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Chapter 1

Organization of a Business

All references in this and the following chapters of the Practice Material: Company to the “Business Corporations Act”, the “BCA” or to the “Act” and to sections are references to the Business Corporations Act, S.B.C. 2002, c. 57, as amended, and to sections of that Act, unless otherwise indicated. References to the “Regulation” are references to the Business Corporations Regulation (B.C. Reg. 65/2004), as amended. References to the CBCA are references to the Canada Business Corporations Act, R.S.C. 1985, c. C-44, as amended, and references to the Company Act are to the Company Act, R.S.B.C. 1996, c. 62.

This chapter and most of the following chapters of the Practice Material: Company will focus on the Business Corporations Act. However, there are several defined terms in the Business Corporations Act that reference or include terms used in the former act—Company Act, R.S.B.C. 1996, c. 62. See, for example, the terms “memorandum” and “articles” in s. 1(1). There also continue to be references to “pre-existing companies”, despite the fact that the two-year period in which companies were to have transitioned has passed, since that term remains and forms the basis for some distinctions for certain provisions.


§1.01 The Unstructured Business

Many people carry on a business without any formal legal organization. Of course, they must obtain business licences and fulfill any particular requirements of their trade, occupation or profession. If a person carries on business alone, the business is called a sole proprietorship. The only legal requirement for a sole proprietorship (apart from laws of general application, such as income tax and licensing provisions) is that if a person is engaged in business for trading, manufacturing or mining purposes, and uses a business name other than his or her own, that person must file a declaration of this name with the registrar. A company that carries on business in a name other than its own also must file a declaration of the name.

A Band is a unique legal structure in Canada that derives power and authority from inherent Aboriginal rights, through the Indian Act, and through delegated authority by agreement. The law recognizes most aboriginal communities as Bands, which consist of members and reserve lands. A Chief and Council govern a Band. Beyond this legal recognition, Bands will often create corporations or societies to conduct certain business and deal with land.

Where two or more people are carrying on a business without formal organization, they will probably be a partnership. The Partnership Act, R.S.B.C. 1996, c. 348 (the “Partnership Act”) defines partnership as “the relation which subsists between persons carrying on business in common with a view of profit” (s. 2).

People carrying on a business together may not be aware that they are legally in partnership. They may have no formal agreement. There is a body of case law concerned with determining whether or not people are in partnership. Generally, the test is related to the law of agency. If individuals carry on a business as agent for, or on behalf of, one another they will be partners. Section 4 of the Partnership Act provides some guidelines for deciding whether or not there is a partnership. The most important guideline is found in s. 4(c), which provides that if a person receives a share of the profits of the business, he or she will be treated as a partner in the business, in the absence of evidence to the contrary. Further, legally separate forms of business organization can be treated as a single entity under the Labour Relations Code, R.S.B.C. 1996, c. 244 or the Employment Standards Act, R.S.B.C. 1996, c. 113.

§1.02 Choosing a Business Structure

Although persons may be sole proprietors or partners without appreciating that fact, they may also deliberately select one of the many alternative forms of business organization. They may decide to form a business corporation, either under a federal or provincial corporation statute or, in a small number of cases, they may decide to form a limited partnership or a limited liability partnership (LLP).

There are three objectives that most clients are interested in achieving:

- limited liability;
- optimal tax position; and
- control of all major decisions.

Unfortunately, no form of business organization allows a client to achieve all three objectives.

---

[§1.03] Sole Proprietorship

Generally, the sole proprietorship is the simplest form of business organization. It is suitable only for someone who intends to carry on a business alone, perhaps with the help of employees. It is not suitable if other people are expected to participate in the ownership of the business.

Potential advantages of a sole proprietorship include the following:

- it is inexpensive to set up;
- only the proprietor has the ability to bind the business (although employees and other individuals who are or are held to be agents of the proprietor can also bind the business); and
- the proprietor can write off losses directly against personal income and achieve close to an optimal tax position.

Some potential disadvantages are:

- there is no limited liability;
- only the proprietor can write off losses; and
- only the proprietor is in a growth position.

[§1.04] Partnership

If two or more people have decided to go into business together, they may choose a partnership for a variety of reasons.

- They may be legally unable to incorporate.
- The organization of the partnership can be simple and inexpensive. There are very few legal requirements for forming a partnership. If two or more people are becoming partners for trading, manufacturing, or mining purposes, they are required under the Partnership Act to file a brief description of their partnership. This is much simpler and cheaper than the incorporating a company under the Business Corporations Act.
- All partners are able to share in the management of the company, in the absence of a partnership agreement that states otherwise.
- In some cases, a partnership may provide tax advantages because business losses can be deducted against other personal income. For example, if the owners of the business expect there will be losses in the first years of operation of the business, they may want to use a partnership so that they can apply these losses as individuals against other sources of income.
- The major disadvantage in a general partnership is the liability it imposes upon the partners. Each partner is personally liable for the losses of the business, and may also be liable for the wrongful acts of his or her fellow partners (and employees) if those acts are committed in connection with the partnership business. There is no public way of restricting the authority of the various partners of a general partnership. Consequently, the acts of one partner in conducting the business, even if not authorized by the others, may bring liability upon them all. This general type of partnership is only suitable for a relatively small number of people who can repose substantial trust and confidence in one another.

Although it is not essential to have a written partnership agreement, it is usually a good idea to have one for the obvious advantages that a written agreement has over an oral one. In addition, the Partnership Act imposes a system of rights and duties upon partners, which they may want to vary. For example, under the Partnership Act, all of the partners are entitled to share equally in the profits of the business. This may not be the arrangement that the partners want and they are free to change this by private agreement. A partnership agreement may be needed for many other reasons, such as to define management responsibilities, and to ensure the partnership’s continued existence after a partner departs. Negotiating and drafting a partnership agreement can be complex and expensive depending upon the needs of the partners and the complexity of their business arrangement.

[§1.05] Limited Partnership

In some cases, the parties may decide to form a limited partnership to carry on a business. Limited partnerships, like corporations, are creatures of statute and do not come into being until the statutory requirements have been fulfilled. In British Columbia, these requirements are found in the Partnership Act.

A limited partnership combines some of the advantages of a partnership with some of the advantages of a corporation. It consists of two kinds of partners—“general” and “limited”. General partners have much the same liabilities, rights and duties as ordinary partners. Limited partners, however, are investors primarily. Their liability for the business debts and obligations of the partnership is limited by the Partnership Act to the amount of capital they have agreed to contribute to it. This form of business organization permits investors the protection of some limitation of their liability while allowing them the income tax advantages of a partnership form of organization (that is, they can deduct losses against personal income). This makes the limited partnership, like the corporation, a way to raise capital for a business. The limited partners’ right to transfer their ownership may be restricted. Also, the rights of the limited partners depend on the agreement creating the partnership and not on statute.
Usually, the general partner of a limited partnership will be the promoter (or a company owned or controlled by the promoter) and the manager of the business. The general partner itself will usually adopt the corporate form, thus ensuring limited liability for its own members. The limited partners are usually individuals seeking the tax advantages of limited partnership participation in the particular type of investment offered.

A limited partnership, though quite simple to form, is in fact a complex and sophisticated form of business organization. A certificate must be filed under s. 51 of the Partnership Act and an extensive limited partnership agreement must be prepared. This agreement is tailored to the particular business that is being undertaken by the limited partnership. For factors to consider in these agreements, refer to the Law Society of BC’s Practice Checklists Manual at Quicklinks > Publications and Resources > Practice Resources > Checklists Manual www.lawsociety.bc.ca/page.cfm?cid=359&t= Checklist-Manual.

Limited partnerships have other potential disadvantages, including the following:

- third parties, such as lenders, are reluctant sometimes to deal with limited partnerships;
- limited partners have no management control, while general partners have no limited liability (unless they incorporate);
- arguably, the Partnership Act does not have protections for limited partners equivalent to the legislated protections for minority shareholders; and
- limited partners who get involved in operations may be deemed to be general partners.

**[§1.06] Limited Liability Partnership**

A limited liability partnership (LLP) is a modified form of general partnership. Like limited partnerships, LLPs are created by statute and do not come into existence until the statutory requirements have been fulfilled. The concept of an LLP is relatively new, having been first developed in the United States in the 1980s. Although this business structure has been used for professional corporations in some other provinces in Canada for several years, LLPs have only been permitted in British Columbia since January 2005.

The Partnership Amendment Act, 2004 amended the Partnership Act to permit the creation of LLPs and the transition of existing general partnerships into LLPs for both professional partnerships and other businesses.

LLPs have many of the same advantages as limited partnerships, with the added benefit that the members of an LLP can take an active role in the business of the partnership without exposing themselves to personal liability for the acts of their other partners beyond the value of their investment in the partnership.

To form an LLP, a registration statement in the prescribed form must be filed with the registrar (Partnership Act, s. 96(2)). However, in most cases, the partners will also enter into an extensive and sophisticated partnership agreement, which governs their respective rights and obligations with respect to each other and the business of the partnership. Once an existing general partnership has been transitioned to an LLP, it must promptly take reasonable steps to notify all of its existing clients, in writing, that the registration has occurred and of the resulting changes in the liability of the partners (s. 107).

The partners of an LLP are personally liable for a partnership obligation if and to the same extent that they would be liable if the obligation was an obligation of a corporation and they were directors of that corporation (s. 105(1)); however, the partners are not subject to the duties imposed on directors or a corporation by common law or under s. 142 of the Business Corporations Act.

**[§1.07] The Corporation**

Most businesses, whether large or small, are carried on in the form of a corporation. A corporation is created by fulfilling the formal requirements of a federal or provincial statute. The result of incorporation is the creation of a separate, distinct legal entity. This means that the corporation can sue and be sued in its own name; enter into contracts as can a natural person, including contracts with its own shareholders; and hold property in its own name.

A “corporation” is an “artificial being, invisible, intangible and existing only in contemplation of law”, a separate legal entity from its shareholders—its liabilities being its own and generally not those of its shareholders. “Company” is a name commonly used for a corporation engaged in business. Watch for specialized uses of the two words “company” and “corporation” in the statutes.

In s. 1(1) of the Business Corporations Act

- “company” means a corporation that is recognized as a company under the Business Corporations Act or a former Companies Act and that has not ceased to be a company;
- “corporation” means a company, body corporate, body politic and corporate, association or society, but does not include a municipality or a corporate sole; and
- “British Columbia corporation” means (a) a company, or (b) a corporation, other than a company or a foreign corporation that is created in or continued into British Columbia;
Generally speaking, British Columbia companies fall into four categories:

- “Public company”, defined in s. 1(1) to include a company that is a “reporting issuer” under the securities legislation of any jurisdiction in Canada or a reporting company under United States securities legislation.
- “Closely held company”, a colloquial term that has come to mean a company with a small number of shareholders who invest together in circumstances that do not require them to have ongoing disclosure or reporting obligations under securities legislation. Also referred to as a “non-reporting company” or a “private company”.
- “Pre-existing company”, defined in s. 1(1) as a company that was recognized as a company under a former Companies Act. The many companies that already existed at the date the Business Corporations Act came into force are pre-existing companies.
- “Pre-existing reporting company” (s. 1(1)), which refers to a small number of companies under the Act that were “reporting companies” under the Company Act but not “reporting issuers” under applicable securities legislation. In practice it will be rare to deal with this type of company.

In the CBCA, a “corporation” is simply defined as a body corporate incorporated or continued under the CBCA and not discontinued under it.

Many Bands incorporate companies under the Company Act or the CBCA to establish a separate legal entity for economic development, owning fee simple lands, or leasing reserve lands. As a Band does not fit the definition of “owner” under the Land Title Act, R.S.B.C. 1996, c. 250, a Band may use a corporation to own fee simple lands. In addition, a Band cannot lease reserve lands without complying with the provisions of the Indian Act, which requires the Ministry of Aboriginal Affairs and Northern Development Canada to enter into a lease on behalf of the Band, unless the Band has obtained authority under the First Nations Land Management Act, S.C. 1999, c. 24. If a Band wants to designate its’ reserve lands for leasing, sometimes a Band-owned company is incorporated to enter into a head-lease with AANDC (ss.37-39, and 53, Indian Act). Once the company has entered into a head-lease, the Band-owned company can then sub-lease the reserve land.

A corporation can be more expensive to set up and maintain than other types of business organizations. However, corporations have a number of attributes that may be advantageous to its shareholders.

The following are some of the advantages:

1. Immortality

A corporation is said to have potential immortality, whereas a partnership is automatically dissolved in a number of situations. For example, if a partnership consists of only two partners and one of them dies, the partnership is dissolved. A corporation, continues to exist even if all its shareholders may change or even if it, for a time, has no shareholders.

2. Limited Liability

Under all Canadian statutes providing for the incorporation of companies, the members who form the corporation and who become its shareholders are only required to contribute toward the debts of the corporation the amount that they have agreed to pay for their shares in the corporation, which may be a very small amount. For example, a corporation may have only one share issued to a single shareholder for $1. Technically, this shareholder's liability for that corporation’s debts is limited to the amount of the $1 share price.

However, limited liability may provide less protection than is often supposed. For example, when a company is borrowing money or entering into a lease, the principal shareholders of the company are frequently required to give their personal guarantees of the company’s obligations. Limited liability does provide some protection, particularly from general trade creditors, and in situations where the company becomes liable for wrongful acts (such as a company employee carelessly driving the company truck on company business and running down a member of the public).

3. Transferability of Shares

Transferring partnership interests can be difficult and cumbersome. However, the shareholder’s interest in a company (shares) may easily be made transferable. In most small companies some restriction on the transferability of shares is likely because, among other reasons, the shareholders often are actively involved in the company and may not want new shareholders joining them who do not have their interest or expertise.

4. Separate Legal Entity

Corporations formed under the various Canadian corporation statutes have the ability to do anything a natural person of full legal capacity can do. However, the types of business that they may carry on may be restricted.

The articles of a British Columbia corporation might contain a prohibition against the company carrying on certain businesses, although such a
prohibition would be unusual. The articles of a British Columbia company set out the rules of conduct for the company and the relationships between its shareholders and the directors (for example, the power of the directors to manage the company). Although the Business Corporations Act permits a company to include very comprehensive rules in its articles, in some cases, shareholders of small companies will enter into a separate shareholder’s agreement to further delineate their rights and duties among them. One advantage of doing so is that, if the needs of the company were to change, it is often easier for the parties to a shareholder’s agreement to amend that agreement than for shareholders to amend the articles.

5. Capital

The corporate form may also make raising capital for the business easier. One of the original purposes of a corporation was to bring together a large number of individuals who could pool their capital (called joint stock) and carry out enterprises that were too costly for a small partnership. Today a corporation may still raise money by selling its shares, which may be of various kinds having many different features. A corporation may also borrow money and issue or grant debentures or other security to its creditors. This may be done with lenders or through the sale of portions of this debt security to private individuals.

6. Tax Advantages

A company’s separate legal personality also provides it with a number of possible tax advantages. Some companies receive preferential income tax treatment (for example, the small business deduction), and companies often provide more flexibility in deferring taxes and in allowing the division of business income. On the other hand, a company can experience less than optimal tax treatment for business losses, particularly if the business never earns a profit against which losses can be taken.

7. Rights and Remedies of Shareholders

Shareholders can participate in the management of the company to the extent they have control over the election of directors or as the company’s articles may otherwise provide. Shareholders have several other rights and remedies, such as legislated protection for minority shareholders (see Practice Material, Company, Chapter 17). A shareholders agreement may be required for management and other purposes and there may be considerable cost involved in negotiating and drafting it.

[§1.07.1] The Unlimited Liability Company

In 2007, British Columbia became the third Canadian jurisdiction to permit the operation of unlimited liability corporations. The primary advantage of this type of corporation is that the tax treatment in the United States makes it attractive to U.S. firms seeking to move investment capital into Canada.

Unlimited liability companies have the same powers as regular companies and are taxed in Canada identically to other corporations. In the U.S., however, the U.S. Income Tax Regulations historically have given a Canadian unlimited liability corporation the opportunity to elect not to be treated as a corporation for U.S. tax purposes but to be treated instead as a partnership (if it has multiple owners) or disregarded entity (if it has a single owner). A tax advantage results because the profits and losses of the Canadian unlimited liability corporation are allowed to flow-through the U.S. unlimited liability corporation to its U.S. shareholders. Given the primary advantage, it is important to understand the differences in language and fees applicable to these companies under the B.C. Business Corporations Act, as compared to the legislation of the other two provinces—Nova Scotia and Alberta. It also is important to stay current with U.S. tax regulations as well as tax treaties. For example, in the fall of 2007, the United States and Canada signed the fifth Protocol to the Canada-United States Income Tax Convention, which amendments impact the tax benefits of some of these entities. The Fifth Protocol came into effect on December 15, 2008. Always obtain tax advice in the U.S. and Canada. These details and strategies are beyond the scope of these materials. For further information, see Chapter 1 of the B.C. Company Law Practice Manual (CLEBC).

In terms of general procedures, unlimited liability companies use the same incorporating procedures that other companies do in B.C. There are a few key differences, which are designed to give the public notice that they are dealing with this special type of company, i.e. by requiring the words “unlimited liability company” or “ULC” in the name of the company (s. 51.21).

Existing B.C. companies may convert to an unlimited liability company by passing a unanimous shareholder’s resolution. However, all shareholders, whether or not their shares carry a right to vote, must agree to the conversion. B.C. companies may amalgamate with other B.C. companies to create an unlimited liability company, but amalgamations between foreign companies and B.C. companies to create an unlimited liability company are not permitted.
[§1.08] Jurisdiction of Incorporation

Once the form of organization has been decided upon, the participants in the business must also decide where to incorporate. In Canada, two types of jurisdictions have authority to incorporate: federal and provincial. Parliament is competent, by s. 91(2) of the Constitution Act, 1867 (“trade and commerce” power), to create corporate entities. Parliament also has power to incorporate by royal prerogative. Section 92(11) of the Constitution Act, 1867 provides that each province shall have the right to incorporate companies “with provincial objects”. In addition, corporations incorporated outside Canada may be permitted under the laws of a province to be recognized as such and to carry on business in the province. For further discussion of this issue, see Chapter 1 of the BC Company Law Practice Manual.

[§1.09] Choice of Jurisdiction

The following matters should be considered when deciding whether to incorporate in the federal or provincial jurisdiction (see also BC Company Law Practice Manual (CLE), §1.6 to §1.38).

- A federal company has the capacity to carry out its purposes throughout Canada as of right. It does not have to worry about name changes if it wants to do business in a province where there is a corporation with a similar name.

- A federal company is subject to provincial laws of general application, but provincial laws cannot discriminate against a federal company (British Columbia Power Corporation v. British Columbia (Attorney General) (1963), 44 W.W.R. 65 (B.C.S.C.)).

- In most provinces, a federal company carrying on business there must register as an extraprovincial company. This is an additional expense, particularly if it is carrying on business only in one province.

- A provincial company can carry on business within its own province as of right, but to carry on business in any other jurisdiction, it must receive the right by registering (or otherwise becoming qualified) as an extraprovincial company in that jurisdiction. Such registration can be refused by the other jurisdiction.

- A provincial company is restricted to provincial objects, in the sense of its business being within provincial legislative jurisdiction (not in the geographical sense).

- Consider the local, national or international/cross-border nature of the business.

- Some provisions in the Business Corporations Act are stricter or more complex than in the CBCA, and vice versa. It is essential to compare provisions concerning the liability of directors; the respective requirements for residence; financial disclosure; meetings of directors; inspection of corporate records; special or exceptional resolutions; continuance to/from other jurisdictions; and share transfer provisions.

- The time element may be relevant. If you must deal through Ottawa under the Canada Business Corporations Act, there may be a greater delay than dealing through Victoria under the Business Corporations Act; however, with electronic filing and messaging being used more widely, it is likely that this factor has little impact on the decision.

[§1.10] Federal Corporations

There are many federal statutes that permit incorporation of companies, but the main one for general incorporation, suitable for almost all purposes, is the Canada Business Corporations Act, R.S.C. 1985, c. C-44.

1. Canada Business Corporations Act (CBCA)

On December 15, 1975, the CBCA superseded the Canada Corporations Act in respect of incorporation of companies previously incorporated under Part I of the Canada Corporations Act (see below). Those companies must have elected to “continue” under the CBCA before December 15, 1980 or were automatically dissolved.

This CBCA was amended by An Act to Amend the Canada Business Corporations Act and the Canada Cooperatives Act, S.C. 2001, c. 14, which came into force on November 24, 2001 (SI/2001-14). The Regulations under both Acts also came into force on that date: see the Canada Business Corporations Regulations, 2001 and the Regulations Amending the Canada Cooperatives Regulations.

Like companies under the Business Corporations Act, companies under the CBCA generally have the capacity and powers of natural persons, except that they may not carry on the businesses described in s. 3(4). Note, in particular, that a CBCA corporation may not carry on the business of a loan company.

2. Canada Corporations Act (CCA)

Part I of the CCA applied to companies incorporated before December 15, 1975 for purposes or objects under the legislative authority of Canada, except railways, telephones, insurance companies, trust companies, loan companies and banks (CCA, s. 5). This Part contains numerous rules and provisions applying to all companies incorporated under the CCA (see below), including provisions relating to corporate powers, capital, shares, corporate changes, meetings, duties, directors, by-laws, regulations, filings, prohibitions, and permissions.
Part II of the CCA governed the incorporation of companies without share capital for the purpose of carrying on national, patriotic, religious, philanthropic, charitable, scientific, artistic, social, professional or sporting character, or the like objects and in more than one province (without gain to its members) (CCA, s.154). On October 17, 2011, the new Canada Not-for-Profit Corporations Act (CNFP Act) was proclaimed in force. Federally incorporated non-share capital corporations will have three years from October 17, 2011 within which to continue under the CNFP Act. From October 17, 2011 to October 17, 2014 there will be two federal statutes in force: (i) the new CNFP Act, and (ii) Part II of the Canadian Corporations Act (CCA), which will continue to govern corporations that have not yet continued under the new CNFP Act. However, all new incorporations must take place under the CNFP Act – no body corporate may be incorporated under Part II of the CCA as of October 17, 2011. Failure of a federal CCA corporation to continue under the CNFP prior to October 18, 2014 will result in its involuntary dissolution. See Practice Material: Company, Chapter 20 for more detail.

Part III contains various statutory provisions and regulations of a general nature that apply only to companies incorporated under special Acts of Parliament.

Part IV permits British and foreign mining companies to carry on operations in the Northwest Territories and the Yukon.


Companies incorporated by Special Acts of Parliament include those specifically excluded from Part 1 of the CCA by s. 5. For example, railways, telephones, insurance companies, trust companies, loan companies, and banks, and those which are required, under certain statutes of general application, to be so incorporated (for example, the National Energy Board Act requires pipeline companies to be so incorporated) are excluded. Companies can also be incorporated by special Act (although within the scope of Part I of the CCA) if special facilities are desired or some obligation or requirement of the CCA must be dispensed with.

Procedures for incorporation of such companies are usually made by an application to the Senate by way of a private bill, although the procedure also can be initiated in the House of Commons. The rules of the Senate prescribe the procedure with respect to applications to Parliament for private bills.

4. Bank Act

All banks are under federal jurisdiction. To incorporate a bank, a special Act or letters patent (see §1.11) are needed, but the form of the statute and provisions as to internal regulations, duties, powers, meetings, capital stock and shares, etc. are set out in the Bank Act, S.C. 1991, c. 46.

5. Trust and Loan Companies Act

The Trust and Loan Companies Act, S.C. 1991, c. 45, is the equivalent of the Business Corporations Act for federal loan and trust companies incorporated by letters patent issued by the Minister of Finance. This Act contains a sunset provision for companies incorporated under this Act to not carry on business after March 31, 2002.

6. Pension Fund Societies Act

The Pension Fund Societies Act, R.S.C. 1985, c. P-8 provides for incorporation of a pension fund society (without a special Act of Parliament or grant of letters patent) by certain officers of a corporation legally transacting business in Canada, upon making a declaration, as set out in the Act, and filing that declaration in the office of Minister of Industry and elsewhere.

7. Others

The Boards of Trade Act, R.S.C. 1985, c. B-6 provides that at least 30 merchants, traders, etc., carrying on business in certain areas with minimum populations, may organize themselves into a corporation as a Board of Trade.

[§1.11] Provincial Corporations (British Columbia)

1. The Business Corporations Act

The Business Corporations Act, S.B.C. 2002, c. 57 is the principal statute dealing with the incorporation and regulation of companies in British Columbia and it is the main focus of these materials. This Act replaced the Company Act, R.S.B.C. 1996, c. 62.

2. Society Act

The Society Act provides for the incorporation of societies which are for national, charitable, scientific, educational, social and other similar purposes, and which may not carry on any trade, industry or business or profession for profit or gain. A society may also be formed, subject to the approval of the Superintendent of Financial Institutions, to provide for certain death, accident, sickness and disability benefits, pensions or annuities to its members.

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Many Bands incorporate societies to establish a separate legal entity, which can deliver programs and services for the benefit of members. A Band’s goal in incorporating a society is to place the society at arms’ length from Band politics and to enable members to be involved in delivering programs and services.

Chapter 20 discusses societies formed under the Society Act, R.S.B.C. 1996, c. 433.

3. Special Acts of the Legislative Assembly
From time to time, the Legislative Assembly incorporates companies by passing a private or public Act. School boards, drainage and sewage disposal boards, park boards, religious orders, professional bodies, schools, unions, universities, and colleges are generally incorporated by public Act.

A private business undertaking may be organized by a special Act passed on a private bill. This is used where the Business Corporations Act does not permit the undertaking to be incorporated under it; for example, an insurance company or trust company. All information should be obtained from the clerk of the House.

4. Financial Institutions Act
The Financial Institutions Act, R.S.B.C. 1996, c. 141 regulates the operations of trust companies, credit unions and insurance companies in British Columbia, and includes provisions respecting the incorporation of these financial institutions. One or more persons may subscribe to a memorandum, adopting articles, filing the prescribed form of application and paying the prescribed fees, to incorporate a trust or insurance company in British Columbia. After approval by the Superintendent of Financial Institutions and registration of the memorandum and articles, a certificate of incorporation is issued.

Certain provisions of the Business Corporations Act are made applicable to a trust company so incorporated.

5. Cooperative Association Act
The Cooperative Association Act, S.B.C. 1999, c. 28 provides for the incorporation of an association by 3 or more persons (subject to certain approvals) to carry on any business or activity on a cooperative basis, except the business of railways, banking, insurance or trust companies. There are certain specific restrictions as to the content of the name, and the capital must consist of an unlimited number of shares.

A memorandum is subscribed to and forwarded to the registrar. It is also necessary to include a set of rules, statement of incorporators, list of first directors and location of the registered office. If the memorandum and other documents are satisfactory, the registrar issues a certificate of incorporation. The statute details the powers of the association and has various statutory provisions with respect to its administration and operation. Certain provisions of the Business Corporations Act apply to cooperative associations.

6. Railway Act
The Railway Act, R.S.B.C. 1996, c. 395 provides for the incorporation of railway companies as well as for the construction, operation and regulation of railways and their tolls, including various matters dealing with railway companies. Various sections of the Business Corporations Act apply.

7. Others
There are many other statutes under which various forms of corporations are or can be created, such as the Community Charter, S.B.C. 2003, c. 26; Vancouver Charter, S.B.C. 1953, c. 55; and Strata Property Act, S.B.C. 1998, c. 43.

Methods of Incorporation

Currently, there are five different methods of incorporating a company in use in Canada.

1. Letters Patent
Quebec, Prince Edward Island and New Brunswick use letters patent as their method of incorporation. Such companies are considered analogous to Royal Charter companies, and accordingly are considered to have the capacity of a natural person. If such a company does any act going beyond the powers contained in its letters patent, such an act is not ultra vires, but merely constitutes a violation of the company’s charter rendering it liable for penalties (or in some cases, dissolution).

2. Registration of Memorandum and Articles
Incorporation by registering a memorandum and articles is the method used in Nova Scotia and Newfoundland and was the method previously used in British Columbia under the Company Act.

Normally these companies do not have the powers of a natural person, but only those given by the governing statute (which are usually quite general) or as set out in the memorandum. As such, the doctrine of ultra vires applies to them.

Generally, companies that are created by “registration” require more filings with government authorities than “business corporations” corporations.
3. Incorporation Application

In British Columbia, one or more persons form a company by entering into an agreement and filing an incorporation application with the Registrar of Companies that complies with and contains the information prescribed by ss. 10(2) and (3) of the Business Corporations Act. See Chapter 3 for a full discussion on incorporation procedures.

Like companies created using the memorandum and articles method of incorporation, British Columbia corporations have only the powers given by their governing statute (which are also quite general) and any acts exceeding those powers are ultra vires and a nullity so far as the company is concerned.

The Business Corporations Act expressly provides (s. 30) that a company has the rights, powers and privileges of an individual of full capacity. In addition, a corporation is capable of acquiring and holding property, rights and interests in joint tenancy in the same manner as an individual (s. 31).

Also a British Columbia corporation has the right, subject to its charter and to other restrictions imposed by law, to carry on business in any jurisdiction outside of British Columbia, to the extent that the laws of such other jurisdiction permit it to do so, and to accept from any lawful authority outside British Columbia powers and rights concerning the corporation’s business and powers (s. 32). If the memorandum (for a pre-existing company) or articles of a company has restrictions on businesses that the company can carry on, or on powers it can exercise, an act contravening these restrictions is not invalid by reason only that it contravenes those restrictions (s. 33(2)).

Section 421 provides that in proceedings by or against the company, there is no constructive notice of documents merely because they are filed with the registrar, or are available for examination at an office of the corporation.

Where the company contravenes or is about to contravene business or power restrictions, certain persons (including shareholders) may apply to court for an order restraining the company from doing any act, or from transferring or receiving any property (s. 228). The court also may provide compensation and other forms of relief.

4. Filing of Articles of Incorporation

Filing articles of incorporation is the incorporation method used in the CBCA and in provinces (including Alberta, Saskatchewan, Manitoba and Ontario) that have adopted Acts based on the CBCA.

It is believed that the doctrine of ultra vires does not apply to this type of corporation. Accordingly, the Acts state that an otherwise ultra vires act is not invalid.

5. Statute

A company incorporated under a particular statute or by a special Act is in the same position as a registration company and is subject to the doctrine of ultra vires. Such a company is not considered to have the capacity of a natural person, but only the capacity that the legislature gives to it.

[§1.13] Further Reading

Continuing Legal Education Society of BC (CLEBC) publications of interest to company law practitioners are:

- Advising British Columbia Businesses, updated looseleaf.
- Charities and Not-for-Profit Law Conference (annual).
- Company Law Deskbook, updated looseleaf for legal support staff and new lawyers.
- Corporate Procedure Basics for Legal Support Staff
- Managing Aboriginal Community Assets (September 2002)
- Partnerships and Societies for Legal Support Staff and Junior Lawyers 2011
- Private Companies Structuring the Entrepreneur (June 2005)
- Working with Partnerships (June 2009)

Business: Company
Chapter 2

Public and Private Companies in British Columbia1

For further discussion of this subject please see the British Columbia Company Law Practice Manual (Vancouver: CLEBC), Chapter 2.

How a company is characterized has implications for how the company may raise capital or finance the business (see Chapters 6 and the Securities Act). How a company is characterized influences how the company should be structured initially, as well as how it can be managed (under the Business Corporations Act).

§2.01 Public Companies

Section 1(1) of the Business Corporations Act defines a public company as

- a reporting issuer (as defined in the Securities Act),
- a reporting issuer equivalent (a corporation that is a reporting issuer or the equivalent of a reporting issuer in any other jurisdiction in Canada),
- a company that has registered its securities in the United States under the Securities and Exchange Act of 1934,
- a company that has any of its securities, within the meaning of the Securities Act, traded on or through the facilities of a securities exchange, or
- a company that has any of its securities traded on a securities exchange or quotation system.

(See Practice Material: Company, §1.07.)

Most of the provisions in the Business Corporations Act dealing with “public companies” are restricted in scope to dealing with issues about the initial structure and ongoing management.

§2.02 Reporting Issuers

Generally, a “reporting issuer” is an issuer that has become subject to the continuous disclosure requirements of the Securities Act and related legislation, in most cases by having had a prospectus receipted by the British Columbia Securities Commission.

§2.03 Private Companies

The term “private company” is not defined in s. 1(1) of the Business Corporations Act because it is not used widely throughout the Act. The term is generally used to mean a company that is not a public company or a reporting issuer.

There is a definition of “private company” in s. 192(1) of the Business Corporations Act, which is used in the limited context of determining the liability of insiders who make use of specific confidential information in connection with a transaction involving any security of that company that benefits that insider or certain related parties. In this context, a private company is defined as a company that is not a reporting issuer, a reporting issuer equivalent, or a company in a class prescribed by regulation (ss. 192(1) and 432(2)(q)(iii)). If an insider uses specific confidential information in this way, then the insider is liable to compensate any person for any direct loss suffered by that person as a result, and is accountable to the private company for any direct benefit or advantage received or receivable by the insider or certain related parties (s. 192(3)). There are certain limited defences available to an insider (s. 192(3)(a)(i) and (ii) and 192(3)(b)) and there is a two-year limitation period for bringing an action under s. 192(3) (s. 192(4)). It is also possible for the parties to a transaction that involves a private company’s securities to agree in writing that s. 192 does not apply to that transaction (s. 192(5)).

While it is commonly assumed that the Securities Act does not apply to private companies and corporations, this assumption is incorrect. In fact, common corporate transactions of private companies must fall within certain exemptions under the Securities Act. Lawyers representing private companies must become familiar with the structure and ongoing management criteria of a “private issuer” as defined in the Securities Act, as well as the exemptions from the registration and prospectus requirements contained in British Columbia securities legislation, including National Instrument 45-106.

The criteria used for determining whether a transaction is exempt from the registration and prospectus requirements of British Columbia securities legislation are based on “closed system” concepts and the public’s “need to know”. These concepts include such factors as:

- relatively few shareholders,
- securities not being traded in securities systems,
- restrictions on transfer of securities,
- the dollar amount of the investment, and
- the relationship between the company’s principals and the prospective investors.

The colloquial term used to describe the type of company that is exempt based on the above factors is “closely held company”.

[§2.04] Consequences of Being a Public Company

All companies registered under the *Business Corporations Act* must have at least one director but public companies must have at least three directors (s. 120). There are special disqualification criteria for directors of public companies in the *Business Corporations Act*. However, lawyers should also be aware of the requirements and qualifications for directors of reporting issuers that are contained in the *Securities Act*.

Special rules that apply to proxy solicitations for pre-existing reporting companies are set out in s.184. Section 185(1) requires reporting issuers and reporting issuer equivalents to provide to their shareholders the annual financial statements that they are required to file with the Securities Commission under the *Securities Act* (or under legislation in other jurisdictions having similar scope and intent). Furthermore, ss. 224 and 225 require public companies to elect an audit committee to review and report to the directors on the company’s financial statements and related auditor’s report before those materials are published. There are professional auditor requirements for reporting companies that cannot be waived (s. 205(c)). Special procedures also apply to change the auditors of a reporting company (s. 210).

Section 203(2) permits the shareholders of a company to waive the appointment of an auditor for a specific financial year by unanimous resolution. Although public companies are not excluded from the application of this section, the requirements of s. 224 and 225 and the provisions of the *Securities Act* make such a resolution by the shareholders of a public company impossible. Section 182(2) allows companies to dispense with annual general meetings if the business required to be conducted at the meeting is consented to in writing by all of the shareholders entitled to vote. Again, public companies are not excluded from the application, but the requirements of the *Securities Act* will likely require a public company to hold an annual general meeting.
Chapter 3

Incorporation Procedures

For further information on this topic, see Chapter 4 of the British Columbia Company Law Practice Manual, (Vancouver: CLEBC). See also the “Checklist for Incorporation under the Business Corporations Act Procedure” in the Law Society’s Practice Checklists Manual Publications and Resources>Practice Resources > Checklists Manual. Also helpful are the provincial government’s Corporate Registry website (www.bcregistryservices.gov.bc.ca), and the seminars and publications by the Continuing Legal Education of BC.

One of the preliminary decisions for a company is what to name it. In British Columbia, there are particular name registration requirements. This chapter provides a description of the company name requirements.

In order to be “incorporated”, a company must also prepare and file, with the registrar of companies, an Incorporation Application, which includes a Notice of Articles (s. 10(1)). The incorporation application must be filed electronically. A description of the incorporation documents and the filing procedures for them follows.

Once the company has complied with the preliminary registration requirements, it must follow certain organizational procedures. These are described later in the post-registration procedure paragraph of this chapter.

[§3.01] Guidelines for Approval of Names

The Registrar of Companies must pre-approve a company’s use of a company name. The following guidelines set out both the procedures for companies to reserve names in British Columbia, and the criteria the registrar considers when deciding whether or not to approve the name.

If the proposed name of the company is the same name as the Band or aboriginal community, the registrar will require a Band Council Resolution to authorize using the name. When using aboriginal names, the registrar may also require a translation.

1. Reservation of Name

The registrar of companies may reserve a name for incorporation of a company under the Business Corporations Act (i.e. an intended company), register a change of name of a company, or register an extraprovincial company name for a period of 56 days from the date of reservation (s. 22(2)). In the case of a company intending to amalgamate, the registrar will allow any reasonable extended period to enable the company to proceed with the amalgamation procedure.

The applicant must fill out all requested information on the Name Approval Request Form. The form includes “Name Approval Request Instructions”, which provides an excellent summary of the requirements prescribed by the BCA. The applicant should submit a list of three names, in order of preference, to avoid repeated requests for single names. The prescribed fee must accompany all name reservation and approval requests. Check the registry website for the current schedule of fees and online name approval request form—www.bcregistrynames.gov.bc.ca/nro/.

Many law firms maintain deposit accounts with BC Online. If the firm has an account, names must be submitted for approval electronically and the registrar will debit the individual account.

2. Form of Name

Generally, names should have a distinctive element followed by a descriptive element and ending with the corporate designation. The distinctive element enables the public to distinguish one company from another so that the services or wares offered by each are distinguishable. This requirement is satisfied if initials, personal name or a geographic location is used.

The descriptive component requirement ensures that each company name indicates the nature of the business of the company. The descriptive element may be specific such as “ABC Muffler Service Ltd.” or may be fairly general such as “ABC Investments Ltd.”.

A company, other than a specially limited company, must have as the last word of its corporate name a corporate designation, that is, “Limited”, “Incorporated”, or “Corporation”, or the abbreviation “Ltd.”, “Inc.” or “Corp.” (s. 23(1)). An “unlimited liability company” must have the words “Unlimited Liability Company” or the abbreviation “ULC, as part of and at the end of its name (s. 51,21(1)). An “unlimited liability company” must have the words “Unlimited Liability Company” or the abbreviation “ULC, as part of and at the end of its name (s. 51,21(1)). Only one of the words “Limited”, “Incorporated”, “Corporation” or “ULC” for its abbreviation may be used.
A “number” name can be assigned to a company if requested. The number used is the distinctive element in the name. In this case a name reservation is not necessary, and the incorporation application states that the name under which the company is to be incorporated is the name created by adding “B.C. Ltd.” after the incorporation number of the company (ss. 10(3)(d)(ii) and s. 22), or in the case of an unlimited liability company “B.C. Unlimited Liability Company (ss.21(1)(b) and 55.212(4)(b)). The registrar will assign a “number” name, which will be the next available certificate of incorporation number, for example “0654321 B.C. Ltd.”. Note that for numbered companies incorporated after March 29, 2004, the number for a numbered company is formatted with a leading zero, plus six digits, plus B.C. Ltd. (Regulation, s.7.1(2)).

3. Registrar’s Discretion as to Names

Section 22(4) of the Business Corporations Act states that the registrar must not reserve a company name unless that name complies with the requirements prescribed by the Regulation and with the other requirements set out in Part 2, Division 2 of the Act (see ss. 23, 24, 25 and 26). These requirements give the registrar some discretion on whether or not a proposed company name is acceptable.

Subsection 7(1) of the Regulation sets out the guiding principle for the approval of a company name, which states that the name must not resemble

- the name of an existing British Columbia company;
- the name of any other corporation registered in British Columbia;
- a name already reserved with the registrar under s. 22 of the Act; or
- the name of an extraprovincial company registered under the Act,

to the extent that, in the opinion of the registrar, it is likely to confuse or mislead. However, the provisions of s. 7(1) do not apply to a federal corporation that wants to register as an extraprovincial company under the Act (Regulation, s. 7(2)).

All name approval criteria apply before incorporation or registration and extend to a name selected for a change of name (s. 263(3)).

If the name of a foreign entity (other than a CBCA company) contravenes any of these requirements, then it must reserve an assumed name in order to make an application to be registered as an extraprovincial company in British Columbia in accordance with s. 22 of the BCA (s. 26(1)). If the foreign entity reserves an assumed name, then the registrar may register that entity as an extraprovincial company with its own name so long as the entity provides an undertaking to the registrar that it will carry on all of its business in British Columbia under that assumed name (s. 26(2)). If an extraprovincial company adopts an assumed name under the Business Corporations Act, then it must acquire all property, rights and interests in British Columbia under that name; it is entitled to all such property, rights and interests, and to all liabilities incurred, as if acquired and incurred under its own name; and it may sue or be sued in its own name, its assumed name or both (s. 26(3)).

4. Name Approval Procedure

The registry staff checks the requested names against the corporate name register to determine if there is an identical name or similar names that in the opinion of the registrar would be likely to confuse or mislead. If there is no name on the register that is similar to the name requested, then further tests (that is, inclusion of the three required elements) are applied before approval of the name.

Lawyers who are assisting company clients with choosing a name should review the Name Approval Request Instructions issued by the registrar (Form 708B).

Before submitting a name, one or more of the following books or periodicals should be consulted by the applicant: telephone directories, city directories, gazettes of place names within British Columbia, trade journals, dictionaries and trademarks, the Internet, and any other publication that can give information and insight into a name.

A NUANS search is a search of a database, which contains the names of all federally and provincially incorporated corporations, business names registered in all provinces except British Columbia and Quebec and all applied for and registered trademarks. Many law firms maintain accounts to conduct NUANS searches for their company clients.

When there is a similarity in names, which may, in the registrar's opinion, be likely to confuse or mislead, the name will not be approved. In order to determine whether the names are too similar, one test is to place the names side by side and check for similarity, using both the sound of the words and appearance of the names to the eye.

Names such as “Tire Shop Ltd.” or “Shoe Store Ltd.” are not distinctive because many companies are carrying on the tire or shoe business. These types of names would be available by prefixing the descriptive portion of the name with a distinctive word such as a coined word, geographical location
or a person’s name. Typical names with the distinctive and descriptive elements would be “Xantrex Tire Company Ltd.” or “Smith’s Shoe Store Ltd.” One word names are not acceptable as they are too general and if used would not be sufficiently distinguished from any other company name starting with the same word, for example, “International Ltd.” is considered similar to “International Holdings Ltd.”

When the first word in a company name is distinctive and is placed before a well-known existing name on the register, the proposed name would not be acceptable. The entire name requested is scanned to see if it contains another existing company name, for example, “Victoria Eaton’s Department Store Ltd.”

A made-up word such as “Calvan” is not considered sufficiently distinctive in itself, as there may be many companies with the same first word in the name; they are acceptable as distinctive elements, however. The addition of a descriptive word makes the name acceptable and makes more names available with “Calvan” as the prefix, for example, “Calvan Holdings Ltd.”

Coined words may be used for the distinctive element of the name, for example, “Altrex Holdings Ltd.” A coined word plus a geographical location, such as “Altrex Canada Ltd.” is also considered sufficiently distinctive.

If the made-up or coined word has been trademarked and the registrar receives a copy of the trade-mark and is satisfied that the name is very distinctive, a one-word name may be considered. Each name is judged on its own merit, for example, “Harmac Ltd.”

A natural person’s full name is considered to be an acceptable corporate name, as are two surnames, and hyphenated separate surnames, for example “Bill Brown Ltd.”; “Green & White Ltd.”; “Brown-Black Ltd.”. Initials are also permitted along with the surname, for example, J.T. White Ltd. Initials are also considered distinctive when followed by a descriptive word, for example, “A.D.E. Enterprises Ltd.”

Numerals may be used in a company name but only as the distinctive element. A year may be used in a name providing it is the year in which the company was incorporated or, in some circumstances, the year in which it commenced business.

5. Extraprovincial Names

Provided there is not a similar name on the register, the registrar sometimes gives special consideration to an extraprovincial company that has been incorporated in another jurisdiction for a considerable period of time. An example is an established extraprovincial company with the name “Spray Painting Ltd.” Before registration, the registrar would require a written undertaking stating that the company would not object if the Registrar of Companies approved the incorporation or registration of a company name including the words “Spray Painting” in the name, for example, “Victoria Spray Painting Corporation”.

6. Name Not to Suggest Government Connection

The word “Government” in a name is not acceptable. Other words that may imply connection with, or approval by, levels of government require consent of the government. Examples of such words are “provincial”, “ministry”, “bureau”, “service”, “agency”, “department” or “board” in connection with government. There are general words in the name which may suggest governmental approval, such as “authorized”, “bonded”, “commission”, “certified”, “institute”, “warrant” and “council”. Any such words should be deleted from the name.

The prohibition of any unauthorized representation as to government authority is found in the Provincial Symbols and Honours Act, R.S.B.C. 1996, c. 380. The words “British Columbia” or “B.C.” or “BC” are considered to suggest connection or implied approval or sponsorship of the British Columbia government and therefore are not usually available other than as part of a numbered company name (for example, 123456 B.C. Ltd.).

When the British Columbia government is implied, written consent must be obtained from the Protocol and Events Branch, Intergovernmental Relations Secretariat. If the name otherwise meets the guidelines, the words British Columbia or B.C. are permitted at the end of a company name providing they precede the words Ltd., Inc., or Corp., for example, “Pacific Storage Warehouse British Columbia Ltd.” Where a company is a subsidiary or affiliate of an existing corporation in another jurisdiction, the words British Columbia or B.C. must be placed in brackets, for example, “Pacific Storage Warehouse (B.C.) Ltd.”
7. Name Not to Suggest Connection with Crown or Royal Family

The name of a company must not suggest or imply a connection with the Crown or any living member of the Royal Family, without first obtaining written consent from the appropriate authority. Words such as "Crown", "Royal", "King", "Queen" and the names of living members of the Royal Family are usually rejected, unless it can be shown that by reason of long bona fide usage the words do not suggest or imply connection with the Royal Family or Crown. Titles of Royal Family members such as "Prince of Wales" are also subject to the same prohibition. An exception to this usage is the well-known and long-standing reference to New Westminster as the "Royal City". Any reference to “Vice Regal” in a company name referring to a product that could be taken as an endorsement is prohibited by the Trade-Marks Act, R.S.C. 1985, c. T-13.

8. Name not to be Objectionable on Public Grounds

If, in the opinion of the registrar, a name is objectionable on public grounds, it will not be approved. A name will not be approved if it includes a vulgar expression, obscene words or racial, physical or sexual slurs. Any reference to a public figure in the name, which could cause embarrassment, would not be approved. A name is usually approved when the person involved consents in writing and the name only affects him or her and not the public generally. The name of a political party or leader is also prohibited without consent.

9. Well Known or Established Names

There are some words that are so well known that it would be against policy to grant them in a name, for example, Exxon, Xerox and Coke. The Corporate Registry does not maintain records of trade names and trademarks and therefore must rely on public knowledge of well-known trade-marks when making a decision on the approval of a name. Where the consent of the holder of a trade-mark or trade name is obtained, the name may be available if it otherwise meets the necessary requirements for name approval.

10. Identical or Similar Names Not Available

The registrar will not approve a proposed company name if it contravenes any of the requirements set out in the Regulation or in Part 2, Division 2 of the Business Corporations Act. One of the most common reasons for rejecting a name is that it is identical, or very similar to the name of an existing company.

The registrar will consider applications to register similar names having regard to the facts and decided cases. If a written consent can be obtained from a company on the register with a similar name to the name requested, the name may be accepted for incorporation or registration. This does not apply to an identical name.

Because most British Columbia companies do not have restricted businesses or powers (s. 33(1)), the question of similarity or being “likely to confuse or mislead” will normally be based on the actual wording of the name itself and not on the businesses actually being carried on by the similarly named companies.

The following is a list of descriptive words that refer to businesses that are usually considered to be similar so that when the distinctive prefix is the same the names are usually considered similar:

- hotel, motel, inn
- investment, securities, loan, acceptance, finance, mortgage, credit, fund, equities, capital, mutual funds
- logging, lumber, sawmill, forest products, timber, pulp
- mining, exploration, resources, oil, petroleum, energy, natural gas
- plumbing, heating, mechanical contracting
- refrigeration, cold storage, ice
- sand and gravel, aggregates, fill
towers, court, apartment, manor, lodge
- transfer, cartage, transportation, forwarding, trucking, reefer, van lines, moving, storage, transport
- warehousing, terminals, storage

The following is a sampling of distinctive prefixes that are similar enough in form so that if the descriptive word in both the names is the same the two names are usually considered similar:

- Arrow, Aero, Airo
- Canada, Canadian, Canadien, Kanada
- Canadian-American, Canam, American Canadian, Amcan
- Coast, Coastal
- North, Northern, South, Southern
- OK, Okanagan, Okanagon, Okan
- Pac West, West Pac, Pacific Western, Western Pacific
- P.G., Prince George
- Regent, Regency
- V.I., Vancouver Island, Van Isle
- West Coast, Wesco, Westco

These lists are not exhaustive but give some idea of the types of words, which because of their
similarity make the names under consideration appear similar.

