;
2. The categories of fiduciary relationships and duties are not closed and, in particular, directors and majority shareholders may owe fiduciary duties to other shareholders in certain circumstances;
3. The determination of whether a fiduciary relationship exists and fiduciary duties are owed, at least outside of the traditional categories, is based on a careful assessment of the facts of the particular case; and
4. Where a small, closely held corporation has existed for a number of years and has been the source of livelihood for all the shareholders, the majority shareholder has a fiduciary duty to disclose the sale of the majority interest and, at a minimum, whether there is to be a premium for the majority shares.

It seems clear that Cory J.A.'s analysis may extend beyond the facts of this case. Essentially, Hood's particular fiduciary duties in the takeover of SDC arise from the imposition of a requirement of "common decency and elementary fairness" between shareholders who were close business colleagues for many years. Hood seems to have achieved his advantage over the other shareholders solely in his capacity as a shareholder, however, the same requirements of decency and fairness could have been applied to Hood in his capacity as a director of the corporation had the advantage he obtained in comparison to the other shareholders been accomplished by use of his position as a director. Moreover, as both a director and the majority shareholder, Hood had access to material information about the value of SDC, information from which the minority was excluded. The benefit he received was directly attributable to his use of that information and, more particularly, to his failure to disclose it. This was information

concerning the company which Hood should not have been permitted to use to his benefit and to the detriment of the other shareholders.

As Bell exemplifies in the majority shareholder situation, the existence of a fiduciary relationship between directors and shareholders and the nature of the fiduciary duties owed may be found following a careful assessment of the facts in each case. The basis on which such duties are imposed is, however, not settled by the cases. Perhaps the most important observation to draw from this decision is that only very infrequently will a set of facts be sufficiently egregious to compel the Ontario Court of Appeal to impose fiduciary duties on a director or majority shareholder in favour of a shareholder.

It should also be noted that the Court of Appeal did not consider the possible application of the statutory oppression remedy to these facts. The basis for this omission is not clear.⁸⁸

Vladi Private Islands Ltd. v. Haase et al.

The Nova Scotia Court of Appeal has accepted the propositions that "a fiduciary duty may be owed by a director to a shareholder" and that the existence of such duty "will depend on the facts of each particular case" in Vladi Private Islands Ltd v. Haase et al.⁸⁹ In this case, Anthony J. Mooney and Joachim Haase were directors of a closely held private Nova Scotia corporation, Mineral Water Company of Canada Limited. According to the plaintiffs' pleadings, during the month of October 1988, the directors decided to make a

⁸⁸ The reasons do not indicate Source Data Control Ltd.'s jurisdiction of incorporation. The oppression remedy came into effect in the OBCA on July 29, 1983 but was in effect as part of the CBCA since the mid 1970s. The events in issue in the case occurred in 1980 and 1981.

⁸⁹ (1990), 96 NSR (2d) 323 at 328.

concerted effort to secure long-term equity financing in the company. Two likely investors were found. The plaintiffs alleged that during negotiations with these investors, Mooney and Haase developed a plan to have one of the company's secured creditors force the company into receivership. The assets of the company were then to be acquired by a company controlled by Haase and, with the backing of the new investors, the company's business would continue and be developed. This plan would clear away claims made by unsecured creditors as well as the interests of the other shareholders. The Court agreed that fiduciary claims could be brought by shareholders in their own right against the directors in such a situation. Presumably the corporation would also have a cause of action against the directors on these facts.

NIR Oil Ltd. v. Bodrug

Shortly after the B.C. Court of Appeal's decision in Dusik v. Newton, the Alberta Court of Appeal considered the issue of an officer's fiduciary duty to disclose an impending takeover to shareholders in NIR Oil Ltd. et al. v. Bodrug et al.⁹⁰ Based on its review and application of the principles in Coleman v. Myers, Allen v. Hyatt and Guerin v. R., the Court observed that "it may well be that in the circumstances of this case it would have been held that Bodrug [an officer] had a fiduciary obligation to the plaintiffs [shareholders] to disclose the information that he had about the offer to be made for Hydrogas shares".⁹¹ The Court did not decide the matter, however, because it was not fully argued. The trial judge had found for the plaintiffs on the basis that Bodrug had violated the insider trading provisions of s.112(1) of the Alberta *Securities Act*, R.S.A. 1970, c.333 through his dealings in the shares of Hydrogas Resources Ltd. which were publicly traded on a stock exchange. That judgement was upheld on appeal. While the Alberta Court of Appeal was not required to make an authoritative pronouncement on the issue of fiduciary obligations to shareholders in the NIR Oil decision, it

⁹⁰ (1985), 38 Alta LR 321.

⁹¹ Ibid, p.330.

appeared willing to extend the Coleman v. Myers principle to impose fiduciary duties on officers and to do so in respect of transactions in the shares of a publicly traded corporation.

LAC Minerals Ltd. v. International Corona Resources Ltd.

LAC Minerals Ltd. v. International Corona Resources Ltd.⁹² is the Supreme Court of Canada's most recent consideration of the law relating to fiduciaries. The reasons delivered by the various judges provide guidance concerning the identification of situations in which a fiduciary relationship will be found to exist and fiduciary obligations will be enforced by the courts. Guidance alone may be extracted from the case in the context of our inquiry relating to directors' fiduciary duties for three reasons. First, LAC Minerals is not a case relating to corporate governance matters. Second, the judges' discussions of fiduciary obligations are obiter. Finally, and most significantly, as LaForest J. notes, the principle on which fiduciary obligations are founded is unclear.⁹³

The Factual Background

Corona Resources Ltd. ("Corona") was engaged in exploration for mineral deposits in the Hemlo area of northern Ontario in 1980 and 1981. Corona had claims to an area of approximately 680 acres. In the course of this exploration program, Corona's geologist, David Bell, formulated a theory that mineralization of the area was widespread. Accordingly, Bell, on behalf of Corona, asked a prospector to attempt to acquire a property of about 400 acres known as the Williams property which was on the west side of and contiguous to the Corona property.

⁹² (1989), 61 DLR (4th) 14.

⁹³ Ibid, p.26.

Some results of Corona's exploration and drilling program were released and published periodically in a trade newsletter. These results came to the attention of LAC Minerals Ltd. ("LAC") and on May 6, 1981 LAC representatives met with Bell and others at the Corona property to learn more about Corona's exploration program. At that meeting, Bell disclosed his theory of the geology of the region. He indicated that the mineral formation continued to the west on the Williams property and that Corona wanted to explore that area.

The parties had meetings and exchanged correspondence during May and June, all with a view to reaching an agreement with respect to the joint development of a mine. During these negotiations confidential information was disclosed to LAC. Both the trial judge and the Ontario Court of Appeal found that there was an industry practice "known to LAC, that LAC would not use confidential information derived out of the negotiating relationship in a manner contrary to the interests of Corona."⁹⁴ Because of this practice and because the trial judge found that it was "obvious" to LAC that it was receiving confidential information from Corona, the trial judge, the Ontario Court of Appeal and LaForest J. took no account of either the lack of discussions between the parties regarding confidentiality or the absence of a confidentiality agreement.

In early June, Corona made an offer to purchase the Williams property. In early July, LAC also offered to purchase the property. LAC's offer was accepted later that month. The parties discontinued their relationship and Corona sued LAC. The trial court found that there was an "industry - recognized practice not to acquire the property which was being pursued by a party with which [the acquiring party]... was negotiating" and that LAC was aware of this practice.⁹⁵

⁹⁴ Ibid, p.36.

⁹⁵ Ibid, p.24.

Fiduciary Duties Arising Outside of a Fiduciary Relationship

The majority of the panel (McIntyre J., Lamer J., as he then was, and Sopinka J.) held that there was no fiduciary relationship between LAC and Corona. A remedy appropriate for breach of fiduciary obligations, the constructive trust, was nonetheless imposed on LAC in favour of Corona.

The two judges in dissent on this aspect of the case, Wilson J. and LaForest J., held that a fiduciary duty arose in LAC. Wilson J. expressed the conclusion in the following passage:

[W]hile no ongoing fiduciary relationship arose between the parties by virtue only of their arm's length negotiations towards a mutually beneficial commercial contract for the development of a mine, a fiduciary duty arose in LAC when Corona made available to LAC its confidential information concerning the Williams property, thereby placing itself in a position of vulnerability to LAC's misuse of that information.⁹⁶
(Emphasis added.)

Wilson J. concluded that LAC breached its fiduciary duty by acquiring the Williams property for itself. Her conclusion is founded on her view that fiduciary duties may arise out of "specific conduct" of parties who are outside of an essentially fiduciary relationship.

