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Director Liability and the Workers' Compensation Scheme: The Divergence Between Policy Goals and Outcomes

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Case Commented On: *Hall v Stewart*, 2019 ABCA 98

The workers' compensation scheme and its effect on directors' personal liability for corporate torts is an area of law that pursues the right policy goals but fails to achieve those goals in its implementation.

This post is about directors' personal liability, the interplay between the *Workers' Compensation Act*, RSA 2000, c W-15 (Act) and common law, and the policy issues that arise from this scheme. When the workers' compensation scheme is superimposed on the common law system, it immunizes the corporation for corporate torts while leaving directors open to suit if they do not purchase special coverage. Their liability is then determined by common law principles.

In *Hall v Stewart*, the director, Stewart, did not purchase additional insurance, leading the Court of Appeal to conclude he could be held personally liable for the tort of the corporation under the two-step Anns/Kamloops test (from *Kamloops (City of) v Nielsen*, 1984 CanLII 21 (SCC), [1984] 2 SCR 2). This post will discuss two issues arising from this decision; first, the policy issue this scheme engenders, which should have been addressed under the second step of the Anns/Kamloops test, and second, the influence of *Nielsen Estate v Epton*, 2006 ABCA 382 (CanLII), affm'g 2006 ABQB 21 (CanLII), on this decision, which the Court of Appeal did not apply.

Facts

Fekete Homes retained DWS Construction Ltd. (DWS) to perform work on the construction of a new home. The respondent, Stewart, a director of DWS, worked on installing a temporary staircase in the basement of the new home. Stewart supervised and participated in the installation. The claimants were employees of another subcontractor. The staircase collapsed and the claimants were injured.

The claimants were compensated for their injuries under the Act but they could not sue DWS for damages, as DWS was an "employer" under the Act. After compensating the claimants, the Workers' Compensation Board (Board) brought this subrogated action against Stewart to recover the amounts it had paid to the claimants.

Issue

The issue in this appeal was whether Stewart could be held personally liable for the personal injury to the claimants. Broadly, the issue was whether a director can be held personally liable for the damage resulting from his own conduct while he was acting as a director for the corporation.

Act

Under the Act, a "dual regime of statutory no-fault compensation and immunity from suit" (at para 9), an injured "worker" cannot sue an "employer" or another "worker" for her injuries (s 23). Under this regime, a director of an employer is neither a "worker" nor an "employer", meaning a director cannot claim compensation under the Act, nor can she be immune from claims under the Act, unless she purchased additional insurance (ss 15, 16).

The workers' compensation system did not extend to Stewart, a director, as he did not purchase additional insurance.

Decision

The Court (Justices Jack Watson, Frans Slatter and Brian O'Ferrall) determined that the main issue in the appeal is "whether a corporate representative like the respondent is personally liable for damage that results from his own tortious conduct" while he was acting as the representative of the corporation (at para 7). Then, the Court split its decision into three parts: one describing the workers' compensation system, the second, discussing corporate personality, and the third discussing personal liability for corporate torts.

The Court noted that since DWS was an employer under the Act, the employees could be compensated in the event of injury while working, and that both DWS and its workers were immune from liability under the Act, s 23. This immunity, however, did not apply to "directors" of "employers", who must purchase separate coverage from the Board. As Stewart had not purchased additional coverage, he was not immune from liability.

Additionally, the fact that Stewart may have been acting as a worker at the relevant time did not change the analysis, as the Act does not differentiate between whether the work was done by a director or worker, but rather, the application is based on "whenever the work done is 'part of the business of the corporation'" (at para 10).

Under the next topic, "The Corporate Personality", the Court discussed the concept of limited liability and separate corporate personality. After noting that the concept of corporate personality is "an essential tool of social and economic policy", it maintained that personal liability would potentially remain when damage is caused by a tortious act (at para 12). Under the next topic, "Personal Liability for Corporate Torts", the Court went on to discuss when an employee or director would be held personally liable for the tortious act, "notwithstanding that they only acted on behalf of the corporation" (at para 12).

