Raising the Bar

Raising the Bar – Fifth Edition

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"Learn from yesterday, live for today, hope for tomorrow."

Albert Einstein

Dear Friends,

We're very pleased to bring you the first 2013 edition of *Raising the Bar*, as our publication hits its second year.

In this issue, we shine a light on the law of fiduciary duties. We discuss which employment relationships attract a fiduciary duty and offer insight into some different applications of this duty which you may not be familiar with.

We share with you some interesting cases from the Ontario courts in the past few months. These decisions deal with a broad range of legal issues you need to know about, including the scope of documentary discovery, the primary factors governing releases, and whether conditional certifications in proposed class actions are possible.

You will also find out whether you are bound to settlement terms if you have not yet agreed upon the wording of the release.

We thank Julia Nanos, Jacqui Luksha and Joshua Concessao, whose hard work and contributions were essential to the publication of this issue.

We hope that you enjoy this issue, and as always, we look forward to hearing from you.

Frank Cesario and Elisha Jamieson
Co-Editors

IN THIS ISSUE

PART 1 – CASES YOU NEED TO KNOW ABOUT

Zenex Enterprises v. Pioneer Ballon, 2012 ONSC 7243 (CanLII)

The Plaintiff brought a motion seeking extensive production, including a "mirror copy" of the Defendant's hard drive. The Plaintiff argued that because certain relevant documents were not originally produced by the Defendant, there must be further undisclosed documents "lurking in its computer." The Plaintiff also sought to examine the methods used by the Defendant to conduct its search.

The Superior Court of Justice clarified the scope of the disclosure obligations found in the *Rules of Civil Procedure*. Rule 30.02 requires the parties to disclose and produce all relevant documents within their possession or control. Should further relevant documents come to light, Rule 30.07 requires that the parties disclose these documents and specify, in a supplementary affidavit, the extent to which the original affidavit requires modification. Parties are not obliged to explain how or where the relevant documents were found, or the methodology used to conduct its search for those documents. Justice Morgan dismissed the Plaintiff's motion, finding that the Defendant complied with these obligations. In the Court's view, it was evident that the Plaintiff was hoping to search the Defendant's computer in order to find an internal email "enabling the Plaintiff to make its case, but of which it has no actual knowledge." However, "this kind of trolling around through unknown waters … goes beyond rightful discovery." Evidence, rather than mere speculation, is needed in order to succeed on a Rule 30.06 motion.

R. v. Imperial Tobacco Canada, 2012 ONSC 6027 (CanLII)

In this case, Justice Rady of the Superior Court of Justice provided a succinct overview of the principles governing releases. The case involved a class proceeding brought against Imperial Tobacco (and others) by the Tobacco Board. Imperial Tobacco had already entered into a comprehensive release executed between it, the government of Canada and the provinces, which included language relating to lost taxes arising from Imperial Tobacco's alleged role in tobacco smuggling. The Court found that the claims made in this class proceeding were not "released claims" as defined in the executed release, and the action could proceed. In so finding, the Court made the following observations regarding "releases":

1. A release does not need a particular form in order to be valid.
2. The principles of contract interpretation apply to the interpretation of releases.
3. Releases must be considered contextually with regard to specific circumstances.
4. A release should be construed in accordance with the purpose for which it was made.
5. Where words are capable of two meanings, a release will be construed to promote the intention of the parties and, where applicable, "to promote a sensible commercial result."
6. A dispute or question that had not emerged at the time of the release cannot be "considered as bound and concluded by the anticipatory words of a general release."

Stewart v. Kempster, 2012 ONSC 7236 (CanLII)

In this personal injury action, the Defendant sought production of the Plaintiff's vacation photos and all other content on the "private" portion of her Facebook account, on the basis the information was directly relevant to the Plaintiff's "enjoyment of life" and her claim for damages. Justice Heeney of the Superior Court of Justice confirmed that the Plaintiff had a privacy interest in the "private" portion of her Facebook page. In the Court's view, it was evident that the Plaintiff expected a degree of privacy given that she excluded "roughly one billion people" from viewing her page. Moreover, the common law on disclosure must reflect *Charter* values such as privacy. With respect to the test for relevance under the Rules, Justice Heeney highlighted that the removal of the "semblance of relevancy" test from the Rules in January, 2010 was intended to "raise the bar" with respect to relevancy. In this respect, restraint ought to be exercised in the discovery process, and it should be conducted with due regard to costs and efficiency.

Justice Heeney dismissed the motion, concluding that the Defendant failed to demonstrate that the photos were relevant to any matter in issue, given that they showed nothing more than the Plaintiff sightseeing. This degree of relevance was not sufficient to justify invading the Plaintiff's privacy. With respect to the request to access all remaining private content, the

Court found it significant that the Plaintiff's "Timeline" did not lead to inferences about what might be contained in the "private" portion of her Facebook page. On this basis, the Court found that the Defendant's request was nothing more than a "fishing expedition."

