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COMMERCIAL LITIGATION

Corporate Neutrality in Shareholder Disputes

by Jessica Mank & Daniel Yaverbaum

In November 2023, the British Columbia Court of Appeal released ***Yen v. Ghahramani***, 2023 BCCA 403, a decision that considered the corporate neutrality principle in shareholder disputes. The corporate neutrality principle refers to the principle that a corporation should remain neutral in disputes among shareholders.

BACKGROUND

The company involved was air-G – a private mobile gaming company. The case involved a dispute between the company's two main shareholders who were in stark disagreement over almost every aspect of the company.

Both had sued each other. The minority sued the majority and the company seeking an order for liquidation.

The majority shareholder and company were separately represented in the liquidation lawsuit. But, as found by the Court of Appeal, the company's response was "certainly not neutral".[1] The company repeated the same allegations against the minority shareholder that had been made by the majority shareholder in his lawsuit. The company also counterclaimed against the minority shareholder.

In response to these pleadings, the minority shareholder sought leave to amend its pleadings to allege that the company had been oppressive by improperly taking sides in the litigation and advancing a counterclaim for tactical purposes. The issue on appeal was whether these pleadings disclosed a cause of action.

THE COURT OF APPEAL'S FINDINGS

The Court found that the difficulty in this case arose from conflict of interest. It held that in a shareholder dispute, a company should not be taking instructions from someone not independent of both sides in the litigation.

In *Yen*, one individual – the majority shareholder – appeared to be instructing both his lawsuit against the minority shareholder and the company's defence. It appeared to the Court that the company had gone considerably father than defending the claim against it.

The Court noted caselaw outside of British Columbia which found that, that where such conflicts arise, the proper course is to require legal representation for the corporation separate and distinct from the legal representation of the majority directors and shareholders. It further noted that ideally, such representation should be chosen independently of the litigating individuals.[2]

However, the Court was not required to resolve whether the company's litigation conduct was improper. It was sufficient to find that a claim of oppression had been properly pleaded, as "even where the corporation is defending itself from dissolution. . . the minority may well have a reasonable expectation that the corporation would adopt a neutral position or that its resources would not be used in support of the majority's position."[3] It also found that the minority shareholder had pleaded unique harm by alleging that the company's

1 *Yen v. Ghahramani,* **2023 BCCA 403**, at para. 13.

2 *Messing et al. v. FDI, Inc.* 439 F. Supp. 776 (D.N.J. 1977).

3 *Yen v. Ghahramani,* **2023 BCCA 403**, at para. 53.

resources were used to fund two separate lawyers, doubling his opposition.

TAKEAWAYS

As noted in ***Yen***, there are few authorities in British Columbia on the application of the corporate neutrality principle and conflicts of interest in shareholder disputes.[4]

In other jurisdictions, the case law on the corporate neutrality principle is further developed. Some points that have emerged from the United Kingdom include:

- There is no absolute rule against active participation by a company in a shareholders' dispute.[5]
- Participation by the company will be appropriate where it is necessary or expedient in the interests of the company as a whole.[6]
- Where the true substance of a dispute is between shareholders, the company should not cause its funds to be expended on the legal costs of the dispute.[7]

Yen v. Ghahramani establishes that claims may exist for oppression based on breach of the corporate neutrality principle, and on conflict of interest. This case suggests that in situations of shareholder conflict it may be appropriate to instruct counsel through independent parties. Whether the caselaw will develop to require such practices remains to be seen.

If you have any questions, please get in touch with **Jessica Mank**, **Daniel Yaverbaum** or any other members of our Commercial Litigation group. Read more about our expertise in this area **here**.

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4 In *Discovery Enterprises Inc. v. Ebco Industries Ltd.*, **2002 BCSC 1236**, the British Columbia Supreme Court found that it had not been improper for the corporation to pay the costs of arbitration in a shareholders' dispute, which the court found was a "reasonable means chosen to avoid the wind-up" of the company.

5 *Halsbury's Laws of England* (4th ed., 2016 Reissue), vol. 7(2); Re a Company (No. 1126 of 1992) [1994] 2 B.C.L.C. 146 (Ch.).

6 *Halsbury's Laws of England* (4th ed., 2016 Reissue), vol. 7(2).

7 *Gott v. Hauge* [2020] EWHC 1473 (Ch.) at para. 53 and *Ross River Ltd. v. Waverley Commercial Ltd.* [2014] 1 B.C.L.C. 454.)

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