Revitalizing Forfeited Corporate Property

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Submitted by: The Ontario Bar Association

ONTARIO BAR ASSOCIATION
A Branch of the Canadian Bar Association

L'ASSOCIATION DU BARREAU DE L'ONTARIO
Une division de l'Association du Barreau canadien

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The Ontario Bar Association ("OBA") appreciates the opportunity to provide input - from lawyers who are experts in the relevant fields - on the Ministry of Infrastructure's (the "Ministry") proposed framework for revitalizing forfeited corporate property (the "Framework"). We look forward to continuing to work with the Ministry as it develops the legislation, regulations and policy to implement the new Framework.

The OBA

(a) Background

As the largest legal advocacy organization in the province, the OBA represents approximately 18,000 lawyers, judges, law professors and students in Ontario. OBA members are on the frontlines of our justice system in no fewer than 38 different sectors and in every region of the province. In addition to providing legal education for its members, the OBA assists government and other decision-makers with several policy initiatives each year - both in the interest of the profession and in the interest of the public.

(b) The OBA's Forfeited Corporate Property Working Group

This submission was formulated by an OBA working group composed of members from our Business Law, Environmental Law and Real Property Law Sections. Together, these sections have 3,000 members, including leading practitioners in each of these fields. The lawyers in these sections would count among their clients virtually every stakeholder interested in the issue of corporate dissolution and forfeited property, including: corporations; shareholders; directors; secured and unsecured creditors, government; developers; financial institutions and other lenders; environmental groups; and citizens and property owners who may be affected by property that falls into disuse and disrepair. The lawyers in the constituting sections of this working group have expertise in, among other things, corporate dissolution and revival, financing, environmental and other corporate liability issues, directors' and officers' liability, environmental approvals processes, adverse possession, title and other property transfer issues.

Introduction

The OBA congratulates the Ministry for its effort to add transparency and efficiency to the transfer of forfeited corporate property. We support the goal of providing a clear and consistent regime for returning properties to productive uses as quickly and safely as possible.

We have addressed three categories of issues with the Framework:

I –Proposals included in the Framework that that are beyond, or even inconsistent with, the government's stated goals and may, in practice, thwart rather than advance those goals;

II – Additional reforms, not included in the Framework, that may be necessary to achieve the government's goals; and

III – Other legal issues including, most significantly solicitor-client privilege issues.

I – Framework Proposals Inconsistent with Government Goals

(a) Issues with Preventing Dissolution in Some Circumstances (Proposal 3.3)

Proposal 3.3 would prevent a corporate entity from dissolving in order to ensure that contaminated lands do not escheat to the Crown. It is, of course, solid public policy to prevent an off-loading of clean-up responsibilities from corporations to taxpayers. However, there may be situations in which a transfer to the Crown is the only way to allow for sufficiently urgent clean up and remediation of a dangerous site. In these cases the public protection would be enhanced by an immediate voluntary dissolution rather than waiting for an event to trigger involuntary dissolution[1]. So, while a default prohibition on voluntary dissolution is sensible, the prohibition should not be absolute. There should be some efficient, summary process for determining when immediate voluntary dissolution and transfer would be in the public interest.

(b) Expanded Officers and Directors Liability (Proposal 3.3)

The *Environmental Protection Act* already provides extremely broad liability for the officers and directors of corporations, particularly those who are in any way at fault in the occurrence of the contamination. Corporate law provides that dissolution of the corporation does not affect this liability – it neither mitigates it nor increases it. While there is no objection to making explicit the fact that dissolution will not absolve officers and directors of liability, the Framework proposal seems to go further than the current state of the law. While the current liability regime provides for strict liability in some

[1] It should be recognized that preventing voluntary dissolution will, in many cases, delay rather than prevent transfer of a contaminated site to the Crown. Corporations that are avoiding fulfilling environmental orders and risking the civil liability of failing to address contamination will likely become candidates for involuntary dissolution at some point as they fail to meet their other obligations.

