Date: 19990329

CORAM:DESJARDINS J.A.
LÉTOURNEAU J.A.
NOËL J.A.

A-752-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

GARY J. CORSANO

Respondent

A-753-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

JON LAWRENCE

Respondent

A-754-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

JOHN HARVEY MACDONALD

Respondent

A-755-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

ERNEST PARSONS

Respondent

A-756-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

SANJIV MAINDIRATTA

Respondent

цЯҐЃл И

A-757-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

GEORGE WHEELIKER

Respondent

Heard at Halifax, Nova Scotia, Friday, March 12, 1999

Judgment delivered at Ottawa, Ontario, Monday, March 29, 1999

цЯГЃл и

REASONS FOR JUDGMENT BY: **NOËL J.A.**
CONCURRED IN BY: **DESJARDINS J.A.**
CONCURRING REASONS IN THE RESULT BY: **LÉTOURNEAU J.A.**

Date: 19990329

CORAM: DESJARDINS J.A.
LÉTOURNEAU J.A.
NOËL J.A.

A-752-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

GARY J. CORSANO

Respondent

A-753-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

JON LAWRENCE

Respondent

A-754-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

JOHN HARVEY MACDONALD

Respondent

A-755-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

ERNEST PARSONS

Respondent

A-756-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

SANJIV MAINDIRATTA

Respondent

A-757-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

GEORGE WHEELIKER

Respondent

REASONS FOR JUDGMENT

NOËL J.A.

[1] These are appeals from the October 3, 1997 decision[1] of O'Connor T.C.C.J. of the Tax Court of Canada, wherein he allowed an appeal by the respondents from an assessment pursuant to subsection 227.1(1) of the *Income Tax Act* (the "*ITA"*) for unremitted federal income tax withheld from the wages paid to the employees of Louisbourg Harbourfront Park Ltd. (the "Corporation").

[2] The appeals were heard together and these Reasons for Judgment are applicable to all. One set of Reasons will be issued and will be filed in each of these cases.

---

[1] Now reported at 98 D.T.C. 1110 [hereinafter *Wheeliker*].

[3] The Corporation was incorporated in 1980 under the *Companies Act*, R.S.N.S. 1967 c.42, as amended (the "Act"). It was a non-profit corporation whose mandate was the enhancement and development of economic activity in the Town of Louisbourg. At all relevant times to this appeal, the Louisbourg Harbourfront Society (the "Society") owned 96% of the shares of the Corporation, with the remaining 4% being held by prior directors of the Corporation in trust for the Society.

[4] The Articles of Association of the Corporation ("Articles") limited the number of directors to a maximum of seven and required that each director hold at least one share of the Corporation. None of the respondents owned a share of the Corporation as required by the Articles but all acted as directors. Further, by March 1993, there were nine directors. No remuneration was paid to the respondents in respect of their services.

[5] During the period January 1992 to October 1993, the Corporation failed to remit to the Receiver General of Canada federal income tax withheld from the wages paid to the Corporation's employees in the amount of $17,886.91.[2] Pursuant to subsection 227.1(1) of the *ITA* the respondents Corsano, Wheeliker and Maindiratta were assessed by the Minister of National Revenue (the

---

[2] Appeal Book, vol. 3 at 390-391 and 409.

"Minister") for source deductions not remitted for the period from January 1992 to October 1993. The respondents Lawrence, MacDonald and Parsons were assessed for the period from November 1992 to October 1993.[3] Section 227.1 of the *ITA* reads:

(1) Where a corporation has failed to deduct or withhold an amount as required by subsection 135(3) or section 153 or 215, has failed to remit such an amount or has failed to pay an amount of tax for a taxation year as required under Part VII or VIII, the directors of the corporation at the time the corporation was required to deduct, withhold, remit or pay the amount are jointly and severally liable, together with the corporation, to pay that amount and any interest or penalties relating thereto.

...

(3) A director is not liable for a failure under subsection (1) where he exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances. [emphasis added]

(1) Lorsqu'une corporation a omis de déduire ou de retenir une somme, tel que prévu au paragraphe 135(3) ou à l'article 153 ou 215, ou a omis de remettre cette somme ou a omis de payer un montant d'impôt en vertu de la Patrie VII ou de la Partie VIII pour une année d'imposition, les administrateurs de la corporation, à la date à laquelle la corporation était tenue de déduire, de retenir, de verser ou de payer la somme, sont solidairement responsables, avec la corporation, du paiement de cette somme, incluant tous les intérêts et toutes les pénalités s'y rapportant.

[...]

(3) Un administrateur n'est pas responsable de l'omission visée au paragraphe (1) lorsqu'il a agi avec le degré de soin, de diligence et d'habilité pour prévenir le manquement qu'une personne raisonnablement prudente aurait exercé dans des circonstances comparables. [mon souligné]

[6] O'Connor T.C.C.J., relying on the decision of this Court in *Her Majesty The Queen* v. *Kalef*,[4] held that the definition of "director" for the purposes of subsection 227.1(1) means a *de jure* director as defined by the incorporating legislation of the corporation. While stating that "there [was]

[3] Memorandum of Fact and Law of the Appellant at 1, Memorandum of Fact and Law of Wheeliker at 1, Memorandum of Fact and Law of Lawrence, MacDonald and Parsons at 1, Memorandum of Fact and Law of Maindiratta at 5, Memorandum of Fact and Law of Corsano at 4.