Wilson J.'s concept of "specific conduct" is significant for understanding directors' common law fiduciary duties to shareholders. Like the relationship between arm's length parties negotiating a mutually beneficial commercial contract, the relationship between

⁹⁶ Ibid, p.16.

a director of a corporation and a shareholder is viewed by some as not per se a fiduciary relationship.⁹⁷ There may, however, be situations in which "specific conduct" fixes a director with specific fiduciary duties owed to a shareholder. The Dusik and Bell cases could be analyzed and the imposition of fiduciary duties justified on this basis. Dusik and Newton had worked hard together for many years to build the Fletcher's business. Similarly, Hood and the other shareholders of Source Data Control Ltd. had worked closely together for many years to earn their livelihood and build the business. Such "specific conduct" may be sufficient to impose on directors and shareholders an obligation to disclose an advantage they intend to take for themselves which advantage is not available to the other shareholders. In fact, Dusik exemplifies a situation in which the court determined that the director/majority shareholder could not take an advantageous sale of his shares unless the minority shareholder was allowed to participate in the sale. (This is akin to the industry practice found in LAC that parties negotiating an agreement in the mining industry will not act so as to appropriate property known to be sought by the other.) Further, Newton and Hood had information about their fellow shareholders, i.e. that they wanted to sell and were prepared to do so at prices lower than those accepted by Newton and Hood, which, while perhaps not a "confidence" in the sense discussed in LAC, placed them in an advantageous position for disposing of their shares. It seems reasonable to suggest that by doing nothing to disrupt the sales of the minority shareholders' shares at lower prices than they were to receive, Newton and Hood were also ensuring that they would receive higher prices for their shares.

Both LaForest J., who found that a fiduciary duty of limited scope arose in the case, and Sopinka J., who found no fiduciary relationship in the case, in their reviews of the law of fiduciary obligations quoted with approval from the judgement of Dickson J., as he then was, in Guerin v. The Queen as follows:

⁹⁷ Because of directors' responsibility to manage the affairs of the corporation and because of their access to corporate information and other property this proposition is debatable.

...[W]here by statute, agreement or perhaps by unilateral undertaking, one party has an obligation to act for the benefit of another, and that obligation carries with it a discretionary power, the party thus empowered becomes a fiduciary. Equity will then supervise the relationship by holding him to the fiduciary's strict standard of conduct.

It is sometimes said that the nature of fiduciary relationships is both established and exhausted by the standard categories of agent, trustee, partner, director and the like. I do not agree. It is the nature of the relationship, not the specific category of actor involved that gives rise to the fiduciary duty. The categories of fiduciary, like those of negligence, should not be considered closed.⁹⁸

Dickson J. refers to a "relationship", one which the courts will supervise. It is "the nature of the relationship, not the specific category of actor involved" which gives rise to fiduciary duties. Clearly the relationship of director and shareholder is not precluded from the imposition of fiduciary duties although this has happened only infrequently.

Both LaForest J. and Sopinka J. also quote with approval from Wilson J.'s reasons in Frame v. Smith in which, in considering the imposition of fiduciary obligations in a relationship (that of custodial to non-custodial parents) which had not previously been considered a fiduciary relationship, she states the following:

...[T]here are common features discernable in the contexts in which fiduciary duties have been found to exist and these common features do provide a rough and ready guide to whether or not the imposition of a fiduciary obligation on a new relationship would be appropriate and consistent.

⁹⁸ (1984), 13 DLR(4th) 321, [1984] 2 SCR 335, [1984] 6 WWR 481, at DLR, p.341.

Relationships in which a fiduciary obligation have been imposed seem to possess three general characteristics:

- (1) The fiduciary has scope for the exercise of some discretion or power.
- (2) The fiduciary can unilaterally exercise that power or discretion so as to affect the beneficiary's legal or practical interests.
- (3) The beneficiary is peculiarly vulnerable to or at the mercy of the fiduciary holding the discretion or power.⁹⁹

(i) Obligation to Act for the Benefit of Another

As noted above in the passage from Dickson J.'s reasons in Guerin, one party must have "an obligation to act for the benefit of another" before that party is considered a fiduciary for the other. Dickson J. states that the obligation may arise under a statute, an agreement or by unilateral undertaking. Are directors under an obligation to act for the benefit of shareholders? Under the OSA and CBCA regulation of take-over-bids, directors of an offeree corporation are required to prepare a circular to make disclosure about their interests, provide shareholders with information about the offeree corporation and advise shareholders whether or not to accept the bid. In discharging this function, directors may be considered statutory fiduciaries for shareholders. It is unlikely that directors will undertake by agreement to act for shareholders, although the converse may occur where shareholders by an unanimous shareholder agreement restrict directors powers to act and thereby release them from their obligation to manage the business and affairs of the corporation to the same extent. Finally, unilateral action by one or more directors on behalf of shareholders seems somewhat unlikely. This leaves another source of obligation on directors to act for the benefit of shareholders, commercial

⁹⁹ (1987), 42 DLR(4th) 81, [1987] 2 SCR 99, 9 RFL(3d) 225, at DLR, pp.98-9.

morality. Cory J.A. would have decided in favour of the plaintiff shareholders on this basis in Bell v. Source Data Control Ltd.

At the Supreme Court of Canada, counsel for LAC argued against using morality as the basis for imposing fiduciary duties. Counsel argued that "imposing a fiduciary relationship in a case such as this would give rise to the greatest uncertainty in commercial law, and result in the determination of the rules of commercial conduct on the basis of ad hoc moral judgements rather than on the basis of established principles of commercial law".¹⁰⁰ LaForest J. rejected these submissions with a threefold answer. First, certainty in commercial law, though an important value, is not the sole value. Secondly, he viewed the result in the case as conforming to the parties' expectations and he rejected the suggestion that giving effect to the parties' expectations could bring commercial law into turmoil. Finally, he viewed the decision as reinforcing business morality and, in particular, accepted business morality in the natural resource development industry. In short, he rejected the notion that "business and accepted morality are mutually exclusive domains."¹⁰¹

Much of LaForest J.'s discussion about the role of morality in commercial law is applicable to the law of corporate governance. First, minority shareholder rights is a set of values additional to the value of majority rule certainty in corporate governance. Certainty of result, as determined by the majority, is not the sole value within the corporation. Secondly, the objectives of developing procedures and ensuring results which protect the reasonable expectations of investors in corporations has been well recognized in Canada in take-over situations since the Kimber Report in 1965. Finally, as LaForest J. commented in LAC, "It is simply not the case that business and accepted morality are mutually exclusive domains." It follows that business morality may well constitute a source from which "an obligation to act for

¹⁰⁰ Footnote 92, pp.42-43.

¹⁰¹ Ibid, p.44.

the benefit of another", as Dickson J. expressed the source of fiduciary obligations in Guerin v. R., arises between director and shareholder.

(ii) Power and Discretion

Both Dickson J.'s and Wilson J.'s descriptions of the characteristics of fiduciaries and fiduciary relationships recognize the importance of discretion and power. Dickson J., in Guerin v. The Queen, stated that a party must have both "an obligation to act for the benefit of another" and "a discretionary power" to act in connection with that obligation in order to be considered a fiduciary. Wilson J., in Frame v. Smith, notes that a fiduciary has some discretion or power which may be exercised unilaterally so as to affect the beneficiary's interests. Directors' power or discretion over shareholders' affairs are generally exercised through the corporation. Election to office by shareholders does not empower directors to affect the interests of shareholders in a direct manner. Of course, each exercise of the directors' power and discretion with respect to the management of the corporation affects shareholders indirectly. Must the power and discretion be directly linked to shareholders' interests to conform to the observations of Dickson J. and Wilson J.? It seems unlikely, for, as LaForest J., in his exegesis of the concept of power and discretion in fiduciary relationships, notes, "[a]ll that power and discretion mean in this context is the ability to cause harm."¹⁰² Certainly, directors by their action or inaction may harm shareholders. They, through the corporation, have the power and discretion to do so. If they cause harm through the exercise of their directorial power, a remedy imposed pursuant to the statutory oppression remedy may be available. Rather than causing harm through the exercise of directorial power, however, directors and other corporate insiders may simply take benefits not available to other shareholders. It is submitted that the concept of "power and discretion" is sufficiently elastic to include the taking of such benefits.

¹⁰² Ibid, p.41.

(iii) Vulnerability

LaForest J. and Sopinka J. disagree about whether vulnerability to another's misdeeds is a necessary condition to the imposition of fiduciary obligations. More specifically, they also disagree about whether vulnerability existed on the facts in LAC. LaForest J. states that "vulnerability is not... a necessary ingredient in every fiduciary relationship."¹⁰³ Nonetheless, he observes, "I would have thought it beyond argument that on the facts of this case Corona was vulnerable to LAC."¹⁰⁴ Sopinka J., by contrast, states, "The one feature, however, which is considered to be indispensable to the existence of the [fiduciary] relationship... is that of dependency or vulnerability."¹⁰⁵ He concludes, "In my opinion, this vital ingredient was virtually lacking in this case."¹⁰⁶ Such polar extremes concerning both the law relating to fiduciary obligations and the factual analysis in this case at the Supreme Court of Canada are disturbing.