Each name is treated on the basis of its own peculiar circumstances when being checked for approval.

11. Statutory Prohibitions or Restrictions on the Use of Words in a Company’s Name

Some statutes, both federal and provincial, restrict or prohibit the use of certain words, for example:

- “Architects”—Architects Act.
- “Board of Trade” or “Chamber of Commerce”—Boards of Trade Act.
- “Credit Union”—Credit Union Act.
- “Provincial”, “Province of B.C.”—Provincial Symbols and Honours Act.
- “Engineers”—Engineers and Geoscientists Act.
- “Canada Standard”, “C.S.”—trade mark of Dominion under or National Trade Mark Labeling Act.
- Names of universities, municipalities and word suggesting government patronage—Trade-marks Act.

12. Miscellaneous Restricted or Prohibited Words

There are many words that are prohibited, restricted or require consent or approval from some level of government or official board or commission before they are available for use in a company name. Some words are not available without a particular consent in any circumstances, and others are unavailable if they do not correctly describe the activities of the company and so mislead the public. The following is a list of the most common of these words.

- “Alcan”, “Shell”, “Gulf”, “Cominco”, “Toyota”, “Esso”, “Alsands”—words referring to very well known trade words or names not available without consent.
- “Amalgamation” and “Affiliation”—available only if the company is amalgamated or affiliated.
- “Architects”—require proof that “Architect” is a member in good standing with the Architectural Institute of B.C.
- “Armed Forces” “Veterans” or special reference to regiment or force—require consent of Dept. of National Defence.
- “B.C. Made”, “Japan Made”, “Product of U.S.A.”—words referring to where product made, not available.
- “Bankruptcy”, “Bankrupt”—not available in company name.
- “Bureau”, “Council”, “Board”—not available unless appropriate consent from government authority setting up council or board.
- “C.P.R”, “C.N.R.”, “B.C. Hydro”, “B.C.R.”—names or initials of well-known utilities and railroads not available.
- “Canadian Club”—not available in company name.
- “Certified”, “Guaranteed”, “Bonded” “Authorized”—not available as suggests government approval.
- “Chartered Accountant”, “C.A.”—require proof that “Chartered Accountant” is a member in good standing with the Institute of Chartered Accountants of BC.
- “Condominiums”, “Strata”—only available if followed by descriptive words such as “Management”.
- “Dentist”—require proof that “Dentist” is a member in good standing with the College of Dental Surgeons.
- “European Common Market”, “E.C.M.”—not available without consent of the E.C.M.
- “Institute”—usually not available as indicates government involvement.
- “Insurance”, “Insurance Brokers”—contact Insurance Council of B.C.
- “Jaycee”—must have consent of Canadian Junior Chamber of Commerce.
- “LL.B.”, “P.Eng.”—not available as corporation not entitled to these designations.
13. Internet Names

A new company starting up a web-based business should ensure that the name selected qualifies as both a corporate name and a domain name if it wants the names to be similar. If the Internet name has a distinctive and descriptive element, then the name may be approved as a corporate name by adding the corporate designation for example, Internet name: ABCInvestments.com; corporate name: ABC Investments.com Ltd.

1. Incorporation Agreement

An incorporation agreement is a short agreement in which the incorporators agree to take shares of the company. The agreement must include the full name of each incorporator and the number of shares of each class and series of shares being taken by that incorporator (s. 10(2)(b)). Also the agreement must be signed and dated by each incorporator (s. 10(2)(b)(ii)(A) and s. 10(3)). The incorporation agreement is held in the company’s records office, not filed with the registrar.

In most cases, the incorporator will have to sign both the incorporation agreement and the articles before incorporation. Consequently, these are often combined.

2. Incorporation Application

The Business Corporations Act requires that certain information be included in the incorporation application (s. 10(3)), including: the completing party statement referred to in s. 15; the full names and mailing addresses of the incorporators; the name of the company; and a notice of articles that reflects the information that will apply to the company upon its incorporation.

A “completing party” is an individual who completes a record that is to be submitted to the registrar for filing (s. 1(1)). Records may be completed in paper form or electronic form. The completing party may also provide the information necessary to complete a record to an agent or employee of the government. Some records, including an application for incorporation, can only be submitted to the registrar in electronic form.

Federal companies are not subject to name approval by the Registrar of Companies and are accepted even though the name is similar or identical to a company on the register in the Corporate Registry.
Section 15(1) of the *Business Corporations Act* requires the completing party to examine the articles and incorporation agreement to ensure that they have been signed in accordance with the requirements of s. 15(2). The completing party must also designate in the incorporation application the names of the persons who have signed both the articles and incorporation agreement (and no others). The completing party must complete these steps before an incorporation application is submitted to the registrar for filing.

3. Form of Incorporation Application

The incorporation application must be in the prescribed form (s. 10(3)(a)), which is Form 1 to the Regulation. The Form 1 must be submitted to the registrar for filing in an electronic format that is compatible with the technical requirements of the registrar (s. 30(2) of the Regulation).

4. Incorporators

An incorporator is a person who, before an incorporation agreement is submitted to the registrar for filing, signs the incorporation agreement respecting the company (s. 1(1)). The incorporation agreement and articles must be signed by every incorporator (ss. 10(2)(c) and 12(3)).

### [§3.03] Notice of Articles

The articles of a British Columbia corporation are held in the records office. They are not filed with the registrar. Instead, a notice of articles is included in the incorporation application (s. 10(3)(e)).

Section 11 of the Act sets out the minimum requirements for a notice of articles, including the following:

- the name of the company (s. 11(b));
- the full name of and the prescribed address for each of the directors (s. 11(c));
- the mailing and delivery address for the company’s registered and records offices (ss. 11(d) and (e));
- any translation of the company’s name that it intends to use outside Canada (s. 11(f));
- a description of the authorized share structure of the company in accordance with s. 53 of the Act (s. 11(g));
- whether there are or were any special rights and restrictions attached to any class or series of shares of the company and, if there are or were any such rights and restrictions, the date that each resolution altering those rights and restrictions was passed (s. 11(h)); and
- whether the articles impose any restrictions on the ability of the company to allot or issue shares (s. 11(i)).

The notice of articles must be in the prescribed form (s. 11(a)). The notice of articles forms part of the Incorporation Application (Form 1 to the Regulation).

Section 53 of the Act sets out the requirements for describing the authorized share structure in the notice of articles. These requirements include a description of the name of each class or series and the kind of shares of which that class or series consists, the maximum number of shares of each class or series that the company is authorized to issue (or state that there is no maximum number), set out the par value of the shares (if applicable) and identify shares without par value as being shares of that kind.

### [§3.04] Articles

The company articles set out the rules for the company’s conduct (s. 12(1)(a)). The articles of a British Columbia corporation remain and are held in the records office, not filed with the registrar.

The articles must be mechanically or electronically reproduced (s. 12(1)(b)), must be divided into consecutively numbered or lettered paragraphs (s. 12(1)(c)) and must be signed by each incorporator (s. 12(3)).

Section 12(2) of the *Business Corporations Act* sets out the minimum requirements for the articles of a company. These requirements include rules for conduct of a company, every restriction, if any, on the business that may be carried on or the powers that may be exercised by the company; the special rights and restrictions that are attached to each class or series of shares of the company, and the name and incorporation number of the company. If the company intends to use any translation of its name outside Canada, then that translation must also be included in the articles (s. 12(2)(c)(iii)).

The *Business Corporations Act* provides for a standard form set of articles (see Regulation, Table 1) that may be adopted by a company in whole or in part (s. 12(4)). The Table 1 articles, unaltered, will rarely “fit” a particular company. Moreover, unless the articles otherwise provide, if a company adopts Table 1 as its articles, then any subsequent amendment to Table 1 will result in an amendment to the company’s articles without the need for the company to pass a resolution to make that amendment (s. 261(2)). Therefore, if a company wants to retain control over the contents of its articles, it should include a provision stating that no subsequent amendment to Table 1 will amend the company’s articles until that amendment has been approved by the company in accordance with the procedure set out in the articles.
When drafting its articles, a company should consider how it will define its fundamental structure. For example, the Business Corporations Act contemplates that the conventional structure will be for the directors to have the power to manage or supervise the management of the affairs and business of the company (s. 136(1)). However, s. 137 makes it clear that the articles may place restrictions on this conventional structure by transferring some or all of this director power to one or more other persons. In most cases the power would be transferred to one or more shareholders. If the articles transfer some or all of that authority to another person, then the directors are relieved of their rights, powers, duties and liabilities to the same extent (s. 137(2)(b)). There is no reason not to include in “custom drafted” forms of articles the types of provisions that are commonly found in a shareholders’ agreement.

Particular provisions often included in articles are the following:

- authorizing a change in the number of directors
- designating what is special business at a general meeting;
- setting a quorum for director and shareholder meetings;
- prohibiting the chair from casting a vote in the event of a tie;
- designating persons “entitled to vote” at shareholder meetings;
- designating a time for deposit of proxy;
- designating a form of proxy;
- restricting powers of directors;
- designating the number of directors;
- allowing directors to resign when annual consent resolutions are prepared;
- setting the procedure for casting votes at directors’ meetings;
- authorizing the appointment of additional directors (s. 122);
- authorizing the appointment of alternate directors;
- designating the method for determining price or consideration for shares without par value (s. 63(1)) (this is mandatory);
- granting the power to pay commissions and discounts (s. 67(1));
- authorizing the removal of directors (ss. 128(3)(b) and 128(4));
- designating the officers (s. 141(1));
- setting procedures for directors’ meetings e.g. notices of directors’ meetings and for meetings by telephone or other media;
- stating that shares need not be redeemed pro rata;
- placing restrictions on when and to whom shares may be issued, including any pre-emptive rights (s. 62);
- setting special rights and restrictions for classes of shares (s. 11(g) and 53);
- placing restrictions on the transfer of shares;
- granting authority for the company to purchase its own shares (s. 77(b));
- allowing an interested director can be counted in the quorum (s. 149(4));
- specifying the type of resolution required to increase authorized capital, if other than a special resolution (s. 54(3)(c)); and
- setting the special majority required to pass a special resolution (s. 1(1)).

When using the Table 1 articles, the solicitor should carefully review the Table 1 provisions on the above topics to ensure that they are suitable for the needs of the particular company.

[§3.05] Incorporation

To effect the incorporation of a company, the incorporation application must be filed with the office of the registrar (s. 10(1)(b)). The incorporation application must be submitted for filing electronically using the Corporate Online system.

Upon submission to the registrar and payment of the prescribed fees, the company will be incorporated on the date and time that its incorporation application is filed with the registrar or on such later date as may be specified in the incorporation application (s. 13(2)). The incorporation date is the first date that the company is recognized under the Act (s. 3(1)(a)).

The registrar must then issue a certificate of incorporation and must record in it the name and incorporation number of the company and the date and time of its incorporation (s. 13(2)). The registrar will then provide the company with the certificate of incorporation and a certified copy (if asked) of the incorporation application and the notice of articles (s. 13(3)(a)). The registrar will also provide a certified copy (if asked) of the incorporation application to the completing party (s. 13(3)(b)).

Once incorporation is effected, the notice of articles and the articles are considered binding contracts among the shareholders and the company (s. 19(1)).
Post-Registration Procedures

The completing party must deliver or mail by registered mail to the records office the originally signed articles and the incorporation agreement (s. 15(1)(b)).

Once a company is registered, it must be organized so as to carry on business. Post-incorporation, the company will do the following: acknowledge incorporation and the certificate of incorporation, the notice of articles and the articles; approve a seal (if any); approve the issue of a share certificate for the share(s) taken by each incorporator and confirm the number of directors and the appointment of the directors listed in the notice of articles.

1. Initial Proceedings of Incorporators

The incorporators are the first shareholders of the company (s. 17). Consequently, they typically complete the rudimentary aspects of organizing the business. The first act of the incorporators is to allot and then issue the share(s) that the incorporators subscribed to by signing the incorporation agreement. An incorporator’s (and other) shares must be paid in full before they are issued (s. 64(2)). The incorporators will also confirm the appointment of the directors listed in the notice of articles as the first directors of the company.

2. Initial Proceedings of Directors

The first directors of the company are the individuals designated as directors of the company in its notice of articles when it is recognized under the Act (s. 1(1)).

The usual purposes of the initial meeting (or written consent resolutions) of the first directors are to approve the allotment and issue of additional shares and the issue of share certificates (if not already issued by the incorporators because of directors’ conflicts) and, if applicable, to approve the transfer of incorporators’ shares and the issue of share certificates. The directors at this stage also appoint officers, fix a quorum for directors’ meetings, determine a fiscal year end, and confirm the location for the records office and registered office as set out in the notice of articles. The directors may also pass other resolutions relating to maintaining corporate records, appointing bankers, and appointing auditors (if any) (ss. 203 and 204).

Other important documents that must be considered at this stage are subscriptions for share allotments; the creation of a central securities register (s. 111(1)); an index of shareholders, if applicable (s. 112); a register of directors (for offices held); the minutes of the directors’ meeting; and the cancellation and issuance of share certificates.

Often, the chief and the council of a Band are the shareholders and directors of the company, if the Band owns the company. A trust declaration document is used to

(a) maintain band council control over the company;
(b) evidence that the shares are issued in trust for the sole and beneficial use and ownership of the Band as represented by band council;
(c) require shareholder decisions be authorized by a band council resolution; and
(d) revoke trust and transfer shares upon certain events (for example, cessation from office).

Some chiefs and band councils are appointed as directors as a matter of course following their election, because changes to directors typically coincide with Band elections. Once a person consents to act as a director, that person must carry out their duties and responsibilities even if they are nominee directors appointed by band council.

Occasionally, Bands or Bands and resource companies enter into joint ventures. The principles relating to Band control of their interest in and shareholding of a joint venture are the same: a joint venture will be structured in a way that the band council can appoint a shareholder(s) and director(s) as provided for in a joint venture agreement.

3. Initial Proceedings of Shareholders

A company may, by ordinary resolution of its shareholders, impose restrictions regarding the times during which a person (other than a current director) may inspect the company’s records. However, those restrictions must permit inspection of those records during the times set out in the regulations (s. 46(8)). Section 13 of the Regulation requires that a company’s records be available for inspection for a period of at least two consecutive business hours per day within statutory business hours (9:00 a.m. to 4:00 p.m., Monday to Friday, excluding statutory holidays observed in British Columbia). This resolution can either be passed at a meeting or consented to in writing.

If there are to be no auditors, a written waiver of their appointment from the holders of all the issued shares is required (s. 203(2)).

Finally, the corporate records must include the minutes of the meeting of the shareholders as described above, or the consent resolutions in lieu of that meeting signed by all shareholders (as permitted by s. 180).
Chapter 4

Share Capital

For further discussion of this subject please see the British Columbia Company Law Practice Manual (Vancouver: CLEBC), Chapter 5.

All legislative sections cited in this chapter and all references to the “Act” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended unless otherwise stated. All references to the “Regulation” are to the Business Corporations Regulation (B.C. Reg. 65/2004), as amended.

§4.01 Introduction

Lawyers working in company law deal daily with company shares, often without considering the large and complex body of law that has made shares such a useful vehicle for commerce and investment. Unlike a partnership, a company is a separate legal entity distinct from its shareholders. But what exactly is a share? What rights does a person have, either against the separate legal entity in which the person is a shareholder, or against the other shareholders of the company?

A share represents a contractual relationship between the shareholders and the company on the terms set out in the articles and notice of articles. A share represents a proportionate interest in the net value of a company (that is, the value that would remain after all the company's liabilities to outside creditors were fully paid). In addition, a share carries with it a bundle of contractual rights emanating from the provisions of the articles and notice of articles of the company (or letters patent or, in the case of a CBCA corporation, articles of incorporation); in addition to the statutory rights provided in the relevant incorporation statutes. When we say certain rights are contractual, it follows that the shareholder may sue the corporation, or any other person who breaches these rights, for breach of contract. It is therefore important to understand the meaning of the various special rights and restrictions that are often attached or removed from share rights.

This chapter reviews some of the typical share rights and what meanings the courts have given them when faced with intra-shareholder disputes, disputes between shareholders and their corporations, or disputes between different classes of shareholders. The chapter also considers the impact of the incorporating statutes such as the Business Corporations Act, S.B.C. 2002, c. 57, as amended, and the Canada Business Corporations Act, R.S.C. 1985, c. C-44 on these rights and restrictions.

§4.02 Kinds and Classes of Shares

The authorized share structure is a bank of shares: it is the maximum number of shares the company may issue and which it has available for distribution. The number of shares in each class may be a specific maximum, or may be specified to be unlimited. Share capital can be subdivided into many types of shares so that special share rights can be allocated to particular shareholders. Each class of shares, however, must consist of shares of the same kind (s. 52(2)). The authorized share structure of a company must be described in the company’s notice of articles (s. 11(g)), which details the name of each class or series of shares, the maximum number of shares of each class or series that the company is authorized to issue (or include a statement that there is no maximum number) (s. 53). In addition, the notice of articles must indicate whether the shares have any par value (s. 53(c)) and whether there are any special rights and restrictions attached to them (s. 11(h)) (but not what the special rights or restrictions are—see §4.04).

A company must have at least one class of shares and those shares must be either “with par value” or “without par value”. If a company has more than one class of shares, some classes can have shares with par value and others can have shares without par value (s. 52(1)). The minimum price for which par value shares may be allotted is their par value. The par value need not be expressed in Canadian currency (s. 52(3)). Unlike the Business Corporations Act, the CBCA does not allow the issuance of par value shares (CBCA s. 24(1)). Shares without par value (or “non par value shares”) may, in theory, be issued for any price or consideration (the “issue price”) that is properly determined at the time of issue (see Practice Material: Company, §6.02.7 as to who has authority to make the determination). Section 64(2) dictates that no share can be issued until it is fully paid, however, s. 65 contains certain exceptions where shares will be deemed to be fully paid.

There is a distinction between “common” shares (or ordinary shares) and “shares with special rights or restrictions” (often called “preference shares” or “preferred shares”). The expressions “preference shares” and “preferred shares” are not formally used in the Business Corporations Act and there is no requirement

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1 Kathleen Keilty, of Blake Cassels & Graydon LLP, kindly revised and updated this chapter in July 2011 and January 2009. Brock H. Smith of Clark Wilson LLP, Vancouver kindly reviewed and revised this chapter in January 2004, updated it in December 2004 and reviewed it again in December 2005. The chapter was based on an article prepared by Mary V. Newbury for the CLE publication, Company Law for Legal Assistants (November 1987); reviewed and revised in January 1996 by Jennifer A. McCarron, Bull, Housser & Tupper, Vancouver.
that they be used. The common or ordinary shares can themselves be in various classes. If they are non-voting, they should be designated as such.

The “special rights and restrictions” that attach to different classes of shares, may include provisions such as whether shares of a particular class hold a preference over those of other classes regarding payment of dividends; whether the dividends are participating; whether dividends are cumulative or non-cumulative; and whether they are redeemable at the option of the company or holder (in the latter event, they are called “retractable”). Further provisions include whether the shares of a particular class are convertible to other shares (s. 76); whether they are voting, voting only in some circumstances, or non-voting (s. 173); and whether they are entitled to preferred status on a winding-up of the company. The same special rights and restrictions can be attached to shares of more than one class or series (s. 58(4)).

**(§4.03) All Shares are Created Equal, or are They?**

If no special rights or restrictions attach to different classes of shares of a company, the shares are presumed to be equal in all respects, no matter what they are called. For example, in *Birch v. Cropper* (1889), 14 App. Cas. 525 (H.L.), the holders of “preference shares” had been given priority in the corporation’s articles for the payment of dividends while the corporation was a going concern. The articles were silent, however, as to how the preference and common shareholders were to share in the distribution of the capital of the corporation upon a winding-up. The House of Lords held that, unless otherwise stated, the preference and common shares ranked equally on a winding-up. Indeed, the preference shareholders were entitled not only to the return of their paid-in capital, but also to share rateably with the common shareholders in respect of the capital surplus of the company. As a result of this “exclusionary” principle in *Birch v. Cropper*, many judgments interpreting special rights and restrictions under the *Company Act* began by asking whether or not the rights claimed by shareholders, and to which they would be entitled if the articles and memorandum were silent, have been sufficiently negatived by the wording used in the articles or memorandum of the company.

The courts, when interpreting share rights, also seem to have adopted a presumption that once a special entitlement has been established in the memorandum or articles, it is *prima facie* exhaustive of that particular type of right (*Will v. United Lankat Plantations*, [1914] A.C. 11 (H.L.)). For example, if a class of preferred shares is established having rights to the prior payment of a dividend of 12% of the amount paid up on the share, that is taken to be an exhaustive statement of the dividend entitlement of the class, so that the holders of those shares are limited to 12% and do not participate further in the profits of the company. However, this principle (which minimizes the operation of *Birch v. Cropper*) is not clear in its scope or application, and may not apply in Canada with respect to rights to share in capital assets on a winding-up of a corporation. It is prudent to ensure that ambiguity does not arise by stating clearly in the articles whether or not a preferred share is intended to be participating in surplus assets.

**(§4.04) Special Rights**

Only the applicable statute and the drafter’s imagination limit the variety of special rights or restrictions that may be attached to shares. For example, the holders of a particular class of shares of a family company may be entitled under the company’s articles to the exclusive use of certain recreational property owned by the company.

Section 58 of the *Business Corporations Act* provides that the special rights and restrictions attached to a share are the special rights and restrictions set out for that share in the company’s articles, and as a result such rights and restrictions are entrenched in the company’s charter. Rights and restrictions attached to shares can also be agreed to outside the articles by way of voting trusts or shareholders’ agreements, but those rights and restrictions will not have the same power to override the default provisions of the *Business Corporations Act*. Refer to §4.05 for an example of the override power regarding voting rights in s. 173 of the *Business Corporations Act*. See also s. 12(2)(b) of the *Business Corporations Act*, which requires all special rights and restrictions to be set out in the articles.

The kinds of rights and restrictions attached to one or more specific classes of shares commonly relate to the following:

- voting rights at general meetings of the company;
- rights to participate in the profits of the company while it is a going concern by way of dividends;
- rights to participate in the capital assets of the company on a winding-up;
- priorities or preferences with respect to income and capital participation;
- pre-emptive rights on the allotment of shares;
- rights of redemption and/or retraction; and
- rights of conversion.

The rights and restrictions dealt with in shareholders’ agreements and voting trusts are typically more specific to the persons who are parties to the shareholders agreement or trust, than corresponding provisions in the articles. In addition to the rights and restrictions mentioned above, shareholders’ agreements and voting trusts usually also settle other specific governance
matters. See further discussion of shareholders’ agreements in Chapter 18.

[§4.05] Voting Rights

Section 173 of the Business Corporations Act codifies the common law principle that unless the charter documents state otherwise, there is a presumption of equality among shares. Normally all shares will be entitled to vote at general meetings of the company and to cast one vote per share, subject to the articles providing otherwise. Depending on the terms of the articles of a company, shares may be voting or non-voting in all circumstances, or they may be voting only in some circumstances. Based on the “exclusionary principle”, it seems likely that once a share is stated to be voting in some circumstances, those are the only circumstances in which it may be voted. However, it is prudent to not take the chance of this question arising and to state clearly that those are the only circumstances in which the shares may be voted. It is also worth noting that in British Columbia non-voting shares may be called “common” even though the concept of a common share might in the past have been taken to suggest full voting rights.

Even shares that are non-voting at general meetings are entitled to be voted at separate meetings of shareholders of the particular class of shareholders, if and when the applicable statute requires. For example, where a company proposes to amalgamate with another and the company has more than one class of shares, the amalgamation agreement must be approved either by a unanimous resolution of all shareholders (whether or not their shares otherwise carry the right to vote) or by a “special separate resolution” (s. 1(1)) of each class or series.

[§4.06] Participation as to Income

The right to share or participate by way of dividend in the income of a company while it is ongoing attaches automatically to a share unless this right is otherwise excluded. Dividend rights may be excluded totally or limited to a fixed return, as is the case with many preference shares. Once a dividend has been so limited, its fixed entitlement is exhaustive unless specific wording is used to permit further participation. In recent times, a variation on the fixed rate of return for preference shares, has been to require that the fixed return be adjusted in accordance with the cost of living.

However, even a preferred shareholder who is entitled to a fixed rate of dividend cannot, unless very clear language is used, force a dividend payment in the absence of a declaration of the dividend by the board of directors of the corporation (Burland v. Earle, [1902] A.C. 83 (H.L.)). In addition, directors may not declare dividends if the payment would render the company insolvent, or if the company is already insolvent, since the outside creditors must always be paid in full first. This rule is codified in s. 70(2). Directors who vote or consent to a resolution declaring a dividend in such circumstances are exposed to civil liability (s. 154(1)(c)).

[§4.07] Cumulative and Non-cumulative Dividends

Generally, dividends may be declared only by directors, and are payable out of profits, capital or otherwise, subject to the company’s charter or another enactment (s. 70(1)). A record date may also be fixed in order to determine which shareholders are entitled to receive a dividend (s. 171(a)).

A shareholder’s entitlement to dividends may be either cumulative or non-cumulative. If a dividend is cumulative, the directors must make up for “missed” dividends of previous periods before paying dividends on junior ranking shares. For example, in the case of a 10% preference share on which dividends have not been declared in 2008 and 2009, dividends may not be declared in 2010 on the common shares unless and until 10% dividends for 2008, 2009 and 2010 have been paid on the preference shares.

Dividend share rights are presumed to be cumulative (Webb v. Earle (1875), L.R. 20 Eq. 556). This presumption may be rebutted, however, by any words indicating that a preferential dividend is to be payable only out of the profits of the particular year. There is also doubt as to whether cumulative rights apply once the company has commenced winding up. It is therefore important where non-cumulative dividends are intended that this be stated explicitly in the share rights and restrictions.

[§4.08] Participation as to Capital Surplus

Share rights also often deal with participation in the capital assets of a company at the time it is wound up or dissolved. If the share rights and restrictions are silent on this point, all shareholders share rateably. Canadian and English courts, however, seem to differ on whether, once a preference in respect of capital repayment is stated, it is prima facie exhaustive. Certainly a preference as to dividends does not imply a preference as to capital surplus or vice versa.

The most common limitation on preference shares is that the holders of those shares are entitled only to the return of the amount paid up on such shares. This limitation leaves the common shareholders (who have probably assumed more risk in the enterprise) to reap the rewards of capital appreciation of the company’s net assets.

A company can set a record date for the purpose of determining which shareholders are entitled to participate in a return of capital upon a liquidation distribution (s. 171(1)(b)).
[§4.09] Pre-emptive Rights
At common law, a shareholder was not entitled to require that he or she be given a first opportunity to subscribe for any subsequent share issue by the company. In some cases, this meant that a dissident shareholder’s position could be “watered down” by the directors through the issuance of sufficient new shares to “drown out” the dissident.

Under s. 41 of the Company Act, this situation was remedied. If the company was a non-reporting company, then the directors were required to offer the shares pro rata to the existing members before allotting new shares for issuance. This requirement extends to pre-existing companies that have not removed the application of the Pre-existing Company Provisions. However, companies incorporated under or transitioned under the Business Corporations Act or companies that have amended their articles to remove the pre-existing company provisions will not be subject to a statutory pre-emptive right on share allotments, but may provide that right in the articles or a shareholders’ agreement (ss. 62 and 442.1).

Likewise, there is no statutory pre-emptive right for share transfers. For this reason, shareholder agreements for many private companies provide for a pre-emptive right, which is exercisable at the time of any share transfer by the other existing shareholders of the company or of the particular class. Basically, this right gives shareholders a right of first refusal to acquire any shares that another shareholder proposes to transfer. The thornier question relates to the circumstances in which the directors of a company may create a new class of shares ranking senior or at an equal rate to existing classes: that issue is discussed later.

[§4.10] Redemption and Retraction
Rights of redemption (entitling a company to require that a shareholder sell his or her shares for a pre-agreed amount) or retraction (entitling a shareholder to require the company to redeem his or her shares), or both, may be attached to shares. The pre-agreed redemption or retraction price of a share usually is not less than the shareholder's original capital investment, but may go much higher. Indeed, preference shares that are redeemable or retractable for a higher amount than their par value are often used for income tax advantages, especially in connection with s. 85 (Income Tax Act) rollovers.

A redemption may not be carried out if the company is insolvent or if it would render the company insolvent (ss. 77(a) and 79). Redemptions are also subject to any restrictions contained in a company’s articles (s. 77(a)).

Under the Company Act, redemptions had to be carried out rateably, or pro rata, among every shareholder of the subject class, unless its charter documents otherwise provided. In other words, if the board of directors resolved to redeem 50% of the issued and outstanding preference shares of the pre-existing company, 50% of the shares held by each shareholder normally had to be redeemed, so that some shareholders could not be favoured over others. This rateable redemption requirement continues for pre-existing companies that have not removed the application of the Pre-existing Company Provisions.

[§4.11] Repurchase/Convertibility
Where no explicit right of redemption is provided for in the articles, a company at common law is prohibited from acquiring shares in its own capital. However, both the Business Corporations Act and the CBCA reverse this rule and permit companies to repurchase their shares in certain circumstances. Under s. 77(b) of the Business Corporations Act, the company only has authority to purchase its own shares if the articles provide authority to do so. Under the CBCA the reverse is true and a corporation may purchase or otherwise acquire its own shares, unless it is prohibited by its articles (CBCA s. 34). As is the case with redemptions, a repurchase may not be carried out under either statute if the company is insolvent or it would render the company insolvent (s. 78; CBCA s. 34(1)).

As with redemptions, an offer to purchase made by a company under the Company Act had to be made in most circumstances rateably to all shareholders of the subject class. This rateable repurchase requirement continues for pre-existing companies that have not removed the application of the Pre-existing Company Provisions (see Table 3, Part 5 to the Regulation).

Corporations may also issue convertible shares. These are shares that may be converted at the option of the shareholder or the company into other classes of shares.

[§4.12] Variations/Abrogations of Special Rights and Restrictions
The special rights and restrictions set forth in a company’s articles and notice of articles constitute an enforceable contract between a shareholder and the company. What protections exist for a shareholder when a company or its majority shareholders attempt to tamper with those rights? The first issue to be addressed in this kind of situation is whether or not there is actually an attempt to vary or abrogate the special rights or restrictions, or whether the proposed action will affect rights and restrictions only indirectly. In many cases, this question can be answered easily. For example, the preference shareholders as a class are entitled to a dividend of 12% on the amount paid up on their shares, and the company purported to reduce this return to 5%. In this scenario, the preference shareholders could rely not only on the common law but on statutory provisions such as s. 61 of the Business Corporations Act and s. 176 of the CBCA. These
provisions prohibit such interference without the approval of the shareholders of the affected class. Under the CBCA, a 2/3 majority vote is required for this approval to be effective. Under the Business Corporations Act, the shareholders of the affected class must approve of the proposed change by a “separate special resolution” (s. 1(1)), which requires a majority vote of at least 2/3, depending on the provisions in the articles of the company and on whether the company is a pre-existing company. Section 227(2)(b) of the Business Corporations Act provides that if a shareholder believes that some act of the company has been done or that a resolution of the shareholders (or of shareholders of a particular class or series of shares) has been passed or proposed that is unfairly prejudicial, then that shareholder may apply to the court for relief. Under s. 227(3), the court has the discretion to make a number of interim or final orders, including an order varying or setting aside the resolution and an order requiring the company to purchase the shares of that shareholder at a price determined by the court. A similar right is provided for in s. 190 of the CBCA for shareholders who vote against (dissent from) the resolution in question. There also may be additional requirements provided in the special rights and restrictions in a company’s notice of articles or articles, which must be complied with before any variation can be effected.

However, there may be circumstances in which a shareholder feels that his or her rights are being abrogated, but the law takes a different view. In White v. Bristol Aeroplane Co. Ltd., [1953] 1 All E.R. 40, a preference shareholder complained that by authorizing the issuance of new common shares, the company had “affected, modified, dealt with or abrogated” his class rights, since the voting rights exercisable by the preference shareholders would thereafter be “watered down” and therefore be worth less than before. The Chancery Court ruled against the plaintiff shareholder, reasoning that the new share issue did not amount to an abrogation even though it would affect the value of the plaintiff’s shares and therefore his enjoyment of them as a practical matter.

The Business Corporations Act uses words with a broader meaning than those in White—“prejudiced or interfered with” rights. Arguably this broader language might produce a different result if a similar case came before a court in British Columbia. The problem of “affecting” rights is avoided by making an explicit statement in the rights and restrictions to the effect that the company may not issue any class of shares ranking prior to or equal with the existing classes of shares without approval by separate special resolution. There may also be other common law or equitable remedies open to a shareholder in this situation.

For further discussion, see Practice Material: Company, Chapter 9, §9.02.
Chapter 5

Governance

For further discussion of this subject please see the British Columbia Company Law Practice Manual (Vancouver: CLEBC), Chapter 6.

All legislative sections cited in this chapter and all references to the “Act” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended unless otherwise stated. All references to the Regulation (“Reg.”) are to section of the Business Corporations Regulation (B.C. Reg. 65/2004), as amended.

§5.01 Introduction

This chapter deals with how companies are run and the duties and responsibilities of the people who run them.

Federal companies differ in some respects and are not dealt with comprehensively in this chapter; however, comparative provisions of the Canada Business Corporations Act, R.S.C. 1985, c. C-44 (CBCA) are mentioned in some sections.

§5.02 Management of the Company

1. Control of the Corporation

While the articles may grant shareholders of a company, or any other person, extensive authority in connection with the management of the business of the company, the general practice is to entrust a board of directors with the exclusive power to manage the company and to grant that power free from interference from the shareholders (derived from s. 136(1)). Usually, the shareholders are left only with the power to change the directors at the annual general meeting or to remove them by special resolution (s. 128(3)(a)), or some other method or resolution as specified in the articles (s. 128(3)(b)).

2. Directors

(a) Election or appointment of directors

Under the Business Corporations Act, the person or persons designated as directors in the notice of articles are the first directors. After that, the Act and the articles govern elections and appointments (s. 122(1) and see Western Mines Ltd. v. The Shield Development Co. Ltd., [1976] 2 W.W.R. 300 (B.C.S.C.)).

Often the articles provide that the directors retire at each annual general meeting and the incoming directors are elected or appointed at that meeting, although this is not mandatory. Directors may appoint additional directors between annual general meetings, if authorized by the articles, and provided that the number of directors added does not exceed 1/3 of the number of first directors (if any of them are still in their first term), or in any other case, 1/3 of the then current number of directors (s. 122(2) and (3)).

Subject to the articles, the remaining directors may fill a casual vacancy on the board (s. 131(b)) unless the articles provide otherwise (s. 130). Sections 131 to 135 set out the rules for filling vacancies and they apply unless the articles provide otherwise.

To be a valid election or appointment, certain procedures must be followed. First a director must consent or acquiesce at the meeting at which the director is elected or appointed (s. 122(4)). Consent can take the form of

(a) written consent (before or after the appointment)(ss. 122(4) and 123 (1) (a)), or

(b) performing functions of, or realizing benefits that are available to, a director after that person knew or ought to have known of the election, appointment or designation (s. 123 (1) (b)).

The consent lasts until revoked, the director’s term ends and that director is not immediately re-appointed, or the director resigns or is removed (s. 123(3)).

The shareholders of private companies may elect directors by a resolution in writing instead of by actually holding a meeting.

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1 Based on an article prepared by Geoffrey Bird for the CLE publication, Company Law (November 1987). Reviewed and revised in March 1994 with the assistance of Harris S. Wineberg, Ladner Downs, Vancouver. Geoffrey Bird of Aydin Bird, Vancouver reviewed and revised this chapter annually from February 1995 to January 2006. Jason Harris kindly reviewed this chapter in November 2011.
A company must file a notice of change of directors with the registrar within 15 days of the change in its directors or the address of a director (s. 127(1)). This will change the company’s notice of articles (s. 127(2) and (3)).

(b) Number

Private companies must have at least one director and public companies must have at least three directors (s. 120).

Commonly, the articles give the shareholders the power to change or fix the number of directors. Always review the company’s articles for the proper procedures and authorities.

(c) Residency requirements

There are no residency or citizenship requirements for directors under the Business Corporations Act (unlike under the former Company Act).

(d) Qualification of directors

Under s. 124(2), those who are not qualified to become or act as directors include: people under the age of 18; people found to be incapable of managing their own affairs; undischarged bankrupts; and people who have been convicted of an offence in the past five years concerning the promotion, formation or management of a corporation or unincorporated business, or an offence involving fraud.

If a director ceases to meet the qualifications of s. 124 or articles of the company, the director does not automatically cease to hold office but is required to resign immediately (s. 124(3)).

(e) Improper election or appointment

Every act of a director will not be invalid merely because of a defect or irregularity that may later be discovered in his or her appointment, election or qualification (s. 143). Be aware that the language of s. 143 may not be as broad as it seems.

(f) Term of office

The articles govern the length of a director’s term of office and typically provide that the term will extend only to the next annual general meeting (s. 128(1)(a)).

(g) Resignation

The resignation of a director must be in writing and delivered to the company or a lawyer for the company. It is only effective at the time the resignation is received, or at the time, date or event specified in the resignation, if that time is later (s. 128(2)). The resignation no longer needs to be received at the company’s registered office as was required under the former Company Act.

(h) Removal

Directors generally retire at each annual general meeting and if others are elected in their place, the term of the retiring directors ceases (if the articles so provide). Otherwise, a director may only be removed as specified in the articles, or by special resolution of the shareholders (s. 128(3)).

If the holders of a class or series of shares have the exclusive right to elect or appoint one or more directors, then only those shareholders may remove those directors (s. 128(4)).

(i) Alternate Directors

Although it is common to appoint alternate directors in British Columbia (and most standard form articles provide a procedure for doing so), there still is no statutory authority for this practice. Section 137 of the Business Corporations Act (which authorizes the transfer of powers of a director to another person if authorized by the articles), seems to contemplate the complete transfer of authority away from the directors, which is not normally what a director intends to have happen when the director appoints an alternate. Section 137 does provide that an alternate director would be subject to the same duties, liabilities and protections as any director of the company, to the extent that the alternate exercised the functions of a director, unless the functions were exercised only under the direction and control of another director, shareholder or senior officer.

Provisions in articles permitting the appointment of alternate directors vary; some provide that the alternate director can only attend directors’ meetings in the place of his or her appointer, while others purport to appoint alternate directors for all purposes. An example is a provision permitting alternate directors to sign directors’ written resolutions in the place of their appointers, although some practitioners have serious doubts about how valid this practice is.
(j) Register of Directors

A company must maintain a register of its directors (s. 126). This register must contain the full names and prescribed addresses of the directors, the date on which each director was elected or appointed, and the date on which each former director became a director and ceased to hold office as a director.

A director may avoid disclosing his or her home address if the director also has an office address where the director usually can be served.

The “prescribed address” for a director or officer is the delivery address of the office the director normally occupies during business hours (including, if different, its mailing address) or the address of their residence (Regulation, s. 2(2)).

3. The Powers of Directors

Section 136(1) of the *Business Corporations Act* states that:

The directors of a company must, subject to this Act, the regulations and the memorandum and articles of the company, manage or supervise the management of the business and affairs of the company.

When a person who is not a director (except those mentioned in s. 138(2)) performs the functions of a director, certain liabilities and obligations of directors will apply to that person (s. 138(1)).

No limitation or restriction on the powers or functions of the directors is effective against a person who does not have knowledge of these limitations or restrictions (s. 136(2)).

The standard form articles of British Columbia companies normally contain provisions similar to the Act.

In practice, the directors provide for the establishment of sound business policies of the company and it is the officers of the company (appointed by the directors) who actually carry out those business policies on a daily basis. Because there is an active duty imposed on directors to manage the company, no distinction may be drawn between active and passive (or nominee) directors and their exposure to liability.

When the appropriate provisions are placed in the company’s articles, the directors may transfer their powers to manage or supervise the management of the business, in whole or part, to others (who need not be shareholders or directors) (s. 137(1)). Consequently, some or all of the shareholders of a company (or other persons) can act as directors of the company if the shareholders want them to. To transfer powers effectively, the articles must clearly indicate (by referring to s. 137 or otherwise) the intention that such powers be transferred (s. 137(1.1)(b)).

When the powers are transferred, the persons to whom these powers are transferred are subject to the same duties and liabilities as any director who exercises these powers (s. 137(2)(a)). And the “regular” directors are relieved from liabilities to the extent that other parties exercise these powers (s. 137(2)(b)). See also *Practice Material: Company*, §18.02.4.

Section 146(1) of the *CBCA* provides similarly. If all the shareholders (or all of the shareholders and a third person) enter into a unanimous shareholder agreement, they may restrict in whole or in part the powers of the directors to manage, or supervise the management of the business and affairs of the corporation, as long as it is otherwise a lawful agreement (s. 146(1)). The shareholders who are party to a unanimous shareholder agreement are subject to the same duties and liabilities as any director who exercises these powers. Like under the *Business Corporations Act*, the “regular” directors of the company are relieved from their duties and liabilities to the extent that other parties exercise powers under the unanimous shareholder agreement.

When a receiver-manager is appointed for a company, the powers of the directors and the officers cease to the extent of the appointment and during the period of appointment (s. 105). The powers and duties of the directors and officers continue with respect to other corporate matters and assets not covered by the appointment of the receiver-manager. If the company is still viable after the receiver-manager has completed his or her job, the powers of the directors and officers then resume. If a liquidator is appointed, the powers of the directors and officers cease, except in so far as the liquidator allows them to continue (s. 334(1)(a)).

4. Officers

The term “officer” is not defined in the *Business Corporations Act*, although “senior officer” is defined in s. 1(1).

A company doesn’t need to have any particular officers, nor is any office with the company required to be filled by a director, unless the articles provide otherwise (ss. 141(1) and (2)).
The qualification criteria for officers are the same as those for directors under s. 124 (s. 141(3)). However, it is an offence for an unqualified person to act as an officer of a company (s. 426(4)). The election and appointment of officers is within the power of the directors, unless the articles specify otherwise (s. 141(1)). Even though there may be an irregularity or a defect in the election or appointment of an officer, his or her acts may still be valid (s. 143). If an officer is removed from office without cause, his or her contractual rights as an employee, if any, still survive, but the appointment as an officer does not of itself create any contractual rights (s. 141(5)).

Only “senior” officers must disclose possible conflicts of interest arising from offices or property held (ss. 147 to 153). The same rules for indemnification and insurance that apply to directors also apply to officers (ss. 159 to 160).

The duties of the officers are directed by the articles and by the directors. Officers must also comply with the Business Corporations Act, the articles (s. 142(1)(c) and (d)). Sections 142(1)(a) and (b) impose a duty on an officer to act honestly, in good faith and in the best interests of the company, as well as a duty of care equivalent to a reasonable person standard.

5. Insiders

“Insider” in respect of a “private company” means (s. 192(1)):

(a) a director or senior officer of the private company,

(b) a person who beneficially owns shares of the private company that carry, in aggregate, more than the prescribed fraction of the votes [currently set at 1/10th (Reg. s. 19)], that may be cast in an election or appointment of directors at a general meeting,

(c) an associate of a person referred to in paragraph (a) or (b),

(d) the private company itself,

(e) an affiliate of the private company,

(f) a person who is employed by the private company or who is retained by it on a professional or consulting basis, or

(g) a director or senior officer of another corporation if that other corporation is itself an insider of the private company.

Every insider of a private company is liable if he or she uses specific confidential information in any transaction relating to any security of the private company (which term includes more than just shares of a company, if it is for the benefit or advantage of the insider or any associate or affiliate of the insider and if such information, if generally known, might reasonably be expected to materially affect the value of the security (s. 192(2)). The insider may be required to compensate any person who suffers a direct loss as a result of the insider’s forbidden conduct, and may also be accountable to the corporation (s. 192(3)).

When insiders and others who are in a “special relationship” to the corporation misuse confidential information, the Securities Act may also impose significant liabilities and penalties on them.

6. Residual Powers of Shareholders

Although for the most part the directors have the exclusive right to manage the business of the company, the shareholders are permitted a role in corporate governance in some areas:

(a) Pre-emptive rights on allotment of shares

Section 41 of the former Company Act granted mandatory pre-emptive rights to existing shareholders of non-reporting companies for later allotments of shares. Each of the existing shareholders of a particular class had a right of first refusal to maintain his or her rateable interest in the company. These rights of first refusal continue to apply under the Business Corporations Act to companies that are subject to the Pre-existing Company Provisions, (Table 3, Part 3 to the Regulation), although the shareholders of a pre-existing company may remove them by altering its notice of articles by special resolution (Business Corporations Reg. s. 45)

In the case of companies incorporated under the Business Corporations Act, such pre-emptive rights are not mandatory. They apply only if they are provided for in the company’s articles.

(b) Disposition of the company’s undertaking

Section 301(1) of the Business Corporations Act provides that a company must not sell, lease or otherwise dispose of all or substantially all of its undertaking unless

- it has been authorized to do so by special resolution, or
- the sale is in the ordinary course of its business.
The ordinary course of business exception would apply when a company, in the course of carrying on its business, sells most of its assets all at once (such as an apartment building or a large machine) but is replacing it with similar asset and continuing the business. This prohibition does not apply to a disposition of the undertaking by way of security, or by a short-term (less than three years) lease, or to parent, subsidiary or sister corporations (in the wholly owned context), or to the sole shareholder of the company (s. 301(6)).

Although it appears directors of a company can avoid the effect of s. 301 by first transferring the undertaking to a wholly owned subsidiary of the company with the intent that the wholly owned subsidiary would then transfer it to a third party, such action may well expose the directors who participated in such a scheme to liability for breach of their duty of good faith. There also is a risk that a court may determine that the “undertaking” of a parent company includes the assets of a subsidiary.

Case law indicates that the meaning of the words “all or substantially all of its undertaking” must be interpreted in a qualitative (how important) as well as a quantitative (what proportion) manner. In particular, a court will examine whether the disposition in question was an unusual transaction or one made in the regular course of business (Lindzon v. International Sterling Holdings Inc. (1989), 45 B.L.R. 57 (B.C.S.C.)).

When a company asks the shareholders to approve the disposition, a shareholder is then entitled to file a notice of dissent and the company may be required to purchase the dissenter’s shares (s. 301(5)).

Section 301(5) provides that any shareholder of a company may send (see s. 7) a notice of dissent to the company in respect of a special resolution to approve or ratify a disposition of substantially all of the company’s undertaking. If a shareholder does, Division 2 of Part 8 (ss. 237 to 247) applies, meaning that the shareholder can have the shares that are the subject of the notice of dissent purchased by the company at their fair value.

If a shareholder intends to dissent, the shareholder should not vote the subject shares in favour of the resolution approving the disposition or sign any consent resolution in writing approving the disposition.

When the special resolution is to approve a proposed disposition, the company should observe the timing requirements in Division 2 of Part 8. The company should ensure that it complies with ss. 240(1) and (2) regarding the sending of material advising all shareholders (voting and non-voting) of their dissent rights (whether or not there is an actual meeting), as the company may not want to continue with the disposition if there are too many dissents.

7. Directors’ Meetings

In order to act, the directors must act together as a board. This does not mean that the directors must always hold a formal meeting, although they cannot be too casual about it either.

A resolution of the directors may be passed without a meeting if each of the directors “entitled to vote on the resolution” consents to the resolution in writing, or in any other way permitted under the Act or by the company’s articles (s. 140(3)). A director who is not entitled to vote on a particular resolution (for example, due to a conflict) does not need to sign the resolution for it to be valid.

A single director may constitute a meeting, but only if the company has one director (s. 140(4)).

Unless the articles specifically forbid it, directors can hold a meeting by telephone or by any other device that allows the participants to communicate with each other at the same time (s. 140(1)(b)).

It is quite proper for a quorum of directors of a company to meet and settle the principles of the subject upon which they are making a decision and to prepare the formal minutes later. However, the courts in British Columbia (more so than elsewhere in Canada) require certain formalities to be observed. In Re Associated Color Laboratories Ltd. (1970), 12 D.L.R. (3d) 338 at 351 (B.C.S.C.), the court approved the statement of F.W. Wegenast in The Law of Canadian Companies (1931) at page 215 in which he said:

...So long as those in attendance are satisfied, the formalities may be reduced to a minimum. The only essentials are that the proper persons should be in attendance and that the minutes should represent their intention.