[4] 96 D.T.C. 6132, [1996] 2 C.T.C. 1 [hereinafter *Kalef*].

little doubt the [respondents] acted as directors by attending directors' meetings and managing the Corporation,"[5] O'Connor T.C.C.J. held both that the respondents were not *de jure* directors as defined by the Act and that *de facto* directors were not directors under the Act. As a result, the respondents were not subject to the vicarious liability imposed by subsection 227.1(1) of the *ITA*.

[7] The *ITA* does not define "director" either for the purposes of the *ITA* as a whole or for the purposes of section 227.1. As this Court held in *Kalef*, it is therefore appropriate to look to the Corporation's incorporating legislation for guidance as to who is a "director" for the purposes of section 227.1. Under paragraph 2(1)(f) of the Act,

> "director" includes any person occupying the position of director by whatever name called; [emphasis added]

I agree with the conclusion of the Tax Court judge that the words "occupying the position of director by whatever name called" brings within the definition a director irrespective of how this position may be designated. This is consistent with the approach of the Chancery Division in *In re Lo-Line Electric Motors Ltd.*[6] where the Court interpreted the identical definition under the U.K. *Companies Act*, 1985. According to the Court:[7]

> ... the words "by whatever named called" show that the subsection is dealing with nomenclature; for example where the company's articles provide that the conduct of the company is committed to "governors" or "managers."

---

5 *Wheeliker*, *supra* note 1 at 1114.

6 [1988] 2 All E.R. 692 (Ch.).

7 *Ibid*. at 699.

[8] As section 2(1)(f) speaks simply to nomenclature and is inclusive, it is therefore necessary look to the provisions of the Act to determine the legislative intent with respect to those who have under the law the status of "director."

[9] Before turning to the relevant provisions, I note that the Act nowhere speaks of *de facto* or *de jure* directors. Rather it uses the term director in various contexts, some of which suggest a reference to a director who is qualified to act as such under the Act, and others which refer to a person who in fact acts as such without being so qualified. The question to be answered is whether the word director only connotes a person qualified to act as such under the Act.

[10] A useful starting point is a consideration of the qualifications imposed by the Act. Section 95 is the most important provision in this respect. It provides in part that:

(1) It shall be the duty of every director who is by the regulations of the company required to hold a specified share qualification, and who is not already qualified, to obtain his qualification within three months after his appointment, or such shorter time as is fixed by the regulations of the company.

...

(3) The office of director of a company shall be vacated, if the director does not within three months from the

date of his appointment, or within such shorter time as if fixed by the regulations of the company, obtain his qualification, or if after the expiration of such period or shorter time he ceases at any time to hold his qualification, and a person vacating office under this Section shall be incapable of being re-appointed director of the company until he has obtained his qualification.

(4) If, after the expiration of the said period or shorter time, any unqualified person acts as a director of the company, he shall be liable to a penalty not exceeding twenty-five dollars for every day between the expiration of the said period or shorter time and the last day on which it is proved that he acted as a director. [emphasis added]

[11] The Articles of Association provide in turn:

106. The qualification of a Director shall be the holding of at least one share in the Company of a class entitled to vote at general meetings of the Company. A director may be appointed and act before acquiring a qualifying share, but, if he has not acquired it within three months of his appointment or election, he shall be deemed to have vacated the office of Director.

...

111. The office of a Director shall ipso facto be vacated:

(a) if he becomes bankrupt, makes an authorized assignment, suspends payment, or compounds with this creditors; or

(b) if he is found a lunatic or becomes of unsound mind; or

(c) if he ceases to hold the number of shares required to qualify him for office or does not acquire them within three months after his election or appointment; or

(d) if by notice in writing to the Company he resigns his office; or

(e) if he is removed by special resolution as provided by Article 116. [emphasis added]

[12] Subsection 95(1) of the Act imposes upon a director the obligation to own the number of shares prescribed by the regulations of the company and provides for a grace period of three months to obtain this qualification. Should a director not obtain the prescribed share qualification within the specified time, or should he or she lose this qualification, subsection 95(3) stipulates that "the office of director ... shall be vacated" and the person concerned "shall be incapable" of holding the office until he or she has obtained the qualification. The Articles reinforce the effect of the disqualification by providing that the person concerned "shall be deemed to have vacated the office of Director"[8] and "the office of Director shall *ipso facto* be vacated."[9]

[13] However, subsection 95(4) acknowledges that persons may act as directors without being qualified, and creates a liability for a penalty for every day during which the breach persists.

---

8 Article 106.

9 Article 111.

[14] The Act also seeks to protect those who in good faith contract with persons who purport to act as directors while not qualified to do so. Section 30 is a codification of the common law "indoor management rule." It provides:

> A company or a guarantor of an obligation of the company may not assert against a person dealing with the company or with any person who has acquired rights from the company that ...
>
> (b) the persons named in the most recent notice sent to the Registrar under subsection (1) of Section 98 are not the directors and officers of the company; ...