The Court first discussed the competing policy objectives at play in this decision. The first is the corporate law objective, to limit personal liability for corporate acts. The second is a tort law one, to compensate injured persons (at para 13).

The Court went on to acknowledge that corporations can owe duties of care to individuals, but noted that corporations must always act through human agents. Sometimes, these agents will also owe a duty to individuals, and other times, the corporation will be vicariously liable for the acts of these agents. Where there is concurrent liability, the question as to whether the individual is personally liable while carrying out the business of the corporation is typically not relevant, as the corporation or its insurers will cover the loss. Where the question becomes relevant is, for a variety of reasons including the workers' compensation scheme, when the corporation is immune from being sued, but the individual tortfeasor is not (at para 14).

The Court found that both DWS and Stewart owed a duty of care here, and that without immunity under the Act, Stewart would be potentially liable in tort (at para 15). Stewart's duty of care arose because he was personally installing the staircase, and he was therefore involved in the accident as both a director and an employee (at para 17).

After listing ten "relevant factors" gleaned by reference to case law, the Court noted that "a comprehensive and integrated test" on when personal liability will attach to torts does not exist (at para 18). It also noted that when considering whether personal liability would attach, "it must be acknowledged that the underlying risk can readily be managed and diverted through the purchase of appropriate insurance" (at para 19). It went on to say that whether insurance was purchased was not the point, but rather, by failing to purchase insurance, the respondent had decided to assume the underlying risk, and could not therefore "seek to pass the risk of recovery of personal injury damages onto injured claimants" (at para 19).

After determining that the respondent was clearly acting on behalf of DWS, and not in his personal interest or independently of the corporation, the Court nonetheless went on to determine that the respondent would be personally liable due to the nature of damages in this case (at para 23). Given that this was a personal injury case, as opposed to one for pure economic loss, the Court cited "strong public policy reasons to ensure that physically injured plaintiffs are compensated" (at para 23). The Court maintained that limited liability was never designed to immunize tortfeasors in these situations (at para 24).

Analysis

My analysis focuses on directors' personal liability and the interplay between the Act and common law. Under the workers' compensation statutory scheme, directors can be immune from claims by injured workers only by purchasing additional coverage, without which, they can be sued, and their liability is determined according to common law principles.

There are two parts to this analysis. First, I will examine the concept of limited liability for corporate actors. Second, I will examine tort liability for corporate actors. In this part, I will discuss a policy issue that arises in relation to the workers' compensation legislative scheme and the applicability of the case, *Nielsen Estate*, to this decision.

Limited Liability

A discussion about the personal liability of corporate actors will typically reference the historical case of *Salomon v A. Salomon & Co.*, [1897] AC 22 (HL). *Salomon* introduced two fundamental concepts of corporate law: that the corporation is a separate legal entity and that shareholders will not be personally liable for the debts and obligations of the corporation. *Salomon* was not about directors; it was about passive investors, meaning the concept of limited liability did not arise to protect directors. Yet, limited liability is frequently referred to in relation to directors, and this is so, not because they were the intended beneficiaries of this doctrine, but rather, because the corporation could not truly be a separate legal entity if stakeholders could hold directors and officers personally liable for its debts and obligations. In other words, even though directors were not the intended beneficiaries of limited liability (the first *Salomon* principle), failing to provide them with some protection would undermine the second principle.

There is oftentimes a confusion surrounding the beneficiaries of limited liability, sometimes arising from a misunderstanding as to the original concept and sometimes from careless usage of language in decisions. Courts frequently refer to directors as being the beneficiaries of limited liability, and while that is not an entirely inaccurate statement, it does reference a historic decision that was never intended to apply to them, and their liability in relation to the corporation is more nuanced than the straightforward principle that arises from *Salomon*. More precisely, whatever limited liability directors and officers possess today does not evolve from *Salomon*, but from the realities involved with managing a corporation. As Justice Hardie Boys stated in the Australian case of *Morton v Douglas Homes Ltd.*, [1984] 2 NZLR 548 (HC), 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" (at 593).

