

CANADA / JUDGMENT

2538520 Ontario Ltd. v. Eastern Platinum Limited

2020 BCCA 313

COURT

British Columbia Court of Appeal

DECIDED

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2020 BCCA 313 2538520 Ontario Ltd. v. Eastern Platinum Limited

COURT OF APPEAL FOR BRITISH COLUMBIA

Citation:

2538520 Ontario Ltd. v. Eastern Platinum Limited,

2020 BCCA 313

Date: 20201116

Docket: CA46370

Between:

2538520 Ontario Ltd.

Appellant

(Petitioner)

And

Eastern Platinum Limited

Respondent

(Respondent)

Before:

The Honourable Madam Justice Bennett

The Honourable Mr. Justice Goepel

The Honourable Madam Justice Griffin

On appeal from: An order of the Supreme Court of British Columbia, dated August 27, 2019 (2538520 Ontario Ltd. v. Eastern Platinum Limited, 2019 BCSC 1446, Vancouver Docket S1811839).

Counsel for the Appellant (via videoconference):

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A.C. Bjornson

Place and Date of Hearing:

Vancouver, British Columbia

June 1, 2020

Place and Date of Judgment:

Vancouver, British Columbia

November 16, 2020

Written Reasons by:

The Honourable Madam Justice Griffin

Concurred in by:

The Honourable Madam Justice Bennett

Dissenting Reasons by:

The Honourable Mr. Justice Goepel (Page 34, para. 144)

Summary:

The appellant applied for leave to commence a derivative action on behalf of the respondent. The judge found that the proposed action in negligence was in the best interests of the respondent, but that the appellant did not prove it was acting in good faith. The appellant argues the judge erred by failing to consider its belief in the merits of the action, drawing unsupported inferences, and finding that a derivative action was not appropriate because the appellant sought to protect the value of its shares. Held: Appeal dismissed, Justice Goepel dissenting. Majority (per Justice Bennett and Justice Griffin): The judge properly considered the appellant's belief in the merits of

the action before finding the appellant had not proven good faith. There was evidence to support the judge's finding that the appellant had ulterior motives. It was not inconsistent for the judge to find a lack of good faith while also finding the proposed action had merit. The judge's best interests analysis was not fully fleshed out. The judge's obiter comment regarding the oppression remedy referred to the appellant's concerns about mistreatment as a minority shareholder and was not an error.

Dissent (per Justice Goepel): The chambers judge properly found the proposed action was in the best interests of the respondent. The judge erred in law in stating that the onus of proving good faith is "substantial", rather than merely on the balance of probabilities, and in failing to consider relevant evidence. The inference that the appellant was driven by ulterior motives was unsupported and warrants appellate intervention. This Court can conduct a fresh analysis of whether good faith was proven, and upon review it was. The appellant met all the criteria for commencing a derivative action.

Reasons for Judgment of the Honourable Madam Justice Griffin:

OVERVIEW

- [1] The appellant, 2538520 Ontario Ltd. ("253"), is a shareholder of the respondent, Eastern Platinum Limited ("EPL"), a British Columbia company. This appeal arises from the dismissal of 253's application under s. 232 of the Business Corporations Act, S.B.C. 2002, c. 57 [BCA], for leave to commence a derivative action on behalf of EPL against various past and present directors and officers of EPL (the "Proposed Defendant Directors").
- [2] The proposed lawsuit alleges that the Proposed Defendant Directors breached fiduciary duties and were negligent in relation to EPL's operations. Specifically, 253 complains about EPL entering into a framework agreement and related transactions with a company, "Union Goal", related to the recovery and sale of chrome from stored tailings at one of EPL's subsidiary's mines in South Africa, the Crocodile River Mine (the "Mine").
- [3] In summary, the breach of fiduciary duty aspect of the claim alleges that the Proposed Defendant Directors preferred their own interests or the interests of third parties, including direct and indirect shareholders of Union Goal, to the detriment of EPL. The negligence aspect of the proposed claim alleges that the Proposed Defendant Directors failed to conduct sufficient due diligence before approving the deal with Union Goal.
- [4] The evidence adduced by 253 in support of its application was that of its Chief Executive Officer, Mr. Rong Kai Hong.
- [5] In reasons indexed at 2019 BCSC 1446, the judge dismissed the application. The judge found that 253 did not prove that it was acting in good faith, which is a necessary condition for leave to commence a derivative action.

- [6] The judge's conclusion that 253 did not prove it was acting in good faith was a finding of fact, made after applying the correct legal test. For the reasons that follow, I conclude that the appellant has not met the standard of showing that the judge made a palpable and overriding error in his finding of fact. I would dismiss the appeal.

JUDGMENT BELOW

- [7] The judge began his judgment by concisely summarizing the background facts of EPL's deal with Union Goal:
- [2] EPL owns, through an indirect subsidiary, a South African platinum and chrome mine known as the Crocodile River Mine. Mining activity from 1980 to 2013 produced tailings that contain chrome oxide and other minerals. The goal of the Retreatment Project is to recover marketable product from those stored tailings. Until work began on the Retreatment Project in late 2018, the mine had been on "care and maintenance" status, meaning that there were no active mining operations since 2013.

THE RETREATMENT PROJECT

- [3] The Retreatment Project is being conducted under contracts with Union Goal Offshore Solutions ("Union Goal") and includes the purchase by EPL of equipment and technology from Union Goal. Part of 2538520's objection is that EPL already had its own retreatment equipment at the mine site.
- [4] In September 2017, EPL received a technical report from Sound Mining, a consultant firm in South Africa, that recommended use of the existing equipment to recover chrome from the tailings. It estimated that EPL could process 6.4 million tons of mineral resources at a total cost equivalent to CAD \$19.7 million, with positive cash flow generated after ten months of operation and a break-even point reached after 25 months. According to Sound Mining, the net present value of the profit to be generated from the project was \$3.82 million.
- [5] Rather than proceeding with the project as envisioned by Sound Mining, EPL entered into a memorandum of understanding with Union Goal in late 2017. That was followed by a "framework agreement", dated March 1, 2018. The specific transactions contemplated by the framework agreement were implemented through a number of further contracts executed in August 2018. The basic structure of the project includes:
- a) The construction of a new plant, financed by a loan and initial payment from Union Goal;
 - b) The purchase of equipment from Union Goal; and
 - c) The sale of recovered chrome to Union Goal.

- [6] EPL expects the new equipment and technology supplied by Union Goal to produce much greater mineral recovery than the older existing equipment, but 2538520 says EPL has refused to disclose what due diligence (if any) it conducted to determine the feasibility of those projections. In any event, it says all of the benefits of that increased recovery will go to Union Goal.
- [7] The petitioner says the amounts EPL will have to pay to Union Goal for equipment and in repayment of financing far exceed the revenue that EPL can obtain from the Retreatment Project. It estimates a shortfall of at least US \$20 million. The agreement allows Union Goal to be paid in EPL shares, rather than cash, but 2538520 says that will result in Union Goal taking over EPL. It says that, as of December 31, 2018, EPL owed Union Goal US \$45 million. If that amount is paid in new shares at EPL's current share price, 2538520 says Union Goal will have more than 75% of the outstanding shares of EPL and existing shareholders will be diluted to the point that their shares will be virtually worthless.
- [8] EPL says the benefits of the transactions include:
- a) Union Goal financing the construction of the new plant;
 - b) The increased production offered by the new technology used in the Union Goal equipment;
 - c) Recovery of platinum group metals, as well as chrome, from the increased tonnage. (Although the chrome is to be sold to and marketed by Union Goal, the platinum group metals will be solely for the benefit of EPL);
 - d) An upfront payment to EPL of CDN \$3.7 million, equivalent to the net present value of the profit projected in the Sound Mining report;
 - e) Union Goal will pay for delivery of the tailings material to the treatment facility, allowing EPL to recover its capital expenditure as well as an additional amount on a per-ton basis; and
 - f) Union Goal is responsible for all operating, re-mining, disposition, and logistics costs of the project.
- [9] EPL also says that, although it must eventually repay Union Goal's loan and pay Union Goal for equipment, it is protected by a "put option" contained in the framework agreement. Either party may provide notice to trigger a negotiating period in which a purchase price can be reached for the equipment. If there is no agreement in 60 days, the equipment is to be re-purchased by Union Goal at a default price equal to the total costs incurred. That would also result in cancellation of the loan from Union Goal.
- [10] 2538520 says the put option does not give EPL unfettered discretion to unwind the transaction or to dictate the financial terms. There is no guarantee that the negotiations called for will result in pricing more favourable to EPL.

- [11] EPL says the arrangement with Union Goal has resulted in the first active operation at the Crocodile River Mine since 2013. The first shipment of 10,000 tons of chrome concentrate was completed in February 2019.
- [8] The judge then reviewed the facts of 253's demand to EPL's board asking it to commence proceedings against the Proposed Defendant Directors. In response to the demand, the board of EPL appointed a special committee of three directors to consider the matter. The special committee was comprised of George Dorin, as board chair and a non-voting member, and Nigel Dentoom and Alex Guan as voting members (para. 12). The latter two men were appointed directors after EPL approved the framework agreement but before it entered into the implementation agreements with Union Goal (para. 12).
- [9] The judge noted that 253 brought its petition within only 10 days of delivering its proposed claim to the company and before the special committee had time to conclude its deliberations (para. 14). A complainant on a derivative action application must meet the condition of having made reasonable efforts to cause the directors of the company to prosecute the proceeding: BCA, s. 233(1)(a).
- [10] There is some basis for an argument by EPL that 253 did not give EPL a reasonable opportunity to respond to its demand to commence litigation, but I do not see this appeal turning on that issue, as the special committee's recommendations were known by the time the petition was heard. However, the eagerness of 253 to proceed without regard to the special committee's deliberations could be seen as a factor relevant to the question of whether 253 was motivated by good faith.
- [11] The credentials of the special committee members were noted by the judge, as well as its recommendation against commencing litigation and its conclusion that the transaction with Union Goal was in the best interests of EPL:
- [16] Mr. Dentoom, who says in his affidavit that he has 45 years' experience in metals, commodity, and mining industries, was chair of the special committee. He says the committee formally met eight times, generally meeting by telephone for one to two hours. The committee reviewed documents, interviewed management, and received information from directors who had been onsite to review the progress of the Retreatment Project.
- [17] Mr. Dentoom says the special committee concluded that it would not be in the best interest of EPL to commence legal action and that recommendation was reported to and accepted by the board on December 17, 2018. He says in his affidavit:
28. The Special Committee's assessment is that the transaction remains in the best interests of EPL and its stakeholders and that the arrangements are such that EPL has taken reasonable and prudent steps to mitigate the risk of financial loss or damage from the transaction. The Framework Agreement allowed EPL to move a key asset out of care and maintenance, reactivate its workforce and utilize new technology that has the potential to significantly increase EPL's revenues, principally at another party's risk. The deal is structured so that

EPL incurs costs that it would incur even if it had decided to proceed with retreatment using traditional technology. However, EPL has positioned itself to access more of its mineral resources, and potentially exploit other related opportunities in the future.

