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CHARITY AND NOT-FOR-PROFIT LAW

Dealing With Corporate Disputes – Planning To Avoid Disputes

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CHARITIES AND NOT-FOR-PROFIT LAW

DEALING WITH CORPORATE DISPUTES – PLANNING TO AVOID DISPUTES

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Introduction:

Despite the altruistic intentions of non-profit and public benefit organizations, many of them are hotbeds of internal disputes. Power disputes are common. Energies which should be directed towards the objectives of the organization are instead directed at in-fighting.

Prudent officers, directors and their counsel need to understand the rights, procedures and remedies available. Many organizations lack proper mechanisms to resolve potentially litigious matters involving problem directors, dissident members, contested elections or conflicts of interest. Directors and members are often unaware of their legal rights at an organizational and individual level. While these issues are most common in volunteer-based organizations, professionally managed ones are not immune to them.

Three Scenarios:

We have chosen three fact situations, to illustrate some of these issues. First we will examine how the chair of the organization can deal with problems as they arise, and then we will review some of the drafting and planning techniques that can be used to reduce the possibility of these problems arising, or at least give the chair the ability to handle them more effectively at a meeting of members when they do arise. We will approach these issues from both ends, since there are obviously times when a dissenting director or member will need to know how to overcome the resistance of a chair who may not be playing the game by the rules.

Scenario 1. The Problem Director

Baskerville-Undershaw Ratepayers Group (“Baskerville”) is a non-profit corporation formed under the *Ontario Corporations Act* (the “OCA”) to promote the interests of a local community group.

Moriarty Building Corporation (“Moriarty”) has proposed a major development project for the Baskerville-Undershaw area and the board of Baskerville, after a long and contentious meeting, has voted to publicly oppose the project.

Moran is a director and the President of Baskerville. She voted against the motion to oppose and has appeared at several public meetings to speak in favour of the project. When asked, she always says that she is appearing in her personal capacity. However, she is a popular person, well-known in the community and is easily identified as the President of Baskerville. There is no

specific provision in Baskerville's by-law preventing Moran from communicating her views on a personal level.

Watson, the Vice-President of Baskerville suspects that, in addition to taking a position contradictory to the one approved the by board, Moran may have an undisclosed financial connection to Moriarty, or stands to benefit financially if the project proceeds, and wants to "fire", remove, or suspend Moran as director and president as quickly as possible.

Watson consults Cliff for legal advice.

Moran consults Gavin for legal advice.

Issues:

1. What duty (if any) does Moran owe to Baskerville as president and director?
2. Is there a conflict of interest, and can Moran be prevented from speaking in favour of the project?
3. Could Moran be "fired" as president or have her membership in Baskerville revoked or suspended?
4. If Moran has failed to disclose a conflict of interest, what actions can be taken against her?
5. Could a court award damages against Moran and if so on what basis?
6. Could the board exclude Moran from a meeting held to discuss and take action against her?

Commentary

Advice to Watson:

Duty of Moran

Moran, as President and Director of Baskerville, has a fiduciary duty to the non-profit. This is usually called the "duty of loyalty". The scope of that duty may be summarized as:

- To act in the best interests of Baskerville at all times
- Not to favour the interests of another party, if that party's interests differ from the interests of Baskerville
- Not to disclose Baskerville's confidential information to any non-member of the board
- To disclose to Baskerville information coming from another party which relates to a planned transaction or operation likely to have a negative impact on Baskerville.

Once a board decision is made, what is the scope of Moran's fiduciary duty of loyalty? Moran now has a new duty, the "duty of neutrality" between the corporation and any other party she

may have a connection to. The scope of this duty is not necessarily clear, since nothing prevents Moran from continuing to advocate a position at the board of either entity. But Moran's duty of loyalty requires her to accept final decisions validly made by the board. All directors must accept the decision of the majority of the directors once the vote has been taken, regardless of whether the result does or does not support the stance taken by the dissenting director. Although Moran is free to indicate, even publicly, what views she holds on the project, she should not actively promote a viewpoint that is contrary to the decision made by the board, while at the same time representing herself as a director or spokesperson of the board. She should make very clear that her views are strictly personal and not the position of the board. A director who publicly opposes or covertly works against the decision is doing so at her peril. See Clifford S. Goldfarb, "Dual Loyalties On Non-Profit Boards: Serving Two Masters"[1].

Conflict & Speaking about the Project

A Code of Conduct, which covers the "duty of loyalty", could deal with this situation. Unfortunately, many board members of non-profit organizations represent the interests of a specific group of stakeholders within the organization. When the board makes a decision that goes against the position of a specific group of stakeholders, the director who represents their interests has a "dual loyalty" problem, in that he/she is bound by the duty of loyalty to support the board decision in public, while at the same time he/she may have a duty to represent the interests of the stakeholder group. A properly crafted Code of Conduct may permit the director to speak in favour of the stakeholders' position.

