

THE PERSONAL TORT LIABILITY OF DIRECTORS

Robert Flannigan*
Saskatchewan

Directors currently enjoy a measure of preferential treatment with respect to their tort liability exposure. Professor Flannigan explains how the jurisprudence has come to this position largely through the operation of a series of confusions. He then examines, and rejects, the various policy arguments that have been advanced to justify a lesser liability for directors. He concludes that the risk-taking of directors is properly regulated by the same general tort responsibility that disciplines the conduct of all other actors.

Les administrateurs de société aujourd'hui jouissent d'un certain traitement de faveur dans leur assujettissement à la responsabilité pour délits. Le professeur Flannigan explique comment, en grande partie à cause d'une série de méprises, la jurisprudence en est arrivée à cette position. Ensuite il examine, pour les rejeter, les divers arguments de politique qui ont été mis de l'avant pour justifier une responsabilité réduite des administrateurs. Il conclut que c'est la même responsabilité pour délits qui gouverne la prise de décisions risquées par les administrateurs et la conduite de toutes autre personne.

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* Robert Flannigan, of the Faculty of Law, University of Saskatchewan, Saskatoon, Saskatchewan.

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I. *Introduction*

It is commonly assumed that both shareholders and directors secured comprehensive statutory limited liability under the general incorporation statutes of the mid-nineteenth century. That assumption is wrong. Directors do not have a statutory limited liability equivalent to that of shareholders. Their liability is instead determined by the law of agency. The failure to appreciate this legal fact, that liability rules for shareholders and directors are predicated on different conceptual foundations, has recently produced a state of confusion in parts of the jurisprudence. The degree of this confusion is, at times, breathtaking. The judges have been either mistaken as to the policies and principles that are relevant, or purposely innovative, and in both respects have confused and complicated the case law. The confusion is magnified when propositions developed in one context bleed or leak into other areas. There are cases, it should be noted, where judges do manage to see through much of the disorder, but they have been overwhelmed, and the confusion remains largely unabated. The greatest degree of confusion is found in the Canadian cases. There is less confusion in the English, Australian and New Zealand courts, but they too have contributed problematic judgments.

The main effect of the recent confusion, together with earlier decisions, is that directors today enjoy a degree of special treatment in relation to their personal tort liability exposure. They benefit, for example, from a lower standard of care, higher liability thresholds for intentional torts and the reluctance of judges to find personal liability where they believe (wrongly) that doing so involves piercing the corporate veil. This special treatment is not merely practically significant; it raises a fundamental policy question: What, if anything, justifies this treatment? The conventional rule is that actors are responsible for the consequences of their actions. This is a manifestation of the universal social norm of risk regulation. We generally permit actors to do as they please, subject to the condition that they compensate those who suffer damages at their hands. The purpose of this ascription of liability is to regulate *ex ante* the risk-taking of the actor. The risk regulation norm would appear to apply to directors in the same way it applies to all other actors. Those who have the power to cause harm must feel, and be disciplined by, the effects of their actions. Only persons assumed to be passive (eg. shareholders, limited partners, trust beneficiaries) escape the initial application of this basic responsibility. Why is the operation of this risk regulation norm attenuated in its application to directors? The jurisprudence, it turns out, does not offer a compelling justification.

It is perhaps no surprise that, despite the lack of justification, special treatment for directors apparently is not regarded as a matter of great consequence

by the general public. Apart from the occasional spectacular company failure that briefly attracts the attention of the public, the discussion that does occur on this issue is largely one-sided. Concerns over personal liability for directors are routinely expressed in the financial press. Regular warnings are issued that existing or proposed liability assignments will have generalized pernicious effects. The standard concerns, repeated endlessly, are that competent individuals will refuse to serve as directors, corporate decision-making will be constrained and inefficient, innovation will be stunted, a competitive disadvantage with other jurisdictions will exist and, in due course, the end of capitalism will come to pass. This flood of concern, although baseless, takes on the appearance of plausibility because it remains essentially unchallenged at the level of public comprehension. The absence of public challenge in the specific context of common law tort liability, however, is explicable. Future tort victims either do not identify themselves as potential victims or tend to be sanguine about their prospects of suffering tort loss. Potential victims (whether individual or corporate) who carry insurance may regard themselves as having little or no incentive to publicly contest the prudence of granting special treatment to directors. Future victims may also understand that the corporation itself will often be held vicariously liable and they may assume that corporations are more likely than individual directors to have the resources to cover any tort losses. The result is that prospective victims, as such, tend not to be politically organized. They therefore do not constitute a significant political force. There is also a socialization of tort injury that tends to deflect public awareness of the worst effects of tortious conduct. Worker compensation benefits, state health care, welfare and other regimes work to conceal the human cost of tort loss. Accordingly, the individuals who constitute the general public do not see themselves as having a material personal stake in the matter of the common law tort liability of directors. If anything, they are likely sympathetic to the concerns expressed about existing or increased personal liability for directors.

The ensuing discussion of the common law tort liability of directors is intended to be comprehensive. Regrettably, that entails the critical review of a very large number of cases. There is no escaping this extended review, however, if one hopes to fully comprehend the existing jurisprudence. For our purposes, the cases may be sorted into four categories. The first two categories include all of the negligence cases. One category is comprised of the line of cases addressing the nature of the duty of care directors owe to their respective corporations. The second category contains the cases dealing with the duty of care directors owe to third parties. The next two categories cover the intentional torts. The third set of cases is concerned with the tort of inducing a breach of contract. The fourth category contains the cases dealing with other intentional torts. After first examining the statutory and common law foundations for shareholder and director liability, the analysis of the four categories proceeds in two historical stages. The first stage covers the period up to the mid-1980's, and the second stage from then through 2001. The first stage is a relatively stable period of judicial tinkering with controversial, but well understood, legal propositions. The beginning of the second stage marks the judicial introduction

of a series of new tests and approaches that have had the effect of seriously complicating and confusing the jurisprudence. Following that analysis, the ostensible justifications for the special treatment of directors are examined. The discussion ends with the conclusion that directors should experience the default application of the general law of tort in exactly the same way as do all other actors.

II. *The 1855 Parliamentary Debate*

The extent to which shareholders or directors today enjoy limited liability with respect to tort claims is initially a question of legislative intent. Accordingly, the inquiry into this matter usefully begins in England with the lengthy parliamentary debate that occurred at the midpoint of the nineteenth century. That debate concluded in favor of general [contractual] limited liability for shareholders, and the resulting English legislation was thereafter copied throughout the Commonwealth.¹ An examination of the debate will disclose the original stated rationale for, and intended scope of, the limited liability principle. That will provide the political baseline for understanding subsequent legislative and judicial developments.

Before turning to the debate itself, it is important to appreciate the commercial circumstances giving rise to the issue.² Limited liability was not a novel idea at the time. In addition to expressly contracting for it, limited liability could be acquired by special Act or through the exercise of the royal prerogative upon the grant of a charter.³ These latter methods of obtaining limited liability, however, were both slow and expensive. The general complaint was that incorporation with limited liability was effectively reserved to the wealthy. Most businesses were in fact conducted through the partnership form. There

¹ The initial 1855 *Limited Liability Act* (18 & 19 Vict. c. 133) was quickly incorporated into the 1856 *Joint Stock Companies Act* (19 & 20 Vict. c. 47). The latter statute was replaced by the *Companies Act* of 1862 (25 & 26 Vict. c. 89) and this was the model for corporate legislation throughout the Commonwealth for many decades.

² For a concise account, see, L.C.B. Gower, *Principles of Modern Company Law*, 4th ed. (London: Stevens & Sons, 1979) c. 3. For more elaborate accounts, see B.C. Hunt, *The Development of the Business Corporation in England 1800-1867* (Cambridge: Harvard University Press, 1936); J.B. Jeffreys, *Business Organization in Great Britain 1856-1914* (1938 doctoral dissertation published in 1977) (New York: Arno Press, 1977); P.L. Cottrell, *Industrial Finance 1830-1914* (London: Methuen, 1980); P. Ireland, "The Rise of the Limited Liability Company" (1984) 12 *Inter. J. Soc. Law* 239; C.E. Amsler et al., "Thoughts of Some British Economists on Early Limited Liability and Corporate Legislation" (1981) 13 *Hist. Pol. Econ.* 774.

³ As to the efficacy of contracting for limited liability, see *Hallett v. Dowdall* (1852), 18 Q. B. 2. With respect to the power of the Board of Trade, see the 1834 *Trading Companies Act* (4 & 5 Will. c. 94) and the 1837 *Chartered Companies Act* (7 Will 4 & 1 Vict. c. 73). The extent of the limitation on liability depended on the specific provisions in the contract, special Act or charter.

were two economic variations of the partnership structure.⁴ One was the traditional fraternal partnership with few members. The other was the joint stock company, a partnership with [typically] many members (called shareholders), delegated management (a board of governors or directors) and freely transferrable interests (shares).⁵ The argument was that the members of both of these types of partnership ought to benefit from the same organizational advantages their wealthier incorporated competitors enjoyed. The government initially reacted to this claim by requiring larger joint stock companies (more than 25 partners) to become incorporated under the 1844 *Joint Stock Companies Act*.⁶ The standard advantages of corporate status, with the express exception of limited liability, were granted by this statute. The demand for limited liability continued, however, and caused the government to act again in 1855. It introduced two bills, one for each of the partnership forms.⁷ The Partnership Amendment Bill purported to give limited liability to passive investors in traditional fraternal partnerships, thereby creating something approaching the limited partnership of the civil law.⁸ The second proposal, the Limited Liability Bill, was intended to provide limited liability to passive investors in joint stock companies.⁹ The former bill, for a variety of reasons, was ultimately withdrawn.¹⁰ Government efforts focussed instead on passing the Limited Liability Bill. The precise issue was whether the privilege of limited liability should be extended generally to business undertakings required to register under the 1844 incorporation legislation.

Two further observations will help frame the debate. As it played out, the debate represented a significant, but limited, challenge to the existing liability configuration the common law applied to shareholders and directors. Under the

⁴ See P. Ireland, "The Triumph of the Company Legal Form, 1856-1914", c. 3 in J. Adams, ed., *Essays For Clive Schmitthoff* (Oxon: Professional Books Limited, 1983).

⁵ Delegated management was not included as a formal defining characteristic of joint stock companies in the 1844 general incorporation legislation. The *Joint Stock Companies Act* 7 & 8 Vict., c.110, s. 2, applied to the subgroup of joint stock companies defined as (1) "Every Partnership whereof the Capital is divided or agreed to be divided into Shares, and so as to be transferrable without the express Consent of all the Co-partners and . . . (2) Every Partnership which . . . shall consist of more than Twenty-five Members."

⁶ *Ibid.* Registration was mandatory for the identified companies. The legislation was intended to regulate business, not necessarily facilitate it.

⁷ See Ireland, *supra* note 4 at 31-33.

⁸ See Hansard, 1855, Vol. 139, beginning at col. 310, 636, 1348; Vol. 140, beginning at col. 473, 2200; Vol. 142, beginning at col. 652; Vol. 143, beginning at col. 338, 801.

⁹ The debate reflected the assumption of passive capital. Note also that the 1844 Act, *supra* note 5, s. 27 authorized the directors to manage the affairs of the company subject to the provisions of the deed of settlement, "but not so as to enable the Shareholders to act in their own Behalf in the ordinary Management of the Concerns of the Company otherwise than by means of Directors." See also Hunt, *supra* note 2 at 130-31.

¹⁰ Another version of the proposed legislation eventually succeeded as the *Partnership Amendment Act 1865* (28 & 29 Vict. c. 86) (Bovill's Act). In other common law countries (eg. U.S., Canada), statutory limited partnerships had already been introduced.

then current law, partners in both the traditional partnership, and the incorporated and unincorporated versions of the joint stock company, were subject to open liability for contract and tort losses.¹¹ The directors of these partnerships, however, did have limited liability of a particular *kind*. They were *agents*, either of the body of partners (unincorporated partnerships) or of the corporation (incorporated partnerships), and were therefore subject to the liability configuration of the general law of agency.¹² As agents, the directors were not liable on contracts properly entered into on behalf of their principals. They were liable, however, for any tortious acts they personally committed, and their principals were simultaneously vicariously liable if the tort occurred in the course of the agency. These liability assignments were the standard consequences of the creation of an agency relationship.¹³ Only one aspect of this liability configuration was challenged in the debate. The arguments addressed only the *contractual* liability exposure of *shareholders* of incorporated joint stock companies. There was no discussion of the open tort liability of shareholders, or the contract or tort liability of directors.

The second observation is a conceptual one. As will shortly appear, the debate did not turn on the elementary legal analysis often employed today to justify limited liability. The common modern justification is that limited liability is simply a logical consequence of separate entity status. That explanation, however, circumvents a full evaluation of public policy. It purports to introduce limited liability through the back door of legal principle. It does not justify limited liability, it only begs the question. What justifies separate entity status if one of its automatic consequences is limited liability? The proposition merely returns us to the issue of limited liability. As it happened, the two Houses of Parliament were not carried by (or even introduced to) that kind of abstract legal claim. Rather, a social choice was consciously made after open consideration of the expected pragmatic consequences of generally extending the availability of limited liability. It was a political process. That was the proper mechanism

¹¹ *Rex v. Dodd* (1808), 9 East. 516, 103 E. R. 670; *Fox v. Clifton* (1830), 6 Bing 776, 130 E.R. 1479; *Barnett v. Burdett* (1846) 6 L. T. 326 (Ex.); *Hallett v. Dowdall*, *supra* note 3; *Greenwood's Case*, (1854), 3 De G. M. & G 459, 43 E. R. 180.

¹² See *The Charitable Corporation v. Sutton* (1742), 2 Atk. 400, 26 E.R. 642; *Hawken v. Bourne* (1841), 8 M. & W. 703, 151 E. R. 1223; *Ferguson v. Wilson* (1866), 2 Ch. App. 77 (C.A.); *Hallett v. Dowdall*, *supra* note 3. That remains the case today. See *Daido Asia Japan Co. Ltd. v. Rothen*, [2001] E.W.J. No. 3997 (Ch.) (Q.L.). Occasionally, however, commentators will argue that the board of directors is some sort of *sui genesis* "organ" of the corporation. This is a confusing, unhelpful and unnecessary theoretical idea, and it has not found its way into the cases as a general proposition. Directors are plainly agents with respect to the conduct of the business. They acquire that status through the statutory default delegation of management to board members. The "organ" notion is said to accommodate the attribution of human characteristics to corporations (eg. *mens rea*), but this is at best a descriptive function with no demonstrated analytical power.

¹³ This agency status was recognized in the 1844 legislation (eg. sec. 45). The statutory liabilities of directors (in both corporate and general legislation) represent supplemental regulation or specific qualifications of the general law of agency.

or process to resolve the issue. The question of limited liability was (and is) a significant matter of public policy and ultimately requires justification in terms of its fit with our actual social needs and concerns. It is not enough to assert a sterile logic that only cloaks the policy choice.

The 1855 debate took place after many years of public discussion and, consequently, the topic was a familiar one to many members of Parliament.¹⁴ The government's initial introduction of the two bills began with a listing of the ostensible mischiefs associated with the existing state of affairs.¹⁵ The liability concern of passive shareholders, it should be noted, was not separately identified as one of those mischiefs. Rather, it appears to have been the basic premise upon which the debate proceeded. Why should passive investors, with no real ability (or desire) to control their investment, be made responsible beyond their capital contribution?

The particular mischiefs the bill purported to address were several. Persons of wealth were said to be deterred from investing in joint stock undertakings because of their potential open liability. So framed, this capital supply argument was a narrow elitist concern. The political weakness of that idea was apparently recognized early on in the debate because it did not reappear in that form in later speeches. Instead, more palatable versions of the capital supply concern were offered. Thus, the mischief became a supposed generalized commercial need for capital and an inability to meet that need because of the current disincentive to the combination of small capitals. Even the poor and working classes were cynically brought into the equation. It was said to be a great inequity that workers could not invest their meagre capital in profitable enterprise without risking financial ruin. The effect of the Bill, it was argued, would be to marry labour and capital. These latter arguments obviously were more carefully calculated to appeal to broad public and private interests and thereby to attract wide public support for the measure. A second mischief was the perceived emigration of business to other jurisdictions (eg. France) where limited liability was supposedly more readily available. The consequences of losing the inter-jurisdictional competition were said to include a loss of fees and duties and even the displacement of London as the financial center of the world. A third ostensible mischief was that the undertakings that already benefited from limited liability had no special claim to that privilege and that it was an unwarranted discrimination to favor them over other business operations. A fourth mischief was the arbitrary exercise by the Board of Trade of its power to confer limited liability on chartered companies. The power was thought to be

¹⁴ See Hunt, *supra* note 2 at 116-44; Gower, *supra* note 2 at 39-47; Amsler et al., *supra* note 2; H.A. Shannon, "The Coming of General Limited Liability" (1931) 2 Econ. Hist. 267; J. Saville, "Sleeping Partnership and Limited Liability 1850 - 1856" (1956) 8 Econ. Hist. Rev. 418; J. Winter, *Robert Lowe* (Toronto: University of Toronto, 1976) at 97-101. Public discussion of liability alternatives prior to 1855 was concerned almost exclusively with the limited partnership (*commenda*).

¹⁵ The bulk of the debate in the two Houses is recorded in Hansard, 1855, Vol. 139, beginning at columns 310, 1378, 1445, 1517, 1895, 2025, 2101, 2123, 2127.

exercised according to the caprice of the government of the day and, accordingly, was unacceptable. Other ostensible mischiefs supposedly associated with the existing state of affairs included creditors being misled by the massed capital of partners, prejudice to shareholders when directors were replaced by directors in whom they did not have confidence and the artificial diversion of capital flows. All of these alleged mischiefs, it was argued, would be cured by a general legislative grant of limited liability to shareholders in registered joint stock companies.¹⁶

In addition to correcting these mischiefs, there would be other benefits. It was claimed, for example, that the principle of limited liability was responsible for the prosperity of those countries where it was generally available. Although England's own economic prosperity was due largely to its geographic location, it was argued that the country would have prospered even further had limited liability been widely available.¹⁷ Other arguments were deployed to undercut the expected opposition. It was said that limited liability was *à fait accompli*, that only respectable companies would acquire the privilege, that opposition represented an interference with freedom of contract, that the industrialists who opposed the bill sought only to secure their own advantage and that, if nothing else, it was an experiment worth trying.¹⁸ The proponents of limited liability also sought to meet the argument that the bill was mischievous because it seriously restricted the rights of creditors to recover what was rightfully owed to them. Their view was that the legislation provided for notice of limited liability and that, consequently, creditors who voluntarily dealt with the company on that basis could not fairly complain.¹⁹

¹⁶ It will be appreciated that a number of these ostensible mischiefs were in fact consequences of earlier grants of limited liability (i.e. preference for limited risk investments, offshore limited liability, industrial discrimination, Board of Trade discretion in granting limited liability). These arguments, accordingly, were of the bootstrapping variety. Once limited liability is granted to one party, the discrimination claim (for example) will inevitably follow. Several of the supposed mischiefs and benefits also involved empirical claims for which there was apparently little or no evidence.

¹⁷ That limited liability was (or is) a primary engine of commercial prosperity is little more than a legal conceit. The industrial revolution was well on its way long before the 1855 adoption of limited liability. International trade, political dominance and technological innovation were the immediate reasons for the economic expansion of England and other countries in the nineteenth century. In terms of efficiency, a default rule of limited liability is of little significance to voluntary creditors, and inefficient where employed as a substitute for liability insurance. The general rule is that a risk will be taken where expected benefits exceed expected costs, including the direct and indirect cost/benefit of limited or unlimited liability.

¹⁸ There were a few other incidental justifications, one of which was that the bill was supported by the legal profession. One reaction to that observation was: "No doubt they were, for it would open a wide field for litigation" (Mr. Muntz, Hansard, 1855, Vol. 139, col. 1382). As for the benefit to solicitors, it was observed that "petty Companies of all kinds would be set afloat by lawyers for the purpose of getting long bills paid to them for their services in promoting the schemes" (Lord Redesdale, Hansard, 1855, Vol. 139, col. 2042).

¹⁹ See, on this point, the remarks in Hansard, 1855, Vol. 139, of Mr. Cardwell, cols. 343-44; Lord Stanley, col. 1920 and the Marquess of Lansdowne, cols. 2123-24. It was clear that all members understood they were assessing the *default* position.

Opponents of the bill doubted that there was any commercial need or demand for limited liability. They rejected the view that capital was in short supply. They thought the poor and working classes would be misled by the idea of limited risk. They concluded that the existing instances of limited liability for certain undertakings were justified by their nature and size. They were not concerned with the administration by the Board of Trade of its discretionary power to grant limited liability. They doubted that the experience of other countries, with different economic conditions, was relevant or comparable to England. Instead, they appealed to the "natural" principle that actors are accountable for the consequences of their actions.²⁰ To brush aside that principle would be to diminish the credit of the country, encourage disastrous speculation and facilitate opportunism and fraud of all kinds. The bill was being pushed through Parliament, it was argued, without due consideration for these concerns, the protection of creditors or the adequacy of the related bankruptcy laws.

On the face of it, the debate was a contest between, on the one hand, the traditional principle of personal responsibility and, on the other, a hodgepodge of economic and social concerns including the commercial health and credit of the country, offshore incorporation and discrimination between industries and social classes. There is, however, another view of the motivating factors, one that has little to do with any concern for the public interest. There are indications that the contest pitted large business against an alliance of small business and large and small investors.²¹ Large business, at least where it was self-capitalized, feared precisely what limited liability was ostensibly intended to accomplish — an increase in the supply of commercial capital. That capital would come from wealthy investors (rather than wealthy business operators) and from the combined capitals of numerous small investors, and would be utilized by small business to expand and compete with large business.²² The effect would be to

²⁰ See the remarks in Hansard, 1855, Vol. 139, of Mr. Strutt, col. 1386 ("the first and most natural principle of commercial legislation was, that every man was bound to pay the debts he had contracted, so long as he was able to do so"). See Hunt, *supra* note 2 at 116-18 and E.W. Cox, *The Law and Practice of Joint Stock Companies*, 6th ed. (London: J. Crockford, 1862) at 1 *et seq.*

²¹ Consider the views of Jefferys, *supra* note 2, c.1; Saville, *supra* note 14 at 431-32; Amsler et al., *supra* note 2; Cottrell, *supra* note 2, c. 3; K.F. Forbes, "Limited Liability and the Development of the Corporation" (1986) 2 J. Law, Econ. & Org. 163; M. Lobban, "Corporate Identity and Limited Liability in France and England 1825 - 67" (1996) 25 Anglo-Am. L. Rev. 397.

²² The attraction for the investing classes was obvious. Investors were typically passive, looking only to obtain a rent for their capital. Investing in an unincorporated joint stock company, however, brought with it open liability. Other investing arrangements could be made, but were also problematic. Investors had always had limited liability if their investment was by way of a loan (*Cox v. Hickman* (1860), 8 H. L. C. 268, 11 ER 431). Sharing in profit, however, rendered their lender status uncertain. They could be, and were, characterized as partners (*Pooley v. Driver* (1876), 5 Ch. D. 458). The statutory grant of limited liability, which simply reversed the default position, displaced (subject to contractual reinstatement) the open liability risk. Limited liability investments were no longer restricted to debt-like investments or to investing in the industries or companies that had limited liability by royal prerogative or special Act.

decrease the profits and influence of the wealthy industrialists. The alliance between small business and large and small investors would be politically significant, obviously, because of their larger constituencies. It was also likely that most Parliamentarians were members of the investor class, with passive capital to invest (preferably on a limited risk basis), who could plainly see where their own interests lay. In any event, this focussed political power, targeting discrete economic objectives, would have little real concern for the supposed broader mischiefs to be corrected by the legislation and would hardly be diverted by a normative claim of personal accountability. The rejection of that claim was the very object of the narrow investor-driven political action. At the same time, of course, it would be tactically advantageous to mask the private objective with an appeal to the public interest.²³

The bill moved quickly through the two Houses and became the *Limited Liability Act*.²⁴ Two related propositions can be taken from this legislative exercise. The first is that Parliament openly granted default *contractual* limited liability to the shareholders of registered joint stock companies. So understood, this was a significant change in the law, but not a significant interference with economic relations. Because limited liability was established as a *default* rule, it could have little substantive impact on voluntary creditors. The actual liability exposure of any party to a voluntary arrangement is invariably determined by their relative economic power, and not by a preliminary assignment of default responsibility. Where it matters, parties will contract around a default rule that does not reflect their relative power. Accordingly, when in 1855 Parliament reversed the default contract liability assignment applied between shareholders and voluntary creditors, it did little to alter commercial or social relations in any substantial way.²⁵

²³ Although large business lost the contest, it must have soon recognized that its own interests were served by limited liability (eg. isolating or segregating risky undertakings in affiliates) as formal opposition from that quarter subsided after the debate.

²⁴ Under sec. 7 of the Act, *supra* note 1, "The Members of a Joint Stock Company . . . shall not be liable, under any Judgment, Decree, or Order which shall be obtained against such Company, or for any Debt or Engagement of such Company, further or otherwise than is herein-after provided" [i.e. any amount unpaid on shares] In the 1856 *Joint Stock Companies Act*, *supra* note 1, the provision (s. 61) provided that "existing Shareholders shall be liable to contribute to the Assets of the Company to an Amount sufficient to pay the Debts of the Company, and the Costs, Charges and Expenses of winding-up the same, with this Qualification, that if the Company is limited no Contribution shall be required from any Shareholder exceeding the Amount, if any, unpaid on the Shares held by him."

²⁵ That is, although a significant *change*, it did not have a significant legal or economic *effect* on voluntary creditors (other than an alleged lawyer-driven (see Ireland, *supra* note 4 at 35-37) increase in the number of incorporations). With respect to its economic impact, see the views of H.A. Shannon, "The First Five Thousand Limited Companies and Their Duration" (1932) 2 Econ. Hist. 396 and "The Limited Companies of 1866-1883" (1933) 4 Econ. Hist. Rev. 290 and the earlier analysis of L. Levi, "On Joint Stock Companies" (1870) 33 J. Stat. Soc. London 1 and "The Progress of Joint Stock Companies With Limited and Unlimited Liability in the United Kingdom During the Fifteen Years 1869-84" (1886), 49 J. Stat. Soc. London 241. The increase in the number of incorporations can be explained by a perceived need to offer investors what they could

The second proposition is that the English legislature granted *only* contractual limited liability, and only to shareholders. It did not consider either the personal tort liability of shareholders or the contract or tort liability of directors. There was no discussion whatsoever of those issues. Confirmation that contractual liability was the only issue considered is found in the majority reaction to the claim the bill would seriously prejudice creditors. As noted above, the proponents of limited liability addressed that objection by observing that the legislation provided for notice of limited liability and that creditors were not prejudiced if they chose to deal with such companies on that limited recourse basis. That rationale obviously has no application to involuntary (eg. tort) creditors.

Accordingly, the expressed intention of the legislature was to alter the existing liability configuration of joint stock companies in only one specific way. There was no evident attempt to speak to, or alter, the tort obligations of shareholders or directors. Those liability assignments therefore remained as they were prior to the debate. That is the important observation for our purposes. There was no political foundation at this time for a general statutory limited liability for tort losses. In particular, the liability configuration for directors continued to be defined by the general law of agency.²⁶ Directors retained their agency immunity for contract breaches, and open liability for tort losses.

III. *The Salomon Decision*

The House of Lords decision in *Salomon v. A. Salomon and Company, Ltd.* is often taken to have confirmed the general limited liability of both shareholders and directors.²⁷ That interpretation of the case, however, is unjustified. The actual decision is considerably narrower in scope. Unfortunately, many judges fail to appreciate the limits of the case and freely appeal to its authority on any issue even remotely connected with limited liability. Judges and commentators who have examined the case more carefully have been less inclined to concede wide relevance to the *Salomon* judgments.