- [12] The judge also noted that the exchange of affidavits in advance of the petition to hear the derivative action application led to 253 demanding production of documents from EPL, which EPL refused. This led to an application by 253 for production of the documents, which was dismissed by Hinkson C.J.S.C., in reasons indexed at 2019 BCSC 570.
- [13] The judge reviewed the proposed notice of civil claim that 253 seeks to file on EPL's behalf against the Proposed Defendant Directors, which alleged they were negligent and breached their fiduciary duties to EPL (paras. 20-21).
- [14] The judge also instructed himself on the legal principles applicable to an application for leave to commence a derivative action pursuant to s. 232 of the BCA. I will address these principles in more detail, but the two conditions that were the primary focus below were the conditions in s. 233(1)(c) and (d), namely that the complainant is acting in good faith and that it appears to the court that it is in the best interests of the company for the legal proceeding to be prosecuted.
- [15] The judge found that 253 had failed to show any basis for a claim against the directors for breach of fiduciary duty (paras. 27-32).
- [16] The judge was satisfied that 253 had raised specific allegations of negligence for which EPL had failed to put forward evidence to show the proposed action was "bound to fail" (para. 44). The judge therefore concluded that the proposed claim in negligence satisfied the "best interests" of the company aspect of the test for granting leave.
- [17] Where the application by 253 floundered was on the good faith requirement. The judge analyzed this requirement by assessing the primary purpose for bringing the action and the extent to which there were ulterior motives (paras. 45-47).
- [18] The judge noted Mr. Hong's evidence that he believes the action would be in the best interests of EPL, but the judge found there was other evidence that called those assertions into question (paras. 48-49).
- [19] The judge reviewed the evidence of Mr. Hong's other personal interests, including his previously thwarted attempt to gain control of EPL, which Mr. Hong had not initially disclosed in his affidavit (paras. 50-53), and his own proposal to buy chrome produced by EPL (paras. 55-56).
- [20] The judge found that the facts suggested that Mr. Hong's personal interests, rather than EPL's interests, were a significant motive for the proposed action (para. 58). The judge concluded that 253 had failed to satisfy the onus of proving good faith (para. 60).

[21] The judge also commented on Mr. Hong's evidence that his goal was to protect his and the applicant's interest in the shares of EPL (para. 62). The evidence was that 253 was concerned that if EPL paid off the loan from Union Goal by issuing shares, this would result in significant dilution of the shareholdings of EPL and diminish the value of existing shares (para. 7). The judge held that this was not properly raised in a derivative action. He noted that if 253 was alleging unfair treatment and damages suffered in its capacity as a minority shareholder, that was a matter to be raised in an oppression claim under s. 227 of the BCA (para. 62).

[22] As a result, the appellant's petition was dismissed.

GROUNDS OF APPEAL

[23] The appellant submits that the judge made three errors in respect of his finding that the appellant was not acting in good faith:

1. First, he committed an error of law by failing to consider the appellant's belief in the merits of the proposed action, which is, as a matter of law, *prima facie* evidence of good faith under s. 233(1)(c) of the BCA;
2. Second, he committed an error by drawing inferences about the appellant's motivations that were not supported by the evidence; and
3. Third, he committed an error of law in finding that the derivative action was not appropriate because the appellant wanted to protect the value of its shares in EPL.

[24] The respondent submits that the appellant's arguments do not raise issues of law but of fact. The primary issue is whether the chambers judge committed a palpable and overriding error in finding that the appellant did not establish it was acting in good faith. The respondent submits that there was no such palpable and overriding error.

[25] Alternatively, the respondent submits even if there was such an error, the order dismissing the application for leave was otherwise justified, as would have been plain had the judge completed his analysis of whether the proposed action was in the best interests of the company. In this regard, the respondent submits that the judge only considered one aspect of the best interests test in respect of the negligence claim, namely, whether the defence was bound to fail. The respondent submits that the judge did not complete his analysis by considering whether the claim had a reasonable prospect of success and whether the litigation was worth the cost and inconvenience to EPL. The respondent's position is that a proper consideration of these components of the best interests test would reach the same result: dismissal of the application.

LEGAL PRINCIPLES APPLICABLE TO DERIVATIVE APPLICATIONS

[26] The power of a court to grant leave to a party to commence an action in the name of and on behalf of a company, known as a derivative action, is found in s. 233(1) of the BCA. The definitions set out in s. 232 are also relevant:

232 (1) In this section and section 233,

"complainant" means, in relation to a company, a shareholder or director of the company;

"shareholder" has the same meaning as in section 1 (1) and includes a beneficial owner of a share of the company and any other person whom the court considers to be an appropriate person to make an application under this section.

- (2) A complainant may, with leave of the court, prosecute a legal proceeding in the name and on behalf of a company
 - (a) to enforce a right, duty or obligation owed to the company that could be enforced by the company itself, or
 - (b) to obtain damages for any breach of a right, duty or obligation referred to in paragraph (a) of this subsection.
- (3) Subsection (2) applies whether the right, duty or obligation arises under this Act or otherwise.
- (4) With leave of the court, a complainant may, in the name and on behalf of a company, defend a legal proceeding brought against the company.

233 (1) The court may grant leave under section 232 (2) or (4), on terms it considers appropriate, if

- (a) the complainant has made reasonable efforts to cause the directors of the company to prosecute or defend the legal proceeding,
- (b) notice of the application for leave has been given to the company and to any other person the court may order,
- (c) the complainant is acting in good faith, and
- (d) it appears to the court that it is in the best interests of the company for the legal proceeding to be prosecuted or defended.

[27] There are additional provisions dealing with costs and control of the proceeding in the remainder of s. 233.

- [28] As mentioned, of the four conditions in s. 233(1) that must be met by an applicant seeking leave to commence a derivative action, the contest below and in this Court centred on two: (i) that the complainant be acting in good faith; and (ii) that it appear to the court that it is in the best interests of the company for the legal proceeding to be prosecuted.

Good Faith Requirement

- [29] The requirement that the complainant be acting in good faith focuses on the primary purpose for the bringing of the derivative action. The primary purpose must be to benefit the company. The onus is on the applicant to provide evidence proving this question of fact: *Jordan Enterprises Ltd. v. Barker*, 2015 BCSC 559 at paras. 27-30.
- [30] The good faith requirement is a separate requirement that must be established by the complainant based on evidence. It cannot simply be presumed, even where the claim can be said to be in the best interests of the company: *Discovery Enterprises Inc. v. Ebco Industries Ltd.* (1997), 40 B.C.L.R. (3d) 43 at paras. 117-118 (S.C.) [*Discovery Enterprises (S.C.)*]; *aff'd* (1998), 50 B.C.L.R. (3d) 195 at para. 5 (C.A.) [*Discovery Enterprises (C.A.)*].
- [31] The evidence that may be considered by the court in determining the good faith requirement includes the applicant's stated belief in the merits of the proposed action. If this evidence is accepted by the court, it is a *prima facie* indication of good faith, but it is not necessarily determinative: *Jordan Enterprises* at para. 29; *Discovery Enterprises (S.C.)* at para. 117. The court must also consider evidence that indicates the applicant has ulterior motives, including considering any existing disputes between the parties.
- [32] A conclusion that there is an absence of "good faith" simply means that the applicant has not met the onus of showing that the primary purpose of the action is to benefit the company. There is no requirement that the respondent show the applicant is acting in bad faith.
- [33] A finding of good faith, or of a failure to prove good faith, is a finding of fact in the purview of the trial judge, typically based on inferences drawn from the record, and the appeal court will not interfere absent a palpable and overriding error: *Housen v. Nikolaisen*, 2002 SCC 33 at para. 10; *Discovery Enterprises (C.A.)* at para. 7.

Best Interests Requirement

- [34] The question of whether it appears to the court to be in the best interests of the company to prosecute the action includes consideration of the merits of the proposed action.
- [35] In this regard, many of the authorities have adopted the language of Tysoe J. (as he then was) in *Primex Investments Ltd. v. Northwest Sports Enterprises Ltd.* (1995), 13 B.C.L.R. (3d) 300 [*Primex (S.C.)*], *var'd* (1996), 26 B.C.L.R. (3d) 357, leave to appeal *ref'd* [1997] S.C.C.A. No. 4. He held that the court should consider whether "the proposed action has a reasonable prospect of success or is bound to fail" and whether the defence is "bound to be accepted": at para. 49; see *Discovery Enterprises (C.A.)* at para. 11. This Court in *Discovery Enterprises*

(C.A.) approved the description of this requirement as requiring the applicant to show "an arguable case" (para. 10).

- [36] The onus is on the applicant, not the respondent. The applicant has to not only plead a proper cause of action, but also have some evidence to support the case that its proposed claim has a reasonable prospect of success. This is why the authorities typically review the evidence of the merits of the proposed claim in considerable detail: see for example *Discovery Enterprises (S.C.)*; *Primex (S.C.)*; *Arkansas Teacher Retirement System v. Lions Gate Entertainment Corp.*, 2016 BCSC 432 [Lions Gate].
- [37] What the authorities illustrate is that the approach to considering the merits of the proposed action lies somewhere on a spectrum. The court should do more than skim the surface of the pleadings and should consider the evidence but ought not to dive so deeply into the merits as to try the case.
- [38] Other factors must also be brought to bear on whether the proposed action appears to be in the best interests of the company, namely whether the potential relief sought in the action makes it worthwhile to the company to undertake the costs and inconvenience of pursuing it: *Primex (S.C.)* at para. 49; *Lions Gate* at paras. 163-165; *Jahnke v. Johnson*, 2018 SKCA 59 at para. 68.

Discretion

- [39] Even where the conditions in s. 233(1) are met, the court retains discretion as to whether to grant leave: *Discovery Enterprises (C.A.)*. Section 233(1) provides that the court "may"--not must--grant leave if the requirements are met.
- [40] Not much has been said about the remaining exercise of discretion to grant or not grant leave. A common approach to the exercise of discretion in analogous circumstances is to consider the required factors as a whole, rather than separately. This is a sensible approach in derivative action applications as well.
- [41] It is conceivable that there may be cases where the requirements are met but so thinly established that in the end the court will exercise its discretion to not grant leave. More likely, however, if an application fails it will fail on one of the requirements of the test.
- [42] Discretionary decisions are given considerable deference on appellate review and may not be overturned absent a palpable and overriding error: *Holdyk v. Adolph*, 2012 BCCA 37 at para. 15.
- [43] I turn now to my analysis of the grounds of appeal.

ANALYSIS**Ground 1: Failing to Consider Mr. Hong's Belief in the Merits**

- [44] Using the conclusory language that has become somewhat standard form in affidavits supporting derivative action applications, Mr. Hong stated in his first affidavit that he believed it was in the best interests of EPL to advance the claims on behalf of EPL and he was pursuing leave for the purpose of pursuing remedies on behalf of EPL against the proposed defendants and for no other or improper purpose.
- [45] On appeal, 253 asserts that the judge made an error of law "by failing to consider" Mr. Hong's stated belief as prima facie evidence of good faith.
- [46] On any fair reading of the judge's reasons, this ground of appeal cannot succeed.
- [47] The judge correctly summarized the principles that apply to the good faith requirement:
- [45] The foregoing conclusion does not end the matter because 2538520 must also show good faith. The meaning of the good faith requirement in s. 233(1) was summarized in *Jordan Enterprises Ltd. v. Barker*, 2015 BCSC 559 at paras. 27-30:
- [27] The onus is on the applicant to establish that the derivative proceeding is being brought in good faith. There is no presumption of good faith. Evidence must be adduced to establish good faith: *Luft v. Ball*, 2013 BCSC 574 at para. 46, citing *Creative Realty Corp. v. 333 Terminal Holdings Ltd.*, 2011 BCSC 638 at para. 19.
- [28] The test for good faith is whether the action is brought for the primary purpose of pursuing the claim on the company's behalf. Factors to consider include: (i) the applicant's belief in the merits of the proposed action, (ii) existing disputes between the parties, and (iii) alleged ulterior motives. See *Luft v. Ball* at para. 46, citing *Bennett v. Rudek*, 2008 BCSC 1278 at para. 46.
- [29] The applicant's belief in the merits of the intended action is not determinative of good faith, but, if accepted by the court, is a prima facie indication that the applicant is acting with proper motives: *Discovery Enterprises Inc. v. Ebco Industries Ltd.* (1998), [1998] B.C.J. No. 1301 at para. 5, 50 B.C.L.R. (3d) 195.
- [30] Ultimately, the existence of good faith is a question of fact to be determined on all of the evidence and the particular circumstances of the case: *Luft v. Ball* at para. 46, citing *Lost Lake Properties Ltd. v. Sunshine Ridge Properties Ltd.*, 2009 BCSC 938 at para. 56.
- [46] That passage was more recently cited in *Lions Gate* at para. 157, which also noted that the onus of proving good faith is "substantial".
- [47] The test of good faith centres around the primary purpose for bringing the action and the extent to which there are ulterior motives: *DeCotiis v. Petromin Resources Ltd.*, 2017 BCSC 514 at para. 48.