In the context of our inquiry, we need to address two questions. First, need shareholders be shown to be vulnerable to directors in order to found fiduciary obligations in particular situations? Second, might shareholders be found to be vulnerable to directors? The answer to the first question depends on whether the reasoning of LaForest J. or Sopinka J. is preferred, while the answer to the second question will depend on the facts of each case.

LaForest J. notes that much of the confusion surrounding the term "fiduciary" is caused by the undifferentiated usage of the term. He discusses three ways in which the term

¹⁰³ Ibid, p.39.

¹⁰⁴ Ibid, p.40.

¹⁰⁵ Ibid, p.63.

¹⁰⁶ Ibid, p.68,

is used.¹⁰⁷ First, the term "fiduciary" is used to describe a certain class of relationship the existence of which gives rise to fiduciary obligations. Examples of this class of relationship include directors and corporations, solicitors and clients, trustees and beneficiaries, agents and principals, the relationship among partners and relationships analogous to the foregoing. LaForest J. observes that "[t]he focus [of this use of the term "fiduciary"] is on the identification of relationships in which, because of their inherent purpose or their presumed factual or legal incidents, the courts will impose a fiduciary obligation on one party to act or refrain from acting in a certain way".¹⁰⁸ In the case of Frame v. Smith, Wilson J., in dissent, concluded that custodial and non-custodial parents constitute a class of fiduciary relationship while the majority did not consider it necessary to address the issue. In the LAC case, Corona did not contend that parties negotiating towards a joint venture constitute a class of relationship which gives rise to fiduciary obligations. Mahon J. in Coleman v. Myers held that directors who purchase shares directly from shareholders constitute such a class while the New Zealand Court of Appeal retreated from this position to hold that the imposition of fiduciary duties in such cases was predicated on "all the surrounding circumstances and the nature of the responsibility which in a real and practical sense the director has assumed towards the shareholder". Canadian courts have followed this view.

LaForest J. discussed a second usage of the term "fiduciary", the usage he felt applied to the situation before the Court in LAC, in the following passage:

The imposition of fiduciary obligations is not limited to those relationships in which a presumption of such an obligation arises. Rather, a fiduciary obligation can arise as a matter of fact out of the specific circumstances of a relationship. As such it can arise between parties in a

¹⁰⁷ Ibid, p.28.

¹⁰⁸ Loc cit.

relationship in which fiduciary obligations would not normally be expected. I agree with this comment of Professor Finn in "The Fiduciary Principle", supra, at p.64:

What must be shown, in the writer's view, is that the actual circumstances of a relationship are such that one party is entitled to expect that the other will act in his interests in and for the purposes of the relationship. Ascendancy, influence, vulnerability, trust, confidence or dependence doubtless will be of importance in making this out. But they will be important only to the extent that they evidence a relationship suggesting that entitlement. The critical matter in the end is the role that the alleged fiduciary has, or should be taken to have, in the relationship. It must so implicate that party in the other's affairs or so align him with the protection or advancement of that other's interests that foundation exists for the "fiduciary expectation". Such a role may generate an actual expectation that other's interests are being served. This is commonly so with lawyers and investment advisers. But equally the expectation may be a judicially prescribed one because the law itself ordains it to be that other's entitlement. And this may be so either because that party should, given the actual circumstances of the relationship, be accorded that entitlement irrespective of whether he has adverted to the matter, or because the purpose of the relationship itself is perceived to be such that to allow disloyalty in it would be to jeopardize its perceived social utility.

It is in this sense, then, that the existence of a fiduciary obligation can be said to be a question of fact to be determined by examining the specific facts and circumstances surrounding each relationship... If the facts give rise to a fiduciary obligation, a breach of the duties thereby imposed will give rise to a claim for equitable relief.¹⁰⁹

While Mahon J. and Cory J.A., as he then was, would impose certain fiduciary obligations on directors in certain transactions as a matter of course, it is this second usage of the term "fiduciary" which best reflects the examination and analysis of the factual context which most courts complete before they will impose common law fiduciary duties on corporate insiders in favour of shareholders.

The third usage of the term "fiduciary" discussed by LaForest J. is the exercise of labelling a fact situation as "fiduciary" in order to justify the creation of a particular remedy even though the facts do not entail particular fiduciary obligations. As LaForest J. comments, "Courts have resorted to fiduciary language because of the view that certain remedies, deemed appropriate in the circumstances, would not be available unless a fiduciary relationship was present."¹¹⁰ He concludes that this usage of the term "fiduciary" "is a misuse of the term".¹¹¹ Interestingly, Sopinka J. acknowledges this form of reasoning from conclusions, but from a different perspective. Rather than being attracted to finding fiduciary relationships, Sopinka J. observes that judges avoid such findings in order to avoid the remedies associated therewith. He states, "The consequences attendant on a finding of a fiduciary

¹⁰⁹ Ibid, p.29.

¹¹⁰ Ibid, p.30.

¹¹¹ Ibid, p.32.

relationship and its breach have resulted in judicial reluctance to do so except where the application of this blunt tool of equity is really necessary."¹¹²

Brant Investments Ltd. v. KeepRite Inc.

Brant Investments Ltd. v. KeepRite Inc.,¹¹³ a recent decision of the Ontario Court of Appeal, takes us from fact situations in which directors have been involved in the purchase and sale of shares of their corporations and in which they have been disproportionately enriched in comparison to the other shareholders. The case does not contain facts which shock the conscience. Rather, the central fact of the case is the purchase by KeepRite Inc. ("KeepRite") of certain assets from parties related to KeepRite. This was a bona fide, though unique, transaction in the course of the KeepRite's business. It was also, however, a transaction to which certain of KeepRite's minority shareholders (the "dissenting shareholders") objected. The case raises the question of whether majority shareholders or directors are fiduciaries for shareholders in the context of such business transactions and, more generally, in the context of the on-going business operations of the corporation. The decision provides insight into the Court of Appeal's likely disposition of fiduciary claims made by shareholders against directors.

Two appeals were considered by the Court of Appeal in this case. The first arises from the dissenting shareholders' application against KeepRite, KeepRite's majority shareholder and that shareholder's affiliates pursuant to the oppression remedy provisions of the CBCA. The second arises from KeepRite's obligation to pay fair value to the dissenting shareholders for their shares pursuant to the dissent rights provisions of the CBCA. In the course of its consideration of the oppression remedy appeal, the Court of Appeal provides further authority for the proposition that in Canada directors generally are not in a fiduciary

¹¹² Ibid, p.60.

¹¹³ Footnote 8.

relationship with shareholders by virtue of office alone. While the Court of Appeal rejected a categorical rule that directors are fiduciaries for shareholders, it confirmed that in certain situations, directors may be in a fiduciary relationship to shareholders. Such situations are to be identified on a case by case basis, and the imposition of fiduciary obligations will depend on the facts of each case.

The Factual Background

The dissenting shareholders were a group of "institutional investors, investment managers, and their nominees".¹¹⁴ Their complaint arose in connection with a transaction between KeepRite and two wholly-owned subsidiaries of KeepRite's major shareholder, Inter-City Manufacturing Ltd. ("ICM"). ICM held approximately 64% of the shares of KeepRite. The dissenting shareholders collectively held approximately 28% of the KeepRite shares and individual minority shareholders collectively held the remaining 8%.

ICM and corporations related to it carried on various businesses including the manufacture and sale of heating equipment. KeepRite manufactured and sold air conditioning equipment. When ICM's interest in KeepRite was acquired, the complementary nature of the two businesses, heating and refrigeration, was considered. Both businesses were seasonal, and it was believed that various efficiencies could be achieved by integrating them.

In October 1982, an officer of KeepRite proposed that the two businesses be fully merged. This result was to be achieved by KeepRite's purchasing certain assets of two of ICM's wholly-owned subsidiaries. The purchase price was to be paid by promissory notes which were to be payable once KeepRite sold an issue of share purchase rights which were to be created.

¹¹⁴ Ibid, p.322.

