1914

*May 12.
*May 18.

THE THEATRE AMUSEMENT COMPANY AND OTHERS (DEFENDANTS)... } APPELLANTS;

AND

LOUIS B. STONE (PLAINTIFF)..... RESPONDENT.

ON APPEAL FROM THE SUPREME COURT OF THE PROVINCE OF ALBERTA.

Company — Disqualification of directors — Taking personal profit — Fraud—Illegal contract—Ratification—Right of action—Shareholder—Recourse by minority—Alberta "Companies Ordinance," N.-W. Ter. Ord. No. 20 of 1901—Construction of statute.

Where the directors of a joint-stock company organized under the Alberta "Companies Ordinance" (N.-W. Ter. Ord. No. 20 of 1901), have violated the provisions of article 57, Table "A," of that enactment, (as to vacating the office of directors,) the consequences involve not only the disqualification of the directors, but also give a right of action on the part of any shareholder for a declaration of such disqualification and for an account of the moneys improperly received by them as profits under contracts between them and the company. Such contracts, being prohibited by the ordinance, could not be ratified by a majority of the shareholders, as the matter is not one merely of internal management. *Burland* v. *Earle* ((1902) A.C. 83), distinguished.

The judgment appealed from (25 West. L.R. 905) was affirmed.

APPEAL from the judgment of the Supreme Court of Alberta (1), reversing in part the judgment of Harvey C.J., at the trial.

The action was brought, against the Theatre Amusement Company, Barney Allen, Julius Allen, Jay Junior Allen and a partnership firm known as The Canadian Film Exchange, by the present respond-

*PRESENT:—Sir Charles Fitzpatrick C.J. and Idington, Duff, Anglin and Brodeur JJ.

(1) 25 West. L.R. 905.

ent, a shareholder in the Theatre Amusement Company, who had also been a partner in the Canadian Film Exchange, but had retired from that partnership previous to the illegal contracts complained of by which the appellants, the Allens, being the remaining shareholders in the Theatre Amusement Company and its directors, had obtained profits improperly from the last-mentioned company. The plaintiff sought a declaration that, by their misconduct, the Allens had become disqualified as directors of the said company, for a refund to the company of moneys received by them as salaries, an account of the moneys improperly received by them, and the appointment of a receiver to carry on the business of the company. At the trial the learned Chief Justice decided that the salaries had been voted by the directors to themselves without proper authority, that they were liable to account to the company for profits made by them in dealing between the company and themselves, that the shareholders could ratify, if they wished, what the directors had done, and that, in the meantime, the court should not interfere because interference should be for the benefit of the company and not for that of a single shareholder whose interests were less than those of the defendants as holders of the majority of the stock. Consequently an order was made for the refund of the amount of the salaries in question, but the plaintiff failed on the other branches of his action. On an appeal to the full court, this judgment was varied by the judgment now appealed from by a direction that, unless a new trial was agreed to, there should be an accounting for the profits improperly obtained by the directors.

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The questions in issue on the present appeal are stated in the judgments now reported.

R. V. Sinclair K.C. for the appellants.

J. A. Ritchie and *Hannah* for the respondent.

THE CHIEF JUSTICE agreed with Idington J.

IDINGTON J.—The respondent and the three defendants, named Allen, owned in equal shares the corporate appellant and composed the partnership firm known as The Canadian Film Exchange. The interest of respondent in the latter concern was bought by the Allens, who continued the business.

The firm had, both before and after the respondent's retirement, sold goods to the appellant corporation, of which the Allens were the directors.

The ordinance under which the incorporation of the Theatre Amusement Company was procured prohibited the directors from doing so at a profit. And, so long as respondent was a member of the firm, they did not sell to the corporation at a profit.

So soon as respondent retired from the firm these directors alone constituting the firm charged a profit in the sales of goods of the same class supplied to the corporation. They admit doing so disqualified them as directors, but claim it was honest to do so and that respondent has, therefore, no remedy except by means of a suit in the name of the corporation, which their ownership of a majority of the stock rendered impossible. I think they are mistaken in their morals and law.