[Emphasis added.]

- [48] The judge understood that the key aspect of the good faith test is that the action be brought for the primary purpose of pursuing the claim for the company's benefit.
- [49] Respectfully, I disagree with my learned colleague that the judge made an error in describing the onus to prove good faith as "substantial". The judge did not treat the onus of proof as higher than the balance of probabilities. This alleged error was not advanced by the appellant as a ground of appeal.
- [50] The judge correctly recognized, in accordance with the authorities, that a derivative action applicant bears an onus of establishing that the application is brought in good faith and this cannot be presumed simply because there is some merit to the proposed claim. The applicant must prove this requirement with evidence.
- [51] The judge's reference in paragraph 46 to Lions Gate, which referred to the onus of proving good faith as "substantial", was a reference to a well-established proposition that good faith will not be presumed and the applicant must bring forward cogent evidence to prove this requirement, which is separate from the requirement that the action be in the best interests of the company: *Discovery Enterprises Inc. (S.C.)* at para. 118; *Tremblett v. S.C.B. Fisheries Ltd.* (1993), 116 Nfld. & P.E.I.R. 139 (N.L.S.C.T.D.) at para. 58.
- [52] Perhaps a more precise word in this context, rather than "substantial", is "substantive", in the sense that the requirement to show good faith is a real and not immaterial requirement. Common usage has blurred the distinction between "substantive" (real) and "substantial" (large) and the two words are sometimes used synonymously. For example, the requirement of a "real and substantial connection", referred to in authorities dealing with procedural and jurisdictional questions, is also sometimes referred to as a "real and substantive connection". As examples, see: *Newman v. Beta Maritime Ltd.*, 2016 BCSC 2257; *Section 1 of the Owners, Strata Plan LMS 2643 v. Kwan*, 2009 BCCA 342; *Lui v. West Granville Manor Ltd. (No. 1)* (1985), 61 B.C.L.R. 315 (C.A.); *Lui v. West Granville Manor Ltd.*, (1987), 11 B.C.L.R. (2d) 273 (C.A.); *Seipp v. Seipp* 2002 BCSC 669; *CLE Owners Inc. v. Wanless*, 2004 MBQB 43; and *J.B. v. J.P.C.*, 2005 ABQB 99.
- [53] In summary, the good faith requirement for leave to commence a derivative action is a separate and substantive requirement for which the onus of proof is on the applicant and requires evidence, and it will not be presumed simply because there is some merit to the proposed action.
- [54] The Lions Gate case cited by the judge in support of the proposition that the good faith requirement is "substantial" in turn relied on the decision of *LaRoche v. HARS Systems Inc.*, 2001 BCSC 140. As was clear in *LaRoche*, the reference to the requirement being substantial does not change the burden of proof from a balance of probabilities, which is the same as saying something is "more likely than not":

[95] These factors, and others, go to the issue of good faith. In *Primex*, Tysoe, J. seemingly agreed that the onus on the Petitioner to establish good faith is a substantial one. In any event, on the basis of Mr. LaRoche's conduct, as well as the evidence pertaining to the merits of the two actions, and to their settlement, although in conflict in some areas, Mr. LaRoche has not satisfied me that it is more likely than not that his primary purpose is the recovery by HARS of fairly substantial sums in the actions, and that he is acting in good faith.

[Emphasis added.]

[55] Likewise while the word "substantial" was used to describe the onus on the applicant in *Tremblett*, this was directed to the need for the applicant to bring cogent evidence, especially in the face of "substantial evidence" to the contrary that brought the applicant's good faith into question. The court stated that the applicant must "bring cogent evidence establishing clearly on a preponderance of evidence that the application is in fact brought in good faith":

58 In my view, the concept of good faith encompassed by the statutory requirements under s. 369 relates to the intention of the applicant - whether the application is brought with the motive and intention of benefiting the corporation, or for some recognized or subliminal purpose or benefit outside that interest. This is not to say, of course, that an action for the benefit of the corporation may not also have a subsidiary benefit for the applicant, even beyond the applicant's benefit as one of a number of shareholders. However, in my view the history of the development of statutory provisions such as s.369 shows that for statutory relief against the strict common law position of non-intervention in majority decisions internal to corporations, in light of the extraordinary power vested in a shareholder or director applicant to use the corporate resources and to create a position of legal conflict between the corporation and others, it is necessary that an applicant bring cogent evidence establishing clearly on a preponderance of evidence that the application is in fact brought in good faith. It must be noted that this obligation is a positive requirement on any applicant for relief under s. 369. It is not one which arises only where there may be evidence to the contrary adduced. In circumstances such as here where, I conclude, there is in fact substantial evidence bringing this aspect into question, there is in turn a substantial obligation on an applicant, including the applicant here, to satisfy the court as to the good faith under which this application, and the proposed action to be sanctioned by it, are brought and proposed by him.

[Emphasis added.]

[56] The standard of "a preponderance of evidence" is the same as the standard of a balance of probabilities: *R. v. Proudlock*, [1979] 1 S.C.R. 525; Sidney N. Lederman, Alan W. Bryant, & Michelle K. Fuerst, Sopinka, Lederman & Bryant: *The Law of Evidence in Canada*, 5th ed (Toronto: LexisNexis Canada, 2018) ch 5 at § 5.61.

[57] In short, the civil standard of proof on a balance of probabilities is not supplanted by the observation that the applicant's onus is substantial.

- [58] Thus, contrary to the view of my colleague in the dissenting judgment, I am of the view that the judge's decision did not run afoul of the well-established proposition that there is only one civil standard of proof, a balance of probabilities, as held in *F.H. v. McDougall*, 2008 SCC 53. The evidence must be "sufficiently clear, convincing and cogent" to satisfy the balance of probabilities test: *McDougall* at para. 46.
- [59] Returning to the ground of appeal that is advanced here, the appellant alleges that the judge did not take Mr. Hong's stated belief in the merits of the claim to be *prima facie* evidence of good faith.
- [60] The judge did take the evidence of Mr. Hong's stated belief into account, expressly referring to it as follows:
- [48] In his first affidavit, Mr. Hong says he believes the derivative action would be in the best interests of EPL because the proposed defendants' conduct has been detrimental to the company and its shareholders. In a second affidavit he says:
70. I confirm that my and the Petitioner's sole economic interest in [EPL] is in our capacity as (direct or indirect) shareholders. I also confirm that none of the other officers, directors or beneficial owners of the Petitioner has any economic interest other than in their capacities as (indirect) shareholders.
- [49] While the authorities establish that such statements can be *prima facie* evidence of good faith, there is other evidence in this case that calls those bald assertions into question. That evidence concerns Mr. Hong's prior dealings with EPL.
- [61] In the end, the judge was not persuaded by Mr. Hong's evidence of his "belief" in the merits. The judge found instead that Mr. Hong had ulterior motives.
- [62] The appellant submits in its factum that, as a matter of law, the applicant's belief in the merits of the action is "an overriding consideration". With respect, that is not an accurate statement of the law. The requirement of good faith requires that the primary purpose of the applicant, in bringing the action, be to benefit the company. That means it is not enough that there is some belief in the merits of the proposed action.
- [63] There is good reason for this. It is not particularly difficult to believe there is some merit to a proposed lawsuit, or to show on a preliminary basis that there is some merit. But a derivative action application can be brought only after the company's own management has declined to prosecute the proposed action. The consequences of approving the derivative action application can be significant for the company's operations. The good faith requirement helps protect against a party meddling in a company's management for ulterior motives.
- [64] The applicant's stated belief in the merits of the action was evidence of good faith but it was not determinative, nor can it be said to have been an overriding consideration. It was some evidence that the judge should have taken into account. Here, the judge did so.

- [65] The judge did not make an error of law in his approach to considering Mr. Hong's stated belief in the merits of the action, nor did he fail to consider relevant evidence in this regard. I would not accede to the first ground of appeal.

Ground 2: Drawing Unsupported Inferences

- [66] The judge made a finding of fact that Mr. Hong had ulterior motives and was not advancing the action for the primary purpose of benefiting the company. This takes me to the next ground of appeal, the appellant's challenge to this finding.
- [67] Determining a party's motives for seeking to bring a derivative claim will necessarily be a matter of drawing inferences from circumstantial evidence. Any well-advised applicant will state its belief that the proposed lawsuit is for the best interests of the company and will not admit to any other purpose. While such evidence is necessary, it is also obviously self-serving. A judge considering such an application is entitled to consider that evidence together with all of the circumstances and draw reasonable inferences from the whole of the evidence.

Personal Motivations

- [68] The judge's conclusion that Mr. Hong was personally motivated, as opposed to acting with a primary purpose of benefiting EPL, was a reasonable inference based on the evidence before the judge.
- [69] When the petition was brought by 253, not much evidence was tendered about 253 except that it was a shareholder of EPL owning 4,392,500 common shares (a minority position representing approximately 4.74% of EPL's shares as of May 2018) and that Mr. Hong was its CEO. Mr. Hong provided the affidavit evidence in support of the petition.
- [70] In his first affidavit, Mr. Hong tried to paint himself as a concerned shareholder who had been rebuffed by the company when he asked it reasonable questions and presented reasonable offers. As the evidence unfolded, it appeared that Mr. Hong had overstated the facts to shape his position.
- [71] For example, Mr. Hong tried to create the impression that despite several requests, EPL unreasonably did not provide him detailed answers to his questions about the Union Goal transactions. In fact, he sent rather general questions in an email in which he did not identify himself as a shareholder or as representing a shareholder, and he immediately escalated to threatening legal proceedings when he did not like the responses he received. The cautious approach of EPL in responding to this apparent stranger to the company was not unreasonable.

- [72] As another example, Mr. Hong criticized EPL's directors for not considering other options and tried to create the impression with the court that he had made his own proposal to purchase chrome offtake, which the EPL directors had ignored. He did not provide any details of that "proposal". In fact, the evidence was that he had made no formal proposal but had simply raised a general interest without details in a January 2018 meeting with Mr. Wallenius, the Chief Financial Officer of EPL, and in a subsequent email in February 2018.
- [73] The affidavit evidence filed by EPL in response to the petition revealed several background facts about Mr. Hong that he did not reveal in his initial affidavit or petition.
- [74] The EPL evidence revealed that Mr. Hong has maintained an interest in purchasing shares of EPL sufficient to control its directors since 2016 and continuing into 2018 and that Mr. Hong believes in part that he was thwarted in his takeover goal by another shareholder of EPL, Ka An Development Co. Ltd. ("Ka An").
- [75] Mr. Hong was associated with a Mr. Hung who tried to obtain the EPL shareholder list in late 2017. Mr. Hong asked to meet with and did meet with Mr. Wallenius in January 2018. Mr. Hong did not identify himself to Mr. Wallenius as a shareholder but stated that, through a company, he had purchased a block of shares, wanted to benefit from those shares, and might want to purchase more shares. He and Mr. Hung wanted to contact significant shareholders. Mr. Hong asked to speak directly to a representative of Ka An.
- [76] In July 2018, Mr. Hong started a lawsuit in Ontario against Ka An and former legal counsel for EPL, the law firm of Fasken Martineau ("Fasken"). In that claim, he alleges that:
- a) he was in a partnership with a company, Beijing Hehe Fengye Investment Co. Limited ("Beijing Hehe"), to buy shares of EPL;
 - b) in 2014, Beijing Hehe, through its wholly owned company Hebei Zhongbo Platinum Co. Limited ("HZP"), sought to purchase the Mine through a share purchase agreement for \$225 million because of the market value of its platinum and chrome reserves and other metals, but in the end it decided not to proceed with that transaction;
 - c) together, Mr. Hong and Beijing Hehe determined it would be more profitable to buy a controlling interest in EPL and take control of the EPL board. That would "combine the resources of Beijing Hehe in selling metal reserves in China with [Mr. Hong's] networks of contacts and business experiences in Western business communities";
 - d) Mr. Hong and Beijing Hehe's primary advisor was a lawyer, Mr. Huang, of Fasken, who was to negotiate with three larger EPL shareholders to purchase shares in EPL from them;
 - e) Fasken did not disclose that at the same time it was acting for Ka An to the same ends, ultimately assisting Ka An in purchasing shares in EPL in May and August 2016;
 - f) Ka An's nominees were appointed to the Board of Directors of EPL in July 2016, "frustrating" Beijing Hehe's desire to control the Board;