A committee (the "Independent Committee") of the board of directors of KeepRite was formed to review the proposed transaction. The members of the Independent Committee were not directors or officers of ICM's parent corporation, Inter-City Gas Corporation, and, while the Court of Appeal's outline of the facts does not so state, it seems clear that they were not directors of ICM or its subsidiaries either. The three committee members, two lawyers and a stock broker, were experienced businessmen. They met five times to review the proposed transaction and in the course of their review they considered various reports concerning "the merits of the proposed acquisition, the price of the assets to be acquired, and the means of financing".¹¹⁵ As McKinlay J.A. notes, "The trial judge found as a fact that the members of the committee were truly independent in the sense that they felt at all times free to deal with the impugned transaction upon its merits".¹¹⁶ Later, she states the following:

The trial judge was satisfied that the independent committee was aware of its mandate, was at all times conscious that this was not an arm's-length transaction, and appropriately carried out its function of assessing the benefits of the transaction to KeepRite. He was completely satisfied on the evidence that the committee carried out its function in an appropriate and independent manner. I see no reason whatever to doubt the correctness of that finding. Neither the evidence nor the argument persuades me that his findings were anything other than appropriate.¹¹⁷

Following its review of the transaction, the Independent Committee advised the KeepRite board that the acquisition would be desirable.

¹¹⁵ Ibid, p.294.

¹¹⁶ Ibid, p.313.

¹¹⁷ Ibid, p.319.

Shareholder approval was obtained to create the new share purchase rights which were to be issued to finance the acquisition. The dissenting shareholders voted against the resolution authorizing the creation of the new share purchase rights. Nonetheless, the impugned transaction was implemented. The dissenting shareholders invoked their right under the CBCA to dissent and be paid fair value for their shares. The KeepRite board offered to pay the dissenting shareholders \$9.00 per share as the fair value for their shares. When the dissenting shareholders refused this offer, KeepRite applied to the court to fix the fair value of the shares. Subsequently, the dissenting shareholders brought an application against KeepRite, ICM and ICM's affiliates for relief under the provisions of the CBCA oppression remedy.

In the early stages of this lengthy piece of litigation, the dissenting shareholders complaint was that the acquisition from related companies was for an amount in excess of fair market value without full disclosure in the circular.¹¹⁸ The dissenting shareholders further alleged that the acquisition would adversely affect their share earnings and the value of their shares.¹¹⁹ Before the Court of Appeal, the focus of the dissenting shareholders' complaint was the role of the Independent Committee. They attacked the Committee's role "on the basis, first, that it was not, in fact, independent, and second, that the advice given by the committee to the directors of KeepRite was not in the best interests of the company and its shareholders."¹²⁰ More specifically, the dissenting shareholders criticized the work of the Independent Committee on the following bases:

- (a) the committee did not consider whether there were alternative transactions open to KeepRite;

¹¹⁸ Brant Investments Ltd. et al. and KeepRite Inc. et al., Re, (1983), 44 OR (2d) 661, at p.662 (HCJ).

¹¹⁹ Loc cit.

¹²⁰ Footnote 8, p.313.

- (b) the committee approved the transaction based upon assurances that certain "synergistic" benefits could be achieved by combining the businesses - they were aware of the need for a strategic plan to realize these benefits but proceeded without obtaining one;
- (c) the committee never received a final report from the consultants retained to review management's assumptions concerning the anticipated synergies; and
- (d) the committee did not commission a valuation of the Inter-City businesses on a going concern basis.¹²¹

The Court of Appeal considered each of these complaints and found that they were each without merit.

Fiduciary Relationships within the Corporation

(i) Fiduciary Relationships and the Oppression Remedy

The arguments of the dissenting shareholders married two bases for relief: the CBCA oppression remedy and an alleged fiduciary relationship between KeepRite's majority shareholder or its nominees, the directors, and the dissenting shareholders. As McKinlay J.A. notes, the dissenting shareholders "argue that the issues of fiduciary duty and oppression are intertwined on the facts of this case and that, if a breach of fiduciary duty were established, that breach would necessarily result in a concurrent finding of oppression under s.234 [now s.241]".¹²² Just as the arguments of the dissenting shareholders marry the oppression remedy

¹²¹ Ibid, p.314.

¹²² Ibid, p.298.

and fiduciary duties, so does the Court of Appeal in its reasons. For example, the Court states the following:

In an application under [CBCA] s. 234 [now s. 241], evidence of any relevant agreement between the parties and evidence of the circumstances of their relationship would appropriately be adduced to assist in determining whether the facts of the case warrant a remedy. Because the statutory scheme of s. 234 is so broadly formulated, the evidence necessary to establish a breach of fiduciary duty would be subsumed in the broader range of evidence which would be appropriately adduced on an application under the section.¹²³

The thrust of this reasoning is that a separate cause of action for breach of fiduciary duty need no longer be made by shareholders. This view would substitute the oppression remedy which is highly discretionary in terms of the fashioned remedy¹²⁴, for the remedies associated with breach of fiduciary duty, which, as we saw in the discussion of Regal (Hastings), Ltd. v. Gulliver in Chapter Two, are rigorously restitutionary. It is regrettable that the Court of Appeal did not explicitly acknowledge that there may be separate causes of action for breach of fiduciary duty and for a statutory oppression remedy, just as the Court below had on two occasions in the history of this litigation explicitly acknowledged that a shareholder may both seek fair value for its shares under the dissent provisions and a remedy under the statutory oppression remedy provisions.¹²⁵

¹²³ Id., p.302.

¹²⁴ Subsection 241(3) of the CBCA contains a lengthy, but not exhaustive, list of remedial measures which a judge “may” impose. Subsection 248(3) of the OBCA contains a virtually identical list.

¹²⁵ See Footnote 118, at pp.663-665 and Brant Investments Ltd. et al. and KeepRite Inc. et al., Re. (1987), 60 OR (2d) 737 at pp. 751-752 (H.C.J.).

The primacy of the statutory oppression remedy undoubtedly follows from the Court of Appeal's inability to find any authority for the imposition of "fiduciary duty on majority shareholders or directors in favour of minority shareholders".¹²⁶ More dramatically, the Court declares, "The enactment of these [statutory oppression remedy] provisions has rendered any argument for a broadening of the categories of fiduciary relationships in the corporate context unnecessary and, in my view, inappropriate",¹²⁷ a declaration which shall be considered further below. In short, the Court indicates that the search for a well-reasoned, clear and consistent law of fiduciary duties to shareholders should cease.

The mixing of the oppression remedy and claims based on fiduciary relationship is unfortunate because it tacitly, and incorrectly, suggests that claims of fiduciary duty against directors are not independent of claims based on the oppression remedy. Put otherwise, the Court of Appeal seems to have adopted the view that the oppression remedy has subsumed claims based on fiduciary relationships in "the corporate context". Such a view goes far beyond what was required for the Court of Appeal to reach its decision in the oppression remedy appeal. The view is dangerous because it may encourage corporate law practitioners not to consider separately claims which may be based on the oppression remedy and claims which may be based on a fiduciary relationship. Such an approach would overlook those factors which may support the imposition of fiduciary duty even though relief under the oppression remedy may not be available.

The dissenting shareholders' marriage of the oppression remedy and fiduciary relationships seems to have been rooted in two questionable propositions of law:

¹²⁶ Footnote 8, p.301.

¹²⁷ Loc cit.

1. that directors or majority shareholders are in a fiduciary relationship to shareholders; and
2. that fiduciaries owe their beneficiaries specific duties.

As to the first proposition, we have already noted that the Court of Appeal addressed it directly, though primarily by reference to precedent and without much consideration of the underlying policy issues. The Court stated that it was referred to no case which "imposes a fiduciary duty on majority shareholders or directors in favour of minority shareholders".¹²⁸ Interestingly, counsel to the dissenting shareholders may have made the first proposition somewhat less clearly than stated above. The trial judge notes that counsel for the dissenting shareholders submitted that "there is a near fiduciary duty of majority shareholders to the minority"¹²⁹ (emphasis added). Although counsel for the dissenting shareholders may have been attempting to establish some new, lower standard of fiduciary relations in the corporation, the Court of Appeal preferred to consider the law along more traditional lines and this case lacked the facts to fall within the traditional ideas of fiduciary relationships. Unfortunately, in reaching this conclusion, the Court of Appeal did not consider the powerful dissent of their former colleague, Cory J.A., as he then was, in Bell v. Source Data Control Ltd. (McKinlay J.A. was a member of the panel which heard the Bell v. Source Data Control Ltd. case and she concurred in the majority reasons delivered by Brooke J.A.) The Court was also apparently not advised of the B.C. Court of Appeal's decision in Dusik v. Newton. Cory J.A. in Bell articulates a limited rule that a director is per se in a fiduciary relationship with shareholders and both Cory J.A. and the B.C. Court of Appeal in Dusik articulate convincing reasons for imposing fiduciary duties on directors in the particular circumstances of those cases. These decisions call courts to determine whether there are convincing reasons for imposing fiduciary duties in a particular case and not to be

¹²⁸ Loc cit.

¹²⁹ 60 OR (2d) 737, p.760.

diverted from this task by the existence of a statutory oppression remedy. In Brant Investments, there were no convincing reasons to impose additional duties on the majority shareholder or the directors, fiduciary or otherwise, as we shall discuss more fully below.

