

Business founder obtains oppression remedy against investors

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The [oppression remedy](#) in Canadian corporate law protects the reasonable expectations of stakeholders in a corporation. Shareholders, directors, and other stakeholders enter into relationships with and within corporations based on certain expectations upon which they are entitled to rely, provided such expectations are determined to be reasonable. Disputes arise when expectations clash. The expectations of the founder of a business, who has seen their original business plan take shape from an idea, may conflict with the investors who fund their dreams. The case of *Phillips-Lubimiv et al. v. Creekside Investments Incorporated et al.*, 2021 ONSC 410 (CanLII), shows how a court balances such conflicting expectations.

The case involved a corporation known as AP1, founded by Aaron Lyon Phillips-Lubimiv ("Phillips") in 2014. Phillips claimed that he and his family invested \$250,000 in API and thousands of sweat equity hours into developing a technology for beacons to be used at airports. AP1 was Phillips's "baby." As commonly occurs, however, the business needed funding from other parties to bring the beacon technology to the market.

In 2015, Phillips met the principals of Creekside Investments Incorporated ("Creekside"), Carl Galli ("Galli") and Peter Cicchi. Creekside was an investment and lending corporation but was not in the business of operating companies. Creekside offered to loan money to AP1 in exchange for 50% of the equity. Phillips agreed and entered into two agreements: (i) an Employment agreement pursuant to which he would remain President and CEO of AP1 for an indefinite time at a gross salary of \$90,000 plus discretionary incentives; and (ii) a Unanimous Shareholders Agreement ("USA"), which required that the only two directors of AP1 would be Phillips and Galli.

Over the next few years, Creekside advanced more than \$4.7 million in largely undocumented loans to AP1. Creekside's shareholdings in AP1 increased to 60% as a result. API hired a Vice-President of Sales, Ziad Feghali, and by early 2019, the company appeared to be on the verge of breaking out. Projects with major U.S. airports were expected to generate revenue of up to \$12 million.

Relationships strained between Phillips and Galli, however, and Phillips was accused of improper withdrawals from AP1's accounts. Mr. Feghali began referring to himself as the President and CEO of API, ostensibly because Phillips was never in the office. In August 2019, after he returned from a business trip, Phillips was presented with a Memorandum of Understanding ("MOU") which was intended to terminate his relationship with AP1 in exchange for four month's salary and the sale of his shares to Creekside at cost.

Predictably, this did not improve the situation. Phillips refused to sign the MOU and was suspended by Galli and AP1's General Counsel, who had been appointed by Creekside without Phillips' knowledge or authorization. Phillips was alleged to have breached the USA, his Employment Agreement, and his fiduciary duties to AP1. Phillips was removed as a bank signing officer and Creekside moved AP1's books and records from its leased premises to a new office in another location.

A "tug of war" for control of the company ensued thereafter, including four separate court applications, and Creekside seeking to appoint a receiver over AP1. Phillips claimed that Creekside and its principals acted in bad faith and were trying to oust him at the point when AP1 was finally in a position to earn significant profits. Creekside's position was that the actions taken against Phillips were the result of an accumulation of misappropriation of funds and other financial abuses which directly affected Creekside since it was financing the entire AP1 operation. Creekside claimed that Phillips had disrupted relationships with AP1's customers and had refused to allow the company access to key electronic documents. While this was going on, an attempt by Phillips and Galli to jointly operate the

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company proved impossible.

In January 2021, Justice C. Gilmore of the Ontario Superior Court of Justice – Commercial List heard an application brought by Phillips under the oppression remedy in the *Canada Business Corporations Act*. The oppression remedy requires a claimant to provide evidence of specific reasonable expectations and to show how those reasonable expectations were breached by conduct that was oppressive, unfairly prejudicial or that unfairly disregarded the claimant's interests: *BCE Inc. v. 1976 Debentureholders*, 2008 SCC 69 (CanLII); 820099 Ontario; *Main v. Delcan Group Inc.* (1999), 1999 CanLII 14946 (ON SC), 47 B.L.R. (2d) 200 (Ont. S.C.J.).

Phillips argued that his reasonable expectations, as the founder of API, were to be involved with the business while it rolled out its technology into the marketplace. While he required funding, he had no expectation that he would be ousted from his positions as President, Director and CEO, and that the company would be packed up and moved to a new location. Phillips pointed to the content of the USA and the Employment Agreement as evidence of his reasonable expectation that he would continue to run AP1 and that his position and involvement in the company would not be unilaterally usurped by Creekside.

Justice Gilmore agreed with Phillips. The USA was signed by Phillips and Galli and there was no doubt it set out their mutual expectations. Further, there was no authority for Creekside to suspend Phillips. If Galli had a concern about Phillips' conduct, he and Creekside were obliged to obtain a Court Order if they sought to do anything that was not permitted in the USA or the Employment Agreement. Justice Gilmore found that Galli's intention on behalf of Creekside was to suspend Phillips from all positions including his position as Director. This conduct alone would be enough to meet the test for oppression, but Justice Gilmore's finding was bolstered by Creekside allowing Mr. Feghali to hold himself out as President and hiring a General Counsel without Phillips's authorization.

Justice Gilmore determined that Creekside used its leverage as the sole source of funding for AP1 to try and obtain concessions from Phillips such as selling his shares at cost and resigning as President, CEO and Director. The MOU was a clear example of Creekside's intention to oust Phillips without regard to the terms of the agreements signed by the parties. Justice Gilmore inferred that the timing of Creekside's actions had to do with AP1 being on the precipice of earning large profits and Phillips being a nuisance by blocking Creekside's plans for the company.

As a consequence of the findings of oppression, Phillips was provided with the opportunity to regain control of AP1 under certain terms and conditions. A valuation of the company showed that the liquidation value of AP1's assets was approximately \$2.3 million while the outstanding liabilities were \$5 million. AP1's shares were therefore worth \$0. Since an order buying out Creekside's shares would not provide Creekside with any monetary relief, Phillips was required to raise financing to pay out Creekside's loans within six months. If he cannot do so then AP1's assets would be sold in the course of receivership.

Creekside argued that allowing Phillips to operate AP1 would be detrimental as the company's main customer had stated that it would not work with him and Phillips would run AP1 "into the ground." However, since AP1 had never made a profit, Justice Gilmore reasoned that providing Phillips with control wouldn't necessarily hurt the situation. It would be up to Phillips to repair and develop client relationships. In the interim, Creekside's loans would continue to accumulate interest.

The decision reflects the court's balancing of the interests between a founder of a business and the investors who provide the funding to bring the business ideas to the marketplace. Often the investors will have little involvement in the day-to-day operation of the business but they may be understandably concerned if they see their financing in peril as a result of poor management decisions or other misconduct. Contracts such as employment contracts and shareholders agreements should be carefully crafted to protect all of the stakeholders' reasonable expectations and to address conflicts that may arise during the critical time period when a start-up company's long-term business plans and products are rolled out into the marketplace. A PDF version is available to download [here](#).

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