- g) the defendant lawyers misused confidential information including the existence of the opportunity to buy EPL at significantly below market value;
 - h) the alleged wrongs allowed Ka An and its owner, Mr. Liu, to buy "control shares" and control the board of EPL;
 - i) this caused Mr. Hong damage in that he lost the opportunity, with Beijing Hehe, to gain control of EPL's Board by purchasing EPL's shares from a major shareholder; and
 - j) the value of this lost opportunity is at least \$225 million.
- [77] As noted, Mr. Hong did not file any evidence revealing the above in his first affidavit. He then filed a second affidavit in support of the petition after the respondent filed evidence that included a copy of the above claim.
- [78] Mr. Hong's second affidavit revealed his continued focus on Ka An. He stated that he was "concerned" that Union Goal might be related to Ka An, and that the CEO of EPL, Ms. Hu (one of the Proposed Defendant Directors), as well as another officer, might be connected to Ka An as well. He went on in his affidavit to reference the "proxy battle" that Ka An "won" in July 2016 and the appointment of EPL directors after this date. He suggested that these "relationships" raised concerns that the Union Goal transactions might be motivated by something other than the best interests of EPL.
- [79] The appellant, through Mr. Hong, sought to convince the judge that the Proposed Defendant Directors were acting in bad faith, seeking somehow to privately benefit or to benefit Ka An. The judge rejected that position, finding no particular, clearly defined allegation or evidence in support of the breach of fiduciary duty claim (paras. 27-32).
- [80] The judge also noted that Mr. Hong had wanted to purchase chrome offtake from EPL himself and felt rebuffed in that regard. That possibility was precluded by the deal with Union Goal (para. 55-56).
- [81] The judge held:
- [57] In short, the CEO of the corporate petitioner, who 2538520 puts forward to give evidence on its behalf, clearly has or has had personal interests separate from whatever concern he may have for the best interests of EPL. He was involved in a failed bid to take over the company. He subsequently was rebuffed or ignored when he sought to enter into a transaction with the company. His efforts were rejected in favour of the very transaction that 2538520 now complains of.
- [58] Those facts clearly suggest that Mr. Hong's personal interests, as opposed to the interests of EPL, are a significant motive for this proposed action. The most likely inference to be drawn from the evidence before me is that the proposed action is an attempt to continue Mr. Hong's unsuccessful takeover bid by other means or to obtain retribution for that bid's failure.

- [59] Evidence of a personal interest may not be fatal to a leave application if it is outweighed by other evidence of good faith. But in the presence of clear evidence that suggests 2538520, through its CEO, is motivated by other interests, a mere assertion of belief in the merits of the claim accompanied by a bald profession of good faith is not sufficient.
- [60] I therefore find that 2538520 has failed to satisfy the onus of proving good faith.
- [82] The appellant takes issue with the judge's inference that the "proposed action is an attempt to continue Mr. Hong's unsuccessful takeover bid by other means or to obtain retribution for that bid's failure" (para. 58).
- [83] The appellant complains now that there was not sufficient evidence for the judge to conclude that 253 was acting in bad faith in seeking leave to commence a derivative action against the Proposed Defendant Directors. However, that is not what the judge found. What the judge found was that 253 had failed to satisfy the onus of proving good faith. As mentioned, good faith in this context means that the primary purpose for the proposed lawsuit is to benefit EPL.
- [84] The judge's finding that Mr. Hong was personally motivated (as opposed to being primarily motivated to benefit the company) was a reasonable inference to draw on the evidence. Mr. Hong has filed a claim in an Ontario court expressing that he had a goal of controlling the board of EPL in a way that would benefit him personally and this was thwarted by Ka An, a major shareholder of EPL. He has exaggerated the facts to suit his interests and advanced allegations of undisclosed conflicts of interest, without evidence, against the Proposed Defendant Directors. He has expressed personal interest in acquiring EPL's assets. He claims in the Ontario action that he has suffered \$225 million in damages by not being able to control the board of directors of EPL.
- [85] There is little doubt that Mr. Hong has concluded without evidence that there is something nefarious about EPL's deal with Union Goal. Having EPL sue the Proposed Defendant Directors on the basis that EPL's current ongoing transactions with Union Goal are improvident or tainted would severely curtail the freedom of the directors to manage the ongoing relationship with Union Goal.
- [86] In short, there was evidence to support the judge's finding of fact that the appellant had ulterior motives and failed to meet the onus of proving good faith. The judge drew reasonable inferences from the evidence and made no palpable and overriding error in reaching this factual conclusion.
- [87] There is one other branch to this aspect of the appellant's argument.

Merits of the Proposed Claim and Good Faith

- [88] The appellant argues that because the judge found that advancing the negligence claim was in the best interests of the company, it was inconsistent for the judge to find that the appellant was not acting in good faith in wanting this action pursued. The appellant relies on *Primex (S.C.)* in this regard.
- [89] There are several problems with this argument.
- [90] First, this argument wrongly suggests that the good faith test is subsumed by the best interests test, which it is not. The good faith requirement is a separate, substantive requirement.
- [91] Second, the appellant fails to distinguish between propositions of law and findings of fact in the authorities.
- [92] The judge in *Primex (S.C.)* agreed that it was self-interested for the applicant to want to prosecute the derivative action, in that it might maximize the value of its shares, but this interest coincided with the interests of the company and was not contrary to the conclusion the applicant was acting in good faith (paras. 41-42).
- [93] *Primex (S.C.)* did not establish a proposition of law that every time there might be merit to a company's claim proposed in a derivative action application, it will prove that the applicant is acting in good faith. That will surely depend on all the circumstances, including the nature of the claim, the strength and value of the claim, and the nature and extent of any ulterior motives.
- [94] When considering the applicant's good faith, the judge in *Primex (S.C.)* took into account the strength and nature of the proposed claim, finding that the company had an arguable case or, to put it another way, had a reasonable prospect of success, and the potential relief was sufficient to justify the inconvenience to the company of being involved in the lawsuit (paras. 40, 49, 59, 83). There was no such analysis by the judge of the proposed claim in the present case.
- [95] As a third point, it is also to be remembered that the judge in the present case found no merit to the claim for breach of fiduciary duty. If, as the appellant suggests, the mere fact the applicant wishes to advance a claim that has some merit should be taken as evidence of good faith, then logically it could also be said that if the applicant wishes to advance a claim without merit, this is evidence of ulterior motives and a lack of good faith.
- [96] Mr. Hong's desire to advance the breach of fiduciary duty claim in the absence of any evidence or even particularized allegations reflects poorly on Mr. Hong's personal motives. There is evidence from which one might infer that he was personally motivated in advancing these allegations and not motivated by the best interests of the company.

- [97] The lack of merit of the breach of fiduciary duty claim to a considerable degree neutralizes the appellant's argument that more weight should have been given to Mr. Hong's belief in the merits of the negligence claim.
- [98] As a fourth point, the appellant's arguments in relation to the good faith component of the test in my view rely too heavily on the judge's finding that the proposed negligence claim was in the best interests of EPL, which I turn to next.

Best Interests Analysis

- [99] I agree with the respondents that the judge's finding that the proposed negligence claim was in the best interests of EPL was not fully fleshed out, perhaps because the judge disposed of the application on the good faith branch of the test.
- [100] It is useful to briefly review the judge's analysis that led him to conclude that bringing the negligence claim was in the best interests of EPL.
- [101] The judge summarized the claim in negligence as based on three types of allegations: failure to conduct sufficient due diligence in regard to the feasibility of the transactions with Union Goal; failure to conduct sufficient due diligence in respect of the experience of Union Goal; and failure to explore or consider other options or offers (para. 20).
- [102] The evidence in support of the latter two negligence allegations was extremely thin.
- [103] The appellant filed evidence regarding the incorrect Union Goal entity when challenging its experience, as was pointed out by EPL's evidence in response.
- [104] The negligent "failure to consider other offers" allegation refers to Mr. Hong's complaint that when he suggested to Mr. Wallenius there might be an opportunity for Mr. Hong to purchase chrome offtake, he was not taken up on it. This unspecified opportunity was not an offer at all given the vagueness of it.
- [105] In fact, EPL's affidavit evidence set out that EPL management held meetings with representatives from significant players in the chrome-mining industry regarding purchasing offtake. These other parties did not offer any other arrangement or technology beyond an offtake agreement, and management considered the Union Goal agreement to offer significantly greater benefits. Further, management considered the option of using EPL's own equipment to mine the tailings, for which they had a feasibility study from Sound Mining, as the "base case" against which they weighed the proposed deal with Union Goal. This would seem to answer the allegation that the Board was negligent in not considering other options.
- [106] Thus, out of three allegations of negligence, the one that was considered in the court below was the allegation that the directors failed to conduct sufficient due diligence before making a decision approving the framework agreement in respect of the Union Goal transaction. In this regard, the judge noted:

- [33] If the proposed notice of civil claim raises any derivative claim for which leave could be granted, it can only be a claim in negligence. On that point, the proposed pleadings allege that the directors failed to conduct sufficient due diligence, to obtain a feasibility study or explore other options to exploit the tailings. The notice of civil claim says:
40. Instead, they allowed [EPL] to dramatically change course from the use of tried and proven technology in the New Plant, the use of which was supported by a detailed technical report. And they changed course to invest significant capital in the New Plant and the use of experimental equipment provided by Union Goal without sufficient support or due diligence in connection with that decision.
- [34] The proposed pleadings allege that the Union Goal transaction will be less profitable for EPL than use of its existing equipment and that all financial benefit from any increased production will go to Union Goal. In broad terms, those pleadings include allegations of breach of duty of care and resulting loss and are sufficient to state a claim in negligence.
- [107] The judge was not satisfied that the evidence from EPL showed that the complaint was "bound to fail" (para. 44) and so concluded that "insofar as the proposed claim is based on allegations of negligence", 253 had satisfied the "best interests" element of the test for leave (para. 44).
- [108] It is difficult to understand how the judge reached that conclusion on all three complaints in respect of the negligence claim, but I will focus on the complaint that the directors were negligent in not conducting sufficient due diligence.
- [109] There is merit to the respondent's argument that the judge did not complete the required analysis when considering whether pursuing the proposed negligence claim was in the best interests of EPL.
- [110] After reviewing the proposed pleadings, the judge concluded that the respondent had not shown the claim was bound to fail. This analysis appears very similar to the conclusion one would reach if there was a challenge to the pleadings alone. But the judge did not examine the other side of the coin: whether the appellant had shown that the negligence claim had a reasonable prospect of success. In my view this would have been necessary here, had the judge not decided the case based on the appellant not proving good faith.
- [111] A proper analysis of the best interests test would also require considering whether the potential for relief, as well as the nature of the claim itself, would justify the cost and inconvenience to the company of pursuing the claim. These considerations overlap to some extent with the question of whether the claim has a reasonable prospect of success.