Aron Salomon had transferred his business to a corporation in exchange for shares and debentures. His wife and five children were also issued one share

obtain elsewhere (ie. limited liability). What was in effect a gift from the legislature became essentially a standard part of the package of terms transferred to investors in exchange for their investment. It was a matter of staying competitive with alternative investments in other corporate units.

²⁶ See *Re Agriculturist Cattle Insurance Company* (1870), 5 L.R. Ch. App. 725; *Thérien v. Brodie* (1893), 4 Que. S.C. 23; *Kuwait Asia Bank E.C. v. National Mutual Life Nominees Ltd.*, [1991] 1 A.C. 187 (P.C.). See also H. Thring, *The Law and Practice of Joint Stock and Other Companies*, 4th ed. (London: Stevens & Sons, 1880) at 99 ("the law of agency covers all the ground necessary to be covered in relation to the position of directors, whether as regards their personal liability for breach of duty or otherwise").

²⁷ [1897] A.C. 22. See G.R. Rubin, "Aron Salomon and His Circle", c. 7 in J. Adams, ed., *Essays for Clive Schmitthoff* (Oxon: Professional Books Limited, 1983).

each in order to satisfy the statutory requirement for seven shareholders.²⁸ When the business failed, the liquidator sought to subordinate Salomon's debentures to the claims of the unsecured creditors of the corporation. The liquidator's main argument was that the legislation was only intended to extend the privilege of limited liability to legitimate registered joint stock companies of at least seven persons. On this point, the liquidator was undoubtedly correct. Even the House of Lords seemed prepared to accept that view. Nevertheless, the liquidator's action was dismissed. Each judge observed that Salomon had complied with the legislation in every respect. The statute did not require that shareholders demonstrate that they were independent actors, or even beneficially interested in the company. The judges could only determine the intention of the legislature from the words of the statute itself, and they concluded that formal compliance with the legislative provisions was sufficient to create a new entity and confer limited liability on shareholders. In essence, the court concluded that the seven shareholder requirement was not a bar to the incorporation of sole proprietorships or smaller partnerships.²⁹ Though the legislature had in fact intended to exclude those economic structures, it had not adequately expressed that intention in the legislation.

For our purposes, it is important to understand what the judges did not address. They considered only the contractual liability of shareholders. They did not address the tort liability of either shareholders or directors. The judgments make this quite clear. A number of the judges pointed out that unsecured creditors had the means to protect themselves. Lord Herschell stated that the "creditor has notice that he is dealing with a company the liability of the members of which is limited, and the register of shareholders informs him how the shares are held".³⁰ Lord Macnaghten noted that the creditors "had full notice that they were no longer dealing with an individual, and they must be taken to have been cognisant of the memorandum and of the articles of association".³¹ Lord

²⁸ The seven shareholder requirement (an arbitrary identification of the size of partnership or business undertaking permitted to register) first appeared in the 1856 *Joint Stock Companies Act*, *supra* note 1. A failure to maintain that number exposed the shareholders to open liability. Sec. 39 of the Act stated that if "any Company registered under this Act carries on business when the Number of its Shareholders is less than Seven, for a period of Six Months after the Number has been so reduced, then every Person who is a Shareholder in such Company during the Time that it so carries on Business after such Period of Six Months shall be severally liable for the Payment of the whole Debts of the Company contracted during such Time ..." Sec. 39 did not survive the processes that produced the 1908 *Companies Act*.

²⁹ See Shannon, *supra* note 25. Another factor possibly contributing to this conclusion was the elimination of the minimum capital requirements initially proposed by the Government in 1855. See Lobban, *supra* note 21. It is interesting to note that enlisting nominal or nominee shareholders to circumvent the seven shareholder requirement was advocated from the inception of the legislation and was utilized for many years before being challenged in *Salomon*. In his 1862 commentary on the legislation, Cox (*supra* note 20 at 23) described the technique under the heading "How an Individual Trader may avail himself of Limited Liability."

³⁰ *Supra* note 27 at 45.

³¹ *Ibid.* at 53.

Watson added that "a creditor who will not take the trouble to use the means which the statute provides for enabling him to protect himself must bear the consequences of his own negligence".³² These judicial observations plainly restrict the *Salomon* analysis to voluntary creditors. Accordingly, the *Salomon* decision tells us nothing about the tort liability of either shareholders or directors.³³ Specifically, it discloses no alteration to the agency liability rules applied to directors.

IV. Shareholder Tort Liability

It is convenient at this point to briefly examine the tort liability of shareholders and thereby set the stage for our primary investigation of the common law tort liability of directors. As discussed above, neither Parliament nor the House of Lords visited the question of tort liability in the course of their respective decisions. Those decisions were premised exclusively on the position of voluntary creditors. Nevertheless, it is regularly *assumed* that the legislature intended to limit the liability of shareholders to both voluntary *and involuntary* creditors.³⁴ That assumption has been a remarkably powerful one and perhaps explains in part why no legislative or judicial body has subsequently thought it necessary to explore the matter [the policy considerations] in any extended or deep way.³⁵

³² *Ibid.* at 40.

³³ See *Morton v. Douglas Homes Ltd.*, [1984] 2 N.Z.L.R. 548 at 593 (H.C.); *Sullivan v. Desrosiers* (1986), 76 N.B.R. (2d) 271 at 278 (C.A.); *Trevor Ivory Ltd. v. Anderson*, [1992] 2 N.Z.L.R. 517 at 525-26 (C.A.); *ADGA Systems International Ltd. v. Valcom Ltd.* (1999), 168 D.L.R. (4th) 351 at 356, 359 (Ont. C.A.), leave to appeal dismissed, [1999] S.C.C.A. No. 124 (Q.L.); *ScotiaMcLeod Inc. v. Peoples Jewellers Ltd.* (1994), 15 B.L.R. (2d) 160 at 185-86 (Ont. Gen. Div.), *affd.* in part (1995), 129 D.L.R. (4th) 711 (Ont. C.A.).

³⁴ One contemporary commentator (Cox, *supra* note 20 at 5) offered the following view, albeit without reference to authority. Note the conceptual confusion in the commentator's summary:

It is the like with other liabilities to which individuals are now subject, but from which partnerships with Limited Liability are exempt. There is a large class of liabilities, known to the law as wrongs, which in the course of business are often done accidentally, but for which the law, nevertheless, makes the doer answerable in damages, such as a stage-coach killing a passenger, a ship running down another ship, undermining a house, and so forth. For none of these acts is a Limited Liability Company responsible beyond the amount of its shares subscribed, and if those shares are paid up, nothing, not even costs, can be recovered by the person wronged if an action be brought; but, practically, no person will bring an action against a Company from which he can recover nothing.

³⁵ Even academic commentary has been sparse. See, for example, (Note) "Should Shareholders Be Personally Liable For The Torts of Their Corporations?" (1967) 76 Yale L. J. 1190; R.E. Zimet, "The Validity of Limited Tort Liability For Shareholders in Close Corporations" (1973) 23 Amer. Univ. Law Rev. 208; H. Hansmann & R. Kraakman, "Toward Unlimited Shareholder Liability For Corporate Torts" (1991) 100 Yale L. J. 1879; D. Leebron, "Limited Liability, Tort Victims, and Creditors" (1991) 91 Colum. L. Rev.

A first observation is that general corporate legislation arguably must be understood to have excused shareholders from liability for any adverse consequences of the exercise of their statutory powers.³⁶ Thus, for example, they are not liable personally for contractual loss caused to any person as a result of their votes on some matter reserved to shareholders in general or special meeting. That, however, is not the end of the matter. There is an important distinction that must be understood before it is possible to fully comprehend the tort liability exposure of shareholders. The distinction is perhaps easiest to explain by describing the effect of incorporating a joint stock company. In the case of a partnership, each partner is personally responsible for tort losses that can not be met out of partnership assets, whether or not that partner was involved in causing the loss. That is the ordinary vicarious liability assigned to partners under the law of partnership. Every partner who commits or participates in the tort is personally liable, and every other partner is vicariously liable. It is this latter vicarious liability that was eliminated by the 1855 legislation. The effect of incorporation in the case of joint stock companies was to strip partners (shareholders) of their principal status in relation to the business undertaking. The corporation became the principal. When this conceptual substitution of principals occurred, the vicarious liability of individual shareholders was transferred to the corporation as the new principal. Nothing in that conceptual transference, however, absolved any party of liability for their own personal tortious conduct.

The legal entity abstraction, even fully recognized, goes only so far. It does not require or permit us to ignore the personal tortious conduct of the real persons it is associated with. Prior to incorporation, the shareholders in a joint stock company were principals in an agency relationship with the directors. Incorporation changed this by creating a new person to replace the body of shareholders as principal. That fictional person did not have the requisite physical *corpus* to cause harm to others and could not physically be personally liable.³⁷ It could only be vicariously liable for the tortious acts of its natural actors. The shareholders it displaced, however, were still able to inflict tort losses on others. They would continue to be liable for those losses unless the legislation dictated a different result. It did not. The conceptual substitution of principals had no theoretical implication for the tortious actions of the now

1565 at 1601 ("Indeed almost every commentator has paused to note that limited liability cannot be satisfactorily justified for tort victims . . . and then moved on as though there is nothing to do about this unfortunate wrinkle in the economic perfection of the law."); R. Thompson, "Unpacking Limited Liability: Direct and Vicarious Liability of Corporate Participants for Torts of the Enterprise" (1994) 47 Vand. L.R. 1.

³⁶ *Kuwait Asia Bank E.C. v. National Mutual Life Nominees Ltd.*, [1991] 1 A.C. 187 (P.C.). Consider *Emerson v. Flint* (1888), 7 U.C.C.P. 161; *Multinational Gas and Petrochemical Co. v. Multinational Gas and Petrochemical Services Ltd.*, [1983] 2 All E.R. 563 (C.A.).

³⁷ Keeping in mind the modern qualification that attribution of the mental state of natural persons will permit a *corporation* to be held legally personally liable.

dislodged shareholders. Their personal tortious conduct was not touched or addressed by the abstract move. They were still ordinary autonomous actors relative to the rest of the world and, as such, subject to the standard tort duties imposed on each and every one of us. Accordingly, shareholders who directly caused or participated in causing tortious loss remained liable as before. This is confirmed by the terminology of the legislation.³⁸ Although the wording of the statutory provisions has varied over time and jurisdiction, typically shareholders are excused from any responsibility for the debts, acts or obligations of the corporation. The personal tort liability of a shareholder is not a debt, act or obligation of the corporation. The distinction also reflects the operative assumption in the limited liability debate that passive shareholders should not be liable without limit for losses beyond their immediate control. Losses they personally cause (i.e. when they are not passive) are within their control, and are therefore properly regulated by open liability.

There is, as it turns out, very little authority on the issue of the personal tort liability of shareholders.³⁹ A large part of the explanation for this is likely that the issue rarely arises in the real world as a *shareholder* issue. Most shareholders are passive investors. The tortious acts they do commit will typically be completely unrelated to the corporation's business, and open liability is clearly the rule for those torts. Even when there is a connection between the tortious act and the business, however, it will usually be because of some other formal or *de facto* capacity or relationship of the shareholder. The shareholder, for example, may be an employee or agent of the corporation. In those cases, shareholder status is irrelevant. The liability of the shareholder will be defined by the coincident employee or agent status.⁴⁰ Nevertheless, in some circumstances, the tortious actions of persons who have no relational status other than shareholder may be connected to the business of the corporation. Shareholders at a general meeting may take it upon themselves to physically eject another shareholder or other speaker unwilling to concede the floor. Or a shareholder may defame others when speaking on corporate matters. These shareholders, though acting in a corporate context, are personally liable. The better view, in any event, is that shareholders (like any other actor) remain personally responsible for their own tortious conduct.

³⁸ See note 24 *supra*. Note that the *Interpretation Act* in most jurisdictions states that words establishing a corporation are to be construed as exempting members from personal liability for the debts, acts and obligations of the corporation.

³⁹ See *Blacklaws v. Morrow* (2000), 187 D.L.R. (4th) 614 at 628-29 (Alta. C.A.) ("We begin our analysis by acknowledging that there will be circumstances in which the actions of a shareholder ... may give rise to personal liability in tort despite the fact that the impugned acts were ones performed in the course of their duties to the corporation.").

⁴⁰ See *B & A Log Homes Ltd. v. Evans*, [1986] N.B.J. No. 535 (Q.B.) (Q.L). Shareholders will obviously also be liable if they assume *principal* status in relation to a particular matter. See *Briess v. Woolley*, [1954] A.C. 333.

V. *Statutory Liabilities of Directors*

The discussion to this point has glossed over the statutory regulation of directors. Directors were subjected to statutory liabilities of various kinds from an early date.⁴¹ These liabilities represent a distinct level or dimension of regulation that is appended or superadded to the common law of agency. This direct regulation has been thought necessary because directors, although agents, are often free of immediate supervision or sanction. Their principals are legal fictions lacking the power to monitor or discipline. Alternative forms of supervision by shareholders or markets have not been thought to offer a sufficient discipline. Hence, the selective statutory ascription of personal liability has been employed to counter the negative incentive effects of the default agency immunity.

The historical trend in this area has been a more or less continuous increase in the range and scope of statutory liability for directors (and officers).⁴² This has been the long term social reaction to the nineteenth century adoption of general shareholder limited liability. It is, in essence, the reinstatement in this context of the universal social norm of risk regulation — that risk-taking should be disciplined by responsibility for its adverse consequences.⁴³ Consider how this has come about. Shareholders (partners) in unincorporated joint stock companies possessed the *de jure* powers of principals and were therefore subject to the standard open liability of principals. In many joint stock companies, however, shareholders were passive (whether by design or circumstance) and the directors effectively controlled the conduct of the business. This prompted the demand for limited liability for shareholders. When that privilege was extended to shareholders, passive investment became protected, and little incentive remained to monitor or discipline the directors. The result was that neither shareholders nor directors (who, as agents, had no contractual liability) were subject to the risk regulation norm. No natural person, in other words, was accountable. Instead, the burden of responsibility was shifted to the corporate

⁴¹ The 1844 *Joint Stock Companies Act*, *supra* note 5, for example, imposed penalties on directors for failing to file returns or permit inspection of the deed of settlement or shareholder lists. The 1855 *Limited Liability Act*, *supra* note 1, imposed fines for not complying with publicity requirements, and open liability for making shareholder loans or declaring dividends when the company was insolvent.

⁴² For an argument that the trend is, or may be, unprincipled, see R. Daniels, "Must Boards Go Overboard? An Economic Analysis of the Effects of Burgeoning Statutory Liability on the Role of Directors in Corporate Governance" (1994-95) 24 Can. Bus. L.J. 229. Cf. R. Howse, "Comments on 'Must Boards Go Overboard'" (1995-96) 26 Can. Bus. L.J. 221.

⁴³ The risk regulation policy informs much of the law, including liability assignments in the non-profit sector. For applications of the risk regulation norm, see R. Flannigan, "Contractual Responsibility in Non-profit Associations" (1998) 18 O.J.L.S. 631; "The Liability Structure of Nonprofit Associations: Tort and Fiduciary Liability Assignments" (1998) 77 Can. Bar Rev. 73 and "The Limits of Status Assertion" (1999) 21 Ad. Q. 397.

fiction.⁴⁴ We [society] experienced the adverse effects of this shift, and moved in specific areas to reassert responsibility for those real persons who controlled or were able to control the undertaking. One early reaction of Parliament was to provide that the memorandum of association could expressly arrange for the contractual liability of directors to be unlimited (i.e. reversing their agency immunity).⁴⁵ In most cases, however, the statutory response was to impose personal liability or fines. An example is the 1890 *Directors Liability Act* which imposed personal liability on directors for untrue statements in a prospectus.⁴⁶ Numerous other statutory provisions have since replaced the agency immunity of directors (and officers) with personal accountability.⁴⁷ The historical process has thus been to redirect legal responsibility to directors (and officers) to contain the *de facto* power left with them as a consequence of delegated management, passive investment and the grant of limited liability. Essentially, after reversing the default rule of *shareholder* liability, we are now well along the path of offsetting that development by reversing the default rule of *director* agency immunity. We are now insisting that the real controlling actors feel, and be disciplined by, the consequences of their risk taking. That is the universal social expectation.

VI. Judicial Recognition of Personal Tort Liability

The nineteenth century jurisprudence confirmed that directors of registration corporations had open personal liability for their tortious actions.⁴⁸ There was no talk, during this time, of a statutory immunity for directors. Their liability

⁴⁴ The corporate entity itself was subject to open liability and, in that sense, the risk regulation policy was given a formal application.

⁴⁵ *Companies Act (1862) Amendment Act*, 30 & 31 Vict. c.131, s.4. The 1867 amendments were intended to address the concern that the statute did not sufficiently protect the rights of creditors. See the remarks of Mr. Cave in Hansard, 1867, Vol. 189, at col. 929. The editors of one journal noted that opt-in liability would be of little interest to company promoters. See Note (Joint-Stock Legislation) (1867) 11 Sol. J. 1032 at 1033: "The principle of making the managers of companies as far as possible the chief sufferers by their own misconduct or mismanagement, is obviously a good one; the only difficulty lies in its application. The framers of the bill would seem to have feared that by making the unlimited liability of directors compulsory they would be deterring useful men from serving in that capacity. The Act makes it *optional* for *new* companies to be formed on this principle. The event may prove us to be wrong, but it seems likely that the promoters of new companies will but seldom choose to visit themselves with so grave a liability. It is difficult to believe in the optional introduction of the *Société en Commandite* principle." See sec. 306(1) of the *Companies Act 1985*, 33 & 34 Eliz. c. 6.

⁴⁶ 53 & 54 Vict., c. 64.

⁴⁷ Others have summarized the range of statutory liabilities imposed on directors and officers. See, for example, M.P. Richardson (ed. for McCarthy Tetrault), *Directors' and Officers' Duties and Liabilities in Canada* (Toronto: Butterworths, 1997).

⁴⁸ Many of the English cases were actions under the "misfeasance" provision of the corporate legislation. See *Re County Marine Insurance Company* (1870), L.R. 6 Ch. App. 104. The provision simply provided "a summary mode of enforcing rights which must

was that of agents. They were personally liable for their own torts, and this liability was not displaced or excused by the coincident vicarious liability of their principals.⁴⁹ There were, however, a number of developments in both the nineteenth and twentieth centuries that suggested special treatment for directors in certain respects. We will consider whether those developments were grounded in a coherent analysis. It is convenient to begin the analysis in this section with a review of the cases dealing with the duty of care directors owe (1) to their corporations and (2) to third parties. We will then examine the cases on intentional torts [for our purposes, all torts other than negligence] and, lastly, briefly mention the judicial attribution of individual intentions to corporations.

A. Negligence

(1) *Duty of Care Owed to the Corporation*

The existence of the duty of care owed by directors to their corporations has never been seriously disputed. The main issue in the cases has been the nature of the default *standard* of care that directors owe to their corporate principals.⁵⁰ The general rule is that all actors, including agents, must exercise the care of a reasonable person. That standard, at least formally, was not applied to directors. The argument, evident in the earliest cases, was that corporations must necessarily be satisfied with a reduced level of care from directors. The claim was invariably premised on the desirability of allowing directors full freedom to exercise their business judgment. The initial concession on the part of judges to this business judgment proposition was to require “*crassa negligentia*” or “gross negligence” in order to find a director personally liable. That judicial approach can be seen in *The Charitable Corporation v. Sutton*, a case involving the directors of a chartered corporation.⁵¹ The action included a

otherwise have been enforced by the ordinary procedure of the Courts.” *Re Canadian Land Reclaiming and Colonizing Company* (1880), 14 Ch. D. 660 at 670. Much later, in *Re B. Johnson & Co. (Builders) Ltd.*, [1955] 1 Ch. 634, the Court of Appeal concluded that common law negligence was not within the section. See, however, F. Oditah, “Misfeasance Proceedings Against Company Directors” [1992] L.M.C.L.Q. 207. See also *Cohen v. Selby*, [2001] 1 B.C.L.C. 176 (C.A.). For Canadian “misfeasance” cases, see *Re Traders Trust and Kory* (1915), 26 D.L.R. 41 (B.C.S.C.); *Re Dominion Trust Co.* (1916), 32 D.L.R. 63 (B.C.C.A.); *Re Owen Sound Lumber Co.* (1917), 33 D.L.R. 487 (Ont. C.A.); *Northern Trust Co. v. Butchart* (1917), 35 D.L.R. 169 (Man. K.B.).

⁴⁹ *Michael v. Alestree* (1676), 2 Lev. 172, 83 E.R. 504; *Perkins v. Smith* (1752), 1 Wils. (K.B.) 328, 95 E.R. 644; *Stephens v. Elwall* (1815), 4 M. & S. 259, 105 E.R. 830; *Weir v. Bell* (1878), 3 Ex. D. 238 (C.A.).

⁵⁰ Some courts and commentators have drawn distinctions between skill, care and diligence. Such distinctions tend to confuse the general assessment of reasonable care. The English Law Commission rejected these distinctions. See *Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties* (Law Commission Consultation Paper No. 153; Scottish Law Commission Consultation Paper No. 105) (1998) at 15.23-15.24.

⁵¹ (1742), 2 Atk. 400, 26 E.R. 642.

claim for negligence, albeit framed as a claim for breach of trust. As in a number of other cases, the argument was that the alleged negligence was such as to amount to a breach of trust in itself or a collateral liability for the breaches of trust committed by other corporate actors.⁵² In *Sutton*, the Lord Chancellor warned against finding liability simply because “bad consequences” resulted from authorized acts. In his view, it was “by no means just in a judge, after bad consequences have arisen from such executions of their [the directors] power, to say that they foresaw at the time what must necessarily happen; and therefore were guilty of a breach of trust”.⁵³ These remarks have been taken to amount to a business judgment justification for the gross negligence standard. The words, however, appear to convey no more than that it is necessary in each case to show that bad consequences were the foreseeable result of the negligent actions.

The other significant feature of the *Sutton* case is the actual standard of care applied by the court. While Lord Hardwicke identified the claim as one for “*crassa negligentia*”, he went on to define the obligation as a duty to act with “reasonable diligence”.⁵⁴ That, on the face of it, appears to be the ordinary standard of care for liability in negligence. As we will see, other judges have similarly defined gross negligence in terms that reflect the ordinary standard, and this conceptual difficulty with differentiating the gross negligence standard has drawn judicial comment on several occasions. Before turning to those cases, however, it is convenient here to offer a few observations about this business judgment justification for the gross negligence standard.

The ostensible connection between the exercise of business judgment and the exercise of due care is not clear in the cases. Consider *Turquand v. Marshall*, a partnership case⁵⁵ that appears to have had a measure of early influence on the question.⁵⁶ With reference to a loan made to one of the directors of the partnership, Lord Hatherley stated:

[H]owever foolish the loan might have been, so long as it was within the powers of the directors, the Court could not interfere and make them liable. They were intrusted with full powers of lending the money, and it was part of the business of the concern to trust people with money, and their trusting to an undue extent was not a matter with which they could be fixed, unless there was something more alleged, as, for instance,

⁵² See *Re Oxford Benefit Building and Investment Society*, (1887), 35 Ch.D. 502. Historically, fiduciary responsibility encompassed both the duty of loyalty and the duty of care. While this is still the case in some jurisdictions, the modern approach is to limit fiduciary accountability to the duty of loyalty, leaving the duty of care to be regulated by general negligence principles.

⁵³ *Supra* note 51 at 644 (E.R.).

⁵⁴ *Ibid.* at 645 (E.R.).

⁵⁵ The analysis is not affected by reason of the fact that the case involved a partnership rather than a corporation. To the extent the business judgment proposition constitutes a valid consideration, it would apply to all commercial actors.

⁵⁶ (1869), L.R. 4 Ch. App. 376.

that it was done fraudulently and improperly and not merely by a default of judgment. Whatever may have been the amount lent to anybody, however ridiculous and absurd their conduct might seem, it was the misfortune of the company that they chose such unwise directors; but as long as they kept within the powers of their deed, the Court could not interfere with the discretion exercised by them.⁵⁷

Although this quote only explicitly (and properly) rejects personal liability for errors of judgment, the words could perhaps be construed as a general denial of liability for negligence premised on a supposed need to accommodate directorial discretion. Lord Hatherley himself subsequently thought his remarks had been misunderstood and he felt compelled to clarify them a few years later in *Overend, Gurney, & Co. v. Gibb*:

It is perhaps hardly necessary to say it, after the explanation I have already given, but I should like to say one word as regards the case of *Turquand* and *Marshall*, which was cited by Sir *Roundell Palmer* yesterday, and referred to by Mr. *Cotton* this morning. I certainly never intended to lay down the strong proposition that a person acting for another as his agent, is not bound to use all the ordinary prudence that can be properly and legitimately expected from any person in the conduct of the affairs of the world, namely, the same amount of prudence which, in the same circumstances, he would exercise on his own behalf. What I did intend to state in that case was, that I could not measure—and I think it would be a very fatal error in the verdict of any Court of justice to attempt to measure—the amount of prudence that ought to be exercised by the amount of prudence which the judge himself might think, under similar circumstances, he should have exercised. I think it extremely likely that many a judge, or many a person versed by long experience in the affairs of mankind, as conducted in the mercantile world, will know that there is a great deal more trust, a great deal more speculation, and a great deal more readiness to confide in the probabilities of things, with regard to success in mercantile transactions, than there is on the part of those whose habits of life are entirely of a different character. It would be extremely wrong to import into the consideration of the case of a person acting as a mercantile agent in the purchase of a business concern, those principles of extreme caution which might dictate the course of one who is not at all inclined to invest his property in any ventures of sua hazardous character.⁵⁸

These additional comments make it clear that the business judgment argument has a limited scope. Directors are required to exercise “ordinary prudence.” We recognize, at the same time, that there is a difference in kind between losses resulting from negligent acts and those arising from taking a risk that ultimately proves unsuccessful. An error of judgment, without more, is not negligence. On the other hand, if an exercise of judgment leads to losses because it was based on negligent preparations or on a failure to prepare, that prior negligence would attract personal liability to the responsible directors. In such a case, the culpability is located in the *preparation* for the exercise of judgment.

⁵⁷ *Ibid.* at 386.

⁵⁸ (1872), L.R. 5 H.L. 480 at 494-95.

There are numerous invocations of the business judgment proposition in the jurisprudence.⁵⁹ Invariably the reference is laconic, with little development of any ostensible analytical connection between exercising business judgment and deploying a lesser degree of care. This suggests that there is no genuine connection between the business judgment argument and a particular *level* of care. In fact, the business judgment argument has no necessary implication for what is or should be the appropriate level of care. The business judgment argument is that a given decision was proper because it involved nothing more than an exercise of judgment. The negligence argument, in contrast, is that due to a lack of care, there was a negligent exercise of judgment. The two arguments are exclusive. One or the other will prevail. It is an entirely distinct argument to assert that a decision was negligently made, but should nevertheless be excused because it was not *grossly* negligent. That is an argument that must find its justification, if at all, in some policy consideration other than the difference between taking a risk and exercising care. That policy must affirmatively justify holding directors to an expectation of care that is less than the ordinary standard of care.