cases, it does not provide for absolute liability. The Framework's proposed liability scheme, on the other hand, does suggest an absolute liability regime for officers and directors of dissolved corporations. The proposal expands the existing liability by retroactively imposing cleanup costs on officers and directors of dissolved corporations despite the fact that they were not at fault. This is problematic in several ways:

(a) A rational corporate law regime requires that dissolution should in no way affect liability. Where dissolution is desirable, it should not be disincentivized by putting directors of a dissolved corporation in a worse position than they would be in if their defunct corporation continued to exist;

(b) Absolute liability has the potential to infringe constitutional and legal rights. At a minimum an absolute liability regime would very likely limit the penalties that can be imposed. Generally, where penalties include a prison term, even regulator offences aimed at the effective enforcement of environmental protection must "allow the accused to exculpate himself by showing that he was free from fault;"[2]

(c) Perhaps most importantly, imposing this expanded liability will discourage qualified people from accepting positions as officers and directors of troubled companies. In that qualified officers and directors may be capable of reversing the company's fortunes and ensuring compliance with various environmental and other standards, the current proposal runs counter the government's goals of restoring corporate property to productive use and avoiding the potential risks of negligent or willful failure to remedy contamination.

It is recommended that the government provide information on, and, if necessary, codify, the current state of the law rather than expanding liability. Such an expansion is a much larger issue than forfeited property and would require much broader and more extensive consultation.

(c) Adverse Possession (Proposal 4.1)

The public policy behind the law of adverse possession is to encourage the productive use of property that would otherwise lay dormant. The Ministry has indicated that it has the same goals with respect to forfeited property. Restricting adverse possession by, for example, stopping the adverse possession clock as proposed in section 4.1 of the Framework is contrary to this goal. There is no significant advantage to the government that would outweigh the threat to the credibility of the Framework that is posed by this seemingly imbalanced and contradictory recommendation. In fact, the recommendation is of very limited value to the government in that:

[2] Rv. Sault Ste. Marie, [1978] 2 S.C.R. 1299

(i) it would be necessary to show 60 years of continuous, notorious and open use before a party can adversely possess Crown–owned land. Take a scenario in which the government acquired the property on the very eve of a ten-year adverse possession claim against the forfeiting private owner. While the matter is not completely free from doubt, the better answer is that the Crown would have 50 years to discover it owned the land before an adverse possession claim would vest. This is sufficient time by any reasonable standard without having to stop the clock; and

(ii) all but a fraction of properties are now registered in the land titles system, which means that adverse possession claims will be very rare. They would generally apply only to already-vested claims (i.e. where the adverse possession period had already elapsed before the property was in land titles) and the very small percentage of properties that have not yet been converted to land titles. Adverse possession claims are extremely unlikely to arise in the forfeited corporate property regime.

So, the recommendation would extend an already generous timeframe in the very unlikely scenario that the government receives land that is not yet registered in land titles. The public policy advantage does not therefore justify the appearance that the government is providing itself with an unfair advantage over potential adverse possessors that is not enjoyed by private property owners.

(d) Fair Treatment of Creditors – Striking the Right Balance (Proposal 2.1)

The dissolution of a corporation should only result in the loss of the property that is owned by the dissolved corporation and should not result in a loss of property by its creditors – particularly secured creditors (who have lent on the security of the assets of the debtor corporation). It matters not whether the security is a mortgage/charge of land, subject to a security interest under the *Personal Property Security Act* or other statutory regime. Extinguishing the security interests of secured creditors is unnecessary and confiscatory, even if it is done on notice. Corporate properties regularly operate while encumbered and allowing creditors to maintain their rights does not preclude returning property to productive use.