Potential for Relief

- [112] While the judge at para. 25 cited the best interests test as including the question of whether the potential relief in the litigation would justify the cost and inconvenience to the company, he did not apply it.
- [113] The judge did not analyze what the potential relief might be if EPL were to sue the directors in negligence. EPL would have to show that it suffered damages as a result of entering into the transaction with Union Goal. The theory of the proposed claim supposes that the Union Goal transaction will be less profitable for EPL than a scenario where EPL chose to use its own equipment. But the evidence before the judge was entirely equivocal in this regard.
- [114] I do not agree with my colleague's analysis of the evidence, which, in my view, overemphasizes the poor state of EPL's finances at the time of the derivative action application and suggests this was solely caused by the Union Goal transaction, and is proof that the transaction was improvident. Respectfully, this conclusion makes too many assumptions and ignores the complicated financial picture of the company before the transaction in question.
- [115] EPL was not doing well before the transaction at issue. It had a \$55 million loss in 2016 and a \$9 million loss in 2017. Since August 2013, the company's projects were in care and maintenance or on hold. Its largest asset was the Mine. The feasibility study by Sound Mining suggested that the Mine required a \$19.7 million investment in order to recover chrome from its tailings and would break even only after 25 months and eventually generate a profit with a net present value of \$3.82 million.
- [116] EPL's directors' rationale for approving the Union Goal transaction was that it would allow EPL to build on what it knew from the Sound Mining report regarding the profit it might be able to generate from the chrome offtake, but with an additional possible upside. The Union Goal transaction would allow EPL to receive upfront \$3.7 million, near the net present value of what it might have generated from the chrome offtake under the Sound Mining feasibility study. What was seen as the key upside for EPL of the Union Goal transaction was the acquisition of new technology and a new plant that would give it the potential for recovery of significantly more platinum group metals (referred to in the evidence as "PGM") than might be recovered using existing technology. The recovery of PGM was a separate resource from the chrome offtake and would be entirely to EPL's benefit.
- [117] Unfortunately, there was no evidence before the court below as to the potential value that might be generated from the recovery of PGM using the new technology that EPL gained in the Union Goal transaction. It is fair to say this was a significant gap in EPL's evidence.

- [118] There were also questions raised by Mr. Hong's evidence. The Ontario lawsuit brought by Mr. Hong indicated that he was of the view that the Mine was worth around \$225 million to him. If recovery of chrome offtake was only worth \$3.82 million (using the Sound Mining feasibility study), this suggests there was something else about the Mine that he considered quite valuable. This something else is unexplained, but the only other resource mentioned in the evidence is the PGM at the Mine.
- [119] The judge was clearly frustrated by the lack of evidence before him. He referred to the fact that the documents purportedly considered by EPL's directors were not in evidence (paras. 38-39). He noted that the missing evidence might support either side's case (para. 41). He in effect drew an adverse inference against EPL for not producing the documents, given that the documents were in EPL's control (para. 42). The judge held that in the absence of the documents, the court was "in no position to assess the reasonableness" of the decision by a special committee of EPL's directors that the litigation was not in the best interests of EPL (para. 41).
- [120] It is apparent that there was an inadequate record before the judge. Both sides made broad statements in their affidavits without detailed evidentiary support. No one on this appeal takes issue with the decision made earlier in the proceeding by Hinkson C.J.S.C. refusing the appellant's application for production of documents by the respondents, so I will not comment on that decision.
- [121] The judge moved directly from the absence of evidence to his conclusion on best interests. To repeat, he concluded:
- [44] 2538520 has raised specific allegations of negligence and EPL has failed to put forward the evidence that it says would show the proposed derivative action is bound to fail. In the result, I cannot say the proposed action is bound to fail. I find that, insofar as the proposed claim is based on allegations of negligence, 2538520 has satisfied the "best interests" element of the test for leave.
- [122] The above paragraph of the judge's reasons suggests he concluded that the best interests test was met simply because 253 had pleaded a cause of action in negligence and EPL did not show that the proposed action was "bound to fail".
- [123] I accept that the judge was in the difficult position of having insufficient evidence before him. Nevertheless, in my view the judge's conclusion that the proposed claim was in the company's best interests was premature. The judge should have first engaged in an analysis of whether the claim had a reasonable prospect of success and whether the potential for relief outweighed the potential costs and inconvenience to EPL of pursuing the claim.

- [124] I do not see how on the evidence before the court it can be determined that EPL will likely suffer damages in relation to the Union Goal transaction or what the potential measure of the damages would be. There were too many gaps in the evidence before the judge and too many unanswered questions. It would be pure guesswork to conclude that a lawsuit claiming the directors were negligent in approving the Union Goal transaction might have the potential to recover significant damages and be worth the inconvenience to EPL.
- [125] The judge understood the appellant to be concerned that EPL could end up unable to pay a debt to Union Goal and would be forced to issue shares to repay that debt, causing dilution to existing shareholders (para. 7). However, there was no real analysis in the judge's reasons as to what the debt that EPL would owe Union Goal in the worst-case scenario might reasonably be, particularly given EPL's right to return equipment to Union Goal at cost and to cancel the loan (para. 9).
- [126] Based on the submissions made to this Court, it appears that in the worst-case scenario for EPL, it could limit its net expenses to something in the range of \$2 million if it decided that the Union Goal equipment was not worth keeping, exercised the put option to return it to Union Goal at cost, and cancelled the loan. However, this figure was far from clear.
- [127] Without considering the potential benefits to EPL of the proposed litigation, it could not be said that the litigation was worthwhile and in the best interests of EPL. Indeed, without analyzing the question of whether there is likely to be a significant loss suffered by EPL by reason of entering the Union Goal transaction (as compared to the position it otherwise would have been in), the court would be unable to conclude that the proposed action has a reasonable prospect of success: *Jordan Enterprises* at para. 37.
- [128] It is worth observing that here, unlike in many successful applications to commence derivative claims noted in the authorities, the proposed claim does not involve a concluded past transaction involving apparent misconduct tainted by director self-interest, dishonesty, or breach of fiduciary duty, such as misappropriation of a corporate opportunity as in *Primex* (S.C.).
- [129] Rather, the proposed claim suggests it was negligent for the directors to approve a transaction with Union Goal, a transaction that is ongoing and has not yet been completed. The benefits or disadvantages of that transaction to EPL have not yet matured. The evidence is thin as to the company's prospects without such a transaction. Even if it can be shown that the directors fell below a standard of care by not subjecting the transaction to sufficient scrutiny, it may well be that the company is not worse off than it otherwise would have been. Further, EPL will have an obligation to mitigate any damages it claims the directors caused it by entering into the transaction.

- [130] A negligence claim will be faced with the defence that the directors' decisions should be given deference in accordance with the business judgment rule. This rule recognizes that directors are often better positioned than the court to determine what is in the best interests of the company. For this reason, the courts accord deference to directors' decisions, so long as they lie within a range of reasonable alternatives: *BCE Inc. v. 1976 Debentureholders*, 2008 SCC 69 at para. 40.
- [131] The appellant did not refer to a single authority where leave was granted to commence a derivative action against the company's directors based in negligence alone. I do not suggest that such an application can never succeed. However, it appears exceptionally rare.
- [132] The judge recognized the existence of the business judgment rule, both in the context of the directors' decision to enter the transactions with Union Goal and in the context of the decision of the special committee that pursuing the litigation was not in the best interests of EPL. I see no error in the judge's criticism of the lack of documentation in support of those decisions. The lack of documentation supports the judge's finding that EPL had failed to show that the proposed derivative action was bound to fail (para. 44) but does not necessarily mean that the appellant showed that the claim had a reasonable prospect of success.
- [133] I do not see the need to comment further on the special committee composition and process in the context of this case.
- [134] My review of the judge's conclusion on the best interests test was merely to illustrate that in my view the appellant places too much weight on that aspect of the decision, given that the analysis was incomplete. The judge did not analyze whether the appellant had shown that the proposed negligence claim had a reasonable prospect of success, nor did he consider whether the potential for relief would outweigh the inconvenience to EPL.
- [135] Contrary to the thrust of the appellant's arguments, the fact the appellant had "belief" in the merits of the proposed lawsuit and the fact that the judge could not conclude, based on the evidence put forward by EPL, that the lawsuit was bound to fail did not inevitably lead to the conclusion that the good faith test was met.
- [136] The judge's conclusions on best interests quite correctly did not dictate the result of the judge's analysis of the good faith requirement.

Conclusion on Ground 2 of Appeal

- [137] I do not see that the judge erred in drawing inferences from the evidence as to the appellant's motivations and in concluding that the good faith test was not met.
- [138] I would dismiss this ground of appeal.

Ground 3: Considering the Appellant's Desire to Protect the Value of its Shares

[139] The appellant also takes issue with the judge's comment regarding Mr. Hong's stated concern about protecting the value of 253's shares. The judge commented at para. 62:

It is entirely proper for a shareholder to be concerned about its position and the value of its shares. But that is not a matter that is properly raised in a derivative action. If 2538520 is alleging unfair treatment and damages suffered in its capacity as a minority shareholder, that is a matter to be raised in an oppression claim under s. 227 of the BCA.

[Emphasis added.]

[140] The appellant submits that pursuing a derivative action because of concern for the value of one's shares in the company is a valid motive. I agree that it can be, provided there is an independent wrong done to the company that is causing the loss in value to the company's shares generally. Further, a wrong that might be pursued by way of the oppression remedy must cause particular damage to the claimant, beyond the more general damage to the value of all shareholders' shares: 1043325 Ontario Ltd. v. CSA Building Sciences Western Ltd., 2016 BCCA 258 at para. 78.

[141] It is obvious that a decline in the value of a company's shares does not constitute proof of company mismanagement, let alone negligence on the part of the directors.

[142] As I read para. 62 of the judge's reasons, he was referring to 253's concern about "its position", alleged unfair treatment and damages suffered in its capacity as a minority shareholder. The appellant had expressed concern about dilution of its shares and Mr. Hong had a history of wanting to take over EPL. The judge was referring to the position of 253 as a minority shareholder.

[143] Further, this comment was made after the judge reached the conclusion that the appellant had failed to satisfy the onus of proving good faith (para. 60) and was obiter. I do not agree with the appellant's reading that the judge was equating the fact of a personal interest in share value with bad faith. I therefore would not accede to the ground of appeal arising from the judge's comment at para. 62.

CONCLUSION

[144] For all of the above reasons, I would dismiss the appeal.

"The Honourable Madam Justice Griffin"

I AGREE:

"The Honourable Madam Justice Bennett"

Reasons for Judgment of the Honourable Mr. Justice Goepel:

INTRODUCTION

[145] I have had the privilege of reading in draft the reasons of Madam Justice Griffin.

Regrettably, I have reached a different conclusion. For the reasons that follow, I would allow the appeal and grant 2538520 Ontario Ltd. ("253") leave to commence a derivative action in negligence in the name of Eastern Platinum Limited ("EPL") against the past and present directors and officers of EPL named in the draft notice of civil claim.

[146] In these reasons I will first give a brief overview of derivative actions. I will then discuss the legislative criteria for the granting of leave. I will next review the background to the dispute, the chambers judge's reasons and the positions of the parties on the appeal. I will then consider those submissions in light of the criteria for leave and the governing case law.

DERIVATIVE ACTIONS -- AN OVERVIEW

[147] Derivative actions allow minority shareholders to bring an action in the name of and on behalf of the company to enforce a right of the company, when those who control the company refuse to do so. Federal and provincial statutes were enacted in the 1970s to permit such actions, which for the most part, had been barred at common law by the rule in *Foss v. Harbottle*, (1843) 2 Hare 461, 67 E.R. 189 (Ch). A detailed history of the legislative response can be found in *L&B Electric Ltd. v. Oickle*, 2005 NSSC 110 [L&B Electric] at paras. 34-41, *aff'd* 2006 NSCA 41 [L&B Electric Appeal] and *Jahnke v. Johnson*, 2018 SKCA 59 at paras. 59-62.

[148] Derivative actions serve two purposes:

1. they ensure that a shareholder has a right to recover property or enforce rights for the corporation if the directors refuse to do so; and
2. it helps to guarantee some degree of accountability and to ensure that control exists over the board of directors by allowing shareholders the right to bring an action against the directors if they have breached their duty to the company.

See: M.A. Maloney "Whither the Statutory Derivative Action?" (1986) 64 Can. Bar Review 309; *Richardson Greenshields of Canada Limited v. Kalmacoff*, (1995), 22 O.R. (3d) 577 at para. 21 [Richardson Greenshields]; and *Budd v. Bertram*, 2018 NSCA 95 at para. 33.

[149] The legislation governing derivative actions is drawn in broad terms and as remedial legislation should be given a liberal interpretation in favour of the applicant: *Richardson Greenshields* at para. 22; *Budd* at para. 35.