Even if majority shareholders or directors were in a fiduciary relationship with shareholders, the dissenting shareholders' second proposition, that fiduciaries must perform specific duties, is weak. As LaForest J. stated in LAC Minerals Ltd. v. International Corona Resources Ltd., "The label fiduciary imposes no obligations, but rather is merely facilitative in achieving what appears to be the appropriate result."¹³⁰ The law imposes appropriate duties on the fiduciary once he is found to be a fiduciary and although there are standard duties such as the duty to make full disclosure, there does not appear to be a uniform and unchanging set of duties which fiduciaries must perform. Particularly in view of the review by the Independent Committee of KeepRite's acquisition of assets from ICM's subsidiaries, it is difficult to accept the dissenting shareholders' proposition that ICM or the KeepRite directors failed to perform or performed poorly fiduciary duties owing to the dissenting shareholders. The lack of need for the imposition of additional fiduciary duties on the directors or majority shareholder may well have influenced the Court of Appeal's thinking about fiduciary duties owed to shareholders.

The dissenting shareholders may have argued that a breach of fiduciary duty constituted oppression within the meaning of CBCA s. 241 because fiduciary duties have been imposed even where directors have acted with the utmost good faith (Regal (Hastings), Ltd., Boardman v. Phipps), while the oppression remedy had, prior to Brant Investments, not been successfully invoked in such situations. The equating of a breach of fiduciary duty with statutory oppression was designed to ensure that even bona fide acts of directors and majority shareholders could form the basis for relief under the oppression remedy. The Court of Appeal, however, did not adopt the dissenting shareholders' equating of breach of fiduciary duty to

¹³⁰ Footnote 92, p.30.

statutory oppression in support of its raising the standard of conduct which may constitute statutory oppression. Rather, based on a strict reading of the statutory oppression remedy and a careful consideration of relevant cases, the Court of Appeal concludes that "evidence of bad faith or want of probity in the actions complained of is unnecessary in an application under s. 234 [now s.241]".¹³¹ The Court of Appeal thereby obviated this reason for making separate fiduciary and oppression claims in a case. The Court of Appeal was able to set the conduct required by the statutory oppression remedy at a high standard without reference to the common law of fiduciary relationships. Did the Court, thereby, subsume fiduciary relationships within the corporation under the statutory oppression remedy?

The grounds of complaint set out in the oppression remedy do not appear to encompass those situations where directors purchase and hold shares of their corporations and in which some judges are prepared to impose fiduciary duties on those directors. The situation outlined in Coleman v. Myers, for example, where a director who is also a minority shareholder purchases (through his corporation) shares of other shareholders is not contemplated by CBCA s. 241(2). Similarly, the statutory grounds of complaint do not, by their terms, apply to situations such as those in Dusik v. Newton or Bell v. Source Data Control Ltd. where directors who are also majority shareholders sell their shares to a third party at prices substantially in excess of those realized by the minority shareholders. In short, there are fact situations where there are convincing reasons to find a remedy but where the grounds of the oppression remedy may be too narrow to provide relief. In some such situations the courts have imposed fiduciary duties. The sphere of the oppression remedy and fiduciary duties as they have been imposed on directors are not entirely identical. Thus, the possibility that fiduciary relationships may exist between directors and shareholders and that fiduciary duties may be imposed on directors has not been completely overtaken by the enactment of the statutory oppression remedy. Such possibilities predated the enactment of the statutory oppression remedy and remain, though

¹³¹ Footnote 8, p.305.

probably narrowed in scope by the enactment of the oppression remedy. In short, where appropriate facts exist, a claim of fiduciary relationship forms the basis of a separate cause of action independent of the oppression remedy.

(ii) Shareholders and Directors as Fiduciaries

The dissenting shareholders asserted that "the common law recognizes a fiduciary duty owed by a majority shareholder to the minority".¹³² The Court of Appeal dealt with the issue of fiduciary duties more broadly and its pronouncements relate to fiduciary duties which may be owed to shareholders by either majority shareholders or directors. A more rigorous segregation of categories of actors within the corporation would have been desirable because there are different reasons for requiring directors and majority shareholders to act in a fiduciary capacity for other shareholders. As discussed previously, directors have inside information which is not necessarily available to any shareholder whether a majority or minority shareholder. Essentially, on the issue of fiduciary duty, it would appear that the Court of Appeal views directors as no more than the nominees of majority shareholders. This approach is in accord with the analysis of shareholder fiduciary duties made by MacIntosh, Holmes and Thompson.¹³³

The Court of Appeal rejected the proposition that directors, by virtue only of the office which they occupy, owe fiduciary duties to shareholders. As discussed in connection with Coleman v. Myers, above, such a proposition may be called a per se rule or a rule of law that directors owe fiduciary duties to shareholders. In rejecting such a per se rule, the Court of Appeal stated that "none of the ... authorities [considered] imposes a

¹³² Ibid, p.298.

¹³³ Op. cit., footnote 79.

fiduciary duty on majority shareholders or directors in favour of minority shareholders".¹³⁴ The Court continued by noting that the enactment of the oppression remedy in the CBCA and CBCA - cognate statutes has stemmed the need to search for a per se rule concerning fiduciary relationships in "the corporate context". The Court stated the following:

The enactment of these [oppression remedy] provisions has rendered any argument for a broadening of the categories of fiduciary relationships in the corporate context unnecessary and, in my view, inappropriate.¹³⁵

In support of this statement, McKinlay J.A. notes the existence of the statutory fiduciary duty imposed on directors in CBCA s. 122 to "act honestly and in good faith with a view to the best interests of the corporation". She continues:

Acting in the best interests of the corporation could, in some circumstances, require that a director or officer act other than in the best interests of one of the groups protected under s.234 [now s.241]. To impose upon directors and officers a fiduciary duty to the corporation as well as to individual groups of shareholders of the corporation could place directors in a position of irreconcilable conflict, particularly in situations where the corporation is faced with adverse economic conditions.¹³⁶

While the offered rationale makes sense in situations in which the corporation's interests and those of its shareholders conflict, such conflicts should be infrequent in a corporation's history.

¹³⁴ Ibid, p. 301.

¹³⁵ Loc cit.

¹³⁶ Loc cit.

Thus, the Court of Appeal has dealt in advance with the infrequent situation of corporation-shareholder conflict by indicating that directors must always act in the best interests of the corporation and can, therefore, never be required to act in the best interests of shareholders. This view is inappropriate since it uses an infrequent occurrence to preclude the development of law intended to protect shareholders from what could be not infrequent prejudicial conduct. More importantly, it seems wrong at law as we have discussed above under the heading "Directors' Responsibility to Manage" in Chapter 3. Arguably, the oppression remedy is an effective check on objectionable treatment of shareholders. The oppression remedy does not convert directors into fiduciaries for shareholders in all circumstances, however. It underscores the point that directors should not treat shareholders unfairly; if directors are viewed as fiduciaries for shareholders, directors would be required to treat shareholders fairly.

Apart from the Court of Appeal's questionable rationale for foreclosing the broadening of categories of fiduciary relationships in "the corporate context", the Court's statement raises further difficulties. First, the phrase "the corporate context" is not clear. As noted above, courts have imposed fiduciary duties on directors in the purchase and sale of shares. Such transactions would seem to be within "the corporate context". Perhaps the Court of Appeal should have used more specific words to describe those relationships where arguments in support of fiduciary relationships have, in its view, been foreclosed by the enactment of the oppression remedy. It may be unnecessary, however, to press this criticism. Perhaps the phrase "the corporate context" was used as a compendious, though imprecise, phrase to identify relationships within the corporation such as the relationship between directors and shareholders or among shareholders. If so, the phrase was used because the Court of Appeal chose not to articulate clear rules governing any particular relationship which is claimed to be infused with a fiduciary character. This reading of the Court of Appeal's statement deprives it of its most extreme meaning which is that no relationships involving shareholders are fiduciary in nature. It is, however, appropriate to restrict the reading of this phrase because it is obiter.

Secondly, the Court of Appeal gives inadequate consideration to the common law basis for imposing fiduciary duties. While it may be that the enactment of the statutory oppression remedy has supplanted the evolving common law of fiduciary relationships, at least in "the corporate context", the Court of Appeal certainly does not provide a clear analysis of how the statutory enactments have codified or modified the common law of fiduciary relations in "the corporate context". In fact, the Court's observation that "a broadening of the categories of fiduciary relationships in the corporate context [is] unnecessary", runs counter to the general law relating to fiduciaries. In Regal (Hastings), Ltd. v. Gulliver, for example, it was apparent from the Law Lords' discussion of the concept of "fiduciary position" that fiduciaries are not limited to those categories of persons traditionally identified as such. A similarly authoritative pronouncement was made by Dickson J., as he then was, in Guerin v. The Queen where he stated, "The categories of fiduciary, like those of negligence, should not be considered closed".¹³⁷ Sadly, while the Court of Appeal in Brant Investments Ltd. v. KeepRite Inc. appears to accept the general proposition that the categories of fiduciary relationships are not closed,¹³⁸ it is clearly of the view that such categories are closed in "the corporate context". The enactment of the statutory oppression remedy does not seem to be a sufficient basis for the Court of Appeal to adopt this view which is so out of step with the authoritative pronouncements of other courts.