Thus, a company is estopped from asserting that a person who is held out as a director was not qualified to act as such. The result is that in such circumstances, the company will be bound as it would be if the person had been qualified.

[15] Similarly, section 97 validates the acts of a director despite the fact that it is later found that he or she lacked qualification at the relevant time:

> The acts of a director or manager shall be valid notwithstanding any defect that is afterwards discovered in his appointment or qualification. [emphasis added]

Similar provisions are common in Canadian corporate legislation and exist so as to protect third parties and ensure a degree of certainty with respect to the effect of corporate transactions.[10] However,

---

[10] See Iacobucci *et al, Canadian Business Corporation: An Analysis of Recent Legislative Developments* (Agincourt: Canada Law Book, 1977) at 269-270.

section 97 does not have the effect of validating the appointment of unqualified directors; rather it validates the "acts" of an improperly appointed director.[11]

[16] It is therefore apparent that the Act recognizes that persons will act as directors without being qualified to do so, and that the legislator has, despite this absence of qualification, chosen to validate those acts in the circumstances that we have seen. The question then becomes whether this statutory recognition of specified acts by persons who act as directors despite their lack of qualification also has the effect of making them directors under the Act.

[17] In my view, section 95 of the Act and the relevant sections of the Articles would be rendered meaningless if the Act was construed as granting the status of director to those who are not qualified. A director is one who meets the requirements imposed under the Act including those prescribed by section 95. Indeed, a penalty is imposed on those who act as director without meeting those requirements. It would be odd if those who breach the Act by acting as directors while not qualified thereunder would nevertheless have the status of director under the Act. As a matter of legislative intent, it seems unavoidable that only those who meet the requirements prescribed by the Act, are directors under the Act.

---

[11] See for example *Oliver* v. *Elliott* (1960), 30 W.W.R. 641 (Alta. S.C.).

[18] In my view, the Act cannot be construed as giving those acting as directors without the requisite qualifications the status of director, nor can it be said that the common law has provided such individuals this status. What the courts have done over the years, however, is devise remedies to assist third parties who deal with persons who act as directors or who are held out by the company as directors although they lack the required qualification or authority.

[19] As I understand it, one principle underlying these common law remedies is that a person who has not obtained the requisite qualifications, is prevented from pleading this failure in order to escape liability attaching to a director. As held by Richards J.A. in *MacDonald* v. *Drake*,

> I cannot assent to the contention that a director, who, with his consent, has been elected and has acted as a director, should, merely because he was not qualified to hold the office, escape liability that he would have incurred if he had been qualified. The true principle seems to be that a man cannot take advantage of his own wrong.[12]

It being recognized in this instance that the respondents acted as directors, in conformity with the will of the shareholders, I see no reason why they should be allowed to assert their lack of qualification to escape the liability cast upon directors by virtue of section 227.1 of the *ITA*.

[20] Thus, while I would agree with the conclusion of the Tax Court judge that those acting as directors without having the requisite qualifications are not directors under the Act, I do not believe that

---

[12] *MacDonald* v. *Drake* (1906), 16 Man. R. 220 (C.A.) at 223.

the respondents can raise this lack of qualification as a defence to their liability under subsection 227.1(1) of the *ITA*.

[21] On the issues of the applicable standard of care and its application to the facts of this case, I agree with the reasons of my colleague, Létourneau J.A. and would dispose of these appeals as he suggests.

"Marc Noël"
J.A.

"I concur.
Alice Desjardins J.A."

[22]

Date: 199903

CORAM:DESJARDINS J.A.
LÉTOURNEAU J.A.
NOËL J.A.

A-752-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

GARY J. CORSANO

Respondent

A-753-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

JON LAWRENCE

Respondent

цЯҐЃл зЗ

A-754-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

JOHN HARVEY MACDONALD

Respondent

A-755-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

ERNEST PARSONS

Respondent

A-756-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

SANJIV MAINDIRATTA

Respondent

A-757-97

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

GEORGE WHEELIKER

Respondent

REASONS FOR JUDGMENT

LÉTOURNEAU J.A.

[1] I have had the benefit of reading the reasons prepared by my colleague Noël J.A. and share his views as to the liability of the respondents. However, I have come to such conclusion from a different approach which needs to be stated. It involves legal considerations with respect to the interpretation of subsections 227.1(1) and (3) of the *Income Tax Act* (Act) and the application of the defense of due care and diligence.

The meaning and scope of the term "director" in subsection 227.1(1) of the *Income Tax Act*

[2] Subsection 227.1(1) of the Act holds jointly and severally liable the directors of a corporation who have failed to withhold, deduct and pay to Revenue Canada the taxes due on salary or wages when so required. Sections 153 and 227.1 which are intertwined read:

> **153(1)** Every person paying at any time in a taxation year
>
> (*a*) salary or wages or other remuneration,
>
> ...

shall deduct or withhold therefrom such amount as may be determined in accordance with prescribed rules and shall, at such time as may be prescribed, remit that amount to the Receiver General on account of the payee's tax for the year under this Part or Part XI.3, as the case may be, ...