There must be a real meeting at which a quorum is present. A meeting cannot be held by polling the directors one by one unless the articles specifically permit this as a way of holding directors’ meetings (s. 140(3)(a)(ii)).
All directors must receive prior notice of the meeting unless they are all present at the meeting. The period of notice need only be what is reasonable in the circumstances, it may be given verbally, and it need not specify the nature of the business to be transacted, unless the articles provide otherwise. It is proper to hold a meeting and later obtain a waiver of notice of that meeting from any directors who did not receive due notice. If a director then refused to give his or her waiver, the meeting would not have been validly held and any resolutions purporting to be passed, of no effect.

As a result of the wording of s. 140(3)(a)(i), resolutions in writing are only effective on the date the last director signs. Even though directors may properly ratify and confirm prior actions and therefore validate them, a resolution of the directors (whether in writing or passed at a meeting) speaks only from the date it is actually passed. Take, for example, the declaration of a dividend. One cannot really say that for the purposes of the Income Tax Act a dividend was declared last December 31 if all of the action relating to it took place the following June when the company’s tax return was being prepared. However, if it could be said that the directors at least considered the matter on December 31 at a “meeting” where a quorum was present and if all directors are prepared to waive notice of the meeting, then it would be proper to prepare minutes of that meeting to reflect the actions that actually took place on December 31.

[§5.03] Duties and Liabilities of Directors and Officers

1. What are the Duties?

The statutory duties of directors and officers are outlined in s. 142 of the Business Corporations Act. Every director and officer must (s. 142(1))

(a) act honestly and in good faith with a view to the best interests of the company,

(b) must exercise the care, diligence and skill that a reasonably prudent individual would exercise in comparable circumstances,

(c) act in accordance with the Act and the regulations, and

(d) subject to paragraphs (a) to (c), act in accordance with the memorandum and articles of the company.

(a) Honesty

This duty includes being truthful, open and above-board with fellow directors. In particular, it prohibits any secret profits or any non-approved conflict of interest.

(b) Good faith and in the best interests of the company

This duty could more broadly be called the duty of loyalty or the fiduciary duty. The director must exercise his or her powers in the best interests of the company as a whole and not for any improper or collateral purpose, especially one that involves the director personally. The Supreme Court of Canada commented on the fiduciary duty in Peoples Department Stores Inc. (Trustee of) v. Wise, 2004 SCC 68. For a full discussion of fiduciary duty see the People’s case and BCE Inc. v. 1976 Debenture Holders, 2008 SCC 69.

In determining whether or not there has been a breach of this duty, there is no general rule to apply. As Chief Justice Laskin said in Canadian Aero Service Ltd. v. O’Malley, [1974] S.C.R. 592 at 620:

The general standards of loyalty, good faith and avoidance of a conflict of duty and self-interest to which the conduct of a director or senior officer must conform, must be tested in each case by many factors which it would be reckless to attempt to enumerate exhaustively.

And at 607:

An examination of the case law . . . shows the persuasiveness of a strict ethic in this area of the law. In my opinion this ethic disqualifies a director or senior officer from usurping for himself or diverting to another person or company with whom or with which he is associated a maturing business opportunity which his company is actively pursuing.

A director must be especially careful if he or she has been appointed to the board to represent the interest of a third party such as a shareholder or creditor. A director has a fiduciary duty to disclose information to the company if it affects the company in an important way, even if such disclosure would harm the interests of the party who appointed him or her (PWA Corp. v. Gemini Group Automated Distribution System Inc. (1993), 103 D.L.R. (4th) 609 (Ont. C. A.), leave to

(c) Care, diligence and skill of a reasonably prudent person

(i) Care

The duty of care requires prudence based on common sense. A director must act deliberately and cautiously and try to foresee the probable consequences of a proposed course of action.

(ii) Diligence

The duty of diligence is the making of those inquiries that a person of ordinary care in that position or in managing his or her own affairs would make. Some examples of the requisite standard of diligence are as follows:

A. attending meetings

A director does not have to attend all directors’ meetings but should try to do so since he or she may be held liable for prohibited matters that happened while he or she was absent. If a director is not present at a meeting at which certain prohibited matters were approved (that is, carrying on restricted businesses, purchasing, redeeming or acquiring shares or paying dividends when the company is insolvent, paying improper indemnities, authorizing improper commissions or discounts or issuing shares without proper consideration), he or she must formally dissent within seven days of hearing about it or be deemed to have approved (s. 154(7)).

Section 123(3) of the CBCA is broader in that it does not restrict the application of the rule to certain kinds of resolutions. The director of a federal company must dissent with respect to any resolutions with which he or she does not want to be associated.

B. relying on other directors

Subject to the duty of care mentioned earlier, the general rule is that a director is not liable for the misdeeds of his or her co-directors if he or she has not participated in the acts resulting in the damage and is not negligent. However, in some American cases, all of the directors of a company have been held equally liable for misinformation in a prospectus, even though all were not active participants in the misstatements.

C. relying on officers and professionals

In being diligent, a director may rely on the officers of the company, although he or she should still be cautious in accepting information from them and should ensure that the officers and professionals have the requisite expertise and credentials.

Section 157(1) of the Business Corporations Act permits a director (but not an officer) to rely in good faith on

(a) financial statements of the company represented to the director by an officer of the corporation or in a written report of the auditor of the company to fairly reflect the financial condition of the company,

(b) a written report of a lawyer, accountant, engineer, appraiser or other person whose profession lends credibility to a statement made by that person,

(c) a statement of fact represented to the director by an officer of the company to be correct, or

(d) any record, information or representation that the court considers provides reasonable grounds for the actions of the director, whether or not that record was forged, fraudulently made or inaccurate.

The group referred to in s. 157(1)(b) is limited to true “professionals” and does not necessarily include experienced but non-professional officers of the company (see People’s Department Stores Inc. (Trustee of) v. Wise, 2004 SCC 68, at paras. 73-78).
Section 157(2) provides that:

A director of a company is not liable under section 154 if the director did not know and could not reasonably have known that the act done by the director or authorized by the resolution voted for or consented to by the director was contrary to this Act.

Note that s. 157(2) applies only to a director, not to an officer. In practice, it would be difficult for a director to avoid liability by relying on s. 157(2).

A director should, as a minimum, examine the financial statements and review the general business activities of the company with the executive officers. However, a director is not required to go behind the financial statements to examine entries in the company’s books.

The directors must be cognizant of the business as a whole. Directors have been found negligent where the actions by an officer of the company resulted in losses, which could have been detected and prevented by proper supervision.

D. relying on outside experts

Directors are not expected to be experts in all fields and frequently must rely on the advice of specialists. They should obtain outside advice when circumstances require, but they must be reasonably assured that the outsider is truly qualified to give the advice sought. Directors may rely on the advice and opinions of an outside expert if the outsider is independent and appears qualified to give the advice and the directors continue to exercise their own judgement.

(iii) Skill

The inclusion in the statutes of the reference to a “reasonably prudent person” requires an ignorant or inexperienced director to rise to the level of a reasonably prudent person in the circumstances, and holds a director with some special skill and knowledge (such as a lawyer) to the standard of a reasonably prudent person with that special skill and knowledge.

It is probable that in interpreting the meaning of “skill”, no allowance will be made by the courts for any shortcoming such as lack of skill, knowledge or intelligence. In applying this test, the courts will probably also consider such factors as:

- the director’s own qualifications;
- the significance of the action;
- the information available to him or her;
- the time available to make the decision;
- the alternatives that were open at the time;
- whether he or she represents a special interest group; and
- whether he or she is an advisor to the company (lawyer, accountant, engineer, etc.).

2. To Whom Are the Duties Owed?

It has long been a principle of common law that directors owe a fiduciary duty only to the company and not to the creditors or anyone else (Percival v. Wright, [1902] 2 Ch. 421). However, subsequent case law has eroded this position to the extent that now the directors may be held responsible to many different groups.

In addition to the fiduciary duties imposed by the Society Act and the BCA, the council of a Band owe a fiduciary duty to members of the Band: Assu v. Chickite, [1999] 1 C.N.L.R. 14 at para. 23 (B.C.S.C.). Accordingly, members of the band council who sit as directors must act in the best interests of members of the Band when making decisions.

(a) Shareholders

The directors of a company may be liable to the shareholders for remedies sought under the oppression remedy or to the company under the derivative action remedy. The latter actions are commenced in order to right a wrong done to the company. The wrongdoers will normally be the directors and officers whose action has resulted in damage to the company. The directors could also be liable to the company for improper use of corporate assets that exist for the benefit of all shareholders or for favouring one group of shareholders over another in a takeover battle.
In *Redekop v. Robco Construction Ltd.* (1978), 7 B.C.L.R. 268 (S.C.), a director failed to disclose his interest in one of the company’s contracts. It was held that the company could recover the secret profits and a minority shareholder was entitled to an order that his shares be purchased either by the company or by the errant director.

In *Malcolm v. Trustee Holdings Ltd.*, 2001 BCCA 161, the Court affirmed that, other than in exceptional circumstances (such as a family relationship or a special relationship of trust and dependency between the parties), the fiduciary duty of the directors is to the company and not to the individual shareholders.

Essentially, if there has been a “corporate mistake” in the conduct of the business or affairs of the company, any interested person may apply to court, under s. 229 of the *Business Corporations Act* (CBCA, s. 247), for an order to remedy that omission, defect, error or irregularity, and it is the directors and officers of the company who must provide the remedy.

(b) Creditors

Generally, directors owe no fiduciary obligation to creditors (*Western Finance Company Ltd. v. Tasker Enterprises Ltd.*, [1980] 1 W.W.R. 323 (Man. C.A.)). Some courts, however, have lifted the corporate veil in order to benefit creditors who have been the victims of unscrupulous conduct. In such cases directors and officers, as agents of the corporation, could be deprived of their immunity and held liable if their actions are tortious.

Under s. 301(2) of the *Business Corporations Act*, if the appropriate requirements for the disposition of an undertaking of the company are not observed, a creditor may apply to the court to enjoin the proposed disposition or set aside the disposition or make any other order the court considers appropriate.

When funds administered by the company are impressed with trust conditions (even those contractually imposed, such as by an agreement with a creditor that funds received under certain conditions are to be held in trust for the creditor), directors have been held personally liable for participating in the breach of trust by the company when the subject funds were intermingled with those of the company (*Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R 787).

The Supreme Court of Canada clarified the nature of the duty of care owed by directors of a company to its creditors in *People’s Department Stores Inc. (Trustee of) v. Wise*, 2004 SCC 68. The trustee in bankruptcy of People’s Department Stores had claimed that in attempting to remedy the financial difficulties of a parent company and its subsidiary, the directors had favoured the interests of one company over the other to the detriment of the creditors and had, therefore, breached their duty of care to the creditors.

The court held that although the directors of a company do owe a duty of care to a company’s creditors (and other parties), such a duty is in the nature of a negligence standard of care (that is, to exercise the care, diligence and skill of a reasonably prudent individual) and is not comparable to the fiduciary duty that is owed by the directors to the company itself (that is, to act honestly and in good faith with a view to the best interests of the company). The court stated (at paragraph 67) that directors and officers will not be held to be in breach of their duty of care if they act prudently and on a reasonably informed basis. The decisions they make must be reasonable business decisions in light of all the circumstances about which the directors or officers knew or ought to have known. Directors are not expected to be perfect and the courts will not second-guess their decisions, but the court will determine whether the directors in reaching their decision exercised an appropriate degree of prudence and diligence.

(c) Employees

Each of the directors and officers of a company may be liable for up to two months’ wages and salaries of certain employees under s. 96(1) of the British Columbia *Employment Standards Act*. This liability includes unpaid commissions of employees. Despite s. 96(1), directors and officers are not personally liable for vacation pay accruing after the director or officer ceased to hold office, or for severance pay or termination pay payable under the *Employment Standards Act*, if the company is in receivership, or is subject to action under the *Bank Act* (Canada) or to a proceeding under an insolvency act.

Directors and officers may also be liable under occupational health laws for injuries caused to employees by unsafe working conditions. Directors and officers should be especially careful if their company deals in toxic substances.
In one instance, the Ontario Court of Appeal allowed an employee to recover damages from the directors personally for breach of his employment contract by holding them liable for the tort of inducing the breach of the contract by the company (Kepic v. Tecumseh Road Builders, supra).

(d) Government

At least 135 provincial and federal statutes provide for liability of directors and officers in certain circumstances.

Many statutes (including the Criminal Code) provide that if the company has committed an offence under that act, every director and officer who authorized, directed, condoned or participated in the offence is liable to the same penalties as if they had personally committed the offence. Fines for such offences range from $50 to $25,000 with the possibility of up to one year of imprisonment.

Some examples of the statutes follow.

(i) Corporate statutes

Section 427(2) of the Business Corporations Act provides for a fine of up to $10,000 for directors and officers who authorize or condone the making of false or misleading statements.

Under the CBCA, failure to provide information to the Director under the CBCA relating to ownership and control, improper use of shareholder lists, failure to comply with proxy requirements, false reporting, and so on, all give rise to fines and/or imprisonment.

(ii) Securities Act

Directors, officers and employees who participate in insider trading activities by buying and selling securities of their company with knowledge of material facts or changes that have not been generally disclosed to the public are liable to very large fines and long terms of imprisonment. Such people are also liable if they advise other persons of inside information or do not provide full, true and plain disclosure in prospectuses and other disclosure documents.

As of July 2008, there is a statutory right of action against the company and its directors, officers and other “influential persons” by investors who purchased shares in the secondary (public) market and who have suffered damages from misleading information released by the company.

(iii) Criminal Code

A person may become a party to the offence of conspiracy (as opposed to being an actual participant) if he or she encouraged the conspirators to pursue their ends (Criminal Code ss. 463, 464 and 465).

(e) Environmental Management Act

The Environmental Management Act, S.B.C. 2003, c. 53 imposes liability on corporations but also on individuals, including directors, officers, agents and employees, for offences committed under that Act (s. 121). Further, a “person” is defined to include directors and officers for the purposes of responsibilities under the remediation provisions.

3. Avoiding the Duties

(a) Nominee director

This term is used to describe a director who serves on the understanding that he or she is merely to obey orders given by someone else. Being a nominee, dummy, honourary, accommodation, or part-time director does not lessen a director’s responsibility or duty unless (and only) where the powers to be exercised by the director have been transferred to another person.

There is no distinction between the duties and responsibilities of inside (active) directors or of nominee or accommodation directors or of outside or part-time directors.

A person may not avoid the responsibilities of a corporate director by accepting the office as an accommodation with the understanding that he or she will not exercise any duties of a director.

(b) Doing nothing

Even if a director has not participated in an illegal act, the director is not necessarily excused. A director must actively dissent within seven days of learning of certain prohibited acts taken by the other directors, or else he or she will be deemed to have consented to such acts (s. 154(8)).

While a director may not be liable for any improper act of which he or she is ignorant or which occurred before he or she became a director, upon learning of such a wrongful act, a director must take immediate and effective steps to absolve himself or herself and satisfy
the duty to protect the company. If a causal connection can be shown between a director’s inaction and a loss suffered by the company, the director may be held liable for the consequences of his or her inaction (Bishopsgate Investment Management Ltd. v. Maxwell, [1993] B.C.L.C. 814 (Ch. D.)).

American courts have also held that a director should take corrective action if he or she becomes aware of suspicious circumstances involving co-directors (Newton v. Hornblower Inc., 585 P.2d 1136 (Kan. 1978)).

(c) Agreement

No provision in a contract or articles relieves a director from the duty to act in accordance with the Business Corporations Act, nor from liability for breaches of duty, negligence, default or breach of trust (s. 142(3)). Any provision in the articles or a contract that would amount to such an exemption would be struck down by the courts, although articles that merely modify the scope of a director’s duty to an extent that does not amount to relief from the duty will be permitted (Rhyolite Resources Inc. v. CanQuest Resource Corp. (1990), 50 B.L.R. 275 (B.C.S.C.)).

4. Prohibited Resolutions

Under s. 154, directors become liable for losses and damages suffered by the company if they vote for or consent to certain resolutions. These resolutions relate to:

- an act contravening the restrictions on any business or power if the company pays compensation to a person (s. 154(1)(a));
- paying an unreasonable commission or discount on the issue of shares (s. 154(1)(b));
- paying certain (non-stock) dividends if the company is insolvent or if the payment renders the company insolvent (s. 154(1)(c));
- purchasing, redeeming, or otherwise acquiring shares for consideration where the company is or is rendered insolvent (s. 154(1)(d));
- making a payment or giving an indemnity to a director, officer or other eligible party contrary to s. 163 (s. 154(1)(e)); and
- issuing shares for less than their par value or that are not fully paid (s. 154(2)).

Some of these prohibited resolutions involve a question of whether a company is insolvent or would be rendered insolvent by the action, so a director can apply to court to determine if a company is insolvent or would be rendered insolvent by the proposed action (s. 70(3)). This application would likely only be useful in extreme cases.

A director who attended a meeting but did not vote for the resolution or who did not attend the meeting may avoid liability when a prohibited resolution is passed by actively dissenting as set out in ss. 154(5) or 154(8). Since a director is deemed to have given consent unless a dissent is made, it is important to follow the procedures set out in these subsections.

A director may avoid liability for a prohibited resolution that has been passed by entering a dissent in the minutes, or by delivering a dissent in writing to the secretary during the meeting, or, more practically, by sending it by registered mail to the registered office promptly after the meeting (s. 154(5)). The company and the secretary of the subject meeting must certify the date and time the dissent is received (s. 155) and must place a copy with the company’s records at its records office (s. 42(1)(o)).

A director cannot dissent if he or she voted for the resolution (s. 154(6)).

The joint and several liability under ss. 154(1) and (2) is in addition to, and not in derogation of, any liability imposed on a director by the Business Corporations Act or any other act or rule of law (s. 154(3)). Anyone else who benefited from the resolution may also be joined (s. 154(2)(b)).

[§5.04] Conflict of Interest

Conflict of interest is the one area where directors and officers are most likely to get into trouble. Although the basic principles that relate to conflicts of interest are clear and although conflicts should be avoided where possible, applying those principles in practice permits a director some latitude. If the director moves carefully, the law may still permit a measure of conflict to co-exist between a director’s own interest and that of the company.

The following is a discussion of how a director could run into conflict, a consideration of what conflicts are permissible, and if those conflicts are not permissible, what forms of protection are available to the director.
1. General

The basic principle was set out in Aberdeen Railway Co. v. Blaikie Brothers, [1854] All E.R. Rep. 249 at 252 (H.L.). It states that no fiduciary shall be allowed to enter engagements in which he has, or can have, a personal interest conflicting, or which possibly may conflict with the interest of those he is bound to protect. So strictly is this principle adhered to that no question is allowed to be raised as to the fairness or unfairness of a contract so entered into.

The meaning of these words was narrowed and clarified by the House of Lords in Phipps v. Boardman, [1967] 2 A.C. 46 (H.L.). The words "possibly may conflict" were interpreted to mean what the reasonable person, in looking at the situation, would think gives rise to a real, sensible possibility of conflict, not what one could imagine might arise out of a situation.

If there is an improper conflict (as opposed to a permissible conflict as discussed later), the errant director must account to the company for his or her profits (Redekop v. Robco Construction Ltd. (1978), 7 B.C.L.R. 268 (S.C.)). This obligation does not depend on bad faith or bad intent, or whether the profit would or should otherwise have gone to the company, or whether the opportunity may not even have been open to the company to take advantage of, or whether the company was in fact damaged, or whether the director had a duty to obtain the source of the profit for the company. The mere existence of the conflict gives rise to the obligation to account.

For a director, a conflict may arise in many situations, including when the director:

- personally contracts with or competes with the company or he or she is a director of two companies that contract with each other.
- does something that is motivated by considerations other than the "best interests of the company" or when he or she does something ostensibly for one reason but also has an important collateral purpose. This is referred to as the "collateral purpose" doctrine. The leading cases relating to this doctrine are Teck Corp. Ltd. v. Millar (1972), 33 D.L.R. (3d) 288 (B.C.S.C.), and Hogg v. Cramphorn Ltd., [1967] Ch. 254, in which the directors used their power to issue shares to themselves and others in order to try to extinguish a contract and defeat a takeover bid.
- learns of or appropriates for himself or herself an opportunity for profit that should have gone to the company. This is called the "corporate opportunity" doctrine. The Supreme Court of Canada set out the principle that a director or officer cannot take a maturing corporate opportunity for himself or herself (Canadian Aero Service v. O'Malley, [1974] S.C.R. 592; see also 3464920 Canada Inc. v. Strother, 2005 BCCA 35)).

Things such as secret benefits, secret commissions and bribes are forbidden and will render the director or officer who took them liable to account, even if they were not gained at the expense of the company and even if the opportunity was not open to the company. A director who takes a bribe in any form, even if it appears to be a gift, is liable to account for it. A director must not accept any gift or remuneration from someone dealing with the company.

2. Disclosure and Ratification

At common law a person in a position of trust (such as a director or an officer of a company), could not benefit in any way from his or her position. About 100 years ago the courts began to relax this rule, provided that the shareholders ratified the action. If the interested director held shares, he or she was entitled to vote in ratification proceedings (North-West Transportation Co. v. Beatty (1887), 12 A.C. 589 (P.C.)). Most jurisdictions have now codified these rules in their corporate statutes so that directors or officers may not be held accountable for profits or gains realized from a contract or transaction with the company in which he or she has a personal interest, provided that the director takes certain steps. These steps are set out in ss. 147 to 153 of the Business Corporations Act and in s. 120 of the CBCA.

Generally, all directors but only "senior" officers (defined in s. 1(1)) must disclose their personal interests in a contract or other transaction (s. 148(1)).

Directors and senior officers need only disclose the contract or transaction when it is material to the company and if the director or senior officer has a material interest in the contract or transaction, or is a director or senior officer of, or has a material interest in a person that has a material interest in the contract or transaction (s. 147(1)). Additional exemptions are provided for in situations that were not required to be disclosed under the Company Act, or for when the only parties to the transaction are the company and various wholly-owned
subsidiaries or when the interested directors or senior officers are the sole shareholders of the relevant company (s. 147(2) and (3)).

Unless the director or senior officer properly discloses his or her interest and has the transaction properly approved, they must account to the company for any profit they make as a result of the transaction (s. 148(1)). If they do not take these steps, the director or senior officer may still be relieved of the obligation to account for profits by the court if the court finds that the transaction was fair and reasonable to the company (s. 150(1)).

A director or senior officer is not liable to account for any profits from the contract or transaction which he or she was required to disclose provided that

1. the disclosable interest was disclosed under the relevant Companies Act and the contract or transaction is approved under s. 149, other than s. 149(3) (s. 148(2)(a)), or

2. the directors who have no conflict approve the contract or transaction after the nature and extent of the interest have been disclosed to them (s. 148(2)(b)); or

3. the shareholders approve the contract or transaction by a special resolution after the nature and extent of the interest have been disclosed to them (s. 148(2)(c)); or

4. even if the contract or transaction is not approved in accordance with s. 149, if the contract or transaction was entered into before the person became a director or senior officer, the interest is disclosed to the directors or the shareholders, and the interested director or senior officer does not participate in any decisions or resolutions relating to the matter (s. 148(2)(d)).

There is no time specified for when the disclosure must be made, so the necessary approval may be given after the transaction has taken place.

No particular form is specified for the disclosure but it must be in writing. “Written” may be by being included in the consent resolution, or in the minutes of the meeting that approved the transaction, or in a written disclosure delivered to the company’s records office (s. 148(3)). Copies of disclosures must be retained at the company’s records office (s. 42(1)(n)(ii)) and shareholders may inspect the relevant portions of the minutes of meetings of directors or directors resolutions or other records that contain the disclosures (s. 148(5) to (7)).

If the company has entered or proposes to enter a material transaction or contract with a company or firm of, or in which, a director or senior officer of the company is a director or senior officer or holds a material interest, it is sufficient disclosure if a written statement is delivered to the company declaring that the interested party has such an interest or holds such a position in the target company or firm (s. 148(4)).

Once the interested director or officer makes the appropriate disclosure, the transaction must be approved by a directors’ resolution or a special resolution of the shareholders (s. 149(1)). An interested director is not entitled to vote on the directors’ resolution (but can vote his or her shares on a shareholders’ resolution) to approve the matters (s. 149(2)) and is entitled to be counted in the quorum for the directors meeting, unless the articles provide otherwise (s. 149(4)).

When all the directors are interested in a transaction, they are authorized by s. 149(3) to vote to approve it on behalf of the company and thereby put it into effect (for example, in the case of the issue of shares to all of the directors). However, this does not mean that if all the directors are interested in the same transaction they may approve it and not be liable to account to the company for any profit. Section 148(2)(b) says that a director does not have to account for profits if the transaction is disclosed and approved by the directors, but the approval is only effective in situations other than those in s. 149(3). Consequently, if all the directors are interested, then they must properly disclose and have the transaction approved by special resolution of the shareholders under s. 148(2)(c), or else they may be liable to account for any profits.

There is no requirement that the transaction be reasonable and fair to the company before the directors and shareholders can approve it. However, if the contract or transaction was not properly approved under s. 148(2), the court may, if it determines that the contract or transaction is not reasonable and fair to the company, enjoin the company from entering the transaction, and/or order that the interested director or senior officer account for their profits, and/or make any other order that the court considers appropriate (s. 150(2)).

A resolution in writing of the directors may still be used when a director is unable to vote because that director has a disclosable interest (s. 149(2)) since only those directors entitled to vote need sign a resolution in writing for it to be valid (s. 140(3)(a)(i)).
A director or senior officer is not required to disclose his or her interest in a contract or transaction merely because (s. 147(4)):

1. the contract or transaction relates to security granted by the company for loans to or obligations undertaken by the director or senior officer or a person in whom the director or senior officer has a material interest for the benefit of the company or its affiliate;
2. it relates to an indemnity or insurance for the director or senior officer under ss. 159 to 165; or
3. it relates to the remuneration of a director or senior officer in his or her capacity as a director, officer, agent or employee of the company or its affiliate; or
4. it relates to a loan to the company, and he or she (or a particular corporation or firm in which he or she has a material interest) has guaranteed or will guarantee the repayment of the loan; or
5. it is with or for the benefit of an affiliated corporation (see s. 2(1) to (4)), and he or she is a director or senior officer of that affiliated corporation (although if the director has some other interest in the affiliated corporation, such as being a shareholder, then the exception does not apply).

Sometimes additional exceptions are included in the articles of a company. It is important to ensure that any provisions in the articles that make exceptions to the conflict provisions are not broader than those in s. 147(4) so as not to mislead the directors and officers. The provisions of the Business Corporations Act take precedence in this area and must be observed (ss. 142(2) and (3)).

Although a director or senior officer may be liable to account for profits if the disclosures and approvals referred to in ss. 148 and 149 are not obtained, the fact that the director or senior officer was interested in the matter does not render the contract or transaction invalid (s. 151). In that event, the court, on the application of the company or any director, senior officer or shareholder may enjoin the company from entering into the proposed contract or transaction, order that the director or senior officer must account for any profit, or make any other order that the court considers appropriate, but only if the court determines that the contract or transaction was not fair and reasonable to the company (s. 150(2)). A court will only set aside a contract or transaction if it is equitable to do so (Ronbar Holdings Inc. v. Realecash Services Inc., [1991] B.C.W.L.D. 1875 (S.C.)).

Keep in mind that the courts impose a high standard of compliance on directors in situations where there is a conflict. Mere disclosure may not be sufficient in all cases. In Levy-Russell v. Tecmotiv Inc. (1994), 13 B.L.R. (2d) (Ont. Ct. (Gen. Div.)) the court stated that even if the director has made full disclosure, the director must continue to place the interests of the company ahead of his own. If the conflict is serious and the stakes are high, resignation by the director may be the only proper way to deal with it.

The directors should always go through the process of disclosure and ratification (that is, comply technically with the statutory rules) even if it may seem unnecessary at the time. If the company has only two or three directors who are the sole shareholders and are aware of the circumstances, one might say, “Who is to complain?”

Any director, senior officer, registered or beneficial shareholder, as well as the company, can complain if the proper steps of disclosure and ratification are not observed (s. 150(2)). In addition, the shareholders may change and the new group, upon discovering the profit formerly made by the directors, may claim for repayment. This is what happened in the case of Abby Glen Property Corporation v. Stumborg (1978), 85 D.L.R. (3d) 35 (Alta. C.A.). The previous directors sold their shares and later had to account for their former, undisclosed profits, even though this profit now amounted to a windfall for the new shareholders since the purchase price of the shares was negotiated without knowledge on either side of this potential claim. Similarly, in the case of Redekop v. Robco Construction Ltd. (1978), 7 B.C.L.R. 268 (S.C.), the court held that because a director did not properly disclose his interest and obtain the necessary approvals, he had to account, even though the director may have been acting in good faith or the business opportunity which the interested director took for himself was not open to the company.

Section 153 states that a director or senior officer who holds any office or possesses any property, right or interest by which, directly or indirectly, a duty or interest might be created in material conflict with his or her duty or interest as a director or senior officer of the company, must disclose the nature and extent of the conflict. The disclosure must be made to the directors promptly after he or she becomes a director or senior officer, or if he or she is already a director or senior officer, promptly after he or she began to possess the property, right or interest or hold the office. However, this section seems to stand alone:
sections 147 to 150 do not seem to apply to it. Consequently, even if disclosure has been made under s. 153, when a specific transaction or contract comes along in which a director or senior officer has an interest, that director or senior officer must still comply with ss. 148 and 149.

The Canadian Aero Service case, [1974] S.C.R. 592, expanded the potential liability of directors and officers in situations where they might be inclined to take a maturing business opportunity for themselves.

If a director or officer wishes to take a “business opportunity” that the company does not wish to pursue, he or she may be able to reduce (though probably not eliminate) exposure to liability by taking the following steps:

- disclose promptly his or her intent;
- resign from the board upon seeing the opportunity emerge;
- offer the opportunity to the company before leaving;
- delay making any profit from the venture for as long as possible;
- avoid taking any of the company’s clients, at least not directly. Any clients who wish to remain with the director should approach him or her, not vice versa;
- avoid luring away any officers or employees of the company, and
- receive from the board and the shareholders their blessing in the form of resolutions, which turn down the profitable opportunity and ratify his or her action.

These steps will not guarantee immunity, but they may help if the director or officer remains adamant in taking advantage of what might be a corporate opportunity.

It is also useful to obtain the unanimous ratification of the action by the shareholders. The case of Canada Safeway Ltd. v. Thompson, [1951] 3 D.L.R. 295 (B.C.S.C.) indicated that the conduct of the director may have been acceptable if the shareholders of the company had unanimously approved his actions after receiving full disclosure.

[§5.05] Protection from Liability

What can a director do to protect himself or herself against liability in a conflict of interest situation, and if found liable, to what extent may he or she be insured or indemnified?

1. Due Diligence

For directors to be able to properly defend themselves if their conduct is called into question, they must be able to show that they were duly diligent (that is, they took all reasonable care) in their conduct as a director. This requirement is particularly important in avoiding responsibility for the conduct of employees who may have caused the company to commit an offence. If directors are able to show on a balance of probabilities that they took all reasonable care, they may avoid liability (R. v. Bata Industries Limited (1992), 9 O.R. (3d) 329 at 362 (Prov. Ct.).

Bata has been cited with approval and adopted in many subsequent cases, although none so far has reconsidered or reviewed the underlying principles.

The due diligence exercised by directors and officers of a corporation is one of the factors taken into account when assessing who is to be ordered to undertake or contribute to remediation under the Environmental Management Act (s. 46(1)).

2. Indemnification

At common law, a company was permitted to indemnify directors in certain circumstances. Most jurisdictions have now codified this ability in their corporate statutes, but it is still only applicable in limited circumstances.

Under the Business Corporations Act a company may indemnify a director, officer or other parties, except regarding certain matters (see ss. 164(a) and (b) and s. 163(2)).

A company may indemnify a past or present director or officer or other persons who acted as a director or officer of affiliates or, at the request of the company, acted as a director or officer or equivalent of a partnership, trust, joint venture or other unincorporated entity (defined as an “eligible party”) against “eligible penalties” (defined in s. 159) relating to their actions as directors and officers of the company (s. 160).

Subject to the prohibitions referred to below, a company must pay the net expenses of an eligible party, after the final disposition of the matter, if the party was substantially successful on the merits, or if he or she was wholly successful on the merits or otherwise (s. 161).
A company may also pay the expenses of an eligible party in advance, provided that the party undertakes to repay the advances if it is later determined that the company is prohibited from paying such expenses (s. 162).

A company cannot pay an indemnity if

- the indemnity or payment is made under an earlier indemnity and at the time the agreement was made the company was prohibited from paying an indemnity by its memorandum or articles (ss. 163(1)(a) and (b));
- the party did not act honestly and in good faith with a view to the best interests of the company (s. 163(1)(c));
- the proceeding was not a civil proceeding and the party did not have reasonable grounds for believing that his or her conduct was lawful (s. 163(1)(d)); and
- the proceeding is brought against the party by the company or an associated corporation (s. 163(2)).

Notwithstanding any of the above limitations, the company or a director or officer may apply to court for an order that the company must indemnify the director or officer for any liability or expenses incurred by the party or for any other related obligations of the company (s. 164).

Although a company may enter into an agreement to indemnify a director or officer, because of the prohibitions the agreement cannot indemnify him or her in all circumstances. A director or officer would be wise to obtain an agreement of indemnity from the company requiring it to indemnify him or her when it is permissible to do so. Also, it is permissible and wise to obtain an agreement from a principal shareholder of the company or from some other outside party to protect against the other circumstances.

3. Insurance

Most company acts allow the company to purchase insurance for directors and officers (Business Corporations Act s. 165 and CBCA s. 124(4)). The Business Corporations Act allows the company to take out insurance on behalf of a director or officer against any liabilities, even those against which the company is not entitled to indemnify him or her.

Although this option is very helpful for directors, it does not solve all their problems. Frequently there are restrictions contained in the insurance policies, which exclude claims for wilful or dishonest acts. Some policies also provide for a large deductible, which in effect prevents a complete avoidance of liability. Although policies used to be issued for up to three years, most now have a term of one year only.

Canadian companies are becoming increasingly interested in obtaining liability insurance for their directors and officers. There are basically two kinds of policies that follow the nature of the liabilities described above. The first type covers directors and officers for personal liability when the corporation either chooses not to or is not permitted to indemnify them or does not have the ability to do so. The second type insures the company itself so that it may be reimbursed for the costs and expenditures it incurs in indemnifying its own directors and officers.

Whether or not insurance is available and how much it costs depends on the individual case. However, because of recent high profile scandals and legal actions against directors and officers, the cost of this type of insurance has increased substantially in recent years and insurance companies have implemented tougher underwriting guidelines. Some of the factors that the insurance companies consider when reviewing a potential client are as follows:

- the scope of the indemnification provisions;
- the amount of coverage desired;
- whether the company shares are widely or closely held;
- the profitability of the company;
- the type of business conducted by the company;
- the degree of control exercised by its parent if the company is a subsidiary;
- the type of products manufactured by the company;
- whether the company frequently offers securities to the public;
- whether the company is involved in acquisitions or mergers or corporate changes; and
- the company’s past loss history.

The policies also have some broad exclusions. They generally do not apply to the following:

- fines and penalties imposed by statutes;
- libel or slander;
- personal gains which are found to be illegal;
- claims made by the company itself.
against the director;

- punitive damages;
- claims brought about or contributed to by the dishonesty of the director or officer; or
- liability for obtaining a secret profit or gaining a corporate opportunity.

In addition, some policies will totally or partially exclude environmental or pollution claims.

It is also possible to obtain policies for senior management personnel who are not otherwise directors or officers of the company but who play a major role in its corporate decisions.

4. Resignation

Although a director is probably wise to resign from the company as soon as he or she sees that things are beginning to go wrong, resignation will not shield the director from liability for matters that have already occurred. Remember the previous comments about a director’s duty to be diligent and the fact that some American cases have held that if a director discovers wrongdoing, he or she has an active duty to do something about it.

5. Trust Funds

Many statutes impose personal responsibility on the directors of companies that fail to observe the statutory rules. Recently, some companies have attempted to protect their directors from personal liability for unpaid wages, taxes, assessments, and so on, by establishing a fund to ensure that such obligations are actually paid by the company. This tactic has met with some limited success in British Columbia; see Re Westar Mining Ltd. (1992), 70 B.C.L.R. (2d) 6, in which the Supreme Court approved the establishment of a trust fund to pay the vacation pay of employees, although the court denied the use of such a fund to secure the unpaid severance pay of the employees.

The directors of an Ontario company tried to protect themselves by establishing a trust fund to pay statutory liens shortly before their company went bankrupt. The court set aside the fund as a preference and allowed a secured creditor to collect the money instead (Central Guaranty Trust Co. v. 775843 Ontario Ltd. (1993), 6 P.P.S.A.C. (2d) 121 (Ont. Ct. (Gen. Div.))). It has been suggested that if the directors establish such a fund far enough in advance of the company’s insolvency, then they may be successful in retaining the fund to pay obligations for which they might otherwise be personally responsible.

6. Relief by Court

Where it appears to the court that in a proceeding against a director, officer, receiver, receiver-manager or liquidator of a company where it appears to the court that the director (or such other person) is or may be liable for negligence, default, breach of duty or breach of trust, but he or she has acted honestly and reasonably and ought fairly to be excused, the court, after taking into consideration all the circumstances of the case, may relieve the director (or such other person), either wholly or partly, from liability, on the terms the court considers necessary (s. 234).

To be entitled to the relief a director must pass three tests, that is, he or she must have acted both honestly and reasonably and also ought fairly to be excused; see Doncaster v. Smith (1987), 15 B.C.L.R. (2d) 58 (C.A.) (a case involving a receiver manager) and Island Realty Investments Ltd. v. Douglas (1985), 19 E.T.R. 56 (B.C.S.C.) (a case involving a director). In general, a director should be excused if his or her default arises from a mere technical defect that would not ordinarily have caused any loss to the company (Doncaster v. Smith).

[§5.06] The Lawyer as a Director

Generally, lawyers make good directors. Their training equips them to articulate their position well, to marshal facts required in making business decisions, and to explain the legal impact of the company’s decisions. They have extensive experience because of their work with many business-related problems. Many lawyers participate in their own businesses separately from their legal practice. For these reasons, they are frequently asked to serve on the board of directors of companies, especially those of their clients.

Problems

For the lawyer who serves as director, serious problems may arise which are different from, and in addition to, all of the other problems that relate to directors in general.

1. Duties

In satisfying the duty of care, a director must exercise that degree of skill that may be reasonably expected of a person of his or her knowledge and experience. In matters in which a lawyer is deemed to have a higher degree of skill than a layperson, the lawyer has a greater burden and responsibility. He or she must therefore take a greater interest in the affairs of the corporation and make more inquiries about its operations.
A leading case illustrating this situation is Escott et al. v. BarChris Construction Corporation (1968), 283 F. Supp. 643, a decision of the U.S. District Court of New York. This case involved a class action for damages sustained as a result of false statements and material omissions in a prospectus contained in a registration statement. One of the directors was a lawyer who was also counsel for the company. Even though there was an express finding that he honestly believed that the registration statement was true and complete, his “unique position” as the director most directly concerned with the statement could not be disregarded. The court said at 687:

As a lawyer, he should have known his obligations under the statute. He should have known that he was required to make a reasonable investigation of the truth of all of the statements in the unexpertised portion of the document, which he signed. Having failed to make such an investigation, he did not have reasonable grounds to believe that all these statements were true . . . As the director most directly concerned with the registration statement and assuring its accuracy, more was required of him in the way of reasonable investigation than could fairly be expected of a director who had no connection with this work.

2. Conflicts

This problem concerns the situation where a person acts as the lawyer for the company at the same time as he or she acts as one of its directors. One of the functions of the board of directors is to monitor the management. It is not always practical for any person to be loyal to the board (as a director is bound to be) and, at the same time, to be loyal to management (as a lawyer is bound to be) since it is from the management that the lawyer receives instructions and the retainer. In general, it is almost impossible for a lawyer to be free from conflict in this situation.

On the question of conflicts of interest, refer to and become familiar with Chapters V, VI and VII of the Code of Professional Conduct, as well as Section 3.4 of the Code of Professional Conduct for British Columbia (the “BC Code”).

Section 3.4 of the BC Code provides several principles to guide a lawyer’s conduct when the lawyer is invited to act as legal advisor and investor, or as legal advisor and in some other role. Note that a lawyer may not act for a client when the lawyer has a direct or indirect financial interest in a matter, or a financial or membership interest in or with the client that would reasonably be expected to affect the lawyer’s professional judgement. Also, a lawyer will be barred from acting if a relative or associate has a financial or membership interest, which would reasonably be expected to affect the lawyer’s judgement (Rule 3.4-26.1).

The provisions in the Code and BC Code do not forbid a lawyer from acting both as lawyer for a company and as one if its directors, although they do point to the dual role as a likely source of problems. Normally, if two clients have mutual dealings, a lawyer is able to decline to act for either or both clients should a problem develop. However, if the lawyer is a director of one of those clients, he or she also faces the difficult decision of having to resign as director.

In securities practice, there is a very high standard of care and diligence expected of lawyers when the prospectus is being prepared. A lawyer may have to act in an adversarial role when conducting examinations and certifications. This adversarial approach is jeopardized when he or she is also a director of the company. This conflict would be particularly pronounced if the company’s chief executives refused to follow his or her advice with respect to disclosure or some other matter. In that case, the lawyer/director may become a party to the decision by the board not to follow his or her own advice.

A lawyer/director is also unable to give an opinion that is free from his or her professional training. If he or she is asked (as every director is) for his or her view on the course of action proposed by the board, the reply will be taken as if it were a legal opinion, whether or not he or she is retained as the board’s lawyer.

At common law, lawyers have been shielded from liability to parties other than clients by the doctrine of privity, but the trend now is to repudiate the doctrine of privity and permit non-clients to recover damages when the injured party had cause to rely on the lawyer who acted as director or officer of the company in which the injured party had some investment (see Hedley, Byrne & Co. v. Heller & Partners Ltd., [1964] A.C. 465 (H.L.), and Chapter 6 of the Practice Material: Professionalism: Ethics).

3. Loyalty

Lawyers acting as corporate counsel are employees of the company. As employees they owe their loyalty to management. They should try to anticipate problems before they actually materialize and must be cautious and conservative.
Directors owe their loyalty not only to management, but also to all the shareholders and employees. Their goal is to create profits for the corporation, even at a risk.

4. Use of Confidential Information

A director must not use confidential or sensitive information to benefit himself or herself or others. This principle applies with even greater force to a lawyer (whether a director or not) because he or she often has access to more sensitive, confidential information about clients than may be the case with other directors. If the lawyer/director should also happen to be a shareholder, he or she may be tempted to buy or sell, or not to sell, shares in the client’s company according to the nature of the information.

5. Privilege

How can the lawyer/director determine whether the information he or she receives is privileged? If the information is received in the lawyer’s capacity as director, it is not privileged; if it is received in the lawyer’s capacity as lawyer, it is privileged.

The best advice is that a lawyer should not serve on the board of a company for which he or she or any member of his or her firm acts as lawyer. Everything a lawyer is expected to do on the board can be done better if he or she is an independent legal consultant.

However, what if a lawyer has to (or wants to) serve on the board of directors of a client company? W.R. Miles suggested the following policy at the 1980 Canadian Bar Association mid-winter meeting, pages F-47 to F-50:

(1) there should be a process to screen the companies for which lawyers in the firm may act as directors;

(2) the lawyer must be kept well informed of corporate affairs and insist upon financial information and regular meetings;

(3) the lawyer should insist on an indemnity from the shareholders of the company;

(4) the lawyer should always be sensitive to potential conflict situations;

(5) the lawyer should establish a close relationship with the auditor; and

(6) in the case of public companies, the lawyer should only purchase or sell shares after publication of the financial statements.
Chapter 6

Finance\footnote{Kathleen Keilty, of Blake Cassels & Graydon LLP, kindly revised and updated this chapter in July 2011 and January 2009. This chapter was based on an article prepared by Carl J. Pines of Owen Bird for the CLE publication, \textit{Company Law} (November 1987) and was revised annually by the author to January 2006.}

References to the “Act” and to the “BCA” are to the \textit{Business Corporations Act}, S.B.C. 2002, c. 57, as amended.

[§6.01] Introduction to Methods of Finance

The three common methods of financing (also known as capitalizing) a corporation are by

- shareholder loan (debt finance);
- share sales (equity finance); and
- corporate borrowing.

In addition, a company can raise money by making profits, but this method involves skills beyond the scope of this chapter.

1. Shareholder Loan (Debt Finance)

The simplest method of capitalizing a company is by shareholder loan; the principal shareholder loans the bulk of the money needed to capitalize the company and subscribes for shares with only a nominal value. There must be at least one common share subscribed for in every company.

(a) advantages

The investment is easily repaid to the shareholder by a simple cancellation of debt as opposed to a reduction of share capital by the redemption or repurchase of shares. Another attraction of debt financing relates to corporate bankruptcy; a shareholder who has financed by way of a shareholder loan will rank at least equally with all other unsecured creditors, instead of below them as a common or preferred shareholder would do. Moreover, a shareholder who makes a loan to the shareholder’s company can always take security from the company and thereby rank above unsecured creditors. However, if any major loan or credit is extended to the company, the outside financier will likely require a postponement of the shareholder security.

(b) disadvantages

In certain circumstances, there may be a detrimental tax consequence to a shareholder who invests in a company by way of a shareholder loan. In the initial phases of a company’s activities, usually there are insufficient earnings to allow the company to pay any interest to the shareholder on the loan. Assuming the small business rate and that the shareholder pays tax at a higher rate, if the company pays tax at approximately 13.5%, then receiving interest is not tax effective for the shareholder since the tax saving to the company is less than the tax cost to the individual shareholder of earning the interest.

When a shareholder borrows money from an outside lender and in turn lend it to the company at no interest, or at a rate of interest that is less than what the shareholder is paying to the outside lender, there is a risk that the interest paid on the outside loan may not be deductible for tax purposes by the shareholder. This is because s. 20(1)(c) of the \textit{Income Tax Act}, R.S.C. 1985, c. 1 (5th Supp) stipulates that only interest on borrowed money used for the purpose of earning income from a business is deductible. If the company is not paying any interest to the shareholder, it is difficult to claim that the outside loan was obtained for the purpose of earning income.

Despite the words of the \textit{Income Tax Act}, the Canada Revenue Agency’s Interpretation Bulletin No. IT-533 indicates that a deduction is permitted for the full interest expense incurred when a taxpayer borrows money to be loaned interest-free to a wholly-owned corporation (or in cases of multiple shareholders, where shareholders make an interest-free loan in proportion to their shareholdings) and the proceeds have an effect on the corporation’s income-earning capacity, thereby increasing the potential dividends to be received.

If a shareholder loans money at no interest to the shareholder’s company, there is a danger that if the company cannot repay the loan, the resultant capital loss will be denied. This is because the shareholder did not make the loan for the purpose of gaining or producing income from a business or property (\textit{Income Tax Act}, s. 40(2)(g)(ii)). Based on the Federal Court of Appeal’s decision in \textit{Byram v. The Queen} (99 DTC 5117), the Canada Revenue Agency has stated that it will not deny the capital loss, provided that a clear connection between the shareholder and the corporation’s
dividend income can be demonstrated.

2. Share Sale (Equity Finance)

A second method of financing a company is to subscribe for and have the company allot and issue shares. The buyers of the shares provide the capital that the company requires and in return acquire rights with respect to voting, dividends, and the return of their capital, to the extent that these rights are provided for in the company’s articles.

(a) advantages

Interest on money borrowed to purchase shares is deductible under s. 20(1)(c) of the Income Tax Act since the purchase of shares is generally recognized as being “for the purpose of earning income from property”. Anyone who does not qualify under the conditions set out in IT–533, should probably finance by way of share purchase rather than by shareholder loan.

(b) disadvantages

As mentioned earlier, funds loaned by a shareholder to a company are easily repaid by a simple cancellation of the debt. However, money paid for shares cannot be returned to the contributor so easily. One way to return such money is to find a buyer for the shares; this may be difficult when a company has few shareholders. Another way is to have the articles of the company specifically provide for the redemption or repurchase of the shares by the company; however, tax consequences may arise on the redemption or repurchase of those shares, depending upon their value and the attributes of the shares at the time of such redemption or repurchase.

The “paid up capital” of the shares for tax purposes is especially important on a share repurchase or redemption. For example, if the shareholder purchases common shares, to the extent that the amount paid by the company for the shares on repurchase exceeds the paid up capital, the shareholder will be deemed to receive a taxable dividend from the company. Once the shares have been redeemed or repurchased, there is a reduction of the paid up capital in the company. This does not mean that the redemption or repurchase of shares cannot be effected, only that care must be taken at the outset when drafting the articles to provide for it (see s. 77 of the B.C.A.). The other main disadvantage to share purchase financing is that shareholders rank below unsecured creditors in the event of bankruptcy.