Brown v. Canada (Attorney General), 2013 ONCA 18 (CanLII)

The Court of Appeal affirmed in this decision that, in the absence of a statement of claim that discloses a cause of action, a class action cannot be "conditionally certified." The Court stated that "certifying a class action in the absence of a statement of claim that discloses viable causes of action is not case management." Unlike the other criteria for certification found in section 5(1) of the *Class Proceedings Act, 1992* ("*Act*"), which are evidentiary in nature, the requirement for a cause of action found in section 5(1)(a) is to be determined on the basis of the pleadings. It must be "plain and obvious" that the statement of claim discloses a cause of action so that the Defendant can "meaningfully respond" to the application for certification.

The Court of Appeal remitted the certification motion to a different case management judge for determination on the basis of an amended statement of claim. The Court held that section 34(1) of the Act, which provides that the same judge shall hear all motions before the trial of the common issues unless he or she becomes "unavailable for any reason", leaves room for circumstances in which the principles of natural justice preclude the case management judge from continuing.

PART 2 – SHINE A LIGHT ON…*THE LAW OF FIDUCIARY DUTY*

Conventional wisdom is that fiduciary obligations only apply to senior management or "key" employees. While for the most part this is an accurate assessment, courts have shown a willingness to impose fiduciary obligations on other types of employees to protect an employer's interests.

In particular, courts have imposed fiduciary obligations on employees who have committed *fraud* against their employer or where they have *assisted* a fiduciary in competing unfairly against the employer. In this piece, we will shine a light on these areas of fiduciary law.

FIDUCIARY LAW: THE BASICS

A fiduciary duty may exist where the following factors are present: (1) the fiduciary undertakes to act in the best interests of the beneficiary; (2) the fiduciary has the power to affect the legal or substantial interests of the beneficiary; and (3) as a result, the beneficiary is vulnerable to the fiduciary.[1]

The Court of Appeal for Ontario has succinctly summarized these principles for employers as follows: "[i]n the employment context, an employee may therefore be said to owe a fiduciary duty to his or her employer where the employee has discretionary power to affect adversely the employer's interests and the employer is vulnerable to the exercise of that power".[2]

When a fiduciary obligation is imposed, what does it mean? The Supreme Court of Canada described the essence of the obligation as requiring a fiduciary to act with loyalty, good faith and to avoid any conflict of duty and self-interest.[3]This is a significant and exacting duty. It is logical that senior, management and key employees attract the duty due to their responsibilities and remuneration, which reflect their status within the employer's organization.

FIDUCIARY OBLIGATIONS AND EMPLOYEES WHO COMMIT FRAUD

Outside the realm of senior employees, courts have been increasingly cognizant of an employer's vulnerability to lower level employees who are in a position to commit a fraud against their employer. Courts have not hesitated to impose fiduciary duties on these employees, especially in situations where employees have responsibility for handling the employer's funds and have shown themselves to be faithless.

The utility of having the duty attach to such employees is evident from a review of recent cases, and is particularly prevalent in the context of an employee who is trying to avoid his or her obligations through a bankruptcy proceeding. In *Navrab Investments Inc. v. Vaidyan*[4], the employee was the manager of the employer food store. The store manager had stolen a total of $78,000 from the employer's cash register. The employer's concern was that the employee would assign himself into bankruptcy, seek a discharge of his debts and liabilities and thereby leave the employer without any avenue of relief.

There is a general rule that a discharged bankrupt is not liable for debts or liabilities incurred prior to his or her assignment into bankruptcy. However, there is an exception where the debt or liability was incurred as consequence of engaging in wrongdoing while acting in a fiduciary capacity. The Court concluded that, as a night manager, the employee held a position of trust over the entire operations of the store during his shifts and that it was a breach of his fiduciary duty to steal from his employer.

In *South Nahanni Trading Company Ltd. v. Grave*[5], the Court imposed a fiduciary duty on the employer's bookkeeper who had signing authority for the employer's general account and corporate bank account. The employee admitted to writing unauthorized cheques to herself. She consented to a judgment for conversion and later assigned herself into bankruptcy. The employer sought a declaration that her discharge from bankruptcy, when it occurred, would not release her from liability.

While recognizing that the bookkeeper was subject to supervision by the employer and its auditors or accountants, the Court nonetheless found a fiduciary duty on the basis that the fact of the fraud demonstrated the employee's ability to take the employer's funds without permission. The employer was clearly vulnerable to the employee's exercise of discretion and power. The fact that there were other employees more senior or with greater managerial responsibilities did not affect the nature of the employee's position and the duties that the position attracted.