153(1) Toute personne qui verse à une date quelconque d'une année d'imposition

a) un traitement, un salaire ou autre rémunération,

...

doit en déduire ou en retenir la somme qui peut être prescrite et doit, au moment fixé par règlement, remettre cette somme au receveur général au titre de l'impôt du bénéficiaire ou du dépositaire pour l'année en vertu de la présente partie ou de la partie XI.3.

227.1(1) Liability of directors for failure to deduct - Where a corporation has failed to deduct or withhold an amount as required by subsection 135(3) or section 153 or 215, has failed to remit such an amount or has failed to pay an amount of tax for a taxation year as required under Part VII or VIII, the directors of the corporation at the time the corporation was required to deduct, withhold, remit or pay the amount are jointly and severally liable, together with the corporation, to pay that amount and any interest or penalties relating thereto.

227.1(1) Responsabilité des administrateurs pour défaut d'effectuer les retenues - Lorsqu'une société a omis de déduire ou de retenir une somme, tel que prévu au paragraphe 135(3) ou à l'article 153 ou 215, ou a omis de remettre cette somme ou a omis de payer un montant d'impôt en vertu de la partie VII ou VIII pour une année d'imposition, les administrateurs de la société, au moment où celle-ci était tenue de déduire, de retenir, de verser ou de payer la somme, sont solidairement responsables, avec la société, du paiement de cette somme, y compris les intérêts et les pénalités s'y rapportant.

[3] The learned Tax Court judge adopted the respondents' contention that the notion of director found in the Nova Scotia *Companies Act* refers to the concept of *de jure* director only and does not incorporate that of the *de facto* administrator recognized by the common law in Nova Scotia. On appeal, both the appellant and the respondents from their respective perspective have argued strenuously against and in support of this legal finding by the Tax Court judge. With respect, I think the respondents' contention is a red herring which has contributed to mask the real issue in the present instance and the proper approach to be taken to the determination of the respondents' liability towards Revenue Canada for the remittances due. As is often the case with a red herring, it gives rise to most

stimulating but generally irrelevant discussions.

[4] As a matter of fact, the governing provision which is in dispute here is subsection 227.1(1) of the Act. It is the scope of this provision which falls to be determined, not the scope of the Nova Scotia *Companies Act*. Much of the focus has been put, unnecessarily in my view, on the ambiguous and free use of the word "director" in the Nova Scotia *Companies Act* and on the proper scope and interpretation of that *Companies Act*. This is, as we shall see, the result of the respondents misconstruing an earlier decision of this Court and the purpose of subsection 227.1(1) of the Act.

[5] Subsection 227.1(1) of the Act imposes liability on all the directors of a corporation who have failed to remit to Revenue Canada the sums due. The word "directors" in the said subsection is unrestricted and unqualified. It is a basic rule of legislative drafting, based on the corresponding rule of interpretation which conditions drafting, that the use of a generic word without restrictions or qualifications conveys the legislator's intention that the word be given a broad meaning. Here, by using the word "directors" without qualifications in subsection 227.1(1), Parliament intended the word to cover all types of directors known to the law in company law, including, amongst others, *de jure* and *de facto* directors.

[6] It bears repeating that there is no disagreement between the parties, and the Tax Court judge so found, that the Nova Scotia common law has developed the concept of *de facto* director. I hasten to add that, in this regard, the legal situation is practically the same in all common law jurisdictions across Canada.

[7] Yet, notwithstanding that, the Tax Court judge concluded that the word "directors" in subsection 227.1(1) of the Act refers only to *de jure* directors. In coming to such conclusion he relied first upon the decision of this Court in *Her Majesty the Queen v. Kalef*[13] to which he gave an erroneous

[13] [1996] 2 C.T.C. 1 (F.C.A.).

interpretation. This is apparent from the following excerpts at pages 8 and 9 of his decision:

> Since the jurisprudence is clear that, for the purposes of subsection 227.1(1) of the Act, to discover the meaning of "director" one must look to the incorporating legislation of the Corporation, one should do so and avoid general principles of common law. Therefore, although they may have been *de facto* directors at common law, they were not under the *Companies Act* and should not be held vicariously liable under section 227.1 of the Act ...
>
> ...
>
> It seems clear that in analyzing the definition of "director" in the *Ontario Business Corporations Act*, which definition is practically identical to paragraph 2(1)(*b*) of the *Companies Act*, the Federal Court of Appeal found that the definition referred to a *de jure* director.

[8] Let me say outright that our Court never decided in the *Kalef* case that the definition in the

Ontario Business Corporations Act referred to a *de jure* director. The Court was called upon to determine if the director of a corporation ceases to be a director for the purpose of subsection 227.1(4) of the Act when a Trustee in Bankruptcy is appointed. It concluded that Mr. Kalef did not fulfil any of the requirements under the *Ontario Business Corporations Act* which would have indicated that he had ceased to be a director. Therefore, he had remained a director notwithstanding the appointment of a Trustee.

