

# KEEPING CURRENT

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## Owner of corporation faces personal liability for stripping assets following lease default

By James R.G. Cook

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Corporations are separate legal persons with their own property rights and obligations. Individual shareholders are not generally liable for any acts or liabilities of the corporation. In some cases, however, a plaintiff may seek to impose personal liability on an owner of a corporation in circumstances where the corporation has no ability to pay a claim.

In *FNF Enterprises Inc. v. Wag and Train Inc.*, [2023 ONCA 92](#), a corporation leased premises in Kitchener, Ontario for use as a canine grooming, training, and daycare business under the terms of a lease that was to run until March 31, 2021.

In the ensuing litigation, the owners of the premises alleged that the corporate tenant abandoned the premises approximately one year before the end of the term, that no further rent was paid, and that the premises were not left in the condition the lease required. The owners further alleged that the business previously conducted at the leased premises by the corporation was moved to a different location in Kitchener under a different name.

The owners sued the corporate tenant but also the individual respondent, who was the corporation's sole director, officer, and shareholder. The owners claimed, in part, that the individual respondent conducted herself in a manner that justified imposing the corporation's liabilities on her and that she acted in a manner that entitled the appellants to relief against her under the oppression remedy in section [248](#) of Ontario's [Business Corporations Act](#) ("OBCA").

The individual respondent brought a motion to have the statement of claim struck against her on the basis that it failed to disclose a reasonable cause of action. The motion judge agreed with her position and struck the claims against her without leave to amend.

On appeal, the owners argued that the gist of their claim against the individual was that she had stripped value from the corporation and caused the business to be carried on elsewhere, knowing that amounts were owed by the corporation under the lease.

“Piercing” or “lifting the corporate veil” is an equitable exception to the rule that a corporation is a separate legal person and that individual shareholders are not generally liable for the corporation’s acts or liabilities.

Under a two-part test for piercing the corporate veil set out in *Transamerica Life Insurance Co. of Canada v. Canada Life Assurance Co.*, [1996 CanLII 7979 \(ON SC\)](#), aff’d [1997] O.J. No. 3754 (C.A.), the courts will disregard the separate legal personality of a corporate entity where (i) the corporation is completely dominated and controlled by the individual and (ii) it is being used as a shield for “fraudulent or improper conduct”. The conduct at issue must give rise to the liabilities that the plaintiff seeks to enforce.

The rationale underlying the exception is that the corporate form may not be abused to the point where a corporation is not truly separate and is being used to facilitate fraudulent or improper conduct: *Yaiguaje v. Chevron Corporation*, [2018 ONCA 472 \(CanLII\)](#).

In *642947 Ontario Ltd. v. Fleischer*, [2001 CanLII 8623 \(ON CA\)](#), at paragraph 68, the Court of Appeal affirmed that the corporate veil can be pierced when those in control of a company “expressly direct a wrongful thing to be done”.

The issue is what is wrongful since an individual could be accused of acting wrongfully every time they direct a corporation to breach a contract or take other steps that may result in claims against the corporation.

In the case at hand, the owners were seeking to recover the rent and other expenses owing by the corporation under its lease. To meet the test for piercing the corporate veil, the wrongful conduct

alleged against the individual owner must have given rise to the corporation’s lease liabilities.

In the Court of Appeal’s view, it was not sufficient to allege that the individual controlled the corporation and made the decisions that it breach the lease. The fact that an individual, in their capacity as director or officer, decided that a corporation should breach a contract does not usually amount to the type of improper conduct that justifies piercing the corporate veil for inducing breach of contract or interfering with contractual relations.

The owners also alleged that the individual treated the corporation’s assets and business as her own and stripped value from the corporation knowing of its lease liabilities. This too was insufficient to ground personal liability since it was not the alleged stripping of assets that gave rise to the corporation’s alleged liabilities. The corporation’s lease liabilities had a source independent of any alleged value stripping by the individual.

Fortunately for the appellant owners, the Court of Appeal reached a different conclusion regarding their oppression claim under section [248](#) of the [OBCA](#).

An oppression remedy claim requires a complainant to show that they had reasonable expectations that were violated by corporate conduct that was oppressive or unfairly prejudicial to or that unfairly disregarded their interests. A creditor may be a complainant under the oppressive remedy in certain circumstances.

In *Wilson v. Alharayeri*, [2017 SCC 39](#), at paragraph [47-55](#), the Supreme Court of Canada held that personal liability may be imposed on a director for oppressive conduct if two criteria are met: (1) the director has the requisite degree of

involvement in the oppressive conduct so that it is attributable to them; and (2) personal liability is fit in the circumstances.

The Court of Appeal noted that there was a distinction between claims of a creditor who could, but did not, protect itself from a risk it assumed when it entered into an agreement with a corporation and those claims of a creditor involving interests that were compromised by unlawful and internal corporate manoeuvres which the creditor cannot effectively protect itself against.

The motion judge erred, in the Court of Appeal's view, in striking the oppression claim as it fell within the latter category. The allegation that the individual stripped value from the corporation knowing of its liabilities is an allegation of unlawful and internal corporate manoeuvres against which the appellant owners, as creditors, could not effectively protect themselves.

In light of the allegation of unpaid amounts owing to creditors, the corporation's sole shareholder was arguably not entitled to use the corporation's money as her own or to appropriate its business. The allegations that she stripped value from the corporation to avoid payment of amounts known to be owing to the appellant owners was an arguable case for a personal remedy against her under the oppression remedy relating to the stripped value. Further, the *OBCA* has a statutory prohibition on directors who are also shareholders from taking assets in priority to, and to the prejudice of, unpaid creditors.

Accordingly, the Court of Appeal allowed the owners' appeal to the extent of permitting them to amend their statement of claim to assert their claim for a personal remedy against the individual under the oppression remedy. Whether

the individual will ultimately be found personally liable for the corporation's obligations under the lease will be determined on another day.

### **Contact us**

If you have a litigation matter and are in need of legal advice, please do not hesitate to contact James Cook, at 416.865.6628 or [jcook@grllp.com](mailto:jcook@grllp.com).

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