CRITERIA FOR LEAVE

[150] In British Columbia, the right to bring a derivative action is now found in s. 232-233 of the Business Corporations Act, S.B.C. 2002, c. 57 [BCA]. Section 233(1) sets out the criteria for granting leave:

233 (1) The court may grant leave under section 232 (2) or (4), on terms it considers appropriate, if

- (a) the complainant has made reasonable efforts to cause the directors of the company to prosecute or defend the legal proceeding,
- (b) notice of the application for leave has been given to the company and to any other person the court may order,
- (c) the complainant is acting in good faith, and
- (d) it appears to the court that it is in the best interests of the company for the legal proceeding to be prosecuted or defended.

[151] There is no issue on the appeal that the appellants have satisfied clause (b). The contest concerns the criteria contained in clauses (a), (c) and (d).

A. Reasonable Efforts

[152] This criterion is intended to ensure that the directors of a company have reasonable opportunity to consider their position before the application is heard by the court. The section does not mean that the proceeding requesting leave cannot be commenced until the expiry of a reasonable period of time for the directors to consider their position: *Intercontinental Precious Metals Inc. v. Cooke* (1993), 88 B.C.L.R. (2d) 101 (S.C.) at para. 32 [IPM].

B. Best Interests of the Company

[153] The overarching requirement for leave is that the proposed action must appear to the court to be in the company's best interests: *Arkansas Teacher Retirement System v. Lions Gate Entertainment Corp.*, 2016 BCSC 432, at para. 157 [Lions Gate]. The best interest criteria requires the court to determine whether a proposed action has a reasonable prospect of success or is bound to fail. In deciding whether the best interest test has been satisfied the court should not attempt to try the case. It is not necessary for the applicant to show that the action will be more likely to succeed than not. If it is asserted that the proposed defendants in the derivative action have a defence to the claim, the court must decide whether such a defence is bound to be accepted. The court should be satisfied that the potential relief in the proposed action is sufficient to justify the inconvenience to the company of being involved in the action: *Primex Investments Ltd. v. Northwest Sports Enterprises Ltd.* (1996), 13 B.C.L.R. (3d) 300 (S.C.) at para. 49 [Primex], varied 26 B.C.L.R.

(3d) 357 (C.A.), leave to appeal denied 1997 S.C.C.A. 4.

- [154] For a court to determine whether an action has a reasonable prospect of success, it must know what the cause of action is, the facts alleged to give rise to it, and the loss alleged to have been suffered: *Mikulic v. Peter*, 2013 BCSC 941 at para. 12; *Jordan Enterprises Ltd. v. Barker*, 2015 BCSC 559 at para. 37 [*Jordan Enterprises*].
- [155] Best interests can be defined as the maximization of the value of a corporation. It is best for a corporation to be profitable, well-capitalized and with strong prospects. The deterioration of a corporation's financial stability is to be avoided: *Carr v. Cheng*, 2005 BCSC 445 at para. 25; *Jordan Enterprises* at para. 25.

C. Good Faith

- [156] Good faith is a question of fact to be determined on all of the evidence and the particular circumstances of the case. The applicant's belief in the merits of a proposed claim, if accepted by the court, is a proper factor and cogent evidence of good faith and a *prima facie* indication that the petitioner is acting with proper motives. Other factors include existing disputes between the parties and alleged ulterior motives: *Discovery Enterprises Inc. v. Ebco Industries Ltd.*, (1998) 50 B.C.L.R. (3d) 195 (C.A.) [*Discovery Appeal*].
- [157] The onus of proving good faith lies on the petitioner. While some trial authorities have suggested the burden is "substantial", Chief Justice Williams in *Discovery Enterprises Inc. v. Ebco Industries Ltd.* (1997), 40 B.C.L.R. (3d) 43 at para. 117 [*Discovery*], *aff'd* *Discovery Appeal*, specifically rejected that proposition and held that good faith only needed to be proved on a balance of probabilities: see also *L&B Electric* at paras. 51-52. That good faith need only be proved on a balance of probabilities is consistent with the Supreme Court of Canada's pronouncement in *F.H. v. McDougall*, 2008 SCC 53 at para. 40, that there is only one civil standard of proof at common law and that is proof on a balance of probabilities.
- [158] The fact that there is a shareholder's battle does not lead to an inference that a party is motivated by bad faith: *Bellman v. Western Approaches Limited* (1981), 33 B.C.L.R. 45 (C.A.); *IPM*; *Primex*; *Discovery Appeal*; *Holdyk v. Adolph*, 2012 BCCA 37.

BACKGROUND

- [159] EPL is a publicly traded British Columbia company engaged in mining in South Africa. Its shares trade on the Toronto Stock Exchange and the Johannesburg Stock Exchange. 253 is a company incorporated under the laws of Ontario. It owns approximately 4.74% of EPL's outstanding shares.
- [160] EPL owns, through an indirect subsidiary, a platinum and chrome mine in South Africa, known as the Crocodile River Mine (the "Mine"). Mining activity from 1980 to 2013 produced tailings that contain chrome oxide and other minerals. In 2018, EPL entered into a series of agreements with Union Goal Offshore Solutions ("Union Goal") to recover

marketable product from the Mine's stored tailings (the "Union Goal Transaction"). 253 alleges the Union Goal Transaction was not in EPL's best interest and its officers and directors were negligent in entering into the Union Goal Transaction.

- [161] The chambers judge and my colleague have set out most of the background events and I need not repeat them. I do wish, however, to highlight certain matters.
- [162] In September 2017, before entering into the Union Goal Transaction, EPL received a technical report from Sound Mining, a consultant firm in South Africa, which recommended use of existing equipment to recover chrome from the tailings. According to Sound Mining, the net present value of the profit to be generated from the project was \$3.82 million.
- [163] Rather than proceeding with the project as envisioned by Sound Mining, EPL entered into a memorandum of understanding with Union Goal in late 2017. That was followed by a "framework agreement", dated March 1, 2018. The framework agreement set out that the parties would negotiate and enter into a series of additional contracts contemplated by the framework agreement. The additional agreements were executed in August 2018 (the "Implementation Agreements").
- [164] The Union Goal Transaction provided for the construction of a new plant, financed by a loan and initial payment from Union Goal; the purchase of equipment from Union Goal; and the sale of recovered chrome to Union Goal. 253 objected to the project, on several grounds including EPL's lack of due diligence and that the amount EPL would have to pay Union Goal for equipment and financing would far exceed the revenue EPL could recover.
- [165] On September 18, 2018, 253's counsel wrote to EPL asking it to commence proceedings against the directors and officers who were involved in approving the Union Goal Transaction. The letter advised that unless the company confirmed by October 2 that it would commence such proceedings, 253 would seek leave to bring a derivative action.
- [166] On September 28, 2018, the board of EPL formed a special committee of directors to consider the matter (the "Special Committee"). The members of the Special Committee were George Dorin, the chairman of EPL's board, Alex Guan and Nigel Dentoom. Mr. Dorin had been a director since July 2016. Mr. Dentoom and Mr. Guan had been appointed directors of EPL on March 28 and April 27, 2018, respectively -- that is, after EPL had entered into the framework agreement but before it entered into the Implementation Agreements.
- [167] On October 23, 2018, counsel for 253 provided EPL with a draft affidavit from 253's CEO, Rong Kai Hong, and a draft notice of civil claim. The proposed named defendants are Diana Hu, Michael Cosic, Bielen Shi, Sheng (Sam) Wang, Douglas Perkins, Mr. Dorin and Mr. Dentoom. Ms. Hu is the CEO of EPL. The other proposed defendants, other than Mr. Dentoom, were directors at the time EPL entered into the framework agreement. In its proposed notice of civil claim, 253 alleged that the defendants were negligent in approving

the Union Goal Transaction and in breach of their fiduciary duty to EPL.

- [168] On November 1, 2018, counsel for EPL advised counsel for 253 of the appointment and composition of the Special Committee and sought additional time for the Special Committee to complete its review of the material that had been submitted. 253 did not wait for the decision of the Special Committee. The petition was filed on November 2, 2018.
- [169] The Special Committee continued its work and ultimately concluded that it would not be in the best interests of EPL to commence legal proceedings against any of the proposed defendants. On December 17, 2018, EPL's board of directors adopted the recommendations of the Special Committee not to commence the legal proceedings proposed by 253.
- [170] Uncontested evidence before the chambers judge indicated that EPL did not know the cost of equipment when it entered into the framework agreement. When the equipment agreement was signed in August 2018, those costs were set at \$41 million.
- [171] On May 14, 2019, EPL's Q1 2019 Condensed Interim Financial Statement disclosed that EPL had capitalized and expended \$64,291,000 on the project. This included both the cost of equipment and cost of construction. It owed Union Goal \$46,919,000.
- [172] Pursuant to the agreements, EPL can only recover revenues of \$16 million leading to a shortfall of almost \$50 million. The agreements do contain a "put option". Pursuant to its terms if the put option is exercised, EPL must return to Union Goal the equipment and Union Goal will in return forgive EPL's indebtedness. If EPL exercises the put option it could reduce its losses to approximately \$2 million.
- [173] Based on this evidence 253 alleges that EPL will suffer as a result of the Union Goal Transaction a loss somewhere between \$2 and \$50 million. In addition, it will lose the \$3.82 million projected profit that it would have earned if it had followed the recommendations in the Sound Mining report.
- [174] EPL did not directly challenge 253's financial calculations. In his affidavit, sworn on January 14, 2019, EPL's Chief Financial Officer, Rowland Wallenius, deposed that the final outcome of the Union Goal transaction could not be determined.
- [175] In EPL's 2018 financial statements, its auditors warned that there was "significant doubt about [EPL's] ability to continue as a going concern".

THE CHAMBERS HEARING

- [176] 253's evidence at the chambers hearing consisted of two affidavits sworn by Mr. Hong. EPL relied on two affidavits from Mr. Wallenius, and an affidavit from Mr. Dentoom. In advance of the hearing, 253 applied to cross-examine Mr. Wallenius and Mr. Dentoom and for production of certain documents referenced in their affidavits. Chief Justice Hinkson dismissed those applications. His reasons are indexed 2019 BCSC 570. EPL did not apply to cross-examine Mr. Hong.

- [177] The chambers judge commenced his reasons by setting out the background to the dispute. He commented on the positions of both parties in relation to certain evidentiary matters. He noted that the notice of civil claim that 253 sought to file alleged the defendants were negligent and in breach of their fiduciary duties to EPL.
- [178] The chambers judge then turned to the law concerning derivative actions. He noted the criteria that were in issue on this application were those dealing with best interest and good faith. He commenced his analysis by setting out the best interest test:
- [25] The requirement that the proposed action be in the best interest of the company was summarized in *Arkansas Teacher Retirement System v. Lions Gate Entertainment Corp.*, 2016 BCSC 432 [Lions Gate], at paras. 163 to 165:
- [163] It is clear that financial well-being of the company is an important consideration in determining its best interests.
- [164] The inquiry of whether the action appears to be in Lions Gate's best interests, therefore, involves considering whether the proposed action is bound to fail, a defence raised is bound to be accepted, and importantly, whether the potential relief will justify the cost and inconvenience to the corporation: *Jordan Enterprises Ltd.* at para. 35, *Discovery Enterprises Inc. v. Ebco Industries Ltd.* (1997), 40 B.C.L.R. (3d) 43 (S.C.) at para. 43, *Mikulic v. Peter*, 2013 BCSC 941 at para. 11. In *Carr*, the court stated at para. 22:
- The balancing between potential relief and inconvenience to the company involves consideration of the amount of the potential claim to ascertain whether the alleged misconduct materially affects the company
- [165] Accordingly, [the petitioner] must show that the potential benefits of commencing and pursuing the claim will justify the cost of the litigation and the inconvenience to the Company, that a reasonable claim exists, and that there is some evidentiary foundation before the Court.
- [179] The chambers judge noted that the draft notice of civil claim alleged both breach of fiduciary duty and negligence. He found that 253 had put forward no evidence that the proposed defendants breached their fiduciary duty. He held that it could not be in the best interest of EPL that its current directors be required to defend themselves in an action based on nothing more than unsupported speculation: at para. 32.
- [180] The chambers judge then went on to consider the claim in negligence. He noted the pleadings alleged the directors failed to conduct sufficient due diligence, to obtain a feasibility study or explore other options to exploit the tailings. He noted the pleadings alleged that the Union Goal Transaction would be less profitable for EPL than the use of its existing equipment and that all financial benefit from any increased production would go to Union Goal.