3. Corporate Borrowing

One of the major reasons that businesses incorporate is the concept of limited liability. A company is a separate legal entity from its shareholders and the potential liability of the shareholders is, in the absence of an agreement to the contrary, the amount they have agreed to pay for their shares. Thus, the optimal financing for any company is to find an outside lender who will loan money to the company directly without taking personal guarantees from the principal shareholders. This maximizes the concept of limited liability. However, lenders typically will not make loans directly to small corporations, or to new corporations, without personal guarantees of the shareholders. This in effect negates the concept of limited liability.

Assuming that a lender is not willing to loan funds to capitalize a company without a personal guarantee, the question then arises as to which of the following methods of financing the company is best:

- direct loan to the company with repayment assured by a shareholder guarantee; or
- loan to the shareholder who in turn makes a shareholder’s loan or purchases shares.

Often the lender dictates the terms of borrowing and the shareholder may not have a choice. Assuming a choice, the answer to the question depends on whether the individual or the company is able to make better use of the interest deduction. If the first option is chosen, only the company is able to take the interest deduction. The company benefits only if there are corporate profits. If the second option is chosen, the individual takes the interest deduction, which can be deducted from other income.

4. Procedural Aspects – Overview

In all methods of assisting a company to raise money, including those listed above, a lawyer must observe various formalities. Certain documents must be prepared and procedures followed to ensure that certain financial transactions in which a company is involved are properly effected. In particular, being familiar with the provisions of the articles is very important. These formalities, procedures and documents will be discussed below in relation to each of the following three aspects of corporate practice:

- the issue of shares;
- the borrowing of money and the granting of security for repayment; and
- restricted transactions (repurchase of
shares, guarantees, etc.).

[§6.02] Issue of Shares

1. Initial Proceedings

When asked to incorporate a company, one of the lawyer’s duties often will be to prepare the incorporation agreement, by which the incorporator agrees to subscribe for one or more shares of the company. The lawyer will also prepare the notice of articles which sets out the names of the first directors of the company. The allotment and issue of shares is then usually effected through a directors’ resolution consented to in writing or, if the client wishes, by a meeting of the directors.

The process for issuing a share is:

1. The shareholder subscribes.
2. The company approves the issuance of shares and sets the price. Typically it is the directors who have authority to issue shares and set the price for shares, but not always. The lawyer must check the company’s charter documents, carefully read ss. 62 and 63, and also always check for any pre-emptive rights of existing shareholders contained in the articles, a shareholders’ agreement, or the Pre-existing Company Provisions that preserve pre-emptive rights for pre-existing companies unless or until the company determines otherwise.
3. The shareholder pays fully for the shares.
4. The company creates a “paper trail” for the payment.
5. The company issues the shares, entering the details in the Central Securities Register (s. 111).
6. The company issues a share certificate representing the shares (s. 107).

The issuance or transfer of any shares must also comply with applicable securities laws. For most private companies an exemption from the registration and prospectus requirements of applicable securities laws is available; however, it is essential for lawyers to confirm the availability of an exemption each time a share is issued or transferred. A detailed discussion of the Securities Act (British Columbia) is beyond the scope of this chapter.

2. Kinds of Shares

Section 52(1)(a)(i) authorizes the company to create shares with par value and shares without par value. Most BC companies are incorporated having common shares without par value. For particular purposes—such as financial “silent partner” shares or for income tax planning—preference shares having a par value will be authorized. Preference shares may specify that they will rank ahead of the common shares in some respects, for example the payment of dividends or the return of capital on liquidation. The Act does not specifically refer to shares as being common, preferred or preference, but rather refers to special rights and restrictions attached to shares (s. 58).

Section 58 contemplates that different classes of shares may be created having special rights or restrictions. The definition of “special rights or restrictions” in section 1(1) is an inclusive one, and thus many different characteristics can be given to shares. The Registrar of Companies office takes the position that rights attached to different classes of shares may be the same except where one class is designated as preferred or preference, in which case some preference must be apparent from the provisions. The different classes are used to achieve certain business or tax planning results and the special rights must be carefully drafted to ensure that the objectives are achieved.

The importance of attaching special rights or restrictions is illustrated by the proposition that the rights attached to a class of shares apply equally to all shares of that class. In Muljo v. Sunwest Projects Ltd. (1990), 60 B.C.L.R. (2d) 343 (C.A.), a shareholder sought priority over another shareholder based upon historic asset contributions to the company. The articles did not provide for any class of shares to have a priority upon dissolution or winding–up and thus the shareholder’s argument was dismissed on the basis of s. 59(3), which provides that every share must be equal to every other share, subject to the special rights and restrictions contained in the articles of a company. It may be that subsections 59(5) and 60(5) have overridden this case in that they provide that special rights and restrictions can be binding on or accessible to only some of the shareholders of a class of shares, however the addition of these provisions should not alter the requirement for such special rights and restrictions to be contained in the articles of a company.
Tax planners have traditionally used par value shares to indicate the amount received as consideration by the company from the sale of those shares. Tax planners also specify par value shares to ensure that paid-up capital is not accidentally increased as a result of a transaction; an increase in paid-up capital may result in a taxable deemed dividend to the subscriber. For this reason, par value shares are often used in “roll over” transactions involving tax deferred transfers of property to a corporation. Care must be taken in such transactions to ensure that a directors’ resolution specifies the exact amount of paid up capital for the shares being issued.

For a more detailed discussion of the various types of shares and some examples of special rights and restrictions see Practice Material: Company, Chapter 4, Share Capital.

3. Securities Registers and Certificates

The Business Corporations Act combines the register of allotments, the register of transfers, and the register of shareholders into one register known as the central securities register, the contents of which are set forth in s. 111. The central securities register must be maintained at the records office of the company (s. 42(1)(d)) or in any other location in British Columbia designated by the directors (s. 111(4)).

While s. 194(3) of the Act provides that a share certificate is evidence of ownership of shares, it is the entry of the holder’s name in the security register which, by definition, results in the person becoming a shareholder of the company, and which gives to that person all the rights that flow to shareholders under the Act (see ss. 1(1), 194(3) and (4)).

In share acquisitions where a lawyer acts either as counsel for the seller or the buyer, an exhaustive chain of title examination can be undertaken to establish ownership of the shares by a thorough vetting of the security register and the resolutions/minutes of the directors effecting allotments and transfers. It is good practice to ensure that the security register is noted–up concurrently with the preparation of any documents or instruments to effect share allotments or transfers, even before the resolutions/minutes effecting the allotments or transfers are signed. It is far easier to correct the register for those infrequent share allotments/transfers that do not “complete”, than it is to try to create registers or note–up all transfers years after the fact.

Shares issued by a company may be represented by a share certificate or may be uncertificated shares (s. 107(2)). Unless the shares of which a shareholder is a registered holder are uncertificated shares, a shareholder is entitled, without charge, to a share certificate certifying the number of shares for which he or she is recorded as owner (s. 107(3)). If the company refuses to issue a certificate, an application may be made to court, under s. 230 of the Act, for an order directing the company to comply.

4. Form of Share Certificates

It is good practice to review any form of pre–printed share certificate before using it to ensure that the requirements set out in s. 57 have been met. If there are rights and restrictions attached to the shares—such as restrictions on transfer or preference share rights—the certificates must state the rights and restrictions or they must be attached to the certificate or, as is most commonly done, the certificate must carry a “statement” or “legend”, which indicates that there are special rights and restrictions and that a copy of the full text may be obtained at the registered office or records office of the company.

5. Dating of Share Certificates and Other Formalities

The certificate must state the date on which it is issued (s. 57(d)). Use either the date in the resolution authorizing the issue of the certificate, or an “as of” date. The share certificate cannot be considered as issued until an appropriate director or officer has signed it (s. 110). In public companies, signatures are mechanically reproduced and a counter signature endorsed on the certificate by the transfer agent (s. 110(b)).

6. Lost Share Certificate

Section 109 states that s. 92 of the Securities Transfer Act applies to lost or destroyed share certificates. Under s. 92 of the Securities Transfer Act, a company must issue a new share certificate to the owner who claims that a share certificate has been lost, destroyed or wrongfully taken, if the owner:

- makes the request for replacement before the company receive notice that the lost, destroyed or wrongfully taken share certificate has been acquired by a protected purchaser;
- provides the company with an indemnity sufficient in the company’s judgement to protect the company from any loss that they may suffer by issuing a new certificate; and
- satisfies any other reasonable requirements imposed by the issuer.
The usual practice is to obtain a statutory declaration as well as an indemnity from the person who requests the replacement certificate.

7. Price for Shares

Section 64(3) provides that a share is not fully paid for until the company has received full consideration for it in past services performed for the company, property or money. Under s. 63(2)(b), par value shares must be issued at a price set by a directors’ resolution and equal to or greater than the par value. Where shares are without par value, s. 63(1) requires that the issue price be set in the manner contemplated in the articles, or if not contemplated in the articles, by a directors’ resolution (or special resolution for pre-existing companies).

Section 72(1) of the Act provides that on the issue of shares without par value, an amount equal to the issue price for those shares is added to the capital of a company, unless the shares were issued for property, in which case it is an amount not greater than the issue price for those shares. Section 72(2) provides that additional amounts can be added to the company’s capital by a directors’ resolution or ordinary resolution. Section 72(3) states that when par value shares are issued an amount equal to the aggregate of their par value is added to the capital of that class or series.

8. Non–Cash Consideration for Shares

Where the number of shares issued by a company increases without a corresponding increase in the value of the assets of the company, the value of the existing shares will be diluted. Thus, where shares are to be paid for by way of consideration other than cash, s. 64(4) requires that the value of property or past services be an amount set by resolution of the directors that is in all the circumstances of the transaction no greater than fair market value. While it is sometimes difficult to determine the fair market value of non–cash consideration, the evil which the section was intended to prevent is far worse; for example, the allotment of shares in exchange for past services or property which have no relation whatsoever to the “fair” value of shares.

The language of the resolution authorizing the issue of shares for a non–cash consideration should fully describe the nature of the property or past services exchanged for the shares and must set out a determination by the directors of the money equivalent received by the company. It is also advisable for the directors to fix the fair market value of the consideration at the actual fair market value, rather than at some other value, for both tax and business reasons.

In Pioneer Distributors Ltd. v. Bank of Montreal (1994), 97 B.C.L.R. (2d) 143 (S.C.), a complicated restructuring was challenged on the grounds (among others) that the fair market value of the property exchanged for the shares had been incorrectly determined by the board of directors. In the circumstances of this case, the judge held that it was nearly impossible to set an accurate amount as being fair market value within the normally accepted meaning of the concept and agreed to a range of error, which was significant. However, an important factor in the case was that no member of the public could become a shareholder or a creditor as the company had been established to assist in the restructuring of a corporation.

9. Limitation of Liability

Under s. 87(2) of the Act, the liability of a member for a share held is limited to the amount actually agreed to be paid for the share.

10. Payment for Shares/the Paper Trail

Section 64(2) requires that every share must be fully paid for before it is issued. The Act provides that each director is to be jointly and severally liable to compensate the company and any shareholder for any loss sustained by reason of an allotment or issue in contravention of s. 63(2)(b) or s. 64 (s. 154(2)). While section 64 does not purport to say that shares issued in contravention are a nullity (Davidson v. Davidson Manufacturing Co. (1977) Ltd. (31 August 1978), Vancouver C776454 (B.C.S.C.) endorsed in Oakley v. McDougall (1987), 37 B.C.L.R. 31 (C.A.), non–payment for shares before they are issued may render the allotment and issue of the shares invalid. Consequently, it is good practice to provide a proper “paper trail” in the directors’ resolution that allots and issues the shares, that is, acknowledgment of receipt from or on behalf of the applicant for the shares of all consideration receivable by the company in full payment for the shares. It may help to prepare and sign an application for the shares indicating that a cheque in payment is attached and to remind the client to deposit the cheque that was drawn to pay for the shares into the company’s bank account.

11. Partly Paid Shares

Before 1973, shares could be issued before the company received the full consideration for them. This resulted in what was known as partly paid shares upon which “calls” or “assessments” could be made. Sections 88 and 89, which preserve the concept of partly paid shares, only apply to
companies incorporated before 1973.

12. Commissions and Discounts

Subsection 67(1) authorizes payment of a reasonable commission or the allowance of a reasonable discount to a person in consideration of the person purchasing or agreeing to purchase or procuring or agreeing to procure, purchasers of its shares. Directors who vote for or consent to a resolution authorizing a commission or discount contrary to s. 67 are jointly and severally liable to the company to make good any loss or damage (s. 154(1)(b)).

13. Restrictions on Subsequent Allotments

When allotting shares at any time following the initial issue of shares, the lawyer must ensure that all sections of the Act (as well as the articles) respecting subsequent allotments are complied with.

Section 41(1) of the Company Act provided that, before allotting shares, the directors had to offer them pro rata to all members as a pre-emptive right. There is no similar requirement under the Act; however, the Business Corporations Act contemplates that the pre-emptive right will continue to apply to pre-existing companies unless the articles state otherwise: see the “Pre-existing Company Provisions” (PCPs in Table 3 of the Regulations). This shows the importance of using a properly prepared set of articles, particularly for public companies.

Many companies have similarly worded provisions in their articles to ensure that each shareholder will not suffer dilution of his or her percentage equity without having the opportunity to preserve it by subscribing for more shares.

The PCPs establish a minimum period of seven days within which shareholders can accept their entitlement. The usual practice in allotting shares in companies in which the shareholders are not quarrelling is to provide for a waiver of the right to receive the pro rata entitlement every time shares are allotted. A general waiver is prohibited (PCP – P13, but a specific waiver is permitted under P14) and the pro rata entitlement rules do not apply to public companies. Care should be taken in the form of a waiver; a signed waiver referring to a specific allotment at a specific price and referring to ss. 40(1) and (4) of the Company Act has been judicially approved (Milburn v. Copperbank Resources Ltd. (1975), 58 D.L.R. (3d) 138 (B.C.S.C.)).

14. Transfer of Shares

Many of the provisions of the Act dealing with the transfer and transmission of shares were repealed in conjunction with the coming into force of the Securities Transfer Act, which now generally governs the transfer of securities, other than transfers effected under ss.227, 291 or 300(7) (s. 106.1). The Securities Transfer Act establishes a complex scheme for the transfer of, and taking security in, share certificates and other securities. A discussion of the taking of security interests in shares and other securities is beyond the scope of this chapter and will not be addressed.

Section 17 of the Securities Transfer Act provides that a person acquires a security if they are a person to whom a security is delivered. Delivery of a certificated security to a purchaser occurs when:

- the purchaser acquires possession of the security certificate;
- another person acquires or acknowledges holding the security certificate on behalf of the purchaser; or
- a securities intermediary, such as a clearing agency or a brokerage, acquires possession of the security certificate, in registered form, and the security certificate is registered in the name of the purchaser, payable to the order of the purchaser, or specially endorsed to the purchaser (Securities Transfer Act s. 68(1)).

Delivery of an uncertificated security occurs when the company registers the purchaser as the registered owner, or another person either becomes the registered owner on behalf of the purchaser or, if previously registered as the owner, acknowledges that they hold the uncertificated security on behalf of the purchaser (Securities Transfer Act, s. 68(2)).

Sections 71 through 76 of the Securities Transfer Act deal with the endorsement of securities. An endorsement may be in blank or special (Securities Transfer Act, s. 71). A special endorsement is an endorsement which specifies to whom the security is to be transferred or who has the power to transfer the security (Securities Transfer Act, s. 71(3)). An endorsement may appear on the share certificate or as a separate document (s. 1(1)). Most share certificates contain such an instrument on the reverse.

An endorsement of a security does not constitute a transfer until the delivery to the purchaser or the purchaser’s agent of:

- the security certificate on which the endorsement appears, or
15. Restrictions on Share Transfers

When preparing the documentation to provide for a transfer of shares, the lawyer must ensure that all sections of the Act are complied with and that all provisions in the articles dealing with the transfer of shares are complied with.

The articles of most private companies prohibit the transfer of shares except with the approval of the directors. This restriction is required in order for the company to avail itself of the “private issuer” exemption under applicable securities laws. The restriction also ensures that those who own the company can limit shareholders to the people of their choice (for example, an astute business acquaintance but not necessarily his or her spouse or children). A restriction on transfer effectively precludes a shareholder from selling his or her shares to an unknown or disliked buyer. The authority for the directors having the absolute right to refuse to approve a transfer of shares, if there is a properly drawn provision in the articles, is well rooted in Canadian and British case law.

It is important to be thoroughly familiar with a company’s articles, not only to be aware of the restrictions on transfer, if any, but also to be cognizant of other peculiarities in the articles that might have an impact on corporate finance. This is particularly true when the corporate records have been transferred from another lawyer’s office, as the articles in use in BC are not consistent on these matters.

16. Transmission

“Transmission” refers to the process by which shares are involuntarily transferred, such as occurs following the death or bankruptcy of a shareholder. Section 118 sets out the items that the company must ask for when the personal representative, for example the executor, requests a transmission of shares. One practice is to transmit the shares into the name of the executor first, and later, when the estate is settled, transfer the shares to the beneficiary. Alternatively, it is possible for the company to transmit the shares to the executor and then immediately transfer the shares to the beneficiary, in one resolution. The important thing to note is that the company is bound to record the transmission provided that the requirements of s. 118 are met, while the transfer of the shares to the beneficiary is subject to all the usual procedures for, and the usual restrictions on, the transfer of shares of that company.

17. Conflicts

Practitioners must be careful when taking instructions from majority shareholders that they do not act in such a way as to prejudice or oppress minority shareholders. The best interests of the company are not necessarily those of the majority shareholders and the first duty of the company’s lawyer is to the company. In fulfilling this duty, a lawyer must make sure that all the directors are properly advised so that they may make informed decisions. Where the situation becomes litigious, the company’s lawyer must be vigilant in acting only for the company; see Mottershead v. Burwood Bay Settlement Company Limited, [1991] B.C.W.L.D. 2113 (S.C.).
§6.03  Borrowing and Granting of Security

1. Introduction

Those lending money to companies usually retain a lawyer to assist in preparing the security documentation. The lender’s lawyer should ensure that the company has the power and capacity to borrow and should prepare proper security documents, which contain all of the necessary provisions to permit the lender to enforce its security. The borrower’s lawyer is usually retained because the borrower wishes to ensure that the lender is not getting more security than was agreed upon. Whether one is acting for a lender or a borrower, the subject of opinions becomes very important and will be discussed under a separate heading later.

2. Capacity to Borrow

Before the 1973 revisions to the Company Act, a company’s memorandum set out elaborate objects and generally adopted all of the powers given to companies by s. 22 of the Companies Act then in force. The 1973 revisions to the Act supposedly cured all problems pertaining to the power to borrow for the purpose of carrying out a company’s objects because every company was (in theory) given the power and capacity of a natural person (s. 30). However, when preparing security documentation for lenders, there are two anomalies to note. Under s. 33 restrictions can be placed in the articles regarding the business to be carried on by a company as well as on its powers.

3. What the Lender’s Lawyer is Looking for

The lender’s lawyer will

- conduct searches at the Corporate Registry and Personal Property Registry, and obtain certified copies of the articles and notice of articles;
- peruse the searches to note any existing charges on assets which he or she is instructed to charge;
- obtain instructions as to whether any encumbrances which exist will be “permitted” or must be discharged or postponed to the charge he or she is preparing;
- peruse the memorandum: if the company is a pre–1973 company, the lawyer will decide whether it has the power and capacity to borrow; if there are restrictions and he or she has doubts, the lawyer may request that the memorandum be “rolled–over” to eliminate any capacity problems;
- peruse the articles looking specifically for a power in the directors to borrow and the restrictions, if any, on execution of documents and use of seal; and
- prepare an enabling resolution sanctioning the borrowing.

This will all be done even though s. 421 states that no person is deemed to have notice or knowledge of the contents of any document concerning the company by reason only that the document has been filed with the Registrar of Companies (that is, at the Corporate Registry). The procedures are undertaken because they have evolved as being prudent practice in lending situations. Also, in lending situations, extensive communication between the lawyer and the loan officer is not the norm; in other words, there may be knowledge of certain matters pertaining to the company not known to the lawyer or the person giving instructions, but known to the person who approved the transaction on behalf of the lender.

4. Opinions

The lender’s lawyer will usually require that the borrower’s lawyer provide an opinion. The lender’s lawyer will rely on this opinion to some extent in giving an opinion to the lender. The borrower’s lawyer’s opinion is usually drafted by the lender’s lawyer to include statements that the company is duly incorporated, validly existing and in good standing, and has the power and capacity to borrow; that all steps have been taken to authorize the borrowing; and that the security documents have been validly executed and delivered and are binding on the company.

The practice in Vancouver with regard to the borrower’s lawyer’s opinion is not uniform. Some lenders’ lawyers feel that such opinions are superfluous, in that the lender’s lawyer has done all the background investigation to assure himself or herself of everything expressed in the borrower’s lawyer’s opinion. One reason for asking for such opinions is to involve a lawyer in the transaction who will be present when the documents are executed, explain them to the client and ensure that they are properly executed. Efforts at establishing a uniform approach to the form and content of such opinions have been undertaken by a committee established in part by the CBABC and the Law Society and reference should be made to “Legal Opinions: Standard Form Security Instruments” prepared by the Solicitors Legal Opinion Committee, and produced in Benchers Bulletin, November 1989 at page 7 and subsequent updates to such forms.
5. Registration of Charges

Registration of charges is governed by the PPSA, which is discussed in detail in Chapter 3 of the Practice Material: Commercial Law.

Before the PPSA came into force, mortgages, debentures and other security instruments executed by companies were filed with the Registrar of Companies, unless the charge pertained solely to motor vehicles, in which case it was filed at the Central Registry. Since charges registered under the old system are continued perfected under the PPSA, documents filed with the Registrar of Companies are still important to determine priorities and the capacity of a company to incur debt.

One of the most significant practice differences resulting from the PPSA is that the Personal Property Registry is a notice registry rather than a document registry. Thus, the document creating the security is not registered, but notice of the document and the collateral charged are registered.

Another important practice point resulting from the PPSA is the ability of a company to grant a purchase money security interest (PMSI). A PMSI creates a priority over all charges previously granted with respect to goods, which are acquired by use of this security interest. Thus, the PMSI concept permits borrowers to finance specific acquisitions in the face of previously granted security agreements, without seeking the security holder's permission. Note, however, that general security agreements may contain covenants by the company not to create indebtedness by a PMSI, with the result that if the lender’s consent is not obtained the company may be in default under the general security agreement.

6. Debentures

Before the PPSA, it was the practice of lenders to require a corporate borrower to grant security over its assets by way of fixed and floating charge debentures. Since the PPSA, the practice has changed and at present, almost all lending institutions in British Columbia use general security agreements rather than debentures as means of obtaining a fixed and floating charge on a borrower’s assets. Debentures are still widely used in public offerings of secured debt and in other situations where there are multiple lenders. In these cases, the debentures are commonly issued under a trust deed that contemplates that the lenders will act in concert, through a trustee.

Business: Company
3. Authority for Purchase or Redemption of Shares

A company may only purchase or redeem its shares if:

- the shares have a right of redemption attached to them (s. 77(a)); or
- the company is authorized by its articles to purchase its shares (s. 77(b)), and

if the applicable solvency test set out under sections 78 or 79 is met.

4. Solvency Test

Sections 78 and 79 prohibit the redemption, purchase or other acquisition of shares if the company is insolvent or if the redemption, purchase or acquisition would render the company insolvent. Insolvent means the inability of the company to pay its debts as they become due in the usual course of business (s. 1(1)).

When the date that the purchase is approved is not the date that the purchase is affected, the question arises as to when the solvency test is to be applied. In Nelson v. Rentown Enterprises Inc. 96 D.L.R (4th) 586 (S.C.), a corporation agreed to purchase its own shares in exchange for certain land and premises. At the time that the purchase was entered into, the corporation was solvent; however, prior to the closing of the transaction, the corporation became insolvent. The question before the court was whether the solvency test in the equivalent sections of the Canada Business Corporations Act was to be applied at the time of entry into the agreement or at the time of completion. The court held that the solvency test must be applied at both dates, that is when the agreement was made and also at the time of performance. The court reasoned that the limitation on the corporation’s power to purchase its own shares was intended to protect creditors and other shareholders from share purchase arrangements that may prefer one or more shareholders in an insolvency situation. The finding that the solvency test must be applied at both dates has been upheld in British Columbia in Lin v. Lee, [1996] B.C.W.L.D. 2010 (S.C.), which also held that a redemption agreement made at the time the company is insolvent or which would render the company insolvent, is intrinsically illegal and cannot be interpreted in any other way, regardless of whether the parties are unaware of the contravention at the time. The Lin case may have been reversed by the effect of s. 78(3), but once again the obligation of directors to act honestly and in good faith and in the best interest of the company embodied in s. 142 results in personal exposure to the directors even though s. 78(3) would have saved what was otherwise an invalid transaction.

5. Requirement to Purchase Pro Rata

The Act continues an important concept from the previous legislation in providing that an offer to purchase shares must be made rateably to every member who holds shares in the class. This concept continues to apply to all pre-existing companies (i.e. companies incorporated prior to the coming into force of the Act) until it alters its notice of articles (see the PCPs – Table 3 of the Regulation). For companies incorporated after the BCA came into force, the concept, as well as other concepts found in the former legislation (and generally viewed as minority shareholder protections), will be optional and in the hands of the drafter of the articles. Thus most practitioners will have developed an extremely detailed checklist of questions to discuss with clients forming multi-shareholder companies as to whether these protections are to apply to these shareholders or not.

The PCPs also provide that a redemption or repurchase of shares must be made rateably unless the articles provide otherwise, once again showing the heightened importance in the drafting of articles.

The PCPs (and the protective devices) are intended to protect minority shareholders by ensuring that the majority cannot redeem or repurchase significant amounts of equity while leaving the minority shareholders “holding the bag” (Dusik v. Newton (1984), 50 B.C.L.R. 31 (S.C.)).

6. Provision of Financial Assistance and Guarantees

One of the most significant changes in the Act is the elimination of many of the restrictions contained in the Company Act pertaining to a company providing financial assistance. These sections generated more litigation than any other with the exception perhaps of the relief from oppression sections.

The BCA provides that a company may give financial assistance to any person for any purpose by means of a loan, guarantee, the provision of security or otherwise (s. 195(2)). Aside from the elimination of a large number of difficult provisions in the former Company Act, a major change inherent in the Act is the elimination of personal liability for directors if a company provides financial assistance at a time when it is insolvent.
7. Lawyers Obligations when Reviewing Security Documents

Even though the merit of problems found in sections 102 and 103 of the former Company Act have been eliminated by the broad sweep of section 195(2) of the Act, lawyers should be vigilant in their review of documentation submitted by legal counsel for a lender.

When lenders are taking security that includes the guarantee of another company for the debt, lender’s counsel will often prepare a resolution for the company giving the guarantee, which recites that the directors have determined that the giving of financial assistance is in the best interests of the guarantor. This is somewhat of a “hold over” from the provisions of the Company Act, which required in certain instances that directors determine that the giving of the financial assistance was in the best interests of the guarantor. When acting for a guarantor, one ought to understand the basis for the directors reaching this decision. When the companies are affiliated or associated, the connection is clear; in other cases it is not. The directors cannot conclude that giving financial assistance is in the best interests of the guarantor, unless there are reasonable grounds for believing the financial assistance is in the best interests of the guarantor. When acting for a guarantor, one ought to understand the basis for the directors reaching this decision. When the companies are affiliated or associated, the connection is clear; in other cases it is not. The directors cannot conclude that giving financial assistance is in the best interests of the guarantor, unless there are reasonable grounds for believing the financial assistance is in the best interests of the guarantor. In reaching such a conclusion, directors can rely on the protection afforded by the “business judgement rule”; in most cases, the courts will not look behind the business decisions of directors who have acted fairly and reasonably.

8. Disclosure Requirements of Section 195

The BCA provides that where a company has provided material financial assistance, the fact must be disclosed if the financial assistance is or was given to a shareholder, a director, an officer or an employee of the company or an affiliate or any of their associates or to any person for the purpose of a purchase by that person of a share of the company or an affiliate (s. 195(3)).

The disclosure must be contained in a “written record” in the company’s records office and is to be made before or promptly after the giving of the financial assistance. The written record must be in a consent resolution of the directors, the minutes of a directors meeting at which the giving is authorized or in the minutes of the directors meeting that follows the giving of the financial assistance (s. 195(7)). The disclosure must include a brief description of the nature and extent of the assistance, together with amount of and the terms on which it was given (s. 195(6)).
Chapter 7

Ordinary Procedures

References to the “Act” and to the “BCA” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended.

For a description of how shares are issued and transferred, see §6.02

[§7.01] Introduction

Both shareholders and directors are involved in carrying out ordinary corporate proceedings. In some cases the BCA provides that the proceedings can be handled quite informally; for example, by reaching an agreement or consensus, by convention, or by holding meetings in accordance with the company’s articles. In other cases the proceedings are more stringently regulated.

When shareholders and directors of a company make decisions, those decisions are recorded by resolutions. The BCA provides for six different types of resolutions: ordinary, special, exceptional, unanimous, separate or special separate. Each of these resolutions may be passed as a consent resolution. In general, if the consequences are significant to a company, the requirements to gain approval are more stringent.

[§7.02] Shareholders’ Meetings

1. Definitions: “Shareholders” and “Resolutions”

A “shareholder” is defined as a person whose name is registered in a securities register of a company as a registered owner of a share of the company or, until such entry is made, a subscriber (in the case of a pre-existing company) or an incorporator (s. 1(1)).

The BCA defines the different types of resolutions in s. 1(1):

- An “ordinary resolution” is a resolution passed at a general meeting by a simple majority of the votes cast by shareholders who have the right to vote or that is consented to in writing by at least a “special majority” of the votes entitled to be cast on the resolution at a general meeting, after the resolution has been submitted to all shareholders entitled to vote on it.

- A “special resolution” is a resolution passed at a general meeting by at least a “special majority” of the votes cast by the shareholders at a general meeting for which the company has given notice of its intention to propose that resolution or that is consented to in writing by all of the shareholders entitled to vote on the resolution at a general meeting.

Note that a “special majority” is the number of votes that a company’s articles state are required in order for the company to pass a special resolution, which must be between 2/3 and 3/4 of the votes cast on the resolution. If the company’s articles do not specify a number of votes, then the number defaults to 2/3.

- An “exceptional resolution” is a resolution passed at a general meeting by a number of votes specified in the company’s articles that is greater than a “special majority” or that is consented to in writing by all of the shareholders entitled to vote on that resolution at a general meeting.

- A “unanimous resolution” is a resolution passed or consented to in writing by all of the shareholders entitled to vote on that resolution.

- A “separate resolution” and a “special separate resolution” are resolutions on which only shareholders holding shares of a particular class or series of shares are entitled to vote. Note s. 181 of the Act, which addresses the procedures for meetings involving separate resolutions.

- A “consent resolution” is a resolution (of shareholders or directors, as the case may be) that is consented to in writing by a sufficient number of shareholders or directors. For a special, exceptional, or unanimous resolution, all shareholders entitled to vote at a general meeting must consent to the resolution, in writing, for it to be effective. For the requirements for consenting in writing to an ordinary resolution or a special separate resolution, refer to subparagraph (b) of their respective definitions (BCA, s. 1(1)). For the requirements of a consent resolution of directors, see the Practice Material: Company, §5.02.7.

In general, ordinary resolutions are required for matters that do not significantly affect the company or its value. Special resolutions are required to approve matters with significant consequences to a company. In some cases, the company may want to use an exceptional resolution to impose a specific threshold of approval that is higher than a special majority. There are several provisions in the BCA...
that require a unanimous resolution of the shareholders. As well, if a company chooses, it could require unanimous shareholder approval in order for an exceptional resolution to pass.

2. Annual General Meetings: Calling, Notice, Quorum and Waiver

Every company must hold its first annual general meeting within 18 months after incorporation and, thereafter, at least once each calendar year and not more than 15 months after the last annual general meeting (s. 182(1)). However, the shareholders have the right to defer the date of an annual general meeting, to consent in writing to all of the business required to be transacted at that annual general meeting or to waive the holding of that meeting or any earlier annual general meeting that the company was required to hold (s. 182(2)). A unanimous resolution is required in order to effect any of these matters. Upon application by the company, the Registrar of Companies may allow the company to hold its annual general meeting on a date that is later than the required meeting date (s. 182(4)).

The articles of a company normally set out the procedures for calling a general meeting. Notwithstanding the articles, the directors of a company must call a general meeting upon the requisition by one or more shareholders holding at least 1/20 of the issued voting shares (s. 167), unless the directors are excused from doing so by s. 167(7). A general meeting also may be called by the court if a company fails to hold a general meeting as required, or if it is impractical to hold or conduct a general meeting in the normal way as prescribed in the Act, the regulations to the Act or the articles (s. 186). The company auditor is entitled to attend any general meeting (s. 219(1)) and must attend at a directors’ meeting when requested to do so (s. 219(2)).

Every company is required to give its shareholders notice of any general meeting (s. 169(1)). The exact notice period is prescribed by regulation, but in any event cannot be more than 2 months before the meeting. Shareholders and any other person entitled to receive notice of a meeting may waive or reduce the period of notice for a particular meeting (s. 170(1)). The waiver or reduction of a notice period need not be in writing (s. 170(2)) and any person who attends at the meeting is deemed to have waived his or her entitlement to notice, unless the attendance is for the express purpose of objecting to the transaction of any business on the grounds that the meeting is not lawfully called (s. 170(3)). Notice is deemed to have been received on the day following the date of mailing, excluding Saturdays and holidays, unless the company’s charter provides for a longer period (s. 6(2)). One should always check the articles for notice provisions (s. 7(1)(b)). The notice of a general meeting should specify the time and place of the meeting, and provide a clear description of the business and matters to be discussed. To determine the shareholders who are entitled to notice of, or to vote at, the general meeting, the directors may fix in advance a date as the record date (ss. 171(c) and (d)). If no date is fixed, then the record date is considered to be 5 p.m. on the day immediately preceding the date on which the notice of meeting was mailed to the shareholders or, if no notice was sent, the beginning of the meeting.

Unless otherwise provided for in the articles, a quorum for transaction of business at a general meeting is two persons entitled to vote at the meeting, whether present in person or by proxy (s. 172(1)(a) and (b)). However, if the number of shareholders entitled to vote at the meeting is less than the requisite quorum, then quorum for that meeting is all of the shareholders entitled to vote at the meeting, whether present in person or by proxy (s. 172(1)(c)).

When a company holds an annual general meeting, the directors must place before each meeting the company’s financial statements prepared in accordance with the Act. For a company that is a reporting issuer, the company must provide the shareholders with a copy of the financial statements and the related auditor’s report that the company is required to file with the Securities Commission under the Securities Act (s. 185(1)(a)). There are similar provisions for a company that is a reporting issuer equivalent (s. 185(1)(b)). For other companies, s. 185(1)(c) requires that the financial statements be prepared in accordance with ss. 198 and 199, unless the shareholders have waived this requirement by a unanimous resolution under s. 200. Section 204 requires a company to appoint an auditor on or before each annual reference date (as defined in s. 1(1)). This appointment commonly occurs at the annual general meeting. Finally, the directors are elected at this meeting. Generally, directors retire at the annual general meeting and are eligible for re-election. One should always check the articles for the rules governing the election process.

All general meetings must be held in British Columbia, unless the articles otherwise provide or unless the company obtains either the consent of the shareholders by ordinary resolution, or the consent of the registrar before the meeting is held (s. 166).
3. Voting

Unless the articles otherwise provide, every shareholder has one vote for each share held by that shareholder (s. 173(1)). At the annual general meeting, voting is generally by a show of hands except where a poll is demanded and except where a shareholder is participating in a meeting by telephone or other communications medium (s. 173(2)). When a vote is taken by a show of hands each shareholder present is entitled to one vote only, regardless of the number of shares he or she holds. Note that the vote by hands includes by proxy if proxies are permitted (see 4 below). Always check the articles of the company for the voting procedures. If a motion is made at any meeting, the chair’s declaration that the motion is carried by the requisite majority is, unless a poll is demanded, conclusive evidence of that fact, without proof of the votes recorded in favour or against the resolution (s. 173(3)). In addition, a subsidiary cannot vote shares of a holding company (s. 177).

At any meeting at which a motion has been submitted, a shareholder or proxyholder who is entitled to attend the meeting may demand a poll. On a poll, every shareholder who votes in person or by proxy may cast the number of votes to which he or she is entitled. Every ballot cast on a poll and every proxy voted at a meeting must be held by the secretary for three months after the meeting, during which period they remain open to inspection at the records office of the company (ss. 173(5) and (6)).

For class meetings, check the articles of the company. If the articles are silent, s. 181 stipulates that the provisions governing general meetings shall apply.

4. Proxies

Check the articles of the company for provisions relating to proxies. A “proxy” is defined in s. 1(1) of the Act as “a record by which a shareholder appoints a person as the nominee of the shareholder to attend and act for and on behalf of the shareholder at a meeting of shareholders”, and is recognized in s. 173. The provisions relating to the form of proxies, information circulars and proxy solicitation requirements for reporting companies that were in the Company Act were not included in the Business Corporations Act, thus leaving these requirements to the Securities Act and comparable legislation in other jurisdictions.

Companies that are reporting companies but not reporting issuers or reporting issuer equivalents (defined in s. 1(1) as “pre-existing reporting companies”) are not subject to securities legislation. Part 13 of the Business Corporations Act sets out certain rules applicable to pre-existing reporting companies. Section 433 of the Act provides for the creation of “Statutory Reporting Company Provisions” that apply to a pre-existing reporting company until it alters its articles to include those provisions in them. The Statutory Reporting Company Provisions are found in Table 2 to the Regulation and include rules relating to proxies and information circulars that are very similar to the provisions of ss. 151-155 of the Company Act. There are also rules relating to general meetings of pre-existing reporting companies in s. 184 of the Act.

[§7.03] Financial Statements

When a company holds an annual general meeting, the directors must place before each meeting the company’s financial statements prepared in accordance with the Act. If a company is a reporting issuer, the company must provide the shareholders with a copy of the financial statements and the related auditor’s report that it is required to file with the Securities Commission under the Securities Act (s. 185(1)(a)). There are similar provisions for a company that is a reporting issuer equivalent (s. 185(1)(b)). For other companies, s. 185(1)(c) requires that the financial statements be prepared in accordance with ss. 198 and 199, unless the shareholders have waived this requirement by a unanimous resolution under s. 200. Section 204 requires a company to appoint an auditor on or before each annual reference date (as defined in s. 1(1)). This appointment commonly occurs at the annual general meeting. On demand by a qualifying debentureholder, companies are required to furnish him or her with the latest financial statement and a copy of the auditor’s report on it (s. 201).

A “qualifying debentureholder” is defined in s. 1(1) to mean a person who holds a debenture and who was the holder of that debenture immediately prior to the coming into force of the Act. In other words, persons who became debentureholders after the date that the Act came into force have no right under the Act to receive this information.

Before a company issues or circulates a financial statement, the directors must approve it. One or more directors signatures must evidence this approval (s. 199(1)). The form and contents of financial statements are prescribed by regulation (see Part 8 of the Regulation).
§7.04 Annual Report

Every company must file with the Registrar of Companies an annual report in the prescribed form (Form 6 to the Regulation) within 2 months of each anniversary date of the company’s recognition under the Act (s. 51). These reports must be filed electronically. The fee for filing annual reports is prescribed by regulation. Failure to file an annual report within this period may result in the registrar dissolving the company (s. 422(1)(a)).

§7.05 Registrar of Companies

1. Records Maintained by the Registrar

   The records maintained by the registrar include:

   (a) Name index and register

      The Index and Register contains the name of every British Columbia company, as well as private Act, extraprovincial and trust companies, cooperatives, and societies.

   (b) Register of dissolved companies

      A record is maintained for every company, extraprovincial company, society, cooperative and trust company that has ever been registered with the Registrar of Companies. The record shows when the company was dissolved or ceased to be registered, and also shows the names of companies that have changed their names.

   (c) Receivers and receiver managers

      A receiver or receiver manager must file with the registrar a notice respecting his or her appointment, change of address and ceasing to act within 7 days after the effective date (s. 106).

   (d) Company files

      Under the Business Corporations Act, very few records are filed with the registrar and most records that must be filed must be submitted in electronic form. Copies of these records can be obtained from the registrar through Corporate Online. All company records (including ones submitted to and issued by the registrar) are maintained at the company’s records office.

2. Filings with the Registrar

   Most records that must be filed with the registrar must be filed in electronic form (see s. 30(2) of the Regulation and the Registry Statutes Amendment Act, S.B.C. 2002, c. 17). It is important to watch for records that are not effective until filed. In addition, the time limits for filings should be noted. The registrar has discretion to refuse filings under s. 408. The consequences of being in default of the duty to file any record required by the Act are set out in s. 422(1).

§7.06 Registered and Records Offices

1. Records Office Functions

   Every company must have a records office and must provide both a delivery address and a mailing address for that office in its notice of articles (ss. 34 and 11(e). A company must keep the company records listed in s. 42 at its records office. A company must make different records available for inspection and copying by certain classes of persons. The following classes can be differentiated:

   • current directors (s. 46(1)(a));
   • former directors (ss. 46(2));
   • shareholders (ss. 46(3)(a), 148(5), 195(8), 46(1)(b)(i));
   • former shareholders (ss. 46(3)(b), 148(6), 195(9), 46(2));
   • qualifying debentureholders (s. 43(3)(a)); and
   • any other person (members of the public) (s. 46(4)-(5), 46(1)(b)(ii)).

   The documents that members of the public are entitled to inspect are broader for companies that are public companies or pre-existing reporting companies (s. 46(4)).

   Companies may, by ordinary resolution, impose restrictions on the times during which a person, other than a current director, may inspect their records, but those restrictions must comply with the inspection times prescribed by regulation. It is best to separate records according to who can inspect them.

2. Duty of Care

   All companies and their agents have a duty of care to prepare and maintain records in a complete state, as required by the Act, and so as to avoid loss, mutilation or destruction and falsification of entries (s. 44(4)(a), (b) and (c)). Also, they have a duty to provide simple, reliable and prompt access to the records and registers required by the Act (s. 44(4)(d)).
3. Copies of Records

If a person entitled to inspect a company record requests a copy of that record, the company must provide to that person the requested copy promptly and, in any event, within 48 hours of the request, excluding Saturdays and holidays (s. 48(1)). The company may prescribe a fee for some, but not all, copies requested by such person (s. 48(1) and (2)).

A person is entitled to receive from the person who has custody or control of a company’s central securities register a list setting out the names and addresses of shareholders of that company and the number of shares of each class or series held by that shareholder (s. 49(1)). There are certain procedural requirements that must be met in order for a person to receive this list (s. 49(2)) and, once the list has been received, there are limitations on the uses that can be made of the information in the list (s. 49(3)).

Section 44 deals with various forms of records. All records must be maintained in a bound or loose-leaf form or, in the case of records that a company must maintain pursuant to s. 42, in the manner prescribed in that section.

4. Records to be kept at Records Office

The Act sets out certain requirements relating to documents that companies must keep at their records office (s. 42) \(^2\). Certain documents must be stored at the records office (s. 42) including:

- the certificate of incorporation;
- a signed copy of the incorporation agreement;
- a copy of the company’s articles;
- a copy of the company's central securities register (unless the directors designate another location under s. 111(4));
- a register of directors;
- minutes of general meetings, class meetings and every directors' meeting, and consent resolutions of shareholders or directors;
- a copy of every document filed and certificate issued by the registrar;
- a copy of written disclosure records; and
- financial statements.

5. Examination of the Records

Section 46 sets out a procedure for examining corporate records. Every current director of a company may examine and take extracts of (“inspect”) any records of that company, without charge. A former director may inspect records in relation to the time when he or she was a director (s. 46(1) and (2)).

Every current shareholder and qualifying debentureholder also may inspect, without charge, all records except certain categories of records (s. 46(3); generally these are the directors’ resolutions and minutes of directors’ meetings).

In addition, shareholders may inspect “portions” of any record that contains a statement that a director or senior officer has a disclosable interest in a material contract or transaction (s. 148(5)), or a disclosure of material financial assistance given by a company to certain categories of persons or in certain circumstances (s. 195(8)).

A member of the public (“any person”) also may inspect certain records. With respect to a public company or a pre-existing reporting company, a member of the public has the same right to inspect as a shareholder does (s. 46(4)), but the person cannot inspect the disclosure records under ss. 148(5) or 195(8). A member of the public has substantially more limited access to the records of any other company (s. 46(5)).

Finally, the articles of a company may also permit shareholders, former shareholders, or members of the public, wider access (ss. 46(1)(b) and (2)). These same sections also give former shareholders limited access to records.

Depending on the person making the inspection, the company may have the right to levy a charge for providing requested copies.

6. Time Coverage of Records

For companies incorporated or transitioned under the BCA, records must be maintained from the date of incorporation or transition, although some records of a transitioned company must be kept for a longer period. Pre-existing companies must also maintain the records required by s. 42(2)(e), subject to the exceptions in s. 42(3). After 7 years, it is possible to move certain records to a location other than the records office, so long as they can be produced for inspection within 48 hours of a request.

\(^2\) Note that s. 43 permits a company to store certain of its records at a different location, so long as the records can be produced for inspection within 48 hours.
7. Other Records and Materials

The following provisions concern records similar to, but not listed in, the records office provisions discussed above. These include subscriptions, share certificates, consents to act as directors, and the like.

Every share certificate issued by a company must state clearly the name of the company and words indicating that it is a British Columbia company (s. 57(1)(a)). The share certificate must also include the name of the person to whom the certificate is issued, the number, class and kind of shares (and the amount of the par value shares, if applicable), date of issue, the certificate number, and a statement outlining any restrictions on transfers as well as the date of issue (s. 57(1)(b) to (f)). If the share certificate is only partly paid up, it must state the amount that has been paid (s. 57(2)). Special rights or restrictions must be noted in the text (ss. 57(3) and 51(4)). A share certificate must have one manual signature (s. 110(1)). Any other signatures required may be printed or mechanically reproduced on the share certificate.

Although a seal is not required in British Columbia to make, vary or discharge a contract (s. 193(1) and (4)), companies without a seal encounter problems with land title offices and lending institutions (Property Law Act, R.S.B.C. 1996, c. 377, s. 16(2)). If a company does have a seal, it must have its name engraved in legible characters upon it (s. 27(2)). The company’s articles govern how to execute documents under seal.

Every company must keep proper accounting records of all financial and other transactions of the company (s. 196(1)). The accounting records of a company must be kept in a place determined by the directors (s. 196(2)). If and to the extent permitted by the articles, a company must allow a shareholder to inspect and obtain a copy of its accounting records (s. 196(4)). The directors may, subject to the provisions of the company’s articles, permit a shareholder to inspect and receive copies of a company’s accounting records (s. 196(5)).

2. Appointment of Auditor

The directors of a company must appoint the first auditor of the company to hold office until the annual reference date following the recognition of the company, or fill any casual vacancy in the office of auditor (s. 204(1) and (4)). Otherwise, on or before each annual reference date the shareholders must appoint by ordinary resolution an auditor to hold office until the next annual reference date (s. 204(3)). If for any reason no auditor is appointed, the court may, on application of a shareholder or creditor, appoint an auditor (s. 204(5)). Prompt notice to an auditor of his or her appointment is required in writing (s. 204(6)). The qualifications of “authorized persons” to act as auditors, as well as the duties and rights of an auditor are set out in ss. 205 to 211. The shareholders must set the remuneration of the auditor, but this power falls to the directors if the shareholders so authorize by ordinary resolution, the articles so provide, or the directors appoint the auditor (s. 207).
Chapter 8

Special Procedures

References to the “Act” and to the “BCA” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended. References to the “Reg.” are to provisions of B.C. Reg. 65/2004, as amended.

[§8.01] Alterations of Notice of Articles Generally

The word “alter” includes “create, add to, vary and delete” (s. 1(1)).

This chapter does not deal with alterations of the notice of articles following the change of address of the records office or registered office or the elimination of the registered office under ss. 37(2), 39(7.1), 41(7) or 40(7), or to a change of directors or of the prescribed address of a director under s. 127(2); see s. 257(1).

1. When Permitted

The notice of articles of a company can only be altered in the manner required or permitted by the Act (s. 257(2)(a)).

In addition to the restrictions in the Act, there may be other restrictions on altering the notice of articles, which are contained in special rights and restrictions attached to classes or series of shares or elsewhere in the articles. In addition, there could be restrictions in various agreements to which the company is a party (traditionally, for example, bank loan agreements).

The alteration of the notice of articles must be authorized by a court order or by a resolution (s. 257(2)(b)). The only exception to this requirement is if an alteration to the articles of a company has been approved under s. 259(1) or has been made by court order, and the alteration of the articles renders incomplete or incorrect any information in the notice of articles, or where special rights or restrictions are created, added to, varied or deleted (see s. 11(h)).