A further observation is that the business judgment proposition does not provide a general justification for the higher threshold of gross negligence. Not all cases of director negligence involve a question of business judgment. There is therefore no business judgment rationale for applying the gross negligence standard in those cases. Other rationales could perhaps be suggested for these cases, but presumably those rationales would have only a narrow application. It might be suggested, for example, that shareholders can not complain of the negligence of directors who are appointed primarily for the association of their names with the corporation. That rationale is only a justification in relation to victims who had the right or power to participate in the selection of the directors. The same objection applies to the notion that shareholders should bear the loss because it was their unwise selection of incompetent directors that produced the loss. In the result, once the need for further justification is recognized, the business judgment proposition assumes only the relevance dictated by its partial

⁵⁹ Some commentators assume that there is no formal business judgment rule in the Commonwealth. The [admittedly terse] judicial statements, along with the conclusions in the cases, however, now clearly establish the existence of the business judgment principle. See *Harman v. Tappenden* (1801), 1 East. 555; 102 E.R. 214; *Re Forest of Dean Coal Mining Company* (1878), 10 Ch.D. 450; *Re Faure Electric Accumulator Company* (1888), 40 Ch. D. 141; *Re Brazilian Rubber Plantations and Estates Limited*, [1911] 1 Ch. 425; *Re Owen Sound Lumber Co.* (1917), 33 D.L.R. 487 (Ont. C.A.); *Shuttleworth v. Cox Brothers and Company (Maidenhead), Limited*, [1927] 2 K.B. 9 (C.A.); *Howard Smith Ltd. v. Ampol Petroleum*, [1974] A.C. 821 (P.C.); *Brant Investments Ltd. v. KeepRite Inc.* (1991), 80 D.L.R. (4th) 161 (Ont. C.A.); *Saratoga Utilities Ltd. v. Long*, [1998] B.C.J. No. 772 (B.C.S.C.) (Q.L). See also *Collier v. Electrum Acceptance Pty Ltd.* (1986), 69 A.L.R. 355 (F.C. Aust.). It will be appreciated that elevation of the business judgment proposition to an operative legal principle is the preferred approach because it precisely targets the concern or mischief. Acceptance of the business judgment rule should have been accompanied by the contemporaneous rejection of the gross negligence standard.

scope. The proposition ultimately seems to amount to no more than that an exercise of judgment, without more, is not a negligent act. That is not in any sense a controversial proposition.

Returning to the question of the level of care, it is worth mentioning a number of coincidental matters that were resolved by the courts. The first was an acceptance of the notion that directors could be excused if they had fairly relied on others. In *Land Credit Company of Ireland v. Lord Fermoy*, directors approved payments that had been made by the executive committee to manipulate share prices.⁶⁰ The claim by the official liquidator (ie. the insolvent corporation) was essentially one of negligence, although again framed as a breach of trust.⁶¹ The defence of the directors was that they did not know the purpose of the payments made by the executive committee. Lord Romilly regarded this defence as equivalent to an admission of liability: "A plea of ignorance by a director, or that anything was done by him for the sake of conformity, is merely a plea of guilty, and it is an admission of liability to account for the sums misapplied".⁶² One of the directors appealed the decision on the ground that he, unlike the others, had not participated in all the meetings and had no real knowledge of the transactions. The Court of Appeal agreed that he should not be held liable.⁶³ The executive committee had apparently concealed the nature of its actions from him. The court concluded that "a director can not be held accountable for being defrauded".⁶⁴ This was one of several cases that established that directors will not face liability if they have no reason to be suspicious of those on whom they rely, even given (in some early cases) their own apparent indolence or neglect of duties.⁶⁵

A second significant point was made by Lord Hatherley in *Overend, Gurney, & Co. v. Gibb*.⁶⁶ He confirmed that directors were not excused from liability simply because their actions were within their authority. In the *Overend* case, the directors had acted within their powers when they purchased a business. Nevertheless, according to Lord Hatherley, it "still remains to be seen whether or not there was *crassa negligentia* in so exercising their power".⁶⁷

⁶⁰ (1869), L.R. 8 Eq. 7.

⁶¹ Most of these early cases were actions by liquidators attempting to realize funds for creditors by enforcing the insolvent corporation's right to recover from negligent directors.

⁶² *Supra* note 60 at 12.

⁶³ (1870), L.R. 5 Ch. App. 763.

⁶⁴ *Ibid.* at 772.

⁶⁵ See *Re Denham & Co.* (1883), 25 Ch.D. 752; *Re Cardiff Savings Bank*, [1892] 2 Ch. 100; *Dovey v. Cory*, [1901] A.C. 477; *Prefontaine v. Grenier*, [1907] A.C. 101; *Huckerby v. Elliott*, [1970] 1 All E.R. 189 (Q.B.); *Blair v. Consolidated Enfield Corp.* (1995), 128 D.L.R. (4th) 73 (S.C.C.). The reliance excuse may, of course, fail. See *Drincqbierv. Wood*, [1899] 1 Ch. 393; *Re Standard Trustco Ltd.* (1992), 6 B.L.R. (2d) 241 (Ont. Sec. Comm.). Note also that in some cases it will be negligent for directors to not seek advice. See *Re Duomatic Ltd.*, [1969] 2 Ch. 365.

⁶⁶ (1872), L.R. 5 H.L. 480. See also *McCullagh v. Lane Fox and Partners Ltd.*, [1995] E.W.J. No. 582 (C.A.) (Q.L.).

⁶⁷ *Ibid.* at 488.

These matters aside, the main issue in the cases was the level of care that could be expected of directors. As noted above, it was common for courts to identify that standard as gross negligence, but at the same time to define that standard in terms that looked very much like ordinary negligence. Lord Hatherley's judgment in *Overend* is an example.⁶⁸ Though he identified the threshold for liability as *crassa negligentia*, he insisted that directors must exhibit "all the ordinary prudence that can be properly and legitimately expected from any person in the conduct of the affairs of the world, namely, the same amount of prudence which, in the same circumstances, he would exercise on his own behalf".⁶⁹ Similarly, in *Liquidators of Western Bank v. Baird's Trustees*, a Scottish case dealing with a joint stock company (partnership), the court accepted the gross negligence standard, but then stated that the duties of directors must be discharged "with ordinary and reasonable care".⁷⁰ The court further observed that "gross negligence in the performance of such a duty, the want of reasonable and ordinary fidelity and care, will infer liability for loss thereby occasioned".⁷¹

A measure of clarity on the matter is found in *Marzetti's Case*.⁷² At trial, Jessel, M.R., concluded that there was "nothing against [the director] to show that there was more than negligence or carelessness on his part, but still he is liable".⁷³ In the Court of Appeal, James, L.J. stated that "directors are not to be made liable on those strict rules which have been applied to trustees . . . [but] they must show something like reasonable diligence".⁷⁴ Brett, L.J. directly responded to the argument that gross negligence was required:

Now it was urged that the payment of the cheque was not such negligence as to make Mr. Marzetti liable, and that there must be gross or crass negligence. I know of no such legal difference between the sorts of negligence which makes a person liable. The question is whether Mr. Marzetti has been guilty of such negligence as would make him liable in an action. Mere imprudence is not such negligence. Want of judgment is not. It must be such negligence as would make a man liable in point of law. Mr. Marzetti has been guilty of not making those inquiries which a person of ordinary care in his position would have made.⁷⁵

⁶⁸ *Ibid.*

⁶⁹ *Ibid.* at 494.

⁷⁰ (1872), 10 Scot. L.R. 116 at 123.

⁷¹ *Ibid.*

⁷² *Re Railway and General Light Improvement Company (Marzetti's Case)* (1880), 28 W.R. 541.

⁷³ *Ibid.* at 542.

⁷⁴ *Ibid.*

⁷⁵ *Ibid.* at 543. Other courts had previously questioned the existence or utility of the gross/ordinary negligence dichotomy. See *Hinton v. Dibbin* (1842), 2 Q.B. 646, 114 E.R. 253; *Wilson v. Brett* (1843), 11 M.&W. 113, 152 E.R. 737; *Grill v. General Iron Screw Collier Company* (1866), L.R. 1 C.P. 600; *Beal v. The South Devon Railway* (1864), 3 H. & C. 337, 159 E.R. 560; *Giblin v. McMullen* (1868), L.R. 2 P.C. 317.

While making allowance for the unsuccessful exercise of business judgment, this decision plainly subjected directors to the ordinary standard of care.

Other subsequent cases adopted a comparable analysis.⁷⁶ In *Leeds Estate, Building and Investment Company v. Shepherd*, the directors were found to have acted negligently when they failed to inquire into or verify in any way the accounts put before them by their manager.⁷⁷ According to Stirling, J., the directors "fail to excuse themselves if they have not taken reasonable care to secure the preparation of estimates and statements of account such as it was their duty to prepare and submit to the shareholders, and have declared the dividends complained of without having exercised thereon their judgment as mercantile men on the estimates and statements of account submitted to them".⁷⁸ In *Re New Mashonaland Exploration Company*, the gross negligence standard was again explicitly rejected. Vaughan Williams, J. stated, during argument, that "*crassa negligentia* is a term to be got rid of".⁷⁹

This line of authority was interrupted by *Lagunas Nitrate Company v. Lagunas Syndicate* where, first Romer, J., and then the Court of Appeal, reasserted (without elaboration or justification) the higher threshold.⁸⁰ At trial, Romer, J. frankly conceded the special treatment this involved: "Now, undoubtedly, directors have always been held by the Courts as being in a very favourable position as compared with other agents in respect of the degree of negligence which will make them liable to an action".⁸¹ In the Court of Appeal, Lindley, M.R. stated that:

The amount of care to be taken is difficult to define; but it is plain that directors are not liable for all the mistakes they may make, although if they had taken more care they might have avoided them: see *Overend, Gurney & Co. v. Gibb*. Their negligence must be not the omission to take all possible care; it must be much more blameable than that: it must be in a business sense culpable or gross. I do not know how better to describe it.⁸²

The initial reaction to this aspect of the *Lagunas* decision was to ignore or overlook it. Several courts, including the House of Lords, continued to use terminology that suggested the proper standard was ordinary negligence.⁸³

It was several years before the gross negligence standard surfaced again in *Re Brazilian Rubber Plantations and Estates Limited*.⁸⁴ Neville, J. recognized

⁷⁶ Cf. *Re Denham & Co.* (1883), 25 Ch.D. 752; (Chitty J. does not cite the *Marzetti* case).

⁷⁷ (1887), 36 Ch.D. 787.

⁷⁸ *Ibid.* at 801.

⁷⁹ [1892] 3 Ch. 577 at 583.

⁸⁰ [1899] 2 Ch. 392.

⁸¹ *Ibid.* at 418.

⁸² *Ibid.* at 435.

⁸³ *Dovey v. Cory*, [1901] A.C. 477; *Merchants' Fire Office, Limited v. Armstrong*, [1901] W.N. 163; *Prefontaine v. Grenier*, [1907] A.C. 101 (P.C.).

⁸⁴ [1911] 1 Ch. 425.

the definition problem with "gross negligence", but he too reverted to the language of ordinary negligence:

I have to consider what is the extent of the duty and obligation of directors towards their company. It has been laid down that so long as they act honestly they cannot be made responsible in damages unless guilty of gross negligence. There is admittedly a want of precision in this statement of a director's liability. In truth, one cannot say whether a man has been guilty of negligence, gross or otherwise, unless one can determine what is the extent of the duty which he is alleged to have neglected. A director's duty has been laid down as requiring him to act with such care as is reasonably to be expected from him, having regard to his knowledge and experience. He is, I think, not bound to bring any special qualifications to his office. He may undertake the management of a rubber company in complete ignorance of everything connected with rubber, without incurring responsibility for the mistakes which may result from such ignorance; while if he is acquainted with the rubber business he must give the company the advantage of his knowledge when transacting the company's business. He is not, I think, bound to take any definite part in the conduct of the company's business, but so far as he does undertake it he must use reasonable care in its despatch.

Such reasonable care must, I think, be measured by the care an ordinary man might be expected to take in the same circumstances on his own behalf. He is clearly, I think, not responsible for damages occasioned by errors of judgment. . . .

In this case, therefore, I must consider whether the directors acted without reasonable prudence in adopting the contract on the information which they possessed.⁸⁵

No analytical relationship or connection was shown in this case between an objective definition of gross negligence and a subjective evaluation of personal competency. Rather, Neville, J. simply asserted that the level of care that can be expected of a particular director is proportionate to the relative ability of that director. Nothing clarifies how that variable level of care relates to a threshold of gross negligence. Apart from that, and for many observers, this analysis represents the low point in the common law for director responsibility. Although supported to some extent by a few earlier cases,⁸⁶ it was clearly inconsistent with the tenor and direction of the immediately preceding jurisprudence. Nevertheless, the case became an authority for the view that directors could only be liable if they chose to perform their duties (as opposed to being liable for neglecting their duties); and that where they did perform their duties, their [incompetent] actions were measured against their own personal knowledge and ability.

It appears to be the subsequent judgment of Romer, J. in *Re City Equitable Fire Insurance Company, Limited* that ultimately firmly reinstated "gross

⁸⁵ *Ibid.* at 436-37.

⁸⁶ *Re Montrotier Asphalte Company (Perry's Case)* (1876), 34 L.T. 716; *Re Denham & Co.* (1883), 25 Ch.D. 752; *Re Cardiff Savings Bank*, [1892] 2 Ch. 100; See also *Re Dominion Trust Co.* (1916), 32 D.L.R. 63 (B.C.C.A.).

negligence" as the formal level of care required of directors.⁸⁷ Even a full quarter century after his judgment in *Lagunas*, however, Justice Romer's analysis remained tentative and guarded:

To the question of what is the particular degree of skill and diligence required of him, the authorities do not, I think, give any very clear answer. It has been laid down that so long as a director acts honestly he cannot be made responsible in damages unless guilty of gross or culpable negligence in a business sense. But as pointed out by Neville J. in *In re Brazilian Rubber Plantations and Estates, Ltd.*, one cannot say whether a man has been guilty of negligence, gross or otherwise, unless one can determine what is the extent of the duty which he is alleged to have neglected. For myself, I confess to feeling some difficulty in understanding the difference between negligence and gross negligence, except in so far as the expressions are used for the purpose of drawing a distinction between the duty that is owed in one case and the duty that is owed in another. If two men owe the same duty to a third person, and neglect to perform that duty, they are both guilty of negligence, and it is not altogether easy to understand how one can be guilty of gross negligence and the other of negligence only. But if it be said that of two men one is only liable to a third person for gross negligence, and the other is liable for mere negligence, this, I think, means no more than that the duties of the two men are different. The one owes a duty to take a greater degree of care than does the other: see the observations of Willes J. in *Grill v. General Iron Screw Collier Co.* If, therefore, a director is only liable for gross or culpable negligence, this means that he does not owe a duty to his company, to take all possible care. It is some degree of care less than that. The care that he is bound to take has been described by Neville J. in the case referred to above as "reasonable care" to be measured by the care an ordinary man might be expected to take in the circumstances on his own behalf.⁸⁸

These remarks do not advance very far, if at all, our general understanding of the difference between gross and ordinary negligence, and certainly do not disclose any *justification* for a lower level of care. It should be borne in mind, in this regard, that it was only necessary for Justice Romer to identify the minimum *possible* standard. If the directors could not meet even that threshold (and they did not), there was no need to precisely establish what was or should be the current standard. It may be added that Justice Romer did not thoroughly review the jurisprudence and did not, in particular, consider the significance of the *Marzetti* case. In any event, this judgment, and that of Neville, J., became generally accepted for their description of the standard of care imposed on directors. This was an accomplishment of some magnitude for these two trial judges, given that they essentially reversed the direction of the developing jurisprudence. It would be some time before their views were seriously reconsidered.

⁸⁷ [1925] 1 Ch. 407. The decision was appealed, but only as to the liability of the auditors of the company. Although it did not examine the jurisprudence, the Court of Appeal expressed its general (even enthusiastic) approval for Romer J's judgment.

⁸⁸ *Ibid.* at 427-28.

(2) Duty of Care Owed to Third Parties

The discussion to this point has focussed on the duty of care that directors owe to their corporate principals. Before leaving this initial discussion of negligence, however, it is necessary to examine the duty of care directors owe to third parties. Here the issue has been the *existence* of the duty, not the *standard* of care associated with that duty. With respect to the *standard* of care, once courts find that a duty is owed by a director to a third party, they appear to apply the general negligence standard of the reasonable person. That is clearly the correct approach, as the status of directors (as directors) is irrelevant to the question of whether they *personally* owe a duty of care to a third party. It is the same at the level of the corporation. Once a corporation is found to personally owe a duty of care to a third party, the applicable standard of care is that of the reasonable person. It is only as between the corporation and its directors that the lower standard has been applied. We now consider when a director will owe a duty of care to a third party.

While the duty of care owed to the corporation is in a sense a status obligation (i.e. associated with the office of "director"), the duty owed by directors to third parties is not. The obligation to third parties arises under the general law when certain criteria are satisfied. As a conventional agency or tort law matter, the modern default rule is that agents are personally liable for negligent acts that cause injury to their "neighbours." That, however, was not the approach taken in 1880 in the English case of *Wilson v. Lord Bury*, where a creditor sued for capital lost through the negligence of the directors.⁸⁹ According to Bramwell, L.J.:

Treating the case as one of contract, the contract was between the plaintiff and the company, and not the directors. Treated as a case of tort, no wrong in the defendants independent of duty is shewn, and no breach of any duty to the plaintiff is shewn in the defendants for the same reason that no contract is shewn to have existed between them. The case is not mended by the statement of claim saying that the negligence was "gross". That will not give a cause of action, unless negligence not gross will, and that will not, unless mere nonfeasance will, and that will not in this case unless it is a breach of contract in the defendants, and that it is not, for there is none with the plaintiff.⁹⁰

Although not entirely clear, this analysis seems to be premised on the assumption that a duty of care could only exist if there were a contractual relationship between the directors (in their personal capacity) and the creditor.⁹¹ There is no reference to the possibility that liability could be independently imposed on the directors through the application of the general tort law duty to take care.⁹²

⁸⁹ (1880), 5 Q.B.D. 518.

⁹⁰ *Ibid.* at 536.

⁹¹ Cf. *Boorman v. Brown* (1842), 3 Q.B. 511; 114 E.R. 603.

⁹² See *Marc Rich & Co. A.G. v. Bishop Rock Marine Co. Ltd.*, [1995] 3 All E.R. 307 at 315 (per Lord Lloyd) (H.L.) ("But I am unable to see why the existence of the contract of carriage should 'mitigate against' a duty of care being owed by a third party in tort. The

Given the relatively undeveloped state of the law of negligence at the time, this is perhaps of no great surprise.

The approach adopted in *Wilson v. Lord Bury* was not in fact the approach employed through the greater part of the twentieth century. Instead, the "neighbour" principle was applied to negligence claims made by third parties. That approach is prefigured in the 1919 decision of the Supreme Court of Canada in *Lewis v. Boutilier*.⁹³ The Supreme Court concluded on the facts that the defendant, the president of the company, had personally put a young employee to work in a dangerous place, thereby negligently causing his death. Anglin J. observed that "the principle of the law of contract embodied in the phrase '*respondeat superior*' does not avail in the law of tort to excuse a wrongdoer whose act has occasioned or contributed to the injury of another".⁹⁴ Accordingly, the president was held personally liable for his conduct. In essence, the court employed the "neighbour" analysis of the modern general law of negligence. There was no suggestion that the absence of a contractual relationship between the president and the employee was of any significance.

It should be apparent that *Wilson v. Lord Bury* and *Lewis v. Boutilier* represent two distinct approaches to the negligence liability of directors to third parties. The functional difference is whether the court is prepared to recognize the default application of general negligence liability. As noted above, judges in subsequent cases were not inclined to follow the restrictive *Wilson* approach. In *Yuille v. B. & B. Fisheries (Leigh), Ltd.*, although neither of the two earlier cases were cited, the court considered both approaches.⁹⁵ The defendant director had argued that he owed no duty of care personally to the plaintiff, his only duty being to the corporation. Lord Justice Willmer rejected this as a general proposition. He offered the hypothetical example of a director who overloaded a ship. He thought the director in such a case would be personally liable for "an act which he could reasonably foresee would be likely to cause injury to other persons who were in law his 'neighbours,' to use the expression used by Lord Atkin in the course of his speech in *Donoghue v. Stevenson*".⁹⁶ Lord Justice Willmer concluded that a plaintiff could hold a defendant liable "if he can establish that he is within the appropriate relationship where duty is owed".⁹⁷ Accordingly, like *Lewis v. Boutilier*, this case accepted the default application of the general law of negligence.

function of the law of tort is not limited to filling in gaps left by the law of contract, as this House has recently reaffirmed in *Henderson v. Merrett Syndicates Ltd.* ... per Lord Goff of Chieveley. The House rejected an approach which treated the law of tort as supplementary to the law of contract, i.e. as providing for a tortious remedy only where there is no contract. On the contrary: the law of tort is the general law, out of which the parties may, if they can, contract.")

⁹³ (1919), 52 D.L.R. 383 (S.C.C.). See also *Thérien v. Brodie* (1893), 4 Que. S.C. 23.

⁹⁴ *Ibid.* at 389.

⁹⁵ [1958] 2 Lloyd's Rep. 596 (Adm. Ct.).

⁹⁶ *Ibid.* at 619.

⁹⁷ *Ibid.*

The same general approach was subsequently employed in cases across the Commonwealth.⁹⁸ In *Berger v. Willowdale A. M. C.*, the Ontario Court of Appeal concluded that the plaintiff was a "neighbour" whom the president of the company "ought reasonably to have had in contemplation".⁹⁹ In the Australian case of *Morton v. Douglas Homes Ltd.*, Hardie Boys J. stated that the "principle of limited liability protects shareholders and not directors, and a director is as responsible for his own torts as any other servant or agent".¹⁰⁰ He went on to explain that: "whilst a director may be liable in negligence to a person with whom the company is dealing, it will only be where he personally, as distinct from the company, owed a duty of care, and failed to observe it. His liability then arises not by reason of his office of director but by reason of a relationship of proximity or neighbourhood existing between him and the plaintiff".¹⁰¹ Thus, at this point in time, the case law appeared to have settled on the conventional "neighbour" analysis. We turn now to consider the personal liability of directors for intentional torts. That investigation is necessary at this juncture in order to later permit a fuller comprehension of the more recent developments in both the negligence and intentional tort contexts.

B. *Intentional Torts*

Where directors personally commit tortious acts, either on their own or jointly with others, the response of the courts has been consistent. In such cases, directors are personally liable.¹⁰² Most of the cases involve claims by third parties, but the claim may also be made by the corporation.¹⁰³ The position was confirmed by Slade L.J. in *C. Evans & Sons Ltd. v. Spritebrand Ltd.*:

Counsel, as I understood his argument on behalf of the appellant, did not attempt to submit that a director of a company will escape personal liability to third parties for torts which he has personally committed by his own hand (or mouth) merely because

⁹⁸ *Fairline Shipping Corporation v. Adamson*, [1975] 1 Q.B. 180; *Berg v. Willowdale A.M.C.* (1983), 145 D.L.R. (3d) 247 (Ont. C.A.), leave to appeal *refd.*, (1983), 145 D.L.R. (3d) 247n (S.C.C.); *Morton v. Douglas Homes Ltd.*, [1984] 2 N.Z.L.R. 548 (H.C.); *Centrepac Partnership v. Foreign Currency Consultants Ltd.*, [1989] 4 N.Z.C.L.C. 64, 940 (H.C.).

⁹⁹ *Ibid.* at 254.

¹⁰⁰ [1984] 2 N.Z.L.R. 548 at 593 (H.C.).

¹⁰¹ *Ibid.*

¹⁰² *Eg. Cullen v. Thomson* (1862), 6 L.T. (N.S.) 870; *Edgington v. Fitzmaurice* (1885), 29 Ch. D. 459 (C.A.); *Parker v. McQueen* (1872), 32 U.C.Q.B. 273; *Weir v. Bell* (1878), 3 Ex. D. 238 (C.A.); *Re Traders Trust and Kory* (1915), 26 D.L.R. 41 (B.C.S.C.); *Said v. Butt*, [1920] 3 K.B. 497; *Johnson v. Ideal Music Publishing Co.* (1921), 20 O.W.N. 326 (Ont. Div. Ct.); *Solloway v. McLaughlin*, [1938] A.C. 247; *Reitzman v. Grahame-Chapman and Derustit Ltd.* (1950), 67 R.P.C. 178 (Ch.); *Wah Tat Bank Ltd. v. Chan Cheng Kum*, [1975] A.C. 507 (P.C.); *Sullivan v. Desrosiers* (1986), 76 N.B.R. (2d) 271 (C.A.). See also *Betts v. DeVitre* (1868), L.R. 3 Ch. App. 429 and the comments on this case in *British Thomson-Houston Company, Limited v. Sterling Accessories, Limited*, [1924] 2 Ch. 33.

¹⁰³ *Attorney-General v. Wilson* (1840), Cr. & Ph. 1, 41 E.R. 389.

he committed the tort in the course of carrying out his duties as director of his company. He can escape personal liability for such torts no more than can an employee acting in the course of his employment for a company, or an agent acting in the course of his agency for a company. I think it important to emphasise these points lest it should be thought that the argument in this case has cast doubts on these particular principles of the law of tort.¹⁰⁴

This particular aspect of director liability has not been directly challenged in the cases. There are statements in some subsequent cases, however, that seem on their face to be inconsistent with this generic tort liability.¹⁰⁵ Nevertheless, Slade L.J. has accurately stated the correct position.

The only tort that has raised an issue of principle with respect to director liability is that of inducing a breach of contract (interference with contractual relations).¹⁰⁶ No particular difficulty arises where the claim is that a stranger induced a breach. Where corporate insiders are involved, however, the courts have denied recovery. This difference was articulated in *Said v. Butt*.¹⁰⁷ McCordie J. first pointed to the breadth of the proposition stated in *Lumley v. Gye*: "[A] person who without just cause knowingly procures a man to commit a breach of his contract with another . . . is liable to an action for tort".¹⁰⁸ He then offered his own view of the application of that principle to directors:

I have searched in vain for any decision which indicates that a servant is liable in tort for procuring a breach of his master's contract with another. If such a cause of action existed, I imagine that it would have been successfully asserted ere this. The explanation of the breadth of the language used in the decisions probably lies in the fact that in every one of the sets of circumstances before the Court the person who procured the breach of contract was in fact a stranger, that is a third person, who stood wholly outside the area of the bargain made between the two contracting parties.

But the servant who causes a breach of his master's contract with a third person seems to stand in a wholly different position. He is not a stranger. He is the alter ego of his master. His acts are in law the acts of his employer. In such a case it is the master himself, by his agent, breaking the contract he has made, and in my view an action against the agent under the *Lumley v. Gye* principle must therefore fail, just as it would fail if brought against the master himself for wrongfully procuring a breach of his own contract.

I hold that if a servant acting bona fide within the scope of his authority procures or causes the breach of a contract between his employer and a third person, he does not thereby become liable to an action of tort at the suit of the person whose contract has thereby been broken. I abstain from expressing any opinion as to the law which may apply if a servant, acting as an entire stranger, or wholly outside the range of his powers, procures his master to wrongfully break a contract with a third person.¹⁰⁹

¹⁰⁴ [1985] 2 All E.R. 415 (C.A.) at 419.

¹⁰⁵ Consider the cases in notes 162, 163, 183, *infra*.

¹⁰⁶ The nomenclature is in transition. The traditional terminology is utilized here.

¹⁰⁷ [1920] 3 K.B. 497. See also *D.C. Thomson & Co. Ltd. v. Deakin*, [1952] Ch. 646 (C.A.); *De Jetley Marks v. Greenwood*, [1936] 1 All E.R. 863 (K.B.).

¹⁰⁸ *Ibid.* at 505.

¹⁰⁹ *Ibid.* at 505-506.

It may be thought that these remarks could be criticized on the ground that authorization normally does not relieve an agent of tortious liability.¹¹⁰ McCardie J., however, was right in refusing to hold the director liable. The proper explanation for this result, moreover, does involve a distinction between those who are acting within the scope of their authority and those who are not.