While Moran has every right to support any cause in her personal capacity, by virtue of the fact that she is the President and a Director of Baskerville, she owes this fiduciary duty and duty of care to Baskerville The fact she spoke in favour of the project at public meetings in opposition to the position taken by the Board can be seen as a breach of Moran's duties to Baskerville. In short, using her position with Baskerville to attempt to influence the members of Baskerville and of the community in a manner contrary to the interests of the corporation as duly determined by the Board is in and of itself is a contravention of the objects of Baskerville.

Can Moran be "fired" or removed from the board?

In Canada, when a director is considered to be a problem because of misbehavior the available remedies are limited.

A special meeting of members could be convened to remove the "dissident" directors by an ordinary resolution and to replace them with more compatible ones. The OCA requires that the right to remove directors, must be set out for in the Letters Patent or by-laws and requires a 2/3 majority (s.67). Baskerville's by-law states:

[1] http://www.grllp.com/profile.aspx?ID=20

Vacating of Office. The office of director shall be automatically vacated:

(a) if he or she should be disqualified pursuant to Section 5.8;

(b) if a director shall resign his or her office by delivering a written resignation to the secretary of the Corporation;

(c) if at a special or general meeting of members a resolution is passed by 2/3 of the members present at the meeting that he or she be removed from office.

All other corporate statutes provide that the removal is by a simple majority vote. The percentage of votes required for this purpose cannot be increased in the articles or by-laws: *Canada Not-for-Profit Corporations Act* ("CNCA"), s.7(5) and 130; *Ontario Not-for-Profit Corporations Act, 2010* ("ONCA"), ss.8(6) and 26).

Where appropriate, proceedings might be brought by the Corporation, claiming damages occasioned by the director's absence and any resultant breach of fiduciary duty. [*Gearing v. Kelly* (1962), 182 N.E. 2d 391 (N.Y. Ct. App.) and see Comment on *Bearing v. Kelly* in (1962) 62 Col. L. Rev. 1518)].

However, the articles or bylaws may impose a quorum higher than the general one prescribed for most matters in respect of certain matters that are considered to be of special importance. In the Ontario decision, Ebrahim v. Continental Precious Minerals Inc.[2012 ONSC 2918, 111 O.R. (3d) 110)], the bylaws established a special quorum requirement of not less than 50 per cent of the shareholders at any meeting considering resolutions to remove, replace or appoint directors. Failure to achieve that quorum had kept the incumbent directors in place for 15 years. This requirement was upheld by the Court against a challenge by a faction of the shareholders.

Duty of Moran & Conflict of Interest

One of the main issues, is identifying the standard of care with precision in not-for-profit organizations. Maurice C. Cullity suggests that identifying the appropriate standard can be difficult in some instances, due to the fact that the "sources of law governing charities and NPO's are at best a mix of the law of trusts, law of corporations and jurisdiction over charitable property by the Courts of equity."[2] As in for-profit organizations, it is equally important for directors of not-for-profit organizations to be aware of any duty they may have, and how this duty might conflict with any outside personal interests.

Moran has a duty to disclose any benefit she might derive from the project, even if it is only the fact that her home might increase in value because of its proximity to the project. The existence and basic nature of this duty was affirmed in *London Humane Society (Re),* 2010 ONSC 5775, [2010] OJ No 4827 (Ont SCJ) where the Court stated that a director has a fiduciary duty to a not-for-profit organization, and as such, must disclose to the corporation the "whole truth" in his or

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[2] Maurice C. Cullity, "The Charitable Corporation: A "Bastard" Legal Form Revisited", online: (2002) 17:1 The Philanthropist 2 at 17 <http://www.thephilanthropist.ca/index.php/phil/article/view/88/88>.

her dealings as a director, and further that the director's interests must not be placed in conflict with those of the corporation.

However, this does not automatically preclude Moran from making any statements in her personal capacity. Moran needs to be mindful that she is required to place the interest of Baskerville first and needs to disclose any potential conflict of interest with Moriarty. Moran, as president and director is required to act in the best interests of the corporation (not for personal interest), and must avoid the *appearance* of a conflict of interest.[3] It would be prudent that Moran make clear, precise and fulsome statements disclosing any potential conflict of interest she might have in respect to the Moriarty development to Baskerville. This was affirmed in *Public Trustee and Toronto Humane Society et al*. 60 O.R. (2d) 236, where it was noted that a director is a fiduciary, and is not entitled to make a profit from his or her office or allow himself or herself to be placed in a position where his or her interests and duties conflict.

s.71 of the OCA currently applies to conflicts of interest with respect to proposed contracts. However, s.141 of the CNCA and s.41 of the ONCA expand the provisions with respect to conflicts of interest to apply to any material contract or transaction or proposed material contract or transaction.