[9] In addition, our Court never decided that, in interpreting the word "director" in subsection 227.1(1) of the Act, one can only look at the company's incorporating legislation and not at the

common law. Here is what our colleague McDonald J.A. wrote:

> The *Income Tax Act* neither defines the term director, nor establishes any criteria for when a person ceases to hold such a position. Given the silence of the *Income Tax Act*, it only makes sense to look to the company's incorporating legislation for guidance.
>
> (my underlining)

[10] There was no need in that case to look at the common law because the statutory law determined when a person ceased to be a director.

[11] In addition, as our Court indicated, the statutory law is to be looked at "for guidance". It is

certainly not exclusive and determinative, especially in the circumstances of the present appeal where the issue is not to determine for the purpose of section 227.1 of the Act whether a person had ceased to be a director (an issue generally governed by statutory provisions), but rather whether a person ostensibly acted as a director and therefore was a *de facto* or acting director (an issue generally governed by common law principles). To use the terms of McDonald J.A., "it only makes sense for guidance" to look at the body of law which can provide the answer to the silence of the Act. In the present instance, such body is the common law.

[12] I should reiterate here that what is in issue through subsection 227.1(1) of the Act is the liability

of the directors of a company, as directing minds of that company, for their own failure to prevent the prohibited act, not whether they engage the responsibility of the company, as I think they do. As early as 1906, the Manitoba Court of Appeal in *MacDonald v. Drake*[14] rejected the defendants' contention that a statutory provision making directors jointly and severally liable for unpaid wages could only be enforced against *de jure* directors. The Court found that although the defendants were not *de jure* directors because they did not hold the required shares in their own right, they were ostensibly elected, attended and took part in the meetings as well as acted as directors. They were *de facto* directors and, therefore, personally liable. Phippen J.A., at pages 229 and 230 wrote:

[14](1906) 16 *Man. Reports* 220.

> The law is clear that the actions of directors "*de facto*" within the powers of the Company are binding upon both the Company and the directors...
>
> I do not think these defendants can now be permitted to set up a defect in their own title to the office, of which they have enjoyed the benefit, to escape a debt, which I do not consider a penalty, to employees in whose favour the statute grants relief.

[13] In *Northern Trust Co. v. Butchart*[15], the Chief Justice of the Manitoba King's Bench Court stated in relation to an allegation of misfeasance and breach of trust against the directors whom he found

[15](1917) 35 D.L.R. 1, at p. 7 (Man. K.B.); see also *Re Canadian Casket Co. Ltd.* 14 C.B.R. 148 (Ont. S.C.).

jointly and severally liable for these acts:

> Whether they were legally elected or not makes no difference. They were *de facto* directors, and for all acts of omission or commission on their part, they are liable in the same manner and to the same extent as if they had been *de jure* as well as *de facto* directors.

[14] In *The Law of Canadian Companies*[16], F.W. Wegenast writes:

---

[16] Toronto, The Carswell Company Limited, 1979, at p. 411; see also *Gower's Principles of Modern Company Law*, London, Sweet and Maxwell, 1992, at p. 143:

> While, *de jure*, people cannot be directors unless they have been properly appointed, they may... be able to bind the company although they have not. Moreover, they may be subject to liability as if they were directors because they have assumed that position.
>
> (my underlining)

> The objection to the *de facto* directors cannot, of course, be invoked by an unauthorized director himself as for example to escape liability... or to escape a statutory liability for wages of workmen or for failure to make government **returns**...; for a *de facto* director is in the same position as an executor *de son tort*.

(my emphasis)

[15] The Tax Court judge also concluded that the term "director" in subsection 227.1(1) of the Act is to be given a narrow meaning because that subsection imposes vicarious liability. He wrote at page 9 of his decision:

> Subsection 227.1(1), in imposing a vicarious liability, refers only to a "director". Subsection 159(3) also imposes vicarious liability on certain transferors of property. It is notable that in subsection 159(2) the *Act* casts a very wide net over who is liable. It refers to "assignee, liquidator, receiver, receiver-

> manager, administrator, executor or any other like person". Surely if the Minister wanted the net cast by subsection 227.1(1) to be wide, words in addition to "director" could have been used, such as "whether *de facto* or *de jure* or "including persons acting as directors" or "manager", "officer" or "any other like person". In my opinion, a provision imposing vicarious liability should be strictly construed and consequently I have done so.