There is simply no tortious act involved when, on behalf of the corporation, authorized directors (i.e. those directors who have the authority to make the *breach decision*) bona fide determine that a particular contractual obligation will not be performed. Where a stranger is involved, the tortious wrongdoing is the interference in the contractual relations of the original parties. Where directors are exercising their authority to terminate the contract, however, there is no interference in that sense. Only the original parties are interacting (because the act of the director is the act of the corporation) and either of those original parties is plainly entitled to refuse performance, subject to the payment of damages. A refusal to perform is a breach of contract – but that is all it is. The act of performing one's authorized duty (to determine whether the corporation will continue to be bound) has no wrongful quality to it other than the breach of contract itself. Those who insist that there is a tort in these circumstances are essentially finding the wrongdoing in the breach of contract. But this can not give rise to a claim in tort unless the mere breach of a contract is a tortious act. If that were the case, then obviously the law of contract would be entirely subsumed by the law of tort. It is clear that a breach of contract may be attended by concurrent tortious liability if the contract is negligently performed or the breach is associated with an intentional tort. It is an unwarranted leap, however, to conclude that the act of deciding to refuse performance is wrongful in a tort sense simply because that act produced the breach of contract. To put it another way, the corporation was not "induced" to breach the contract. It's own internal decision-making mechanisms produced the breach. No external force influence on the part of someone lacking authority was involved. Accordingly, the correct position is that, if directors act *bona fide* in the interests of the corporation and within their authority in refusing performance, there is no tort at all. As it is, the

¹¹⁰ *Perkins v. Smith* (1752), 1 Wils. K.B. 328, 95 E.R. 644; *Sands Qui Tam v. Child* (1693), 3 Lev. 351, 83 E.R. 725; *Cranch v. White* (1835), 1 Bing. (N.C.) 414, 131 E.R. 1176; *Bennett v. Bayes* (1860), 5 H. & N. 391, 157 E.R. 1233. See F. Reynolds, *Bowstead and Reynolds on Agency*, 16th ed. (London: Sweet & Maxwell, 1996) at 635 ("It is in general no defence to an action against a tortfeasor for the tortfeasor to prove that he acted under the authority, instructions or orders of another.").

The difference in the nature of the authority usually given to ordinary agents (and employees) as compared to directors explains why ordinary agents (and employees) will more often be liable for inducing a breach of contract. Directors typically possess the authority (express or implicit) to refuse further performance on a contractual obligation. Ordinary agents normally do not have that kind of authority and therefore will act wrongfully (by interfering) when they seek to "induce" a breach by their corporate principals. Without the requisite authority, their position is equivalent to that of strangers. It is not always well understood in the cases that the requisite authority is the authority to make the "breach" decision.

courts have effectively come to this same conclusion, though they have formally treated the matter as an exception to the rule or as an issue of justification.¹¹¹ It would certainly be preferable, however, for the judges to recognize that there is simply no tort (of inducing breach) where directors act within their authority to cause the corporation to breach its contractual obligation.

The next question is whether directors are personally liable even though they do not themselves perform the intentional tort. The answer is that they are liable if they direct or procure the commission of the act. Directors are not liable merely by reason of their status as directors.¹¹² Nor are they liable merely because they are supervisors or managers of the workers who commit the tort.¹¹³ They are personally liable, however, if they initiate or direct the tortious act. In effect, it is a tort to order or direct the commission of a tort. Although there were earlier cases,¹¹⁴ the leading cases are *Rainham Chemical Works, Limited v. Belvedere Fish Guano Company, Limited*¹¹⁵ and *Performing Right Society, Limited v. Caryl Theatrical Syndicate, Limited*.¹¹⁶ In the *Belvedere* case, Lord Buckmaster stated that directors were personally liable where the tortious acts were "expressly directed by them".¹¹⁷ In *Caryl*, Lord Atkin confirmed that: "Prima facie a managing director is not liable for tortious acts done by servants of the company unless he himself is privy to the acts, that is to say unless he ordered or procured the acts to be done".¹¹⁸ Lord Atkin went on to clarify the views earlier expressed by Lord Buckmaster in *Belvedere* in one respect. According to Lord Atkin, "express" direction was not necessary: "If the

¹¹¹ *ADGA Systems International Ltd. v. Valcom Ltd.* (1999), 168 D.L.R. (4th) 351 (Ont. C.A.); (treated as exception); *McFadden v. 481782 Ontario Ltd.* (1984), 47 O.R. (2d) 134 (Ont. H.C.); *369413 Alberta Ltd. v. Pocklington* (2000), 194 D.L.R. (4th) 109 (Alta. C.A.) (treated as issue of justification). See also W. A. Richardson, "Making an End Run Around the Corporate Veil: The Tort of Inducing Breach of Contract" (1984-85) 5 Adv. Quart. 103. To simply say that the immunity of directors is an exception or is justified is to beg the question. The real basis for the immunity would be that which makes it an exception or justifies it. None of this is necessary or helpful, however, as the proper approach to director liability is to determine whether or not (on the basis of an authority analysis) a tort occurred. The justification argument, however, would remain relevant as a general defence to liability for inducing a breach of contract. See *Edwin Hill & Partners v. First National Finance Corp plc*, [1988] 3 All E.R. 801 (C.A.).

¹¹² *British Thomson-Houston Company, Limited v. Sterling Accessories, Limited*, [1924] 2 Ch. 33; *Prichard & Constance (Wholesale) Ltd. v. Amata Ltd.* (1924), 42 R.P.C. 63 (Ch.); *Northern Electric Co. v. Burkholder*, [1935] 4 D.L.R. 598 (Ex.); *Blacklaws v. Morrow* (2000), 187 D.L.R. (4th) 614 (Alta. C.A.).

¹¹³ *Weir v. Bell* (1878), 3 Ex. D. 238 (C.A.); *Cargill v. Bower* (1878), 10 Ch. D. 502; *Performing Right Society, Limited v. Caryl Theatrical Syndicate, Limited*, [1924] 1 K.B. 1 (C.A.); *Wah Tat Bank Ltd. v. Chan Cheng Kum*, [1975] A.C. 507 (P.C.); *Mancetter Developments Ltd. v. Garmanson Ltd.*, [1986] Q.B. 1212 (C.A.).

¹¹⁴ *Mill v. Hawker* (1874), L.R. 9 Ex. 309; *Said v. Butt*, [1920] 3 K.B. 497.

¹¹⁵ [1921] 2 A.C. 465.

¹¹⁶ [1924] 1 K.B. 1.

¹¹⁷ *Supra* note 115 at 476.

¹¹⁸ *Supra* note 116 at 14.

directors themselves directed or procured the commission of the act they would be liable in whatever sense they did so, whether expressly or impliedly".¹¹⁹

The liability conclusion in these two cases was uniformly applied or endorsed in numerous subsequent decisions.¹²⁰ This apparently settled state of the jurisprudence was disturbed in certain respects, however, by the judgment of the Canadian Federal Court of Appeal in *Mentmore Manufacturing Co., Ltd. v. National Merchandising Co. Inc.*¹²¹ According to Justice Le Dain, the issue of director liability involved a conflict between corporate law and tort law:

What is involved here is a very difficult question of policy. On the one hand, there is the principle that an incorporated company is separate and distinct in law from its shareholders, directors and officers, and it is in the interests of the commercial purposes served by the incorporated enterprise that they should as a general rule enjoy the benefit of the limited liability afforded by incorporation. On the other hand, there is the principle that everyone should answer for his tortious acts. The balancing of these two considerations in the field of patent infringement is particularly difficult. . . .

This is a principle that should apply, I think, not only to the large corporation but also to the small, closely held corporation as well. There is no reason why the small, one-man or two-man corporation should not have the benefit of the same approach to personal liability merely because there is generally and necessarily a greater degree of direct and personal involvement in management on the part of its shareholders and directors. This view finds support, I believe, in the cases. It has been held that the mere fact that individual defendants were the two sole shareholders and directors of a company was not by itself enough to support an inference that the company was their agent or instrument in the commission of the acts which constituted infringement or that they so authorized such acts as to make themselves personally liable: see *British Thompson-Houston Co., Ltd. v. Sterling Accessories, Ltd.* (1924), 41 R. P. C. 311; *Prichard & Constance (Wholesale), Ltd. v. Amata, Ltd.* (1924), 42 R. P. C. 63. It is the necessary implication of this approach, I think, that not only will the particular direction or authorization required for personal liability not be inferred merely from the fact of close control of a corporation but it will not be inferred from the general direction which those in such control must necessarily impart to its affairs.¹²²

Although there had been allusions to this supposed conflict in earlier cases, this was the first significant case to explicitly appeal to these seemingly opposed

¹¹⁹ *Ibid.* at 15. Directors may be personally liable for their individual direction or for their collective direction as a board. See *Mill v. Hawker* (1974), L.R. 9 Ex. 309; *T. Oertli AG. v. E.J. Bowman (London) Ltd.*, [1956] R.P.C. 282 (Ch. D).

¹²⁰ *British Thomson-Houston Company, Limited v. Sterling Accessories Limited*, [1924] 2 Ch. 33; *O'Brien v. Dawson* (1941), 41 S.R. (N.S.W.) 295; *Reitzman v. Grahame-Chapman and Derustit, Ltd.* (1950), 67 R.P.C. 178 (Ch.); *T. Oertli AG. v. E.J. Bowman (London) Ltd.*, [1956] R.P.C. 282 (Ch. D.); *Alliance Tire and Rubber Co. Ltd. v. Alliance Tire and Rubber Co. of Canada Ltd.* (1972), 4 C.P.R. (2d) 106 (F.C.T.D.); *Wah Tat Bank Ltd. v. Chan Cheng Kum*, [1975] A.C. 507 (P.C.); *Daido Asia Japan Co. Ltd. v. Rothen*, [2001] E.W.J. No. 3997 (Ch.) (Q.L.). See also *Scott v. Riehl* (1958), 15 D.L.R. (2d) 67 (B.C.S.C.) (breach of trust).

¹²¹ (1978), 89 D.L.R. (3d) 195 (F.C.A.).

¹²² *Ibid.* at 202-203.

corporate/tort policy considerations.¹²³ The discussion was all somewhat unfortunate, however, because the ostensible policy conflict identified by the court did not (and does not) exist. It is doubly unfortunate, moreover, because the existence of the supposed conflict has been accepted [assumed] in subsequent cases and has driven [and enfeebled] their analyses.¹²⁴

In *Mentmore* itself, the policy considerations were neither investigated nor developed in any deep or systematic way. Justice Le Dain nevertheless offered the following tentative views as to the test he would apply:

What, however, is the kind of participation in the acts of the company that should give rise to personal liability? It is an elusive question. It would appear to be that degree and kind of personal involvement by which the director or officer makes the tortious act his own. It is obviously a question of fact to be decided on the circumstances of each case. I have not found much assistance in the particular case in which Courts have concluded that the facts were such as to warrant personal liability. But there would appear to have been in these cases a knowing, deliberate, wilful quality to the participation: see, for example, *Reitman v. Grahame-Chapman & Derustit Ltd.* (1950), 67 R.P.C. 178; *Oertli A.G. v. E.J. Bowman (London) Ltd.*, [1956] R.P.C. 341; *Yuille v. B. & B. Fisheries (Leigh), Ltd. & Bates*, [1958] 2 Lloyd's Rep. 596; *Wah Tat Bank Ltd. et. al. v. Chan Cheng Kum*, [1975] A.C. 507 (P.C.).¹²⁵

Here Justice Le Dain has fabricated an entirely novel general criterion for director liability. The nature of this "knowing, deliberate, wilful" quality, however, remains unclear. Nor is it apparent how the presence of that quality of conduct demonstrates, beyond satisfaction of the elements of the tort itself, that the director has made the tortious act his own.¹²⁶ The English authorities he relied on certainly did not support, or clarify, the position he adopted. Nor was it helpful when he later added that "The precise formulation of the appropriate test is obviously a difficult one" and "[r]oom must be left for a broad appreciation of the circumstances of each case to determine whether as a matter of policy they call for personal liability".¹²⁷

¹²³ See *Rainham Chemical Works, Limited v. Belvedere Fish Guano Company, Limited*, [1921] 2 A.C. 465; *British Thomson-Houston Company, Limited v. Sterling Accessories Limited*, [1924] 2 Ch. 33 at 38-39. The discussion in both of these cases is actually a response to the distinct claim that the corporation was acting as the agent or alter ego of the directors.

¹²⁴ The supposed conflict is also asserted by some commentators. See R. Grantham & C. Rickett, "Directors' 'Tortious' Liability: Contract, Tort or Company Law?" (1999) 62 *Mod. L. Rev.* 133. Contrast the views of J. Lowry & R. Edmunds, "Personal Liability of Company Directors" (1998) 77 *Can. Bar Rev.* 467 and G. Shapira, "Liability of Corporate Agents: *Williams v. Natural Life Ltd.* in the House of Lords" (1999) 20 *Comp. Lawy.* 130.

¹²⁵ *Supra* note 121 at 205.

¹²⁶ One might separately question the meaning of the phrase "makes the tortious act his own". See *Microsoft Corporation v. Auschina Polaris Pty Ltd.* (1996), 142 A.L.R. 111 at 124 (F.C. Aust.) ("With respect, I do not find the formula, 'making the tortious act his own' particularly illuminating"). Courts have subsequently indicated that a separate interest or an assumption of responsibility on the part of directors will "make the act their own".

¹²⁷ *Supra* note 121 at 205.

On the matter of the ostensible conflict between corporate law and tort law, only a few observations need be made. It is abundantly clear that neither Parliament nor the House of Lords in *Salomon* purported to confer limited tort liability on directors of corporations. It is simply not the case, as Justice Le Dain would have it, that directors "enjoy the benefit of limited liability afforded by incorporation." Directors are *agents* and, as such, are subject to the standard open tort liability associated with that status. This aspect of agency liability is just a specific manifestation of the general principle that actors are liable for their personal tortious conduct. This personal tort liability had been confirmed without reservation again and again in both the negligence and intentional tort cases reviewed above. It was plain that no conflict of the kind asserted by Justice Le Dain in fact troubled the jurisprudence.

Nor was there any theoretical conflict. It is usually claimed that the conflict arises from the separate legal existence of the corporation. Since it is the tort of the corporation, it is said, only the corporation can be liable. But that is plainly wrong. The separate existence of the principal does not excuse the personal liability of an agent in any other context. Incorporation does not change that result for directors. The only effect of incorporation is to substitute the corporation for the shareholders as the legal principal. Without the separate existence of the corporation, the directors would be agents of the shareholders. With incorporation, they become agents of the corporate entity. The shareholders, who are no longer principals, accept a new legal position defined by statute relative to the corporation and to each other. There is no discernable conflict with tort law in any of this unless it can be said that there is also some sort of conflict between tort law and the general law of agency.

Another observation has to do with Justice Le Dain's expressed concern for one-person corporations. That concern has reappeared in subsequent cases, the supposed mischief being the effective negation of limited liability for such corporations.¹²⁸ The concern, however, is overstated, both in terms of the suggested mischief and the implied social desirability of adjusting the legal position. Directors are not personally liable merely because they are directors. Nor are they liable for the torts of other agents or employees unless they participate in, or direct, the tortious act. Because these rules apply equally to the directors of both one-person and other corporations, they all have the same liability exposure. The only reason that directors of one-person corporations are at greater risk in this respect, as Justice Le Dain recognized, is that they are more likely to be personally involved in committing or directing the tortious act. To somehow relieve them of their standard tort responsibilities, however, is to discriminate in their favor. In terms of social desirability, there is no compelling reason to do so. Notwithstanding the pastoral solicitude some judges have for one-person companies (which are less likely to carry adequate insurance), it is doubtful that the public would easily concede that it is a social good to favor this

¹²⁸Eg. *Trevor Ivory Ltd. v. Anderson*, [1992] 2 N.Z.L.R. 517 (C.A.).

large class of directors with a degree of immunity that other directors, other corporate staff, and ordinary citizens, do not enjoy.

The *Mentmore* decision achieved a measure of notoriety in England when it was adopted in part by Nourse J. in *White Horse Distillers Limited v. Gregson Associates Limited*.¹²⁹ Nourse J. recognized the novelty of the *Mentmore* analysis, but found it compelling:

Although I do not find it very easy to reconcile all the passages to which I have referred or which I have quoted, I believe that the principles embodied in the *Mentmore* decision can be stated as follows. Before a director can be held personally liable for a tort committed by his company he must not only commit or direct the tortious act or conduct but he must do so deliberately or recklessly and so as to make it his own, as distinct from the act or conduct of the company. It is unnecessary for him to know, or have the means of knowing, that the act or conduct is tortious. It is enough if he knows or ought to know that it is likely to be tortious. The facts of each case must be broadly considered in order to see whether, as a matter of policy requiring the balancing of the two principles of limited liability and answerability for tortious acts or conduct, they call for the director to be held personally liable.

In the light of the position adopted by Mr. Nicholls, it is not strictly necessary for me to decide whether the principles so stated represent the law of England. The test for liability which they prescribe is evidently higher than that adopted in some of the English authorities, for example in the judgment of Atkin L.J. in *Performing Right Society Limited v. Caryl Theatrical Syndicate Limited*, [1924] 1 K.B. 1 at 14 and 15, where it is held to be enough that the director should expressly or impliedly direct or procure the commission of the tortious act. Subject to the question of policy, there is, in my view, much to be said for the higher test, particularly in regard to its requirement that the director should make the act or conduct his own as distinct from that of the company. That would seem to be an entirely rational basis for personal liability. Conversely, it would seem to be irrational that there should be personal liability merely because the director expressly or impliedly directs or procures the commission of the tortious act or conduct. In the extreme, but familiar, example of the one-man company, that would go near to imposing personal liability in every case. As for deliberateness or recklessness and knowledge or means of knowledge that the act or conduct is likely to be tortious, I think that these may on examination be found to be no more than characteristic, perhaps essential, elements in the director's making the act or conduct his own.¹³⁰

This approach did not long survive in England. In short order, the Court of Appeal essentially rejected the *Mentmore* and *White Horse* liability test. In *C. Evans & Sons Ltd. v. Spritebrand Ltd.*, Slade L.J. questioned the views expressed in the two cases, particularly the idea that a deliberate and wilful participation was required.¹³¹ He was also concerned that the effect of the new approach would be to treat directors more kindly than other agents or employees. He concluded that *Belvedere* and *Caryl* remained the law, though he did cryptically concede that in some cases "broad considerations of policy may be

¹²⁹[1984] R.P.C. 61.

¹³⁰*Ibid.* at 91-92.

¹³¹[1985] 2 All E.R. 415.

material” in deciding whether a director had procured the commission of the tort.¹³²

This is a convenient point to momentarily suspend our analysis of the intentional tort cases. From this time, and for some time, the jurisprudence appears to take on a further measure of complication and confusion. Before passing to that more recent case law, however, it is useful to examine another development that will help in making sense of what lies ahead.

C. Identification/Attribution

The other development that has had an impact in this area is the judicial innovation of attributing the fault or intentions of individuals to their corporate employers. The usual bases for corporate responsibility are authorization (of agents or employees) and vicarious liability. Neither of these permit *personal* liability for a corporation in cases where intention or *mens rea* is an element of the claim or charge. Because the corporation itself has no physical mental presence, it could be considered personally immune from claims involving a mental element. To overcome this logic, courts in some jurisdictions have employed an “identification” theory to attribute the intentions of individuals to corporations.¹³³ Those who are the “directing mind” of the corporation for the particular purpose will qualify for this attribution to, or identification with, the corporation.¹³⁴

This attribution concept, it should be apparent, has nothing whatsoever to do with the tort liability of directors.¹³⁵ It is relevant only to whether the *corporation* is personally liable in some respect. The claim in the present context is that the *director* is personally liable for a tortious act. Still, there are cases in this area that purport to apply the “identification” and “directing mind” notions. This has only confused the jurisprudence.

¹³² *Ibid.* at 425.

¹³³ *Lennards Carrying Company, Limited v. Asiatic Petroleum Company, Limited*, [1915] A.C. 705; *Tesco Supermarkets Ltd. v. Nattrass*, [1971] 2 All E. R. 127 (H. L.); *Canadian Dredge & Dock Co. Ltd. v. The Queen* (1985), 19 D.L.R. (4th) 314 (S.C.C.); *Meridian Global Funds Management Asia Ltd. v. Securities Commission*, [1995] 3 All E. R. 918 (P.C.).

¹³⁴ *H. L. Bolton (Engineering) Co. Ltd. v. T. J. Graham & Sons Ltd.*, [1957] 1 Q.B. 159 at 172 (“Some of the people in the company are mere servants and agents who are nothing more than hands to do the work and cannot be said to represent the mind and will. Others are directors and managers who represent the directing mind and will of the company, and control what it does. The state of mind of these managers is the state of mind of the company and is treated by the law as such.”).

¹³⁵ See D. Wishart, “The Personal Liability of Directors in Tort” (1992) 10 Co. & Sec. L.J. 363; P. Watts, “Company Law” [1992] N.Z. Recent Law Rev. 219; “The Company’s Alter Ego — A Parvenu and Imposter in Private Law” [2000] N.Z.L.R. 137 and “The Company’s Alter Ego — An Imposter in Private Law” (2000) 116 L.Q.R. 525.

VII. *Jurisprudential Turmoil in the Late Twentieth Century*

In the last decade (more or less) of the twentieth century, certain parts of the jurisprudence in some jurisdictions passed into a state of serious confusion. The onset of the additional confusion was due in part to novel judicial analysis and in part to a failure by judges to appreciate the inapplicability or irrelevance of a variety of legal concepts. Prior to this decade of disorder, the legal position of directors was relatively clear, if not entirely satisfactory. Although there were cases that employed general tort law principles in both the negligence and intentional tort contexts, there were a number of inexplicable divergences. While it was clear that directors were subject to open personal liability for their negligent actions, the standard of care they owed to their principals was formally different from that expected of other agents. It was also clear that directors were personally liable both for committing or directing intentional torts. There was a difference between jurisdictions, however, as to the quality or nature of the behaviour that triggered the liability. In those jurisdictions where liability depended on conduct that exhibited a "knowing, deliberate, wilful quality," directors were again treated more favorably than other tortfeasors. New developments have now altered or added to this case law in significant respects. We will examine the recent cases to see the course the law has taken. This will be done in reverse order relative to the preceding section, dealing first with intentional torts and then with negligence. Because the Canadian jurisprudence has been the most confusing, we begin with it.

A. *Intentional Torts*

Many of the recent Canadian decisions on intentional torts are concerned with the tort of inducing a breach of contract.¹³⁶ We will examine those cases first, and then the cases dealing with directors participating in or directing the commission of other intentional torts. It is useful at this point, however, to note the clear distinction between, on the one hand, causing a breach of contract and, on the other, directing the commission of a tort. Instructing another to commit a tort is itself a tortious act. It is either a joint participation in the tort (the actors are joint tortfeasors) or a separate tort of procuring a tortious act.¹³⁷ Causing

¹³⁶ It is perhaps no surprise that there are numerous inducement claims. Plaintiffs have an incentive to make the claim because it offers the prospect of recovery from an asset pool beyond that of the corporation. The claim may also provide a measure of leverage in settlement discussions (see text at notes 138—40 *infra*). Defendant directors, for their part, have an incentive to defend if, as is often the case, the *Said v. Butt* principle is a plausible argument for them. The confusion and uncertainty of the jurisprudence would also be a factor encouraging litigation.

¹³⁷ The current view seems to be that different persons who separately instruct and commit the tort are joint tortfeasors. See *The Koursk*, [1924] P. 140; *Brooke v. Bool*, [1928] 2 K.B. 578; *T. Oerli AG. v. E.J. Bowman (London) Ltd.*, [1956] R.P.C. 282 (Ch. D.); *MCA Records Inc. v. Charly Records Ltd.*, [1996] E.W.J. 1306 (Ch.).

a corporation to breach a contract, in contrast, is not *per se* a tortious act. It depends on whether the actor (eg. the director) had the requisite authority to cause the corporation to breach the contract.

One other preliminary point may be made with respect to claims of inducing a breach of contract. The courts have expressed a concern with litigants advancing personal claims against directors for tactical reasons and it may be that this concern has been a factor in the development of the jurisprudence.¹³⁸ In *ADGA Systems International v. Valcom Ltd.*, Carthy J. recognized "the policy concern expressed by the Divisional Court, and other General Division judges, over the proliferation of claims against officers and directors of corporations in circumstances which give the appearance of the desire for discovery or leverage in the litigation process".¹³⁹ His response to this concern, however, was that it should not inappropriately influence the courts into "protecting all conduct by officers and employees in pursuit of corporate purposes".¹⁴⁰ That is the proper response. Litigants are entitled to make their claims. The control mechanism for unfounded claims is an application to dismiss for failing to disclose a cause of action. Tactical pleading may also be penalized in the assessment of costs. A concern with tactical litigation is obviously not properly addressed by altering the substantive law or by endorsing a bias or presumption against personal liability for directors. These judicial expressions of concern with litigation tactics, accordingly, can carry no freight in the analysis or development of the substantive personal tort liability of directors. Let us now turn to a review of the inducement cases.

For many years, Canadian cases addressing claims of inducing a breach of contract were unremarkable.¹⁴¹ The issue was usually whether the director had

¹³⁸ See *C. Evans & Sons Ltd. v. Spritebrand Ltd.*, [1985] 2 All E.R. 415 (C.A.); *Foy v. Royal Bank* (1995), 37 C.P.C. (3d) 262 (Ont. Gen. Div.); *Industrial Ecology Inc., v. Kayar Energy Systems Inc.*, [1997] O.J. No. 204 (Ont. Gen. Div.) (QL); *Srebot Farms Ltd. v. Bradford Co-operative Storage Ltd.*, (1997), 145 D.L.R. (4th) 331 (Ont. Gen. Div.), affd. (1998), 163 D.L.R. (4th) 190 (Ont. C.A.). *1175777 Ontario Ltd. v. Magna International Inc.* (2001), 200 D.L.R. (4th) 521 (Ont. C.A.). At least one judge purported to actually assess whether the pleading of the claim was tactical. See *Industrial Ecology Inc. v. Kayar Energy Systems Inc.*, [1997] O.J. No. 204 (Ont. Gen. Div.) (QL). See also *O'Keefe v. Ontario Hydro*, [1980] O.J. No. 1258 (Ont. H.C.) (QL). Presumably, however, that question cannot arise once it is determined that a cause of action has or has not been made out.

¹³⁹ (1999) 168 D.L.R. (4th) 351 at 355 (Ont. C.A.), leave to appeal refd. (2000), 183 D.L.R. (4th) vi (S.C.C.).

¹⁴⁰ *Ibid.* See also *United Canadian Malt Ltd. v. Outboard Marine Corp. of Canada* (2000), 48 O.R. (3d) 352 (Ont. Sup. Ct.); *Jama (Litigation guardian of) v. McDonald's Restaurants of Canada Ltd.*, [2001] O.T.C. 203 (Ont. Sup. Ct.).

¹⁴¹ *Einhorn v. Westmount Investments Ltd.* (1970), 11 D.L.R. (3d) 509 (Sask. C.A.); *Neyland v. Genstar Ltd.* (1977), 76 D.L.R. (3d) 697 (B.C.S.C.); *Katz v. Tannenbaum*, [1982] O.J. No. 256 (Ont. H.C.) (QL); *Campbell v. Saskatchewan Crop Insurance Board*, [1984] 2 W.W.R. 127 (Sask. Q.B.); *Fink v. 511996 Ontario Ltd.* (1984), 37 R.P.R. 253 (Ont. H.C.); *Acme Bldg. & Construction Ltd. v. Leadway Masons Group Inc.* (1986), 35 B.L.R. 17 (Ont. Dist. Ct.); *Kepic v. Tecumseh Road Builders* (1987), 18 C.C.E.L. 218 (Ont. C.A.). In at least one case, neither the plaintiff nor the judge appeared to recognize the potential claim for inducing a breach of contract. See *Schouls v. Canadian Meat Processing Corp.* (1983), 147 D.L.R. (3d) 81 (Ont. H.C.).

acted *bona fide* when causing the corporate breach. It was not until the late 1980's that an analytical fog descended on the Canadian jurisprudence. A number of cases can now be identified as having significantly contributed to the new judicial tangle. One source of confusion was the 1987 judgment of Justice Anderson in *Lehndorff Canadian Pension Properties Ltd. v. Davis & Co.*¹⁴² With reference to *Said v. Butt*, Justice Anderson stated that: "I take this judgment to mean that if a director acts within the scope of his authority and with good faith and if there is any breach of contract, the company is liable as the act of the director is the very act of the company itself... However, if the director acts in bad faith and outside the scope of his authority, then he may become personally liable in tort".¹⁴³ That is essentially a faithful restatement of the *Said v. Butt* principle.¹⁴⁴ Thereafter, however, a series of confusions are introduced. Justice Anderson went on to characterize the defendant directors as the "directing mind" of the corporation, with the consequence that their acts were the acts of the corporation.¹⁴⁵ The point of employing the directing mind concept in this way is not clear. Every act of every authorized agent or employee is the act of the corporation, not just the acts of persons who qualify as directing minds. It may be that Justice Anderson utilized the directing mind notion to identify as immune from tortious liability only those corporate agents (eg. directors, senior officers) who typically possess the authority to terminate the contractual performance of the corporation. That, however, would be an elliptical and confusing usage even for lawyers. The directing mind idea is normally associated with *corporate* liability. As well, there may be a number of directing minds in a corporation and not all of them will have the authority to end contractual obligations of the corporation. It would lessen the confusion in this area if the question were left as one of authority, as Justice Anderson's initial remarks had indicated.