In such a case, the company may alter the notice of articles to reflect the alteration to the articles without obtaining the authorization of a further court order or resolution (s. 257(3)). In effect, the resolution or court order altering the articles is sufficient authorization.

2. Types of Resolutions

An alteration of the notice of articles can be authorized by one of three types of resolutions:

- the type of resolution specified by the Act (s. 257(2)(b)(i)),
- if not specified by the Act, the type of resolution specified by the articles (s. 257(2)(b)(ii)), or
- if neither of the above applies, a special resolution (s. 257(2)(b)(iii)).

Some of the sections in the Act dealing with alteration of the notice of articles, in effect, refer to s. 257 (see s. 54(3)(a) and (b) dealing with alterations to the authorized share structure) or specifically refer to s. 257 (see s. 263(1) dealing with changes of a company’s name).

The types of shareholders’ resolutions that could be specified (either in the Act itself or in the articles) include ordinary resolutions, special resolutions, exceptional resolutions and special separate resolutions.

An alteration of the notice of articles could also be done by directors’ resolution if so specified by the Act (see s. 263(2)) or by the articles.

3. Filing with the Registrar

If the notice of articles is being altered under s. 257, the company must file with the registrar a notice of alteration (s. 257(4)). A notice of alteration must be filed electronically (s. 407(a) and Reg. s. 30(2)(e)). (See §8.09.1.)

If the company is not in good standing, the registrar may refuse to accept any filing relating to the company (s. 411(1)(a)). A company will not be in good standing if its annual reports are not filed up-to-date or if the information in the corporate register shows that there is no director of the company.

After an alteration of the notice of articles takes effect under s. 257, the registrar must give to the company a certified copy of the notice of articles, as altered, if requested to do so (s. 257(6)).

4. When Effective

An alteration of the notice of articles under s. 257 is effective

(1) on the date and time that the notice of alteration is filed with the registrar, or

(2) subject to a withdrawal of the notice of alteration, if the notice of alteration specifies a date, or a date and time, on which the alteration to the notice of articles is to take effect that is later than the date and time on which the notice of alteration is filed with the registrar (which cannot be more than 10 days later (s. 410 and Reg. s. 31(b)),

(a) on the date and time specified in the notice of alteration, or

(b) if a date but no time is specified in the notice of alteration, then at the beginning of the specified date (s. 257(5)).

The alteration of the notice of articles takes effect as set out above, whether or not there actually has been a court order or a resolution referred to in s. 257(2) (s. 257(5)).

5. Withdrawal of Notice of Alteration

Section 258 provides that between the time that a notice of alteration is filed with the registrar and before the alteration to the notice of articles takes effect (as set out in s. 257(5)), the company or any person who appears to the registrar to be an appropriate person to do so, may withdraw the notice of alteration by filing with the registrar a notice of withdrawal.

[§8.02] Alterations of Articles Generally

1. When Permitted

Subject to s. 256, there are no restrictions in the Act on when the articles can be altered.

Section 256(1) prohibits pre-existing companies from altering their articles, with very narrow exceptions (s. 256(2)(a) and (c)), which deal with transition matters or restoration matters and with certain minor alterations mentioned below.

However, once a pre-existing company has complied with the relevant transition rollover provisions in s. 370(1)(a) and (b) or 436(1)(a) and (b), it can then alter its articles at any time (s. 256(2)(b)).

There is a general rule at common law that an alteration of the articles must be bona fide and in the best interests of the company as a whole; that is, in the sense of the shareholders of the company generally.

There may be restrictions on the alteration of the articles contained in special rights or restrictions attached to classes or series of shares, or elsewhere in the articles. In addition, there could be restrictions in various agreements to which the company is a party (traditionally, bank loan agreements).

While most alterations of the articles will require a resolution of some kind (or a court order), any individual may insert in the articles the incorporation number of the company and the name and any translation of the name of the company, regardless of whether there has been a resolution directing or authorizing that insertion (s. 12(5)).

These insertions will not constitute a breach or contravention of, or default under, any security agreement or other record, and are deemed not to be an alteration of the company’s charter for the purposes of such security agreement or other record (s. 12(6)).

While most of this section deals with resolutions altering the articles, court orders could also alter the articles.

Section 259, which is the general section dealing with alterations of articles, does not specifically deal with an alteration of the articles of a company by court order, but does refer to such an alteration generally in s. 259(8). A court order is contemplated in s. 257(3) if the alteration of the articles will alter information in the notice of articles. Presumably, such a court order (with the exception of one under an arrangement) would take effect at the time of pronouncement of the order, or any later date and time specified in the order (see s. 259(8)).

2. Types of Resolutions

Generally, the provisions relating to the types of resolutions required to alter the articles are similar to those relating to the alteration of the notice of articles, namely,

- the type of resolution specified by the Act (s. 259(1)(a)),
- if not specified by the Act, the type of resolution specified by the articles (s. 259(1)(b)),
- if neither of the above applies, a special resolution (s. 259(1)(c)).
Some of the sections in the Act dealing with alteration of the articles, in effect, refer to s. 259 (for example, see s. 54(3)(b) dealing with alterations to the authorized share structure) or specifically refer to s. 259 (for example, see s. 261(3) dealing with an alteration to Table 1 articles). Some sections specifically require a special resolution (for example, s. 259(2)) or a special separate resolution (for example, s. 259(3)), both dealing with altering required majorities for those resolutions.

In some cases, the Act may require a shareholders’ resolution (as opposed to a directors’ resolution) without specifying the type of shareholders’ resolution (ordinary or special), for example, creating, varying or deleting special rights or restrictions attached to shares; in this case, if there is nothing in the articles, a special resolution would be required (s. 58(2)). See also s. 60(3), which deals with alterations relating to a series of shares.

The types of shareholders’ resolutions that could be specified (either in the Act itself or in the articles) could include ordinary resolutions, special resolutions, exceptional resolutions and special separate resolutions.

An alteration of the articles could be done by directors’ resolution, if so specified by the Act (for example, see s. 60(1)(b) relating to series of shares), or the articles and assuming that the Act does not require some kind of shareholders’ resolution.

3. Alteration of Articles Affecting Notice of Articles

Section 259(4) deals with the situation in which an alteration of the articles would render incorrect or incomplete any information in the notice of articles or would alter special rights or restrictions attached to shares (because of s. 11(h)).

In such a case, the company must

- note on the resolution altering the articles that the alteration does not take effect until the notice of articles is altered to reflect the alteration of the articles;
- deposit the resolution altering the articles at the company’s records office; and
- after complying with the above, alter the notice of articles (under s. 257) to reflect the alteration to be made to the articles (s. 259(4)).

The alteration of the notice of articles does not need a separate authorizing resolution.

4. When Effective

An alteration of the articles that affects the notice of articles as described above is effective only when the alteration of the notice of articles takes effect under s. 257(5), as set out above (s. 259(5)).

Any other alteration of the articles is effective

(a) on the date and time that the resolution altering the articles is received for deposit at the company’s records office; or

(b) if the resolution specifies a date, or a date and time, on which the alteration to the articles is to take effect that is later than the date and time on which the resolution is received for deposit at the company’s records office:
   (i) on the date and time specified in the resolution altering the articles, or
   (ii) if a date but no time is specified in the resolution, then at the beginning of the specified date (s. 259(6)).

5. Subsequent Copies

When the articles of a company are altered, every copy of the articles issued after the date the alteration takes effect must either reflect the alteration or have attached to it a copy of the resolution, court order or other record by which the articles were altered (s. 262).

Any company that contravenes this requirement commits an offence (s. 426(1)(a)).
an amalgamation under s. 271(6)(a)(ii). It is also relevant with respect to ordinary resolutions in writing; see paragraph (b) of the definition of “ordinary resolution” in s. 1(1).

The resolution that specifies or changes the special majority under s. 259(2) must, itself, be a special resolution, passed (if at a general meeting) by whatever special majority applies to the company at that time (s. 259(2)).

A special resolution can also be consented to in writing by the holders of all shares entitled to vote at general meetings (s. 1(1)).

2. Special Separate Resolutions

A company may alter its articles to specify or to change the majority of votes required for a special separate resolution at a class or series (of shares) meeting, again provided that that majority is at least two-thirds and not more than three-quarters of the votes cast on the special separate resolution (s. 259(3)), passed (if at a meeting of the class or series) by whatever majority applies at the time.

Again, whatever majority is chosen will apply to all special separate resolutions of the class or series of shares. There is no ability to have different majorities for different kinds of special separate resolutions dealing with different matters in the same class or series. See the definition of “special separate resolution” in s. 1(1).

To make this alteration, first, there must be a special resolution of the shareholders (s. 259(3)(a)).

In addition, if any shares of the particular class or series are issued and outstanding, then a special separate resolution of the shareholders holding those shares is required (s. 259(3)(b)), passed (if at a meeting of the class or series) by whatever majority applies at the time.

A special separate resolution can also be consented to in writing by the holders of all the shares of a class or series (s. 1(1)).

[§8.04] Altering Table 1 Articles

If a company has Table 1 as its articles, or if a provision of Table 1 is adopted by a reference in the articles of a company, any regulation that amends Table 1, or that provision, will automatically effect a corresponding alteration to the articles of the company, at the time the regulation comes into force, without the necessity for a resolution to make that alteration, unless the articles otherwise provide (s. 261(2)). It is not clear what the phrase “unless the articles otherwise provide” means, aside from an express statement in the articles that all or some of the Table 1 provisions are not altered automatically on an alteration of Table 1 by regulation.

If one of the provisions in Table 1 is altered by the company (that is, by a resolution under s. 259), which is specifically permitted by s. 261(3), then any subsequent amendments to Table 1 will not affect that altered provision (s. 261(4)).

[§8.05] Altering Restrictions on Businesses and Powers

If a company has restrictions on the businesses it can carry on or on the powers it can exercise, these restrictions must be contained in the articles of the company (s. 12(2)(a)). When the intention is to change, remove or create such restrictions, the articles of the company are altered.

The alteration (within the extended meaning of “alter” in s. 1(1)) of any restriction on the businesses carried on or to be carried on by a company, or on its powers, is not specifically provided for in the Act, and simply falls into the general provisions relating to altering the articles of a company. The required resolution will be determined under s. 259(1).

Section 260 provides that any shareholder may send a notice of dissent to the company in respect of a resolution to alter any restriction on the powers of the company or on the business it can carry on.

[§8.06] Exceptional Resolutions

The articles of a company can contain an exceptional resolution provision. This provision may specify that a particular provision of the notice of articles or of the articles of the company may not be altered or that the company or the directors may not take an action unless the resolution to authorize the alteration or the action is passed as an exceptional resolution (s. 264(1)).

An exceptional resolution, if to be passed at a general meeting, must be passed by a specified majority set out in the articles, and that majority must be greater than a special majority and, if to be consented to in writing, must be consented to in writing by all the shareholders holding shares that carry the right to vote at general meetings (see the definition of “exceptional resolution” in s. 1(1)).

An exceptional resolution provision in the articles cannot be varied or deleted unless the variation or deletion is itself authorized by an exceptional resolution (s. 264(2)).

The articles of a pre-existing company that has completed a transition rollover under s. 370(1)(a) and (b) or s. 436(1)(a) and (b) might include a provision that could not have been altered under the Company Act.

Where a pre-existing company has such a provision in its articles (after its transition rollover), the provision cannot be altered unless ordered by the court, or authorized by a unanimous resolution signed by all the shareholders of the company, whether or not their shares otherwise carry the right to vote (s. 264(3) and (4)).

[§8.08] Majorities—Conflicts Between Articles and Business Corporations Act

Section 265 provides that if a company is required or permitted under the Act or its articles to pass a resolution, and if there is a conflict between the Act and the articles regarding the majority of votes required to pass the particular resolution, the resolution must be passed by the greater of the majority of votes required by the Act and the majority of votes required by the articles.

[§8.09] Voluntary Change of Name

1. General

Section 263 contains the requirements of the Act relating to the voluntary change of the name of a company and to the adoption of, and the change of, any translation of the name of a company. This change will involve, primarily, an alteration of the notice of articles.

A translation of a company’s name is for use outside Canada only (s. 11(f)). The English form or French form (or a combined form) must be used for the actual name of the company (s. 25(1) and (2)) and it must be set out in the notice of articles (s. 11(b)) and the articles (s. 12(2)(c)(ii)). A translation of a company name must also be set out in the notice of articles in letters from the English alphabet (s. 12(2)(c)(iii) and Reg. s. 10).

2. Resolutions

Section 257 specifies the resolution (and other procedures) that is required in order to authorize an alteration to the notice of articles of a company to change its name or adopt or change any translation of its name (see s. 263(1)).

In the case of a change of the name of a company, the type of resolution is the type specified in the articles (s. 257(2)(b)(ii)) or, if none is specified in the articles, it is a special resolution (s. 257(2)(b)(iii)).

The resolution to adopt or change a translation of a company’s name may be a directors’ resolution or an ordinary resolution (ss. 257(2)(b)(i) and 263(2)).

3. New Name

The resolution to change a company’s name can authorize a change to three different types of name.

The first type is a name that is specifically referred to in the resolution (s. 263(3)(a)).

The second type is a name that is to be chosen by the directors (s. 263(3)(b)).

The third type is a name composed of the incorporation number of the company followed by “B.C. Ltd.” (or, in the case of an unlimited liability company, followed by “B.C. Unlimited Liability Company) (s. 263(3)(c)).

4. Reservation of Name

Unless the new company name is to be the name created by adding “B.C. Ltd.” after the incorporation number of the company, it must be reserved under s. 22 (see ss. 263(3)(a) and (b)).

If there is no reservation of the name existing at the date the change of name is to take effect, the notice of alteration is deemed to be withdrawn on that date and deemed not to have effected any alteration to the notice of articles contemplated by the notice of alteration (s. 263(4)).

There is no requirement to reserve a translation of a company name.

5. Filing with the Registrar

The company must file with the registrar a notice of alteration (s. 257(4)).

If the company is not in good standing, the registrar may refuse to accept any filing relating to the company (s. 411(1)). A company will not be in good standing if its annual reports are not filed up-to-date or if the information in the corporate registry shows that there is no director of the company.

After the alteration to the notice of articles takes effect, the registrar must give the company a certified copy of the notice of articles as altered, if requested to do so (ss. 257(6), 263(5)(a)(ii) and 263(6)(a)).

In addition, the registrar must issue and furnish to the company a certificate of change of name showing the change of name and the date and time the change took effect (s. 263(5)(a)(i)). The registrar does not issue a certificate in the case of an
adoption of, or a change of, a translation of a company’s name.

In addition, after a change of a company’s name (but again, not after an adoption or a change of a translation of a company’s name), the registrar must publish a notice of the change of name on a government website (s. 263(5)(a)(iii) and Reg. s. 6).

6. Withdrawal of Notice of Alteration

Section 258 provides for the withdrawal of a notice of alteration changing the name of a company or adopting or changing any translation of the name of a company (see above).

7. When Effective

Section 257(5) deals with the time at which an alteration to the notice of articles changing the name of a company or adopting or changing the translation of the name of the company takes effect (see §8.01.5).

8. Alteration of Articles

After an alteration to the notice of articles has taken effect under s. 257(5) to change the name of a company, the company must promptly alter its articles to reflect that change of name (and any translation of the new name) (s. 263(5)(b)).

Similarly, after an alteration to the notice of articles has taken effect under s. 257(5) to adopt a translation of the name of a company or change any translation of the name of a company other than to reflect the change of the name of the company, the company must promptly alter its articles to reflect that translation or the change of the translation of that name (s. 263(6)(b)).

Any such alteration to the articles does not require a resolution (s. 263(7)). See also, ss. 12(5)(b) and (6). Section 259 does not apply to a change of name or to an adoption or change of any translation of a name (s. 259(7)) and accordingly s. 257(3) does not apply.

9. Effect of Change of Name

A change of name, whether voluntary or involuntary, does not affect any of the rights or obligations of the company, nor does it render defective any legal proceedings by or against the company and any legal proceedings that may have been continued or commenced against the company under its former name may be continued or commenced against the company under its new name (s. 263(8)). The same comments apply to translated names.

10. Filings in Records Office

When the company’s name has been changed, the certificate of change of name issued by the registrar must be filed in the records office (s. 42(1)(a)).
Chapter 9

Capital Alterations

For further information on this topic, see Chapter 10 of the British Columbia Company Law Practice Manual, 2nd edition (Vancouver: CLEBC).

All legislative sections cited in this chapter and all references to the “BCA” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended, unless otherwise stated and references to the “Reg.” are to provisions of B.C. Regulation 65/2004, as amended.

[§9.01] Creation, Variation or Deletion of Special Rights or Restrictions

1. Alteration of Special Rights or Restrictions

A company may create and attach, or vary or delete, special rights or restrictions to the shares of any class or series of shares of the company, whether issued or unissued (s. 58(2)(a) and (b)). Special rights or restrictions may also be altered by court order.

If special rights or restrictions are altered under s. 58(2)(a) or (b) and any right or special right attached to issued shares is prejudiced or interfered with, then the consent, by a special separate resolution, of the holders of shares of that class or series will be required (s. 61).

In order to alter special rights or restrictions attached to shares, a company must alter its articles to reflect the creation, attachment, variation or deletion, as the case may be (s. 58(3)(b)). This means that s. 259(1), (4) and (5) (dealing with alterations of articles) applies. (See Chapter 8.)

Section 58(2)(a) could be used when new classes of shares are created and special rights or restrictions are to be attached to them. Note that it can also be used when a series of shares is created, although normally the directors do this under s. 60(1)(b). Similarly, s. 58(2)(b) could be used when a class or series is being cancelled and accordingly its special rights or restrictions are being deleted.

But the BCA contains specific provisions in s. 54(1)(a) and (b) permitting a company to create, and in s. 54(1)(j) to eliminate, a class or series of shares. This would almost invariably include the creation, or deletion, of special rights or restrictions (as well as an alteration to the notice of articles). It is not clear how s. 54(1)(a) and (b) and (j) and s. 58(2)(a) and (b) fit together in these circumstances (see below).

Section 58(2)(a) could also be used when an existing class (or series) of shares is acquiring additional special rights or restrictions. Similarly, s. 58(2)(b) could be used when existing special rights or restrictions are being varied.

2. Type of Resolution

The type of resolution required under s. 58(2) (and accordingly s. 259(1)) is the type of shareholders’ resolution specified by the articles, or, if the articles do not specify the type of resolution, a special resolution. This results in an anomaly in that under s. 58(2), the articles cannot specify a directors’ resolution but a directors’ resolution can effect changes under ss. 54(1)(a) and (b).

Any alteration of special rights or restrictions will require an alteration to the notice of articles because s. 11(h) requires that the notice of articles set out, in respect of each class and series of shares, whether there are special rights or restrictions attached to that class or series, and the date of each resolution (and court order) altering those special rights or restrictions.

In addition, if special rights or restrictions are being created or deleted as part of the creation or elimination, respectively, of a class or series of shares, the description of the company’s authorized share structure will have to be altered in the notice of articles (ss. 11(g) and 53).

Section 259(4) applies when these capital alterations are made. Consequently, the company must note on the resolution altering the articles that it does not take effect until the notice of articles is altered to reflect the alteration to the articles. The company must deposit that resolution (with the notation on it) at the company’s records office and then alter its notice of articles under s. 257 to reflect the alteration that was made to the articles.

The alteration to the notice of articles will require the filing with the registrar of a notice of alteration (s. 257(4)), and the alteration of the notice of articles, and therefore the alteration of the articles themselves (see s. 259(5)), will take effect as set out in s. 257(5). (See Chapter 8.)

§9.02 Interfering with or Prejudicing Class or Series Rights

Section 61 provides that a right or special right attached to issued shares must not be prejudiced or interfered with under the BCA, or under the notice of articles or articles, unless the holders of the particular class or series of shares consent. Such prejudice or interference may arise as a result of a resolution under s. 58 but it could arise in some other way as well.

Section 61 refers to “right or special right”. The term “special rights or restrictions” is defined in s. 1(1). “Right” is not defined but presumably means a right attached to all shares by operation of common law or the BCA, unless taken away by the articles and would include such things as the right to attend and vote at general meetings (see s. 173(1)), the right to participate in the distribution of assets on dissolution of the company, and the right to receive dividends.

The meaning of each of the words “prejudice” and “interfere” in s. 61 is not clear, although the phrase “unfairly prejudicial” has received some attention in cases under the equivalent of s. 227(2)(b). The words might be held to have a wider meaning than a variation or deletion of special rights or restrictions under s. 58 that is detrimental to that particular class (or series) of shares. For example, it is not clear if creating a new class of shares that ranks ahead of an existing class with special rights or restrictions under s. 58, some English cases dealing with similar, but not identical, language have drawn a distinction between a variation of a right or special right attached to a share and some act that is not such a variation but merely affects the enjoyment of that particular right or special right. The courts have held that only the former situation gives remedies to an aggrieved shareholder. This distinction has been followed in at least one British Columbia case (Re Trend Management Ltd. (1977), 3 B.C.L.R. 186 (S.C.), following Greenhalgh v. Arderne Cinemas Ltd., [1946] 1 All E.R. 521 (C.A.) and White v. Bristol Aeroplane Co. Ltd., [1953] 1 All E.R. 40 (C.A.)).

If it is decided that a particular act (such as a resolution under s. 58) may prejudice or interfere with a right or special right attached to a class or series of issued shares, the consent of the shareholders of that class or series must be obtained under s. 61.

This consent requires a special separate resolution (defined in s. 1(1)) of that particular class or series.

In addition to the consents required under the BCA, care should be taken to comply with any provisions in the articles that require consents of holders of shares of a particular class or series if their special rights or restrictions are being altered or affected, or if preferential rights are being given to shares of a different class, or in any other circumstances which may apply. The wording of the particular paragraph in the articles is usually different from that in s. 61 and very often can lead to a situation in which no class or series consent is required under the BCA but consent is required under the articles.

§9.03 Series of Shares

1. Creation of Series

The special rights or restrictions attached to the shares of a class of shares may provide that the class includes or may include one or more series of shares (s. 60(1)(a)).

The distinctive element of a series of shares so permitted by the class special rights or restrictions is that the directors, by resolution, can

- determine the maximum number or that there is no maximum number of shares of the series or alter any such determination, and authorize the alteration of the notice of articles accordingly (s. 60(1)(b)(i)),
- alter the articles and authorize the alteration of the notice of articles to create an identifying name for the shares of the series, or alter any such identifying name (s. 60(1)(b)(ii)), and
- alter the articles and authorize the alteration of the notice of articles to attach special rights or restrictions to the shares of the series, or alter any such special rights or restrictions (s. 60(1)(b)(iii)).

Note that the authority for the directors must be in the special rights or restrictions attached to the particular class of shares of which the particular series of shares forms a part.

Series shares give flexibility by allowing the directors to set such things as dividend rates or redemption rates for shares, without the time and expense of calling an extraordinary general meeting of shareholders to create these particular special rights or restrictions by creating a new class of shares.
In such a case, an alteration of the notice of articles and the articles can be carried out simply by a resolution of the directors. Even so, ss. 257 and 259 will apply (see Chapter 8), as might s. 61 (see §9.02).

The rights of the directors under s. 60(1)(b) are in addition to the rights of shareholders under the _BCA_ to authorize or make the same alterations, determinations and authorizations with respect to shares if those shares are part of a class whose special rights or restrictions provide for one or more series of shares of the class (s. 60(2)).

A series of shares can also be created by a resolution under s. 54(1)(b) and at the time of incorporation (or other recognition of the company (s. 52(1)(b)). Again, the special rights or restrictions of the class of which the series is a part must provide for series (s. 52(1)(b)).

In the case of a creation of a series of shares by resolution under s. 54(1)(b), see §9.01 with respect to the anomaly between s. 54(1)(a) (which would also apply with respect to s. 54(1)(b) and (j)) and (3) and s. 58(2).

2. Safeguards

Certain safeguards are built into the series of shares concept, requiring rateable payment of cumulative dividends and return of capital (s. 60(7)) and prohibiting one series from having priority over another series of the same class with respect to dividends and a return of capital (s. 60(6)).

Every share in a series of shares must have attached to it the same special rights or restrictions as are attached to every other share of that series. In addition, the special rights or restrictions attached to the shares of a series must be consistent with the special rights or restrictions attached to the shares of the class of shares of which the series is a part (s. 60(4)).

If shares of a particular series are issued, the maximum number (if any) of shares of the series which can be issued and the identifying name of and the special rights or restrictions attached to the series (and the concurrent alterations of the articles and notice of articles) may be altered, authorized or determined only by the type of shareholders’ resolution specified by the articles or, if not so specified by the articles, by a special resolution, and such changes cannot be made by a directors’ resolution (s. 60(3)). If none of the shares of the particular series created under s. 60(1)(b) are issued, the directors can make such changes (s. 60(1)(b)), as well as the shareholders.

[§9.04] Changes in Authorized Share Structure

Section 54(1) sets out a lengthy list of permitted changes to the authorized share structure and the shares of a company. At the end of the list there is a catch-all permitting the company to otherwise alter its authorized share structure or shares when required or permitted to do so by the _BCA_ (s. 54(1)(n)).

1. Classes and Series of Shares

Section 54(1)(a) and (b) permits a company to create one or more classes of shares and one or more series of shares. In the case of series of shares, this is in addition to the rights given to directors to create series of shares under s. 60.

Similarly, s. 54(1)(j) permits a company to eliminate any class or series of shares, provided that none of the shares of the class or series are allotted or issued.

Note the anomaly mentioned at §9.01 regarding these sections and s. 58(2).

2. Maximum Number of Shares

Section 54(1)(c) permits a company to reduce the maximum number of shares that the company is authorized to issue out of any class or series of shares.

Section 54(1)(c) also permits the increase of the maximum number of shares that a company is authorized to issue out of any class or series of shares, and the total elimination of that maximum number of shares, in which case an infinite number of shares of the particular class or series can be issued. If a series of shares is to have no maximum number, the same should apply to its class.

Section 54(1)(d) permits a company to establish a maximum number of shares that the company is authorized to issue out of any class or series of shares, where no maximum number for that class or series is established at the time.

3. Subdivision of Shares

Under s. 54(1)(e) and (f), a company may subdivide its shares.

Any unissued or fully paid issued shares _with par value_ can be subdivided into a greater number of shares with a smaller par value (s. 54(1)(e)). The product of the number of shares multiplied by their par value must be the same before and after the subdivision (s. 54(2)).

Any unissued or fully paid issued shares _without par value_ can be subdivided into any greater number of shares without par value (s. 54(1)(f)).
If not all the par value shares of a class are being subdivided then two separate classes will be necessary (with different identifying names), because all par value shares in a class must have the same par value (s. 52(2)).

It is not possible to subdivide a series of par value shares without subdividing the whole class or turning the series into a separate class (which would probably require revising the special rights or restrictions attached to the shares).

4. Consolidation of Shares

The opposite of a subdivision of shares is a consolidation. Under s. 54(1)(g) and (h) a company may consolidate its shares.

Any unissued or fully paid issued shares with par value can be consolidated into a smaller number of shares with a larger par value (s. 54(1)(g)) and, again, the product of the number of shares multiplied by the par value must be the same before and after the consolidation (s. 54(2)).

Any unissued or fully paid issued shares without par value can be consolidated into any smaller number of shares without par value (s. 54(1)(h)).

As with a subdivision, if not all the par value shares of a class are being consolidated, two classes will be necessary (with different designations), because all par value shares in a class must have the same par value (s. 52(2)).

It is not possible to consolidate a series of par value shares without consolidating the whole class, or turning the series into a separate class (which would probably require revising the special rights or restrictions attached to the shares).

5. Par Value Shares

Section 54(1)(i)(i) permits a company to decrease the par value of any of its shares with par value. The section specifically states that this is subject to s. 74 (reduction of capital; see §9.05).

Section 54(1)(i)(i) covers both unissued and, subject to s. 74, issued par value shares.

Section 54(1)(i)(ii) permits a company to increase the par value of any of its shares, provided that none of the shares of that class of shares are allotted or issued. The language of s. 54(1)(i) seems to contemplate the change being made to all the shares of the class, and this fits with s. 52(2).

Par values do not have to be in Canadian currency (s. 52(3)), so s. 54(1)(i) would also apply to foreign currency par values. There is no provision for changing par values from one currency to another.

6. Change of Shares

A company may change any unissued or fully paid issued shares with par value into shares without par value (s. 54(1)(k)) and may change any unissued shares without par value into shares with par value (s. 54(1)(l)).

Shares without par value can only be changed into shares with par value if they are unissued. Issued shares with par value can only be changed into shares without par value if they are fully paid.

Each class of shares must consist of shares of the same kind. If they are par value shares they must all have the same par value (s. 52(2)).

7. Alteration of Identifying Name of Shares

The identifying name of any shares, whether issued or unissued, may be altered (s. 54(1)(m)).

The identifying name of shares should not be misdescriptive of the characteristics of the shares; for example, if part of the name is the word “preferred” then the shares should be preferred over other classes of shares of the company in some respect.

Because s. 58(4) permits different classes and series of shares to have identical special rights or restrictions, the identifying names of classes (or series) might be the only distinction between them.

8. Procedure

The procedure for a company to carry out any of the capital alterations under s. 54(1) will be determined by s. 54(3), which divides the changes into three categories.

(a) Alteration of notice of articles

If the capital alteration will make information reflected in a company’s notice of articles incorrect or incomplete, the notice of articles must be altered to reflect that change (s. 54(3)(a)).

When only the notice of articles is being altered, s. 257(2), (4), (5) and (6) applies (see Chapter 8). These subsections set out the type of resolution required, the filing requirements with the registrar, when the alteration takes effect, and the registrar’s duties (see Chapter 8).

(b) Alteration of notice of articles and articles

When the effect of a change under s. 54(1) would render information in both the articles and the notice of articles incorrect or incomplete, then that change must be effected by altering both the notice of articles and the
articles to reflect the change (s. 54(3)(b)).

For any such alteration, s. 257(2) to (6) and s. 259(1), (4) and (5) apply with respect to the types of resolutions required, filings with the registrar and when the changes take effect (see Chapter 8).

(c) No alteration to notice of articles

Section 54(3)(c) deals with cases in which a change contemplated by s. 54(1) has no effect on the information in the notice of articles of a company. In such a case, the type of resolution required is that specified by the articles or, if the articles do not specify the type of resolution, a special resolution (s. 54(3)(c)).

The resolution will presumably be effective at the time it is passed or at such later date and time as is specified in it; there is nothing specifically covering this situation in the BCA.

In the unlikely event that some kind of alteration under s. 54(1) might alter the articles, but not have any effect on the notice of articles, s. 259(6) would apply.

[§9.05] Reduction of Capital

A company may reduce its capital in any way by a special resolution, provided that the capital is reduced to an amount that is not less than the realizable value of the company’s assets less its liabilities (s. 74(1)(b)).

If it is reduced below that amount, the reduction of capital requires court approval (s. 74(1)(a)). Court approval is still an option even if the capital is not reduced below that amount (s. 74(1)(b)). Presumably, the application for court approval could be authorized only by directors’ resolution, although it may be helpful, in some circumstances, to be able to advise the court that some level of shareholder approval had been obtained.

[§9.06] Exceptions to Reduction of Capital Requirements

Section 75 permits certain reductions of capital and cancellations of shares without, where otherwise applicable, the requirement for the special resolution or court order on a reduction of capital under s. 74(1). In addition, a company can do these particular reductions and cancellations without having to change the company’s authorized share structure (s. 75).

Any of the enumerated acts in s. 75 may be done whether or not there is any provision relating to them in the memorandum or articles of the company. However, if there are any such provisions, then the company can only do the acts on the terms and in the manner provided in the memorandum or articles (s. 75). The reference to the memorandum is only applicable with respect to pre-existing companies that have not done a transition rollover.

The particular acts that a company may do without a special resolution or court order under s. 74(1) and without changing its authorized share structure are:

1. the redemption or purchase of shares in the normal manner under s. 77, or under s. 227(3)(g) (the oppression remedy), or under Division 2 of Part 8 (the dissent remedy) (s. 75(a));
2. the acceptance of a surrender of shares by way of gift or for cancellation (s. 75(b));
3. the conversion of fractional shares into whole shares in accordance with s. 83, either on a subdivision or consolidation of shares under s. 54(4) (s. 75(c)(i)) or on a redemption, purchase or surrender referred to in paragraphs (1) and (2) above (s. 75(c)(ii)).

Section 75(c)(i) provides that a conversion of fractional shares into whole shares on a subdivision or consolidation under s. 54(4) does not require that the authorized share structure of the company be changed. However, it is possible that in very limited circumstances a consolidation or subdivision could push the number of issued shares over the maximum number of shares of the particular class or series which the company is authorized to issue. It would probably be necessary in this case to increase (or eliminate) that maximum number under s. 54(1)(c).

[§9.07] Concurrent Alterations of Authorized Share Structure and Shares

If a company proposes two or more alterations to its authorized share structure or shares the Shareholders’ authorizations for the alterations required or permitted by the BCA or the articles may be expressed in one resolution and the consents or authorizations of a class or series may be expressed in one separate resolution of the class or series (s. 55(1)). This does not apply to directors’ resolutions and each alteration to a company’s authorized share structure or shares must be approved by a separate directors’ resolution (see ss. 257(2)(b)(ii), 259(1)(b) and 60(1)(b)).

If the shareholders’ resolutions required to authorize particular alterations have different majorities under the BCA and under the articles, s. 55(2) provides that the single shareholders’ resolution under s. 55(1) must be passed by the highest required majority of authorizing or consenting votes of the various resolutions.

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FOR FURTHER INFORMATION ON THESE TOPICS, SEE CHAPTER 11 OF THE BRITISH COLUMBIA COMPANY LAW PRACTICE MANUAL (VANCOUVER: CLEBC)
Chapter 14

Dissolution

For further information on this topic, see Chapter 12 of the British Columbia Company Law Practice Manual, 2nd edition (Vancouver: CLEBC).

All legislative sections cited in this chapter and all references to the “BCA” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended, unless otherwise stated. References to “Reg.” are to provisions in B.C. Regulation 65/2004, as amended.

§14.01 Dissolution by Registrar for Failure to Comply

1. Introduction

Section 422(1) provides that the registrar may dissolve a company or cancel the registration of an extraprovincial company when the company or extraprovincial company:

(a) has for two consecutive years failed to file with the registrar its annual report or any other record as required by the BCA or any predecessor act;

(b) fails to comply with an order of the registrar, including an order to change its name or assumed name;

(c) fails, without reasonable excuse, to return an erroneous record to the registrar within 21 days after a request under s. 420(1);

(d) tenders a cheque for fees under s. 431 which is dishonoured;

(e) in the case of a pre-existing company, fails to observe the transition provisions in s. 370 or s. 436; or

(f) in the case of an extraprovincial company, fails to ensure it has an attorney for service under s. 386 or breaches an undertaking to use an assumed name under s. 26(2).

2. Procedure

The registrar first sends a letter informing the company of its failure to comply with the BCA and of the registrar’s powers of dissolution, or, when an extraprovincial company, of cancellation of its registration (s. 422(2)).

If, within one month after the date of the letter, the registrar does not receive a response indicating that the failure has been, or is being, remedied or an otherwise satisfactory response, the registrar publishes a notice on a government website (Reg. s. 6) that the company will be dissolved or, in the case of an extraprovincial company, that its registration will be cancelled, at any time after one month from the date the notice is published unless:

(a) “cause to the contrary is shown” (s. 422(4)(b)(i));

(b) the company or extraprovincial company satisfies the registrar that it is not in default, that the default has been remedied or that all reasonable steps are being taken to remedy the default (s. 422(4)(b)(ii)); or

(c) a copy of an entered court order to the contrary is filed with the registrar (s. 422(4)(b)(iii)).

Failing those exceptions, the registrar may dissolve the company or cancel the registration of the extraprovincial company at any time after the one month from publication of the notice (s. 422(5)), at which point the company is dissolved or, in the case of an extraprovincial company, its registration is cancelled. Another notice is then published indicating that the company has been dissolved (s. 424 and Reg. s. 6).

3. “Letting it Die”

Having the company dissolved for a failure to comply with the BCA is often used as an inexpensive form of dissolution when the company has no assets or liabilities. The company simply fails to file annual reports, and then at any time after two years, two months and one day after the effective date of the last filed annual report, the company can be dissolved as set out above. The same result will happen when a pre-existing company fails to carry out a mandatory transition rollover within the required time.

Similarly, the registrar will cancel the registration in British Columbia of an extraprovincial company for failure to file annual reports in such a situation (s. 422(1)(a)). There is no practical reason for adopting this method of cancelling registration,
however, as the same result can be achieved by simply sending a notice to the registrar that the company has ceased to carry on business in British Columbia (s. 397(b)).

It may be inappropriate to counsel a client not to file annual reports, or do a mandatory transition rollover, in order to be dissolved, because that is counselling the client to disobey a statute. Nevertheless, it is fairly common for a lawyer to point out the option of letting the company die.

The BCA requires the annual reports to be filed and the mandatory transition rollover to be done, and, in the case of annual reports, the failure gives rise to certain penalties.

Furthermore, when a company does have some assets at the time of its dissolution those assets will vest in the government in accordance with s. 4(1) of the Escheat Act (in the case of land) or s. 344(2) of the BCA (in the case of other assets).

If a company is to be “allowed to die” it may be prudent to use a simple form of conveyance to transfer all assets to the shareholders with a power of attorney to survive the dissolution.

[§14.02] Dissolution by Request

1. Introduction

Also known as “short-form dissolution”, dissolution by request under s. 314 is generally used when all the company’s debts and liabilities have been paid or discharged or adequately provided for or when the assets of a subsidiary have been transferred or “rolled” into its parent, often under the Income Tax Act. A company having significant assets or liabilities may need to use the liquidation provisions of ss. 319 to 343, also called “long-form dissolution”. This is often the case with large or active businesses.

Section 313 limits all dissolution and liquidation proceedings to solvent companies. When a company is unable to pay its debts as they come due and wants to dissolve, the directors should either make adequate provision for the payment of each of its liabilities (see §14.02.2(b)), or proceed under one of the available statutes for insolvent persons. (See §14.01 for ethical concerns about counselling a client to simply allow a company to die for failing to file returns.) When a company is found to be insolvent under the Bankruptcy and Insolvency Act, any dissolution proceedings under the Business Corporations Act must be stayed (s. 313). After the assets of a company have been liquidated and distributed under the Bankruptcy and Insolvency Act or the Winding-up and Restructuring Act, the company will still exist and can only be dissolved by action taken in accordance with the procedures of the Business Corporations Act.

2. Procedure

(a) Required steps

A company can be dissolved in a short-form dissolution if it

(i) passes an ordinary resolution authorizing it to be dissolved (s. 314(1)(a)), and

(ii) files with the registrar an application for dissolution containing a statement that an affidavit complying with s. 316(2) and sworn by a director has been obtained and deposited in the company’s record office (s. 316(1)(b)).

Section 314(2) permits a company that has not issued any shares to be dissolved if it is authorized to do so by a directors’ resolution rather than an ordinary resolution.

Special resolutions authorizing the dissolution are also acceptable (because a special resolution by definition is also an ordinary resolution).

When the company has remaining assets to be distributed, a special resolution should be passed because of s. 301, if not exempted by ss. 301(6)(d) or (f). Note that this special resolution gives rise to a right of dissent (s. 301(5)) and note the requirements of s. 240.

The company must be in good standing at the time the application for dissolution is filed.

Upon filing the application for dissolution, the registrar publishes a notice on a government website (Reg. s. 6) and issues a certificate of dissolution showing the date and time of dissolution, and furnishes a copy of the certificate to the applicant and to the person required under s. 351 to retain the records of the company (s. 345).

(b) The affidavit

The person swearing the affidavit must be a current director of the company (s. 316(1)(a)).

The wording of the affidavit must follow s. 316(2) and must state that:

- the company’s dissolution has been duly authorized in accordance with s. 314(1)(a) or (2), as the case may be;
• the company has no assets; and
• the company has no liabilities as a result of s. 315(6) or otherwise, or has made adequate provision for the payment of each of its liabilities.

When a director cannot swear such an affidavit, the longer liquidation procedures should be followed.

A debt or liability that has been assumed by a third party, without the consent of the original creditor in the form of either a novation or a release in favour of the company, remains a debt or liability for the purposes of the affidavit. Without such a release or novation, it is not possible to swear an affidavit that the company has no liabilities in those circumstances.

This problem has been addressed in s. 316(2)(c)(ii), which permits the director to swear an affidavit that the company has made adequate provision for the payment of each of its liabilities. Presumably, this would include the assumption of the company’s liabilities by a financially healthy parent company.

(c) Documentation

Various instruments are required to transfer assets when registration is required, such as a Form A freehold transfer for real property, a bill of sale for goods not in possession, motor vehicle transfer forms and so on. In addition, there should be an assumption and distribution agreement or general conveyance agreement assigning the assets of the company to the shareholder or shareholders. The party assuming liabilities should be careful not to inadvertently assume liabilities for which it would not otherwise be responsible. Often the purpose of dissolution is to leave behind a failed company, and having another party assume its liabilities may defeat this purpose. However, this raises the question of whether the affidavit can comply with s. 316(2)(c)(ii) (see above).

(d) Surviving power of attorney

Using an agreement with general assignment language will avoid the problem of unknown or forgotten assets being forfeited to the government. One of the most important provisions in such an agreement is the grant of an irrevocable power of attorney coupled with an interest from the dissolving company to the parent company or its president, or to a shareholder (if the dissolving company is not a subsidiary) to file all necessary tax returns and elections and to do and execute all acts and transfers necessary to complete the assignment of the assets to the recipient. Otherwise, because the company does not exist, it cannot execute documentation. Note the requirements of the **Power of Attorney Act**.

(e) Indemnifying directors and officers

It is frequently desirable to have the parent company (if it has the power and capacity) of a dissolving subsidiary agree to indemnify the officers or directors of the subsidiary for liabilities related to their acting to dissolve the company, including with respect to income taxes.

3. Extraprovincial Companies

A foreign entity that wants to have its registration as an extraprovincial company cancelled can simply file with the registrar a notice of ceasing to carry on business in British Columbia (s. 397(b)). Alternatively, the extraprovincial company may simply stop filing annual reports (but see §14.01.3 with respect to counselling this), in which case its registration will eventually be cancelled by the registrar under s. 422(1)(a).

The registrar will also cancel the registration of an extraprovincial company if he or she receives notice from the registrar (or equivalent authority) of the foreign entity’s jurisdiction that the foreign entity has ceased to exist (s. 397(a)). The registrar cannot dissolve an entity that has been incorporated in another jurisdiction; it can only cancel the registration of the extraprovincial company in British Columbia.

[§14.03] Voluntary and Court Ordered Liquidation

1. Introduction

Liquidation is the process by which a company with assets and liabilities is “wound up”, as its debts and liabilities are satisfied, and any remaining assets distributed to the shareholders, following which the company is dissolved.

The liquidation process can be voluntary or under a court order. The shareholders of the company initiate a voluntary liquidation; a court may order liquidation on application of any one of a number of “appropriate” persons.
For the most part, the process of liquidation is the same regardless of whether the liquidation is voluntary or court ordered. The same powers and responsibilities are attached to the role of the liquidator, for instance.

See §14.02.1 with respect to insolvent companies.

2. Voluntary Liquidation

(a) Introduction

Voluntary liquidation under Division 3 of Part 10 is used when the company to be dissolved has extensive debts and liabilities, not all of which may be known at the commencement of proceedings. In contrast to dissolution by request, a company can be fully “wound up”, even if it has assets that have not been distributed or debts that have not been paid.

(b) Special resolution and shareholders’ meeting

A voluntary liquidation begins with a special resolution resolving to liquidate the company (s. 319(1)). For a voluntary liquidation, “commencement of the liquidation” is defined in s. 312 as the later of the time and date that the special resolution is passed, and the time and date specified in the special resolution (or, if no time is specified, the beginning of the date specified).

(c) Appointment of liquidator

At the shareholders’ meeting (or in a consent resolution in writing), the shareholders also appoint (by ordinary resolution) a liquidator to liquidate the company and distribute the company’s assets (s. 319(2)).

The liquidator must be someone who is qualified to be a receiver or receiver-manager under s. 64(2) of the Personal Property Security Act; although when all the shareholders of the company give their written consent, a person mentioned in s. 64(2)(e) of the Personal Property Security Act (an insider or auditor of the company or of an affiliate) is qualified to be the liquidator (s. 327(1)).

No act of a liquidator is invalid merely because of any defect in the liquidator’s appointment or qualifications (s. 328).

The company must, promptly after the resolutions to liquidate and appoint a liquidator are passed, file with the registrar a statement of intent to liquidate (s. 321(1)). Unless the liquidator’s appointment is reflected in a filed statement of intent to liquidate, the liquidator must file with the registrar a notice of appointment within 10 days of the commencement of the liquidation (s. 329(1)(a)), or “promptly” if appointed after such commencement (s. 329(1)(b)).

(d) Notices

The liquidator must publish, promptly after the commencement of the liquidation (s. 330(a)), a notice in the Gazette, and in a newspaper that is distributed generally where the company has its registered office, that the company is in liquidation (s. 331(1)(a)). The notice must require any person:

- indebted to the company to pay the amount owing to the liquidator (s. 331(2)(a)),
- having custody or control of any property, rights or interests of the company to deliver them, or provide control of them, to the liquidator (s. 331(2)(b)),
- with a claim against the company to provide particulars to the liquidator within two months after the date of publication in the Gazette (s. 331(2)(c)).

The liquidator must also, promptly after publishing the notice of liquidation, send a notice to the last known address of each known creditor (s. 331(1)(b)). The notice must also be sent to any creditor of whose claim the liquidator becomes aware within two months after the date on which the notice was published in the Gazette (s. 331(4)).

The notice must disclose that the company is in liquidation and must include:

- a statement of the amount, if any, that the liquidator in good faith accepts is owing by the company to the particular creditor;
- a statement that the liquidator will provide to that recipient a list of all the company’s known creditors and amounts the liquidator accepts are owing to them; and
- a statement that the recipient of the notice has four months from the date of publication of the notice in the Gazette to pursue any claim for money owed by the company in excess of the amount stated in the notice (s.331(3)).
(c) Limits on claimants

Section 332(1) limits those who may claim against a company in liquidation or against its liquidator, unless the court orders otherwise (s. 332(1)(d)), to:

- those in receipt of notices;
- those to whom the liquidator refused or neglected to send a notice; or
- persons who provide written notice of their claim to the liquidator within two months of the notice published in the Gazette and to whom the liquidator refuses or neglects to send a notice under s. 331(4).

Creditors in receipt of notices must not claim amounts greater than those specified in the notice unless they bring legal proceedings to dispute the specified amount, or persuade the liquidator that a greater amount is owing to them, within four months after the publication of the Gazette notice, unless the court orders otherwise (s. 332(2)).

(f) Powers and duties of liquidator

(i) general

The liquidator must take into the liquidator’s custody or control the company’s property, rights and interests of the company (s. 330(b)) and must:

- dispose of the assets of the company other than assets to be distributed in kind to the shareholders (s. 330(d));
- invest money in investments approved for trustees pending distribution to creditors and shareholders (s. 330(h)); and
- after paying or providing for all liabilities, distribute the remaining assets in money or in kind among the shareholders according to their rights and interests in the company (s. 330(m)).

(ii) keeping records

The liquidator must keep proper records of all matters relating to the liquidation (s. 330(e)). The liquidator must indicate that the company is in liquidation on every invoice, order for goods and business letter issued by the liquidator or on which the name of the company appears (s. 330(f)) and use the designation of “liquidator” on any record on which the liquidator’s name appears (s. 330(g)).

The liquidator must file with the registrar an annual liquidation report instead of an annual report for the company (s. 330(k)).

The liquidator must also take into his or her custody or control the company’s corporate records (s. 330(b)(i)) and other records (s. 330(b)(ii)), and ensure that the corporate records are maintained and made available as required under Division 5 of Part 2 of the BCA (s. 330(e)).

The liquidator must establish a liquidation records office (s. 333(1)) in British Columbia (s. 333(2)) where certain records relating to the liquidation will be retained and where access to such records may be made available during statutory business hours.

(iii) managing the company

The liquidator has very broad powers to manage or supervise the management of the company and to exercise those of its powers not required to be exercised by the shareholders (s. 334(1)(a) and (b)). The powers of the directors and officers cease on appointment of the liquidator except to the extent that the liquidator approves their continuation (s. 334(1)(a)).

(iv) cease carrying on business

The company must cease carrying on business after the commencement of the liquidation except to the extent that the liquidator considers necessary or advisable for the liquidation (s. 340(2)). When the company is carrying on business during the liquidation, the liquidator must produce financial statements for the company at least once every 12 months (s. 330(j)).

(v) recovery of property

Any past or present director, receiver, receiver-manager, officer, employee, banker, auditor, shareholder, beneficial owner of shares or agent of a company in liquidation, or of any its affiliates, must deliver any property of the company in that person’s custody or control to the liquidator and must also provide full disclosure to the liquidator with respect to any such property, or property which has
been disposed of by the company, except any disposed of in the ordinary course of business of the company (s. 335 (1)).