It is understandable that the government does not want to take on liability to creditors that exceeds the value of the property. However, this goal can be achieved in a more balanced way than appears in the current Framework proposal. The legislation that implements the Framework could provide that the Province, in effect, steps into the shoes of the dissolved corporation (receiving its equity in the property subject to any valid security interests encumbering such property) except that the Province's liability is limited, on a without recourse basis, to the forfeited property. Thus, if Ontario acquires forfeited property worth $3 unencumbered but that is actually encumbered by security interests totaling $4, the Province has no residual liability if the property is sold for $4 or

less. This represents a better balance of interest that the currently proposed scenario in which the Province could eliminate the security interest and would be $3 better off than the dissolved corporation whose property was forfeited. The Province in the latter scenario would effectively be receiving a property interest that the transferring corporation did not have to give.

To buttress the non-recourse liability protection for the province, there may be some advantages in using a special-purpose, government-owned corporation to receive all forfeited corporate property. It would provide a layer of insulation against the Province inadvertently taking on unwanted liabilities (whatever their source may be).

(e) Limitation period for Return of Property to a Revived Corporation (Proposal 2.2)

The goals of having fewer properties forfeited to the government and reducing the administrative burden on government are not served by the proposed drastic reduction of the period in which a corporation may reclaim its property upon revival – from 20 years to three years. There are several reasons that this is undesirable:

(i) the drastic shortening of the period appears confiscatory. Three years is, in practice, an unduly short timeframe for shareholders and other investors to discover and take action to recover corporate property, including reviving the corporation for that purpose. The inappropriateness of this proposed time limit is evidence perhaps most starkly by the very wide gap between the 20 years in which a corporation can revive itself versus the three years in which it can reclaim its property after doing so. Given that reclaiming the benefits of property for the true owners (shareholders etc.) is the whole raison d'être for revival, the drastic gap in these two time periods is not sound policy.

(ii) the "saving" provision that would allow a revived corporation to seek special government permission to reclaim property after the expiry of the new three-year period is problematic in that:

a. it will increase the administrative burden on government by necessitating a new process that, in turn, leads to appeals and judicial reviews. Under past regimes that required an application after five years, practitioners and the government found delays and administrative resource requirements to be too great;

b. it will put the government in a conflict of interest in deciding whether to return valuable forfeited or escheated property. Even assuming appropriate division between the ministries who benefit and ministries who decide, bias will be perceived;

c. it will disadvantage smaller shareholders who are more likely to just let it go rather than seek to reclaim the property in some manner; and

d. it could cost employees their jobs – as some businesses continue to operate for some time without being aware that the underlying corporation has been inadvertently dissolved (because a notice was sent to a former address of the corporation's registered office);

(iii) where a corporation is revived to continue the business that it has been conducting during the period from its dissolution to its revival, that corporation is in the best position to use their former properties quickly. The government, on the other hand, may spend many years rehabilitating the property for alternative use or locating a buyer with the same land and facility needs as the dissolved corporation. A longer timeframe for reclaiming property may, in fact, be a quicker and more efficient way of returning the property to productive use.

Rather than an impractical three-year timeframe combined with a burdensome system of seeking government permission to effectively extend the timeframe, we would recommend a single, final timeframe of ten years, following the dissolution date, in which corporate property will be returned to a corporation upon revival. This is a more appropriate balancing of the goals of returning property to productive use quickly and ensuring that there are fewer properties under government management and more under the control of rightful owners.

The ten-year ultimate limitation would also align with the period suggested in the relief-from-forfeiture process proposed in section 2.6. Aligning the two time periods would, in fact, eliminate the cumbersome relief from forfeiture process as well. Rather than a three year timeframe layered with two cumbersome processes (the permission process in 2.5 and the relief from forfeiture process in 2.6) there would be a single time limit for, and no cumbersome administrative process around, the return of forfeited corporate property to a revived corporation or others with an ownership claim. The property would escheat after ten years, subject only to the remaining interest of creditors.

II – Additional Reforms

The following reforms are necessary corollaries of the reforms outlined in the Framework and will assist the Ministry in achieving its stated goals.