Moran does owe a duty to Baskerville, but is also entitled to provide a *personal* viewpoint to the public (outside her role as a director). These personal viewpoints need to be conveyed in a very neutral manner, in order to ensure her fiduciary duty is not breached. In speaking publicly about the Moriarty building, it must be made clear that this is only Moran's personal viewpoint, and does not in any way represent the position of the Baskerville organization. Further, it needs to be abundantly clear that Moran's personal viewpoint is not being put forward in an attempt to persuade the community against the position of Baskerville.

Can Moran be excluded from a board meeting held to discuss and take action against her?

It appears that the answer is that Moran cannot be excluded from any board meetings.

> *Nathan's Company Meetings for Share Capital and Non-Share Capital Corporations* (10th edition)
>
> **25. Right to attend, and participate by directors**
>
> Every director has the right to attend and participate in all meetings of the board of directors.[4] A director cannot be excluded from meetings of the board.[5]
>
> *Comment:* A director can enforce his or her rights to be present and vote at meetings of the board.[6] Shareholders and members are entitled to have the directors engage in a meaningful interchange

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[3] Ontario Public Guardian and Trustee, "Duties, Responsibilities and Powers of Directors and Trustees of Charities", (9 December 2010) online: Ministry of the Attorney General. <http://www.attorneygeneral.jus.gov.on.ca/english/family/pgt/charbullet/bullet3.asp> [OPGT].

[4] *Boak v. Woods* (1926), 36 B.C.R. 456, [1926] 1 D.L.R. 1186 (C.A.).

[5] *Hayes v. Bristol Plant Hire Ltd.,* [1957] 1 All E.R. 685; *Howard v. Dench*, [1942].
2 D.L.R. 177 (B.C.C.A.); *Trounce v. NCF Kaiapoi Ltd.* (1985), 2 N.Z.C.L.C. 99,422 (H.C.). See also *Kalisman et al. v. Friedman et al.,* 2013 C.A. No.8447-VCL (Del. Ch.).

> of ideas and views before a board decision is made. All directors should be given an opportunity to engage in meaningful discussion at a meeting. Directors should be proactive and are expected to contribute, but within limits. This means that they should not raise more than their fair and reasonable quota of questions, which in reality will be limited, considering the short period of time usually set aside for discretionary issues at board meetings. Even though the majority directors can normally bind the minority directors on any vote, the minority have a right to be heard at any meeting of directors. See *Great Western Railway Co. v. Rushout*.[7] See also *Cameron v. Campney and Murphy*.[8]

As a practical matter, the board could form a committee and delegate the matter to it. Whether Moran, as a director, has the right to attend meetings of committees is beyond the scope of this comment.

Can Moran be "fired" or suspended from the board?

Arguably the draconian step of removing or "firing" Moran from her position as director requires quite a high threshold of bad conduct on Moran's part. It was affirmed in *Chu v. Scarborough Hospital Corporation*, 2006 CanLII 42784 (ON SC) that a board of directors cannot change the definition of membership in the corporation, except as permitted by its letters patent and by-laws. Thus, Watson could not "move quickly" to eliminate Moran's board position or membership without following proper by-law procedures and complying with the *OCA*.

Kimberley Cunnington-Taylor has argued that the removal by the members of a validly elected director is a 'serious matter' which is often overturned by the courts when the board attempts to usurp authority[9] which properly lies only with the members. It is true that in certain instances the Courts have been somewhat less strict about compliance with charter and by-law provisions; however, in *Lee* v. *Lee's Benevolent Association of Ontario*, 2005, it was made clear that corporate law must be strictly adhered to when dealing with the removal and election of directors.[10]

However, if the CNCA applies, an application could be made to the court under ss.241 and 253(3) for an oppression remedy. These sections give the court authority to make interim or final orders relating to any act or omission of a corporation that is oppressive or unfairly prejudicial to the interest of any director or officer. While there is no specific oppression remedy in the OCA or ONCA, an application can be made under ONCA s.136(b)(3) for the "just and equitable" winding up a corporation on application of the corporation or a member. On such an application the court has power under s.138 to "make the order applied for ,,, or may make *any interim or other order as is considered just*…". [italics added]. These provisions are carried forward into the ONCA from OCA ss.243(d) and 245.

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[6] *Harben v. Phillips* (1882), 23 Ch.D. 14 (C.A.), unless disqualified from voting or being present because of an interest in the contract. See Rule 32 and commentary.
[7] (1852), 5 De G. & Sm. 290, 64 E.R. 11221 (Ch.D.).
[8] (1993), 85 B.C.L.R. (2d) 93 (B.C.S.C.).
[9] Kimberley A. Cunnington-Taylor, *The More Things Change, the More they Stay the Same*, (May 2012) at pg 3, 6.
[10] CarswellOnt 180, 136 A.C.W.S. (3d) 465, [2005] O.J. No. 194 (Ont. Div. Ct. Jan 10, 2005) affm'g [2004] O.J. No. 6232.