[16] I have already pointed out that if Parliament intended in subsection 227.1(1) to cover all kinds of directors, it needed only to do as it did, that is to say use the word "director" without restriction. Looking at the terms "assignee, liquidator, receiver, receiver-manager, administrator or executor" to which the Tax Court judge refers in the passage quoted, it begs the question whether Parliament should have also said in order to cast a very wide net: "assignee whether *de facto* or *de jure*, liquidator

whether *de facto* or *de jure*..., administrator whether *de facto* or *de jure*, executor whether *de facto* or *de jure*? To put the question is to answer it. In drafting subsection 227.1(1) with a view to casting a wide net, should Parliament have written, at the sure risk of forgetting some other types of directors, that the liability extended to "the directors of the corporation, whether *de facto* or *de jure*, whether nominal, passive or active[17], whether volunteer or paid, whether inside or outside directors and whether directors of a profit or a not-for-profit corporation? Or is it not reasonable to assume that, by using the word "director" in an unrestricted and unqualified manner, Parliament intended to cover all these types of

[17] *White (J.) v. M.N.R.*, [1990] 2 C.T.C. 2566, at page 2574. The Tax Court refused to read such classification of directors in subsection 227.1(1) with a view to providing relief to some but not others.

directors as well as all those who may exist in Canada pursuant to provincial laws, including statutory laws?

[17] That Parliament intended to give a broad and unrestricted meaning to the word "director" in subsection 227.1(1) is evidenced by the nature of the obligation put on the corporation and its directors, the nature of the debt owed by the corporation and the nature of the relationship between the corporation, the directors, the employees and the Crown. In this respect, the learned Tax Court judge, in my view, lost sight of these elements and, as a result, gave too restrictive an interpretation to subsection 227.1(1).

[18] Indeed, the debts owed to the appellant are not of the same nature as the commercial debts owed to suppliers in the ordinary course of business. Furthermore, contrary to a supplier who elects to do business with a given corporation, the Crown is an involuntary creditor since the amount and extent of its claim are determined by the number of employees that the corporation hires and the remuneration it pays. In addition, the sums due, which generally are made of taxes and contributions to social and insurance benefits, are for the benefit of both the employees and the public. Moreover, they are not moneys earned by the corporation by its trading activities. It is for these reasons that the Courts in England have treated these debts owed to the Crown as "quasi-trust" moneys. In *Re Lo-Line Electric*

Motors Ltd.[18], Sir Nicolas Browne-Wilkinson V-C stressed this fact and the prejudice resulting to a company's employees. He quoted with approval the following excerpt from the decision of Vinelott J. in *Re Stanford Services Ltd.*[19]:

> The directors of a company ought to conduct its affairs in such a way that it can meet these liabilities when they fall due, not only because they are not moneys earned by its trading activities, which the company is entitled to treat as part of its cash flow (entitled that is in that the persons with whom it deals expect the company to do so) but, more importantly, because the directors ought not to use moneys which the company is currently liable to pay over to the Crown to finance its current trading activities. If they do so and if, in consequence, PAYE, national insurance contributions and VAT become overdue and, in a winding up, irrecoverable, the court may draw the inference

[18][1988] 2 All E.R. 692, at pp. 697-98.

[19][1987] BCLC 607, at p. 617.

> that the directors were continuing to trade at a time when they ought to have known that the company was unable to meet its current and accruing liabilities, and was unjustifiably putting at risk moneys which ought to have been paid over to the Crown as part of the public revenues to finance trading activities which might or might not produce a profit. It is, I think, misleading (or at least unhelpful) to ask whether a failure to pay debts of this character would be generally regarded as a breach of commercial morality. A director who allows such a situation to arise is either in breach of his duty to keep himself properly informed, with reasonable accuracy, as to the company's current financial position ... or is acting improperly in continuing to trade at the expense and jeopardy of moneys which he ought not to use to finance the company's current trade.

[19] In my view, subsection 227.1(1) ought not to have been given an unduly restrictive interpretation which had the effect of compromising the valid social objectives sought to be attained by the provision. The fact that it imposes liability on the directors personally for their own failure to act

does not justify the restrictive interpretation put on the word "director" by the learned Tax Court judge. In view of the broad wording of "director" in subsection 227.1(1), a failure to recognize the responsibility and liability of persons acting as *de facto* directors amounts to condoning and inviting the performance of acts and omissions by such persons which are detrimental to employees and the public in a trust-like situation. The words of Hodgins J.A. in *Re Owen Sound Lumber Co.*[20] are quite appropriate:

> As to the second point, I agree with the view of Middleton J., that, when the directors assumed the fiduciary office of director, they became liable in all respects as though rightly appointed to that office. To hold otherwise would be to say that a man might do wrongful acts affecting the company's assets,

[20] [1917] 38 O.L.R. 414, at p. 421.

> and yet enjoy immunity if he could show some defect in his appointment. If this were the case, it would become fashionable to usurp the office on these terms rather than to accept it in a legitimate but less favoured way.

[20] In my respectful view, this is even truer when, in a trust-like situation, the wrongful acts are prejudicial to both the employees and the public.

The standard of care and diligence applicable in the present instance

[21] The learned Tax Court judge was of the view, at pages 19 and 20 of his decision, that the standard of care applicable to the directors of a not-for-profit corporation, such as the Louisbourg Harbourfront Park Limited Corporation (Corporation), was a standard less rigorous than the one governing the directors of corporations run for profit. He relied upon the decision of this Court in *Soper v. Her Majesty the Queen*[21] that he understood to mean that there were "different standards of care applicable to inside and outside directors"[22]. I note in passing that this Court in *Soper* expressly stated that it did not establish a different standard of care for inside and outside directors. Robertson J.A., at

[21] [1998] 1 F.C. 124.