A second confusion emanating from Justice Anderson's judgment is found in his statement that: "It is clear that when a director of a company engages in discussions and makes decisions relating to the company's business, he is acting within the scope of his authority...."¹⁴⁶ This statement is seriously misleading. It reverses the basic logic. Directors only make decisions for the corporation *if they are acting with authority*. In addition, on the face of it, the statement is too broad. Read as a general proposition without regard to its inducement context, it suggests that directors are not personally liable for any tort as long as they are authorized to do the act. That, on the authorities, is flatly wrong. Whether it is negligence or an intentional tort, directors are not generally excused from liability because their actions are authorized.¹⁴⁷ It is only in the specific case of the tort of inducing a breach of contract that the authorization or power to breach contracts has such an

¹⁴² (1987), 10 B.C.L.R. (2d) 342 (B.C.S.C.).

¹⁴³ *Ibid.* at 350.

¹⁴⁴ See text at notes 107 — 111 *supra*.

¹⁴⁵ *Supra* note 142 at 350. Justice Anderson was not the first to utilize the directing mind terminology. See, for example, *Windsurfing International Inc. v. Novaction Sports Inc.* (1987), 18 C.P.R. (3d) 230 (F.C.T.D.).

¹⁴⁶ *Ibid.*

¹⁴⁷ See authorities at notes 49, 66, 104, 110 *supra*.

effect,¹⁴⁸ and that is because authorization means there is no wrongful conduct beyond, or distinct from, the breach of contract.

A third confusion is introduced by Justice Anderson's statement that a director "can only attract personal liability if he is acting outside the scope of his authority in being motivated by advancing a personal interest contrary to the interests of the company, or by fraud, or with malice".¹⁴⁹ This proposition is too narrow. The listed circumstances indicate ways in which directors would not be acting *bona fide*. But acting *bona fide* is not a complete defence. The list leaves out (unless it is implicit) the simple case of a director who acted *bona fide* but nevertheless had never been granted authority to determine whether the corporation will continue to perform its contractual obligations. That director would be personally liable for inducing a breach.

The 1989 decision of the Newfoundland Court of Appeal in *Imperial Oil Ltd. v. C & G Holdings Ltd.* is a second source of complication and confusion.¹⁵⁰ It is apparent that the court had a good grasp of the existing jurisprudence. The court, however, was not satisfied with the state of the law. It did not feel there were sufficient limits on the ability of third parties to hold directors liable for deliberately inducing a breach of contract. The court took the view that further limits were required "because of the relationship of directors to their company and the need to reconcile obligations emanating from that relationship with the general duty to refrain from interfering with the bargains of others.... The general duty to abstain from knowingly violating the legal rights of others must be weighed against the concomitant obligations of a director to the company and his or her functions relative to its operations".¹⁵¹ Justice Marshall went on to observe that malice had previously been rejected as a limiting factor.¹⁵² His own solution was to add a distinct new limit in the form of "affirmative proof that the dominating purpose of the director's act was aimed at depriving the aggrieved party of the benefits of the contract".¹⁵³ This was plainly an innovation on the part of the court and an overt attempt to judicially revise the law. The most striking feature of this particular exercise of judicial power was the absence of any sort of supporting analysis or justification. The ostensible policy conflict and the "dominant purpose" test were simply asserted. No connection was made between the two, nor were either explained or developed in any way.¹⁵⁴ This is all problematic, obviously, because

¹⁴⁸ See text at notes 110 — 111 *supra*. Consider *Newswest Corp. v. Glendar Holdings Ltd.*, [2001] 9 W.W.R. 312 (Sask. Q.B.).

¹⁴⁹ *Supra* note 142 at 351.

¹⁵⁰ (1989), 62 D.L.R. (4th) 261 (Nfld. C.A.).

¹⁵¹ *Ibid.* at 264.

¹⁵² *Ibid.* at 266.

¹⁵³ *Ibid.*

¹⁵⁴ Justice Marshall's conclusions appear to rest on the assumption (*ibid.* at 268) that: "If the propriety of a director's actions within the company is to be subjected to scrutiny and justification at the instance of third parties, it would greatly enhance the opportunity to pierce the corporate veil, impair the freedom of decision by the directing minds of the company and diminish the facility of corporate action". The short answer to this expression of concern is that the law rightly regulates the external consequences of internal decisions.

it is a feature of *every* transaction that the respective parties will consider their own internal duties and whether serving those duties might have an external effect in interfering with or violating the legal rights of others. In other words, if this is a conflict, it is not an escapable one. And since the supposed conflict is not restricted to directors, it cannot support special treatment for them. As for the “dominant purpose” test, one could scarcely imagine a better device for completely eradicating by indirection any director liability for inducing breach. It would take little effort, for example, to compose a letter or memorandum, or otherwise cosmetically manipulate an arrangement *ex ante* or *ex post*, to create evidence that one’s motive was always to serve the corporate interest, and not to deprive the aggrieved party of a contractual benefit. Finally, apart from these considerations, this deprivation test looks very much like another attempt to introduce into the jurisprudence something akin to a malice test for director liability.

The other confusion that appears in the case is the court’s apparent framing of its analysis as a question of “piercing the veil”.¹⁵⁵ Determining whether a director is liable for inducing a breach simply does not raise the piercing issue. Indeed, except where shareholder immunity from vicarious liability is challenged, no corporate veil issue arises in connection with any question of individual personal tort liability. The corporate veil does not shield the tortious actions of any actor. In the particular case of the tort of inducing breach of contract, the immunity accorded to directors by *Said v. Butt* is premised entirely on the presence or absence of the appropriate authority. The issue is whether or not there is a tort at all, and that has nothing to do with piercing the corporate veil. Rather, the authority approach necessarily involves *respecting* the separate entity status of both corporations and directors.

The judgment of Justice MacFarland in *Ontario Store Fixtures v. Mmmuffins Inc.* is a third source of confusion.¹⁵⁶ Justice MacFarland proposed another formal revision of the criteria necessary to found a claim for inducing breach of contract. In this instance, the judge seems headed in the right direction, though not on the right track.¹⁵⁷ Justice MacFarland was of the view that “to give rise to a separate claim for intentional inducement of breach of contract as well as a claim for breach of contract arising out of the same circumstances,

¹⁵⁵ *Ibid.* at 266-68. The view that director liability is a piercing issue appears to be widely held. A representative example of this mistaken view is provided by L. Bradford, “Corporate Officer Not Liable for Subordinate Employees’ Tortious Conduct” (1997) 30 Suffolk U.L. Rev. 545 at 546-47 (“Corporate law, which treats the corporation and its members as separate legal entities, generally insulates shareholders, officers, and directors (officers) from personal liability for actions taken on behalf of the corporation. Accordingly, in disputes involving commercial transactions or corporate debts, courts normally limit liability to the corporation itself. Many courts, however, have extended personal liability to corporate officers who actively participate in or direct tortious acts. This practice has translated into the doctrine of ‘piercing the corporate veil’.”).

¹⁵⁶ (1989), 70 O.R. (2d) 42.

¹⁵⁷ As with the “justification” rationale, Justice MacFarland’s approach involves conceding the tort (the wrong track).

there must be separate identities of interest, otherwise there is mere duplication under another label".¹⁵⁸ He later stated that: "A plaintiff must plead facts which point to a specific tortious act which is independent of the breach of contract".¹⁵⁹ Justice MacFarland is plainly insisting on some kind of wrongful act or conduct apart from the breach of contract itself. Without that wrongful conduct, there is no actionable tort. His review of a number of cases indicated that directors would be liable if they acted without authority, either because of a lack of authority or because their actions were fraudulent or otherwise wrongful, and therefore not authorized. While Justice MacFarland is close to the mark, the difficulty with his judgment is that the issue of authority is obscured when the analysis is recast as a question of whether there are "separate identities of interest." That is because the terminology may contemplate or accommodate something beyond an independent tortious act.¹⁶⁰ Even that latter interpretation, however, is problematic if it implies that some *other* nominate tort (ie. other than the tort of inducing a breach of contract) is required. The basis for excusing directors from liability for inducing a breach is that they acted with authority. If they have authority, there is no tort. If they do not have the authority to cause the corporation to breach, they are interfering with the contractual relation of others. This interference is wrongful because it was not authorized. It is this interference that constitutes the tort. The issue of authority is tied exclusively in this way to this particular tort. All of this can easily be lost sight of when judges are directed to search for "separate identities of interest."

The analysis in the foregoing cases, along with the "wilful participation" test in *Mentmore*,¹⁶¹ would complicate and confuse the jurisprudence for the ensuing decade. The progress of this obfuscation was facilitated at least in part by the fact that the Canadian judiciary largely ignored the jurisprudence that pre-dated these cases. As it happened, although there were many cases decided in the course of that decade, there was little conceptual consistency or insight.¹⁶² Some judges applied the "wilful participation" test, others the

¹⁵⁸ *Supra* note 156 at 44.

¹⁵⁹ *Ibid.* at 47.

¹⁶⁰ "Separate identities of interest", on the face of it, is potentially inclusive of a wide range of considerations and could conceivably accommodate even different subjective motives.

¹⁶¹ See the cases at note 187 *infra*.

¹⁶² *Prism Hospital Software Inc. v. Hospital Medical Records Institute* (1987), 18 C.P.R. (3d) 398 (B.C.S.C.), leave to appeal dismissed, (1987), 18 C.P.R. (3d) 401 (B.C.C.A.); *Hirsh Co. v. Minshall* (1987), 17 C.P.R. (3d) 153 (F.C.T.D.), *revd.* (1988), 22 C.P.R. (3d) 268 (F.C.A.); *Katun Corp. v. Technofax Inc.* (1988), 22 C.P.R. (3d) 269 (F.C.T.D.); *Colonia Life Holdings Ltd. v. Fargreen Enterprises Ltd.* (1990), 1 O.R. (3d) 703 (Ont. Gen. Div.); *Desimone v. Herrmann Group Ltd.*, [1991] O.J. No. 929 (Ont. Gen. Div.) (Q.L.); *Coldwell Banker Canada Inc. v. Remac Builders Hardware Inc.* (1991), 18 R.P.R. (2d) 137 (Ont. Gen. Div.); *United Cooler (Niagara 1980 Ltd.) v. Zafir*, [1992] O.J. No. 1258 (Ont. Gen. Div.) (Q.L.); *Clairmont v. London Life Insurance Co.*, [1992] O.J. No. 2191 (Ont. Gen. Div.) (Q.L.); *Leblanc v. Trans Canada Truck Driving Academy Inc.*, [1993] O.J. No. 360 (Ont. Gen. Div.) (Q.L.); *Ashdown v. Jumbo Video Inc.*, [1993] O.J. No. 1169 (Ont. Gen. Div.) (Q.L.); *Truckers Garage Inc. v. Krell* (1993), 3 C.C.E.L. (2d) 157 (Ont.

"dominant purpose" test. A number of judgments display confusion on the authority question. There are overly-broad statements regarding the effect of authority.¹⁶³ Some judges speak of "justification." Several judgments frame the issue as one of "piercing the veil." Many judges thought it relevant to ask whether the director was or was not a "directing mind." Others asked whether there was a "separate identity of interest." In some cases, particular tests or approaches were applied or incorporated without reference to any others. It was more common, however, for judges to draw on different combinations of the new considerations. There are very few cases where the judges appear to appreciate the novelty or mistaken application of the various tests and approaches. Only occasionally does a judge comment on the perplexing state of the authorities.¹⁶⁴ Some judges, while confused in other respects, did appear to recognize that the effect of the case law would be to give special treatment to directors.¹⁶⁵ It may fairly be added to the foregoing critical account that there was accurate and careful analysis in many of these cases, and arguably a correct result in most. The overall experience, however, was disorder. The result was an opaque case law.

It is not necessary to review each of the cases to appreciate the level of confusion that had been introduced. It is enough to illustrate with a few

C.A.); *Painblanc v. Kastner* (1994), 58 C.P.R. (3d) 502 (Fed. C.A.); *Tree-O Marketing Inc. v. Bio-Cosmetics Inc.* (1994), 26 C.P.C. (3d) 169 (Ont. Gen. Div.); *Jackson v. Trimac Industries Ltd.* (1994), 20 Alta. L.R. (3d) 117 (Alta. C.A.); *Butler v. Dimitrieff*, [1994] O.J. No. 3518 (Ont. C.A.) (QL); *Levi v. Chartersoft Canada Inc.* (1994), 8 C.C.E.L. (2d) 10 (Man. Q.B.); *Aspiotis v. Coffee Time Donuts Inc.*, [1995] O.J. No. 419 (Ont. Gen. Div.) (QL); *National Trust v. Furbacher*, [1995] O.J. No. 3566 (Ont. Gen. Div.) (QL); *Foy v. Royal Bank* (1995), 37 C.P.C. (3d) 262 (Ont. Gen. Div.); *Polimeni v. Danzinger* (1995), 26 C.C.L.T. (2d) 256 (Man. Q.B.); *Pace v. DelZotto* (1996), 24 B.L.R. (2d) 263 (Ont. Gen. Div.); *Craik v. Aetna Life Insurance Co.*, [1995] O.J. No. 3286 (Ont. Gen. Div.) (QL), affd. [1996] O.J. No. 2377 (Ont. C.A.) (QL); *Jim Pattison Developments Ltd. v. Fudex International Inc.* (1996), 30 B.L.R. (2d) 65 (Alta. Q.B.); *Peart v. SSA Ontario Corp.*, [1996] O.J. No. 4545 (Ont. Gen. Div.) (QL); *Heimrath Porsche Service Ltd. v. Porsche Cars Canada Ltd.*, [1997] O.J. No. 2335 (Ont. C.A.) (QL); *Digital.Doc Services (Canada) Inc. v. Future Shop Ltd.*, [1997] B.C.J. No. 1689 (B.C.S.C.) (QL); *Rudd Management Ltd. v. Byrne*, [1997] O.J. No. 5121 (Ont. Gen. Div.) (QL); *Century Services Inc. v. Multi-Corp. Inc.* (1997), 57 Alta. L.R. (3d) 21 (Alta. Q.B.); *Industrial Ecology Inc. v. Kayar Energy Systems Inc.*, [1997] O.J. No. 204 (Ont. Gen. Div.) (QL); *Torgan Enterprises Ltd. v. Contact Arts Management Inc.*, (1997), 35 O.T.C. 339 (Ont. Gen. Div.).

¹⁶³ *Eg. Ashdown v. Jumbo Video*, [1993] O.J. No. 1169 at para. 69 (Ont. Gen. Div.) (QL) ("In general, actions done in a representative capacity on behalf of a corporation are protected by the shield of limited corporate liability.").

¹⁶⁴ *Jim Pattison Developments Ltd. v. Fudex International Inc.* (1996), 30 B.L.R. (2d) 65 at 83 (Alta. Q.B.) ("The case law is not consistent on what is required to make the principals of a company liable for the company's breach of contract.").

¹⁶⁵ Consider *Prism Hospital Software Inc. v. Hospital Medical Records Institute* (1987), 18 C.P.R. (3d) 398 at 400 (B.C.S.C.), leave to appeal dismissed (1987), 18 C.P.R. (3d) 401 (B.C.C.A.); *Jackson v. Trimac Industries Ltd.* (1994), 20 Alta. L.R. (3d) 117 at 123-124 (Alta. C.A.); *Simpson v. Consumers' Association of Canada* (1999), 41 C.C.E.L. (2d) 179 at 259 (Ont. Gen. Div.); *1005633 Ontario Inc. v. Winchester Arms Ltd.* (2000), 8 B.L.R. (3d) 176 (Ont. Sup. Ct.).

examples. One significant case was the decision of the Ontario Court of Appeal in *ScotiaMcLeod Inc. v. Peoples Jewellers Limited*.¹⁶⁶ The case involved a claim for negligent misrepresentation, but has subsequently had an impact beyond that particular context. That impact was due largely to the catalogue of circumstances the court identified as exhausting the possibilities for the imposition of personal liability on directors.¹⁶⁷ Such a catalogue would (and did) make the case an attractive one to cite where litigants believed either they were included within, or excluded from, the specified categories. As part of that catalogue, Justice Finlayson stated that: "Absent allegations which fit within the categories described above, officers or employees of limited companies are protected from personal liability unless it can be shown that their actions are themselves tortious or exhibit a separate identity or [sic] interest from that of the company so as to make the act or conduct complained of their own".¹⁶⁸ Justice Finlayson here seems to disconnect or distinguish the tort liability of directors from the "separate identity or [sic] interest" test. He later appears to reconnect them, however, when he equates the positions of senior officers with directors and finds that both classes of agent have the same immunity where they are the "directing minds" and have the "same identity of interest".¹⁶⁹

Elsewhere in his judgment, Justice Finlayson had insisted that: "To hold the directors of Peoples personally liable, there must be some activity on their part that takes them out of the role of directing minds of the corporation".¹⁷⁰ None of this, however, including his review of a number of cases dealing with the "identification theory", is particularly helpful. Focussing on whether directors are directing minds of the corporation is, in the present context, a confusion. In the inducement cases, the issue is whether the directors had the authority to terminate contractual performance. That issue is conceptually distinct from whether or not a director is a directing mind for some corporate purpose. For other intentional torts, it would simply be wrong to excuse directors because they are directing minds. Authorization to do the act has no immunizing effect outside the inducement context.¹⁷¹ Interfering in contractual relations without authority is the tortious act in the inducement cases. In other intentional tort cases, liability for the tort does not depend on the presence or absence of authority.

The authority question was also misunderstood in *Polimeni v. Danzinger*.¹⁷² The court stated that directors would not be liable for inducing a breach if they acted within their "scope of employment."¹⁷³ That, however, is

¹⁶⁶ (1995), 129 D.L.R. (4th) 711 (Ont. C.A.).

¹⁶⁷ *Ibid.* at 720.

¹⁶⁸ *Ibid.*

¹⁶⁹ *Ibid.* at 725.

¹⁷⁰ *Ibid.* at 721.

¹⁷¹ See text at and in note 110 *supra*.

¹⁷² (1995), 26 C.C.L.T. (2d) 256 (Man. Q.B.). See also *Levi v. Chartersoft Canada Inc.* (1994), 8 C.C.E.L. (2d) 10 (Man. Q.B.).

¹⁷³ *Ibid.* at 265.

not the test. Rather, the issue is whether the director had the authority to terminate the contractual obligations of the corporation. That is a question of "scope of authority," not "scope of employment." The two notions are distinct, with scope of employment being the more capacious legal construction. Employees, for example, may not have authority to do an act, but the act will still be within their "scope of employment" because it constituted a mode of performing their duties. They may therefore make their employer vicariously liable, even though they acted without authority, in addition to their own personal liability. Apart from that analysis, the court also purported to explain the inducing breach "exemption from liability" as premised on either an "alter ego" or "justification" rationale.¹⁷⁴ Neither of these formulations are required, however, once it is understood that the issue is simply authorization. The issue is whether or not the tort of inducing breach occurred (a question of authority), not whether the tort (once conceded) is justified.

The above cases are but illustrations of the confusion that characterized the inducement cases. In 1999, a good deal of this confusion was seemingly relieved by the judgment of the Ontario Court of Appeal in *ADGA Systems International Ltd. v. Valcom Ltd.*¹⁷⁵ This was potentially a significant Canadian decision on the issue of the personal liability of directors for inducing a breach of contract. The case dealt with a claim for inducing a breach of fiduciary obligation, but that claim was assumed (for the purposes of the summary judgment proceeding) to be equivalent to a claim for inducing a breach of contract.¹⁷⁶ Speaking for the court, Justice Carthy cut away much of the conceptual novelty that had accumulated over the decade. The judgment, in this regard, is as important for what it omits to mention as for what it expressly addresses. There is no mention of a requirement for either a "wilful participation" or a "dominant purpose." Nor does Justice Carthy himself enlist the "directing mind" concept. In his express analysis, there is further pruning. Justice Carthy properly rejected the proposition that the liability issue had anything to do with the *Salomon* case or with piercing the veil. He observed that "where, as here, the plaintiff relies upon establishing an independent cause of action against the principals of the company, the corporate veil is not threatened and the *Salomon* principle remains intact".¹⁷⁷ He also properly rejected the proposition that directors could avoid liability if they were acting in the best interests of the corporation.¹⁷⁸ Lastly, when referring to the catalogue of circumstances identified by Justice Finlayson in *ScotiaMcLeod*, he stated that: "The operative portion of this paragraph is the

¹⁷⁴ *Ibid.* at 265-66.

¹⁷⁵ (1999), 168 D.L.R. (4th) 351 (Ont. C.A.), leave to appeal refiled., (2000), 183 D.L.R. (4th) vi (S.C.C.). Consider the views of the significance of this case offered by C. Feasby, "Corporate Agents' Liability in Tort: A Comment on *ADGA Systems International Ltd. v. Valcom Ltd.*" (1999) 32 Can. Bus. L.J. 291 and C. Nicholls, "Liability of Corporate Officers and Directors to Third Parties" (2001) 35 Can. Bus. L.J. 1.

¹⁷⁶ *Ibid.* at 355. Whether an actor is liable for inducing a breach of fiduciary obligation is arguably addressed under the rubric of the "knowing participation" analysis.

¹⁷⁷ *Ibid.* at 356.

¹⁷⁸ *Ibid.* at 361ff.

final sentence which confirms that, where properly pleaded, officers or employees can be liable for tortious conduct even when acting in the course of duty".¹⁷⁹ All of this represented a major potential rehabilitation of the jurisprudence.

A number of matters, however, remained uncertain or unresolved. Justice Carthy recognized that the general rule was that "persons are responsible for their own conduct".¹⁸⁰ He regarded *Said v. Butt* as a justified exception to this general rule. As we have seen, however, it is not an exception at all. Rather, if directors act with authority when causing the corporation to breach its contract, there simply is no tortious conduct of which to complain. There has not been any wrongful (unauthorized) interference with the contractual relations of the original parties. The other concern with the judgment is Justice Carthy's use of quotations from earlier cases that made reference to the "directing mind" of the corporation and to the need for a separate identity of interest to support the inducement claim. As discussed earlier, these concepts appear to be employed by the courts to explain why the authorized breach of contract by the corporation does not *per se* give rise to tortious liability on the part of the corporate agent who made the breach decision.¹⁸¹ In that respect, these considerations are conceptually redundant to an authority analysis, and can profitably be jettisoned. Failing to do so will imply that they address some other unclear concern, and that will have the effect of extending the confusion indefinitely.

The decision in *ADGA* held out the prospect of a coherent jurisprudence for claims of inducing a breach of contract.¹⁸² Its promise, however, may not soon be realized. Rather than building on the analysis, subsequent cases have been back-sliding into confusion (a path dependence effect). This perhaps could have been expected, given Justice Carthy's failure to explicitly reject some of the earlier tests, and the references in his quoted material to other questionable notions. Other judges also might not appreciate the significance of the *ADGA* analysis or may be reluctant to reject the earlier decisions of their colleagues. In any event, a number of confusions have continued into subsequent judgments, from the deprivation motive (dominant purpose), to directing minds and piercing the veil.¹⁸³ It would be unfortunate, however, if the opportunity to abate the existing confusion were lost.

¹⁷⁹ *Ibid.* at 364. See also *Lana International Ltd. v. Menasco Aerospace Ltd.* (2000), 190 D.L.R. (4th) 340 (Ont. C.A.); *Unisys Canada Inc. v. York Three Associates Inc.*, (2001), R.P.R. (3d) 138 (Ont. C.A.).

¹⁸⁰ *Ibid.* at 357.

¹⁸¹ See text at notes 142-60 *supra*.

¹⁸² Consider the view expressed in *Pryce v. Vuckovich*, (2000) 144 O.A.C. 256.

¹⁸³ Consider *Cavendish Promotions Inc. v. Tourism Industry Association of Prince Edward Island*, [1998] P.E.I.J. 63 (P.E.I.S.C.) (Q.L.); *Jade Agencies Ltd. v. Meadow's Management Ltd.*, [1999] B.C.J. No. 214 (B.C.S.C.) (Q.L.); *Rafiki Properties Ltd. v. Integrated Housing Development Ltd.* (1999), 45 B.L.R. (2d) 316 (B.C.S.C.); *Balanyk v. University of Toronto* (1999), 1 C.P.R. (4th) 300 (Ont. Sup. Ct.); *Simpson v. Consumers' Association of Canada* (1999), 41 C.C.E.L. (2d) 179 (Ont. Gen. Div.); *Squires v. Corner Brook Pulp and Paper Ltd.* (1999), 44 C.C.E.L. (2d) 246 (Nfld. C.A.); *Meditrust*

We turn now to the recent Canadian cases dealing with other intentional torts. We have left these cases to this point because a number of them have incorporated some of the confusions found in the inducement cases. Until recently, with one exception or diversion, the Canadian courts had faithfully applied the main English authorities.¹⁸⁴ Recall that directors are personally liable if they (1) actually participate in the tortious act or (2) procure its commission.¹⁸⁵ Establishing either of these possibilities, along with the elements of the particular tort, is sufficient to make a director liable. In *Morgan v. Saskatchewan*, Justice Tallis concisely summarized the English position as follows:

So a director is not to be held liable merely because he is a director but may be liable when he participates in or orders a tortious act and cannot escape personal liability by asserting that his act was merely the act of the corporation. In other words, the "corporate veil" is not to be used as a shield to protect shareholders and directors when they have been guilty of wrongdoing. This approach is consistent with the notion that everyone should be answerable for his tortious acts.¹⁸⁶

Healthcare Inc. v. Shoppers Drug Mart, (1999), 1240 O.A.C. (Ont. C.A.), leave to appeal dismissed, [1999] S.C.C.A. No. 530 (QL); *Immocreek Corp. v. Pretiosa Enterprises Ltd.* (2000), 186 D.L.R. (4th) 36 (Ont. C.A.); *Dodge v. Kaneff Homes Inc.*, [2000] O.J. No. 1455 (Ont. Sup. Ct.) (QL); *1005633 Ontario Ltd. v. Winchester Arms Ltd.* (2000), 8 B.L.R. (3d) 176 (Ont. Sup. Ct.); *Albayrak v. Nesbitt Burns Inc.* (2000), 4 C.C.E.L. (3d) 78 (B.C.S.C.); *Blacklaws v. Morrow* (2000), 187 D.L.R. (4th) 614 (Alta. C.A.); *369413 Alberta Ltd. v. Pocklington* (2000), 194 D.L.R. (4th) 109 (Alta. C.A.); *Thibeault v. Canadian Airlines International Ltd.*, [2000] B.C.J. No. 1626 (B.C.S.C.) (QL); *Morriss v. British Columbia*, [2001] B.C.J. No. 369 (B.C.S.C.) (QL); *Zesta Engineering Ltd. v. Cloutier* (2001), 7 C.C.E.L. (3d) 53 (Ont. Sup. Ct.); *1174538 Ontario Ltd. v. Barzel*, [2001] O.J. No. 580 (Ont. Sup. Ct.) (QL); *Cityscape Richmond Corp. v. Vanbots Construction Corp.* (2001), 8 C.L.R. 196 (Ont. Sup. Ct.); *Kay Aviation b.v. v. Rofo* (2001), 202 D.L.R. 683 (P.E.I. C.A.); *565486 Ontario Inc. v. Tristone Properties Inc.* (2001), 54 O.R. (3d) 689 (Ont. Sup. Ct.); *Unisys Canada Inc. v. York Three Associates Inc.*, (2001), R.P.R. (3d) 138 (Ont. C.A.). As to the personal liability of shareholders, see *Campbell v. T. Nelson Canada*, [2000] O.J. No. 670 (Ont. Sup. Ct.) (QL); *Phasecom Systems Inc. v. CUC Broadcasting Ltd.*, [2001] O.J. No. 1950 (Ont. Sup. Ct.) (QL). See also *DeMarchi v. Reel Records & Tapes Ltd.*, [2001] O.J. No. 846 (Ont. C.A.) (QL).

