

# Piercing the Corporate Veil: When Directors, Officers and Shareholders of a Corporation will be Personally Liable

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Most business people understand that a company is a separate legal “person” from its members and, by its creation, limits the personal liability of any individual officer, director or shareholder for its behavior.

This legal principle has been around since the 1800s, established in the now famous English House of Lords case, *Salomon v Salomon*. It is not always applied by the courts, however, and there are certain circumstances where the courts will “look behind” or “lift the corporate veil” to find individuals responsible for bad company acts.

A recent decision by the Ontario Court of Appeal, *Shoppers Drug Mart Inc. v. 6470360 Canada Inc.*, illustrates how these circumstances are continually evolving and, more importantly, confirms the legal test the court will apply in determining whether the corporate veil should be pierced.

In *Shoppers*, under a contract between Shoppers Drug Mart Inc. and 6470360 Canada Inc., carrying on business as Energyshop Consulting Inc./Powerhouse Energy Management Inc. (647), Shoppers directed utility companies to send their bills for Shoppers to 647. 647 then collected and organized the bills and periodically sent a remittance summary to Shoppers, setting out the total amount of that period’s utility bills payable by Shoppers.

On receiving a remittance summary, Shoppers would transfer the invoiced amount to a bank account that was in the joint names of 647 and 647’s sole officer, director and shareholder, Michael Wayne Beamish. This “clearing” account was used to receive all funds from Shoppers,

and in turn, to pay Shoppers' utility bills. Beamish signed off and approved every transfer from the clearing account. 647 either used the funds received from Shoppers to pay Shoppers' utility bills or transferred them to a separate bank account that was used to pay 647's operating expenses. The "operating" account was also in the joint names of both 647 and Beamish.

Soon after Shoppers received an anonymous telephone call and fax indicating that funds it paid into the clearing account were being used for activities other than the payment of utility bills, it concluded that something was amiss with its relationship with 647 and then delivered a notice to 647, terminating its services.

Following receipt of the termination letter, instead of paying Shoppers outstanding utility bills, Beamish caused 647 to transfer large sums of money from the clearing account to the operating account. After this, Shoppers began to receive notices of default from various utility providers in respect of outstanding invoices that, in its view, 647 ought to have paid.

Shoppers commenced an action against both 647 and Beamish to recover its funds and brought a motion for summary judgment against them seeking payment of the funds that had been misappropriated. Beamish responded with two motions to dismiss the action against him personally.

The motions judge found for Shoppers against 647, but dismissed Shoppers' claim against Beamish personally, relying solely on English case law for this determination. Shoppers appealed.

On appeal, Madam Justice Sarah E. Pepall stated that the motions judge had erred in reaching the conclusion that Beamish had not been unjustly enriched by the misappropriation and that the "corporate veil" -- the protection against personal liability that incorporation can provide -- should not be pierced. She set aside the order dismissing the action against Beamish and substituted an order granting Shoppers judgment against Beamish *personally*.

In doing so, the Court confirmed that the leading Court of Appeal case on the question of when the corporate veil may be pierced in Ontario and when an individual may be exposed personally is *642947 Ontario Ltd. v. Fleischer* and is therefore the appropriate test to apply.

Quoting from *Fleischer*, the Court stated that "only exceptional cases that result in flagrant injustice warrant going behind the corporate veil" and continued:

"Typically, the corporate veil is pierced when the company is incorporated for an illegal, fraudulent or improper purpose. But it can also be pierced if when incorporated "those in control expressly direct a wrongful thing to be done"... "the courts will disregard the separate legal personality of a corporate entity where it is completely dominated and controlled and being used as a shield for fraudulent or improper conduct."

Applying the correct legal test from *Fleischer*, the Court said there was no doubt that Beamish was the directing mind and caused a misappropriation and misrepresentation by 647 and the

ensuing unjust enrichment. He had sole signing authority over the accounts and authorized the transfer of significant amounts of money, which were supposed to be dedicated to the payment of utility bills, to an operating account in the names of himself and a company of which he was the sole shareholder. He expressly directed and caused the wrongful act. In these circumstances, therefore, there was an unjust enrichment and it was appropriate to pierce the corporate veil.

Not only is *Shoppers* a case of “what-not-to-do” as a sole officer, director and shareholder of a company, but it also serves as a pointed reminder that incorporation does not always afford protection from personal liability.