(vi) distributing assets

A liquidator may distribute assets of the company to the shareholders in kind, or may exchange all or substantially all those assets for securities of another corporation, which the liquidator will then distribute to the shareholders (s. 336(1)).

(vii) preparing accounts

Accounts of the liquidation, showing how it has been conducted and the disposition made of the company’s assets, must be prepared at least once in every 12-month period after the appointment of the liquidator, and whenever directed by the court or (in a voluntary liquidation) an ordinary resolution. They must also be prepared at two stages of the liquidation: before the liquidator pays or makes provision for the liabilities of the company, and promptly after making such payment or provision but before distributing the assets of the company to shareholders (s. 338(1)).

(viii) when a creditor or shareholder cannot be located

When the whereabouts of a creditor or a shareholder are unknown, s. 337 provides a mechanism whereby the liquidator may, after making reasonable efforts to determine the whereabouts of the creditor or a shareholder, pay or deliver amounts or property due to that party to the administrator under the Unclaimed Property Act.

(g) Powers of shareholders in voluntary liquidations

The shareholders can restrict the power of the liquidator by requiring shareholder approval of certain matters (s. 320(1)).

The shareholders also have the power to remove the liquidator by a special resolution passed at a general meeting, if notice has been given to the liquidator and to each creditor whose unpaid claim exceeds $1,000 (s. 322(1)(b) and Reg. s. 24). Given the use of the words “passed at a general meeting”, a consent resolution is probably insufficient.

A vacancy in the office of a liquidator may be filled by an ordinary resolution or by the directors if they have been authorized to do so by an ordinary resolution (s. 322(3)).

(h) Reversing a voluntary liquidation

At any time after a statement of intent to liquidate is filed and before the company is dissolved, the company, or any other person who appears to the registrar to be an appropriate person to do so, may file a notice of withdrawal and thereby withdraw the statement of intent to liquidate (s. 323).

(i) Completion of liquidation

Within three months after all the assets of the company have been distributed to the shareholders, the liquidator must prepare final accounts showing how the liquidation has been conducted and how the assets of the company have been disposed of (s. 341(1)(a)). The liquidator must deposit those accounts in the liquidation records office and send a notice to the shareholders informing them that they may inspect and receive a copy of the final accounts for a period of at least three months from the date of the notice (s. 341(1)(b) and (c)). The liquidator must not apply for dissolution of the company until that three-month period has expired (s. 341(3)).

Before distributing assets to shareholders, the liquidator should obtain the usual statutory clearance certificates (for example, Income Tax Act, Canada Pension Plan, Social Service Tax Act, Employment Insurance Act and so on).

Promptly after the expiry of the three-month period during which shareholders may inspect the final accounts, the liquidator must file with the registrar an application for dissolution stating that the final accounts have been prepared and deposited in the liquidation records office and, in the case of a court ordered liquidation, that a copy of an entered order under s. 342 approving the dissolution of the company has also been deposited in the liquidation records office (s. 343).

In the case of voluntary liquidation, the company will be dissolved on the beginning of the day one month after the date on which the application for dissolution is filed with the registrar (s. 343(2)(b)). In the case of a court ordered liquidation, the company will be dissolved when the application is filed, or on any later date (and time, if any) specified in the
application (s. 343(2)(a)). The court may defer this date (s. 343(3)).

(j) Changes with respect to liquidators

A liquidator who ceases to act must file a notice of ceasing to act as liquidator with the registrar within seven days (s. 329(1)(d)).

(k) Remunerating the liquidator

The shareholders may by ordinary resolution either set or authorize the directors to set the remuneration for each liquidator appointed in a voluntary liquidation (s. 319(2)(b) and s. 322(5)).

Section 326 provides that the court must set the remuneration of a liquidator appointed by the court.

3. Court Ordered Liquidation

A court ordered liquidation may be initiated by an application made by the company, a registered or beneficial shareholder, a director or any other person (including a creditor of the company) whom the court considers an appropriate person to make such an application (s. 324(1)).

The court may order that a company be liquidated and dissolved if an event occurs which triggers liquidation according to the memorandum or articles of the company, or if the court otherwise considers it “just and equitable” to order the liquidation and dissolution of the company (s. 324(1)(a) and (b)).

When the court makes such an order, it must, in that order, appoint one or more liquidators (s. 324(4)). The appointment of the liquidator takes effect on the commencement of the liquidation (s. 324(5)), which is the date of the liquidation court order, or the later date (and time, if any) specified in the order (s. 312).

The liquidator’s responsibilities under a court ordered liquidation are substantially the same as under a voluntary liquidation. Many of the provisions of the BCA governing liquidation (and most of the above comments) apply to both a court ordered and a voluntary liquidation. Some of the differences have been mentioned above, and others are:

- a court ordered liquidation cannot be discontinued without a court order under s. 325(3)(v);
- if a court appointed liquidator is not qualified to act, the liquidator is not required to resign but instead must seek directions from the court (s. 327(2)(b)); and
- a court appointed liquidator must obtain a court order approving the dissolution (s. 342(1)).

4. Dissolution Following Liquidation

As mentioned, a liquidator appointed by the court must, before applying for dissolution of the company, obtain an order of the court approving that dissolution (s. 342). No court approval is required for dissolution in a voluntary liquidation.

In addition s. 342(3) specifies that the court may order that the liquidator be discharged effective on the dissolution of the company or at any other time the court orders. A liquidator in a voluntary liquidation can be discharged by a court order under s. 350(1). The order discharges the liquidator from all liability in respect of any act or default of the liquidator (ss. 342(3) and 350(3)). The liquidator’s liabilities, if any, will survive the dissolution (s. 347), unless the liquidator’s liabilities are discharged by the order.

After dissolution, the registrar must issue a certificate of dissolution and furnish a copy to each liquidator, and publish a notice of the dissolution (s. 345).

[§14.04] Post-Dissolution Matters

1. Survival of Liabilities

Proceedings may be continued against a company after its dissolution or brought against a company within two years after its dissolution as if the company had not been dissolved (s. 346 (1)).

Section 347 provides that subject to ss. 348(2) and (4) and 350(3), the liability of every director, officer, liquidator and shareholder of a dissolved company shall continue and may be enforced as if the company had not dissolved.

When assets of the company are distributed to a shareholder in anticipation of, during, or as a result of the company’s liquidation or dissolution, the court may add the shareholder as a party to litigation, determine the amount for which the shareholder is liable and the amount the shareholder must contribute to satisfaction of the plaintiff’s claim and direct payment of those amounts (s. 348(1)), provided that the shareholder is not liable unless added as a party within two years after the date of dissolution (s. 348(2)). The shareholder’s liability is limited to the value of the assets he or she received, as at the date of
distribution (s. 348(4)).

It is usually advisable for all the officers and directors to resign well in advance of dissolution. When a company is restored and persons have not resigned, they are also reinstated in their respective roles as officers and directors.

2. Recordkeeping

Sections 351 to 353 establish how the records of a dissolved company required under s. 42 and, if a liquidator was appointed, of the liquidation required under s. 333(1), are to be maintained and how one may obtain access to them.

The person responsible for the records will be the person shown in the application for dissolution as having custody of the records (s. 351(2)(a)(i) and (b)), or if there was no application for dissolution, the person responsible will be whoever had custody of the records at the time of dissolution (s. 351(2)(a)(ii).

The records must be retained for two years or until the expiration of any shorter period the court orders (s. 351(2) and Reg. s. 25).

The obligation to retain the records includes the requirement that the records be made available for inspection during statutory business hours by any person who would have been entitled to inspect the company’s records before dissolution (s. 352). A party entitled to inspect the records is also entitled to a copy of any of them.
Chapter 15

Restoration

For further information on this topic, see Chapter 12 of the British Columbia Company Law Practice Manual, 2nd edition (Vancouver: CLEBC).

All legislative sections cited in this chapter and all references to the “BCA” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended, unless otherwise stated. References to “Reg.” are to provisions in B.C. Regulation 65/2004, as amended.

§15.01 General

1. Introduction

The registrar can restore a dissolved company or the registration of an extraprovincial company whose registration has been cancelled (s. 356). The court can order that a dissolved company, or the registration of an extraprovincial company whose registration has been cancelled, be restored (s. 360).

The restoration may be a full restoration or, where the applicant is not a “related person”, restoration for a limited period (ss. 356(2) and 360(2)). After that period expires, the company is again dissolved, or the extraprovincial company’s registration is again cancelled (ss. 359(1) and 361(1)), unless the restoration period is extended. Alternatively, a “related person” may apply for a limited restoration to be converted to a full restoration (ss. 359(2)(a) and 361(2)(a)).

2. Assets of Dissolved Company

When a company ceases to exist while it still has assets, those assets will become the property of the government through the doctrine of escheat (in the case of land) or under s. 344(2) of the Business Corporations Act (in the case of all other assets). Assets held in joint tenancy vest in the other joint tenant at the date of dissolution (s. 344(2)(a)).

When a corporation holding land in British Columbia is dissolved, the land immediately escheats under the Escheat Act. Land held by a British Columbia company in a federal territory or another province will escheat under the common law Crown prerogative (which is regulated by the Escheats Act (Canada)) or a provincial statute. The British Columbia Escheat Act and the Business Corporations Act work in tandem to return land located in British Columbia to a restored company in a reasonably convenient way.

If a company is restored within two years after its dissolution, any land in British Columbia that had escheated to the government vests in the company, subject to the terms of any court order, as though the company had not been dissolved. In the case of a restoration after that two-year period, the return of the escheated land requires an order of the court, notice of the application for that order having been served on the government.

In the case of assets other than land, their title passes immediately to the government on the dissolution of a company (s. 344(2)). If money or other assets of a dissolved company have vested in the government as a result of its dissolution, upon restoration of the company any such assets not disposed of by the government vest in the company automatically (s. 368(1)(a)). The government must return to the company any assets in its custody, and pay to the company the amount of any money it received and the amount of any money realized from the disposition of any of the assets.

Conflicts of laws principles provide that title to assets is governed by the laws of the jurisdiction in which they are situate, so other assets located outside British Columbia will be governed by local laws, which will determine what happens to ownership of them when the company is dissolved.

3. Restoration Discretion

The registrar has no discretion to deny restoration if an application is filed under s. 356, unless a court order to the contrary is filed with the registrar (s. 358(1)). The court has discretion to order a restoration if it is satisfied that a restoration is appropriate (s. 360(5)); therefore the court has discretion to deny the application if it considers the restoration inappropriate.

4. Who Can Apply

Any person can apply for a limited restoration, but only a related person can apply for a full restoration (ss. 356(2), 359(2), 360(2), 361(2)). A related person means, in the case of a dissolved company, a director, officer or shareholder at the time of dissolution, or the heir or personal or other legal representative of a deceased shareholder (ss. 354(2)(a)(i) and (ii)). In the case of an extraprovincial company which has had its registration cancelled, a related person means the entity itself or a director, officer or shareholder (or,

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for a limited liability company, a manager or member) (ss. 354(2)(b)(i) and (ii)).

In an application to the court (but not to the registrar) for a full restoration, or conversion of a limited restoration to a full restoration, “related person” also includes any person the court orders an appropriate person to make the application (s. 354(2)(a)(iii) and (b)(iii)).

Any person is free to apply later for an extension of the period of a limited restoration (ss. 359(2)(b) and 361(2)(b)).

5. Reasons for Applying

Assets of a dissolved company vest in the government, so it will be necessary to restore the company to reacquire these assets. A dissolved company is also incapable of paying debts and discharging liabilities. A dissolved company’s assets, other than land in British Columbia, that vested in and were received by the government, are available to judgment creditors who apply to the minister for recovery against those assets within two years of the date of its dissolution (s. 349). Creditors may, therefore, seek to restore the company in order to realize against assets or otherwise collect after the two-year period.

Legal actions can only be taken against a dissolved company within two years after its dissolution (s. 346(1)(b)). Therefore, a party wishing to proceed against a company (or against someone else in circumstances in which judgment must first be obtained against the company) after that two-year period must have the company restored.

6. Time Limits

In the case of a company which was dissolved or an extraprovincial company which had its registration cancelled, before the coming into force of the Business Corporations Act, an application for restoration cannot be made to the registrar more than ten years after the dissolution or cancellation (s. 356(4)). In such a case, the application must be made to the court under s. 360. Otherwise there are no time limits on restoration.

§15.02 Procedure for Restoration

1. Publication and Mailing of Notice

Before applying for restoration, the applicant must publish notice of the application in the Gazette (s. 355(2)(a)).

The applicant must also mail notice of the application to the last address or mailing address of the registered office of the dissolved company or, in the case of an extraprovincial company, of its attorney (or, if none, to the last address in British Columbia of its head office), all as shown in the corporate register (s. 355(2)(b)).

When a restoration is as a result of an application to the registrar under s. 356, the restoration cannot take place until 21 days after the later of publication in the Gazette or mailing of notice to the last address shown in the corporate register (s. 363(1)).

2. Form and Content of Application to Restore

The requirements for a restoration application made to the registrar are largely set out in s. 357. All restoration applications must contain the date on which notice was published in the Gazette (s. 357(1)(a)) and the date on which the notice required under s. 355(2)(b) was mailed (s. 357(1)(b)).

When an application is for restoration of a company, it must contain details of the name reservation (or that the name will be the incorporation number plus “B.C. Ltd.”) and, in the case of a full restoration, a statement explaining the applicant’s status as a related person and the addresses of the proposed registered and records offices of the company (s. 357(2)).

A restoration application for an extraprovincial company must contain details of the name reserved or, in the case of a federal corporation, the name of the corporation. For a full restoration application, a statement must also be included giving the nature of the applicant’s status as a related person. An application for a full restoration must also include addresses for the post-restoration head office of the foreign entity and for each of the attorneys it will have following restoration (s. 357(3)).

If the required application is filed, the registrar has no discretion to deny restoration (s. 358). However, the registrar has a very broadly worded power to require an applicant for restoration to submit any records and information the registrar may require (s. 356(3)(b)). This probably is to be used to require applicants to file missing annual reports and similar records.

3. Consent of the Registrar

Sections 360(3) and 361(3) require that notice and a copy of any documents filed in the court for the application for a restoration or for the conversion of a limited restoration to a full restoration be sent to the registrar, and that the registrar must consent to the restoration. The consent must be provided to the court (ss. 360(4)(b) and 361(3)(d)(iii)). The registrar may make such consent subject to any terms and conditions the registrar considers appropriate.
In the case of an extraprovincial company, the registrar may also require a certificate of status from the home jurisdiction of the extraprovincial company confirming its continued existence.

4. Limited Restorations

Section 354(1) defines “limited restoration” to mean a restoration of a company, or of the registration of an extraprovincial company, for a limited period (up to two years). When the limited period of restoration expires, the company is dissolved or the registration of the extraprovincial company is cancelled (ss. 359(1) and 361(1)). The registrar will then publish notice of the dissolution or cancellation of registration on a government website (s. 359(4) and Reg. s. 6).

When there has been a limited restoration by the registrar, an application may be filed with the registrar within the limited period of restoration to either convert it to a full restoration, if the application is made by a related person (s. 359(2)(a)), or to extend the period to any later date the registrar considers appropriate, if the application is made by any person (s. 359(2)(b)). An applicant for a full restoration must comply with the notice requirements for an initial restoration application (s. 359(3)).

The court may similarly extend or convert a limited restoration, whether the limited restoration was by the court or the registrar (s. 361(2)). In the case of conversion of a limited restoration to a full restoration, the applicant must provide the registrar with notice of the application and copies of the records filed with the court (s. 361(3)(b)) and obtain the registrar’s consent to the conversion (s. 361(3)(c)). Only a related person can apply to convert the limited restoration to a full restoration (s. 361(2)(a)).

5. Court Order

Unless the order states otherwise, the restoration of the company will be without prejudice to the rights of any third party who has acquired any rights before the company’s restoration (see s. 360(7)). The same applies to a restoration by the registrar (s. 358(2)).

Promptly after a court order is made under s. 360 or 361, the applicant must file with the registrar a restoration application, including a statement that an entered court order has been obtained under s. 360(5) or 361(2)(a) or (b), as the case may be, and any other records the registrar may require (s. 362(1)). Upon receipt of that application the registrar must, unless an entered court order to the contrary has been filed with the registrar, restore the extraprovincial company, restore the registration, extend the restoration, or convert a limited to a full restoration, as applicable (s. 362(2)).

Section 360(5) provides that the court can make an order restoring a company or the registration of an extraprovincial company subject to the conditions and on the terms the court considers appropriate.

Section 360(6) provides that the court may give directions and make provisions it considers appropriate for placing the company or extraprovincial company and every other person in the same position, as nearly as may be, as if the company had not been dissolved or the registration of the extraprovincial company had not been cancelled.

[§15.03] Effect of Restoration

Upon completion of a restoration, the company is deemed to have continued in existence as if it had not been dissolved and proceedings may be taken as if it had not been dissolved (s. 364(4)).

Similarly, if the registration of an extraprovincial company is restored, the registration is deemed not to have been cancelled and proceedings may be taken as if the registration had not been cancelled (s. 365(3)).

After the restoration, the registrar publishes a notice on a government website and issues a certificate of restoration (s. 367(1) and Reg. s. 6). The restoration is effective at the time and date shown in the corporate register (s. 364(1)).
Chapter 16

Extraprovincial Companies

For further information on this topic, see Chapter 13 of the British Columbia Company Law Practice Manual, 2nd edition (Vancouver: CLEBC).

All legislative sections cited in this chapter and all references to the “BCA” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended, unless otherwise stated. References to “Reg.” are to provisions in B.C. Regulation 65/2004.

British Columbia recognizes the existence of foreign entities incorporated or organized under the laws of other provinces, under federal law and under the laws of other countries so long as they register under Part 11.

[§16.01] The Registration Requirement

Section 375(1) of the Business Corporations Act requires every foreign entity (with the exceptions below) to register as an extraprovincial company under the Business Corporations Act within two months after the foreign entity begins to carry on business in British Columbia.

1. Foreign Entities Exempted from Registration

The extraprovincial company provisions of the BCA do not apply to a foreign entity if it is a bank or if the only business that it carries on in the province is constructing and operating a railway (s. 375(3)(a) and (b)).

A foreign entity whose principal business consists of the operation of one or more ships is not required to be registered under the BCA if the foreign entity does not maintain in the province a warehouse, office or place of business under its own control, or under the control of a person on behalf of the foreign entity (s. 375(4)). Every resident agent or representative of such an entity must file a notice containing the information required by s. 375(5).

2. Alberta Corporations

British Columbia and Alberta signed the Trade, Investment and Labour Mobility Agreement (the “TILMA”) in April 2006, with the intent to reduce barriers to trade, investment and labour mobility across these provinces. The Trade, Investment and Labour Mobility Agreement Implementation Act, S.B.C. 2008, c. 39 (referred to as the “TILMA Act”) and the regulations under that act implement BC’s obligations under TILMA. In addition, the BCA was amended to empower the government to make regulations to allow extraprovincial registrations between designated provinces (see BCA, ss. 399.1-388.3). These latter regulations, which govern the registration and reporting requirements in BC of corporations incorporated under the Alberta Business Corporations Act, came into force on April 27, 2009 (see the Extraprovincial Companies and Foreign Entities from Designated Province Regulation, known as the “TILMA Regulation”). So far, Alberta is the only designated province.

In essence, an Alberta company that fulfills its registration and reporting requirements in Alberta will be deemed to have met the requirements in BC. Furthermore, companies who meet the definition of extraprovincial company as defined in s. 1(1) of the TILMA Regulation may carry on business in BC without maintaining a representative office or enterprise, or being resident of BC as a condition. These companies are also exempt from many of the filing, maintenance and other reporting provisions of the BCA (see s. 3 for an inclusive list). For example, these companies are exempt from filing annual reports and from almost all fees that are usually payable by extraprovincial companies to the extraprovincial registrar (see TILMA Regulation s. 3(2)).

For a more complete description of the TILMA Act and TILMA Regulation, see §13.4A-§13.4D in British Columbia Company Law Practice Manual, 2nd edition (Vancouver: CLEBC).

3. Carrying on Business

Section 375(2) of the BCA states that a foreign entity is deemed to carry on business in British Columbia if

(a) its name, or any name under which it carries on business, is listed in a telephone directory

(i) for any part of British Columbia, and

(ii) in which an address or telephone number in British Columbia is given for the foreign entity,
(b) its name, or any name under which it carries on business, appears or is announced in any advertisement in which an address or telephone number in British Columbia is given for the foreign entity,

(c) it has, in British Columbia,
   (i) a resident agent, or
   (ii) a warehouse, office or place of business, or

(d) it otherwise carries on business in British Columbia.

Even if clauses (a), (b) and (c) do not apply, there is also clause (d), which requires consideration of the extensive jurisprudence relating to the common law tests of carrying on business to determine whether by some other test the foreign entity is carrying on business within the province. Because it is not always clear whether a foreign entity is carrying on business, and because failure to register is an offence under s. 426(1)(b), if there is any doubt, it is normally prudent to register.

Section 375(3)(c) provides that a foreign entity is not deemed to carry on business in the province merely because it has an interest as a limited partner in a limited partnership carrying on business in the province. By implication, if a corporation is a general partner of a limited partnership or is a partner of a regular partnership, and the partnership carries on business in the province, then the foreign entity is subject to the extraprovincial company provisions of the BCA.

4. Effect of Registration

Section 378(1) provides that a notation in the corporate register that a foreign entity has been registered as an extraprovincial company is conclusive evidence that it has been duly registered on the date and time shown.

No act of a foreign entity, including any transfer of property to, or by, the foreign entity, is invalid by reason only that the foreign entity was not, at the time of that act, registered as an extraprovincial company (s. 378(4)(b)).

Registration will protect the name of the foreign entity to the extent that other corporations with the same or similar names will not be able to incorporate or register extraprovincially in British Columbia (except for federal corporations).

5. Limited Liability Companies

Many American states provide for the formation of limited liability companies (often referred to as LLCs). These are statutory unincorporated associations that combine certain elements of corporations, such as limited liability of owners, and certain elements of partnerships.

The definition of “foreign entity” expressly includes a limited liability company (s. 1(1)) (as well as foreign corporations). Accordingly, limited liability companies are subject to the same rights, restrictions and obligations as are granted to, and imposed on, foreign corporations by the BCA.

§16.02 Registration Procedure

1. Name

A name reservation should be obtained before submitting the registration statement. An extraprovincial company will not be registered by a name that does not comply with the Regulation and with the other requirements of the BCA (s. 22(4)). An exception to this provision is a federal corporation seeking extraprovincial registration in British Columbia.

2. Assumed Name

If the name of a foreign entity contravenes the Regulation or any of the requirements set out in the BCA, the foreign entity must, if it wants to be registered as an extraprovincial company, reserve an assumed name (s. 26(1)). This rule does not apply to federal corporations (s. 26(5)).

The foreign entity must provide an undertaking to the registrar that the foreign entity will carry on all of its business in British Columbia under that assumed name. On registration, the extraprovincial company is deemed to have adopted the assumed name (s. 26(2)).

An extraprovincial company that has adopted an assumed name under the BCA must acquire all property, rights and interests in British Columbia under its assumed name, is entitled to all property, rights and interests acquired, and is subject to all liabilities incurred, under its assumed name, as if the property, rights and interests and the liabilities had been acquired and incurred under its own name, and may sue or be sued in its own name, its assumed name or both (s. 26(3)).

No act of an extraprovincial company, including transferring or acquiring any property, rights or interests, is invalid merely because the extraprovincial company did not do so under its assumed name (s. 26(4)).
3. Registration Requirements

Every extraprovincial company that requires registration under the **BCA** must:

1. complete and file with the registrar a registration statement (s. 376(1)(c)(i)); and
2. submit to the registrar any other records the registrar may require (s. 376(1)(c)(ii)), including a certificate of status (or other proof of existence) for foreign entities incorporated or organized outside Canada.

Every extraprovincial company that is not registered as required by the **BCA** commits an offence (s. 426(1)(b)) and is liable to a fine not exceeding $100 for each day that the offence continues (s. 428(3) and Reg. s. 35).

4. Registration

When the foreign entity has filed the registration statement and other records as required by s. 376 in satisfactory form and paid the necessary fees, the registrar must, if the foreign entity is a federal corporation, and may in any other case, register the foreign entity (s. 377(1)) and issue a certificate of registration showing that the foreign entity is registered as an extraprovincial company under the **BCA** (s. 377(2)). The certificate will show the date and time of registration in British Columbia. The registrar must also publish a notice on the government website (s. 377 and Reg. s. 6).

**[§16.03] Duties of an Extraprovincial Company**

1. Attorneys

Unless the extraprovincial company has, under its charter, its head office within the province, an extraprovincial company is required to have an attorney (s. 386(1)). The attorney must be either an individual who is resident in British Columbia, or a British Columbia company (s. 386(2)). Each attorney is deemed to be authorized by the extraprovincial company to accept service of process on its behalf in each legal proceeding by or against it in British Columbia, and to receive each notice to it (s. 388). See also s. 9(2).

The mailing and delivery addresses of an attorney must be:

1. in the case of an attorney that is an individual, the address of the office in British Columbia at which the individual can usually be reached during statutory business hours (s. 386(3)(a)); or
2. in the case of an attorney that is a company, the address of the company’s registered office (s. 386(3)(b)).

The initial attorney or attorneys for an extraprovincial company are those specified in its registration statement (s. 387). Thereafter, an extraprovincial company may appoint one or more persons to be attorneys by filing a notice of appointment of attorney (s. 389(1)).

When an attorney intends to change the attorney’s mailing or delivery address or both, the extraprovincial company or the attorney must file with the registrar a notice of change of address of attorney (s. 391(1)).

An extraprovincial company may revoke the appointment of an attorney by filing with the registrar a notice of revocation of appointment of attorney (s. 393(1)). A revocation of the appointment of an attorney does not take effect until the extraprovincial company has appointed one or more replacement attorneys (unless under its charter its head office is in British Columbia, in which case it does not need to appoint an attorney) (s. 393(3)).

An attorney of an extraprovincial company who intends to resign must provide a written resignation to the extraprovincial company at its head office at least two months before the date on which the resignation is to take effect (s. 395(1)(a)). Promptly after complying with this obligation, the attorney must file with the registrar a notice of resignation of attorney (s. 395(1)(b)).

2. Annual Reports

Every extraprovincial company registered under the **BCA** is required to file an annual report within two months after each anniversary of the date of its registration (s. 380(1)(a)) unless another date has been prescribed, in which case it must be filed within two months after each anniversary of the prescribed date (s. 380(1)(b)).

3. Amalgamations

Under s. 379(1), if a foreign entity that is registered as an extraprovincial company is party to an amalgamation or similar process, the extraprovincial company must provide to the registrar the records and information the registrar may require and must file with the registrar, within two months after the effective date of the amalgamation, a notice of amalgamation of extraprovincial company. From the time of the amalgamation or similar process, the amalgamated extraprovincial company is seized of and holds and possesses all land of the amalgamating entities that is located in British Columbia (s. 379(4)).
This requirement does not apply if the amalgamation or similar process results in a British Columbia company (for example, the amalgamation of an extraprovincial company with a British Columbia company to create a British Columbia company under s. 269(b)).

4. Change of Name

If an extraprovincial company changes its name, the extraprovincial company must file with the registrar a notice of change of name of extraprovincial company and any other records the registrar may require (s. 382(1)(a)). Before filing the records, the extraprovincial company must either reserve its new name under s. 22 or, if its new name contravenes any of the requirements of the Regulation or of the BCA and the extraprovincial company does not have an assumed name under which it intends to continue to carry on business in British Columbia, adopt an assumed name (s. 382(1)(b)). The requirement to obtain a name reservation or to use an assumed name does not apply to a federal corporation (s. 382(4)).

An extraprovincial company that has adopted an assumed name under the BCA may either cancel its assumed name and carry on business in British Columbia under its own name, if the name becomes available, (by filing with the registrar an application to change assumed name) or change its assumed name to another assumed name (by obtaining a name reservation and by filing an application to change assumed name (s. 383(1))).
Chapter 17

Shareholders Rights and Remedies

For further information on this topic, see Chapter 14 of the British Columbia Company Law Practice Manual, 2nd edition (Vancouver: CLEBC).

All legislative sections cited in this chapter and all references to the “BCA” are to the Business Corporations Act, S.B.C. 2002, c. 57, as amended unless otherwise stated.

§17.01 Introduction

Shareholder disputes are more common than most people would expect. Frequently, shareholders embark on some business venture without any formal agreement; rather, they have a loose understanding of the financing and conduct of the business and a "standard" set of company articles. This pattern leads to trouble. Moreover, even where a shareholder agreement exists, conflict may arise from a variety of conditions. For example, although remedies may be built into a shareholder agreement to deal with some foreseen problems, it may not address the unanticipated. Some examples of common problems are:

- Equal “partners” in a business may reach a deadlock on the future of the venture.
- “Partners” may develop a lack of confidence in their colleagues but be unable or unwilling to finance their “buy-out” under a shareholder agreement.

Whether or not a shareholder agreement exists, the remedies under the Business Corporations Act, S.B.C. 2002, c. 57 may be required to resolve a dispute. These remedies are explored in this chapter.

§17.02 Court Proceedings


   In the following discussion, the term “court” refers to the Supreme Court of British Columbia (s. 1(1)).

   All applications to court under the Business Corporations Act must be made by application. Under the Supreme Court Civil Rules, B.C. Reg. 168/2009, such applications must be made by petition (see Supreme Court Civil Rules 2-1(1), (2) and 16-1) and the “application” is normally the hearing of the petition. Note that the court has the power to convert a proceeding commenced by a petition to a civil claim in the appropriate circumstances.

   Unless notice is explicitly required, an application may be brought without notice (s. 235). If an order is obtained without notice, any person affected by the order has the right to apply to set it aside or vary it on grounds of material misrepresentation, that an application without notice was inappropriate, or on its merits (Supreme Court Civil Rule 8-5(3)). In most cases a company’s shareholders will be persons affected by an order that was obtained without notice.

   Documents may be served on a company at its registered office or personally on a director, senior officer, liquidator or receiver manager of the company (s. 9).

2. Rectification of Irregularities

   The court may, either of its own motion or on the application of any interested person, make an order to rectify or modify the consequence of any omission, defect, error or irregularity in the conduct of the business or affairs of a company, which causes a breach of the BCA or the company’s memorandum, notice of articles or articles, or renders proceedings at a meeting or a consent resolution ineffective (s. 229).

   On application by a company, a shareholder or an “aggrieved person”, the court may also correct the company’s articles, notice of articles or memorandum, minutes of any shareholders or directors meeting or resolution or any of the company’s registers. The court has the power to correct information wrongly entered or retained in, or wrongly deleted or omitted from, these records, and to compensate anyone who suffered a loss as a result of the incorrect information (s. 230).

3. Relief from Oppression

   A shareholder of a company may apply for a court order, under s. 227, on the following grounds:

   - the affairs of the company are being or have been conducted, or the powers of the directors are being or have been exercised, in an oppressive manner, or
   - some act of the company has been done (or is threatened) or some resolution of the members has been passed (or has been proposed) that is unfairly prejudicial to one or more of the shareholders.

   For the purposes of s. 227, a shareholder includes a beneficial owner of a share of the company and any other person who, in the court’s discretion, is a proper person to make an application under s. 227.
Fairness is something the court will be concerned with when considering oppression applications. A fundamental reasonable expectation is of fair treatment. Has the majority been dealing honestly and fairly with the minority shareholders when conducting its affairs or when exercising powers of the directors? This will depend on the factual circumstances in which the oppressive behaviour has taken place.

The shareholder must be able to point to conduct affecting him or her as a shareholder, not just as a director, officer or employee.

According to the Supreme Court of Canada’s decision in BCE Inc. v. 1976 Debentureholders, 2008 SCC 69, there is a two-part test for whether there has been oppression. The shareholder must prove that

1. the shareholder’s reasonable expectations been violated; and
2. that violation amounts to oppression or unfairly prejudicial conduct.

There must be evidence to verify that the shareholder actually held the reasonable expectations that the shareholder claims have been violated and the conduct complained of must be “oppressive”.

Conduct that is burdensome, harsh and wrongful is oppressive (Scottish Co-operative Wholesale Society v. Meyer, [1958] 3 All E.R. 66 (H.L.). According to the Supreme Court of Canada in BCE, supra, oppressive conduct means conduct that is coercive, an abuse of power or suggestive of bad faith.

Examples of behaviour that has satisfied the court as oppressive in the circumstances include majority shareholders appointing themselves to paid offices of the company, and majority shareholders paying themselves excessive salaries or bonuses thereby absorbing profits that would otherwise be paid to shareholders as dividends.

It is not necessary for a shareholder to prove an element of bad faith on the part of those conducting the company’s affairs but the shareholder must demonstrate a lack of probity and a failure to deal honestly and fairly with the majority. What is important is the effect of the conduct complained of (Safarik v. Ocean Fisheries Ltd. (1993), 10 B.C.L.R. (2d) 246 (S.C.)).

Conduct that is not oppressive may be unfairly prejudicial since the threshold is lower (Elliott v. Opticom Technologies Inc., 2005 BCSC 529). One basis for successfully proving unfairly prejudicial conduct is for a shareholder to satisfy the court that they have been denied a legitimate expectation to participate in the direction of the company’s business affairs.

Breaches of the company’s obligations under the BCA or its articles can also be oppressive or unfairly prejudicial.

The case law is divided on the effect of a shareholder agreement on a shareholder’s ability to seek remedies under s. 227. The courts generally have held that where the shareholder agreement contains remedies for the conduct complained of similar to those sought under s. 227, the shareholder should pursue his or her rights under the agreement. But breaches of a shareholder agreement can be evidence of oppression or unfairly prejudicial conduct.

The court may order either interim or final relief. Examples of available remedies are listed in s. 227(3). The most common types of relief granted are the following:

- orders that remedy the specific conduct complained of;
- orders requiring the company or other shareholders to purchase the wronged shareholder’s shares;
- orders that appoint a receiver or receiver manager; and
- orders for liquidation and dissolution.

If the court makes a payment order and the company is insolvent or payment would make it insolvent, it must pay as much as possible without becoming insolvent (s. 227(5) and (6)).

A shareholder may seek to hold a company’s directors or officers personally liable for oppression or unfairly prejudicial conduct. To succeed, the shareholder will have to establish that specific directors or officers did specific things that amounted to oppression. They will also have to show that the circumstances support the oppression being remedied by requiring the directors or officers to personally compensate the shareholder. That may be so in cases where the directors or officers personally benefited from the oppressive conduct or furthered their control over the company through it.

It is important to note that the provisions of s. 227 differ from the analogous provisions of the Federal, Ontario and Alberta Acts. For example, under those acts shareholders, creditors and directors can all bring oppression proceedings. Under s. 227 shareholders alone can. Under the other statutes complainants can bring proceedings where corporate conduct “unfairly disregards” their interests. Relief is unavailable under s. 227 in these circumstances.
4. Derivative Actions

As distinguished from relief from oppression proceedings, a shareholder or director brings a derivative action in the name and on behalf of the company (s. 232(2)). The purposes of derivative actions are to enforce any right, duty or obligation enforceable by the company, or to recover damages for any breach of those rights, duties or obligations (s. 232(2)). A shareholder or director of the company may also, with leave of the court, defend an action brought against the company (s. 232(2) and (4)).

Section 233(1) requires the shareholder or director, when applying to the court, to have made reasonable efforts to cause the directors to prosecute or defend an action. The shareholder or director must notify the company, and any other person the court may order, of the application. The section also requires that the shareholder or director be acting in good faith and that it appears to be in the best interests of the company that the action be brought or defended. In addition, if the party bringing the derivative action is a shareholder, the shareholder must have been a shareholder at the time of the transaction that has given rise to the cause of action.

In Carr v. Cheng, 2005 BCSC 445, the Court held that appearing to be in the best interests of the company means that the proposed action must be arguable or have a reasonable prospect of succeeding and, if successful, must maximize the value of the company, which may require consideration of the interest of the shareholders, employees and others.

The derivative action may not be discontinued, settled or dismissed without the court’s approval (s. 233(5)). The court may issue interim and final orders regarding the directions for the conduct of the action and costs for the action (s. 233(3) and (4)).

Section 233(6) states that no derivative action is to be stayed or dismissed by reason only that it can be shown that an alleged breach of a right, duty or obligation owed to the company has been or might be approved by the shareholders of that company. However, evidence of that approval or possible approval may be taken into account by the court when making an order under s. 232.

5. Order for Liquidation and Dissolution

A company may be liquidated and dissolved by court order, under s. 324 of the BCA, if the court thinks it just and equitable to do so, and as a remedy for oppression. Such an order is a drastic remedy. Consequently, a heavy onus rests on the applicant to persuade the court to grant such an order. The essential factor is that the relationship between the company’s shareholders has deteriorated to such an extent that they have neither trust nor confidence in each other’s ability to manage the company’s affairs. The courts are particularly likely to order a liquidation where it appears that the basis of the company was mutual confidence among the shareholders; where the shareholders agreed all were to participate in management; or where a shareholder agreement restricts shareholders’ ability to liquidate their investment.

In the case of a family company, the courts have held it is appropriate to take a more liberal approach to liquidation. The courts have found it would be just and equitable to liquidate a family company where one family member after working in the business for many years was excluded from management, even though he was never a director and there was no wrong doing by the other family members; see Safarik v. Ocean Fisheries Ltd. (1996), 12 B.C.L.R. (3d) 342.

It is important to note that, once the court is satisfied it would be just and equitable to liquidate the company, it is not limited to making a liquidation order. Under s. 324(3), the court may make any of the orders available under s. 227. While a liquidation order is a drastic remedy, the test of showing that it is just and equitable that the company be liquidated may be easier to meet than that required for the court to find the shareholder is being oppressed. This may enable a shareholder to access the “oppression” remedies in s. 227 through the “back door” of the liquidation provisions of s. 324.

[§17.03] Dissent Proceedings

1. General Information

In certain circumstances, a registered shareholder who disagrees with a proposed corporate action can require the company to purchase his or her shares for their “fair value” (s. 237(1)). The actions giving rise to a right of dissent are as follows:

- an alteration in the articles of a company (or the memorandum of a pre-existing company) by altering the restrictions on the business carried on or to be carried on by the company, or on its powers (s. 260);
- a proposed amalgamation (ss. 272, 287);
- approval of an arrangement (where permitted);
- a proposed disposition of all or substantially all of its undertaking (s. 301(5));
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- a proposed continuance outside of B.C. (s. 309); or
- in respect of any resolution or court order or arrangement permitting dissent.

Under similar legislative provisions in Alberta (Alberta Business Corporations Act), the Alberta Court held that notwithstanding the clear statement that only registered shareholders are to exercise dissent rights, the company had so conducted itself as to be estopped from denying a beneficial shareholder the right to do so: Lay v. Genevest Inc., [2005] A.J. No. 247.

2. Waiver

A shareholder may waive their right to dissent with respect to a particular corporate action (s. 239(1)), by providing to the company a waiver, which sets out specified information (s. 239(2)). In that event, the shareholders’ right of dissent terminates (s. 239(3) and (4)). A shareholder may not waive their right to dissent generally (s. 239(1)).

3. Notice of Corporate Action

The company must notify each of its shareholders of corporate actions from which they have a right to dissent. If shareholders are entitled to dissent from a resolution that is to be considered at a shareholders’ meeting, the company must notify them of the meeting, the resolution, and their right of dissent, before the meeting (s. 240(1)). The notice period depends on the company’s situation. If the shareholders are entitled to dissent from a consent resolution or resolution of directors, the company may, at least 21 days before the specified date, notify them of the resolution and their right to dissent (s. 240(2)). If the company does not, and the resolution is passed, or if a court order provides for a right of dissent, the company must notify any shareholders who did not vote in favour of the resolution, sending them a copy of the resolution and a statement of their right to dissent, within 14 days after the passing of the resolution (ss. 240(3) and 241).

4. Notice of Dissent

A shareholder who intends to dissent from corporate action must send the company a written notice of dissent, within a specified time. The notice must specify the shares in respect of which the shareholder is dissenting, and whether the shareholder is a registered or beneficial owner of the shares or both (s. 242(1) – (4)). If the notice does not comply with s. 242, the shareholders’ right of dissent terminates (s. 242(5)).

5. Notice of Intention to Proceed

If a company that receives a notice of dissent intends to continue with the corporate action, it must send the dissenting shareholder a notice of intention to proceed stating that and advising the shareholder about how their dissent is to be completed (s. 243).

6. Completion of Dissent

A dissenting shareholder who receives a notice of intention to proceed must, if they still want to dissent, send the company or its transfer agent, within one month, their share certificates and a written statement that they require the company to purchase their shares (s. 244(1)). The shareholder is then deemed to have sold the shares, and the company to have purchased them (s. 244(3)). Once the shareholder has done this, the shareholder may not vote or exercise any shareholder rights in respect of the shares (s. 244(6)). Again, if the shareholder fails to comply with this requirement, their right to dissent terminates (s. 244(4)).

7. Payment

The dissenting shareholder and the company can agree on the fair value of the shares (s. 245(1)). If they cannot agree, either may apply to the court to determine the fair value of the shares or apply for an order that value be established by arbitration or by reference to the registrar or a referee (s. 245(2)). (In Re Anthem Works, 2005 BCSC 766, the Court declined to summarily reject an argument that the motives of shareholders in acquiring their shares and exercising their dissent rights were relevant to the fair value of the shares.) The company must then promptly pay that amount to the shareholders (s. 245(1) and (3)), unless the company is insolvent, or payment of the fair value would make it insolvent, in which case the company must notify the shareholders of that and not pay (s. 245(5)). The dissenting shareholder may then either withdraw their notice of dissent within 30 days, or claim against the company for the unpaid amount (s. 245(4)).

8. Loss of Right to Dissent

In addition to losing dissent rights when not complying with the requirements set out earlier, a shareholder loses their right of dissent, if the company abandons the corporate action that has given rise to the right of dissent, a court permanently enjoins the action, or the shareholder votes in favour of the action or withdraws the notice of dissent with the company’s consent (s. 246). When these events occur, the company must return the share certificates to the shareholder and the shareholder regains the ability to vote the shares and exercise shareholder rights (s. 247).
Chapter 18

Shareholders’ Agreements

§18.01 Introduction

It is common for two or more companies or individuals to decide to carry on business together, whether as partners, co-owners or shareholders of a company. Often it is advisable to define in advance the relationship between the parties and their respective obligations to the business and each other. It may be difficult to convince the parties that an agreement is necessary, but they will recognize the need the first time a dispute arises.

This chapter deals specifically with shareholders' agreements, but many of the same principles apply for co-ownership agreements and partnership agreements. Whether the parties choose to be shareholders, partners or co-owners depends on tax and other considerations. The following discussion reviews the model shareholders’ agreement (the “model agreement”) and the matters that might be addressed in such an agreement for a British Columbia company that is not a reporting issuer.

§18.02 Business Corporations Act

Note that a shareholders’ agreement is just one tool available to a lawyer to implement the business agreement between the shareholders and the company. It is an instrument that supplements the company's constating documents and the applicable corporate statute.

In order to determine what matters should be addressed in a shareholders' agreement, it is useful to look briefly at the protections and benefits that are found in the legislation, or which might be included in a company’s articles or in its notice of articles. When conducting such a review, it is essential to distinguish between those companies that were incorporated under the Business Corporations Act and those incorporated under the Company Act in order to determine how, if the latter, the company has dealt with the Pre-existing Company Provisions (“PCPs”) (s. 442.1(1)). The PCPs apply to a pre-existing company unless and until the company alters its articles to remove them or adopt other provisions in their place.

A few of the provisions in the Business Corporations Act that may be beneficial to a shareholder are discussed in the following paragraphs.

1. Allotment

Before allotting shares of a pre-existing company, the PCPs require that those shares must be offered rateably to the current shareholders, unless the company has amended its articles to remove this requirement. Companies incorporated under the Business Corporations Act, or those pre-existing companies that have made the necessary revisions to their articles to relieve them of this obligation, are not bound by this requirement, and, accordingly, may need to address this issue in a shareholders' agreement.

2. Purchase or Redemption

When a pre-existing company proposes to purchase or redeem its own shares, subject to certain exceptions, the PCPs require that the offer to purchase or redeem must be made rateably to every shareholder of the class or series to be purchased or redeemed, unless the company has amended its articles to remove this requirement. Companies incorporated under the Business Corporations Act or those pre-existing companies that have made the necessary revisions to their articles to relieve them of this obligation, need not make this offer and may need to address this issue in a shareholders' agreement.

3. Approval by Special Resolution or Exceptional Resolution

The Business Corporations Act contains many provisions that require the company to obtain the approval of the shareholders by special resolution. A special resolution is the approval of shareholders by a special majority of between two-thirds and three-quarters of the votes cast, depending upon the articles and whether the company is a pre-existing company. Absent a specific provision in the articles, a three-quarters majority will be required for any pre-existing company and a two-thirds majority will be required for any company incorporated under the Business Corporations Act. A company may specify its special majority to be any amount not less than two-thirds and not more than three-quarters.

Special resolution protections under the Business Corporations Act include the following: continuation out of British Columbia (s. 308(2)), removal of directors (s. 128(3)), power to alter the memorandum (in pre-existing companies), notice of

1 Kathleen Keilty of Blake Cassels & Graydon LLP kindly revised this chapter in July 2011 and January 2009. Reviewed and revised annually from February 1996 to January, 2005 by Douglas G. Shields, Davis & Company, Vancouver. This chapter is based on a paper prepared originally by H. Laing Brown for Continuing Legal Education.
articles and articles (Part 9 - Company Alterations), approval of amalgamation (s. 271), disposing of all or substantially all its undertaking (s. 301) voluntary liquidation and the appointment of a liquidator (s. 319). These sections highlight the importance of the relative percentages of shares and the obvious value of having sufficient votes to either pass or defeat a special resolution.

Under the Business Corporations Act the articles can provide for the approval of certain matters by exceptional resolution, being a majority specified to be in excess of the special majority required to pass a special resolution.

[§18.03] Notice of Articles and Articles

The next tools for documenting the business agreement between the shareholders are the notice of articles and articles of the company. These "charter documents" of the company can contain various protections for shareholders, including the following:

- Section 33(1)—the articles may restrict the business that the company can carry on or its powers. These restrictions could be used, for example, to limit the ability of the company to grant guarantees.

- Section 58 and 61—special rights or restrictions may be attached to share classes. There are no significant statutory limitations on the types of special rights or restrictions that may be attached to shares of the company in order to assist shareholders in realising the business agreement that they have reached.

- Section 264—the articles may restrict the company or the directors from taking certain actions, or from altering certain provisions of the articles or notice of articles, without first passing an exceptional resolution. This requirement could be used, for example, to limit the ability of the directors to make capital expenditures exceeding a certain dollar amount without an exceptional resolution.

In addition to the above matters, which are most appropriately contained in the notice of articles or articles, there are many topics that might be contained in the shareholders' agreement or the articles of the company. There are a number of factors to consider when determining whether portions of the business agreement between the shareholders should be placed in the company's charter documents or in a separate shareholders' agreement.

- The notice of articles and articles can be amended by a special resolution of the shareholders. As a result, the notice of articles and the articles are not in themselves effective to protect the interests of minority shareholders who hold less than that number of votes required to defeat a special resolution. While it may be possible to get around this problem by attaching special rights and restrictions to separate classes of shares, this can be cumbersome. On the other hand, if this type of provision is included in a shareholders' agreement, then the agreement, unless otherwise provided, would only be subject to amendment with the unanimous approval of the parties.

- While the shareholders' agreement requires unanimous approval for amendment, it can otherwise be less awkward to amend than the notice of articles or articles that require compliance with the relevant statutory provisions, including holding meetings, passing required resolutions and making the necessary filings with the Registrar of Companies office.

- The articles must be maintained at the records office of the company and, together with certain other documents, may be made available for inspection by the public. The obvious disadvantage is that the shareholders may wish to keep certain aspects of their agreement private.

- Section 137 of the Business Corporations Act provides that the articles may restrict or transfer the powers of the directors to manage or supervise the management of the business and affairs of the company to one or more other persons. Any such restriction contained in a shareholders' agreement may not be valid or enforceable as a result of the common law rule against fettering a director’s discretion. Using of s. 137 of the Business Corporations Act to transfer powers should be approached with caution because the person to whom directors’ powers are transferred also takes on the duties and liabilities of a director with respect to the exercise of those powers. For example, a shareholder normally may act in his or her own best interests, but once having taken on the powers of directors, will be obliged to act in the best interests of the company in exercising the transferred powers (see ss. 137(2) and 138).
There are other considerations or understandings among shareholders that might be more appropriately set out in a shareholders' agreement. These are discussed in more detail in the paragraphs of this Chapter which follow and include:

- the ability or requirement of a shareholder to participate in the management of the company in general, or "Conduct of the Affairs of the Company";
- the inflow of money to the company, or "Financing and Shareholders' Contributions";
- the outflow of money from the company, or "Distribution of Profits";
- control over who is entitled to hold shares in the company, or "Restrictions on the Transfer of Shares or Right of First Refusal";
- dispute resolution and the liquidity of a shareholder's investment in the company or "Compulsory Buy-Out";
- what happens on the death of a shareholder or "Investment Sale on Death"; and
- how to deal with a shareholder who defaults in his or her obligations or "Default".