¹⁸⁴ *Omark Industries (1960) Ltd. v. Gouger Saw Chain Co.* (1964), 45 C.P.R. 169 (Exch.); *Alliance Tire and Rubber Co. Ltd. v. Alliance Tire and Rubber Co. of Canada Ltd.* (1972), 4 C.P.R. (2d) 106 (F.C.T.D.); *Baslow v. Fabri Trak Canada Limited*, [1980] 2 F.C. 238 (F.C.T.D.); *Beaver Steel Inc. v. Skylark Ventures Ltd.*, [1983] B.C.J. No. 54 (B.C.S.C.) (QL); *AAA Royal Ambulance Service Ltd. v. Howes* (1986), 48 Sask. R. 43 (Sask. Q.B.); *Hall-Chem Inc. v. Vulcan Packaging Inc.* (1994), 12 B.L.R. (2d) 274 (Ont. Gen. Div.); *Parisian Fashions Ltd. v. Petrus* (1996), 6 R.P.R. (3d) 219 (Alta. Q.B.); *Craig v. North Shore Heli Logging Ltd.* (1997), 34 B.L.R. (2d) 119 (B.C.S.C.). *Riscoe v. S All-Port Yacht Sales Inc.*, [2001] O.J. No. 2456 (Ont. Sup. Ct.) (QL).

¹⁸⁵ *Supra* notes 115-20.

¹⁸⁶ (1985), 31 B.L.R. 173 at 180-81 (Sask. C.A.).

The one diversion from the English position (primarily but not exclusively in cases of patent infringement), was the adoption of the *Mentmore* "wilful participation" threshold for liability.¹⁸⁷

The traditional position has been challenged, if not altered, over the past several years by the sporadic adoption of the confusions found in the inducing breach context. The judges have, in this respect, complicated what had been a relatively straightforward jurisprudence. Consider, for example, the relevance of the "piercing" idea. Note that Justice Tallis, in his remarks cited above, denied that the issue of personal liability had anything to do with the corporate veil. That is the correct view. An example of the proper approach is also found in the judgment of the British Columbia Court of Appeal in *B.G. Preeco I (Pacific Coast) Ltd. v. Bon Street Holdings Ltd.*,¹⁸⁸ where directors were held personally liable because they actually committed the fraudulent acts. Counsel for the plaintiff had suggested that this could be characterized as a piercing of the veil. The court rejected that view, instead finding a direct liability for fraud: "In my view, the proper remedy is not to lift the corporate veil, but to award damages for fraud against the individuals and the company that committed the fraud".¹⁸⁹ This was forcefully reiterated by Justice Rouleau in *Shibamoto & Co. v. Western Fish Producers, Inc. Estate (T.D.)*: "With due respect to the defendants, the issue of whether or not this is a proper case for the lifting of the corporate veil is completely irrelevant to the argument concerning the personal liability of Mr. Nordmann. In my opinion, the determination of Mr. Nordmann's liability must be based upon the legal principle that an individual who directs a tort to be committed is personally liable regardless of the fact that he is an officer of the company for whose benefit the tort is executed".¹⁹⁰ Then, in *Bakerview Trout Farm (1983) v. Petgus Holding Ltd.*, Justice Williamson stated: "Having found fraud, it is appropriate to make an award against Filis personally. I reject counsel's suggestion this amounts to the legal sin of piercing the corporate veil".¹⁹¹ Contrast this direct approach with the analysis in *Island Getaways Inc. v. Destinair Airlines Inc.* where the court framed a claim of

¹⁸⁷ Exx: *Visa International Service Association v. Visa Motel Corporation* (1984), 1 C.P.R. (3d) 109 (B.C.C.A.); *Dictionnaires Robert Canada SCC v. Librairie Du Nomade Inc.* (1987), 16 C.P.R. (3d) 319 (F.C.T.D.); *Windsurfing International Inc. v. Novaction Sports Inc.* (1987), 18 C.P.R. (3d) 230 (F.C.T.D.); *Pater International Automotive Franchising Inc. v. Mister Mechanic Inc.* (1989), 28 C.P.R. (3d) 308 (F.C.T.D.); *Serel v. 371487 Ontario Ltd.*, (1996), 180 O.T.C. 135 (Ont. Gen. Div.); *Norac Systems International Inc. v. Prairie Systems and Equip. Ltd.* (1997), 72 C.P.R. (3d) 303 (F.C.T.D.); *Paula Lishman Ltd. v. Erom Roche Inc.* (1997), 72 C.P.R. (3d) 214 (F.C.T.D.); *Cudworth Drilling Ltd. v. MacDonald* (1998), 174 Sask. R. 225 (Sask. Q.B.), affd., (2000), 207 Sask. R. 216 (C.A.); *B.B. Bargoons (1996) Corp. v. 744776 Ontario Inc.*, (1998), 83 C.P.R. (3d) 225 (F.C.T.D.).

¹⁸⁸ (1989), 43 B.L.R. 67 (B.C.C.A.).

¹⁸⁹ *Ibid.* at 79.

¹⁹⁰ [1991] 3 F.C. 214 at 236 (F.C.T.D.).

¹⁹¹ [1996] B.C.J. No. 983 at para. 26 (B.C.S.C.) (QL).

fraudulent misrepresentation as a "piercing" issue.¹⁹² Justice Rutherford was of the view the defendant "is not entitled to the protection that the law affords to companies and their agents by way of limited liability and the notion of the corporate veil".¹⁹³ This appeal to the piercing concept was simply unnecessary. The defendant committed the tort and that by itself engaged personal liability.

Other confusions associated with the inducement cases found their way into the international tort area. In *347154 Ontario Ltd. v. John Garay and Associates Ltd.*, a director was liable for conversion because he was the "directing mind" of the corporation and it was said to be a proper case for piercing the veil.¹⁹⁴ In *Concord Construction Inc. v. Camara*, the court decided that the director was the "directing mind" and that his fraudulent acts had induced his corporation to breach its contract with the plaintiff.¹⁹⁵ The judge ought simply to have found the director liable for fraud, rather than trying to characterize the wrong as inducing a breach of contract. A claim of conspiracy to engage in price-fixing and bid-rigging was asserted in *North York Branson Hospital v. Praxair Canada Inc.*¹⁹⁶ Justice Cumming insisted that "to sustain a civil action against the directing minds of corporations, there must be some allegation of conduct on the part of those directing minds that is either tortious in itself or exhibits a separate identity or interest from that of the corporations".¹⁹⁷ It should be obvious, however, that the "separate identity" argument can have no general application in the context of intentional torts. It is clear that directors can be jointly liable with the corporation for the one tort. In *Hoare v. Tsapralis*, Justice Ground dealt with a director who had ordered the demolition of a building.¹⁹⁸ That act, in the circumstances, constituted the tort of waste, and the director should have been held directly liable for procuring the commission of the tort. Justice Ground, citing *ScotiaMcLeod*, nevertheless excused the director because there was no evidence that he "was acting in his own interest as opposed to the interest of the corporation, that he was acting outside the scope of his employment, or in a manner inconsistent with the objects of, or interests of, [the corporation]".¹⁹⁹ As noted earlier, however, it is no excuse that the director was

¹⁹²(1996), 29 B.L.R. (2d) 298 (Ont. Gen. Div.). See also *Chenier v. Johnson* (1964), 48 D.L.R. (2d) 380 (B.C.S.C.); *Lewis v. Smith*, [1991] O.J. No. 1992 (Ont. Gen. Div.) (Q.L). Consider *1175777 Ontario Ltd. v. Magna International Inc.* (2001), 200 D.L.R. (4th) 521 (Ont. C.A.) (liability of directors of parent corporation).

¹⁹³*Ibid.* at 312.

¹⁹⁴(1996), 15 E.T.R. (2d) 79 (Ont. Gen. Div.). See also *Baltimore Aircoil of Canada Inc. v. Process Cooling Systems Inc.* (1993), 16 O.R. (3d) 324 (Ont. Gen. Div.), rev'd. (1996), 30 O.R. (3d) 159 (C.A.).

¹⁹⁵(1992), 4 C.L.R. (2d) 263 (Ont. Gen. Div.).

¹⁹⁶(1998), 84 C.P.R. (3d) (Ont. Gen. Div.). See also *Normart Management Ltd. v. West Hill Redevelopment Co.* (1998), 155 D.L.R. (4th) 627 (Ont. C.A.).

¹⁹⁷*Ibid.* at 21.

¹⁹⁸(1997), 10 R.P.R. (3d) 89 (Ont. Gen. Div.). See also *Monogram Products Inc. v. 546332 Ontario Limited* (1996), 27 O.R. (3d) 335 (Ont. Gen. Div.).

¹⁹⁹*Ibid.* at 97.

acting in the interests of the corporation.²⁰⁰ Nor is it correct in assessing director liability (outside the inducement context) to consider whether directors acted within the scope of their authority or "employment".²⁰¹ All of this obviously extends the confusion.²⁰² It is perhaps enough at this point to deprecate this leakage of the inducement confusions into the cases dealing with other intentional torts and to express the hope that it will not continue.

Perhaps the most troubling feature of the Canadian jurisprudence on intentional torts is that it represents an entirely insular collection of developments. Courts in other jurisdictions have not felt compelled to refashion this area of the law. The confusions that have afflicted the Canadian case law are generally not found in the English, Australian and New Zealand judgments. The traditional position remains firmly in place in those countries. With respect to liability for inducing a breach of contract, the current view was succinctly expressed by Master Kennedy-Grant in the New Zealand case of *Cook Strait Skyferry Ltd. v. Dennis Thompson International Ltd.*²⁰³ According to the Master, "a director may be liable for procuring a breach of contract by the company of which he or she is a director if he or she does not act bona fide or does not act within the scope of his or her authority".²⁰⁴ There is no talk in these courts of piercing the veil or of considerations such as a "dominant purpose" or a "separate identity of interest".²⁰⁵ With respect to other intentional torts, the judges are again committed to the traditional position. The English judges appear to rely heavily on the views expressed by Justice Slade in *C. Evans and Sons Ltd. v. Spritebrand Ltd.*²⁰⁶ The Australian courts rely on the English authorities to confirm that directors are personally liable if they participate in or direct the tortious

²⁰⁰ See text at note 178 *supra*.

²⁰¹ See text at notes 147, 149 *supra*. See also *Paragon Controls Ltd. v. Valtek International*, [1998] A.J. No. 58 (Alta. C.A.) (QL) where the court rejected the proposition that directors are excused from liability for intentional torts (eg. conspiracy) if they are acting within their authority.

²⁰² Query the analysis in *Lapensee v. First Choice Industries Ltd.* (1992), 46 C.P.R. (3d) 115 (Ont. Gen. Div.); *Davis v. First Choice Ltd.*, [1992] O.J. No. 1256 (Ont. Gen. Div.) (QL) and *Saratoga Utilities Ltd. v. Long*, [1998] B.C.J. No. 772 (B.C.S.C.) (QL).

²⁰³ [1993] 2 N.Z.L.R. 72 (H.C.). See also *O'Brien v. Dawson* (1941), 41 S.R. (N.S.W.) 295 (C.A.); *Holding Oil Finance Inc. v. Marc Rich & Co. A.G.*, [1996] E.W.J. No. 3653 (C.A.) (QL); *Hinds v. Uellendahl*, (Sup. Ct., N. Terr., Aust.) (12 December 1995) (unreported).

²⁰⁴ *Ibid.* at 78.

²⁰⁵ The "justification" rationale discussed in some Canadian cases is attributed to English sources. See *Polimeni v. Danzinger* (1995), 26 C.C.L.T. (2d) 256 (Man. Q.B.); *Pace v. DelZotto* (1996), 24 B.L.R. (2d) 263 (Ont. Gen. Div.).

²⁰⁶ [1995] 2 All E.R. 415 (C.A.). See: *Elite & Premiere Ltd. v. Elite Modelling Agency Ltd.*, [1996] E.W.J. No. 1297 (Ch.) (QL); *MCA Records Inc. v. Charly Records Ltd.*, [1996] E.W.J. No. 1306 (Ch.) (QL); *Farmers Build Ltd. (In Liquidation) v. Carier Bulk Materials Handling Ltd.*, [1997] E.W.J. No. 1539 (Ch.) (QL); *Springsteen v. Flute International Ltd.*, [1998] E.W.J. No. 4620 (Ch.) (QL); *BBC Worldwide Ltd. v. Pally Screen Printing Ltd.*, [1998] E.W.J. No. 4508 (Ch.) (QL); *Daido Asia Japan Co. Ltd. v. Rothen*, [2001] E.W.J. No. 3997 (Ch.) (QL).

act.²⁰⁷ The Australian courts have also explicitly rejected the *Mentmore* “wilful participation” test.²⁰⁸ None of these courts have been tempted to adopt the new tests or approaches found in some of the recent Canadian cases.²⁰⁹ In the result, and it is indeed quite stark, there is a wide divergence between the jurisprudence of these countries and that of Canada.

B. Negligence

We temporarily suspended our historical review of the negligence cases at that point (the 1980’s) when the Canadian cases on inducing a breach of contract began to reshape the jurisprudence on intentional torts. At that time, in the negligence area, the duty of care owed by directors to their corporation was still predicated on Justice Romer’s summary of the law in *Re City Equitable Fire Insurance Company, Limited*.²¹⁰ Although the judges continued to assert the supposed distinction between gross and ordinary negligence, the justification for the higher standard remained unclear.²¹¹ As for the duty of care directors owed to third parties, the cases indicated that directors were subject to the ordinary application of the general negligence (“neighbour”) principle.²¹² Since that time, in both instances, the law has shifted. We will first consider the cases dealing with the duty of care owed to the corporation.

²⁰⁷ *Kalamazoo (Aust) Pty Ltd. v. Compact Business Systems Pty Ltd.* (1985), 84 F.L.R. 101 (Qld. S.C.); *G.M. (North Melbourne) Holdings Pty Ltd. v. Young Kelly Pty Ltd.*, (F.C. Aust., Vict. Dist.) (May 27, 1986); *Australasian Performing Right Association Limited v. Valamo Pty Limited* (1990), 18 I.P.R. 216 (F.C.); *Martin Engineering Co. v. Nicaro Holdings Pty Ltd.* (1991), 100 A.L.R. 358 (F.C.); *Microsoft Corporation v. Auschina Polaris Pty Ltd.* (1996), 142 A.L.R. 111 (F.C.); *Kimberly-Clark Australia Pty Limited v. Arico Trading International Pty Limited* (1998), 42 I.P.R. 111 (F.C.); *Henley Arch Pty Ltd. v. Clarendon Homes (Aust) Pty Ltd.*, (F.C. Aust., Vict. Dist.) (July 24, 1998). Query the judgment of Lee J. in *King v. Milpurrru* (1996), 136 A.L.R. 327 (F.C.), *Private Parking Services (Vic) Pty Ltd. v. Huggard*, [1996] Aust. Torts Reports 81-396 (S.C. Vic.); where he appears to predicate liability to third parties on a director’s breach of duty to the corporation.

²⁰⁸ *Microsoft Corporation v. Auschina Polaris Pty Ltd.* (1996), 142 A.L.R. 111 (F.C.); *Henley Arch Pty Ltd. v. Clarendon Homes (Aust) Pty Ltd.*, (F.C. Aust. Vict. Dist.) (July 24, 1998). Cf. *King v. Milpurrru* (1996), 136 A.L.R. 327 (F.C.), where Beazley J. expressed his preference for the *Mentmore* test.

²⁰⁹ Consider whether it is a new confusion to extend the “assumption of responsibility” analysis applied in negligence cases to intentional torts. See text at notes 272-276 *infra*.

²¹⁰ [1925] 1 Ch. 407.

²¹¹ See, for example, *Multinational Gas and Petrochemical Co. v. Multinational Gas and Petrochemical Services Ltd.*, [1983] 2 All E.R. 563 at 587 (C.A.) (“[the distinction between negligence and gross negligence amounting to misfeasance] must, I apprehend, lie in the state of mind of the director.”); *Kuwait Asia Bank E.C. v. National Mutual Life Nominees Ltd.*, [1991] 1 A.C. 187 at 221 (H.L.) (“[directors owed] duty to perform their duties as directors without gross negligence”).

²¹² See text at notes 93-101 *supra*.

(1) *Duty of Care Owed to the Corporation*

As noted, Justice Romer's judgment remained authoritative throughout the Commonwealth for most of the twentieth century. Consequently, the standard of care expected of directors continued to be low. That appears to have changed somewhat in recent years. A few judgments suggest that there has been a perceptible judicial elevation of the common law standard.²¹³ It would seem, for example, that directors will now be liable if their failure to keep themselves appropriately informed of corporate affairs contributed to the loss. For the most part, however, recent change has involved statutory redefinition of the duty of care. Some attempts at general redefinition, it should be noted, were unsuccessful. One such attempt was the 1971 recommendation of the Dickerson committee to elevate the standard of care.²¹⁴ The recommended wording was that every director shall "exercise the care, diligence and skill of a reasonably prudent person".²¹⁵ According to the committee:

The formulation of the duty of care, diligence and skill owed by directors represents an attempt to upgrade the standard presently required of them. The principal change here is that whereas at present the law seems to be that a director is only required to demonstrate the degree of care, skill and diligence that could reasonably be expected from him, having regard to his knowledge and experience — *Re City Equitable Fire Insurance Co.* [1925] Ch. 425—under s. 9.19(1)(b) he is required to conform to the standard of a reasonably prudent man. Recent experience has demonstrated how low the prevailing legal standard of care for directors is, and we have sought to raise it significantly.²¹⁶

The proposed upgrade proved to be unacceptable to powerful interest groups, however, and the final provision was redrafted (ambiguously) to require directors to "exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances".²¹⁷ The subsequent understanding of the altered provision in some quarters was that it no longer

²¹³Exx. *Daniels v. Anderson* (1995), 37 N.S.W.L.R. 438 (C.A.); *State of South Australia v. Clark* (1996), 19 A.C.S.R. 606 (S.C.S.A.); *Soper v. Canada* (1997), 149 D.L.R. (4th) 297 (F.C.A.). See also *Re Australasian Venezolana Pty Ltd.* (1962), 4 F.L.R. 60 (S.C. Aust. Cap. Terr.); *Distribulite Ltd. v. Toronto Board of Education Staff Credit Union Ltd.* (1987), 62 O.R. (2d) 225 (Ont. H.C.).

²¹⁴Dickerson *et al.*, *Proposals for a New Business Corporations Law for Canada* (Ottawa: Information Canada, 1971). For an account of earlier reform proposals in England, see the Law Commission Consultation Paper No. 153 (Company Directors), *supra* note 50, Part 13 and the White Paper on *The Conduct of Company Directors*, (Cmd. 7037). For the Australian experience, see P. Redmond, "The Reform of Directors' Duties" (1991) 15 U.N.S.W.L.J. 86. See also the discussion in *Soper v. Canada* (1997), 149 D.L.R. (4th) 297 (F.C.A.), of the earlier attempt to upgrade the Ontario standard. See also *Byrne v. Baker*, [1964] V.R. 443 (Vic. S.C.).

²¹⁵*Ibid.* Vol. II at 74 (para. 9.19(1)(b)).

²¹⁶*Ibid.* Vol. I at 83 (para. 242).

²¹⁷*C.B.C.A., R.S., 1985, c. C.44, see 122(1)(b).*

represented or implied a significant departure from the traditional subjective common law standard.²¹⁸

Other recent reform efforts have been more successful. Statutory redefinition for particular purposes (taxation, wrongful trading, disqualification), for example, has been achieved. English,²¹⁹ Australian²²⁰ and Canadian²²¹ statutory provisions have been recognized as elevating the standard of care for specific purposes, albeit sometimes only marginally. More significantly, the statutory developments in England have had a further effect in that they have provided the foundation for what is thought by some to be an overt judicial reconstruction of the common law standard. Significant change, in this respect, only occurred with the enactment of *The Insolvency Act 1986*²²² and *The Company Directors Disqualification Act 1986*.²²³ In dealing with wrongful trading, the former statute replaced the common law standard of care with a combined objective/subjective standard.²²⁴ The latter statute, disqualified directors who were unfit, including unfitness by reason of incompetence.²²⁵ It was generally understood

²¹⁸ *Soper v. Canada* (1997), 149 D.L.R. (4th) 297 at 313 (F.C.A.) ("I am in general agreement with that assessment [that the provision established only a slightly more onerous regime than previously existed and one that retains much of its original, subjective character]"). Others insist that the standard was changed from a subjective to an objective one. See *Canada Business Corporations Act Discussion Paper: Directors' Liability* (Ottawa: Industry Canada, 1995), at 4 ("The standard of care was increased by the CBCA in 1975 from the common law subjective standard to an objective, reasonable person standard."). Consider, *Blair v. Consolidated Enfield Corp.* (1995), 128 D.L.R. (4th) 73 (S.C.C.).

²¹⁹ See notes 222-39 *infra*.

²²⁰ *Commonwealth Bank of Australia v. Friedrich* (1991), 5 A.C.S.R. 115 (Vic. S.C.); *Morley v. Statewide Tobacco Services Ltd.*, [1993] 1 V.R. 423 (C.A.); *Standard Chartered Bank of Australia Ltd. v. Antico* (1995), 38 N.S.W.L.R. 290 (S.C.); *Metropolitan Fire Systems Pty Ltd. v. Miller*, (1997), 23 A.C.S.R. 699 (F.C., N.S.W.) (25 June 1997) (unreported); *Macgregor v. Australian Securities Commission*, (1997) (Admin. Appeals Tribunal, Gen. Admin. Div.) (25 June 1997) (unreported); *Australian Securities Commission v. Donovan*, [1998] 986 F.C.A. (August 20, 1998).

²²¹ *Grindrod & District Credit Union v. Cumis Insurance Society, Inc.*, [1985] B.C.J. No. 2229 (B.C.C.A.) (QL); *Merson v. M.N.R.* (1988), 89 D.T.C. 22 (T.C.C.); *Soper v. Canada* (1997), 149 D.L.R. (4th) 297 (F.C.A.).

²²² 34-35 Eliz. II, c. 45. For a summary account of the difference between sections 212 and 214 of the Insolvency Act 1986, see *Cohen v. Selby*, [2000] E.W.J. No. 6521 (C.A.) (QL).

²²³ 34-35 Eliz. II, c. 46.

²²⁴ Sec. 214(4) of the Act is as follows:

[T]he facts which a director of a company ought to know or ascertain, the conclusions which he ought to reach and the steps which he ought to take are those which would be known or ascertained, or reached or taken, by reasonable diligent persons having both —

- (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company, and
- (b) the general knowledge, skill and experience that that director has.

²²⁵ See S. Griffin, *Personal Liability and Disqualification of Company Directors* (Oxford: Hart Publishing, 1999) c. 7.

that the new provisions were intended to protect the public by raising the standard of conduct required of directors.²²⁶

Commentators have taken the view that the new legislation provided the impetus and foundation for a general judicial reconsideration and redefinition of the common law standard of care.²²⁷ They identify Hoffman, J. as the judge largely responsible for triggering the change. Although he had expressed traditional views in an earlier case,²²⁸ he relied on the new legislation to redefine the standard, first in *Norman v. Theodore Goddard*,²²⁹ and again in *Re D'Jan of London*.²³⁰ In the *Norman* case, he simply accepted the submission of counsel that the objective test in the *Insolvency Act* was an accurate statement of the common law duty. Then, two years later, in *Re D'Jan of London*, he explicitly concluded that, in his view, "the duty of care owed by a director at common law is accurately stated in s. 214(4) of the *Insolvency Act 1986*".²³¹ It is not in fact clear, however, that Hoffman, J. appreciated that he was altering the common law standard, or that today he would agree that it is necessary to do so.²³² Nevertheless, his judgment has been taken to support a new common law threshold of care for directors.

The new statutory provisions, within their scope of operation, have in fact produced changes in the standard of care in certain respects. In the disqualification context, a number of propositions have emerged. As in the personal liability cases, directors cannot be disqualified for "commercial misjudgment",²³³ or for properly relying on others.²³⁴ They will be disqualified, however, for neglecting or ignoring their duties.²³⁵ It is no longer acceptable for directors to be nominal directors or figureheads. They must inform themselves about the affairs of the corporation. It has also been established that directors may be found unfit where they fail to file records and returns or produce (or read and

²²⁶ *Re Barings plc; Secretary for Trade v. Baker*, [1999] 1 B.C.L.C. 433 (Ch.); *Re Landhurst Leasing plc*, [1999] 1 B.C.L.C. 286 (Ch.).

²²⁷ Griffin, *supra* note 225 at 27-28; E. Ferran, *Company Law and Corporate Finance* (Oxford: Oxford University Press, 1999) at 216-17; A. Walters, "Directors Duties: The Impact of the Company Directors Disqualification Act 1986" (2000) 21 Comp. Lawy. 110; P. Loose, M. Griffiths & D. Impey, *The Company Director: Powers, Duties and Liabilities*, 8th ed. (Bristol: Jordans, 2000) at 152-53.

²²⁸ *Re Dawson Print Group Ltd.*, [1987] B.C.L.C. 601 (Ch.).

²²⁹ [1991] B.C.L.C. 1028 (Ch.).

²³⁰ [1994] 1 B.C.L.C. 561 (Ch.).

²³¹ *Ibid.* at 563.

²³² See Lord Hoffmann's remarks on the occasion of the fourth Sainer Lecture, published at (1997) 18 Comp. Lawy. 194.

²³³ *Re Lo-Line Electric Motors Ltd.*, [1988] B.C.L.C. 698 (Ch.); *Re CU Fittings Ltd.*, [1989] B.C.L.C. 556 (Ch.).

²³⁴ *Norman v. Theodore Goddard*, [1991] B.C.L.C. 1028 (Ch.).

²³⁵ *Re Park House Properties Ltd.*, [1997] 2 B.C.L.C. 530 (Ch.); *Re Westmid Packing Services Ltd.*, [1998] 2 All E.R. 124 (C.A.); *Re Kaytec International plc.*, [1999] 2 B.C.L.C. 351 (C.A.); *Re Galeforce Pleating Co. Ltd.*, [1999] 2 B.C.L.C. 704 (Ch.).

understand) accounts.²³⁶ These latter propositions, it should be apparent, represent a departure from the older liability cases and possibly would be of considerable significance when negligence of that kind constitutes the basis for a common law claim for damages against directors personally.

Two other aspects of the disqualification cases are important for their reflection or replication of earlier judicial analyses. One feature is the adoption of a high negligence threshold for disqualification. In some of the early disqualification cases, the judges asserted a requirement for "gross" incompetence.²³⁷ In later cases, this became a requirement for a "serious", "high" or "marked" degree of incompetence.²³⁸ No clear justification was offered for this liability threshold for some time. Recently, however, in *Re Barings plc*, Jonathan Parker, J. stated the "reason for that is the serious nature of the disqualification order, including the fact that . . . the order will prevent the respondent being concerned in the management of any company".²³⁹ This would seem to be a weak rationale, however, given that a disqualification order is intended, once serious misconduct is established, to achieve that very result (ie. remove the director from management).

