

## Recent developments impacting unanimous shareholder agreements in Ontario

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Unanimous shareholders agreements (USAs) are an important mechanism for establishing governance arrangements among shareholders for private companies in Ontario and most other Canadian jurisdictions. USAs are critically important to the ability of majority shareholders, such as private equity sponsors, to exercise control over the management of corporations in an efficient and practical manner. Conversely, USAs can establish and safeguard the rights of the minority shareholders. Two recent decisions of the Ontario Court of Appeal provide important guidance on how certain common USA provisions could be interpreted when majority and minority interests diverge.

### Waiver of statutory minority shareholder protections

In *Husack v. Husack*, the Ontario Court of Appeal upheld a lower court decision holding that a minority shareholder could not exercise statutory dissent rights in connection with a sale of substantially all assets of the corporation. The Court reached this conclusion notwithstanding that Ontario's *Business Corporations Act* (OBCA) provides for dissent rights in such circumstances and does not expressly contemplate that these rights can be modified or waived by a USA. The case dealt with a liquidation of assets of a family-controlled corporation in accordance with the will of a deceased family member. In this case, the USA expressly authorized the controlling shareholder to cause the corporation to effect a sale of substantially all assets and contained a general waiver by the shareholders of any statutory rights under the OBCA that conflicted with the USA, without expressly stating that dissent rights were waived.

Although the waiver in the USA was drafted broadly and did not refer to specific provisions or rights under the OBCA, the lower court held that the intention to waive dissent rights was "clear and unambiguous." The grant to the controlling shareholder of the exclusive authority to sell all or substantially all of the corporation's assets was sufficiently clear to oust the shareholder approval and dissent rights in connection with such a sale under the OBCA. The lower court noted that contractual waivers of statutory benefits are generally permissible absent a public policy reason not to enforce the waiver, and that no such public policy reason had been established in this case. In upholding the lower court's decision, the Court of Appeal also looked to the "constituent purpose" of the corporation, which in this case was to manage and operate the assets of the corporation in accordance with the decedent's will.

*Husack* indicates that a carefully drafted USA can benefit from a significant degree of judicial

deference, even when it includes provisions that waive important statutory minority shareholder protections.

## Compliance with contractual conditions for share repurchases

In *Leeder Automotive Inc. v. Warwick*, the Ontario Court of Appeal held that a corporation that had purported to exercise a right to purchase a minority shareholder's shares pursuant to the corporation's USA (characterized as a "right of first consideration") had repudiated the buy-sell provisions of the USA by making a purchase offer that did not comply with the valuation provisions of the USA. The case deals with a USA containing a "buy-sell mechanism" pursuant to which a shareholder who wishes to sell their shares must first provide notice to the corporation. The corporation was entitled to purchase the shares, on delivery of notice to the selling shareholder, for a purchase price determined in accordance with a valuation procedure stipulated in the USA.

The Court of Appeal upheld the lower court's finding that the corporation had materially breached the terms of the buy-sell provisions. The Court held that a standalone agreement had been created upon the provision of the notice to the corporation by the shareholder, together with the corporation's acceptance of the offer to sell. However, the corporation's failure to observe key conditions of the USA constituted a repudiation of this standalone agreement. The corporation's material breaches of the USA included

1. unilaterally selecting a non-independent valuator, when the USA required mutual agreement on an independent valuator
2. conducting the required appraisals in advance of the valuation date specified in the USA
3. relying on an unaudited valuation prepared on a "Notice to Reader" basis without applying GAAP, contrary to the express requirements of the USA

As the innocent contractual party, the minority shareholder was entitled to elect whether to continue with the contract in the face of the breach or to terminate it. He elected to terminate the share purchase transaction and remain a minority shareholder within the company. The Court's reasons do not address the status of the USA buy-sell provisions in the event that the shareholder decides to sell his shares in future. The Court's reasons suggest that only the standalone agreement arising from the buy-sell provisions was repudiated, not the underlying provisions of the USA.

*Warwick* demonstrates the importance of strictly complying with the terms of the USA when exercising purchase rights under the agreement, and the remedies that can be sought by minority shareholders where such terms are not complied with. The case also underscores the importance of carefully considering the terms of such buy-sell provisions at the drafting stage.