The exercise of having the parties discuss with the lawyer their understanding of the business agreement amongst them with respect to the conduct of the affairs of the company is beneficial in itself. It gives the shareholders the opportunity to set out their understanding of the business agreement, and the lawyer the opportunity to raise points that may be addressed in a shareholders' agreement and which the shareholders have not considered.

The model agreement and this chapter are based on the following assumed fact situation:

- the company has just been incorporated under the BCA;
- there are three individual shareholders who each own one-third of the issued and outstanding common shares of the Company;
- each shareholder is to contribute equally by way of loan;
- each shareholder will be actively involved with the company through a separate employment contract;
- a shareholder may wish unilaterally to transfer his or her interest in the company to a company which he or she controls without the necessity of the approval of the other shareholders and a substantial amendment to the body of the agreement; and
- where there is a corporate shareholder, an individual will be appointed as that corporate shareholder's representative.

By breaking down the various general areas that might be addressed in a shareholders' agreement, it is possible to address any concerns raised by the shareholders and discuss the response to these concerns in the model agreement and to discuss any other matters or considerations which might be dealt with in a shareholders' agreement.

[§18.04] Parties

The parties to a shareholders' agreement are each of the shareholders and usually the company (essential if the company is to provide covenants such as the purchase of shares from a shareholder under the agreement). If a shareholder is a corporation, it may be advisable also to have its shareholders as parties to the covenant regarding control of the shareholder company.

The lawyer must be careful to determine who the client is. Conflicts may arise during the course of negotiating a shareholder agreement as shareholders will often have competing interests. The lawyer should determine at the outset who the client is and inform all parties in writing, being careful to explain the significance of that party being represented and to advise each of the unrepresented parties to obtain independent legal advice before they execute the agreement.

[§18.05] Conduct of the Affairs of the Company

The shareholders' agreement should set out how the affairs of the company will be managed and who will make the decisions. These provisions will relate to the control of the company and the protection of any minority shareholders.

1. Management of the Company

A shareholders' agreement usually contains covenants relating to management of the company, including the following:

- The number of directors and who may appoint and remove nominees to the board. The agreement may provide that each shareholder may appoint one nominee, but there may be circumstances where a shareholder will have the right to appoint more than one director or where the parties will agree to appoint a neutral or independent director to break any deadlocks.
• The quorum for the transaction of business by the directors. The quorum may require a nominee from each shareholder to be present or may provide that a smaller number can transact business.
• Where meetings are held, who can call them and the notice required.
• Decisions the directors can make.

2. Major Decisions
In any business, there will be certain important decisions that will require the unanimous or special approval of the directors or the shareholders. Examples include: making major capital expenditures; borrowing or granting security for capital expenditures; conducting non-arm's length transactions; changing bank signing officers; approving budgets; entering into major or material contracts; acquiring or disposing of property; and issuing dividends and additional shares.

3. Employment Contracts
If shareholders will be running the business, the parties may wish to have separate employment or management contracts entered into between the company and those shareholders. Cross default provisions should be used to ensure that a default by a shareholder under his or her employment contract will trigger a default under the shareholders' agreement.

4. Non-Competition, Non-Solicitation and Confidentiality Agreements
Often it is important that the shareholders agree not to be involved in competing businesses within the market area of the company's business, either while they are shareholders or for a certain period of time afterwards. The clauses must be reasonable as to scope of activity, geographic area and time or they risk being found unenforceable as contrary to public policy. In the absence of any non-competition covenants, employee shareholders may also be subject to fiduciary obligations that would prevent them from competing with the company. Similar covenants or agreements may be appropriate or necessary to deal with the non-solicitation of employees, customers or suppliers, and the handling and treatment of confidential information.

Without the benefit of specific provisions in a shareholder agreement, the conduct of the management and the affairs of the company will simply be carried out in accordance with the Business Corporations Act and the company's articles. Consequently, a majority of the shareholders will be able to elect a board of directors, who in turn will appoint the officers of the company. Subject to various provisions in the Business Corporations Act, the directors will be free to manage and conduct the affairs of the company as they see fit.

As each of the three shareholders in our assumed fact situation are "minority" shareholders, two of the three could, in the absence of a shareholders’ agreement, act together to elect only themselves to be board members, and they in turn could be appointed the only officers of the company. Arguably, they could also ensure that the company does not employ or distribute dividends or other distributions to the other shareholder. As none of the shareholders knows at the outset who may be the one left out, it is in the best interest of each to resolve this situation fairly. The model agreement allows for each shareholder to be a director or to nominate a director to a three person board. This ratio maintains the same relative voting power on the board as exists at a meeting of shareholders.

The model agreement also provides for a quorum of three at a board meeting: paragraph 3.03. This provision is consistent with the shareholders' desire that a board meeting not be held without all the directors being present. Paragraph 3.04 ensures that one director is not able, through continued non-attendance, to stalemate the directors' ability to manage and conduct the affairs of the company.

In regulating the conduct of the affairs of the company in a shareholders' agreement, it is necessary to obtain the desired balance between protecting the interests of minority shareholders and hamstringing the efficient management of the company. The balance obtained in each situation will differ depending on the wants and needs of the particular shareholders and the company.

The model agreement contains an extensive list of the major decisions that can only be undertaken with a 75% majority vote of the directors. Where there are three directors, this in substance requires unanimous agreement. The list of major decisions considered in paragraph 3.05 of the model agreement leans heavily to the side of protecting the interests of minority shareholders while arguably running the risk of hamstringing the efficient operation of the company.

The list of major decisions in the model agreement may well be reduced once reviewed by the shareholders. However, it is usually better to start with an extensive list and cut, than to start with a short list and attempt to determine what has been omitted.

Note that the shareholders' agreement does not specifically contain the details of the employment or management agreements between the company and its shareholders. It is usually more appropriate to have these agreements separate from the actual shareholders' agreement, although any amendments to employment or management agreements by the company are viewed as major decisions with the concomitant restrictions contained in paragraph 3.05 of the model agreement.
The model agreement also contains an attempt at preventing competition by the shareholders with the company, which is applicable both while the shareholder is involved with the company and also for a "reasonable" period after the shareholder has ceased involvement in the company. The requirements of a company with respect to protection against competition will be different in each situation and the lawyer must ensure that this most important and difficult clause is properly suited for the particular company and its reasonable needs for protection. If the clause is not reasonable in light of the particular circumstances, the courts may determine that the provision is not enforceable.

One matter which is not contained in Part 3 of the model agreement is the question of which shareholders will hold positions as officers of the company and what the functions of those offices are to be. The lawyer should consider whether the provision in the agreement as to which shareholders will hold certain offices is enforceable in the face of an argument that the discretion of the directors has been fettered.

§18.06 Financing/Shareholders' Contributions/Distribution of Net Profit

Part 4 of the model agreement provides for the initial contribution of the shareholders to the company by means of subscribed capital and loans. There are further provisions that additional funds required by the company will be obtained, to the greatest extent possible, by borrowing from a chartered bank or other lending institution.

However, except with the unanimous agreement of the shareholders, no shareholders are required by the model agreement to guarantee the indebtedness of the company. It further provides that where the company is unable to obtain funds by borrowing, a majority of the board can require that shareholders lend additional funds to the company. These loans will be made rateably in proportion to a shareholder's common shareholdings in the company and will be repaid rateably. There is a further obligation that shareholders subordinate and postpone their loans to permanent financing. Notwithstanding, consideration should be given to securing these loans so as to maintain priority over other third-party creditors.

Part 10 of the model agreement provides remedies to the shareholders who contribute to the company against a shareholder who defaults in his or her obligations to loan the company money. Alternative methods of achieving this include:

- diluting the reluctant shareholder's interest in the company; or
- paying a high rate of interest to those shareholders who do respond with further capital.

Simply diluting the reluctant shareholder's position may be possible through offering shares in the company for sale to the shareholders. However, in most closely held companies (as well as in our assumed fact situation), a shareholder's investment in the company consists not only of shares, but also of shareholders' loans. Consequently, it may be difficult to achieve the desired degree of dilution of the equity of a shareholder, and also maintain the desired mix of loans and shares. A further difficulty is presented in the determination of the appropriate price for the shares that are being proposed to be allotted and issued.

Paying a high rate of interest to shareholders who contribute the required capital may be a solution, however, as with all means of attempting to require shareholders to inject more capital, this method also has potential for abuse where the shareholders are of unequal financial means.

The distribution of profits of the company is a complex subject, which must be resolved after carefully viewing the business, operations and financial structure of the company. While most companies retain part of their earnings to be reinvested in the company and pay part of their earnings out to the shareholders, the shareholders should be concerned as to how much money is paid out to them and when and how it is paid. Absent any written agreement or specific rights and restrictions attached to the shares, the directors will have the authority to make such assessments and all determinations associated with distributing profits.

Money can be paid out in the form of salary, dividends, interest payments on shareholders' loans, payment of shareholders' loans or return of capital. The desired mix for each company will depend partly on tax considerations and partly on the nature of the contributions made by the shareholders. Accordingly, it is very difficult to predetermine a mix that will be in the best interests of all concerned for all time.

It may be possible to achieve a desired formula for the return to the shareholders by using a mixture of shares (preferred and common) and by having interest-bearing shareholders' loans. It also is possible to have only one class of shares and a dividend policy with respect to those shares. These policies may include:

- a fixed return on investment;
- a percentage of net profits;
- a percentage of net profits subject to a working capital ratio, a veto by certain shareholders, or the surplus exceeding a particular figure; or
- a combination of the above.

It is most important that any policy regarding the return to shareholders be realistic in terms of the corporation's need to retain funds for the furtherance of its business interests.
There are basically two different kinds of pre-emptive rights. The first, a right of first refusal, requires that the selling shareholder obtain an offer from a particular buyer before offering the shares to the other shareholders. With proper disclosure clauses, this procedure has the advantage of informing the remaining shareholders about the prospective buyer, thereby enabling them to determine whether or not they wish that person to be a shareholder with them in the company. The obvious disadvantage of this scheme is that it is very unlikely that a prospective buyer would be willing to go to all the trouble and expense of making an offer and negotiating a deal when he or she is aware that the offer is subject to a right of first refusal by the remaining shareholders of the company.

The second pre-emptive right, or right of first offer (used in Part 5 of the model agreement), allows the offering shareholder to offer his or her investment in the company to the remaining shareholders without first having entered into an agreement with a third party. If this offer is not accepted within the period of time stipulated in the shareholders’ agreement, the offering shareholder has a further period of time within which to locate a prospective third party buyer and complete the sale of his or her investment in the company to that person (on no better terms and conditions than were offered to the remaining shareholders). Arguably, the selling shareholder could already have reached agreement with a third party before commencing the offering of his or her investment in the company under the pre-emptive rights set forth in the shareholders’ agreement.

Whichever of the above methods is used, it can be a hardship or an inconvenience on the remaining shareholders either to have to produce a substantial amount of money in a relatively short period of time, or to face the prospect of having a third party shareholder of whom they may not approve.

This problem can be mitigated in several ways, including the following, which have been used in the model agreement:

- extend the pre-emptive rights to the company itself so that the company can use its assets to finance the payment of the purchase price (may have significant income tax consequences for the selling shareholder);
- restrict the price to some agreed upon formula for valuation; or
- provide that the purchase price may be paid by the buyer(s) over a period of time.

These provisions are obviously for the benefit of the shareholders that are retaining their investment in the company. Given that these shareholders are staying with the company, it is thought that the continuing viability of the company should not be impaired by the necessity...

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[§18.07] Restrictions on Transfer/Right of First Refusal or Offer

In a closely held company, the shareholders will usually be actively involved in the management of the company and, accordingly, will not want to be forced to work with someone they do not approve of. Consequently, the shareholders’ agreement should provide for some restriction on the transfer of shares by shareholders, both inter vivos and upon the death of a shareholder.

It should be recognized that an absolute prohibition on share transfers will be invalid, and that any restrictions on transfers will likely be narrowly construed.

The usual provisions to give some control over the admission of new shareholders include the following:

- requiring the approval of the directors or shareholders of all transfers of shares;
- giving the shareholders the pre-emptive right to purchase shares before the sale of the shares to a third party; and
- providing tag-along or drag-along rights to facilitate an orderly transition.

With respect to the first control mechanism, the unanimous consent of directors and/or shareholders before a transfer of shares may be too onerous a restriction and may be subject to abuse. Such a provision may make it virtually impossible for a shareholder to dispose of his or her interest in the company. While the predominant desire may be to ensure that the present shareholders are not forced to deal with a shareholder they do not approve of, the liquidity of the investment of each shareholder must also be taken into consideration.

The use of pre-emptive rights may be a relatively simple method of accomplishing both of the first two goals noted above. It can be a relatively easy provision to implement, where the shareholder desiring to sell his or her investment is permitted to establish the sale price and the terms and conditions of sale. However, it may be desirable to ensure that the offer being made by the proposing transferee is within certain guidelines of price, terms and conditions, which can be predetermined in the shareholders’ agreement.
of an immediate large capital outlay to purchase the investment of the shareholder that is leaving the company.

Where the company is to be the buyer of shares, the company's articles should be reviewed to confirm whether it must make an offer to every shareholder of the class of shares to be purchased to purchase rateably. The lawyer should consider whether a waiver of those shareholders' rights by the remaining shareholders is sufficient or whether the company must actually make the offer and have the remaining shareholders refuse.

Paragraph 5.06 of the model agreement requires that each share certificate representing shares of the company will have endorsed on it a notice that the shares represented by the certificate are transferable only in compliance with the shareholders' agreement. The obvious purpose of this notice is to alert any potential buyers of the restrictions on transfer contained in the shareholders' agreement. Further, the provision of this notice is consistent with s. 57(1)(e) of the Business Corporations Act, which requires that restrictions on the transfer of shares will be noted in a conspicuous statement on the face of the certificate. While this section of the Business Corporations Act may more particularly refer to restrictions contained in the articles of the company, the practice contemplated in paragraph 5.06 of the model agreement is a good one.

Note that some forms of articles may provide for restrictions on the transfer of shares that may be in conflict with or create ambiguities as to the procedure set out in the shareholders' agreement. The articles may have to be amended accordingly. Finally, pre-emptive rights may be enhanced by adding "drag-along" or "tag-along" provisions.

Drag-along rights (also called draw-along rights) usually require that if a shareholder or group of shareholders holding a certain majority of the outstanding shares (collectively, the "transferors") receive a bona fide arm's length offer to purchase the transferors' shares they can require that all other shareholders of the company sell their holdings to the same buyer on the same terms, including price per share.

In most cases drag-along rights are granted by minority shareholders to majority shareholders (and not vice versa) and are intended to facilitate situations in which a buyer wants to acquire all of the issued shares of a company that is controlled by the majority shareholder. This permits the majority to control negotiations for the sale of the company to a third party purchaser, and makes the company considerably more attractive to the third party purchaser who need not worry that a minority shareholder could prevent the sale of 100% of the company.

Conversely, tag-along rights (also called piggy-back rights) offer a degree of protection to minority shareholders. Under a tag-along right, minority shareholders are entitled to require that, before the transferor (in most cases a controlling shareholder) is entitled to accept an arm's length third party offer, the minority shareholders must be made the same offer by the buyer.

Part 6 of the model agreement uses drag-along and tag-along rights for buyers seeking an aggregate of 60% of the issued and outstanding shares in a company.

[§18.08] Compulsory Buy-Out

It may be difficult for a minority shareholder of a closely held corporation to find a ready market for his or her investment in the company should he or she decide to withdraw. The question as to whether a withdrawing shareholder should be entitled to compel the company or the other shareholders to purchase his or her shares is a difficult one. The biggest problem with any option to compel the purchase of shares is arriving at a fair value. The various means of establishing a price may include:

- providing that the price be set by a third party (for example, the auditors or some independent arbitrator);
- providing a formula (for example, book value, fair market value or using past or current earnings);
- using a combination of the above; or
- providing that the parties are to agree each year among themselves as to the value of the shares, and that this value will be in force for the ensuing year.

If a third party sets the price, the third party should be totally independent. Although there may be some advantage in having the value of the shares assessed by someone already familiar with the company, there is a danger of bias. However, it is sometimes thought by the shareholders that the advantages of having the company's auditors or outside accountants determine the value outweigh the potential bias.

The determination of an appropriate formula for valuation is an area where the lawyer should quickly realize the limitations of his or her expertise. The auditors or accountants for the company and the shareholders themselves are likely to be far better judges of what is an appropriate method for determining value with respect to the investment in the company. Alternatively, the company may wish to engage the services of a chartered business valuator to determine the most appropriate method.

While it might be advantageous to provide that the members will agree in each year as to the fair value of the shares, this should not be the only method of valuation. There is a good chance that the shareholders will fail to determine the value, thereby having any earlier agreement quickly become stale-dated. Certainly, where one of the shareholders perceives that he or she is on the way out and the others are aware of this also, a
conflict is created.

Part 7 of the model agreement uses a "shotgun" or "roulette" clause in an attempt to solve the problem of an otherwise illiquid investment. It also is useful as the ultimate remedy (and threat) for dispute resolution, whether or not either side of the dispute is in default or breach of its obligations. The dispute may simply be as to the future direction of the company. Notwithstanding, it is often inappropriate to use a shotgun clause in shareholders' agreements, particularly when there are inequities in the relative financial capabilities of the shareholders.

The model agreement enables one or more of the shareholders desiring to offer all, but not less than all, of his or her investment in the company to give notice to the remaining shareholders requiring that they either sell their investment to the instigator, or purchase the instigator's investment. This can be a simple and very effective clause where there are only two shareholders or two groups of shareholders in the company. However, in the facts assumed in this chapter and the model agreement, there are three shareholders and the simplicity of a compulsory buy-out has evaporated. Where all of the offerees elect to take the same action there is little confusion. However, where one of the remaining shareholders elects to sell to the instigator and the other elects to buy from the instigator, a rather complex vicious triangle results. The language for the solution to this problem is untested and should be considered closely before use.

As an alternative to a "shotgun" provision, it may be desirable to include a clause which allows a shareholder to require that the other shareholders either purchase his or her investment in the company or agree to sell 100% of the shares of the company to a third party. Obviously, this provision requires a third party who is willing to buy the shares of the company, and is based on the assumption that it is easier to sell all of the company than a fraction of it. This is certainly true where that fraction happens to be less than one-half.

§18.09 Investment Sale On Death

The concerns regarding the transfer of shares on the death of a shareholder, or the representative of a shareholder where that shareholder is a company, are essentially similar to those where there is an inter vivos transfer. On one hand, the remaining shareholders will want to ensure that the shares do not go to the heirs of the deceased shareholder. Alternatively, each shareholder will probably want to ensure that his or her investment in the company will be purchased from his or her estate at a fair price, and on terms and conditions that will enable the estate to be "cashed out" of its investment in the company.

Where the value of the deceased shareholder's investment in the company is substantial, there is potential for hardship and inconvenience on the remaining shareholders, which may threaten the viability of the company. There are several ways in which this additional burden of having to purchase the investment of the deceased shareholder can be lightened, including:

- the company could take out policies of insurance on the life of each of the shareholders to fund the acquisition of the deceased's investment in the company from the estate;
- the purchase price payment could be spread over a period of time; and
- the company could become involved in the purchase of the investment, thereby enabling it to use its financial resources and assets to finance the payment of the purchase price.

The model agreement is drafted to provide that the remaining shareholders will purchase the deceased's investment in the company. In order to lessen the hardship that will result, two of the above three provisions have been included in the model agreement, for example:

- Part 8 of the model agreement requires that the company maintain life insurance policies on the lives of each of the shareholders, if possible, in minimum amounts determined as a percentage of the estimated value of each shareholder's investment in the company. If any of the shareholders are uninsurable, all of the provisions in the model agreement relating to the investment sale on death should be reconsidered; and
- the payment of the purchase price is to be made over a period of time. This, of course, is not the case where the proceeds of insurance are sufficient to pay the purchase money at the closing.

Some of the advantages of having the company purchase the life insurance on the lives of its shareholders are as follows:

- the premiums on the insurance are paid at the company's level. If the marginal tax rate of the company is lower than that of the shareholders, the cost of funding is cheaper than under a criss-cross arrangement;
- the payment of premiums by the company may be a deductible expense to it if the life insurance policy is assigned to a financial institution as collateral for a loan as provided in Interpretation Bulletin IT-309R2; and
- it is less complicated to have the company purchase the insurance on the lives of its shareholders than to have the shareholders purchase crisscross insurance.
However, the tax consequences of life insured corporate buy/sell arrangements in private companies must be considered. Before the April 1995 Income Tax Act amendments, it was possible to structure buy/sell arrangements in a shareholders' agreement so that any taxable capital gain to the deceased shareholder on death would be offset against a capital loss to the deceased's estate on a redemption of the deceased's shares.

Under this type of arrangement, the company would purchase and pay the premiums on insurance on the life of the shareholder. Shortly after the death of the shareholder the company would use the net life insurance proceeds to redeem the deceased's shares. The company would then elect to treat any deemed dividend to the estate as a capital dividend, which would be distributed to the estate tax-free. The estate would be deemed to have disposed of the shares for proceeds of disposition equal to the sale price less the amount of the capital dividend. This would result in a capital loss to the estate, which would be offset against the capital gain realized by the deceased shareholder, resulting in no net tax being payable on the appreciation of the deceased's shares.2

However, changes to s. 112 of the Income Tax Act generally limit the capital loss to the estate on the redemption of shares by the company to 50% of the capital gain realized by the deceased shareholder.

There is a limited grandfathering of existing buy/sell arrangements under the amendments. If a company was the beneficiary of an insurance policy on the life of a shareholder on April 26, 1995 and a written buy-sell agreement was in place before April 1, 1997, the "old" rules will apply.

Now that the amendments are in effect, it is advisable to consult a tax practitioner before drafting a life-insured buy/sell arrangement. Generally, a lawyer drafting a shareholders' agreement should consider carefully the personal and tax situation of the individual shareholders and the company before proposing any particular structure for a life-insured corporate buy/sell. In particular, the lawyer should consider whether an individual shareholder has exhausted his or her $750,000 lifetime capital gains deduction on qualified small business corporation shares; whether a spousal rollover is available or appropriate; and whether a deferred sale would not result in a more favourable tax treatment.

Part 9 of the model agreement was not drafted with the amendments in mind, and must be adapted to the particular tax situation of a company and its shareholders. Consult a tax practitioner and your client's accountant.

[§18.10] Default

Default under the shareholders' agreement can take the following forms:

- a shareholder may default in his or her obligations under the shareholders' agreement; or
- one of the shareholders may default in his or her agreement to advance additional monies to the company when requested.

In a shareholders' agreement, it also is necessary to provide for a situation in which a shareholder is no longer employed by the company. The model agreement takes a somewhat extreme position in enabling the non-defaulting shareholders to cause the forced sale by the defaulting shareholder of his or her investment in the company upon default as defined. Lesser remedies are also available. It is the intention that the threat of a forced sale of the investment, perhaps at a slightly reduced price, will be incentive to each of the shareholders to be good corporate and contractual citizens. This Part, together with the compulsory buy-out in Part 7 of the model agreement, works not only as a means of curing a default or providing liquidity to the investment of a shareholder, but acts also as the "big stick" which encourages each of the shareholders to find some alternate and less drastic solution to the problems which may be developing between the shareholders.

[§18.11] Tax Considerations

Practitioners should keep certain income tax issues in mind when drafting shareholders' agreements3. These income tax issues touch on the subjects dealt with in this chapter.

A corporation that is controlled by one or more non-resident or public company shareholders will not qualify as a Canadian controlled private corporation ("CCPC")4 and, as such, will not qualify for a number of important tax benefits, including eligibility for the lowest possible corporate tax rate. Accordingly, if possible, shareholders' agreements should be drafted so as to ensure that non-resident or public company shareholders do not hold sufficient voting shares to elect a majority of the members of the board of directors unless there are compelling commercial reasons for giving such shareholders control of the corporation.

Income tax issues also can have an impact on financing and shareholder contribution - distribution issues. For example, the choice of the vehicle by which a

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2 In the first year after death, capital losses of the estate can be carried back to offset any capital gains of the deceased individual on deemed capital gains and losses determined immediately before death.

3 The following discussion examines certain tax issues that typically arise when drafting shareholders' agreements. This is not an exhaustive discussion of tax issues relating to shareholders' agreements and it is always recommended that a tax practitioner be consulted when drafting a shareholder agreement.

4 As that term is defined in the Income Tax Act (R.S.C. 1985, c. 1).
shareholder finances the corporation (that is, shares, loans or guarantees) will impact on that shareholder's ability to claim a tax loss in the event that the corporation does not succeed. In particular, losses realized on bad loans, or on payments made to honour guarantees, can only be deducted for income tax purposes where it can be demonstrated that the loan or the guarantee was granted for the purpose of earning income.

According to current jurisprudence and administrative position of the Canada Revenue Agency ("CRA"), loans or guarantees made by shareholders can be said to have been made for the purpose of earning income on the basis that the shareholder had an expectation of earning dividend income. However, persons other than shareholders may not be able to demonstrate the requisite expectation of income for loans or guarantees made to corporations in which they do not hold shares. Where there is no expectation of income, the lender or guarantor cannot deduct the loss realized on the loan or guarantee against other income. Generally, this situation can be remedied by charging interest on loans and guarantee fees on guarantees.

The drafting of the buyout provisions of a shareholders' agreement can have tax implications also. For example, a right to purchase shares or to cause the corporation to repurchase shares exercisable on the occurrence of an event, other than the death or permanent incapacity of another shareholder, will generally be deemed to have been exercised by the holder of such right for income tax purposes. If the corporation has non-resident or public company shareholders, the existence of such buyout rights could render the corporation ineligible for CCPC status. In general, to the extent that a clause cannot be unilaterally exercised by non-resident or public company shareholders to obtain control over a majority of the votes in a corporation, such rights will not have any impact on the CCPC status of the corporation. The current administrative position of the CRA is that buyout rights which cannot be unilaterally exercised by a shareholder to acquire control of a corporation will not be taken into account for determining whether or not a corporation is a CCPC. The examples given by the CRA of clauses which are not problematic include shotgun and right of first refusal clauses.

Income tax issues will have a significant impact on the provisions of the shareholders' agreement relating to investment sale on death. Where shares of the corporation qualify for the $750,000 capital gains exemption, the estate of a deceased shareholder and his or her spouse may each wish to take advantage of this exemption. To take advantage of this income tax benefit it may be necessary to provide for a "put/call" option upon death as opposed to the mandatory sale of shares provided for in Part 7 of the model agreement. The use of the "put/call" type option can balance the need of the surviving shareholders to prevent the involvement of the heirs of the deceased in the management and control of the corporation with the need of the heirs of the deceased to minimize the income taxes payable on the buyout.

Some shareholders who held shares before April 27, 1995 may be exempt from the application of the stop loss rule referred to in §18.08 and as such can benefit from the special tax advantages available with proper planning. A repurchase of grandfathered shares can be done on a tax-free basis to the extent of the portion of the repurchase price that is funded with life insurance. A share will be grandfathered where the following conditions are met:

(a) the share was owned by the individual (or a spouse or spousal trust) on April 26, 1995;

(b) the ultimate redemption or repurchase of the share following the death of the shareholder is made under a written agreement that was in place on April 26, 1995; or

(c) on April 26, 1995, a corporation held life insurance on the life of the shareholder (or spouse) and one of the main purposes for the acquisition of the insurance was to fund the repurchase or redemption of the share following the death of the shareholder (or spouse). Moreover, the share must ultimately be repurchased or redeemed with the proceeds of life insurance on the life of the shareholder (or spouse).

Practitioners who are asked to draw up shareholders' agreements for corporations that existed before April 27, 1995 should determine whether or not any particular shares of the corporation are grandfathered.

Where the shareholders do not benefit from the grandfathering rules, the shareholders' agreement must be structured to ensure the maximum amount of flexibility in order to take into account the different interests of the heirs of the deceased shareholder and the surviving shareholders. This means that the death buyout provisions should provide for either a corporate repurchase of the shares from the estate or heirs of the deceased or a cross-purchase of such shares from the surviving shareholders.

If the buyout is to be funded with corporately held life insurance, the shareholders' agreement may provide that the life insurance proceeds will be distributed to the surviving shareholders to be used to fund the cross-purchase. This may ensure that the heirs of the deceased shareholder are not prejudiced from a tax point of view and that the maximum possible tax benefit is derived by the surviving shareholders from the life insurance capital dividend.
Different considerations will ultimately determine the tax impact of the buyout such as whether or not the deceased and his or her heirs are eligible to claim the capital gains exemption of the disposition of the shares, as well as whether or not the buyout is funded with life insurance or by the corporation. Ultimately, the balance of interests can probably be best determined at the time of death and, therefore, the shareholders' agreement should contain the maximum amount of flexibility to ensure that different options are available in the structuring of the buyout. Furthermore, the parties may ultimately determine at the time of death that their common interests require that the buyout be done in a manner different than that provided in the shareholders' agreement and may agree to act on that basis.
Chapter 19

The Canada Business Corporations Act¹

All section references in this chapter are to the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 (“CBCA”) unless otherwise indicated.

[§19.01] Introduction

The purpose of this chapter is to review, briefly, the law relating to CBCA corporations. This chapter includes matters every lawyer practising in British Columbia should know about CBCA corporations (whether or not he or she has a significant involvement with them) and problems that practitioners encounter from time to time in dealing with CBCA corporations. This chapter also refers to the *Business Corporations Act* (British Columbia) (“BCA”), and to companies incorporated under that Act (“BCA companies”); it assumes that the reader is reasonably knowledgeable about BCA companies, and to avoid lengthy duplication, the chapter mentions only the more important ways in which CBCA corporations differ from BCA companies.

Effective November 24, 2001, the federal government amended the CBCA and the *Canada Cooperatives Act: An Act to Amend the Canada Business Corporations Act and the Canada Cooperatives Act*, S.C. 2001, c.14 (SI/2001.14). This legislation was the first major revision to the CBCA since it was enacted in 1975 and was intended, in the words of Industry Canada, to “expand shareholder rights, enhance global competitiveness, clarify responsibility, eliminate duplication and reduce costs”.

The amendments to the CBCA have made incorporating under this statute very attractive. When deciding whether to incorporate under the CBCA or BCA, consider, among other things, the current and future objectives of the corporation. For example, how does the corporation intend to manage start-up and long-term financing? Where are the shareholders located and who are they? Are there market interests in other provinces and/or in the United States?

[§19.02] Capacity and Powers of CBCA Corporations

A CBCA corporation has the capacity and powers of a natural person, subject to restrictions in the CBCA (s. 15). Note that a CBCA corporation may not carry on the business of a bank, insurance company, trust company or loan company (s. 3(4)). It also may not carry on the business of a degree-granting institution, unless expressly authorized to do so by the applicable regulatory authorities governing educational institutions (s. 3(5)). Restrictions on capacity may be provided for in a corporation’s articles, although s. 16(3) states that no act of a corporation is invalid by reason only that it is contrary to its articles or the CBCA.

[§19.03] Comparison of a CBCA Corporation with a BCA Company²

This section compares some key provisions of the CBCA with those of the BCA.

This discussion emphasizes the differences between the two acts and summarizes the effect of those acts in order to highlight these differences. When giving advice on specific issues arising under either of the acts, refer directly to the acts.

1. Differences
   (a) Out-of-Province Shareholders and Out-of-Province Contractors

   Lawyers and businesses use the CBCA because it is understood throughout Canada. While it is federal legislation, many provinces have adopted acts that are virtual copies of the CBCA. To a certain extent, therefore, the CBCA has become the national standard. British Columbia, on the other hand, has chosen to adopt an act that is unique. Companies with shareholders or contractors in other provinces may find it easier to deal with those people if the company operates as a CBCA corporation under a statute that is understood across Canada, rather than under the unique BCA.

¹ Peter J. Brown and Diane E. Campbell, both of Edwards, Kenny & Bray LLP, kindly revised this chapter in November 2010 and February 2012. Peter Brown also revised the chapter in July 2005, July 2006 and June 2008. This chapter, other than §19.03, was revised in March 1997, 1999 and 2001 by Lawrence W. Talbot, Gowling Lafleur Henderson LLP, Vancouver. Reviewed and revised in January 1995 by Gregory D. Lewis, Bull, Housser & Tupper, Vancouver. The chapter in its first version was based on a paper prepared by E.F. Horsey, Q.C for a Continuing Legal Education Seminar in 1983.

(b) Name Protection

Most provinces have legislation that requires a company incorporated elsewhere to be registered in the province if the company carries on business in the province. CBCA corporations have name protection, which enables them to use their corporate name anywhere in Canada, subject to trademark rights. Companies incorporated under provincial legislation must register under a name that is acceptable to the registrar of the province concerned. In some provinces, this can create difficulties if another company that has incorporated in the province in question is already using the company’s name.

(c) Disability if not Registered

Most provinces impose a penalty on extra-provincial companies that do not register, as required by their legislation. This penalty normally takes the effect of an inability to commence an action with respect to a contract formed in the jurisdiction unless and until the company completes the registration requirements. For constitutional reasons, this disability cannot apply to a CBCA corporation, but can apply to a BCA company.

(d) Drafting Style

The CBCA is drafted simply and is easy to understand. It deals with most issues in more general terms than the BCA does.

By contrast, the BCA has adopted a more complex drafting style. As a result, it is more difficult to understand, but has the advantage of greater precision.

(e) Residence of Directors

The CBCA requires that 25% (and in limited circumstances a majority) of the directors of a CBCA corporation be “resident Canadians” as defined in the CBCA. If a corporation has fewer than four directors, at least one director must be a resident Canadian.

There is an exception for holding companies. Only one-third of the directors need be resident Canadians in the case of a holding corporation earning in Canada directly or through its subsidiaries less than 5% of its gross revenues on a consolidated basis.

The BCA has no residency requirements for directors.

(f) Due Diligence Defence for Directors

The due diligence defence available to directors under sections 123(4) and (5) of the CBCA is slightly broader than the comparable defence under the BCA, in that the CBCA recognizes any means of exercising the “care, diligence and skill that a reasonably prudent person would have exercised in comparable circumstances”. The BCA on the other hand, lists the specific items on which a director can rely. However, in practice, the distinction may not be very great.

(g) Transfer of Directors’ Powers

The BCA allows powers normally reserved to directors, and the liability which goes along with those powers, to be transferred to the shareholders, including for example, paying a dividend, hiring a new chief executive officer, and starting a new line of business. Under the CBCA, the same result can be achieved by a unanimous shareholders’ agreement. However, under the BCA, the provision must be put in the articles themselves, without the need of a separate agreement, thereby avoiding conflict between two documents that govern the company’s affairs. Putting the provision in the articles makes it available to the general public but does not necessarily make it binding on third parties (see ss. 33, 136, 137 and 146 of the BCA).

(h) Alteration of Charter Documents

The BCA provides a great deal of flexibility in the level of approval required to alter the charter documents. For example:

(i) The definitions of “special resolution” and “special majority” in the BCA provide that a special resolution can require anything between a two-thirds majority and a three-quarters majority, as the articles provide. Without a provision in the articles, a special resolution requires two-thirds of the votes cast in the case of a company incorporated under the BCA, and three-quarters of the votes cast in the case of a pre-existing company that has not removed the application of the Pre-existing Company Provisions of the Regulation to the BCA.

(ii) The BCA states that subject to the minimum requirements of the BCA, the articles can stipulate that provisions of the charter documents can be altered by whatever level of resolution is provided
for in the articles, in some cases including even a directors’ resolution. The BCA also states that a company may even specify in its articles that a provision of its notice of articles or its articles may not be altered unless the resolution is passed as an exceptional resolution, which is a resolution passed by a majority greater than the two-thirds or three-quarters majority referred to in paragraph (h)(i).

(i) Share Rights

Under section 59(5) of the BCA special rights or restrictions may apply differently to some shareholders than to others. This section permits, for example, a provision in the rights and restrictions attached to a class of shares that no shareholder can vote more than 25% of the shares, or that shares, when owned by the founder, will have ten votes per share and when owned by anyone else will have only one vote per share. This would not be a valid provision under the CBCA (McClurg v. Canada (1990), 76 D.L.R. (4th) 217 (S.C.C.) and Bowater Canadian Ltd. v. R.L. Crain Inc. (1987), 62 O.R. (2nd) 752 (C.A.)).

(j) Records

The record keeping responsibilities imposed on the people who maintain the records of a BCA company are greater than those imposed on the people who perform a similar function for a CBCA corporation. For example, under the BCA, the company’s records are the only source for the rights and restrictions attached to shares, whereas under the CBCA, the share characteristics can be verified by checking filings made with the Director. The BCA also contains a more extensive list of the records to be kept and who can see those records. Under the BCA, many documents, including all minutes and resolutions of shareholders and directors, must be date and time stamped when received in the records office. There is no similar provision under the CBCA.

(k) Financial Issues

i. payment of dividends

The CBCA has two rules governing the payment of dividends:

- The corporation must be able, both before and after payment of the dividend, to pay debts as they become due.

- The realizable value of the corporation’s assets must, after payment of the dividend, be at least equal to the aggregate of its liabilities and stated capital of all classes.

The BCA contains the first rule but not the second. The omission from the BCA of the second rule makes it easier to pay dividends in certain circumstances under the BCA. Of course, under both statutes, the directors must be satisfied that the payment of dividends complies with their duty to act prudently and in the best interest of the company.

Similarly, the rules in the CBCA for redemptions and repurchases of shares also refer to the stated capital account, but the BCA does not.

ii. waiving financial statements and annual general meetings

The CBCA requires that an annual general meeting of shareholders be held annually and that financial statements be placed before the shareholders at that meeting. The BCA contains similar provisions but allows the shareholders to waive the production and publication of financial statements by unanimous resolution of all shareholders (including non-voting shareholders) and to waive the holding of an annual general meeting by a unanimous resolution of all voting shareholders.

iii. par value shares

The BCA allows companies to have par value shares, while the CBCA, in common with most other corporate legislation in Canada, has abolished par value shares.

(l) Liability for Wages

Section 119 of the CBCA makes directors liable to employees of the corporation for all debts not exceeding six months’ wages. The comparable provision in British Columbia is contained in the Employment Standards Act, which provides, in section 96, that the liability is limited to two months’ wages, but applies to officers as well as directors.

(m) Holding Shares of Parent

The BCA permits a company to hold shares of its parent corporation while the CBCA prohibits a corporation from owning shares of its parent except in limited circumstances.
(n) Going Private Transactions

A going private transaction is defined generally to be a transaction that results in the interest of a holder of equity shares of a corporation being terminated without the consent of the holder and without the equity shares being exchanged for comparable equity securities.

The *CBCA* refers all such transactions to provincial securities laws. Provincial securities laws generally require that such transactions be approved by a majority of the shareholders whose equity shares will be acquired. The *BCA*, on the other hand, seems to provide in section 289(1)(c) that in the case of an arrangement, which is the most common method followed to achieve a going private transaction, the transaction must be approved by a special majority of the shareholders whose shares will be cancelled. This special majority will be either two-thirds or three-quarters, depending on what the charter documents of the company provide. The effect is to increase the level of minority support required for the transaction.

2. Similarities

(a) Pre-Emptive Rights on New Share Issues

The provision requiring pre-emptive rights on new share issues has been removed from the *BCA*, making it parallel to the *CBCA*.

(b) Indemnification of Directors

The *BCA* has removed the requirement to obtain court approval before indemnifying a director and also permits a company to advance defence costs. Both these provisions are similar to the *CBCA*.

(c) Amalgamations

The *BCA* provides, like the *CBCA*, that amalgamations can be accomplished without court order. The *BCA* also provides for short form vertical and horizontal amalgamations. But, unlike the *CBCA*, the *BCA* provides for inter-jurisdictional amalgamations, if the other jurisdiction also provides for them.

(d) Electronic Meetings

The *BCA* provides for electronic meetings of shareholders and directors, as does the *CBCA*.

(e) Financial Assistance

The *BCA*, like the *CBCA*, has removed the prohibition against a company giving financial assistance in connection with the purchase of its shares.

(f) Unlimited Number of Authorized Shares

The *BCA* provides, as does the *CBCA*, for a company to have an unlimited number of authorized shares.

§19.04 Words with Special Meanings under the *CBCA*

Under the *CBCA*, certain terms are used:

- “articles” or “articles of incorporation” correspond to parts of the “incorporation application and notice of articles” of a *BCA* company;
- “by-law” or “by-laws” correspond to the bulk of the articles of a *BCA* company;
- “Director” means the Director appointed under the *CBCA*;
- “distributing corporation” is defined in the Canada Business Corporations Regulations, s. 2. The definition means a “reporting issuer” or “distributing corporation” as defined under any provincial securities or business legislation. A distributing corporation corresponds to a “reporting issuer” under the *BCA* and to a “reporting issuer” under the *Securities Act* (British Columbia);
- “incorporator” means a person who signs the articles of incorporation under the *CBCA*;
- “security” means a share of any class or series of shares or a debt obligation of a corporation and includes a certificate evidencing such a share or debt obligation;
- “special resolution” means a resolution passed by a majority of two-thirds; and
- “shareholder” is an undefined term, but as used in the *CBCA* it simply means the holder of a share.

§19.05 Incorporation Procedures

1. Name Selection and Reservation

(a) General rules

The same general rules apply when selecting a name for a *CBCA* corporation as for a *BCA* company. Each name must contain a distinctive element (perhaps a surname or other unique term), a descriptive element (e.g. Manufacturing, Consulting, Trading) and a mandatory legal element (e.g. Corp., Inc., Ltd.). These rules are located in the Canada Business Corporations Regulations (the "Regulations"): Part 2. The Name Granting Compendium and the Electronic
Training on Federal Corporate Name Granting provide guidelines for interpreting the name regulations.

For a name to be accepted, you must have a Newly Upgraded Automated Name Search ("NUANS"), a search that compares a proposed corporate name or trade-mark with databases of existing corporate bodies and trade-marks. A NUANS report may be ordered directly from the NUANS “Do it yourself” Real-Time System or with the assistance of a private search house (which may also provide advice, recommendations and other related services).

If you want to ensure that a name is available before you file your Articles of Incorporation, you may request that the Director approve the proposed name in advance. You do this by submitting the applicable NUANS search and a Corporate Name Information Form (there is no additional fee for this service). This approval, if granted, is valid for the life of the NUANS search report (90 days from the date when the report is requested).

Because finding an appropriate name can be time-consuming and it may be important to have the corporation incorporated quickly, many corporations incorporate with a number name (e.g., 123456 Canada Ltd.). Corporations Canada issues the number. The name is left blank in the articles when filed.

A change of name can take place later when a name has been accepted. The NUANS database has the names of all corporations incorporated in all jurisdictions in Canada, all business names used in Canada, and also all trade marks and trade names. A NUANS search report must be filed with the articles where a name (other than a number name) is used unless the name has been pre-approved, in which case you must file a copy of the name approval document.

(b) Special rules as to names

Often, both an English and a French form of the name will be used. The name must end with the words “Limited”, “Incorporated” or “Corporation”, their abbreviations, or the French version of those words (s. 10).

2. Documents

Under the CBCA the by-laws are not a public document and need not be filed. The articles of incorporation are a public document and accordingly must be filed.

In order to incorporate a CBCA corporation, certain required documents and a fee must be sent to Corporations Canada, Industry Canada, 9th Floor, Jean Edmonds Towers South, 365 Laurier Avenue West, Ottawa, Ontario K1A 0C8. The documents and fees are as follows:

- Articles of Incorporation (Form 1);
- Initial Registered Office Address and the First Board of Directors (Form 2);
- if you requested prior approval of the name of the corporation, the letter from the Director approving the name (with a copy of the NUANS report);
- if you did not request prior approval of the name, a NUANS report not more than 90 days old and a Corporate Name Information Form (unless you are requesting a number name, for which, in most circumstances, a NUANS report is not required); and
- incorporation fee as prescribed (as of November 1, 2010 it was $250, or $200 if filings are through the Corporations Canada Online Filing Centre).

Copies of Form 1 and Form 2 are attached to this Chapter as Precedents 7 and 8.

See the CBCA Incorporation Kit for details on the completion of these documents. The Kit may be accessed on the Internet at: http://strategis.ic.gc.ca/epic/internet/incd-dgc.nsf/en/h_cs02141e.html.

Corporations may transmit notices and documents to the Director in electronic form (ss. 258.1). Payment of any prescribed fees may be made by credit card or a deposit account maintained with Corporations Canada at the time of filing. The use of the electronic filing methods (fax and e-mail) is voluntary, and paper-based filing remains available. Electronic filing may be done through Corporations Canada Online Filing Centre: http://strategis.ic.gc.ca/cgi-bin/sc_mrksv/corpdir/corpFiling/register.cgi?lang=e. All “key” CBCA applications are available online.
3. Articles of Incorporation

Following are some of the features and effects of the articles of incorporation of a CBCA corporation.

- The articles of incorporation must state the province or territory in Canada where the registered office is to be situated and the actual address must be set out in the Form 2 – Initial Registered Office Address and the First Board of Directors.
- The articles of incorporation must state the restrictions (if any) on share transfers.
- The articles of incorporation must state the number of directors, or the minimum and maximum number.
- The articles of incorporation may state any provisions permitted by the CBCA or by-law to be set out in the by-laws of the corporation (s. 6(2)).
- The articles of incorporation do not constitute an agreement of an incorporator to be a shareholder of the corporation. In fact, the incorporator does not automatically become a shareholder of the corporation. The CBCA articles of incorporation merely constitute an application by incorporator(s) to form a corporation.
- The incorporators do not become the first directors of the corporation under the CBCA. The directors of the corporation are those individuals listed in the Form 2 – Initial Registered Office Address and the First Board of Directors.
- A corporation comes into existence when a certificate of incorporation is issued.
- At the time of incorporation, a CBCA corporation has no by-laws.
- A CBCA corporation may have the benefit of, and be bound by, a pre-incorporation contract entered into on its behalf before it came into existence although, in order to do so, it must, by action or conduct signifying its intention to be bound by it, adopt it within a reasonable time after the corporation comes into existence (s. 14(2)).

4. Organizational Meetings

The organizational meeting of the directors of a CBCA corporation is similar to the organizational meeting of a BCA company except:

- the directors of a CBCA corporation must pass by-laws. The CBCA corporation by-laws are effective when made by the board of directors. The by-laws are effective only until the next shareholders’ meeting, and accordingly, it is common to have the shareholders approve the by-laws immediately after the organizational meeting of the directors. Resolutions in writing of both the directors and shareholders are effective in the same way as they are under the BCA (sample by-laws are attached to this Chapter as Precedent 9);
- at the organizational meeting, the directors should approve subscriptions for, and authorize the issuance of, shares because, before the actual allotment and issuance, the CBCA corporation has no issued or outstanding shares or shareholders.

5. Registered Office

A CBCA corporation must at all times have a registered office in the province in Canada specified in its articles (s. 19). Its corporate records must be maintained at its registered office or at any other place in Canada designated by its directors (s. 20). These records will contain:

- the articles and by-laws and a copy of any unanimous shareholders' agreement;
- minutes of meetings and resolutions of shareholders;
- copies of all notices of directors and notices of change of directors or a director’s address; and
- a securities register that complies with s. 50.

In addition, the corporation is obliged to prepare and maintain adequate accounting records, minutes of meetings, and resolutions of directors and committees of directors.

6. Rights of Examination of Corporate Records

Shareholders and creditors of a corporation, their personal representatives and the Director may examine the articles, by-laws, a copy of any unanimous shareholders agreement, minutes of meetings and resolutions of shareholders, copies of directors’ notices, and the securities register (s. 21(1)). Only the shareholders and creditors, their personal representatives and the Director are entitled to examine these records if the corporation is a non-distributing corporation. On the other hand, any person may examine such records of a distributing corporation (subject to some other requirements as described below).
Any person who wants to examine the securities register of a distributing corporation must make a request to the corporation or its agent. An affidavit must accompany the request (s. 21(1.1)). The affidavit must confirm that the list will not be used, except in connection with:

- an effort to influence the voting of a shareholder of the corporation;
- an offer to acquire securities of the corporation; or
- any other matter relating to the affairs of the corporation.

Under the *CBCA*, incorporation is regarded as a right, so it is difficult for a member of the public to inspect the records of a *CBCA* non-distributing corporation.

[§19.06] **Corporate Finance**

The *CBCA* does not contain the concept of “private” corporations or “reporting issuer”. It does contain certain provisions applicable to corporations that are “distributing corporations” (for example, the requirement for not fewer than three directors under s. 102(2)). However, most of the *CBCA* applies in the same way to corporations that are publicly traded as to those that are not.