The second feature is the routine reference in the cases to the need to disqualify directors in order to discourage abuse of the privilege of limited liability.²⁴⁰ In *Secretary of State v. Ettinger*, for example, Nicholls, V.C. stated:

Limited liability is a valuable tool in the promotion of trade and business, but it must not be misused. Those who make use of limited liability must do so with a proper sense of responsibility. The directors' disqualification procedure is an important sanction introduced by Parliament to raise standards in this regard. Those who take advantage of limited liability must conduct their companies with due regard to the ordinary standards of commercial morality.²⁴¹

In *Secretary of State v. Gray*, Neill, L.J. insisted that those "who trade under the regime of limited liability and who avail themselves of the privileges of that regime, must accept the standards of probity and competence to which the law requires company directors to conform".²⁴² The assumption these and other

²³⁶ *Re Cladrose Ltd.*, [1990] B.C.L.C. 204 (Ch.); *Secretary of State v. Ettinger*, [1993] B.C.L.C. 896 (C.A.); *Re Firedart Ltd.*, [1994] 2 B.C.L.C. 340 (Ch.); *Re Continental Assurance Co. of London plc*, [1997] 1 B.C.L.C. 48 (Ch.).

²³⁷ *Re Dawson Print Group Ltd.*, [1987] B.C.L.C. 601 (Ch.); *Re Lo-Line Electric Motors Ltd.*, [1988] B.C.L.C. 698 (Ch.).

²³⁸ *Re Sevenoaks Stationers (Retail) Ltd.*, [1991] 3 All E.R. 578 (C.A.); *Re Barings plc*, [1999] 1 B.C.L.C. 433 (Ch.).

²³⁹ [1999] 1 B.C.L.C. 433 at 484 (Ch.).

²⁴⁰ See, for example, *Re Stanford Services Ltd.*, [1987] B.C.L.C. 607 (Ch.); *Re Westmid Packing Services Ltd.*, [1998] 2 All E.R. 124 (C.A.).

²⁴¹ [1993] B.C.L.C. 896 at 899 (C.A.).

²⁴² [1995] 1 B.C.L.C. 276 at 289 (C.A.).

²⁴³ See text at notes 2-33 *supra*.

²⁴⁴ Law Commission Consultation Paper No. 153 (Company Directors), *supra* note 50.

²⁴⁵ S. Deakin & A. Hughes, *Directors' Duties: Empirical Findings, Report to the Law Commissions*, ESRC Centre for Business Research, University of Cambridge, 1999.

judges seem to be operating under is that directors have a statutory limited liability akin to that of shareholders. As we have seen, that is simply incorrect.²⁴³

The most recent development relating to the duty of care that directors owe to their corporate principals is the English Law Commission consultation paper on directors duties.²⁴⁴ The Commission is contemplating a general statutory redefinition of the standard of care. In the consultation paper, the Commission briefly reviewed a few cases and then canvassed what it understood were the advantages and disadvantages of possible alternatives to the traditional common law standard of care. No specific recommendations were made. The Commission instead undertook to conduct empirical research on the issue. That research, consisting primarily of a survey of the views of directors, was published in a 1999 report.²⁴⁵ Respondents to the survey favored replacing the traditional common law standard with a combined objective/subjective alternative.²⁴⁶ This kind of "preference" data, however, is of limited utility. The issue of the standard of care is one of public policy, and not one simply for the directors to determine for themselves. It is for the relevant community to set the default liability terms upon which individuals may serve as directors. The issue, once again, is whether directors should be treated differently from all other actors with respect to their tort liability exposure.

(2) *Duty of Care Owed to Third Parties*

By the late 1980's, it could fairly be concluded that the "neighbour" principle (itself a developing concept) determined whether a director owed a duty of care to a third party.²⁴⁷ The only significant qualification of this liability involved a parallel development on the question of the recovery of economic loss. Courts across the Commonwealth had expressed concerns with negligence claims by third parties for economic loss. In *Hedley Byrne & Co. Ltd. v. Heller & Partners Ltd.*, the House of Lords had accepted the possibility of recovery for economic loss for negligent misstatement.²⁴⁸ After a good deal of judicial discussion in the years following the decision,²⁴⁹ the House concluded in *Henderson v. Merrett Syndicates Ltd.* that economic loss was recoverable if there had been an "assumption of responsibility".²⁵⁰ According to Lord Goff,

²⁴⁶The authors of the survey, *ibid.* (see Table 14) framed this alternative as follows: "[A] director would owe the company a duty to exercise the care, skill and diligence which would be exercised in the same circumstances by a reasonable person having both the knowledge and experience that might be reasonably expected of a person in the same position as a director, and the knowledge and experience which that director had."

²⁴⁷See text at notes 93-101 *supra* and cases at note 269 *infra*. Consider *Aird v. Harmony House of Kirkland Lake*, [2001] O.J. No. 2988 (Ont. Sup. Ct.) (QL).

²⁴⁸[1963] 2 All E.R. 575 (H.L.); Cf. *Derry v. Peek* (1889), 14 A.C. 337 (H.L.).

²⁴⁹See *Murphy v. Brentwood District Council*, [1990] 2 All E.R. 908 (H.L.); *Caparo Industries plc v. Dickman*, [1990] 1 All E.R. 568 (H.L.).

²⁵⁰[1994] 3 All E.R. 506 (H.L.).

Hedley Byrne had “established that, in certain circumstances, a duty of care may exist in respect of words as well as deeds, and further that liability may arise in negligence in respect of pure economic loss which is not parasitic upon physical damage”.²⁵¹ The rationale offered by Lord Goff was that “the concept provides its own explanation why there is no problem in cases of this kind about liability for pure economic loss; for if a person assumes responsibility to another in respect of certain services, there is no reason why he should not be held liable in damages for that other in respect of economic loss which flows from the negligent performance of these services”.²⁵² A few years later, in *Williams v. Natural Life Health Foods Ltd.*, the House of Lords specifically confirmed the application to directors of the “assumption of responsibility” test for third party economic loss claims in negligence.²⁵³

The decision in *Williams* was not unexpected. It was only a specific application of the general principle confirmed in *Henderson*. The decision had also been anticipated by a number of earlier cases arising in other jurisdictions. In *Kuwait Asia Bank E.C. v. National Mutual Life Nominees Ltd.*, a Privy Council case out of New Zealand, Lord Lowry observed that “although directors are not liable *as such* to creditors of the company, a director may by agreement or representation assume a special duty to a creditor of the company”.²⁵⁴ That same possibility was recognized in the Scottish case of *Nordic Oil Services Ltd. v. Berman*.²⁵⁵ Of particular significance, however, was the decision of the New Zealand Court of Appeal in *Trevor Ivory Ltd. v. Anderson*.²⁵⁶ Although the analysis in that case is flawed in a number of respects,²⁵⁷ the court did clearly accept that the test for the recovery of loss

²⁵¹ *Ibid.* at 518.

²⁵² *Ibid.* at 521.

²⁵³ [1998] 1 W.L.R. 830 (H.L.). See also *Burns v. Shuttlehurst Ltd.*, [1999] 2 All E.R. 27 (C.A.); *Hamble Fisheries Ltd. v. L. Gardner & Sons Ltd.*, [1998] E.W.J. No. 3530 (C.A.) (QL).

²⁵⁴ [1991] 1 A.C. 187 at 219 (P.C.).

²⁵⁵ [1993] S.L.T. 1164 (Ct. Sess.).

²⁵⁶ [1992] 2 N.Z.L.R. 517 (C.A.).

²⁵⁷ Concerns with the analysis in the case include (1) Justice Cooke’s facile discounting of several earlier cases, (2) his misguided view (*ibid.* at 523) that it “behoves the Courts to avoid imposing on the owner of one-man company a personal duty of care which would erode the limited liability and separate identity principles associated with the names of Salomon and Lee”, (3) his view (shared by Justice Hardie Boys) that attribution of the acts of directors to the corporation meant that *prima facie* only the corporation should be liable and (4) his suggestion that incorporation *per se* amounts to an effective unilateral declaration of limited liability with respect to personal tort liability exposure. See the critical comments of D. Wishart, “Anthropomorphism Rampant: Rounding Up Executive Directors’ Liability” [1993] N.Z.L.J. 175 and “The Personal Liability of Directors in Tort” *supra* note 135 ; G. Fridman, “Personal Tort Liability of Company Directors” (1992) 5 C.L.R. 41; G. Shapira, “Liability of Corporate Agents: *Williams v. Natural Life Ltd.* in the House of Lords” *supra* note 124; P. Watts, “The Company’s Alter Ego — A Parvenu and Imposter in Private Law” [2000] N.Z.L.R. 137 and “The Company’s Alter Ego — An Imposter in Private Law” *supra* note 135.

caused by negligent directors was whether there had been an "assumption of responsibility." In *Williams*, in any event, the application of the assumption of responsibility test was apparently not in dispute. Speaking for a unanimous House, Lord Steyn stated that:

It is clear, and accepted by counsel on both sides, that the governing principles are stated in the leading speech of Lord Goff of Chieveley in *Henderson v. Merrett Syndicates Ltd.* [1995] 2 A.C. 145. First, in *Henderson's* case it was settled that the assumption of responsibility principle enunciated in *Hedley Byrne & Co. Ltd. v. Heller & Partners Ltd.* [1964] A.C. 465 is not confined to statements but may apply to any assumption of responsibility for the provision of services. The extended *Hedley Byrne* principle is the rationalization or technique adopted by English law to provide a remedy for the recovery of damages in respect of economic loss caused by the negligent performance of services.²⁵⁸

This is not the place to evaluate the *Williams* decision.²⁵⁹ The question of the recoverability of pure economic loss is a general one in tort law. Whether or to what extent such loss should be recoverable is a policy issue of wide scope.²⁶⁰ In

²⁵⁸ [1998] 1 W.L.R. 830 at 834 (H.L.).

²⁵⁹ One ancillary aspect of the judgment must, however, be mentioned. Lord Steyn's obiter comments negating the joint tortfeasor characterization require clarification in view of, among other things, the common understanding that the vicarious liability of principals makes them joint tortfeasors with their agents. See *The Koursk*, [1924] P. 140; *New Zealand Guardian Trust Co. Ltd. v. Brooks*, [1995] 1 W.L.R. 96 (P.C.). See also J. Lowry & R. Edmunds, "Personal Liability of Company Directors" (1998) 77 Can. Bar Rev. 467.

²⁶⁰ The argument most commonly offered to restrict recovery of economic loss is that of "indeterminate" exposure. According to Justice Cardozo in *Ultramares Corporation v. Touche*, 174 N.E. 441 at 444 (NY App 1931), the mischief would be "liability in an indeterminate amount for an indeterminate time to an indeterminate class." This concern, however, is of little real significance for at least three reasons. First, the objection is essentially that quantum, time and class are unpredictable or open-ended. This may be so in limited respects at any particular point in time and from time to time. The concern, however, evaporates at the same rate the law is clarified or given greater definition. In other words, the indeterminacy concern has no significant implication for the content of the legal regime (eg. the determination of the boundaries of the class). The extent to which recovery for the negligent infliction of economic loss should be permitted is a question of content. The second reason is that, before the fact, every loss is an indeterminate one, both in terms of initial damage and impact over time. Different people suffer different losses and suffer losses differently. The quantification of the actual loss (after applying general causation and remoteness limitations) must await the crystallization (actual or projected) of the particular damage caused by the tortious conduct. That sort of indeterminacy is unavoidable. Thirdly, the law has established general quantum and temporal caps on liability. Quantum is capped at the level of personal bankruptcy (in practical operation, a relatively generous second chance) and time is capped by limitation periods. These caps operate to limit liability in hundreds of thousands of instances every year. The indeterminacy concern, for these and other reasons, is largely an empty one. It may be added that judges appear to be relatively comfortable in dismissing or discounting the indeterminacy concern on the facts. See *Rivtow Marine Ltd. v. Washington Iron Works*, (1973), 40 D.L.R. (3d) 530 (S.C.C.); *Smith v. Eric S. Bush* (a firm), [1989] 2 All E.R. 514 (H.L.); *Hercules Managements Ltd. v. Ernst & Young* (1997), 146 D.L.R. (4th) 577 (S.C.C.); *NBD Bank, Canada v. Dofasco Inc.* (1999), 181 D.L.R. (4th) 37 (Ont. C.A.), leave to appeal refd. (2000), 183 D.L.R. (4th) vii (S.C.C.).

the particular case of directors, there does not appear to be anything about their circumstances that would make their stake in the matter distinct from that of any other actor.²⁶¹ Their liability in this respect will therefore be determined by the general considerations brought to bear on the issue in that wider discussion.

A number of observations are nevertheless in order with respect to this development. The first is that the assumption of responsibility test is applied only to negligence claims for pure economic loss.²⁶² The courts have explicitly denied its application to claims for economic loss associated with personal injury or damage to property.²⁶³ It is said, with a confidence that belies the controversy associated with the issue, that the "infliction of physical injury to the person or property of another universally requires to be justified. The causing of economic loss does not".²⁶⁴ Presumably, therefore, these circumstances (injury to person or property) will continue to be governed by the traditional "neighbour" test of duty. The second observation is that, due to the aforementioned fragmentation of the law and other substantive concerns, the reception of the assumption of responsibility test in some cases has been equivocal or critical. Both the general question of recovering for pure economic loss and the specific question of the appropriateness of the assumption of responsibility test remain controversial in England.²⁶⁵ Given this reaction, it may well be that the assumption of responsibility notion is not the final answer to the economic loss question. For the moment, however, it is the formal English position in so far as directors are concerned.

In Canada, although the courts are also struggling with the economic loss question,²⁶⁶ they seem oblivious to the English developments relating to

²⁶¹ A point that appears to be conceded by Lord Steyn (*supra* note 258 at 835).

²⁶² Some commentators seem to assume that the *Williams* decision is of general application, rather than only to claims of economic loss. See R. Grantham & C. Rickett, "Directors' 'Tortious' Liability: Contract, Tort or Company Law?" (1999) 62 Mod. L. Rev. 133; S. Griffin, "Company Director's Personal Liability in Tort" (1999) 115 L.Q.R. 36.

²⁶³ *Murphy v. Brentwood District Council*, [1990] 2 All E.R. 908 (H.L.); *Mobil Oil Hong Kong Ltd. v. Hong Kong United Dockyards Ltd.*, [1991] 1 Lloyd's L.R. 309 (P.C.); *Bellefield Computer Services Ltd. v. E. Turner & Sons Ltd.*, [2000] E.W.J. No. 320 (C.A.) (QL).

²⁶⁴ *Murphy v. Brentwood District Council*, [1990] 2 All E.R. 908 at 934 (H.L.). See also *Mobil Oil Hong Kong Ltd. v. Hong Kong United Dockyards Ltd.*, [1991] 1 Lloyd's L.R. 309 at 328-29 (P.C.) ("In most claims in respect of physical damage to property the question of the existence of a duty of care does not give rise to any problem, because it is self-evident that such a duty exists and the contrary view is unarguable.")

²⁶⁵ Consider *Bellefield Computer Services Ltd. v. E. Turner & Sons Ltd.*, [2000] E.W.J. No. 320 (C.A.) (QL); *Merrett v. Babb*, [2001] 3 W.L.R. 1 (C.A.); *Parkinson v. St. James and Seacroft University Hospital NHS Trust*, [2001] E.W.J. No. 1761 (C.A.) (QL). See also the earlier critical comments in *Smith v. Eric S. Bush* (a firm), [1989] 2 All E.R. 514 (H.L.); *Caparo Industries plc v. Dickman*, [1990] 1 All E.R. 568 (H.L.).

²⁶⁶ See *Hercules Managements Ltd. v. Ernst & Young* (1997), 146 D.L.R. (4th) 577 (S.C.C.); *Martel Building Ltd. v. Canada* (2000), 193 D.L.R. (4th) 1 (S.C.C.); *Blacklaws v. Morrow* (2000), 187 D.L.R. (4th) 614 (Alta. C.A.).

director liability for negligence claims by third parties.²⁶⁷ Specifically, the *Williams* case has yet to have a discernable impact.²⁶⁸ The Canadian cases are a mixed bag in terms of cogent analysis. While there are cases that apply the standard "neighbour" analysis,²⁶⁹ there are several others that are infected with some of the confusions generated in the intentional tort cases.²⁷⁰ There is no reason for this other than that the Canadian jurisprudence has become so muddled by these ubiquitous confusions that it is difficult for judges and counsel to find clarity even with a great deal of effort. One consequence may be that counsel will simply adopt other means (eg. the oppression remedy)²⁷¹ to frame and pursue questions of director liability.

There is one other English development that is conveniently discussed at this juncture. It is an issue respecting liability for intentional torts. It is addressed here because it involves the potential scope of application of the "assumption of responsibility" test considered above in the negligence context. In *Standard Chartered Bank v. Pakistan National Shipping Corporation (No. 2)*, it was found as a fact that a director had orchestrated the fraudulent tendering of falsely dated bills of lading.²⁷² Normally a finding of direct involvement in the

²⁶⁷ It may be that Canadian courts have simply ignored the English developments because of the controversy or because of the different Canadian approach to negligence claims. Canadian courts have continuously applied the two-fold test in *Anns v. Merton London Borough*, [1977] 2 All E.R. 492 (H.L.). See *NBD Bank, Canada v. Dofasco Inc.* (1999), 181 D.L.R. (4th) 37 (Ont. C.A.), leave to appeal refd. (2000), 183 D.L.R. (4th) vii (S.C.C.). *Cooper v. Hobart* (2001), 206 D.L.R. (4th) 195 (S.C.C.).

²⁶⁸ The decision has been cited in very few of the numerous Canadian cases. See *Millgate Financial Corp. v. B.F. Realty Holdings Ltd.* (1998), 28 C.P.C. (4th) 72 (Ont. Gen. Div.).

²⁶⁹ *Medina v. Danbury Sales (1971) Ltd.*, [1991] O.J. No. 2225 (Ont. Gen. Div.) (QL); *Hall-Chem Inc. v. Vulcan Packaging Inc.* (1994), 12 B.L.R. (2d) 274 (Ont. Gen. Div.); *British Columbia v. R.B.O. Architecture Inc.* (1994), 27 C.P.C. (3d) 80 (B.C.C.A.); *Nairne v. Wagon Wheel Ranch Ltd.*, [1995] O.J. No. 1234 (Ont. Gen. Div.) (QL), affd. [1998] O.J. No. 533 (Ont. C.A.) (QL); *NBD Bank, Canada v. Dofasco Inc.* (1999), 181 D.L.R. (4th) 37 (Ont. C.A.), leave to appeal ref'd. (2000), 183 D.L.R. (4th) vii (S.C.C.); *Anger v. Berkshire Investment Group Inc.*, [2001] O.A.C. 301.

²⁷⁰ *Leon Kentridge Associates v. Save Toronto's Official Plan Inc.*, [1990] O.J. No. 488 (Ont. Dist. Ct.) (QL); *Hopwood v. 927463 Ontario Ltd.*, [1995] O.J. No. 3184 (Ont. Gen. Div.) (QL); *Highbern Holdings Inc. v. Ronzino*, [1994] O.J. No. 2035 (Ont. Gen. Div.) (QL); *Power Contracting Inc. v. Falby*, (1995), 20 C.L.R. (2d) 100 (Ont. Gen. Div.); *ScotiaMcLeod v. Peoples Jewellers Limited* (1995), 129 D.L.R. (4th) 711 (Ont. C.A.); *McKinlay Transport Ltd. v. Motor Transport Industrial Relations Bureau of Ontario (Inc.)*, (1996), 96 C.L.L.C. 210 (Ont. Gen. Div.); *Toronto Dominion Bank v. Alfred*, (1996), 28 C.L.R. (2d) 163 (Ont. Gen. Div.); *Rushton v. Condominium Plan No. 8820668*, (1997) 202 A.R. 299 (Alta. Q.B.). See also *MacEwen Petroleum Inc. v. Petro-Canada*, [2001] O.J. No. 2362 (Ont. Sup. Ct.) (QL).

²⁷¹ Consider *Budd v. Gentra* (1998), 43 B.L.R. (2d) 27 (Ont. C.A.); *American Reserve Energy Corp. v. McDorman* (1999), 48 B.L.R. (2d) 167 (Nfld. S.C.); *Comtrade Petroleum Inc. v. Ziering*, [2001] O.T.C. 555 (Ont. Sup. Ct.).

²⁷² [2000] 1 Lloyd's L.R. 218 (C.A.).

fraudulent act would have resulted in personal liability for the director.²⁷³ The Court of Appeal, however, concluded that because the director made the fraudulent representations on behalf of the corporation, only the corporation could be liable. That reasoning, it should now be appreciated, is simply mistaken. On the authorities, the fact that an act is authorized does not excuse (outside the inducement context) the personal tort responsibility of a director.²⁷⁴

Of more significance to the immediate discussion is that Justice Aldous went on to insist that the assumption of responsibility test confirmed in *Williams* for negligence claims of economic loss was equally applicable to intentional torts. Referring to *Williams*, Justice Aldous, stated:

In those quoted passages, Lord Steyn had in mind that the cause of action relied on was negligence. However the principles stated are applicable to other torts, in particular to deceit. There must be an assumption of responsibility such as to create a special relationship by the plaintiff with the director or employee himself. Whether that exists is to be judged objectively with the primary focus on things said and done by the director or employee. It is necessary to enquire whether the director conveyed directly or indirectly to the plaintiff that he assumed a personal responsibility towards the plaintiff.²⁷⁵

This is a bold, but flawed, assertion. No “special relationship” is required in the ordinary case to establish liability for intentional torts. It is enough to prove the elements of the particular tort. No considerations peculiar to directors appear to suggest a different conclusion. As it happened, the views of Justice Aldous soon attracted critical commentary from his own court. In *SX Holdings Ltd. v. Synchronet Ltd.*, Justice Potter offered the following observations:

Mr. Ashton has argued with force that, in cases of fraud and deceit, it is by no means easy to see as a matter of policy or logic why the hegemony to be accorded to the principle of company law concerning the separate personality of companies should lead to a ‘let out’ of this kind for an individual who knowingly defrauds another in the name of a company in which he is interested, for his own financial benefit. Whereas liability for negligence is a liability imposed in respect of inadvertent damage caused to one’s ‘neighbour’ and/or upon the postulate that the defendant has assumed a personal responsibility towards an injured claimant, liability in deceit is imposed on the basis of harm deliberately (or recklessly) caused by a representor to a ‘targeted’ representee. In this connection I observe that, in another context, Lord Steyn has made clear the strength of the rationale, in terms of deterrence and morality, which underlies the imposition of wider personal liability upon a defendant who is an intentional wrongdoer than that which is imposed upon one less blameworthy in the sliding scale of civil damages: see the Smith New Court case at p. 279. Thus there is much to be said for the view that there are strong countervailing reasons of policy why personal liability should not be avoided simply on the basis that the representation was purportedly made, and understood to be made, in the representor’s capacity as a company director, particularly when he is the controlling shareholder and moving

²⁷³ The argument was technically unavailable to the plaintiff because of a failure to plead and the refusal of the court to allow an amendment.

²⁷⁴ See authorities at notes 147, 201 *supra*.

²⁷⁵ *Supra* note 272 at 235 (C.A.).

spirit in relation to that company, use of whose name is adopted as part and parcel of his own fraudulent scheme.²⁷⁶

Justice Potter has here essentially reiterated the prevailing view that performing the tortious act with authority does not release an actor from personal liability and that the assumption of responsibility test has no general relevance or application to intentional torts.²⁷⁷

C. *Fragmentation*

This completes our review of the cases. It is apparent that the area is fragmented in a number of ways. The standard of care expected of directors varies depending on whether the common law or a statutory standard is involved. The standard of care is also different depending on whether it is owed to the corporation or to third parties. In the case of intentional torts, a new test applied originally in cases of patent infringement (wilful participation) has been haphazardly extended to other torts. Two other new tests (dominant purpose, identity of interest) were initially formulated for the tort of inducing a breach of contract, but have subsequently found their way into the cases dealing with negligence and other intentional torts. Another kind of fragmentation is based on the nature of the loss. Pure economic loss resulting from intentional torts is recoverable. If the economic loss is instead the result of negligence, it may be recovered when suffered by the corporation, but not where suffered by third parties, unless associated with damage to the person or property of the third parties. Finally, there is fragmentation amongst jurisdictions. The novel tests fashioned in Canada have not been generally adopted elsewhere. There may also be a difference with respect to the recovery of economic loss depending on whether the *Anns* or *Murphy* approach is ascendent in a given jurisdiction. Given this fragmentation, and much of it unjustified, it is not difficult to understand the sense of disorder, confusion and complication found in the area.

The obvious solution to a problem of fragmentation, unless that fragmentation is justified, is to consolidate. A significant degree of consolidation would occur spontaneously if the courts recognized that the liability of directors for inducing a breach of contract is solely a question of authority. Such recognition would render redundant the novel tests ostensibly developed to control the availability of that tort claim. Those tests presumably could then be expunged from the jurisprudence, including from those other areas into which they have leaked (i.e. other intentional torts, negligence claims by third parties). That would eliminate the fragmentation in the Canadian cases as well as the fragmentation between Canada and other common law countries. Other consolidations (eg. in the conceptual approach to economic loss) could eventually further reduce the

²⁷⁶ [2000] E.W.J. No. 5156 at para. 25 (C.A.) (QL).

²⁷⁷ See *Daido Asia Japan Co. Ltd. v. Rothen*, [2001] E.W.J. No. 3997 (Ch.) (QL) and P. Watts, "The Company's Alter Ego — An Imposter in Private Law" *supra* note 135.

fragmentation. At some point, directors would be liable in all jurisdictions for their negligence or intentional torts in the same way as all other actors. That would be the preferred position unless special considerations unique to directors require a different treatment. We turn now to examine the arguments others have offered to defend and justify the preferential liability position of directors.

VIII. *The Justification Question*

It should be clear at this point, notwithstanding the numerous cases where judges wrongly assume the matter to be a question of separate entity status or piercing the veil, that directors do not have a limited liability equivalent to that of shareholders. The liability assignments of shareholders and directors may *look* the same in significant respects (limited contractual liability, open personal tort liability, limited vicarious liability), but they are constructed on different foundations. The limited liability of shareholders is statutory and premised largely on their operational passivity. In contrast, the foundation for the liability rules applied to directors is the common law of agency. The relevant rules of that liability regime are familiar. Directors have limited contractual liability because their relationship with the corporation and third parties is a disclosed agency. Where the agency is undisclosed, they have open contractual liability. Liability for their own negligent conduct, like that of other agents, is open. They have no vicarious liability for the tortious acts of other workers. They are personally liable, however, if they direct or participate in the intentional torts of other workers. This entire array of agency liability assignments is informed by the risk regulation norm. Nothing we have seen in the jurisprudence, apart from the obvious confusions, suggests that this norm is inapplicable or inappropriate in the context of the tort liability of directors.

While formally recognizing the open tort liability of directors, some judges have tinkered with the content of the liability assignments. Although it may be changing, directors have been held to a low standard of care relative to the corporation. As well, in Canada, directors will escape liability for inducing a breach of contract if the novel tests (i.e. dominant purpose, identity of interest) recently introduced into the case law are not satisfied. Directors may also be excused their intentional torts by the *Mentmore* “wilful participation” test. Additionally, the volume of the jurisprudence, its confusion, warnings about tactical pleading and the idea that a piercing of the corporate veil is involved all tend to frustrate or intimidate judges, and likely generate or contribute to a reluctance to impose personal liability on directors. Collectively, this amounts to a significant degree of special treatment for directors. The question is then one of justification. What, if anything, justifies this special treatment? We have partially addressed that question at different points in the preceding discussion. We now focus more closely on the policy question.

Directors are exposed to three general kinds of civil liability — liability for negligence, liability for intentional torts and liability for breaches of statutory

obligations. The content of the liability rules for each of these classes of liability is potentially determined by different policy considerations. The analysis is simplified here, however, because of the restricted scope of the discussion. First, it is unnecessary to test the specific policy considerations that may be relevant to the various statutory obligations imposed on directors. Our subject matter is limited to common law tort liability. Secondly, there may not be a material controversy in the intentional tort context. The different treatment directors enjoy with respect to intentional torts has largely come about because of conceptual confusion over a supposed conflict between corporate law and tort law, the application of the "piercing" notion and a failure to properly comprehend the operation of the tort of inducing a breach of contract. These are simply confusions or mistakes, rather than relevant policy considerations. The response to such mistakes is to recognize them and arrange for their correction. Still, some of the suggested policy considerations examined below, if valid, imply a general relief that would include special treatment in relation to intentional torts. Thirdly, the policy considerations ostensibly limiting recovery for pure economic loss need not be investigated here. Whatever those policy considerations might be, they are not specific to directors. The extent to which limits on the recovery of pure economic loss are justified is a broader question for separate review. Accordingly, the following discussion will focus on the policy considerations said to be relevant to tort loss other than pure economic loss.