[22] *Id.* at p. 155.

p. 156, wrote:

> At the outset, I wish to emphasize that in adopting this analytical approach I am not suggesting that liability is dependent simply on whether a person is classified as an inside as opposed to an outside director. Rather, that characterization is simply the starting point of my analysis.

[22] Relying upon the decision in *Soper*, the respondents argued that the standard of care found in subsection 227.1(3) of the Act is inherently flexible and, therefore, there are different standards to meet different situations. Accordingly, there would be one standard for inside directors, one for outside directors, one for directors of a not-for-profit corporation, one for volunteer directors and another one for paid directors. To accept this approach begs the thorny question: which of all these different

standards should a Court apply if one is, at the same time, an outside director acting without remuneration in a not-for-profit corporation?

[23] It is true that in *Soper*, this Court wrote that "the standard of care laid down in subsection 227.1(3) of the Act is inherently flexible"[23]. It is obvious, however, on the reading of the decision, that it is the application of the standard that is flexible because of the varying and different skills, factors and circumstances that are to be weighed in measuring whether a director in a given situation lived up to the standard of care established by the Act. For, subsection 227.1(3) statutorily imposes only one standard

[23] [1998] 1 F.C. 124, at p. 155.

to all directors, that is to say whether the director exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.

[24] I agree with counsel for the appellant that the rationale for subsection 227.1(1) is the ultimate accountability of the directors of a company for the deduction and remittance of employees' taxes and that such accountability cannot depend on whether the company is a profit or not-for-profit company, or I would add whether the directors are paid or not or whether they are nominal but active or merely passive directors. All directors of all companies are liable for their failure if they do not meet the single standard of care provided for in subsection 227.1(3) of the Act. The flexibility is in the application of

the standard since the qualifications, skills and attributes of a director will vary from case to case. So will the circumstances leading to and surrounding the failure to hold and remit the sums due.

[25] In my respectful view, it was an error for the Tax Court judge to conclude that the standard of care was different and less rigorous in not-for-profit corporations. As a result, he misinterpreted and misapplied the evidence that was before him.

Application of the standard of care and diligence to the respondents

[26] In the present instance, the failure to withhold and remit the sums due to the Crown began in November 1992. Some of the respondents (Lawrence, Parsons, MacDonald and Wheeliker) learned of it at the January 13, 1993 meeting of the directors while the others (Corsano and Maindiratta) were appraised of the fact at a subsequent meeting on February 3, 1993. In the case of respondents Corsano, Wheeliker and Maindiratta, they knew of the financial difficulties of the Corporation as of November 1992.

[27] Yet, somewhat surprisingly, the failure to withhold and remit the sums due lasted until October 1993 when the Corporation finally went bankrupt. This means that, as of their learning of the financial difficulties of the Corporation or its failure to remit, all the respondents were under a positive duty to act to prevent failure to make current and future remittances and not simply to cure default after the fact[24]. At best, the duty existed for some directors for nine months. At worst, for others, the omission to prevent failure lasted 12 months.

[28] The evidence revealed that no positive steps were taken to prevent the Corporation's failure to

[24] *Soper v. R.*, [1998] 1 F.C. 124, at pp. 158, 160 and 161.

remit current and future source deductions when it started to experience financial difficulties. At the January 13 and February 3, 1993 meetings, no action was taken by the directors with respect to the matter.

[29] At the March 3, 1993 meeting, respondent Corsano, upon becoming aware of the arrears in remittances, gave an instruction to the Manager to pay such arrears with a receivable that the corporation was expecting. Again, there is no evidence of steps or measures taken to address the problem for current and future remittances. Numerous cheques were co-signed by the directors up to September 1993 and remitted to suppliers. The May meeting of the Board of Directors also gave rise

to no corrective measures to prevent additional failures. There was no follow-up on the direction to pay past dues given at the March meeting.

[30] At the July meeting, respondent Corsano allegedly learned for the first time that his March direction to the Manager had not been implemented and, therefore, that the previous sums were still owing to the Crown. He also became aware that throughout the period, the current remittances too had not been paid. He instructed that every cent be sent to the Crown. This, however, was not meant to be what it said since the suppliers were nonetheless to be paid in order to keep the business going[25].

[25] See the testimony of Mr. Corsano in Supplement to Appeal Book, vol. 15. pp. 112-113.

Indeed, shortly after the meeting, he interceded with the Manager to ensure payment of a supplier's invoice to the detriment of Revenue Canada[26]. Therefore, as the evidence reveals, payment of the Crown's debts was not made and there was no follow-up of any kind to ensure the implementation of such direction. Moreover, once again, no positive steps were taken such as setting up controls to account for remittances, asking for regular reports from the manager on the ongoing use of such controls and ensuring at regular intervals that the remittances have taken place. And the failure continued to occur for some more months. In fact, the directors delegated their authority on this matter to the Manager, but literally failed to control its exercise notwithstanding clear evidence of repeated omissions

[26]See Common Appendix I, vol. 3, pp. 366-368.

and failures on the Manager's part. The delegation amounted to nothing less than abdication.