Today, shareholders' limited liability is codified in the *Alberta Business Corporations Act*, RSA 2000, c B-9 at s 46(1), when they are acting as passive investors. The provision broadly states, "shareholders of a corporation are not, as shareholders, liable for any liability, act or default of the corporation" (with a few listed exceptions). Directors and officers do not have the blanket immunity provided by s 45. Rather, any immunity they might enjoy arises under specific statutory provisions and discrete areas of the common law.

Personal Liability for Torts

One of the most difficult questions in corporate law is the extent to which personal liability should be imposed on directors for the tortious conduct of the corporation, in particular, for negligence. Oftentimes, the actions of directors are seen to be those of the company in one of two ways: these actions are either characterized as the vicarious actions of the company or, by identifying the director as the company, the director's actions are those of the company itself (see G. H. L. Fridman, "Personal Tort Liability of Company Directors" (1992) 5 Canterbury L Rev 41 at 47). So, when is a director identified with the company and when is she seen as a separate person and therefore subject to personal liability? As the Court noted in *Hall v Stewart*, "[t]he law on when personal liability will attach to corporate torts is not clear" (at para 18). In a more direct comment on director liability, Robert Flannigan maintained, "The Canadian cases are a mixed bag in terms of cogent analysis. While there are cases that apply the standard "neighbour"

analysis, some of the confusions generated in the intentional tort cases. 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" ("The Personal Tort Liability of Directors" (2002) 81 Can B Rev 247 at 307). For a recent in-depth discussion on this topic, see Shannon O'Byrne, Yemi Philip and Katherine Fraser, "The Tortious Liability of Directors and Officers to Third Parties in Common Law Canada (2017) 54 Alta L Rev 871.

The area dealing with director and officer liability in Canada has generated two streams of case law. The first stream originated from the case, *ScotiaMcLeod Inc. v Peoples Jewellers Ltd*., 1995 CanLII 1301, 26 OR (3d) 481 (ONCA), leave refused [1996] SCR viii. In *ScotiaMcLeod*, the Ontario Court of Appeal provided a broad immunity for directors, maintaining that personal liability would be rare absent "findings of fraud, deceit, dishonesty or want of authority on the part of employees or officers" (at 491). Therefore, "[a]bsent 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 interest from that of the company so as to make the act or conduct complained of their own" (at 491).

The second stream originated in another Ontario Court of Appeal decision, *ADGA Systems International Ltd v Valcom Ltd*., 1999 CanLII 1527, 43 OR (3d) 101 (ONCA), which was in harmony with the earlier case of *London Drugs Ltd v Kuehne & Nagel International Ltd*., [1992] 3 SCR 299, 1992 CanLII 41 (SCC). Although the *ADGA* Court claimed its decision was consistent with *ScotiaMcLeod* (at 107, 112), in fact, it was almost entirely opposite. *ADGA* maintained that "in all events, officers, directors and employees of corporations are responsible for their tortious conduct even though that conduct was directed in a bona fide manner to the best interests of the company" (at 107). There was one caveat created in *ADGA*, which was not explored by the Court, where it noted that employees, officers, and directors could be protected in "limited circumstances where, for instance, they are acting in the best interests of the corporation with parties who have voluntarily chosen to accept the ambit of risk of a limited liability company" (at 113).

In sum, one stream suggests directors and officers are liable for all tortious conduct, with an unexplored caveat, and the other suggests they are not liable for any tort that is not intentional, such as fraud. Subsequent case law has done little to resolve the confusion in this area, as some cases rely on *ScotiaMcLeod*, some on *ADGA*, and some combine aspects of both cases. More recently, the Supreme Court's decision in *Peoples Department Stores Inc. (Trustee of) v Wise*, 2004 SCC 68 (CanLII), found that directors can have a duty of care to third parties such as creditors. Some have interpreted this statement as an implicit overruling of *ScotiaMcLeod* (O'Byrne et al, *supra* at 874).