One of the curious aspects of this decision is that while the Court of Appeal lowers the curtain on a categorical or per se rule that directors are fiduciaries for shareholders, the Court then raises the curtain to reveal the continued rule that directors may come to be fiduciaries for shareholders in certain circumstances. McKinlay J.A. states, "Courts impose fiduciary duties only in situations where someone stands in a particular position of trust by virtue

¹³⁷ Footnote 98.

¹³⁸ See, for example, footnote 8, p.298.

of an agreement or as a result of the circumstances and relationship of the parties".¹³⁹ The Court provides no guidance concerning the factors which may create an appropriate set of circumstances or an appropriate relationship for the imposition of fiduciary duties on a director or a majority shareholder in favour of a minority shareholder. Clearly, however, the facts of this case do not constitute such circumstances or such a relationship.

The transaction at issue, though unique, was a bona fide transaction in the business of KeepRite. In deciding whether to enter into the transaction and in setting the terms of the transaction, the directors sought to observe the statutory fiduciary duty imposed on directors in the exercise of their powers and discharge of their duties to "manage the business and affairs of... [the] corporation" as required by CBCA s.102(1). In this regard, the position of the KeepRite directors differed greatly from that of the directors in Dusik v. Newton and Bell v. Source Data Control Ltd. who, in selling their shares, were not exercising their powers or discharging their duties to manage the business and affairs of the corporations there in issue.

Not only were the KeepRite directors subject to a statutory fiduciary duty in favour of the corporation, but it is also difficult to find fault with their conduct from the perspective of the shareholders. Assuming that the KeepRite directors were in a fiduciary relationship to the dissenting shareholders, what fiduciary duties could they be considered to have breached? The impugned transaction was disclosed to all KeepRite shareholders and the requisite level of shareholder assent to the transaction was obtained. The activities of the KeepRite directors also differed greatly from the activities of the directors in Dusik v. Newton and Bell v. Source Data Control Ltd. who were not at all forthright with the other shareholders.

Bearing in mind LaForest J.'s view that fiduciary obligations are not predetermined and immutable but are, rather, crafted in the circumstances of particular cases to

¹³⁹ Ibid, p.302.

achieve the appropriate result, the dissenting shareholders argued that there were fiduciary duties, other than the standard duties of making disclosure and obtaining assent, which the KeepRite directors were obliged to perform. These duties may be extracted from the Court of Appeal's reasons to include a duty to consider "any available alternative transaction", not to enter into the impugned transaction unless it is "at least as advantageous to the company and to all shareholders" as any such alternative transaction, to resist any "undue pressure" from the majority shareholder to enter into the transaction and, in the case of the majority shareholder, not to apply any such pressure, and to ensure that "the substance of the impugned transaction and the process of decision-making leading to its acceptance" are "intrinsically fair to the dissenting shareholders".¹⁴⁰ Essentially, the dissenting shareholders argued that a high standard of impartiality is required of a corporation's decision-makers in a related party transaction and that such decision-makers have a duty to find the best deal for their corporations. Such a duty is, however, statutorily imposed by CBCA s. 122 subject to certain limits of reasonableness. As McKinlay J.A. notes, "To suggest that directors are required, when entering into a transaction on behalf of the corporation, to consider every available alternative transaction is unrealistic. The extent to which directors should inquire as to alternatives is a business decision, which, if made honestly in the best interests of the corporation, should not be interfered with".¹⁴¹

It is arguable that ICM obtained some special benefit from the transaction that other shareholders did not obtain. ICM or its subsidiaries wished to sell certain assets to KeepRite and the proceeds of the sale could be paid to ICM by dividends, presumably on a tax-free basis. There was, therefore, an indirect benefit to ICM, the value of which cannot be quantified on the basis of the facts contained in the Court of Appeal's reasons. It should be noted that the dissenting shareholders argued that a burden of proof to demonstrate compliance

¹⁴⁰ Ibid, p.311.

¹⁴¹ Ibid, p.312.

with the fiduciary duties discussed in the previous paragraph arises where "a dissenting shareholder has shown that an impugned transaction involves benefits to one group of shareholders in which dissenting shareholders do not share, and a corresponding detriment to the dissenting shareholders which the other group of shareholders do not suffer".¹⁴² Does the possibility of dividends from its subsidiaries constitute such a benefit to ICM? Certainly the impugned transaction placed ICM as a shareholder of KeepRite in a position no different from that of any other shareholder of KeepRite. Moreover, any indirect benefit received by ICM was obtained at the cost to its subsidiaries of their divestiture of certain assets, a divestiture not made by any of the dissenting shareholders. The trial judge concluded "that there were [no] benefits to ICG [ICM's parent corporation] which were not shared by the dissenting shareholders" and "that the dissenting shareholders suffered... [no] detriment which ICG did not suffer".¹⁴³ Certainly, where a benefit has been received by one group of shareholders and a corresponding detriment has been experienced by other shareholders, there is ground for complaint. We reasonably expect that shareholders will be treated fairly and equally as between themselves. Put otherwise, we expect that directors will deal with shareholders on an even-handed basis.¹⁴⁴

¹⁴² Ibid, p.311.

¹⁴³ Loc cit. Concerns about the possibility of minority shareholder abuse in related party transactions such as this have led the OSC to issue Policy Statement 9.1 - Disclosure, Valuation, Review and Approval Requirements and Recommendations for Insider Bids, Issuer Bids, Going Private Transactions and Related Party Transactions (1991), 14 OSCB 3345.

¹⁴⁴ As a statutory basis for these expectations, see OBCA s. 22(6) which states "Except as provided in section 25 [which relates to shares of a class issuable in series with various rights as between the series], each share of a class shall be the same in all respects as every other share of that class". See also s. 24(5) of the *Alberta Business Corporations Act*, SA 1985, c. B-15 which states "Subject to section 27, if a corporation has more than one class of shares, the rights of the holders of the shares of any class are equal in all respects." There is no corresponding provision in the CBCA, however the Ontario Court of Appeal in Bowater Canadian Ltd. v. R.L. Crain Inc. (1987), 39 BLR 34, echoing the Alberta provision, held that the rights attached to a class of shares of a CBCA corporation must be provided equally to all shares of that class based on the principle that rights attach to the share and not to the shareholder.

But the facts of this case contain no suggestion that the price paid for the assets was too high or that the terms of payment were too onerous, factors which could constitute an abuse of minority shareholders in related party transactions.

Just as the circumstances of the case formed no basis for the court to impose fiduciary duties on the KeepRite directors or on ICM, so too the relationship between the parties. The dissenting shareholders were sophisticated, financially substantial investors.¹⁴⁵ KeepRite was not a closely-held corporation such as those where claims of fiduciary duty against directors in favour of vulnerable shareholders have hitherto succeeded. KeepRite was a publicly-traded corporation. Its shares were listed on The Toronto Stock Exchange. There was no evidence that any of the dissenting shareholders sustained the type of damage sustained by the minority shareholders in Dusik v. Newton or Bell v. Source Data Control Ltd., the type of damage to which the directors of those corporations could reasonably be expected to be attuned and from which those directors could reasonably be expected to protect the corporation's shareholders.

To summarize, there was no agreement by which the KeepRite directors or ICM assumed a position of trust vis-a-vis the dissenting shareholders and the facts of the case did not constitute "circumstances" or a "relationship of the parties" which justified imposing fiduciary duties. McKinlay J.A. concludes, "[O]n the facts of this case, I do not consider that the respondents, the board of directors of KeepRite, or the members of the independent committee owed a fiduciary duty to the appellants".¹⁴⁶ In short, the facts of this case formed a poor context for asserting that the directors or the majority shareholder owed fiduciary duties to the dissenting shareholders. Naturally, had the dissenting shareholders succeeded in their argument that directors and majority shareholders owe fiduciary duties to shareholders by virtue

¹⁴⁵ Footnote 8, p.322.

¹⁴⁶ Ibid, p.302.

of their respective positions alone, the factual context would not have been so important and the result may have differed.