The benefit of the oppression remedy under the CNCA, OCA and ONCA, is that it is an equitable remedy, which gives broad jurisdiction to the Court to fashion a fair result.

Thus, depending on the manner in which Moran was removed or suspended, if it was not made in compliance with any by-laws or in contravention of the applicable Acts, a court can fashion declaratory remedies or compliance orders, along with potential cost awards.

Although this is not an option for an organization like Baskerville, it is not uncommon to request that a director sign a resignation on being appointed, which may be accepted at any time. We have seen these where an international organization sets up a Canadian representative body, or where a stakeholder has the right to appoint a director to a board. It remains to be seen whether there remains a duty to act fairly in accepting a pre-signed letter of resignation and whether such a decision could also be open to challenge.

Can Moran be disciplined or her membership terminated?

A provision may be made in a CNCA or ONCA corporation's articles or by-laws to discipline or terminate a member's membership. Section 158 of the CNCA provides that "The articles or by-laws may provide that the directors, the members of any committee of directors or members of a corporation have power to discipline a member or to terminate their membership. If the articles or by-laws provide for such a power, *they shall set out the circumstances and the manner in which that power may be exercised* [emphasis added]. Section 51 of the ONCA requires that procedure to be done in good faith and a reasonable manner, and sets out the requirements for such procedure. To be effective, the procedure must be set out in the articles or by-laws of a non-share corporation. Membership can carry with it significant benefits, such as equity ownership, medical or pension plans, free golf games etc. and depriving the member of such benefits cannot be undertaken capriciously or without appropriate process.

There are several interesting cases dealing with removal of members:

In *Sol Sante Club v. Grenier* [[2006] B.C.S.C. 1804], the plaintiff's probationary membership was terminated by the Board. There were no specific provisions in the by-laws or articles with a separate process to be followed when expelling a probationary member as opposed to a regular member. According to the By-law, the process to be followed was that there had to be a special resolution of the members. Mr. Grenier was denied the right to a hearing before the Board and the Board simply terminated his membership. The judge reviewed the law and concluded that while directors could exercise all the powers that the society could exercise, there had to be strict compliance with a provision in the By-law relating to expelling a member. The Court pointed out that there had to be a substantial degree of procedural fairness in the exercise of such a harsh remedy, which had been denied Mr. Grenier. Accordingly, the termination of his probationary membership was exercised in a manner contrary to the provisions of the by-law and the expulsion was set aside.

In the case of *Schaer v. Barrie Yacht Club* [(2006), 34 B.L.R. (4th) 36 (Ont. S.C.J.)], the Court considered whether to issue an injunction prohibiting Mr. Schaer from being on or near the Club premises and for a declaration that he had been properly expelled from the Club and no longer a

member. The central issue was whether the termination of Schaer's membership was valid. The Court held that it was not appropriate for it to review the decision made by the executive committee of the Club, but it was appropriate to examine the circumstances in which it was made, and whether those circumstances revealed a failure to deal with the issue in accordance with principles of natural justice. It is only in the instance of such a failure that the Court should interfere with the decision made. The Court in this case declined to interfere and granted a permanent injunction against Mr. Schaer.

There have been other cases that have upheld these principles. A decision of the British Columbia Supreme Court in *Struchen v. Burrard Yacht Club* [(2008) 46 B.L.R. (4th) 228 (B.C.C.A.)] provides a further example. Here, three members of a yacht club challenged their suspension or expulsion from the club. One of them lost his membership, which meant he lost the right to moor his boat at the marina, which was an important element of his social and family life. The Court held these members were improperly disciplined. There was a failure to comply with the basic requirements for a fair process, including a finding that the club's board had already decided that Struchen should be disciplined before the meeting took place. This violated the general principle that a body should not proceed where there is a reasonable apprehension of bias. A new hearing was ordered. The Court stated (p.241):

> The rationale for affording a person an opportunity to be heard is the idea that people will listen with an open mind to that which is said and reach a considered decision. It cannot be presumed that at a future time a member will be deprived of membership where, as here, it is established that not all the allegations were soundly made.

What is clear from these cases is the importance of "getting it right" in regard to process and compliance. The procedure set out in the articles or by-laws must be followed to the letter and every step must show compliance and fairness.

This was affirmed in *Rexdale Singh Sabha Religious Centre v. Chattha*, 2006 CanLII 39456 (ON CA), in which the Court made it abundantly clear that where proper procedure was not followed to change the members of an organization in compliance with the OCA, and where there has been a failure to comply with this Act, membership cannot be created, removed, and approved by directors.