The discussion on the proper stream of case law is too broad to explore here, and many papers have been devoted to the subject. It is safe to say, however, that the *ADGA* line of reasoning entirely removes the benefit of operating within the corporate entity. Human actors will always direct corporate acts, and if they can always be concurrently liable with the corporation, the first principle of *Salomon* ceases to exist. Articulating a test as to when personal liability should

apply, one that is not entirely on either end of the spectrum, or in other words, one that is not an all-or-nothing test, has eluded courts for the last several decades, though they have managed to articulate a few principles. One, which is a broader tort principle, and which is the path pursued in *Hall v Stewart*, is that a duty of care is easier to find when the nature of damages is personal injury.

Here, the Court started its analysis by relying on the *ScotiaMcLeod* line of cases. It found that, "[t]he work that caused the injury was clearly done on behalf of the corporation, was in the best interest of the corporation, and did not reflect any personal interest of the respondent", and, as a result, concluded, "[i]t could not be said that the respondent's allegedly negligent conduct was in any respects 'independent' of the business of the corporation" (at para 22). In *ScotiaMcLeod*, personal liability does not attach to a director unless there is "some activity on their part that takes them out of the role of directing minds of the corporation" (*ScotiaMcLeod*, at para 26). Until that point, the Court of Appeal was in agreement with the two judgments below. The Master had found that "Stewart was doing exactly what DWS was engaged to do" (unreported) and therefore identified with the company. The chambers judge similarly noted, "There was no evidence of any act by Mr. Stewart other than acts performed by him within the scope of his employment" and that even if it was found the stairs had been negligently constructed, "such negligence would be in relation to the job Mr. Stewart was employed to do for DWS… and would not constitute an overt or extraordinarily tortious act that would take him outside the protection of the corporation" (unreported). Up until this point in the reasoning, all three decisions were in agreement. But the Court of Appeal broke with the lower court judgments, finding liability because the workers had suffered physical harm. It reached its conclusion by applying the two-step Anns/Kamloops test.

In negligence cases, the Anns/Kamloops test is applied to determine whether a duty of care is owed for the harm. The first step considers whether a *prima facie* duty of care exists, which requires looking into whether there is proximity between the parties, or, in other words, "whether there is a sufficiently close relationship between the plaintiff and the defendant that in the reasonable contemplation of the latter, carelessness on its part may cause damage to the former" (*Hercules Managements Ltd. v Ernst & Young*, [1997] 2 SCR 165, at para 22). If a duty exists, the second step requires looking into whether any policy reasons exist to limit that duty. When the negligence results in physical harm or property damage, a duty of care is more easily established than when the outcome is pure economic loss because it is reasonably foreseeable that one's negligent actions could result in physical injury to one's co-workers. As it was put in *Hercules Managements*,

> In the context of actions based on negligence causing physical damage, determining whether harm to the plaintiff was reasonably foreseeable to the defendant is alone a sufficient criterion for deciding proximity or neighbourhood under the first branch of the *Anns/Kamloops* test because the law has come to recognize (even if only implicitly) that, absent a voluntary assumption of risk by him or her, it is always reasonable for a plaintiff to expect that a defendant will take reasonable care of the plaintiff's person and property. (at para 25)

In *Hall v Stewart*, the deciding factor appeared to be that the workers were physically harmed, leading the Court to find that both parts of the test were met; it concluded that, "there is clearly a 'duty of care' to avoid injuring one's co-workers, and no residual policy considerations to exclude liability" (at para 23).

Two issues arise from the Court's judgment here. The first is about the Court's failure to find no residual policy concerns to exclude liability in this case. The second deals with a precedent deemed inapplicable by the Court and which, if applied, arguably would have required the court to refrain from finding liability. I deal with each separately.

a. Policy Concerns Under Step Two of Anns/Kamloops Test

Even if a duty can be established under the first step of the Anns/Kamloops test, we should not be so quick to dismiss the policy part, as the structure of the workers' compensation scheme should raise one policy concern in particular.