[31] The learned Tax Court judge gave a number of reasons to support his conclusion that the respondents had exercised the degree of care, diligence and skills required in the circumstances.

[32] First, he concluded that the freedom of the Board to act was curtailed to a large extent by the Louisbourg Harbourfront Park Society (Society) which owned 96% of the shares of the Corporation. Such finding is not supported by the evidence with respect to the issue at stake. It is true that the Society would not relinquish its shares in the Corporation to let it go private. But this is a far cry from

interfering with the Corporation's obligations under subsection 227.1(1) of the Act. In his testimony, Mr. Wheeliker, who was the chairman of the Board, admitted in cross-examination that the Society did not prevent the Board from exercising its control over the Corporation[27]. Nor did it get involved in the policy decisions made by the Board or interfere with the day to day operations of the Corporation[28]. Although there was undoubtedly a desire by the Society to keep the Corporation going, there was no evidence of the Society preventing the Corporation from withholding and remitting to Revenue Canada the source deductions.

---

[27] Supplement to Appeal Book, vol. XII, p. 163.

[28] *Id.*, at pp. 163-164.

[33] Second, the Tax Court judge found some comfort in the fact that, at the March meeting, the Board instructed the Manager to send to Revenue Canada a receivable expected from Enterprise Cape Breton Corporation. In my view, this fails to address the issue. Such payment would have corrected default and paid the past remittances, but the issue of the current withholding and remittances was left unaddressed. No steps were taken to put an end to the on-going failures and to prevent the likely on-coming failures.

[34] Third, the Tax Court judge considered as a positive factor the fact that the Board had taken

great care in hiring a qualified person as Manager and were justified in trusting him. With respect, there was evidence that the directors knew early in the process of the failures to remit sums to Revenue Canada. In addition, according to the directors, the Manager did not follow their instructions to pay Revenue Canada. Yet, no swift and diligent measures were taken to address this alleged disobedience by the Manager and correct the situation for the past and the future. In his testimony, Mr. Corsano admitted that he had serious concerns about the Manager's ability to run the company, especially as he was disregarding the directives of the directors, but yet, as a principal director, he did not call a meeting of the Board to discuss the issue and take the necessary appropriate corrective measures[29].

[29]Supplement to Appeal Book, vol. 15, at pp. 128-130.

[35] Fourth, in assessing the respondent's due diligence, the Tax Court judge took in consideration the fact that the directors were satisfied that the asset values of the Corporation would be sufficient to meet the claims of all creditors, including Revenue Canada. With respect, this is an irrelevant consideration. The obligation on the directors is to prevent a failure, not to condone it systematically, as the respondents did, in the hope of eventually correcting it because there would be enough money in the end to pay all the creditors.

[36] Fifth, he was satisfied that the directors made inquiries at the meetings of the Board with respect

to the status of remittances. He may have been satisfied that such behaviour was sufficient to meet the less rigorous test that he was applying to the situation. However, this is obviously not enough to meet the burden imposed by subsection 227.1(3).

[37] Finally, he considered the fact that the Society dismissed all the directors of the Corporation and send it into bankruptcy, thereby preventing these directors from continuing to try and keep the business going and getting in a healthier financial position.

[38] Again, this is, in my view, an improper consideration to take into account in assessing the degree of care and diligence exercised by the directors. At the time of their removal, they had been in default of withholding and remitting the source deductions for almost one year. As the Court said in *Re Stanford Services Ltd.* (*supra*), in the passage previously quoted, the directors ought to have conducted the affairs of the Corporation in such a way that it could "meet these liabilities when they fall due... because the directors ought not to use moneys which the company is currently liable to pay over to the Crown to finance its current trading activities".

[39] In conclusion, I believe the learned Tax Court judge took into consideration factors, which either taken in isolation or as a whole, cannot justify his conclusion with respect to the liability of directors pursuant to subsections 227.1(1) and (3) of the Act.

[40] As sad as it may be, especially with respect to the respondents who acted as benevolent directors and gave their time, it is simply not possible to find that they have exercised the degree of care and diligence expected to prevent a failure to withhold and remit when such known failure was allowed to repeat itself uninterruptedly for one year. This Court would be remiss of its duty to enforce the law if it were to condone acts or omissions performed by experienced, informed and warned directors which

fall below the standard of care, diligence and skill expected from them pursuant to subsection 227.1(3) of the Act.

[41] For these reasons, I would allow these appeals, I would set aside the decisions of the Tax Court judge, and I would dismiss the appeals by the respondents Wheeliker, Corsano and Maindiratta from the assessments made by the Minister of National Revenue pursuant to subsection 227.1(1) of the *Income Tax Act*. With respect to the respondents Lawrence, Parsons and MacDonald, I would, rendering the decisions that the Tax Court judge ought to have rendered, allow their appeals in part and refer the assessments back to the Minister for reconsideration and reassessment on the basis that the liability of these three respondents for failure to withhold and remit begins as of January 13, 1993. As the appellant is not seeking costs, I would issue no order as to costs.

"Gilles Létourneau"
J.A.