CHAPTER 6

CONCLUSION

The process of securities and corporate law reform in the 1960s and 1970s led to the enactment of various statutory fiduciary obligations on directors and insiders. Chief among these were the take-over bid rules and the insider trading rules. Unfortunately, a unified set of principles governing the position of the shareholder was not among these reforms. Thus, shareholders, particularly of closely-held corporations, have had to look to the courts to fashion appropriate remedies. Sometimes the courts have been willing to extend a remedy in unregulated take-over situations, as in Dusik v. Newton,¹ and sometimes they have not, as in Bell v. Source Data Control Ltd.² The cases yield highly unpredictable results. Cases such as these have presented to the courts the opportunity to unify certain elements of Canadian corporate law; to synthesize the principles underlying the statutory reforms and to articulate appropriate common law fiduciary principles; in short, to develop a single, predictable law of shareholder rights. Sadly, this has not occurred.

It appears that the Canadian courts, with the aid of securities and corporate law reformers, have disposed of the authority of Percival v. Wright³ although some recent decisions repeat the law unamended from the era of Percival v. Wright. Berger J. in Roberts et al. v. Pelling et al. takes virtually from the pages of Percival v. Wright the continued common law position that "there is no fiduciary obligation as between shareholders, and no general

¹ (1985), 62 BCLR 1 (CA).

² (1988), 40 BLR 10, 66 OR(2d) 78 (Ont CA).

³ [1902]2 Ch 421.

fiduciary obligation owed by a director to shareholders".⁴ Moreover, the courts remain concerned about possible conflicts between a director's duties to the corporation and to the corporation's shareholders.⁵ As the Dusik and Bell cases demonstrate, some Canadian courts and judges have been willing to impose fiduciary duties on directors in certain situations involving the purchase and sale of the corporation's shares. In fact, the fiduciary principles involved have been extended to other corporate insiders, namely to majority shareholders in Dusik and Bell and, arguably, to officers in NIR Oil Ltd. v. Bodrug.⁶ There is also an indication in NIR Oil that the principles extend beyond the confines of closely-held corporations and apply to publicly-traded corporations. Further, the decision in Vladi Private Islands v. Haase suggests that fiduciary duties may be imposed on corporate insiders in situations other than share purchase and sale transactions.⁷

The common law of fiduciary relations between corporate insiders and shareholders was significantly developed by the seminal decision in Coleman v. Myers.⁸ This area of common law continues to develop as new situations in which fiduciary duties may properly be imposed are identified. Likewise the theoretical framework of the law of fiduciary relations continues to develop. The misdirected analogies used in Percival v. Wright may be thankfully forgotten. They have been replaced by the illuminating analysis of decisions such as the Supreme Court of Canada's recent decision in LAC Minerals Ltd. v. International Corona Resources Ltd.⁹ Although the Supreme Court is clearly composed of two factions concerning

⁴ (1981), 16 BLR 150 (BCSC) at p. 153.

⁵ See Brant Investment Ltd. v. KeepRite Inc.(1991), 3 OR(3d) 289 at p.301.

⁶ (1985), 38 Alta LR (2d) 321 (Alta CA).

⁷ (1990), 96 NSR (2d) 323 (NSCA).

⁸ [1977]2 NZLR 225 (SC); [1977]2 NZLR 297 (CA).

⁹ (1989), 61 DLR (4th) 14.

the expansion of the law of fiduciary relations, new uses of the common law of fiduciary relations within corporations are suggested by decisions such as LAC Minerals. The development of fiduciary duties within the corporation may, however, be restricted by the statutory regime governing corporations. The Ontario Court of Appeal in Brant Investments Ltd. v. KeepRite Inc., has held that the statutory oppression remedy and the statutory fiduciary relationship imposed on directors in favour of their corporations support the conclusion that there is no absolute fiduciary duty owed by directors to shareholders. The reluctance of the courts to impose fiduciary duties,¹⁰ the rarity of fact situations sufficiently egregious to warrant the imposition of fiduciary duties,¹¹ and the enactment of various statutory remedies¹² combine to indicate that the common law of fiduciary duties within corporations does not hold the promise of further rich development. It may be predicted that in those situations in which there are alternative bases of liability such as statutory liability for insider trading based on specific confidential information or common law fiduciary duty liability, the courts will decline to impose common law fiduciary duties. Accordingly, the range of fact situations in which fiduciary duties may be imposed should not be expected to expand rapidly.¹³

¹⁰ As discussed by Sopinka J. in LAC Minerals Ltd. v. International Corona Resources Ltd., at p.60.

¹¹ For example, Bell v. Source Data Control Ltd.

¹² For example, Brant Investments Ltd. v. KeepRite Inc.

¹³ Commentators have mixed views on the likely future for the law of fiduciary relations in Canadian corporate law. J.G. Macintosh, J. Holmes and S. Thompson in "The Puzzle of Shareholder Fiduciary Duties" (1991), 19 CBLJ 86 conclude at p.137, "We predict that it will not be long before the courts explicitly recognize the existence of shareholder fiduciary duties." The decision of the Ontario Court of Appeal in Brant Investments Ltd. v. KeepRite Inc. would appear to have dealt a serious blow to this prediction. This view is shared by B. Welling in Corporate Law in Canada: The Governing Principles (Toronto: Butterworths, 1991) at p.635 where the author states, "The analysis of the Ontario Court of Appeal, reviewing the nature of minority remedies in Canada in Brant Investments Ltd. v. KeepRite Inc. ... should finally dispose of the notion of majority shareholders as fiduciaries for the minority: time will tell."

The process of developing "the common law of responsibility of corporate management"¹⁴ has been slow, probably slower than the Federal Task Force would have contemplated, but there have been some notable achievements. Chief among these are the Dusik case and its progeny Vladi Private Islands and NIR Oil. Such development should continue with the aid of the LAC Minerals jurisprudence. Unfortunately, this development is not without points of pause: Bell v. Source Data Control Ltd. Further, despite its sparkling analysis on several issues, the Brant Investments Ltd. decision is a rather retrograde step.

The decision in Brant Investments Ltd. really amounts to a rejection of the idea that directors and majority shareholders owe fiduciary duties to shareholders. One can see Percival v. Wright arising, phoenix-like, from its resting place in legal history on this reading of Brant Investments. Undeniably, the Court of Appeal was correct when it stated, "To import the concept of breach of fiduciary duty into ... [the oppression remedy] provision would ... complicate its interpretation and application ..."¹⁵ This reason, alone, does not justify the conclusion that the "enactment of these provisions has rendered any argument for a broadening of the categories of fiduciary relationship in the corporate context unnecessary and, in my view, inappropriate."¹⁶ The Court of Appeal also states that importing the concept of fiduciary duties to shareholders into the oppression remedy "could be inimical to the statutory fiduciary duty imposed upon directors in [CBCA, s.122(1)]."¹⁷ (Emphasis added.) It is apparent that the Court's view is that directors must act in the best interests of the corporation exclusively. As we discussed above under the heading "Directors' Responsibility to Manage", CBCA, s.102(1)

¹⁴ Canada, Proposals for a New Business Corporation Law for Canada (Ottawa: Information Canada, 1971), v. I, para. 477, p.159.

¹⁵ Footnote 5 at p.301.

¹⁶ Loc cit.

¹⁷ Loc cit.

may well impose duties on directors in favour of shareholders. This statutory duty, supplemented by cases requiring directors to act in the interests of the company as a whole and by cases such as Coleman v. Myers, in which fiduciary duties are imposed on directors, suggests that a balancing of competing fiduciary claims in favour of the corporation and in favour of shareholders may be required in some cases. This conclusion is supported by the limitation on directors' statutory fiduciary duty to the corporation, which is that directors are required to act only "with a view to the best interests of the corporation"; they are not obliged to act solely in the best interests of the corporation. Who is to balance competing fiduciary claims when the courts so utterly deny that such an exercise is required?

Such a balancing function is undoubtedly difficult, but it is one for which courts have traditionally been viewed as well suited. As John Howard has shown, cases involving claims of fiduciary duty have all been resolved on moral grounds.¹⁸ As we have seen in Rathie v. Montreal Trust Co.,¹⁹ Coleman v. Myers, Bell v. Source Data Control Ltd. and LAC Minerals Ltd. v. International Corona Resources Ltd., the courts are attuned to commercial morality and are motivated to achieve the desired result based on such morality. As Professor Cheffins has suggested, a full review of the morality employed by the courts in fiduciary duty cases would be desirable.²⁰ As MacIntosh, Holmes and Thompson point out, the Canadian judiciary is by training and tradition conservatively bound to statute and precedent.²¹ Their recourse to the realm of commercial morality is one way in which the Canadian judiciary may unleash these ties.

¹⁸ J. Howard, "Fiduciary Relations in Corporate Law" (1991), 19 CBLJ 1.

¹⁹ [1953]2 SCR 204, [1953]4 DLR 289 (SCC).

²⁰ B.R. Cheffins, "Law, Economics and Morality: Contracting Out of Corporate Law Fiduciary Duties" (1991), 19 CBLJ 28, p.47.