In *Pearson (Applicant) v. Eganville and District Senior Citizens' Needs Association* (Respondent) (25 November 2010), Ottawa, Court File No. 10-49107 (Ont. Sup. Ct.)(unreported) Justice H. McLean ordered that the resolution of the Board of Directors (of the Respondent) to permanently suspend the Applicant was *ultra vires* the authority of the Board of Directors, and awarded costs in the sum of $6,500 to the Applicant.

Under s.51(5) of the ONCA a member who claims to be aggrieved because he or she was disciplined or terminated may apply to the court under s.191, which gives the court the authority to make any order that it thinks fit. Further, ss.174 (1) and 174 (2) provide that an application for an investigation can be made to the Court where the powers of directors have been exercised in a manner that is oppressive or unfairly prejudicial, and allows the Court with jurisdiction to make any order that it thinks fit.

<u>Scenario 2.   Contested Elections</u>

In contemplation of the AGM of Baskerville, a slate of seven directors is put forward in the notice of meeting by the existing board, now chaired by Watson. Moran, who is no longer a director, rises at the meeting to move that her own slate of seven directors be elected instead. There are therefore 14 candidates nominated for seven positions.

In addition, Moran deposits a substantial number of proxies with the secretary of the meeting. Alerted the day before the meeting to the possibility that this nomination and proxy fight might happen, Watson and other board members have been scrambling to collect proxies supporting their slate, but are not sure that they have enough votes to have a majority of their candidates win the election.

The chaos inside the organization has caused unwarranted disputes between members, with the potential for complete disruption within the organization.

Watson consults Cliff for legal advice.

Moran consults Gavin for legal advice.

Issues:

1. Can Watson rule the nomination from the floor of Moran's slate to be out of order?

2. Can Watson adjourn the meeting for a few days to gather more proxies?

3. Would any of this be different if Baskerville was continued under the CNCA or the ONCA?

4. Can Watson defer voting on the election, change the order of the agenda, call for a long lunch break, or otherwise delay the vote, for the purpose of soliciting more proxies in support of his slate?

<u>Commentary:</u>

The fact situation is modelled loosely on the Delaware case of *Portnoy v. Cryo-Cell International, Inc.* See the Appendix for the summary of the facts and decision.

Advice to Moran:

Inherent jurisdiction

It would be essential to advise Moran that if the organization was becoming overly reckless with disputes, newly elected members, and contested elections, the Courts do have inherent

jurisdiction in not-for-profit matters. While the Courts are generally reluctant to intervene, based on the case law, they would likely intervene in this matter.

In *Pathak v. Hindu Sabha*, 2004 CarswellOnt 3284 (ON SC) the Court cited *Ontario (Public Guardian and Trustee) v. Aids Society for Children (Ontario)*, [2001] O.J. No. 2170 and affirmed its inherent jurisdiction to intervene and make specific orders and remedies when appropriate and necessary in charitable and not-for-profit matters.

This was also affirmed in *Public Trustee and Toronto Humane Society et al*. 60 O.R. (2d) 236 (1987), where it was stated that the Court's powers are broad, and in Ontario the Courts do have inherent jurisdiction to intervene in not-for-profit organizations.

In *Pathak v. Hindu Sabha*, the Court intervened in order to help a religious organization. While distinguishable on certain facts, the principles remain valid. The Court analyzed a variety of factors including whether the Board of Directors administered the by-laws accurately, whether the members wanted to proceed with a ss.295 and 296 meeting to have the existing Board of Directors removed. The Court also looked at the best interests of the organization, the history of litigation within this group and decided not to provide relief for the applicants because to do so "would further destabilize the charity and distract it from the charitable work and the purposes for which it was created." Further, in this case the Court also made determinations on whether individuals would be considered members of the organization.

In *Doder v. Radojkovic*, 1987 CarswellOnt 189, [1987] O.J. (Ont H.C.) the Court exercised its power by directing that a meeting of the members be called in the organization, held, and conducted in a specific manner outlined by the Court. Moran could also ask for the Court to intervene and provide guidance on how voting and contested elections should proceed. In *Doder v. Radojkovic*, the Court took steps to prevent any unseemly membership drives, as might have happened in the Baskerville meeting.

It is also crucial to properly and fairly interpret and apply the governing by-laws and the requirements pertaining to voting in directors, and membership approval. In *Deol v. Grewal*, 2008 CarswellOnt 5060 (ON SCJ) Justice Patillo found that there was a complete absence of prior notice of the proposed resolutions to appoint a new president, and newly elected members into the organization. As a result, the meeting was found invalid, and the Court ordered that the election of a new president and directors be set aside, and the election of forty-three new members also be set aside.