A recent decision of the Court of Appeal for Ontario indicates that the willingness of courts to impose a fiduciary obligation on lower level employees is not restricted to situations where the rules of bankruptcy discharge might work an injustice against the employer.

In *Enbridge Gas Distribution Inc. v. Marinaccio*[6], the Court imposed a fiduciary obligation on the employer's operations supervisor. The employee had devised a scheme to defraud his employer by hiring contractors and approving invoices with no intention of having the work completed. Rather, the employee would divide the payments with partners who would pose as contractors for the projects. By the time the scheme was discovered, the employee had defrauded his employer of $6.5 million.

In imposing fiduciary obligations, the Court concluded that the employee's very ability to perpetrate such a large scale fraud over an extensive period of time was evidence that he occupied a fiduciary position. It should be noted that the Court was also reluctant to disturb the earlier finding of a fiduciary obligation where the issue was not contested in the courts below.

The employer also gained another important advantage: the ability to sue the fiduciary employee's partners in the scheme for the tort of knowing assistance in breach of a fiduciary duty. This aspect of the law is discussed further below.

These cases show that courts are mindful of an employer's vulnerability to employees who, while not necessarily senior management, exercise their discretion over a certain sphere of the employer's enterprise and possess the ability to cause considerable harm to their employer's interests.

FIDUCIARY DUTIES AND UNFAIR COMPETITION

Unlike instances of fraud, courts are generally unwilling to impose a fiduciary obligation on more junior employees in a manner that would restrict their ability to compete with their former employers. However, one exception to this prevailing tendency is where the employee has assisted a fiduciary to breach his obligations and compete unfairly with the employer.[7] This exception is also important for employers because it permits the employer to pursue as a remedy the wrongful gains made by the departing employees, rather than limiting itself to the losses it has suffered.[8]

In *Sanford Evans List Brokerage v. Trauzz*[9] , the fiduciary was the employer's vice-president and was responsible for an entire division. She left her employment and began to work for a competitor. The employee was joined by two junior employees who, at the time of their resignation, were the office manager and sales account representative. Upon leaving their employment, the former employees began soliciting clients with whom each of them had contact while employed by the Plaintiff. The Court imposed a fiduciary duty on the junior employees who had left with the vice-president.

In *DiFlorio v. Con Structural Steel Ltd.*[10], the fiduciary was a long service employee who had a specialized expertise that was unique within the employer's organization. The case involved a falling out among the principal owners of a family business. The employee chose to join a competing business set up by the family member who had sold his ownership interest in the company. The manner and timing of his departure left the employer without any access to the highly specialized expertise the departing employee possessed. The employee's title during his employment was estimator and shop foreman. The Court held that, as a consequence of his specialized expertise and role in the organization, the departing employee was a key employee and part of the employer's senior management. It also stated, however, that fiduciary obligations would attach regardless of his position as a key employee since they specifically apply to a non-fiduciary employee who departs with a fiduciary for the purpose of setting up a competing business.

CONCLUSION

Employers should be mindful that they may have several employees, in addition to senior management or "key" employees, who the law will consider to be fiduciaries. These fiduciaries owe exacting duties to the employer. Where an employer is vulnerable to an employee's exercise of discretion, the courts will be open to imposing a fiduciary obligation to protect the employer's legitimate interest. Therefore, employers should be aware of their rights to hold faithless employees to account. The protection of your organization could depend upon it.

PART 3 – DID YOU KNOW?

Did you know that…when parties enter into Minutes of Settlement subject to the execution of a release, they are bound to that settlement even if the wording of the release has not yet been agreed upon? It's true. (*Di Gennaro v. BMO Nesbitt Burns Inc.*, 2013 ONSC 37 (CanLII)).

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[1] *Galambos v. Perez*, 2009 SCC 48 at paras. 68-70; *Enbridge Gas Distribution v. Marinaccio*, 2012 ONCA 650 at para. 16

[2] Enbridge, *ibid.*

[3] *Can. Aero v. O'Malley,* [1974] S.C.R. 592 at pp. 605-606.

[4] [2012] O.J. No. 5704 (Ont. S.C.J.)

[5] (2007) 36 C.B.R. (5th) 115 (Ont. S.C.J.)

[6] 2012 ONCA 650 (CanLII)

[7] *Alberts v. Mountjoy et al.*, [1977] O.J. No. 2334 at pg. 4 (H.C.J.).

[8] *Can. Aero ibid.* note 1 pg. 622

[9] [2000] O.J. No. 1394 (Ont. S.C.J.)

[10] [2000] O.J. No. 340 (Ont. S.C.J.)