²¹ Op. cit., pp.96-100.

The enactment of the oppression remedy has significantly reduced the need for shareholders to resort to claims of fiduciary duty. MacIntosh, Holmes and Thompson observe that "the courts have in effect imposed a fiduciary code of conduct on the activities of controlling shareholders through the statutory oppression remedy."²² The statutory oppression remedy has afforded shareholders greater access to court-sanctioned remedies than claims of fiduciary duty have done and seems to have reduced the scope of claims of fiduciary duty, cases such as Vladi Private Islands notwithstanding. Future fiduciary claims against directors may best be restricted to share transactions and other situations in which a special relationship between director and shareholder is established. If claims of fiduciary duty are to survive in corporate law jurisprudence, such claims must proceed independently of claims under the statutory oppression remedy even when the facts in support of both types of claims are "intertwined" as they may have been in Brant Investments.²³

If the Canadian law of directors' and insiders' common law fiduciary duties to shareholders withstands the recent assault from the Brant Investments decision, a process of identifying and unifying the underlying principles of the law must continue. Should directors be invested with certain fiduciary duties such as the duty of disclosure in limited, objectively verifiable situations such as significant share transactions? Should fiduciary duties be predicated on less objective facts such as director-shareholder relationships of particular dependence and vulnerability? Should the courts impose a regime of full take-over bid procedures on all corporations? Certainly, the cost of full-blown fiduciary duties benefitting shareholders of all

²² Ibid, p.130.

²³ Counsel to the dissenting shareholders argued that "the issues of fiduciary duty and oppression are intertwined on the facts", footnote 4, p.298. Unfortunately the Court of Appeal also intertwined the law of fiduciary duties and the statutory oppression remedy in its decision and, effectively, jettisoned the former.

corporations would be high.²⁴ These are examples of significant issues which await further consideration.

The Canadian law of directors' and insiders' fiduciary duty to shareholders is in need of unification in principle. By way of encouragement for continuing the development of this area of the law and of continuing to explore the "considerable bevy of problems"²⁵ which such development raises, we should bear in mind the closing words of Louis Loss's speech of over twenty years ago:

The ultimate point is that the host of problems attendant upon the recognition of something like a fiduciary duty on the part of directors and other insiders when dealing with shareholders cannot be swept under the rug. One way or another they must be met and solved.²⁶

The extent to which the courts can develop this area of the law is unclear. Canadian courts appear increasingly unwilling to impose fiduciary obligations on corporate insiders. But, the courts do not want to close the curtain on the law of fiduciary relations in the corporate context. Interestingly, on the page of the Brant Investments Ltd. judgment following the lowering of the curtain on the "broadening of the categories of fiduciary relationships in the corporate context", the Ontario Court of Appeal raises the curtain to reiterate that fiduciary duties are imposed "in situations where someone stands in a particular position of trust".²⁷

²⁴ For a discussion of the costs associated with the imposition of fiduciary duties and methods and benefits of contracting out of those duties see B.R. Cheffins, op. cit.

²⁵ L. Loss, "The Fiduciary Concept as Applied to Trading by Corporate "Insiders" in the United States" (1970), 33 Mod L Rev 34, p.46.

²⁶ Ibid, pp.51-52.

²⁷ Footnote 5, pp.301-302.

Law reformers have recently considered the role and responsibilities of directors and insiders.²⁸ It is time for the courts to impose fiduciary duties on directors in favour of shareholders, not just in favour of corporations, where directors use their powers and knowledge for their personal advantage or for a shareholder's disadvantage. We have focused on the fiduciary duties of directors to shareholders, but as we have seen in our review of recent cases, it is often difficult to isolate the role played by directors. Often directors are majority shareholders or officers of the corporation. Moreover, it is not uncommon for directors to act as nominees of those major shareholders who elect them. We should not forget the lessons of the Kimber Committee in the 1960s. It would be undesirable to solve the problem of Percival v. Wright, to solve the problem of directorial abuse of shareholders, and ignore the abuse of shareholders which may be caused by other insiders. Accordingly, where by virtue of statute or number of votes, an insider has a unique power to act to his or her exclusive advantage or to the disadvantage of other shareholders and where such power is not attributable to the insider's own property or knowledge, the law should regulate the use of that power. To the extent that the oppression remedy obviates the need to impose fiduciary duties on insiders to curb the abuse of insider power, so be it. But, courts should not seek to restrict the ambit of fiduciary duties on directors and other corporate insiders. If this recent development in Brant Investments Ltd. v. KeepRite Inc. continues, a new round of corporate law reform may be required. It is unlikely that corporate law reformers would again place their faith in the courts to develop the law as they did in the 1960s and 1970s.

²⁸ See Institute of Law Research and Reform, Corporate Directors' Liability (Edmonton: Institute of Law Research and Reform, 1989) and Consumer and Corporate Affairs, *Insider Trading and the Canada Business Corporations Act* (Ottawa: Minister of Supply and Services Canada, 1991).

APPENDIX
TAKE-OVER BID CIRCULARS

The contents of a take-over bid circular outlined by the Kimber Committee in its Report were as follows:

1. The number and designation of any securities of the offeree company beneficially owned, directly or indirectly,
 - (a) by the offeror, including, where the offeror is a company, securities so owned by any subsidiary or parent (as defined in Appendix C of this Report) of such company,
 - (b) by each director and each executive officer (as defined in Paragraph 2.07 of this Report) of the offeror,
 - (c) and, where known to such directors or executive officers, by each holder of more than ten per cent of any class of equity securities (as defined in Appendix C) of the offeror company,or, if none are so owned, a statement to that effect;
2. for six months preceding the date of the offer, the number and designation of any securities of the offeree company traded, including the purchase price or sale price and the date of each transaction, by the persons designated in the preceding paragraph, where known to such directors or executive officers;
3. if the offer is conditional upon acceptance in respect of a minimum number of shares tendered under the offer, particulars of such condition;
4. particulars of the method and time of payment of the consideration (whether cash or securities) to be paid for the shares sought to be acquired;
5. if an agent is making the offer on behalf of an undisclosed principal, whether or not the agent has taken any steps to ascertain that the undisclosed principal

will be in a position to implement the offer if it is accepted by the offerees and, if so, what steps;

6. where the information is reasonably ascertainable, a summary showing, in reasonable detail, the volume of trading and price range, in the six months preceding the date of the offer, of the securities sought to be acquired;
7. particulars of any arrangement or agreement made or proposed to be made between offeror and any of the directors or executive officers of the offeree company (including particulars of any payment or other benefit proposed to be made or given) as to compensation for loss of office or as to their remaining in or retiring from office, in the event that the offer is successful; and
8. particulars of any information within the knowledge of the offeror which indicates any material change in the financial position or prospects of the offeree company since the date of the last published annual or interim financial statements of the offeree company.

(Kimber Report, pp.73-74.)

The prescribed contents of the circular to be issued by the directors of the offeree company were as follows:

1. the number and designation of any securities of the offeree company beneficially owned, directly or indirectly, by each director and each executive officer of the offeree company, and, where known to such directors or executive officers, by each beneficial owner of more than ten per cent of any class of equity securities of the offeree company or, in each case, if none are so owned, a statement to that effect;
2. whether or not each director and each executive officer of the offeree company and, where known to such directors or executive officers, each beneficial owner of more than ten per cent of any class of equity securities of the offeree company has accepted or intends to accept the offer in respect of securities to which the offer relates so owned by him;
3. where the offer is being made or has been made by a company, whether or not any securities of the offeror company are beneficially owned, directly or indirectly, by each director and each executive officer of the offeree

company, and, where known to such directors or executive officers, by each beneficial owner of more than ten per cent of any class of equity securities of the offeree company and, if so, the number and designation of such securities so owned by each such person;

4. particulars of any arrangement or agreement made or proposed to be made between the offeror and any of the directors or executive officers of the offeree company (including particulars of any payment or other benefit proposed to be made or given) as to the compensation for loss of office or as to their remaining in or retiring from office, in the event that the offer is successful;
5. whether or not any director or executive officer of the offeree company and, where known to such directors or executive officers, any beneficial owner of more than ten per cent of any class of equity securities of the offeree company has any interest in any material contract to which the offeror is a party and, if so, particulars of the nature and extent of such interest;
6. if the securities sought to be acquired are not listed on a recognized stock exchange and the information is reasonably ascertainable, a summary showing in reasonable detail the volume of trading and price range of such securities in the six months preceding the date of the offer;
7. particulars of any information within the knowledge of the directors or executive officers of the offeree company indicating any material change in the financial position or prospects of the offeree company since the date of the last published annual or interim financial statements of the offeree company; and
8. particulars of any other material facts not disclosed in the foregoing.

(Kimber Report, pp.75-76.)

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