The Court has the inherent jurisdiction to make injunctive and declaratory relief, including but not limited to: the determination of who would be considered a member for voting, an order setting out how the new general meeting should be convened, and held, set out the contents of the notice for meeting and proxy forms, who is entitled to vote, and appoint individuals who can count the votes.

Advice to Watson:

Nomination out of order

It would be prudent to advise Watson that the articles or bylaws of some corporations restrict nominations of directors to those nominated within a specified time in advance of the meeting on the grounds that it is important that the shareholders or members, many of whom may grant proxies or otherwise not attend the meeting, have full information as to the issues before the meeting.

This appears to be a growing trend. Even Institutional Shareholder Services Inc. favours advance notice of nominations. The B.C. judgment in *Northern Minerals Investment Corp. v. Mundoro Capital Inc*. [2012 B.C.S.C. 1090] upheld the validity of an Advance Notice Policy adopted by the board of directors by resolution, rather than one contained in the incorporating documents or bylaws. A typical advance notice by-law might provide:

> Advance Notice By-law – Directors
>
> 1. Prior to the Annual Election Meeting of the Corporation, the Board shall appoint a Nominations Committee which shall solicit nominations for the directors to be elected at such meeting, and for the President and Vice-President, if applicable. Any Voting member may nominate persons to stand for election under this Section. All nominees must be Voting members and otherwise qualified to be directors of the Corporation and must consent in writing to stand for election.
>
> 2. A list of nominees may be circulated with the notice calling the meeting and, in such case, additional nominees may be nominated in writing to the Secretary not less than 10 days prior to the meeting. The Secretary shall circulate a complete list of those nominated not less than seven days prior to the meeting. If there are insufficient persons nominated via the foregoing process to fill all positions to be elected at the meeting, nominations will be accepted from the floor at the meeting.

As Kimberley Cunnington-Taylor notes, there are quite a few for-profit cases that provide insight into the courts' determination of contested elections which not-for-profit practitioners should be aware of. For example, in *Ewart v. Higson-Smith*, 2009 CarswellOnt 4376, 61 B.L.R. (4th) 228 (OntSC), a board adjourned the annual meeting of shareholders for 24 days the day before the meeting was scheduled, as a "dissident group" was planning to propose an entirely different slate of directors, essentially blindsiding the meeting. The Court here wanted to ensure that proper information was given to all shareholders before the meeting, and as a consequence approved the boards' action in adjourning the meeting[11].

Watson could cite this case law to support asking for an adjournment, as full information is required before this type of meeting of Baskerville. Ultimately, the members are entitled to exercise their franchise fairly and with reasonable notice and information. The Court will often

[11] Kimberley A. Cunnington-Taylor, *Charity and Not-for-profit Law- The Nuts and Bolts of Non-Share Capital Corporate Law*, OBA (2013) at pg 26.

view its role as protective of member's rights rather than in supporting one executive group over another.

Supplementary concerns:

1. Would any of this be different if Baskerville was continued under the CNCA or the ONCA?

Advance deposit of proxies:

All three statutes provide that the proxy need not be a member – CNCA s.171 and Regulation ss.74(2), ONCA ss.64(1), OCA s.84(1). But OCA ss.84(5) and ONCA s.64(4) permit the board to require 48 hours advance deposit of proxies. The CNCA doesn't: Reg. ss.74(2)(b) permits it to be deposited at the place of the corporation not later than the last business day before the meeting or given to the chair at the meeting.

Scenario 3. Member Disputes – The "Surprise" Motion

When the meeting proceeds to "other business" Moran moves a resolution that Baskerville support the project and that the board be instructed to act accordingly. No previous notice of this motion was provided to the board and it is not on the agenda for the meeting. Baskerville's by-laws do not provide for the giving of advance notice of resolutions. Watson rules the motion out of order, without giving reasons, and calls for a motion to adjourn, which passes. Moran, insists on speaking and challenges the ruling of the chair. Watson simply declares the meeting closed and leaves, as do many other members.

At this point there are still enough members present to constitute a quorum, a majority of whom support Moran. So Moran asks for a motion declaring the meeting has not been properly adjourned. She then asks for a motion appointing herself as chair. Finally she asks for a motion in support of the project, all of which pass.

Questions:

- If the notice of meeting provides, as the final agenda item, "To transact such further or other business as may properly come before the meeting or any adjournment or adjournments thereof", does that permit Moran to raise her motion?
- When Watson finds out what has happened, what action can she or the board take to invalidate the decisions made after her closing of the meeting and preventing Moran from speaking or publishing anything stating that Baskerville supports the project.
- how would the member litigate it and how would the corporation or the board defend?