The workers' compensation scheme is a substitute for common law tort liability. If a "worker" is injured in the course of his employment, the worker has remedies under the scheme that substitute his rights at common law. This scheme is a "historic trade-off", by which "workers lose their cause of action against their employers but gain […] compensation that depends neither on the fault of the employer nor its ability to pay" (*Pasiechnyk v Saskatchewan (Workers' Compensation Board)*, [1997] 2 SCR 890, at paras 24-25). This scheme is only possible if employers are "forced to contribute to a mandatory insurance scheme", whereby employers pay into a fund in exchange for "freedom from potentially crippling liability" (*Pasiechnyk* at para 25).

Under the Act, directors are neither "workers" nor "employers", which means they do not automatically have the benefit of immunity from suit. They can get it, but only by applying to the Board for special coverage. Courts have opined that the purpose of excluding directors from the employer's immunity is to "encourage executive officers to consider the safety of their employees and to avoid the creation or maintenance of dangerous situations" (*Berger v Willowdale A.M.C.*, 1983 CanLII 1820 (ONCA), at para 43).

These policy goals are sensible, but the structure of the legislation will not produce the desired outcomes. If the goal is to provide workers with compensation through a no-fault scheme, then the scheme requiring all employers to contribute to the fund achieves that goal. If the goal is to motivate directors to act more carefully, however, having the option of purchasing special coverage undermines that goal. The option of purchasing special coverage results in a system where directors who are immune from suit are not those who are more careful, but rather, they are those who can afford to pay for the coverage.

In this case, the Court considered the availability of insurance to be important in reconciling the "competing policy objectives of tort law and corporate law" (at para 19), deciding that, "In assessing whether a corporate representative should be exposed to personal liability for corporate acts, it must be acknowledged that the underlying risk can readily be managed and diverted through the purchase of appropriate insurance" (at para 19). If the Court is saying that the

availability of insurance means there are no unreasonable structural problems with imposing liability, then it is not asking the right question. The funds employers must pay under the workers' compensation scheme are burdensome, especially on smaller companies, meaning directors of these companies are less likely to have special coverage. Therefore, when the Court said that by failing to purchase insurance, the respondent had decided to assume the underlying risk, and could not therefore "seek to pass the risk of recovery of personal injury damages onto injured claimants" (at para 19), it was not allowing for the possibility that failing to purchase insurance is not necessarily a decision made entirely on the basis of voluntary risk assessment so much as on a consideration of affordability. A scheme where the avoidance of liability is based on the ability to pay for immunity is not one that will encourage directors to act carefully.

b. Precedent*: Nielson Estate*

The second issue arising from the *Hall v Stewart* judgment is the Court's refusal to rely on the case of *Nielsen Estate*. In that case, the corporate director was found personally liable because he owed a duty of care to "maintain a safe workplace". The director was not directly involved with the incident that had caused the death of the worker, but the court found that by failing to "maintain a safe workplace", the director's acts were "tortious in themselves" (at para 21).

In *Hall v Stewart*, the Court found the *Nielsen Estate* case inapplicable, for two reasons. First, the Court found that amendments to the Act subsequent to *Nielsen Estate* broadened the relevant provision to "make this analysis unnecessary" (at para 17). Second, Stewart was actively involved in installing the staircase, as both a director and an employee, whereas in *Nielsen Estate*, the corporate director was not actively involved in the accident and the discussion centred on his conduct only as a director. I will discuss and counter the two reasons, then discuss how *Nielsen Estate* could have influenced this judgment.

Reasons One & Two

First, the Court of Appeal determined that the *Nielsen Estate* case was inapplicable because it dealt with the legislation prior to its amendment. *Nielsen Estate* was decided under a provision that excluded a director from the system if the work he was performing was "in the individual's capacity as a director" whereas now, the exclusion is broader, deeming directors not to be workers regardless of the nature of the work they were performing and excluding a director when the work was done as "part of the business of the corporation". As a result of being decided under the older, narrower provision, the *Nielsen Estate* trial judgment spent some time considering whether Epton had been acting as a director, which led the Court of Appeal in *Hall v Stewart* to conclude that it was "therefore no longer necessary to identify whether the work was being done 'as a director' or in some other capacity" (at para 17). This is true, in that it is arguably unnecessary to discuss the capacity in which Epton was performing the work, but it does not affect the legal points in the *Nielsen Estate* judgment, as to when liability will attach to corporate torts.