Their first practice of selling at cost price was

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honest. As things then stood it cost them nothing to be honest.

The change from that to selling at a profit involved what was clearly illegal and a breach of trust. Their partner had a right to believe his trustees would not so change as to adopt illegal practices merely to beat him out of a fractional advantage.

I cannot say that their devious courses developed a very high standard of honesty. And I do not think, in law, the respondent is to be driven to trust to the honest voting of such fellow shareholders as his only hope of relief.

No one can question the law as laid down in *Burland* v. *Earle*(1), and the other like cases, but the extension of the doctrine to making it the systematic daily method of doing business so that those possessing the majority of the stock can so use their power and opportunity to drain the corporate body of all its sources of profit giving, and render dividends impossible, or the possibility thereof to be the measure of the rapacity of the directorate, is something not yet recognized in law. Yet such seems to be what is involved in the principle to be maintained in allowing this appeal.

Indeed, I am tempted to suggest that lest other honest men be also led astray by the like application of the apparently logical reasoning put before us on behalf of the appellants, and alleged to rest on such high legal authorities, the sooner every legislative body can obliterate from its incorporating Acts the power of any shareholder by his own vote to help himself to sell his property to the company in which he is

(1) [1902] A.C. 83.

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a shareholder, the better it will be for the moral health of the business community.

The appeal should be dismissed with costs.

DUFF J.—I think this appeal is disposed of by reference to article 57 of Table "A." That article declares the effect of a director entering into a contract with the company or being interested in a contract with the company; the effect is that the director becomes divested, as between himself and the company, of his *de jure* authority as director. If, therefore, the transactions in question are to be treated as contracts made between the directors and the company the effect of the very first transaction was to divest each of them of his authority as director. These persons having during this series of transactions continued to act in the capacity of directors they cannot, in my opinion, be allowed to say as against the company, or as against any shareholder of the company, that they were wrongfully in office, in other words, they cannot be permitted to deny that, in purchasing the goods in question, they were acting as agents for the company or that they are accountable, as such, for the profits. It is contended, however, that this is a position which only can be taken by the company itself. This contention rests upon an entire misconception of the effect of the articles of association of a company incorporated under the "Companies Act" of Alberta. The articles of association are binding upon the company, the directors and the shareholders, until changed in accordance with the law. So long as they remain in force, any shareholder is entitled, unless he is estopped from taking that position by some conduct of his own,

to insist upon the articles being observed by the company, and the directors of the company. This right he cannot be deprived of by the action of any majority. In truth, the articles of association constitute a contract between the company and the shareholders which every shareholder is entitled to insist upon being carried out.

ANGLIN J.—I would dismiss this appeal on two grounds.

The contracts complained of were in violation of article 57 of the Articles of Asosciation. N.-W. Ter. Ordinances, 1901, ch. 20, sch. "A." The penalty of disqualification for the offending directors is imposed by that article. But that does not exhaust the consequences of an infraction of its provisions. The making of such contracts by the directors was prohibited. They could, therefore, be ratified only by a unanimous vote of all the shareholders and not by any majority however great. The question is not one of internal management and, as such, subject to the control of the majority.

On the evidence, the changes in the dealings between the company and the partnership, known as the Film Exchange, after Stone had ceased to be a member of that partnership, whereby profits from those dealings resulted to the partnership, was a fraudulent breach of trust on the part of the directors which no majority of the shareholders could render binding on the company. Other than the films, as to which there is no complaint, the articles supplied by the partnership to the company would appear to have been purchased by the partnership for the very purpose of being re-sold to the company.

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On these grounds this case is distinguishable from *Burland* v. *Earle*(1), relied upon by counsel for the appellants.

BRODEUR J.—I agree that this appeal should be dismissed with costs.

Appeal dismissed with costs.

Solicitors for the appellants: *Lent, Jones & Mackay.*
Solicitors for the respondent: *Hannah, Stirton & Fisher.*

(1) [1902] A.C. 83.