(a) An Efficient Corporate Revival Regime

The effective disposition or continued use of corporate property will sometimes depend on the efficient revival of a corporation. Currently, under the *Business Corporations Act* ("OBCA"), there are three ways that a corporation can be dissolved and two very different revival processes apply.

1. The corporation can be involuntarily dissolved for failure to file a tax return or file a notice of change under the *Corporations Information Act*, it can be administratively dissolved. In these circumstances the corporation can be revived with retrospective effect through an administrative application process if that application is made within 20 years from the date of dissolution.

2. A corporation can also be involuntarily dissolved for cause – typically not complying with the requirements to have at least one director and a board consisting of at least 25% resident Canadians. In this case, dissolution falls under a different provision and the administrative revival regime does not apply. Rather, the Legislature must pass a Private Act to revive the corporation.

3. A corporation can be voluntarily dissolved (which is common but through inadvertence failed to transfer all of its property before obtaining its certificate of dissolution). Reviving this corporation will also require the passing a Private Act.

Passing Private Acts is expensive for the applicant and a waste of Legislative time and resources.

The OBCA should be revised to adopt a consistent approach and reduce the administrative/Legislative burden by providing that, in all cases, a dissolved corporation can be revived with retrospective effect by filing articles of amendment (except in those rare cases where the shareholders wish to revive a corporation outside the ten-year revival window and seek a return of its property through the saving provision). Where the dissolution was for cause, the Director's consent should be required so that the Director can ensure that whatever caused the dissolution (e.g., non-compliance with board composition requirements) is cured as part of the revival. The same analysis applies under the pending *Not-for-Profit Corporations Act, 2010* (which is not yet proclaimed).

(b) Method of Proof Regarding Corporate Property (Proposal 1.1)

The Ministry's suggestion that voluntary dissolution requires a corporation to demonstrate that it has dealt with all of its property is a sensible way to reduce the number of properties forfeited to the government, particularly inadvertently, and to ensure the owners and creditors of a corporation receive the benefit of disposition before dissolution. However, the proposed statutory declaration, while necessary, may not in and of itself be sufficient proof of this. Corporations on the verge of dissolution

may not be functioning at full managerial capacity and may, in fact, be in significant disarray. Internal records of property may be incomplete or poorly organized and a proper record review may not take place. In short, the company may not know with sufficient certainty what property it has, may do an incomplete job of disposing of it and may inaccurately report full disposition on the statutory declaration. In order to ensure due diligence and accuracy in this regard, it is advisable to require the corporation to complete certain searches and attach the results to the statutory declaration - a "clear" search from Teraview in respect of the corporation's real property is likely the most critical example. Attaching search results will help to ensure the proper searches were done and done properly.[1]

(c) Notice to Automatic Recipients (Proposals 2.4 and 2.5)

The proposed streamlined process for orphaned subdivision and condominium properties provides that specified parties receive the forfeited land/unit without their consent. We recommend the addition of a notice requirement to this process. Notice to the proposed recipient would:

(i) help ensure that the recipient has an opportunity to effectively manage the property upon receipt (arranging for insurance and maintenance contracts etc.); and

(ii) allow for any disputes (eg. disputes regarding whether the proposed recipient is the proper recipient) to be resolved before transfer rather than by way of multiple transfers and reversals.

(d) Title Certainty Issues (Proposal 4.9)

The government understandably wishes to eliminate the cumbersome administrative process that currently arises when a "purchaser" seeks relief after discovering that the purported "vendor" was a dissolved corporation and was not, therefore, a legal entity capable of conveying title. In order to eliminate this problem, the Ministry recommends that a corporate search become a mandatory step in any transfer of corporate land. Lawyers will be required to state in the electronic title transfer that a corporate search has been done to ascertain that the vendor is an active corporation. This recommendation is a good one. However, in order to ensure that it has optimum effect, the following corollary reforms are necessary:

(a) currently, the chain of title and corporate status information is not effectively displayed on the available search-result documents, in that ownership searches

[1] Currently, a "clear" search would have to be conducted in each of 54 counties. It may be necessary for Teraview to streamline this search to allow for an efficient process for dissolving corporations, government and others searching for corporate property.