Second, whether a person was acting as a director, or as both a director and an employee, does not change the underlying analysis on director liability. A director's involvement in the incident, and the extent to which that director was performing the acts for the corporation, are the factors

determining liability. Whether that work was also done in the director's capacity as an employee does not diminish the overall liability. Failing to draw a distinction between Stewart's two capacities, and deciding his liability using principles of director liability, should have led this Court to rely on the *Nielsen Estate* case.

With regard to Stewart's liability as an employee, Stewart had brought an application to summarily dismiss the action against him in the decisions below, claiming that his actions were committed as an employee of DWS, not as an officer. The Court of Appeal lumped them both in the same category when questioning the potential liability of "officers and employees" when they cause damage by a tortious act and when questioning whether "an employee or director" will be held personally liable (at para 12).

At common law, certain torts trigger the same liability for any corporate actor, be it a director, an officer, or an employee. In *London Drugs*, where the issue was whether the employees were entitled to the benefit of their employer's limitation of liability clause, the majority held that the employees "unquestionably" owed a duty of care to the appellant, whose transformer they had physically damaged (at para 182). In *ADGA*, the Court maintained,

> These Canadian authorities at the appellate level confirm clearly that employees, officers and directors will be held personally liable for tortious conduct causing physical injury, property damage, or a nuisance even when their actions are pursuant to their duties to the corporation. (at para 26)

This same liability was recently confirmed in *Blacklaws v 470433 Alberta Ltd.*, 2000 ABCA 175 (CanLII), where a majority of the Alberta Court of Appeal wrote:

> We begin our analysis by acknowledging that there will be circumstances in which the actions of a shareholder, officer, director or employee of a corporation 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. Where those actions are themselves tortious or exhibit a separate identity or interest from that of the corporation so as to make the act or conduct complained of their own, they may well attract personal liability. (at para 41)

Nielsen Estate and How it Could Have Been Used

Had the Court of Appeal considered the *Nielsen Estate* case in *Hall v Stewart*, it may have led them to conclude that Stewart should not be liable for negligence.

Nielsen Estate should be considered with another Alberta case, *Bower v Evans*, 2016 ABQB 717 (CanLII), as the two cases help frame how directors' actions and involvement can give rise to liability. In *Nielsen Estate*, the director had both a duty to oversee workplace safety, which he did not fulfill, and he had been involved in the attempt to lift the beam while knowing there were safety problems. These factors led the court to find that Epton's acts were tortious in themselves. In *Bower v Evans*, the directors had not been involved with the work that was undertaken, they were not present when the work was being done, and they were not expected to give anyone instructions on how to do the work. *Bower v Evans* commented that the situation in *Nielse*

n Estate was not "authority for the proposition that a director who fails to carry out the duties of a director, or is negligent in doing so, is automatically personally liable. Rather, there must be something more, sufficient to establish independent tortious liability". In *Bower v Evans*, the Court found no evidence that the directors had any "operational involvement" (at para 18).

Bower v Evans and *Nielsen Estate* fall at either end of the spectrum: there was no operational involvement in *Bower v Evans* and there was involvement and direction while knowing of safety concerns in *Nielsen Estate*. In *Hall v Stewart*, which falls directly in the middle, there was operational involvement by Stewart, which may have even been negligent, but Stewart's actions, as found by all three courts, were performed within the scope of his employment and not done in furtherance of his own interests. This finding does not fall within the standard articulated in *Nielsen Estate*, showing how acts can become tortious in themselves. Had *Nielsen Estate* been considered, the *Hall v Stewart* decision may have been different.

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