- [181] The chambers judge next noted that EPL relied on the "business judgment rule" which accords deference to a business decision by directors for a corporation as long as it lies within a range of reasonable alternatives. He noted that the business judgment rule does not prevent a court from finding directors negligent if they fail to use reasonable care in obtaining necessary information or failed to consider facts that they knew or should have known or ignored important information that was in their possession. He noted that EPL had failed to disclose various documents which the Special Committee alleged had affected their decision. He said in the absence of that material, the court was in no position to assess the reasonableness of the Special Committee's decision.
- [182] The chambers judge concluded that 253 had satisfied the best interest element of the test for leave. In that regard, he said:
- [44] 2538520 has raised specific allegations of negligence and EPL has failed to put forward the evidence that it says would show the proposed derivative action is bound to fail. In the result, I cannot say the proposed action is bound to fail. I find that, insofar as the proposed claim is based on allegations of negligence, 2538520 has satisfied the "best interests" element of the test for leave.
- [183] The chambers judge then turned to the good faith criteria. He commenced his discussion as follows:
- [45] The foregoing conclusion does not end the matter because 2538520 must also show good faith. The meaning of the good faith requirement in s. 233(1) was summarized in *Jordan Enterprises Ltd. v. Barker*, 2015 BCSC 559 at paras. 27-30:
- [27] The onus is on the applicant to establish that the derivative proceeding is being brought in good faith. There is no presumption of good faith. Evidence must be adduced to establish good faith: *Luft v. Ball*, 2013 BCSC 574 at para. 46, citing *Creative Realty Corp. v. 333 Terminal Holdings Ltd.*, 2011 BCSC 638 at para. 19.
- [28] The test for good faith is whether the action is brought for the primary purpose of pursuing the claim on the company's behalf. Factors to consider include: (i) the applicant's belief in the merits of the proposed action, (ii) existing disputes between the parties, and (iii) alleged ulterior motives. See *Luft v. Ball* at para. 46, citing *Bennett v. Rudek*, 2008 BCSC 1278 at para. 46.
- [29] The applicant's belief in the merits of the intended action is not determinative of good faith, but, if accepted by the court, is a *prima facie* indication that the applicant is acting with proper motives: *Discovery Enterprises Inc. v. Ebco Industries Ltd.* (1998), [1998] B.C.J. No. 1301 at para. 5, 50 B.C.L.R. (3d) 195.
- [30] Ultimately, the existence of good faith is a question of fact to be determined on all of the evidence and the particular circumstances of the case: *Luft v. Ball* at para. 46, citing *Lost Lake Properties Ltd. v. Sunshine Ridge Properties Ltd.*, 2009 BCSC 938 at para. 56.

[184] He then set out the onus of proving good faith:

[46] That passage was more recently cited in *Lions Gate* at para. 157, which also noted that the onus of proving good faith is "substantial".

[Emphasis added.]

[185] The chambers judge noted that the test of good faith centres around the primary purpose of bringing the action and the extent to which there are ulterior motives. He reviewed evidence concerning Mr. Hong's prior dealings with EPL, including his involvement in a 2016 proxy battle in which he unsuccessfully attempted to gain control of EPL. He noted the proxy battle had led to litigation in Ontario in which Mr. Hong had sued EPL's major shareholder Ka An Development Co. Limited ("Ka An") and EPL's corporate lawyer Fasken Martineau DuMoulin LLP ("Fasken"). He cited *DeCotiis v. Petromin Resources Ltd.*, 2017 BCSC 514 [DeCotiis] for the proposition that a petitioner's prior involvement in a previously unsuccessful attempt to take over a company was a relevant factor in finding a failure to satisfy the onus of good faith.

[186] The chambers judge also noted that in addition to the previous involvement in a takeover bid, Mr. Hong had made his own proposal to buy chrome produced from EPL tailings. The chambers judge found that Mr. Hong, the CEO of 253, clearly has or has had personal interest separate from whatever concerns he may have for the best interest of EPL. In that regard, the chambers judge noted that Mr. Hong was involved in a failed bid to take over the company, and subsequently, rebuffed or ignored when he sought to enter a transaction with the company to buy chrome produced from the tailings. He concluded that those facts clearly suggest that Mr. Hong's personal interest were a significant motive for the proposed action, and the most likely inference to be drawn from the evidence is that the proposed action is an attempt to continue Mr. Hong's unsuccessful takeover bid by other means or to obtain retribution for that bid's failure. While acknowledging that evidence of a personal interest may be not fatal to a leave application if it is outweighed by other evidence of good faith, the judge held that in the presence of clear evidence that suggests 253 is motivated by other interests, the mere assertion of belief in the merits of the claim is not sufficient. He found that 253 had failed to satisfy the onus of proving good faith.

[187] The chambers judge then went on to comment that Mr. Hong's evidence suggests that 253 is seeking to protect its interest as a shareholder rather than to advance the interests of the company. He noted that while it is entirely proper for a shareholder to be concerned about its position and the value of its share, it is not a matter properly raised in a derivative action. He suggested that if 253 was alleging unfair treatment and damages suffered in its capacity as a minority shareholder, that was a matter that should be raised as an oppression claim under s. 227 of the BCA.

[188] In the result, the chambers judge concluded that 253 had failed to satisfy the good faith requirement in s. 233(1)(c) of the BCA and the petition must be dismissed with costs.

ON APPEAL

[189] On the appeal, 253 submits that the chambers judge made three reversible errors in respect of his finding that the appellant was not acting in good faith. In particular, they submit:

- a. he committed an error by failing to consider the appellant's belief in the merits of the proposed action, which is, as a matter of law, *prima facie* evidence of good faith under s. 233(1)(c) of the BCA;
- b. he committed an error by drawing inferences that were not supported by the evidence related to the appellant's motivation; and
- c. he committed an error in law in finding that the derivative action was not appropriate because the appellant wanted to protect the value of its shares in EPL.

[190] EPL supports the trial judgment and submits the chambers judge did not make any of the alleged errors. It further submits that the petition should, in any event, have been dismissed on the basis that 253 did not meet the best interest precondition under s. 233(1)(d).

[191] In this regard, it submits that the best interest test includes three conditions. The first two comprise a merits threshold: (1) whether the proposed action is bound to fail; and (2) whether the defence raised is bound to be accepted. The final is a balancing exercise: (3) whether the potential relief justified the cost and inconvenience to the corporation.

[192] EPL submits that the chambers judge limited his consideration as to whether the proposed action was bound to fail, and failed to consider the second and third aspects of the test. In its submission, a correct and complete application of the test with respect to the proposed negligence claim would lead to a finding that the best interest precondition was not met.

[193] EPL submits that the chambers judge made the following errors:

1. he improperly reversed the burden of proof with respect to the proposed negligence claim in finding that EPL failed to put forward evidence that the proposed derivative action was bound to fail;
2. he misapplied the best interests test by failing to consider:
 - a) whether the defence is bound to be accepted; and
 - b) the cost and inconvenience of proceeding to EPL; and
3. he refused to defer to the Special Committee in his analysis of cost and inconvenience or conduct his own analysis of whether the cost and inconvenience favoured leave or dismissal.

- [194] EPL further submits that the chambers judge did not make a finding on the reasonable efforts criteria. In that regard, EPL submits that 253 commenced the action prior to the Special Committee having sufficient time to consider the proposed claim.
- [195] EPL also submits that the statutory test does not make leave mandatory upon fulfillment of the four requirements. It submits that courts retain the discretion to decline granting leave even in circumstances in which the four criteria have been met. In the circumstances of this case, it submits that if this Court concludes that all of the criteria have been met, the matter should be referred back to the chambers judge to make submissions within the framework of this Court's decision and the chambers judge be given the opportunity to exercise his discretion.

ANALYSIS

A. Best Interest

- [196] As did the chambers judge, I begin my analysis with the best interest criteria. I do so for two reasons. The first is that the best interest criteria is the overarching requirement for leave. Unless the action is in the best interests of the corporation, leave will not be granted. The second is that notwithstanding that best interest and good faith are separate requirements under the BCA, the finding that a proposed action is in the best interests of the company can support a conclusion that the petitioner is acting in good faith and is a relevant consideration in assessing the issue of good faith: *Primex* at para. 32; *L&B Electric Appeal* at para. 64; *Lost Lake Properties Ltd v. Sunshine Ridge Properties Ltd.*, 2009 BCSC 938 at para. 57, *aff'd* 2011 BCCA 473.
- [197] The chambers judge found that the negligence action was in EPL's best interests. EPL submits, and my colleague agrees, that the chambers judge failed to consider two required aspects of the test for best interests: (1) whether the defence raised is bound to be accepted, and (2) the costs and inconvenience of the corporation of bringing the action. EPL submits that the business judgment rule provides a complete answer to both aspects of the test.
- [198] Section 142(1)(a) of the BCA sets out the duty of care owed by directors:
- 142 (1)(a) A director or officer of a company, when exercising the powers and performing the functions of a director or officer of the company, as the case may be, must
- (b) exercise the care, diligence and skill that a reasonably prudent individual would exercise in comparable circumstances
- [199] In *Peoples Department Stores Inc. (Trustee of) v. Wise*, 2004 SCC 68 [Peoples], the Supreme Court of Canada set out the test a plaintiff must meet to succeed in a negligence claim against a director:

- [66] In order for a plaintiff to succeed in challenging a business decision he or she has to establish that the directors acted (i) in breach of the duty of care and (ii) in a way that caused injury to the plaintiff: W. T. Allen, J. B. Jacobs and L. E. Strine, Jr., "Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law" (2001), 26 Del. J. Corp. L. 859, at p. 892.
- [200] In *Peoples* the Court recognized the importance of the business judgment rule:
- [64] The contextual approach dictated by s. 122(1)(b) of the CBCA not only emphasizes the primary facts but also permits prevailing socio-economic conditions to be taken into consideration. The emergence of stricter standards puts pressure on corporations to improve the quality of board decisions. The establishment of good corporate governance rules should be a shield that protects directors from allegations that they have breached their duty of care. However, even with good corporate governance rules, directors' decisions can still be open to criticism from outsiders. Canadian courts, like their counterparts in the United States, the United Kingdom, Australia and New Zealand, have tended to take an approach with respect to the enforcement of the duty of care that respects the fact that directors and officers often have business expertise that courts do not. Many decisions made in the course of business, although ultimately unsuccessful, are reasonable and defensible at the time they are made. Business decisions must sometimes be made, with high stakes and under considerable time pressure, in circumstances in which detailed information is not available. It might be tempting for some to see unsuccessful business decisions as unreasonable or imprudent in light of information that becomes available *ex post facto*. Because of this risk of hindsight bias, Canadian courts have developed a rule of deference to business decisions called the "business judgment rule", adopting the American name for the rule.
- [67] Directors and officers will not be held to be in breach of the duty of care under s. 122(1)(b) of the CBCA if they act prudently and on a reasonably informed basis. The decisions they make must be reasonable business decisions in light of all the circumstances about which the directors or officers knew or ought to have known. In determining whether directors have acted in a manner that breached the duty of care, it is worth repeating that perfection is not demanded. Courts are ill-suited and should be reluctant to second-guess the application of business expertise to the considerations that are involved in corporate decision making, but they are capable, on the facts of any case, of determining whether an appropriate degree of prudence and diligence was brought to bear in reaching what is claimed to be a reasonable business decision at the time it was made.
- [201] EPL submits that the business judgment rule applies to both the decision to enter the Union Goal Transaction and the subsequent decision of the Special Committee to not commence proceedings. It says that as a result of the rule the derivative action is bound to fail. It further submits that the decision of the Special Committee is determinative as to whether bringing the proceedings are in the best interests of the company.

