



Court of Appeal overturns supervising judge's 'pre-emptive strike' against Stelco directors

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In late March, the Ontario Court of Appeal overturned the decision of Mr. Justice Farley to remove two new directors of steelmaker, Stelco Inc., during its restructuring under the *Companies' Creditors Arrangement Act* ("CCAA"). In ordering the Stelco directors reinstated, the Court of Appeal highlighted that the discretion given by the CCAA to the court supervising a restructuring is not unlimited and stressed that the removal of corporate directors is "an extreme form of judicial intervention" that is to be exercised very rarely.

At the time of the Court of Appeal's decision in *Stelco Inc. (Re)*¹, Stelco had been under court-ordered protection from its creditors under the CCAA for more than a year and had been undergoing a court-approved capital raising process involving several bids to purchase Stelco and four of its subsidiaries. Farley J. had been supervising the CCAA process from its outset. The two directors at issue, Messrs. Woollcombe and Keiper, had been associated with two corporations which owned almost 40% of Stelco's common shares. Employee stakeholders of Stelco objected to the appointment of Woollcombe and Keiper – believing that they were likely to favour bids that maximized shareholder value at the expense of bids that might be more favourable to the interests of current and retired Stelco employees.

A week after Woollcombe and Keiper was named as directors, Farley J. found it "appropriate, just, necessary and reasonable" to declare their appointments of no force and effect. Farley J. did so on the basis that there was a risk that Woollcombe and Keiper might not in the future live up to their obligations to act solely in the best interests of Stelco, the fallout from which might be

very detrimental to Stelco and its ability to successfully emerge from its restructuring. Farley J. purported to remove the two Stelco directors under the "inherent jurisdiction" of the court to control its own process and pursuant to his broad discretion under section 11 of the CCAA.

The Court of Appeal found that Farley J. lacked the jurisdiction to remove the directors and that his decision had to be set aside. Firstly, it rejected the idea that the court has the inherent jurisdiction to remove directors, stating that the court's inherent jurisdiction should not apply where a statutory scheme for the removal of directors is already in place and, in any event, should be limited to situations involving the *court's process* and not interfere with a *company's process* by removing directors.

The Court of Appeal also rejected the claim that Farley J. had jurisdiction to remove directors under the CCAA, finding that the *Canada Business Corporations Act* ("CBCA") and its provincial equivalents are the statutes governing the removal of directors. The court went on to find that the removal of directors under the CBCA and similar statutes is an exceptional remedy that is rarely exercised, given courts' historical reluctance to interfere with internal corporate affairs. Quite simply, it is not appropriate to read into the discretion under s.11 of the CCAA the ability to supplant another applicable statute, such as the CBCA or the discretion to grant an extraordinary remedy such as the removal of directors.

While the Court of Appeal rejected the removal of the directors in this case, it affirmed prior decisions that, in some circumstances, directors can be removed during an insolvency proceeding.

However, such an order should not be made absent clear evidence of misconduct amounting to oppression as defined under the CBCA (and its provincial equivalents) and a court determination that the continuing presence of one or more corporate directors is harmful to the company and its stakeholders.

In *Stelco*, there was no such evidence and no such finding. The decision of Farley J. to remove Woollcombe and Keiper as directors was based upon speculation as to how they might act in any future restructuring and further speculation as to the dire consequences of such anticipated future misconduct. Mere speculation was not enough to found an extraordinary remedy removing corporate directors. As such, the decision was overturned and the directors reinstated.

Postscript – Stay denied pending leave to the Supreme Court of Canada²: A week after the *Stelco* decision was released, the parties were back before the Court of Appeal arguing about whether the decision to reinstate Woollcombe and Keiper as *Stelco* directors should be stayed pending an application for leave to appeal to the Supreme Court of Canada. In denying a stay, Feldman J.A. acknowledged that the *Stelco* restructuring process could be largely completed over the next several months - which would render moot any question of whether Woollcombe and Keiper should be allowed participate in that process as *Stelco* directors. Feldman J.A. found that the balance of convenience favoured denying a stay of the Court of Appeal's decision – as to do otherwise would amount to implementing a lower court decision to remove the directors that had been found to be made without jurisdiction.



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¹ For the full text of the court's decision, see: <http://www.ontariocourts.on.ca/decisions/2005/march/M32289.htm>

² For the full text of the court's decision on whether to grant a stay of the order reinstating the *Stelco* directors, see: <http://www.ontariocourts.on.ca/decisions/2005/april/M32289.htm>