Commentary:

Generally, matters brought up under "Other Business" and which have not been disclosed in the notice of the meeting should not be of a substantive nature.

> *Nathan's Company Meetings for Share Capital and Non-Share Capital Corporations* (10th edition)
>
> Chairman's discretion to rule motions out of order
>
> **72. Business not mentioned**
>
> 1. Important business not mentioned in the notice convening a meeting of shareholders or members cannot be transacted.[12] If such business is conducted at a meeting, it may be declared null, but this will not render the whole meeting irregular.[13]
>
> *Comment:* When special business is intended to be transacted at an annual meeting, special notice must be given. Within limits, the business of which notice was given may be varied,[14] but the meeting cannot go beyond the purposes for which it was called. [p.78]

Another way of minimizing this type of incident is to require advance notice of any resolutions a member wishes to place on the agenda. A typical advance notice by-law provides:

> Advance Notice By-law – Resolutions
>
> Resolutions to be put before any meeting of members can be made only by a Voting member. Any resolution to be tabled at a meeting must be filed with the Secretary at least 14 days prior to the date fixed for the meeting. The Secretary shall provide a copy of the agenda for the meeting to the members not less than seven days prior to the date fixed for the meeting. No other resolution shall be permitted to be proposed at the meeting without the consent of a two-thirds vote of members present at the meeting. If notice of a special meeting is given sufficiently in advance of the date of such meeting to allow for the solicitation of resolutions to be put before such meeting, the Board may apply the requirement for prior notice to resolutions to be submitted to such special meeting.

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[12] See Rule 50. *Irvin v. Irvin Porcupine Gold Mines Ltd. and Mulliette*, [1940] O.W.N. 315, [1940] 3 D.L.R. 785 *n*, leave to appeal refused (H.C.J.); *McDougall v. Black Lake Asbestos & Chrome Co. Ltd.* (1920), 47 O.L.R. 328 (S.C.H.Ct.D.); *Longfield Parish Council. v. Wright* (1918), 88 L.J. Ch. 119. Failure to mention ratification of by-law increasing number of directors as a purpose of the meeting renders the notice defective (*Gray v. Yellowknife Gold Mines Ltd.*, [1945] O.R. 688 (H.C.J.)).

[13] *Re Second Standard Royalties Ltd.* (1930), 66 O.L.R. 288, [1930] O.J. No. 45 (H.C.J.) (Q.L.); *Re British Sugar Refining Co.* (1857), 3 K. & J. 408, 69 E.R. 1168.

[14] A notice of meeting for the voluntary winding up of a company and the appointment of Was liquidator is proper where the meeting approved the winding up but appointed M as liquidator (*Bethell v. Trench Tubeless Tyre Co.*, [1900] 1 Ch. 408). Where the notice stated that three named persons would be appointed directors, and, instead, five were appointed, the notice was upheld (*Betts & Co., Ltd. v. McNaghten*, [1910] 1 Ch. 430). Where a notice states that it is proposed to remove any of the directors all may be removed (*Isle of Wight Ry. Co. v. Tahourdin* (1883), 25 Ch.D. 320).

Proposals

A member who wants to ensure that a matter is put on the agenda could also take advantage of the "proposal" provisions of s.163 of the CNCA (virtually identical to s.56 of the ONCA), or the similar provisions of OCA s.296. Once the member puts the request forward, unless the directors are entitled under the applicable statute to refuse to put it to the meeting, it must be dealt with at the meeting, at least to the point of discussion and a vote. It would seem that a proposal to have Baskerville change its position to support the project would not fall within any of the grounds that permit the board to refuse to put the proposal on the notice of meeting. The request for the proposal under the CNCA must be given to the board at within 90-150 days prior to the anniversary of the prior annual meeting (Reg.67). Under the OCA, it must be received by the board 10 days before the meeting. The member can also require the board to circulate a 500 word statement under the CNCA, or 1,000 words under the OCA.

4. Practice Note on Unanimous Member Agreements

Section 170 of the CNCA provides that a non-soliciting corporation can have a unanimous members agreement, or UMA, which restricts in whole or in part the powers of the directors to manage the corporation. The agreement may be among all the members of a corporation that is not a soliciting corporation, or among all the members and one or more persons who are not members. The non-members could therefore be directors or total outsiders. A one-member corporation could by a written declaration create such an agreement, which effectively binds the directors.

In effect this shifts the duties, powers and liabilities of the board to the members, but only to the extent of the restriction in the exercise of the powers of the directors. The members, however, are not bound by the legal principle that a director's discretion, absent such an agreement, may not be fettered. This is an interesting and potentially useful mechanism which would allow a parent national or governing organization to control the actions of a local or affiliated body. It may also permit a director to have a "dual loyalty". It is very new in Canada, and, to my knowledge, there has as yet been no litigation which may help to delineate its scope and limitations. Because it is analogous to the concept of a "unanimous shareholders agreement", found in most business corporations acts, it is likely to be interpreted in the same manner by the courts.