are presently limited by county. Consideration should be given to creating a province-wide ownership search to facilitate this type of search. The ministries involved should coordinate the information available to satisfy the searching obligation created;

(b) the proposal appears to recommend that a lawyer search and make a declaration as to the status of the corporation that is currently purporting to transfer the subject property. There may still be title imperfections if a corporation that transferred the property in an earlier transaction was dissolved or otherwise non-existent at the time of that previous transfer. Searching the current vendor's status would not resolve these pre-existing title issues and a requirement to search all previous corporate vendors is costly, impractical and would discourage efficient land transfers from dissolving corporations. In order to ensure clear title, encourage the efficient transfer of property and avoid legal disputes and appeals to the government, it is recommended that any "corporate status" issues that may have arisen on previous transfers be essentially "erased". Precedent for this can be found in the *Planning Act*.

III- Other Legal Issues

(a) Privilege (Proposal 4.4)

The Framework proposal suggests providing, to the Minister of Infrastructure:

> express authority …to compel production, from anyone the Minister considers appropriate…of information regarding the dissolved corporation or the forfeited corporate property (Draft Framework at p.25).

Like any authority to compel production of documents and information, this authority will be subject to solicitor-client and related privileges. The Minute Books and other documents belonging to the dissolved corporation will be the property of the government (having forfeited to the government with the other property of the corporation) and, therefore, available to it the government. However, there may be privileged information that fits within the overly broad discretion outlined in the Framework. For example, a lawyer representing a third-party with a litigation claim against the corporation or a lien claim on the forfeited property would have opinions and correspondence related to the legal strength of the claims. While this would be "information regarding the … forfeited corporate property" it would clearly be privileged and, therefore, not compellable.

We assume that, at the implementation stage, there will be a recognition of the privilege that limits compellability. The common law will imply this recognition absent express

provisions to the contrary (which provisions would not be constitutionally appropriate in this circumstance). However, we recommend explicit recognition of the privilege in order to ensure all those dealing with the issue have a clear understanding of the limits of compellability. An explicit recognition of this privilege can be found in the OBCA:

> 166. Nothing in this Part shall be construed to affect the privilege that exists in respect of communications between a solicitor and his or her client. R.S.O. 1990c. B. 16, s. 166

and in other statutes by which the government compels the production of information. The *Broader Public Sector Accountability Act*, for example, provides:

> 1(3) Nothing in this Act shall operate so as to require the disclosure of information that is subject to solicitor-client privilege, litigation privilege or settlement privilege. 2010, c. 25, s. 1 (3).

The latter provision includes the appropriate description of all of the applicable legal privileges that may apply in the circumstances addressed by the Framework.

(b) Other Issues with Respect to Ongoing Management

The draft Framework seems to address issues surrounding the initial transfer of land from forfeited corporate properties: the strength of title; the fungibility of the interest acquired by the government (i.e. how quickly and easily can the government transfer its interest); ensuring the government does not take on an inappropriate degree of liability as a result of the transfer etc. This is in and of itself a worthwhile and ambitious agenda for the first round of reform. When, however, the government undertakes reform with respect to the ongoing management of forfeited lands, the OBA will have additional comments, including:

(a) it should be possible for the public to objectively determine which sites have escheated to the Crown;

(b) the province should have a clear and transparent process for identifying and managing the environmental risks of such properties, especially where they threaten public health and/or the legitimate interests of innocent third parties; and.

(c) an important secondary factor discouraging the reuse of contaminated sites is the expense, delay and uncertainty involved in the risk assessment process. We recommend that there be full public consultations and a further reform to the Ministry of Energy and Infrastructure Class Environmental Assessment processes.

Conclusion

Once again, the OBA appreciates the opportunity to provide input on the complex issues raised by the proposed Framework. We look forward to the next stage of consultation and continuing to work with the Ministry as the Framework is finalized and implemented.