

Appeal Court to consider fairness to corporations of "golden parachutes"

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Corporate employers in Ontario may soon receive guidance from the Court of Appeal about the enforceability of overly generous "golden parachute" agreements with executives. At issue is subsection 132(7) of the province's *Business Corporations Act*, which provides that material contracts between a corporation and a director or officer are permissible if the director or officer disclosed his or her interest in the contract and the contract is "reasonable and fair to the corporation" at the time it was approved.

The Ontario Court of Appeal will be asked to consider a decision of the Ontario Court, General Division, which declared that the severance provisions in Peter Scott Rooney's contract with his employer were unenforceable due to their unreasonableness. Rooney was a director and principal shareholder in Cree Lake Resources, the corporation with which he had a management services contract and from which he was seeking the severance. Rooney's contract had provided for the severance to be paid in the event two directors not proposed by Rooney were elected to the board. There was no right of termination on notice.

Rooney was removed from his position in July 1996, shortly after his initial contract had been extended to run until April 2001 and his compensation doubled. His removal, which triggered a severance entitlement of \$235,000, was effected to avoid conflict with dissident shareholders distressed over a change in the corporation's direction. Although the severance was negotiated down to \$175,000, the dissidents expressed shock at Rooney's ouster as CEO. They wanted to remove him from the board, but to retain his services in management. The new board opposed Rooney's claim, principally on the grounds that the management agreement was unenforceable. Rooney sued for wrongful dismissal.

In *Rooney v. Cree Lake Resources Corp.* (July 29, 1998), the General Division Court agreed with the board. Noting that, under the Act, the contract did not have to be reasonable or fair to directors, but rather to the corporation, it rejected Rooney's argument that the purpose of the contract was to provide stability. Under the golden parachute clause, the corporation, with assets of \$338,000, would have to pay Rooney "as much as \$240,000". Such a "catastrophic" result meant the contract could not be reasonable or fair to the corporation: "A contractual provision which could result in the payment of unearned compensation in a lump sum equal to over 70 per cent of Cree's assets, when there is no reasonable prospect of any sudden influx of capital or income, could not possibly be in Cree's best interests. This was clearly an attempt, in the guise of providing stable leadership, to entrench a particular board and management, and, as such it is repugnant to any concept of reasonableness and fairness."

However, the Court held that Rooney had been wrongfully dismissed, and awarded him six months' notice. Rooney is appealing the decision. We will keep readers advised of developments in the case.

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