1. **No Par Value Shares Only**
   Shares of a *CBCA* corporation must be no par value shares. If rights, privileges, restrictions or conditions are attached to shares, they must be set out in the articles (s. 24).

2. **Unlimited Number of Shares Permitted**
   It is not necessary for a *CBCA* corporation to have a limited number of authorized shares or capital. It is common for the articles to provide that the corporation may issue an unlimited number of shares.

3. **Shares to be Fully Paid**
   A share may not be issued until the consideration for the share is fully paid in money, or in property or past services that are not less in value than the fair equivalent of money that the corporation would have received if the share had been issued for money (s. 25(3)). “Property” does not include a promissory note, or a promise to pay, that is made by a person to whom a share is issued, or a person who does not deal at arm’s length, within the meaning of that expression in the *Income Tax Act*, with a person to whom a share is issued (s. 25(5)).

4. **Stated Capital**
   The *CBCA* corporation must maintain a separate “stated capital account” for each class and series of shares that it issues. The corporation must add to the appropriate stated capital account the full amount of any consideration it receives for any shares it issues (s. 26, except in certain specific circumstances where it may choose to add less).

5. **Directors May Fix Special Rights**
   Section 27(1) provides that the articles may authorize the issue of any class of shares in one or more series and may authorize the directors to fix the number of shares in and determine the designation, rights, privileges, restrictions and conditions attaching to shares of, each series, subject to limitations set out in the articles. This can be a useful provision; it permits a distributing corporation, which may have many shareholders, for example, to fix the terms of a preferred share issue by simply filing the required articles of amendment, without having to call a shareholders’ meeting to approve the rate of dividend that is payable (which sometimes must be fixed immediately before a public issue).

6. ** Trafficking in Shares**
   Except in certain circumstances, a *CBCA* corporation may not hold shares in its parent corporation (s. 30(1)); by contrast, a *BCA* company may, although it is not entitled to vote such shares (*BCA*, s. 177). A *CBCA* corporation may purchase its own shares under certain conditions and a pro rata offer need not be made (s. 34).

[§19.07] **Security Certificates, Registers and Transfers**

Part VII of the *CBCA* governs Security Certificates, Registers and Transfers of securities. Under the *CBCA*, it is not a statutory requirement that the date of issue of a certificate representing a security be stated on the certificate, although it must be noted in the securities register (s. 50).

1. **Negotiable Instruments**
   If transfer restrictions are not noted on a security certificate of a *CBCA* corporation, the certificate becomes a negotiable instrument (s. 48(3)). Therefore, it is valid in the hands of a *bona fide* purchaser without knowledge of any defect in title.

A *CBCA* corporation has a duty to register a transfer of shares and is liable if it issues a security certificate to a person not entitled to it. However, if, after the issue of a new security
certificate to an owner who claims that his or her security certificate has been lost, destroyed or wrongfully taken, a bona fide purchaser presents the original security for registration of a transfer, the corporation is not required to register it if registration would result in “overissue” (i.e., issue shares beyond its authorized capital). In such circumstances, the corporation must purchase a security for the person entitled to the validation or issuance of that security if it is reasonably available. If it is not reasonably available, it must pay to the holder an amount equal to the price the last purchaser for value paid for the invalid security (s. 52(1)).

In view of the “negotiability” provisions of the CBCA, it can be quite dangerous to issue replacement security certificates for a lost or stolen security. Consequently, most CBCA corporations’ by-laws require that a bond be put up if a fresh security certificate is issued and the old security certificate hasn’t been produced.

Part VII of the CBCA contains provisions that persons who present securities for the recording of a transfer or who issue securities warrant title and validity of the securities.

2. Registers

The provisions relating to registration of securities (for example, for registrations of allotments and transfers of shares and of members and debentureholders) are quite simple (s. 50).

§19.08 Directors and Officers

Provisions regarding Directors and Officers are found under Part X of the CBCA. Directors of a CBCA corporation fulfill the same role as the directors of a BCA company. Under the CBCA, “the directors shall manage, or supervise the management of, the business and affairs of a corporation” (s. 102(1)).

1. Restraints on Directors' Powers

What restraints can be placed on directors as to their management of the business and affairs of a corporation?

Under the CBCA, the rights and obligations of the directors are subject only to any unanimous shareholder agreement (s. 102(1)). A unanimous shareholder agreement is a written agreement among all shareholders of a corporation, or among all the shareholders and one or more persons who are not shareholders, which restricts, in whole or in part, the powers of the directors to manage, or supervise the management of, the business and affairs of the corporation (s. 146(1)). A unanimous shareholders’ agreement is binding on the directors (s. 102(1)). Further, the CBCA provides that the shareholders have the rights, powers, duties and liabilities of a director to the extent that the unanimous shareholder agreement restricts the powers of the directors to manage, or supervise the management of, the business and affairs of the corporation (s. 146(5)).

2. Shareholder Democracy

Under the CBCA, the directors are to be elected by ordinary resolution at the first meeting of shareholders and at each succeeding annual meeting at which an election of directors is required. Directors are to be elected to hold office for a term not later than the close of the third annual meeting of the shareholders following the election (s. 106(3)). Accordingly, directors must be elected by the shareholders (subject to the right of the directors to appoint up to one third new directors between annual meetings if provided for in the articles (s. 106(8)) and they must be elected for a term not exceeding three years.

Under the CBCA, directors generally may be removed by ordinary resolution (s. 109).

As noted earlier, directors' powers also may be limited by unanimous shareholders’ agreements.

3. Residence

At least 25% of the directors of a CBCA corporation must be “resident Canadians” s. 105(3)). However, if a corporation has less than four directors, at least one director must be a resident Canadian. Section 114(3) ensures that at least 25% of directors at any directors' meeting are resident Canadians.

If a CBCA corporation engages in an activity in Canada that is in a prescribed business sector (see Part 1, s. 16 of the Regulations), then a majority of the directors must be resident Canadians. Similarly, corporations that are subject to ownership restrictions as specified in the Regulations and corporations that individually are subject to ownership restrictions (for example, Petro-Canada) are to have a majority of Canadian residents on their boards (s. 105(3.1)). However, if a corporation that is subject to restricted ownership has only one or two directors, that director or one of the two directors, must be a resident Canadian (s. 105(3.3)). Section 114(3) ensures that a majority of directors at any directors' meeting are resident Canadians.

If the corporation is a holding corporation and earns 95% of its revenues offshore, then only one-third of the directors must be resident Canadians (s. 105(4)).

Business: Company
4. By-laws

The directors may make, amend or repeal by-laws, effective immediately. However, the shareholders must approve the changes by ordinary resolution at the next meeting of shareholders or the by-law ceases to be effective (s. 103(3)).

At an annual meeting of a *CBCA* corporation, a shareholder entitled to vote at the meeting may make a proposal to make, amend or repeal a by-law (s. 103(5)). The proposal and a statement in support (the combined maximum number of words cannot exceed 500) must be included in a management proxy circular sent out in respect of that meeting (s. 137 and Part 6, s. 48 of the Regulations).

5. Delegation of Directors’ Powers

The *CBCA* specifically permits directors of a corporation to appoint from their number a managing director (who is a resident Canadian) or a committee of directors, and to delegate to such managing director or committee any of the powers of the directors (with certain exceptions) (s. 115).

6. Standard for Directors’ Duties

Directors and officers in exercising their powers and discharging their duties must act honestly and in good faith with a view to the best interests of the corporation, and must exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances (s. 122). The standard is essentially the same as under the *BCA*.

Like the *BCA*, the *CBCA* requires a director (and officers who are not also directors) to disclose conflicts of interests. If a director or officer is a party to a material contract or a material transaction (whether made or proposed) with the corporation, that director or officer must disclose, in writing or by requesting to have it entered in the minutes of meetings of directors, the nature and extent of such interest (s. 120). The same obligation arises if the director or officer:

- is a director or an officer, or an individual acting in a similar capacity, of a party to the contract; or
- has a material interest in a party to the contract or transaction.

If a director or officer discloses his or her interest as required, and does not vote on the approval of the contract or transaction, and the contract or transaction is subsequently approved by the directors or shareholders, the contract or transaction is not invalid provided that it was reasonable and fair to the corporation when it was approved.

A director or officer who acts honestly and in good faith but who does not disclose his or her interest is not accountable to the corporation or its shareholders for any profit realized from a contract or transaction, if

(a) the contract or transaction is approved or confirmed by special resolution at a meeting of the shareholders;

(b) disclosure of the interest was made to the shareholders in a manner sufficient to indicate its nature before the contract or transaction was approved or confirmed; and

(c) the contract or transaction was reasonable and fair to the corporation when it was approved or confirmed (s. 120(7.1)).

If the director or officer didn’t disclose the interest, a court may, upon application of the corporation or any of its shareholders, set aside the contract or transaction on any terms that it thinks fit, or may require the director or officer to account, or both (s. 120(8)).

There is a specific provision under the *CBCA* for indemnity and also for the maintenance of insurance for the benefit of a director against liability incurred by him or her as a director (s. 124). Among other things, the statutory indemnification rules expressly allow the corporation to advance defence costs, provide for indemnification in respect of investigative proceedings, and allow the corporation to indemnify a director or officer (or person acting in a similar capacity) of another entity.

7. Officers

Under the *CBCA*, there is no specific provision requiring that certain officers be elected or appointed. Nor does the *CBCA* require that the president be a director. Appointment of officers is under the control of the directors, subject to the articles, by-laws, and any unanimous shareholder agreement (s. 121). It is common for the by-laws of a *CBCA* corporation to set forth specifically the duties of officers of the corporation. Officers of a *CBCA* corporation have the same duty of care and obligation to disclose conflicts of interest as directors (s. 120 and s. 122).
§19.09 Insider Trading, Going Private Transactions and Squeeze-Out Transactions

Under the CBCA those Parts of the Act that prescribe particular treatment for distributing corporations essentially “harmonize” the procedures for dealing with transactions and dealings of distributing corporations and their officers/directors with provincial securities legislation.

Part XVI, section 193, expressly permits “going-private transactions” (GPTs), as defined by the Regulations (see s. 3(1) of the Regulations). Essentially, the definition refers to amalgamations, arrangements, consolidations or any other transaction that would result in the termination of shareholder interests with compensation, but without consent and without a replacement of equivalent value in a participating security; so, it covers the situation where a distributing corporation becomes a private corporation without the consent of the shareholders. The definition is broad and intended to cover all transactions, whether or not a related party in involved. While these transactions are permitted, it is clear that a corporation may not carry out a GPT unless it complies with any applicable provincial securities laws.

The CBCA provisions relating to insider trading—Part XI, ss. 126-131—harmonize with provincial securities legislation. The definition of “insider” covers most instances where insider trading might be expected to occur. The Regulations, rather than the Act, prescribe the number of shares or votes that an individual must hold to be deemed an “insider” (Regulations, ss. 39 and 40). Also, the civil liability provisions define “security” for insider trading purposes expansively in order to help deter insider trading by allowing civil actions to be brought based on that broader definition. Finally, provisions were added in 2001 to impose civil liability on persons who communicate undisclosed confidential information (s. 131).

Part XVI s. 194 expressly permits “squeeze-out transactions”, as defined in s. 2(1) of the CBCA. A “squeeze-out” transaction is a transaction that relates to a non-distributing corporation. The transaction means one that would “require an amendment to its articles and would, directly or indirectly, result in the interest of a holder of shares of a class of the corporation being terminated without the consent of the holder, and without substituting an interest of equivalent value in shares issued by the corporation, which shares have equal or greater rights and privileges than the shares of the affected class”. Section 194 expressly permits a squeeze-out transaction if it is approved by an ordinary resolution of each class of shares that are affected by the transaction.

§19.10 Shareholders

Many of the provisions of the CBCA relating to shareholders are similar to those of the BCA.

1. Meetings

Under the CBCA, the first annual meeting of shareholders must be held not more than 18 months after the date of incorporation, and thereafter, not more than 15 months after the holding of the last annual meeting (s. 133). However, financial statements not more than six months old must be presented to the annual meeting (or to the shareholders signing resolutions in lieu of the meeting, which is permitted under both the BCA and the CBCA).

Meetings must be held at the place within Canada that is named in the by-laws, or if the by-laws do not name a place, then a place within Canada that the directors determine (s. 132(1)). If the articles specify a meeting place outside Canada, or if all shareholders entitled to vote agree, meetings can be held in that place (s.131(2)). In addition, meetings can be held by electronic means (ss. 132(4), (5)).

2. Record Dates

The CBCA has specific provisions permitting directors to fix a date for determining which shareholders are entitled to receive notice of meetings. Under the CBCA, the Regulations prescribe these time-periods (s. 134 and Regulations, s. 43).

3. Form of Notice of Meeting

The CBCA provides that the notice of a meeting of the shareholders at which special business is to be transacted shall state the nature of that business in sufficient detail to permit the shareholder to form a reasoned judgement on it, and shall state the text of any special resolution to be submitted to the meeting (s. 135(6)).

The notice must comply with the prescribed time periods: not less than 21 days, nor more than 60 days, before the meeting (Regulations, s. 44). Note with respect to voting that the CBCA provides that “unless the articles otherwise provide, each share of a corporation entitles the holder thereof to one vote at a meeting of shareholders” (s. 140).

4. Right to Vote

The corporation must prepare a list of shareholders entitled to vote as of the record date for a meeting of shareholders that shows the number of shares held by each shareholder (s. 138). A shareholder whose name appears on
such list of shareholders is entitled to vote the shares shown opposite their name at the meeting to which the list relates.

5. Cumulative Voting

Under s. 107 of the CBCA the articles may provide for cumulative voting in respect of an election of directors. This provision is not often used.

§19.11 Financial Disclosure

1. Report of Directors

Under the CBCA it is not necessary to place a report of the directors before the annual meeting.

2. Approval of Financial Statements

Financial statements are to be prepared in accordance with Canadian GAAP, which means generally accepted accounting principles as set out in the CICA Handbook – Accounting or the CIAC Public Sector Accounting Handbook, as those handbooks are amended from time to time. CBCA corporations that are also registered with the U.S. Securities and Exchange Commission may prepare financial statements using the generally accepted accounting principles established by the Financial Accounting Standards Board of the United States.

As of January 1, 2011, distributing corporations are required to prepare their financial statements in accordance with the International Financial Reporting Standards (“IFRS”). Non-distributing corporations have the choice to use either IFRS or the accounting standards developed for private enterprises.

The CBCA specifically provides that the directors must approve the annual financial statements. The manual signature of one or more directors or a facsimile of the signatures reproduced in the statements evidences director approval. The corporation shall not issue, publish or circulate copies of the financial statements unless so signed and the financial statements are accompanied by the report of the auditor of the corporation, if any (s. 158). The CBCA does not require the directors to approve and sign any interim financial statements.

A corporation must, not less than 21 days before each annual meeting, send a copy of the financial statements and auditor’s report, if any, to each shareholder, except shareholders who have informed the corporation in writing that they do not want a copy of those documents (s. 159(1)).

3. Filing of Annual Financial Statements

There is no requirement under the CBCA to file any financial statements of a corporation with the Director, although companies that are reporting issuers may be required to file their annual and interim financial statements with applicable securities commissions. A distributing corporation under the CBCA that has any outstanding issue of securities that are held by more than one person must send a copy of its annual financial statements to the Director (s. 160).

However, under Policy Statement 11.28.1 – Exemption from the Filing of certain Documents (Single Filing Exemption), a corporation that is required to file its annual financial statements with a provincial securities commission or regulator under a provincial securities act is exempted from filing them with Corporations Canada, as the financial statements are publicly available on the Internet through SEDAR (System for Electronic Document Analysis and Retrieval). SEDAR is the system used for electronically filing most securities related information with the Canadian securities regulatory authorities. Filing with SEDAR started January 1, 1997 and is now mandatory for most reporting issuers in Canada.

4. Waiver of Auditor

A corporation that is not required to file its annual financial statements with the Director may, by unanimous resolution of its shareholders (including the shareholders not otherwise entitled to vote), waive the appointment of an auditor until the next annual meeting of the shareholders (s. 163).

5. Independent Auditor

The CBCA does not require that an auditor be a member of the Canadian Institute of Chartered Accountants or the Certified General Accountants Association of British Columbia or otherwise certified by the British Columbia Auditor Certification Board. A person is disqualified from being an auditor of a corporation if he or she is not independent of the corporation, any of its affiliates, or the directors or officers of the corporation or its affiliates. Under the CBCA independence is a question of fact but the Act prescribes certain relationships in respect of which a person is deemed not to be independent (s. 161).

6. Resignation or Removal of Auditor

The provisions of the CBCA relating to removal or resignation of auditors and replacements are quite detailed. For example, an auditor is required to attend a meeting of the corporation if a
shareholder gives notice to the auditor or former auditor that he or she should attend and answer questions relating to his or her duty as an auditor (s. 168(2)). In addition, no person may accept an appointment as an auditor if he or she is replacing an auditor who has resigned, or has been removed, or whose term of office has expired, until he or she has requested and received from the auditor a written statement of the circumstances and the reasons why, in that auditor's opinion, he or she is to be replaced (s. 168(7)). Also, if a corporation proposes to replace an auditor, the corporation must issue a statement as to why (a copy must go to each shareholder) and the proposed replacement auditor may make a statement in which he or she comments on the reasons referred to in corporate statement (s. 168(5.1) and (6)).

§19.12 Fundamental Changes

1. Special Resolution
   The concept of “fundamental change” is essentially the same under the CBCA as under the BCA. The definition of “special resolution” under the CBCA means “a resolution passed by a majority of not less than two-thirds of the vote” (s. 2(1)). It is by special resolution that most fundamental changes are authorized. Under the CBCA, the notice of a meeting of shareholders is required to contain the text of any special resolution (s. 135(6)) and notice must be given within the prescribed time (s. 135(1)). Consequently, there is effectively a 21-day minimum notice period for a CBCA special resolution, unless all shareholders consent to waive notice of the meeting.

2. Meaning of “Fundamental Change”
   The term “fundamental change” is not defined in the CBCA. Essentially, “it is a change in the constitution of the corporation, or the nature of its business, that is so severe that it fundamentally changes the arrangement under which a shareholder purchased his or her shares in a corporation”.

   In a CBCA corporation, that change may be as simple as a change in the name or may be as severe as an amalgamation with another corporation, changing not only the business but also the capital structure of the corporation.

3. Dissent Proceedings
   Under the CBCA if the change is a “fundamental change”, then there are provisions for dissent proceedings, under which a shareholder may require that the corporation purchase his or her shares for their “fair value” if the “fundamental change” is made. The CBCA provision permitting dissent proceedings (s. 190) is available when the corporation resolves to:
   - amend its articles to add, change or remove any provisions restricting or constraining the issue, transfer or ownership of shares of that class;
   - amend its articles to add, change or remove any restriction on the business or businesses that the corporation may carry out;
   - amalgamate with another corporation, otherwise than under s. 184;
   - be continued under the laws of another jurisdiction (“exported”);
   - lease, sell or exchange all or substantially all of its property other than in the ordinary course of business; or
   - carry out a going-private transaction or a squeeze-out transaction.

   The CBCA permits the dissenting shareholder to have his or her shares purchased by the corporation.

   There is no right of dissent with respect to the following situations.
   - Where an oppression remedy effects an amendment of the Articles (s. 241(5)).
   - If an amendment to the articles is effected under the reorganization provisions of the CBCA (s. 191(7)).

   Pursuant to subsection 190(26), the corporation may not purchase the shares from a dissenting shareholder if there are reasonable grounds for believing that:
   - The corporation is or would after the payment be unable to pay its liabilities as they become due; or
   - The realizable value of the corporation’s assets would thereby be less than the aggregate of its liabilities.

4. Procedure
   Once a special resolution for “fundamental change” has been passed, articles of amendment are sent to Corporations Canada, in duplicate, on the printed form, together with a cheque for the fee (or filed electronically), after which the Director is obliged to issue the certificate of amendment.

   If the amendments become complicated, the directors may restate the articles of incorporation,
file the restated articles with Corporations Canada, and the Director will issue a restated certificate of incorporation, which will supersede the original articles of incorporation and all amendments (s. 180). This is an easy method for keeping the articles of a CBCA corporation accurate and clear.

5. Amalgamation

The CBCA provides for amalgamations of CBCA corporations with other CBCA corporations (s. 181).

If a CBCA corporation is to be amalgamated with a body corporate subsisting under the laws of another jurisdiction there will have to be a "continuance" so that both corporations are governed by the laws of the same jurisdiction; then the amalgamation can proceed. This is not the case with an arrangement, however.

Under the CBCA, court approval is not required. The Director is obliged to satisfy himself or herself, on statutory declaration evidence, that creditors will not be prejudiced by the amalgamation (this procedure can be more onerous than if court approval were required—see the requirements of s. 185 of the CBCA). The Director then issues the certificate of amalgamation.

There is provision under the CBCA for a “short form amalgamation”, which saves a great deal of time when a subsidiary is amalgamating with its holding body corporate (“vertical short-form amalgamation”), or when two or more wholly-owned subsidiary corporations of the same holding body corporate are amalgamating (“horizontal short-form amalgamation”). In these instances, the amalgamation is approved by a resolution of the directors of each amalgamating corporation and certain other conditions must be met (ss. 184(1) and (2)). This short form of amalgamation saves a great deal of time and no artificial non-arm’s length amalgamation agreement is required and no shareholder approval is required (s. 184).

In situations other than a short-form amalgamation, the amalgamating CBCA corporations are required to enter into an agreement setting out the terms and means of effecting the amalgamation (s. 182). The directors must submit the amalgamation agreement for approval to a meeting of the holders of shares of the amalgamating corporation of which they are directors and, subject to certain exceptions, to the holders of each class or series of such shares (s. 183). It should also be noted that when an amalgamation takes place under the CBCA, it is not necessary that shares of the amalgamated corporation be issued to shareholders. Shares of a parent or other corporation can be issued instead, making for some interesting planning and acquisition possibilities.

A CBCA corporation may amalgamate with one or more bodies corporate under certain other federal statutes—the Bank Act, the Canada Cooperatives Act, the Cooperative Credit Associations Act, the Insurance Companies Act or the Trust and Loan Companies Act. In the case of an amalgamation with such bodies corporate, the application must be made to the Office of the Superintendent of Financial Institutions, and the CBCA will not apply to the amalgamated corporation.


6. Arrangements

A corporation may carry out a procedure referred to as an “arrangement”. While generally intended to provide a mechanism for a corporation in financial difficulties to reorganize its affairs with the consent of its shareholders and/or creditors, the arrangement procedure can be used to accomplish a number of corporate transactions that would not otherwise be possible.

The CBCA provides a list of the type of transactions included within the definition of an “arrangement” (s. 192). The definition contemplates transactions involving a corporation and its shareholders/creditors and transactions involving another corporate entity (which may not be a CBCA corporation). Section 192 of the CBCA requires a corporation wishing to carry out an arrangement not to be “insolvent”, and that there not be any other “practicable” way to carry out the transaction. In addition, the Director is required to be notified, and will often participate in the court hearings.

For more information on CBCA arrangements, see Policy Statement 15.1 – Policy Concerning Arrangements under Section 192 of the CBCA. The Policy Statement is available via the Internet: http://strategis.ic.gc.ca/epic/internet/incd-dgc.nsf/en/cs01073e.html.

7. Extraordinary Sale, Lease or Exchange

Pursuant to s. 189(3) of the CBCA, a sale, lease or exchange of all or substantially all of the property of a corporation other than in the ordinary course of business requires the approval of the shareholders by special resolution. In order to obtain shareholder approval, the notice of meeting must include a copy or summary of the agreement of sale, lease or exchange and state that a
dissenting shareholder is entitled to be paid the fair value of the holder’s shares by the corporation.

The meaning of “all or substantially all” has been examined in the case law and establishes a combined qualitative and quantitative analysis of the transaction in question. The underlying rationale behind the requirement in s. 189(3) is to protect shareholders from a fundamental change in the corporation that strikes at the heart of the corporate purpose and existence of the corporation.

[§19.13] Continuances (Export and Import)

Bodies corporate subsisting under the laws of other jurisdictions may be continued as corporations under the CBCA (imports). As well, CBCA corporations may be continued as bodies corporate under laws of another jurisdiction (export). See sections 187 and 188 of the CBCA. Two examples of where this procedure is commonly used are:

- if, for example, a company that is incorporated under the BCA moves its head office to Toronto and wishes to be governed by a statute with which its officers and lawyers resident in Toronto are more familiar, it may be continued as a CBCA corporation; or
- if an amalgamation is desired between a CBCA corporation and a body corporate incorporated in another jurisdiction, it may be necessary for the body corporate in the other jurisdiction to continue as a CBCA corporation or, alternatively, for the CBCA corporation to continue as a body corporate in the other jurisdiction.

1. Export

In order for a CBCA corporation to be exported, a special resolution of the shareholders is required. Also, the Director must be satisfied that the continuance will not adversely affect the creditors or shareholders of the corporation. Policy Statement 9.4 (“Steps to Follow for an Export Transaction”) provides that the Director considers the continuance of a CBCA corporation into all provinces and territories other than Prince Edward Island, Quebec, the Northwest Territories and Nunavut will not adversely affect the rights of creditors and shareholders. To export to a jurisdiction recognized under Policy Statement 9.4, the Director requires only a letter from the corporation stating that a special resolution of the shareholders authorizing the continuance has been passed, plus the applicable filing fee. To export into any other jurisdiction, the corporation must provide certain documentation to the Director to satisfy the Director that the continuance will not adversely affect the creditors or shareholders of the corporation (as listed in Policy Statement 9.4 – Steps to Follow for an Export Transaction, which may be accessed via the Internet: http://strategis.ic.gc.ca/epic/internet/incd-dgc.nsf/en/h_cs02141e.html).

In addition, no export will be allowed unless the property of the corporation will continue to be the property of the continued body corporate; the continued body corporate continues to be liable for the obligations of the corporation; an existing cause of action, claim, or liability to prosecution is unaffected; all civil, criminal, or administrative actions or proceedings pending by or against the corporation may be continued to be prosecuted by or against the continued body corporate; and any conviction, ruling, judgment, or order in favour of or against the corporation may be enforced by or against the body corporate. There is no requirement that the legislation of the jurisdiction into which the corporation proposes to continue permit bodies corporate under its laws to continue under the CBCA.

2. Import

In order for a body corporate to import itself under the CBCA, it must be authorized to do so under the laws of the jurisdiction that apply to it. In addition, it must comply with the requirements of such jurisdiction with respect to its export from that jurisdiction and file evidence of authorization from the exporting jurisdiction to the import under the CBCA with the Director, together with the same documents as are required for incorporation under the CBCA (except that the articles of incorporation are replaced by articles of continuance in the form that the Director fixes). All rights and obligations of the importing body corporate are preserved under the CBCA (s. 187(7)). For further information, see Policy Statement 9.1 – Continuance (Import) Kit. This Kit may be accessed via the Internet at: http://strategis.ic.gc.ca/epic/internet/incd-dgc.nsf/en/h_cs02141e.html.

[§19.14] Compulsory and Compelled Acquisitions

In B.C., the Securities Act (B.C.) governs takeover bids. A takeover bid under the Securities Act (B.C.) requires the acquisition of 20% or more of the issued shares of a company.

In addition, Part XVII of the CBCA deals with Compulsory and Compelled Acquisitions. These provisions are intended to make it possible that any bid for all the shares of a class, whether or not the shares are voting, can be followed up by a compulsory acquisition in certain circumstances. The CBCA
provides for compulsory acquisition of the shares of holdout shareholders where the offeror receives more than 90% acceptance of his or her bid within 120 days of the bid being made (s. 206). In terms of evaluation, the CBCA gives the holdout shareholder (the “dissenting offeree”) the alternate right to demand an independent valuation of his or her shares, in accordance with rules that parallel the valuation rules relating to a shareholder's appraisal right. See s. 206(9)-(18).

Under s. 206.1, a minority shareholder of a distributing corporation can, in certain circumstances, force the majority shareholder to purchase their shares. Compulsory acquisitions are only applicable to distributing corporations.

[§19.15] Summary Dissolution, Liquidation and Dissolution and Revival

1. Summary Dissolution

Section 210 of the CBCA permits a summary dissolution if all assets have been disposed of and liabilities have been paid, and provided that a special resolution of each class of shareholders has been passed and articles of dissolution (in the form fixed by the Director) are filed with the Director.

2. Long Form Dissolution

A longer dissolution procedure is available under s. 211 when the directors (or a shareholder who is entitled to vote at an annual meeting of the shareholders) propose the voluntary liquidation and dissolution of a corporation. This procedure usually includes the appointment of a liquidator. The corporation must pass a special resolution that the corporation be dissolved and file a Statement of Intent to Dissolve with the Director. For further information, see Policy Statement 10.1 – Steps to Follow to Dissolve a Corporation. This Kit may be accessed at: http://strategis.ic.gc.ca/epic/internet/incd-dgc.nsf/en/h_cs02141e.html.

3. Revival

Section 209 of the CBCA provides for the revival of a dissolved corporation in a manner similar to the restoration provisions of the BCA. An “interested person” may apply for revival of a dissolved corporation. The CBCA defines “interested person” in s. 209(6) as including, among other persons, a shareholder, director, officer, employee, creditor, person who has a contractual relationship with the corporation and a trustee in bankruptcy for the corporation. The most common reasons for applying for revival include attempts to reclaim property that had not been disposed of prior to the corporation’s dissolution, or to bring an action against the corporation.

[§19.16] Investigation and Remedies

1. Investigation

The provisions for investigation under Part XIX of the CBCA provide for essentially the same rights as those under the BCA. On an application from a security holder or the Director, a court having jurisdiction where the corporation has its registered office may order an investigation to be made of the corporation and any of its affiliated corporations on the grounds and subject to the provisions as stated in Part XIX.

2. Derivative Actions

Under the CBCA a complainant may apply to the court to commence or defend an action on behalf of a corporation or to intervene in any action to which any such body corporate is a party (s. 239).

3. Oppression Remedy

A complainant may apply to court under s. 241 of the CBCA for relief from conduct that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer. The remedy granted to a complainant under s. 241 is often referred to as the “oppression remedy”. The court may make any order it thinks fit, including a restraining order, an award of damages, appointment of a receiver or receiver-manager, the dissolution of the corporation, the forced acquisition of securities or the amendment of the corporation’s articles or by-laws or a unanimous shareholder agreement.


A CBCA corporation is obliged to file an annual return (s. 263). This return must be filed within 60 days after the anniversary date of incorporation of the corporation (Regulations, s. 5). Failure to file the annual return within one year of the due date can lead to dissolution of the corporation, although Corporation Canada’s current practice is to target corporations that have failed to file their returns for two consecutive years (s. 212). The corporation also will have to file an annual return in each provincial jurisdiction where it is registered as an extraprovincial corporation.

Section 254 provides that a notice or document required to be sent to or served on a corporation may be sent by registered mail to the registered office of the corporation shown in the last notice filed under s. 19.
Chapter 20

Not-for-profit Organizations

[§20.01] Introduction

Not-for-profit organizations and their volunteers play an important role in our society, many providing services and activities that otherwise would not be provided. These organizations take various forms, including social clubs, associations, trusts, private and public foundations, societies, cooperatives and corporations without share capital.

While many not-for-profit organizations are unincorporated, many of them are incorporated, provincially under the Society Act, R.S.B.C. 1996, c. 433 or federally under the Canada Not-for-profit Corporations Act, S.C. 2009, c. 23. Many not-for-profit organizations are also registered charities under the Income Tax Act (Canada) (see §20.14).

[§20.02] Advantage of Incorporation

The most common reason to incorporate a not-for-profit organization is to take advantage of limited liability. Many not-for-profit organizations put on activities in which individual members could incur liability: in some of these circumstances liability is certainly possible if unincorporated, while in these same circumstances, if incorporated, these same members may avoid liability.

[§20.03] Essential Difference Between an Incorporated Not-for-profit Organization and a Company

A company incorporated provincially or federally carries on a business or industry, divides its capital into shares, and has as its main objective to make profits. By contrast, an incorporated not-for-profit organization may operate for those purposes and objects stated in its governing statute and its constitution, without profit or gain to its members.

Neither a society nor a not-for-profit corporation has capital divided into shares.


[§20.04] New Canada Not-for-profit Corporations Act


The purpose of the Canada Not-for-profit Corporations Act is to provide a modern corporate governance framework for the regulation of federally incorporated not-for-profit organizations. The statute is modeled on the Canada Business Corporations Act and provides a much more attractive federal option than the previous legislation. Part II corporations are required to transition to the Canada Not-for-profit Corporations Act by October 17, 2014. This timeframe is not a hard deadline. Part II Corporations are merely required to commence the transition process prior to that date. In addition, Industry Canada will provide notice prior to dissolving a Part II Corporation for failure to transition.

[§20.05] Society Act (B.C.) or Canada Not-for-profit Corporations Act

Currently, there are far more B.C. societies incorporated under the Society Act than federally incorporated organizations operating in the province. Incorporation under either the Society Act or the Canada Not-for-profit Corporations Act has its advantages and disadvantages. Some advantages of each follow.

Society Act advantages

• it is the provincial statute that tends to be better known in B.C.;
• the government officials who oversee B.C. societies are located in B.C. and are therefore somewhat easier to communicate with than those in Ottawa;
• there is no requirement to file financial statements with the registrar of companies, whereas the Canada Not-for-profit Corporations Act requires that financial statements be filed with Corporations Canada;
• it does not impose different governance requirements on societies based on the amount of funding they receive from public sources;
• it does not require that non-voting members be allowed to vote as a separate class in respect of certain proposals and transactions (e.g. dissolution).
Canada Not-for-profit Corporations Act advantages

- It provides a not-for-profit corporation with the powers, rights, and privileges of a natural person without limiting those powers to the pursuit of its purposes;
- It does not restrict the types of purposes a not-for-profit corporation can be incorporated for (note that the CRA does impose restrictions on registered charities);
- It authorizes the members of a not-for-profit corporation to pass written resolutions in lieu of meetings, including annual general meetings;
- It authorizes a not-for-profit corporation to operate in any province of Canada as of right;
- It authorizes members of non-soliciting corporations to enter into unanimous member agreements through which they may agree to restrict the powers of the directors to manage and supervise the activities and affairs of the corporation;
- It authorizes not-for-profit corporations to hold meetings of their members by electronic means and provides for absentee voting;
- There is more flexibility in structuring by-laws, because there are fewer minimum requirements than under the Society Act;
- It is based on a more modern corporate governance model.

§20.06 Cooperative Associations

A cooperative is an organization owned by its members who use its products or services on a community-owned and cooperative basis. Cooperatives can provide a broad range of products or services, and can be either not-for-profit organizations or for-profit enterprises.

An example of not-for-profit cooperatives are housing cooperatives, which are by far the most common type of cooperatives in British Columbia. Housing cooperatives are subsidized by federal or provincial government housing agencies, or both.

A cooperative can be incorporated provincially under the Cooperative Association Act (B.C.) or federally under the Canada Cooperatives Act.

§20.07 Public and Private Foundations

A foundation is a registered charity whose primary purpose is to make grants to other charities and to those organizations recognized by the federal government as “qualified donees”. The difference between a private foundation and a public foundation is that a private foundation obtains more than 50% of its capital from one source and often has family or other non-arm's length directors. On the other hand, a public foundation obtains its capital from more than one source and has an arm's length board. A private foundation is not permitted to engage in any business activity.

A foundation must meet the requirements prescribed by the Income Tax Act, which include being constituted and operated exclusively for charitable purposes. In addition, a foundation may be structured as either a trust (formed pursuant to a trust document and managed by trustees) or corporation (incorporated under the Society Act or, the Canada Not-for-profit Corporations Act).

§20.08 Society Act (BC)

The remainder of this chapter is primarily focused on societies incorporated under the Society Act. Such societies are the predominant type of not-for-profit organizations operating in British Columbia. All section references in sections §20.08 to §20.13 are to the Society Act, R.S.B.C. 1996, c. 433, unless otherwise indicated.

The Society Act has remained largely unchanged since 1977. Amendments to the Act have received royal assent and will likely come into force in 2012. These amendments remove cross references to the Company Act’s dissolution and restoration provisions and incorporate those provisions directly into the Society Act.

The British Columbia Ministry of Finance commenced a large scale policy review of the Society Act in December 2009. The two fundamental issues which are being addressed concern the nature of the corporate vehicle which is most appropriate for societies and whether a more sophisticated business law framework should be adopted. Under the current legislation, societies are subject to a greater number of rules and regulatory constraints than corporations are pursuant to the Business Corporations Act, S.B.C. 2002 c. 57.

§20.09 Purposes and Characteristics

An organization may be incorporated as a society for certain purposes as set out in the Society Act. Under s. 2(1), the “purposes” of the society may include national, patriotic, religious, philanthropic, charitable, provident, scientific, fraternal, benevolent, artistic, educational, social, professional, agricultural, sporting, or any other useful purpose, but not for the purpose of carrying on any trade, industry, business or profession for profit or gain.

When insurance benefits may be provided, it is necessary to obtain the written consent of the Superintendent of Financial Institutions before incorporation (s. 2(1)(d)). A society cannot be incorporated for the care of children without the written consent of the director designated under the Child, Family and Community Service Act, R.S.B.C. 1996, c.46.
(s. 2(1)(a)). Nor can a society be incorporated as a hospital without the written consent of the minister responsible for the administration of the Hospital Act (s. 2(1)(b)). The registrar of companies is responsible for requesting the consents prescribed in section 2. Note that many Bands incorporate under the Societies Act to establish a separate legal entity to deliver family and child services, health services, fisheries, treaty negotiations, tribal affairs and education.

[§20.10] Registrar of Companies

The Registrar of Companies is the “registrar” under s. 1.

[§20.11] Incorporation Procedure

1. Name Approval and Reservation

The first step in incorporation is to ensure the proposed name of the society is available for approval by submitting a Name Request form under the same process as is required for companies under the Business Corporations Act, S.B.C. 2002, c. 57 (s. 3(6)).

2. Constitution and By-laws

Five or more persons may apply for incorporation of a society by filing a constitution and the by-laws of the proposed society according to Forms 1, 2 or 3 (s. 3(1)(a)(i)).

When setting out the purposes of the proposed society, note that there are various restrictions contained in the Society Act in addition to the ones referred to above (s. 2).

By-laws are analogous to the articles of a company. There is a statutory form of by-laws in Schedule B to the Society Act, similar to Table 1 of the Business Corporations Act (which the society may choose to adopt); see s. 3(1)(a), 6(2) and Schedule B.

The by-laws in Schedule B are often adequate, especially for relatively small societies, but they are rarely ideal and contain some significant limitations. Instead, it is usually best to ensure that the by-laws are tailored to the society from the start, especially considering that it can be difficult to amend a society’s by-laws. In any event, the by-laws must comply with the Society Act and, if applicable, will need to be approved by the Charities Directorate, Canada Revenue Agency at the time of application to register as a charity for income tax purposes.

Section 6(1) of the Society Act requires that by-laws set forth the following seven matters:

- terms of admission of members and their rights and obligations and when they cease to be in good standing;
- conditions under which membership ceases and the manner (if any) in which a member may be expelled;
- procedure for calling a general meeting;
- voting rights at general meetings, whether proxy voting is allowed, and if so, provisions for it;
- appointment and removal of directors and other officers and their duties, powers and remuneration (if any);
- exercise of borrowing powers; and
- preparation and custody of minutes of proceedings of meetings of the society and of the directors.

Corporate registry staff no longer examine by-laws at the time of incorporation or when by-laws are changed. Instead, the registry is the repository of the by-laws for public access. Consequently, a society must ensure its by-laws comply with section 6.

3. Additional Filings

On an application for incorporation, there must also be filed with the constitution and by-laws:

- a list of the persons appointed by the applicants to act as the first directors of the society, stating their full names and resident addresses (see s. 3(1)(a)(ii), Form 4). A society must have at least 3 directors (s. 24(4)), one of whom must be ordinarily resident in B.C. (s. 24(5));
- a notice setting forth the address of the society (see s. 3(1)(a)(iii), Form 5); and
- the prescribed fees (s. 3(1)(b)).

There is an appeal to court of any refusal of the registrar of companies to incorporate (s. 96).

Society Act forms may be obtained from www.bcregistryservices.gov.bc.ca.

[§20.12] Organizational Matters

1. Annual General Meetings

The first annual general meeting of the members of a society must be held not more than 15 months after the date of incorporation and, after that, an annual general meeting must be held at least once in every calendar year and not more than 15 months after the previous annual meeting (s. 56). A society
must give not less than 14 days’ written notice of a general meeting to those members entitled to receive such notice, unless such members waive or reduce the notice period by unanimous consent in writing (s. 60).

2. Annual Filings
Pursuant to s. 68, within 30 days after each annual general meeting, a society must file with the registrar an annual report in Form 11. In addition, a notice of change in directors of a society (other than at an annual general meeting) must be submitted without delay in Form 7 (s. 24(7)). Also, a society must file a notice of every change to its address in Form 5 (s. 10(1)(b)).

3. Financial Statements
Further to amendments made to the Society Act in 2004, a society is no longer required to submit financial statements to the corporate registry on an annual basis, although it must produce financial statements and submit them to the members at each annual general meeting (ss. 64 and 65). A society that is not a reporting society must also, on demand by a member or a debenture holder of the society, provide to the member or debenture holder a copy of its latest financial statements (s. 39(3)).

In addition, a society must provide any person a copy of a financial statement on request by the person to do so (s. 95(3)). Pursuant to a request under s. 95(3), the society may charge a person up to $10 for a copy of a financial statement, plus $0.50 per page for photocopying fees.

4. Reporting Societies
A society may be a “reporting society” as defined in ss. 1 and 38. Reporting societies must meet more stringent standards with respect to financial reporting. For example, a non-reporting society may have an auditor, but a reporting society must have an auditor (s. 41(1)). Reporting societies must furnish financial statements to the auditor and members at least ten days before the annual general meeting (s. 39(1)), while non-reporting societies need only furnish financial statements to its members at each annual general meeting or to other persons upon request pursuant to ss. 39(3) and 95(3).

5. Location of Records
All documents of a society including its financial records must be kept at its registered address, unless the directors, by resolution, permit some of the records to be kept at places other than at the registered address of the society (s. 11).

6. Register of Members
A society must keep a register of its members (s. 70(1)). A society that fails to keep a register of members in accordance with the Society Act commits an offence (s. 70(3)).

§20.13 Operational Matters

1. Directors and Officers
Directors and officers of a society are subject to a number of duties and liabilities under various statutes and the common law. In general, there is little distinction between the duties and liabilities of directors and officers of a society and the duties and liabilities of directors and officers of a company, notwithstanding that the individuals involved with a society may be volunteers. A society’s directors and officers are exposed to personal liability on a broad range of issues, including penalties if the society fails to remit withheld taxes or neglects to pay wages to its employees.

Many societies have figurehead or honorary directors, who bring a certain prestige to a society or are granted the position as an acknowledgement of faithful volunteer service to the organization. These directors often play a passive role and do not become involved in the management or the supervision of management of the society. However, such directors would not be relieved from liability by reason of their lack of involvement in the organization’s affairs and, in fact, could be exposed to increased liability for failing to fulfil their duties in an appropriate manner.

2. Borrowing
The provisions of the Business Corporations Act, (B.C.) relating to borrowing apply to societies (s. 35(1)). Also, a society must not issue a debenture unless authorized by special resolution (see s. 35(3)).

3. Corporate Status
Many small societies do not keep the records required by the Society Act and the Business Corporations Act (B.C.). In the event of litigation, borrowing or purchasing a major asset, it is prudent to review the corporate records in detail to determine whether the society is in a legal position to do what is proposed. The following are two types of deficiencies you may find:

- failure to file an annual report with the result of either not being in good standing with the registrar of companies or of being struck from the register;
• failure to have a proper register of members and directors.

If these corporate registries are not up to date, it becomes difficult to provide an opinion of whether members’ or directors’ resolutions have been passed properly.

4. Capacity

In the event of litigation, borrowing or a significant transaction, it is also imperative to ensure that the society has the capacity to do what is proposed. Subject to restrictions in the Society Act, a society has the powers and capacity of a natural person of full capacity only as may be required to pursue its purposes (s. 4(1)(d)). Furthermore, the constitution or by-laws of the society may contain limitations on what the society is able to do or, because the corporate registry is now only a repository for by-laws, the by-laws may not comply with the requirements of the Society Act, which may put into question whether the society has the legal capacity to do what is proposed.

[§20.14] Applying for Charitable Status

Many societies and other not-for-profit organizations want to become registered charitable organizations under the Income Tax Act (Canada). There are a few basic advantages to being a registered charity:

• registration allows an organization to issue official charitable donation tax receipts for gifts received;
• once the organization is registered, it is exempt from paying income tax (under Part I of the Income Tax Act (Canada));
• a registered charity may receive grants from charitable foundations;
• charitable status may be beneficial to the organization in terms of public perception.

There are some limitations imposed on registered charities:

• the reporting requirements for registered charities are quite onerous and the organization must keep detailed records, file annual returns and meet disbursement quotas;
• the activities of the organization must be and continue to be exclusively charitable;
• there are significant limitations on what political activities the organization may be involved in;
• there are restrictions on when and where the organization may disburse donations it receives.

The registration process for a charity that submits a properly completed application may take between three to four months. The application is more likely to succeed if the constitution and by-laws have been appropriately drafted with a view to the organization becoming a registered charity (for example, the constitution should set out purposes that are exclusively charitable).

[§20.15] Lawyer as Director

1. General Comments

Being asked to serve as a director for a not-for-profit organization is an honour and may be an excellent opportunity to contribute to the community. It is also a significant responsibility and a lawyer should only accept a directorship after careful consideration of the nature of the commitment and a due diligence review of the organization itself.

2. Insurance

The B.C. Lawyers’ Compulsory Professional Liability Insurance Policy does not cover lawyers for errors and omissions arising out of a lawyer’s activities as a director or officer. A lawyer who acts as a director or officer of a not-for-profit organization should ensure that its by-laws require the organization to indemnify directors and officers. He or she should also ensure that the organization has and maintains appropriate Directors and Officers Liability Insurance, and that it has the authority and capacity to do so. Alternatively, the lawyer may arrange for his or her own insurance coverage.

3. Duties

In matters in which a lawyer is deemed to have a higher degree of skill than a lay person, the lawyer has a greater burden and responsibility. He or she must therefore take a greater interest in the affairs of the organization and make more inquiries as to its operation.

4. Other Considerations

Many not-for-profit organizations ask a lawyer to become a director as a way of obtaining free legal advice. This approach may not make much sense if the lawyer primarily practices in an area of law that is unrelated to the activities of the organization. In any event, the lawyer should attempt to clarify the expectations of what his or her role will be.

The lawyer who acts as a director of a not-for-profit organization at the same time as providing legal advice to the organization must also consider the potential for conflicts in acting as a director and in providing legal advice to management. On the question of conflicts of interest, refer to Chapters V, VI and VII of the Code of Professional Conduct, as well as Section 3.4 of the BC Code.
1. **Definition**

In general terms, pro bono legal services are legal services for persons of limited means or for not-for-profit organizations, without expectation of a fee. Lawyers have a general professional responsibility to contribute to their community by providing pro bono legal assistance. In particular, the legal profession has an obligation and responsibility to facilitate the due administration of justice by providing legal assistance when legal aid is not available. Of course, there is also a significant personal reward simply from being involved in such activities.

2. **Insurance**

The B.C. Lawyers’ Compulsory Professional Liability Insurance Policy provides insurance coverage to lawyers who purchase the policy (generally lawyers in private practice) for their pro bono legal services, including such services provided to not-for-profit organizations.

In addition, coverage is extended to lawyers in good standing who do not purchase the policy (such as insurance-exempt, non-practising and retired lawyers), for claims arising out of their performance of certain pro bono services defined in the policy as “sanctioned services”. Services are sanctioned services if:

- they are provided by a lawyer to an individual solely through a pro bono legal services program;
- they are not for the benefit of a person previously known to the lawyer, including a family member, friend or acquaintance; and
- both the service and the program are approved by the Law Society.

If a claim arises out of a lawyer’s provision of sanctioned services, the usual financial consequences of a paid claim are waived (e.g. deductibles and surcharges). This is the case regardless of whether the lawyer has purchased the policy. For more information on pro bono approved programs and services, please refer to the “Approved Programs” section of the website of the Access Pro Bono Society of British Columbia at: [http://probononet.bc.ca/approvedprograms.php](http://probononet.bc.ca/approvedprograms.php).

The wording of the Policy governs any claim or potential claim which may arise. Lawyers should consult with the Lawyers Insurance Fund on specific questions regarding coverage for pro bono legal services.

3. **Other**

For more information on insurance coverage for pro bono legal services, please refer to the “Information Sheet: Pro Bono Services and other resources” available on the Law Society’s website at [http://www.lawsociety.bc.ca/page.cfm?cid=209&t=Coverage-for-pro-bono-legal-services](http://www.lawsociety.bc.ca/page.cfm?cid=209&t=Coverage-for-pro-bono-legal-services).