APPENDIX

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David PORTNOY, Plaintiff,
v.
CRYO-CELL INTERNATIONAL, INC., A Delaware corporation, Mercedes Walton, Gaby W. Goubran, Jagdish Sheth, Ph.D., Anthony P. Finch and Scott Christian, Defendants.

C.A. No. 3142-VCS.

Court of Chancery of Delaware.

Submitted: November 30, 2007.
Decided: January 15, 2008.

OPINION

STRINE, Vice Chancellor.

This case involves a challenge to the results of a contested corporate election. Cryo-Cell International, Inc. ("Cryo-Cell" or the "Company") is a small public company that has struggled to succeed. By early 2007, several of its large stockholders were considering mounting a proxy contest to replace the board.

One of those stockholders, Andrew Filipowski, used management's fear of replacement to strike a deal for himself to be included in the management slate for the 2007 annual meeting. Another stockholder, plaintiff David Portnoy, filed a dissident slate (the "Portnoy Slate").

Going into the week of the annual meeting, Cryo-Cell's chief executive officer, defendant Mercedes Walton, was desperate because, in her words, "the current board and management [were] losing by huge margins." Aside from actually asking the FBI to intervene in the proxy contest on the side of management, Walton ginned up a plan with Filipowski to win the proxy contest. That plan involved Walton acting as a "matchmaker" by finding stockholders willing to sell their shares to Filipowski. In exchange for this alliance, Walton promised Filipowski that if their "Management Slate" prevailed, Cryo-Cell's board would, using their power as corporate directors, expand the board to add another seat that Filipowski's designee would fill. That designee was a subordinate who had within the recent past resolved an SEC insider trading investigation by agreeing to disgorge trading profits and to be jointly liable for trading profits made by his tippees. This plan was not disclosed to the Cryo-Cell stockholders, who did not realize that if they voted for management, they would in fact be electing a seven, not six member board, with two, not one, Filipowski representatives.

In an effort to secure another key bloc of votes, Walton used a combination of threats (the ending of cooperation on key projects) and inducements (the long-sought but never before granted removal of a restrictive legend) to secure the vote of Saneron CCEL Therapeutics Inc. That leverage was enhanced by the fact that Cryo-Cell owned 38% of Saneron's shares and that Saneron depended on Cryo-Cell's laboratory space to conduct many of its own operations. Notwithstanding that, Saneron had gone into the week before the meeting undecided about how to vote. Walton "locked up" Saneron only after employing these persuasive strategies involving the threatened withholding and actual granting of concessions on the part of Cryo-Cell as a corporation.

Even after employing these methods, Walton and her board went into the day of the annual meeting fearing defeat. They had rented the meeting room from the 11 a.m. start time only until 1 p.m. But Walton did not want to close the polls and count the vote when the scheduled presentations at the meeting were over. So She had members of her management team make long, unscheduled presentations to give her side more time to gather votes and ensure that they had locked in two key blocs. She overruled motions to close the polls.

Even after the filibusters, Walton still harbored doubt that the Management Slate would prevail if the vote was counted and the meeting was concluded. So, at around 2 p.m., Walton declared a very late lunch break, supposedly in response to a request made much earlier.

In fact, Walton desired the break so that she would have more time to seek votes and so that she could confirm that the major blockholders had switched their votes to favor the Management Slate. Only after confirming the switches did Walton resume the meeting at approximately 4:45 p.m., declare the polls closed, and have the vote counted.

The post-meeting vote count resulted in the Management Slate squeaking out a victory by an extremely small margin. Immediately after that, Walton began preparing to add Filipowski's designee to the Cryo-Cell board. Only after this challenge was brought to the election by Portnoy did that process slow down, and only for the obvious reason that the litigation was brought.

In this opinion, I decline Portnoy's request to declare his side the victor in the election process. But I do agree with him that the election results were tainted by inequitable behavior by Walton and her allies and must be set aside. In particular, I conclude that the Cryo-Cell stockholders cast their votes in ignorance of material facts regarding the promise made to Filipowski regarding a second board seat and the pressure that Walton was exerting on Saneron—both of which involved the use by Walton of corporate resources and fiduciary authority motivated by the desire to protect herself from the risk of losing her corporate offices.

Rather than seating a board for the Cryo-Cell stockholders, I believe the more appropriate remedy to be a requirement that Cryo-Cell have another election at a special meeting to be held promptly. Because the stockholders should not be required to bear extra expense because of management's misconduct, the Management. Slate will be required to fund their own reelection campaign and to pay any costs incurred by the Company to hold the special meeting, including the cost of a special master to preside over the meeting.