Before addressing the specific policy considerations, it is important to make one general observation about what is at stake in this discussion. The substantive issue is the content of the default liability structure we wish to install in this context. The general default rule with respect to negligence is that actors owe a duty of care to those identified by the law as their "neighbours." The default standard of care associated with this duty is that of the reasonable person. The general rule with respect to intentional torts is that actors are liable to those who are able to establish the elements of a particular tort. The current liability assignments for directors conflict with these general default rules in the ways discussed above. The default tort liability rules for directors, in other words, differ from (and displace) the general default regime applied to all other actors. The question is whether there is anything to justify this different default position. That question is of greater significance in the tort context than in the contractual setting. If an interaction between parties is contractual or voluntary, the content of the default liability rules can be adjusted *ex ante* by those parties to reflect their relative willingness to bear (or insure against) tort losses. That sort of negotiation is normally not practicable or contemplated in the tort context. Tort victims commonly suffer their injury as an accident (negligence) or as a target (intentional torts), and prior negotiation is unlikely in either case (except where the victim is the corporation). Consequently, while it is important to craft the right default rule for contractual interactions, it is critical to do so in the tort context.

We begin the policy discussion by briefly noting the implications to be derived from an economic analysis and from the availability of insurance cover.

The economic analysis of liability assignments generally confirms the efficiency of the risk regulation norm. On the specific issue of the tort liability of directors, however, there is little written, and as yet no definitive analysis.²⁷⁸ Commentators have tended to concentrate on the efficiency of holding *shareholders* liable for tort losses.²⁷⁹ The conclusion is that shareholder liability for tort loss can be justified in certain respects. Extrapolation of that analysis from the typical passive shareholder to the typical risk-projecting director indicates that open tort liability for *directors* is justified. The position of directors relative to third party victims gives them superior information for the purposes of risk-bearing and risk-shifting. Happily, this corresponds with their current actual open tortious liability. There is no compelling economic argument, in any event, that directors as such should receive special treatment relative to other actors exercising comparable management functions. To the extent such an argument depended on secondary *ex post* considerations (eg. risk-bearing, risk-shifting), it would be insufficient to displace the primary social policy of risk regulation. The latter policy intentionally imposes a cost on actors in order to discipline their risk-taking, irrespective of their subsequent capacity either to bear the loss or to shift it to others.²⁸⁰

The availability of liability insurance has been a significant factor in discussions of director liability. Concern that it would cease to be available for certain potential liabilities, for example, led to calls for a general contraction of liability for directors.²⁸¹ The "insurance crisis" that propped up this argument, however, was an over-reaction and, in any event, temporary. It may also be doubted that the insurance market would disappear. Prices may change (the expected response to a liability revision), but the market will remain. Beyond that, the idea that *ex post* insurance considerations should drive the design of substantive liability assignments is flawed. The true practical implication of liability insurance is rather different. The availability of insurance cover actually demonstrates that claims of special treatment for directors are barren. Like other actors, directors (or their corporations) may insure against tort losses. The cost of that insurance, as in the case of other actors, will properly reflect the expected damages particular directors will inflict on their victims (the corporation and third parties). Losses will thereby ultimately be internalized to the corporation or industry in question. This ability to avoid the loss by prior contractual arrangement simply dissolves the claim for special treatment. All actors have

²⁷⁸ See Daniels, *supra* note 42; C. Gosnell, "The Personal Liability of Corporate Agents: Who Should Bear Pure Economic Losses?" (1997) 55 U.T. Fac. L.R. 77.

²⁷⁹ See the articles at note 35 *supra*. See also D. Goddard, "Corporate Personality — Limited Recourse and its Limits" c. 2 in C. Rickett & R. Grantham, eds., *Corporate Personality in the Twentieth Century* (Oxford: Hart Publishing, 1998).

²⁸⁰ See an application of this proposition in Flannigan, *infra* note 282.

²⁸¹ R. Daniels & S. Hutton, "The Capricious Cushion: The Implications of the Directors' and Officers' Insurance Liability Crisis on Canadian Corporate Governance" (1993) 22 Can. Bus. L.J. 182; S. Ansell, "Directors' and Officers' Liability Insurance — Recent Reforms and Developments in Australia and New Zealand" (1995) 23 A.B.L.R. 164.

the same opportunity to contract away the responsibility initially assigned to them for personally causing a loss. Having said this, however, it must be understood that the availability of insurance can not properly be used to justify or condemn the original liability assignment.²⁸² Nevertheless, as a practical matter, the effect of insurance is to discount the claim for special treatment.

A. Recruitment

Numerous policy arguments have been advanced to justify limited tort liability for directors. The most frequently proffered is the recruitment argument. This is a generic argument that for the past century has been found in close proximity to any proposal to hold directors personally liable.²⁸³ It is equally congenial to the immunity claim for each of the civil liability classes. The proposition is that able persons will be deterred from serving as directors by the prospect of personal liability. Corporations and, in turn, the community, will suffer serious consequences as a result. As a justification, however, this proposition does not carry much freight. Indeed, it teeters on the brink of puerility. It may initially be observed that the argument only has relevance for a small subclass of directors. For most corporations, directors will not have the option of vacating or declining the office. The majority of corporations are small or family undertakings where major shareholders necessarily assume the management function of directors. The recruitment proposition therefore applies primarily at the level of larger corporations looking for executive and independent directors.²⁸⁴ Accordingly, if this is the justification, the law has

²⁸² See R. Flannigan, "Enterprise Control: The Servant — Independent Contractor Distinction" (1987) 37 U.T.L.J. 25 at 35:

Insurance is merely an ex post facto consideration for a person who is potentially subject to an insurable liability. Insurance follows liability: it can hardly be used to create or justify liability. Another observation relates to the effect of the insurance function. The fact is that it is the manifest function of insurance to distribute the risk of potential liability. That this may reduce the effectiveness of a legal rule concerned with risk regulation, however, is no criticism of the rule itself. Rather, to the extent that the efficacy of the rule is distorted by the insurance it prompts, the insurance regime alone is open to criticism. The realization which follows these observations, of course, is that, although there is undoubtedly a place for insurance in a risky world, there is no place for it in an analysis of what may justify a rule that subjects a person to an insurable liability.

²⁸³ The recruitment argument literally pops up everywhere as a primary, often exclusive, reason for limiting the liability exposure of directors. Both commentators and judges glibly and uncritically reference this justification. Consider the references collected in T. Frankel, "Fiduciary Law: The Judicial Process and the Duty of Care" [1993] Issac Pitblado Lectures 143 at 159-60.

²⁸⁴ Some judges and commentators regard the positions of executive and independent directors as different in kind. They also note the potential constraints on independent directors (eg. limited information, internal domination). The differences, however, do not justify any adjustment to liability rules concerned with risk regulation. As for the potential constraints, truly independent directors would [should] simply not tolerate them. The existence of such constraints is a *valid* reason to vacate or decline the office.

shaped itself to benefit a tiny elite of professional directors who are otherwise well able to protect themselves through negotiated arrangements with their corporate employers. This limited relevance of the recruitment argument is particularly interesting (and problematic) because of the degree of the protection it would confer on professional directors. To the extent the argument successfully prevents reform of the status quo, professional directors benefit from a standard of care that is two levels below what it might otherwise be. The standard that could have been applied to them is that of the reasonably prudent *director*. That standard is higher than that of the reasonable person, which is in turn higher than the existing subjective standard of care. Maintaining this benefit for an elite subclass hardly represents a significant social concern today.

The recruitment argument also fails because of its general application to any undertaking. First observe that a liability assignment associated with an office implicitly contemplates that candidates will decline that office where, having assessed their own abilities and resources, they conclude that the risk of liability is unacceptable. This, of course, is an expected, and salutary, result. And who better to make this decision *ex ante* with full information than the candidates themselves? They make their decision with knowledge of the extant liability assignments and may be presumed to understand the legal consequences of tortious conduct on their part. No one questions this basic operation of liability assignments. Instead, conceding the need to regulate the conduct of directors, the argument is that the law must not *excessively* deter candidates from accepting the office. Thus, in the negligence context, the argument is that raising the standard of care to that of the reasonable person would have the undue secondary effect of rendering more difficult the recruitment of competent directors, and that this consideration should therefore nullify the proposed change to the standard. The difficulty with this kind of reasoning, quite apart from the oxymoronic view that a *reasonable* care standard would *excessively* deter, is that it has equal application to every other office or occupation. There are no calls from other actors, however, to replace or decrease the standard of care that governs their work. Physicians, for example, are subject to the reasonable doctor standard and this regularly results in liability awards against them. Consider the positions of actors in other occupations. Electricians and mechanics are expected to exercise reasonable care so that their work does not lead to injuries to others. It is rare for any of these groups of actors to complain that they have a recruitment problem resulting from an excessive liability burden. They do not make that argument, obviously, because it is neither plausible nor acceptable. We would not tolerate a low standard of care for our physicians or for the mechanics who maintain the safety of our vehicles. Consider also that the lawyers, auditors and others who advise directors are held to an objective reasonable care standard. Directors, it seems, do not tolerate a low standard of care from those who work with them or under their direction. Their advisors, in any event, do not assert the recruitment complaint. The recruitment proposition therefore plainly lacks credibility in most every context, and one wonders how it musters the patina of cogent argument in the context of director liability. The public view is generally that basic functions require reasonable regulation for

the protection of others. The view of directors seems to be that the importance of their function is such that they have a singular claim to relief from the ordinary standard of care. Of course, the net effect of maintaining a lower standard is to ensure that their important work will continue to be performed by less competent actors.²⁸⁵

At least part of the hostile reaction to upgrading the standard of care for directors was (and is) attributable to a concern that it would interfere with some rudimentary corporate planning practices. It is common, for example, for corporate proprietors to appoint their spouses or children as directors. They are advised to do this for control and taxation (income-splitting) purposes; and only infrequently for the management skills of the family member. A spouse, for example, may be handsomely paid to act as a director, and because there is no objective competency requirement, the tax department may find it difficult to establish that the spouse's income was not justified. Thus, under the traditional jurisprudence, the low standard of care both protects the spouse against tort liability and hinders the tax department's argument of improper income splitting. Another practice is adding "names" to the board for marketing, political representation or other purposes. The corporation might, for example, appoint a former socialist politician to facilitate negotiations with unions, or some other political actor to build economic relations (secure contracts) with the government currently in power. These appointments become more difficult if the candidates must concern themselves with the operation of the corporation. In many cases, neither the candidate nor the corporation desire that kind of involvement. This is all quite understandable, but it does not justify the lower standard of care. Corporate planning considerations such as these cannot drive the design of liability assignments. It is not enough to assert that incompetent or disinterested directors may serve other purposes.

The decision to engage in any occupation is a private decision. The law has an impact on this private decision by setting the default liability assignments for the particular position. Potential director candidates make these private decisions on a cost/benefit analysis. Candidates for other occupations perform the same analysis. The recruitment argument applies at this private level. The argument is that candidates will decline the office because the increased cost represented

²⁸⁵ The recruitment argument was made to the Dickerson committee in the course of its deliberations regarding the content of what was to become Canada's current federal corporate legislation. Dickerson *et al*, *supra* note 214 at 83 (Vol. I). The committee flatly rejected the recruitment argument:

We are aware of the argument that raising the standard of conduct for directors may deter people from accepting directorships. The truth of that argument has not been demonstrated and we think it is specious. The duty of care imposed by s. 9.19(1)(b) is exactly the same as that which the common law imposes on every professional person, for example, and there is no evidence that this has dried up the supply for lawyers, accountants, architects, surgeons or anyone else. It is in any event cold comfort to a shareholder to know that there is a steady supply of marginally competent people available under present law to manage his investment.

by the increased liability exposure will reduce the net benefit associated with the work. The usual reaction to an increase on the cost side, however, is to arrange an increase on the benefit side. If the corporation wishes to have the services of particular candidates, it will consider whether (on its own cost/benefit analysis) it is willing to increase the benefit. In other words, a negotiation will take place. On this view, the recruitment concern is again devoid of any real significance. Potential candidates will not decline the office; they will bargain for additional benefits to offset the perceived cost increase. Corporations will only lack competent directors, accordingly, if they are unwilling to pay for them. In this sense, there is only a *pricing* issue here, not a recruitment one. Moreover, it is not even a significant pricing issue, given that the expected cost increase from a potential increase in liability exposure would often be negligible, either in terms of the probability of the event (which decreases as the competency of directors increases) or the change in insurance premium.

The recruitment argument tends to be asserted as a self-evident proposition. There is, however, no satisfactory empirical basis for it. Two kinds of empirical evidence may be considered. The preferred evidence would be an independent analysis demonstrating that special treatment for directors produced a net social gain over a regime where liability was defined by the general law of tort. That kind of empirical evidence does not exist. The other kind of evidence is found in surveys of the views of directors as to the effect on them of increased liability exposure. The anecdotal data usually indicates that directors, or candidate directors, are sufficiently concerned with their liability exposure that they contemplate vacating or declining the office. This response is both predictable and self-serving.²⁸⁶ In a policy analysis, however, it is of virtually no significance absent knowledge of the circumstances and motives of the survey respondents. Do these actors understand that courts will not second guess their business judgment? Do they understand that they are not liable if they reasonably rely on the advice and expertise of others? Did the corporation decline to obtain comprehensive liability insurance for them? Was the remuneration offered by the corporation enough to offset the potential liabilities? Were these actors concerned that they did not possess the ability to fulfill the duties of the office? Did they conclude that the need to become and remain conversant with the affairs of each corporation meant that they could not accept additional appointments? Were their survey answers tactical responses designed to elicit an instrumental conclusion from an easily manipulated survey? Without this kind of knowledge, we can not know whether the decision was an informed or honest one. Even if it were possible to account for information deficiencies, pricing considerations or tactical responses, however, this kind of evidence would remain unhelpful. The personal views of directors are still subjective conclusions. These views do not tell us whether the benefit of liability rules

²⁸⁶ A recent Canadian example of the collection of anecdotal evidence is found in the *Corporate Governance Report* of the Standing Senate Committee on Banking Trade and Commerce (August, 1996).

promoting due care and discouraging harmful acts are fully offset by the loss of directors who are supposedly both competent and risk-averse. Without a sound logical or empirical foundation, the recruitment argument fails.

B. *Selection*

Another policy consideration may initially appear more compelling on the particular issue of the standard of care expected of directors. The argument is that directors should only be held to a subjective standard of care because the corporation selected them with knowledge of their level of competence. This is in effect a "reap what you sow" argument. The reasoning would also appear to furnish an explanation for the different standards of care owed to the corporation and to third parties. Ultimately, however, this too fails to provide a satisfactory justification. It is a flawed proposition, firstly, because in many cases it will not be a fair assumption that the corporation was aware of a candidate's level of competence *in situ*, either generally or in relation to specific matters. Secondly, the corporation also selected its *other* workers, and they are held to the reasonable person standard. There is therefore no justification in the selection proposition for treating directors more kindly than other workers. If there is to be special treatment on a selection rationale, it would have to extend to all agents and employees. Thirdly, the argument is only tenable if the effects of the negligence are limited to the corporation itself. That, however, will not be the case for many negligent acts of directors. Either directly or indirectly, effects will be felt by third parties. Decisions arrived at without due care will injure third parties even though they may not have an actionable claim. This alone should justify the general (rather than special) standard, for then all third parties will suffer remote unrecoverable injury on the same basis. A fourth point involves dropping the assumption that a corporation chooses its directors. In many corporations, both large and small, the directors choose themselves. This consideration strips the selection argument of any practical significance.

C. *Constrained Decisions*

It is frequently claimed that decisions of directors will be constrained or chilled by the prospect of increased liability and that, consequently, risk taking will tend to become more conservative. There are a number of obvious difficulties with this claim. First, if more conservative decisions reduce the probability of tort loss, the liability assignments will have produced their *intended effect*. The claim must therefore be that increased liability exposure would *unduly* constrain decision-making. There is no hard evidence of that, however, and it is implausible. Business decisions are driven by pressing market forces, rather than relatively remote contingent personal liability considerations. Secondly, all of the directors in a given industry will face the same range of potential liabilities. Individual directors may react differently to the liability

risk, but their decisions are formally constrained in the same way. Consequently, because directors are equally exposed, there is essentially no constraint at all. Thirdly, sole proprietors and partners (and ordinary citizens), who all trade with open liability, do not advance the chill argument. Consider also that many directors trade with open *contractual* liability because of the personal guarantees they have provided to third parties. There is never a claim by these directors that their decisions are unduly constrained by this often large and immediate potential liability. Fourthly, the availability of insurance obviously diminishes this constraint argument in the tort context. Lastly, the perception or claim of constraint suggests a failure to comprehend the existing jurisprudence. The business judgment rule exists precisely to accommodate this concern.²⁸⁷ There is no tort liability for loss resulting from an unsuccessful exercise of business judgment. If, however, the exercise of judgment is negligent or involves ordering the commission of a tort, there is a risk of liability. That, again, is an intended liability. It may be added that directors who misapprehend the application of the law will (and should) suffer the usual effects of competition from those who better assess and address the risk of tort liability exposure. Accordingly, there is no *unintended* constraint on the decision-making of directors.

D. *Quantum of Liability*

It is occasionally asserted (and regularly implied) that it is unfair to impose on directors what are potentially “staggering” liabilities. This argument falls short for several reasons. Directors, like the rest of us, have always been exposed to “staggering” liability in connection with their work performance. They have open personal liability when they fail to meet whatever standard of care applies to them or when they direct, or participate in, the commission of intentional torts. The losses for which they are plainly liable may easily amount to very large sums. Secondly, directors are also exposed to potentially staggering liability for losses they cause in their everyday non-corporate activities. All of us are in the same position. If we cause an accident that results in serious injury to others, we may be personally liable for “staggering” damage awards. For most of us, the solution to the problem of potential liability is to obtain third party liability coverage with our home and vehicle insurance. The only general limitation on this exposure is the [relatively accessible and generous] liability cap represented by personal bankruptcy. It is not at all clear why directors should alone benefit from what in effect would be a more favourable cap.

²⁸⁷ See also A.L.I. *Principles of Corporate Governance: Analysis and Recommendations*, Vol. 1 (St. Paul: American Law Institute, 1994) at 135. (“The basic policy underpinning of the business judgment rule is that corporate law should encourage, and afford broad protection to, informed business judgments (whether subsequent events prove the judgments right or wrong) in order to stimulate risk taking, innovation, and other creative entrepreneurial activities.”)

Thirdly, staggering liability means that there are victims with staggering *losses*. In the absence of contributory negligence, there is no good reason to grant special relief to directors and force their innocent victims to shoulder the losses. Directors, it may be added, will only have to compensate their victims for those “staggering” losses to the extent they possess “staggering” wealth. Fourthly, there seems to be an implication in the quantum argument that very large losses, simply because they are large, should be distributed or spread beyond the directors themselves. This inchoate implication, however, is not reflected in the law. Loss distribution *happens* in most every case, but it is not mandated. Whoever is initially assigned the loss, it will likely be distributed under an insurance regime (to other insured parties), or if not insured and unbearable, to creditors or to the public through state programs that care for those who are injured. Loss distribution by itself, however, justifies nothing.²⁸⁸ It only describes what happens to the loss once the liability has been assigned to a particular actor. That initial assignment has never been determined by the size of the potential tort loss.

The quantum fear has led to proposals for an explicit liability cap short of bankruptcy. One such proposal was considered in a 1995 discussion paper produced by the Canadian government.²⁸⁹ The anonymous authors of the paper identified a number of difficulties with a cap:

Several objections can be made to a liability cap. First, limiting the liability faced by directors essentially transfers that liability, and the risk, from them, their corporations, and their insurers back to the injured party. That party could be the corporation’s employees, creditors, the government, or other third parties.

Second, a cap imposed on both large and small corporations could never be optimal; it would reflect a considerable trade-off and might be neither efficient nor effective. In the case of large corporations, even a very large liability cap might not even come close to approaching the potential liabilities faced by directors and, as such, it might negate the effectiveness of directors’ liability as a deterrence mechanism. In the case of small corporations, a large cap probably would always be larger than any liability that directors of these small corporations face.

Third, the TSE report on corporate governance in Canada recommends against capping directors’ liability. The report states that:

We do not think a cap could be effectively implemented simply through amendments to a corporation’s governing statute. A cap would require coordination amongst the jurisdictions imposing personal liability on directors of a particular corporation — a practical impossibility.

Fourth, the liability capping laws in the United States were adopted in response to a concern about excessive levels of directors’ liability to shareholders, arising particularly through class actions. The main areas of concern in Canada have arisen largely in

²⁸⁸ See Flannigan, *supra* note 282 at 28-29 for a discussion of loss distribution in the context of vicarious liability.

²⁸⁹ Canada Business Corporations Act Discussion Paper: Directors’ Liability (*supra* note 218).

respect of statutory liabilities. It could be argued that it is inappropriate for corporate legislation to attempt to affect compliance regimes established by other legislation. This could be seen as an unfair imposition of corporate policy goals upon goals enacted by other legislation.²⁹⁰

The authors concluded that a liability cap should not be adopted. As a practical (political) matter, of course, it would be difficult to justify a cap for the benefit of directors, but not other occupations.

E. *Other Arguments*

A variety of other policy considerations have been offered to support special treatment for directors. It is argued, for example, that innovation is hindered or checked to the extent directors are subject to open liability. This curious argument is often framed in near apocalyptic terms. There is not a shred of evidence, however, to support it. Innovation will normally be a serendipitous event or the result of targeted research and development programs. In neither case will the prospect of personal liability likely have any effect on the generation of innovation by the other workers who actually do it. There is no demonstrated link between director liability and stunted innovation. Another argument is that directors will move their corporations to jurisdictions with less onerous liability assignments. That, however, is an irrelevant consideration to the extent the directors intend to continue to carry on business (and commit torts) within the original jurisdiction. Further, the limited savings in tort liability costs would rarely, if ever, justify the costs of leaving the jurisdiction. Beyond that, it must be obvious that the laws of a community must first be concerned with the protection of its own citizens. It is far from a compelling argument that directors might choose to exploit the weaker legal position of tort victims in other jurisdictions. A related argument is that "excessive" liability (with increased liability protection costs) will fetter the international competitiveness of domestic corporations. The idea here seems to be that we must reduce liability exposure by some significant order of magnitude [presumably to the lowest level of general tort law protection maintained in other jurisdictions] in order to achieve unrelated trade objectives. That is an idle proposition. A fourth argument is that markets sufficiently regulate the conduct of directors. Markets, however, do not operate early enough or deep enough to effectively regulate the risk-taking of individual directors. There is a general understanding that liability rules are required well below the thresholds where markets begin to have effect. Another argument is that directors should not be liable in the same way as others because they act collectively as a board. This is plainly a weak argument in the tort liability context. If the board collectively acts negligently or directs the commission of a tort, every director is personally liable. The fact

²⁹⁰ *Ibid.* at 42.

that the action was collective is not an excuse, it is merely *joint* responsibility. A different complaint, apparently seriously made, is that the prospect of liability will necessitate a legal opinion for every business decision. That is but instrumental hyperbole. Another argument is that experienced directors of established corporations should be encouraged to sit on the boards of *other entities* which need their professional assistance. These other entities might be non-profit organizations, corporations in financial difficulty or small entrepreneurial corporations whose success is said to be essential to the economy. This seems to suggest a public subsidy in the form of a liability reduction for directors who take on additional directorships of charitable, distressed or struggling corporations. It is thin gruel. There is nothing in the circumstances of such corporations that would appear to excuse the tortious conduct of directors who dabble part time in their affairs. Another complaint is that liability concerns result in the devotion of excessive time to due diligence procedures. Again, however, due diligence procedures are an intended or elicited response to liability assignments. It is the function of the directors (and their advisors) to arrange for the due diligence that is appropriate for the particular matter or transaction. If the due diligence they order is excessive, it would be the result of their own analytical or information failures, and they have only themselves to blame. Finally, it is occasionally claimed that expanding director liability will open the floodgates of litigation. An initial difficulty with this proposition is that a change in the law does not necessarily, or even usually, imply an increase in litigants or litigation. A second difficulty is that the floodgates argument is never a good reason for denying relief where that relief is justified by substantive public policy. It is incoherent to refuse recognition of legitimate claims solely because affected citizens will assert those claims.

The underlying premise of several of the foregoing arguments is that we (the relevant community) must accept the prospect of an increased risk of tort loss in order to secure other objectives (eg. facilitate recruitment, decision-making, innovation, capital investment/retention, international competitiveness and philanthropic managerial activity). We are to subsidize the risk-taking of directors by discounting our right to hold them responsible for the tortious harm they cause. The attainment of those objectives, however, does not justify exposing the community to a higher risk of injury. The remaining arguments fail to provide a credible alternative justification. The universal consensus is that actors should bear the consequences of their own tortious conduct. None of the foregoing arguments constitute a good reason to displace the operation of that social norm.

IX. Conclusion

The purpose of this exercise has been to critically examine the common law tort liability of directors. That examination disclosed a measure of confusion and uncertainty in the jurisprudence. The progression to this state of affairs is not difficult to trace. Directors were initially treated differently in relation to the

standard of care they owe to their principals. Seemingly in an effort to accommodate the exercise of business judgment, the courts set the formal threshold for liability at “gross” negligence. In other respects, directors were subject to general tort law principles. This case law remained relatively stable through much of the twentieth century. Confusion was introduced, however, by the Canadian case of *Mentmore Manufacturing Co., Ltd. v. National Merchandising Co. Inc.* One confusion was the introduction of a new liability threshold for intentional torts that subsequently found only spotty acceptance in the cases. The second, more significant, confusion was Justice Le Dain’s assertion of a conflict between the principles of tort law and corporate law. It was a false conflict, but it infected the jurisprudence. The process of confusion accelerated in the last decade of the century. Canadian courts went their separate way with a collection of new approaches and tests that had the effect of decreasing the tort liability exposure of directors. Much of the confusion first arose in cases dealing with the tort of inducing a breach of contract. It then spread to cases dealing with other intentional torts and with negligence. The bulk of the confusion is the result of conceptual errors, or judges proposing innovations to address what they regarded as an unsatisfactory state of the law. A few judges moved to arrest the confusion, but it appears their efforts were a temporary respite. The result is that the Canadian jurisprudence is in a muddle. There is less confusion in the courts of other jurisdictions, but they too exhibit uncertainty over such matters as the standard of care and the recovery of pure economic loss.

There are those who believe that directors share statutory limited liability with shareholders. There is no basis whatsoever for that belief. It is clear, however, that while the tort liability of directors is open, it is not as open as it is for other actors. The courts in Canada have produced a case law that directly and indirectly confers a degree of special protection on directors. Directors are less likely to be fixed with responsibility for their tortious actions because of higher liability thresholds and because of the judicial hesitation created by the existence and content of the various confusions. The question is whether this special treatment is justified. The courts, perhaps understandably, have offered little in the way of explicit policy analysis. They have preferred legalistic “corporate personality” arguments that only suppress or conceal the policy issue. A number of ostensible policy considerations, however, can be found in the cases and literature. When the premises, incentives and consequences of those policy arguments are tested, the conclusion is that there is no sound policy basis for treating directors more kindly than other actors. It perhaps should be added here that there is no suggestion in any of this that directors are less worthy beings. It is only that they are not a special case in so far as their tort liability exposure is concerned. They must accept the responsibility we all have for our tortious actions. That is the conventional discipline required by the risk regulation norm. Directors should experience the default application of the general law of tort in exactly the same way as do all other actors.