- [202] The two decisions raise different considerations. I will deal with each in turn.
- [203] In regard to the Union Goal Transaction, 253 put before the judge a body of evidence, based almost entirely on EPL's public disclosures, which suggested that the Union Goal Transaction was financially doomed from the outset. The capital costs of the project far outstripped any potential revenues. Rather than proceeding with a project using existing equipment that was projected to generate profits of \$3.82 million, the directors chose the Union Goal Transaction. There is now significant doubt about the company's ability to continue as a going concern. The question for the Court in the derivative action will be whether the directors in proceeding with the Union Goal Transaction exercised the care, diligence and skill that a reasonably prudent individual would have exercised in comparable circumstances.
- [204] The chambers judge was well aware of the business judgment rule. He correctly described it as follows:
- [40] The effect of the business judgment rule is that if, after consideration of relevant and reasonably available information and advice, the directors made a reasonable business decision, a claim against them cannot succeed even if others might have come to a different conclusion or their decision turns out to be wrong. But it does not prevent the Court from finding directors negligent if they failed to use reasonable care in obtaining necessary information, or failed to consider facts that they knew or should have known, or ignored important information that was in their possession.
- [Emphasis added.]
- [205] The chambers judge concluded that he could not find on the evidence put forward by EPL that its defence based on the business judgment rule was bound to succeed. In this regard it must be emphasized that EPL had total control of document production. It chose what internal documents to disclose and what it would withhold. By way of example both Mr. Dentoom and Mr. Wallenius referred in their affidavits to internal financial analysis and modeling that was conducted in connection with the decision to enter into the Union Goal Transaction, but did not attach that documentation to their affidavits.
- [206] While at trial a defence based on the business judgment rule may succeed, that is not the test for determining whether the derivative action should go forward. 253 put before the chambers judge an evidentiary record that satisfied the judge that the proposed action has a reasonable prospect of success and was not bound to fail. The onus then shifted to EPL to establish that their defence is bound to succeed. This it failed to do.
- [207] I do not accept EPL's submission that the chambers judge reversed the burden of proof. Nor do I agree with my colleague that the chambers judge did not consider the evidence in determining that the proposed claim in negligence satisfied the best interest test for leave. The chambers judge fully understood the need for evidence to support the allegations in the notice of civil claim. It was the lack of evidence that doomed the fiduciary duty claims.

There was in this case evidence before the chambers judge that supported 253's allegations in negligence. The chambers judge found that 253 had raised specific allegations of negligence and EPL had failed to put forward evidence that would show their defence is bound to succeed. That finding was clearly open to the chambers judge on the evidence before him.

- [208] The decision of the Special Committee raises a somewhat different issue. It goes to the question as to whether the proposed litigation is in the best interest of the company.
- [209] Whether a proceeding appears to be in the best interest of a corporation is not restricted to the apparent strength of the proposed action. In *Jahnke*, the court set out the considerations that must be considered:
- [68] That noted, I should clarify that the "interests of the corporation" inquiry is not tightly restricted to nothing more than an assessment of the apparent strength of the proposed action. This is because, as recognized in the Dickerson Report itself, there are circumstances when it would clearly not be advisable for a corporation to pursue a claim even where success seems almost certain. I have in mind here, for example, situations such as those where an action will cost far more to prosecute than it can possibly yield in damages, where pursuing a claim will harm important and ongoing business relationships, or where going to court will generate problematic publicity for the corporation. In all of these sorts of situations, the narrow question of whether a claim is arguable will not properly answer the question of whether that claim is in the interests of the corporation. This is not a new idea. Cases where a court has been prepared to consider more than just the chances of success for a proposed action include *Schadegg v Alaska Apollo Resources Inc.*, 1994 CarswellBC 2132 (BC Sup Ct), *Melnyk v Acerus Pharmaceuticals Corporation*, 2017 ONSC 1285, *Maxwell v Schuman*, 2005 BCSC 1430, *Discovery Enterprises Inc. v Ebco Industries Ltd.* (1997), 1997 CanLII 4375 (BC SC), 40 BCLR (3d) 43 (Sup Ct), and *Primex Investments*. Thus, while the strength of the proposed action is the central consideration in any s. 232(2)(c) inquiry, it is not the only consideration or, necessarily, the deciding consideration.
- [210] EPL submits that the chambers judge should have deferred to the decision of the Special Committee that the litigation was not in the company's best interest. It submits the decision not to pursue litigation is a business decision that engages the business judgment rule meaning the court should defer to such a decision where it is reasonable and has been made impartially. The question that then arises is whether the decision of the Special Committee concerning the best interest of the corporation is determinative of the issue. On this question, there is a divergence of judicial authority.

- [211] In *Schafer v. International Capital Corp.* (1996), 153 Sask. R. 241 (Q.B.), aff'd [1997] S.J. No. 374 (C.A.) [Schafer], Justice Baynton held that the business judgment rule creates a presumption that if the directors of a corporation make an informed decision that the disadvantages outweigh the advantages of commencing an action, that decision reflects the best interest of the corporation. In this regard, he said:
- [25] In determining this issue the "Canadian version" of the sound business judgment rule applies. The rule is in effect a presumption that if the directors of the corporation make an informed decision that the disadvantages outweigh the advantages of commencing the action, then this is what is in the best interests of the corporation. The decision to commence or not to commence an action is like any other business decision that is ordinarily a matter of internal management to be left to the discretion of the directors absent instruction from the shareholders. Courts seldom interfere with such intra vires discretion unless the directors are guilty of misconduct equivalent to breach of trust, or unless they stand in a dual relation which prevents an unprejudiced exercise of judgment. If there is misconduct or a dual relation then the presumption that the decision of the directors is in the best interests of the corporation will not apply.
- [212] In *L&B Electric*, Justice Moir challenged the assumption that the legislation implied any presumption in favour of the directors. In his detailed analysis, found at paras. 32-40 of his reasons, he traced the legislative history of derivative actions in Canada and suggested that it was born of a desire to radically reform the common law. He rejected the reasoning in *Schafer*. He concluded his analysis as follows:
- [42] In my assessment, the broad purpose of s. 4 is to allow minority shareholders to enforce rights of their corporations when management will not do so. There is no purposive reason to read the restraints in s. 4 more restrictively than the text plainly provides. In my assessment, the scheme underlying s. 4 involves the private use of civil remedies to enforce duties, as the alternative to public regulation. Again, this suggests there is no disharmony between the scheme and the plain text. Therefore, I respectfully reject the reasoning in *Schafer*. There is no presumption in favour of the directors' opinion. Mr. Oickle bares the onus of satisfying the Court that he is acting in good faith and his proposed suit on behalf of the corporation appears to be in the interests of the corporation. Nothing less, but nothing more.
- [213] If it were necessary to choose between the two positions, I would favour the analysis of Justice Moir in *L&B Electric*. The question as to whether or not the proceeding appears to be in the best interest of the corporation is one to be made by the judge hearing the application, not the directors. If the drafters of the legislation had wished to insert such a presumption into the legislation, they could have done so.
- [214] In this case, however, it matters not which of the two approaches is correct. As noted by Justice Baynton in *Schafer* the presumption does not apply in circumstances in which the members of the Special Committee are in a dual relation which prevents an unprejudiced

exercise of judgment. In this case, the directors on the special committee were in such a dual relationship. Mr. Dorin had been a director since July 2016, and was a member of the board when it entered into both the framework agreement and the Implementation Agreements. Mr. Dentoom and Mr. Guan, while they were appointed to the Board after the framework agreement was signed, were members when the Implementation Agreements were signed. Mr. Dorin and Mr. Dentoom will both be defendants if the litigation proceeds. In the circumstances, there is no presumption in favour of the decision of the Special Committee: L&B Electric Appeal at para. 73.

- [215] While the chambers judge was not required to defer to the views of the Special Committee, he did have to consider the cost and inconvenience to the corporation of the litigation. I do not accept the submission that the chambers judge did not.
- [216] At the hearing EPL devoted several pages of its written submissions setting out those alleged costs and inconvenience. They were also detailed in Mr. Dentoom's affidavit. The submissions included the following: (1) that all EPL directors have indemnification agreements requiring EPL to advance and indemnify them for any and all costs incurred that are not covered by the insurance; (2) EPL's limited working capital should not be spent on legal expenses for a claim against its directors; (3) the proposed action could cause business disruption and carries the risk that key personnel might resign; (4) the action would disrupt the company and its people at a critical junction in EPL's business and the share price is unlikely to react favourably; (5) the proposed claim may hamper EPL's ability to attract talented directors; and (6) the litigation may damage EPL's business relationship with Union Goal.
- [217] These matters were all before the chambers judge. He correctly noted that the legal test includes consideration of whether the potential relief will justify the cost and inconvenience to the corporation. The amounts in issue in this potential lawsuit are significant. The evidence before the judge indicated that the core financial stability of EPL was threatened by the Union Goal Transaction. The company's auditors have queried whether the company can continue to carry on business because of the agreement. The potential damages are in the millions of dollars, and the sole recourse of the company would appear to be against the proposed defendants. I do not accept that the judge did not consider the cost and inconvenience in finding it was in the best interest of the company to pursue the litigation. In finding that the petitioner had satisfied the best interest element of the test for leave, the chambers judge implicitly found that the case justified the cost and inconvenience to EPL.
- [218] If the chambers judge did fail to carry out the analysis, this Court can do so in any event. It is not necessary to return the matter to the judge. In my opinion the case justifies any possible cost and inconvenience to EPL. In any case in which an action is going to be brought against a company's directors, there will be cost and inconvenience. It is inevitable. Those costs must be weighed in the context of remedial legislation which is intended to give shareholders the right to bring an action against the directors if they have breached

their duty to the company.

[219] In this case, the cost issues raised by EPL go to the legal expenses of the potential proceeding, and the suggestion that EPL may be obliged to indemnify the directors and officers if their costs are greater than the insurance that is in place. I will deal with each of those considerations in turn.

[220] The BCA, in sections 233(2-4), deals directly with the question of costs of a derivative action. Those sections read:

Powers of court in relation to derivative actions

233 (2) Nothing in this section prevents the court from making an order that the complainant give security for costs.

- (3) While a legal proceeding prosecuted or defended under this section is pending, the court may,
 - (a) on the application of the complainant, authorize any person to control the conduct of the legal proceeding or give any other directions for the conduct of the legal proceeding, and
 - (b) on the application of the person controlling the conduct of the legal proceeding, order, on the terms and conditions that the court considers appropriate, that the company pay to the person controlling the conduct of the legal proceeding interim costs in the amount and for the matters, including legal fees and disbursements, that the court considers appropriate.
- (4) On the final disposition of a legal proceeding prosecuted or defended under this section, the court may make any order it considers appropriate, including an order that
 - (a) a person to whom costs are paid under subsection (3) (b) repay to the company some or all of those costs,
 - (b) the company or any other party to the legal proceeding indemnify
 - (i) the complainant for the costs incurred by the complainant in prosecuting or defending the legal proceeding, or
 - (ii) the person controlling the conduct of the legal proceeding for the costs incurred by the person in controlling the conduct of the legal proceeding, or
 - (c) the complainant or the person controlling the conduct of the legal proceeding indemnify one or more of the company, a director of the company and an officer of the company for expenses, including legal costs, that they incurred as a result of the legal proceeding.

- [221] Pursuant to s. 233(3)(b), while a derivative proceeding is ongoing, the court is authorized to make interim cost orders. At the conclusion of the litigation, the court may make any cost order it considers appropriate. 253 has not sought, nor suggested it will seek, an order for interim costs. Absent such an order, if leave is granted, 253 will be responsible for the costs incurred in prosecuting the proceeding. EPL's exposure to legal costs would likely only arise if the proposed derivative claim is successful.
- [222] In regard to the question of indemnification for the directors, it is far from clear whether this is a realistic concern. EPL has not disclosed the terms or limits of the insurance policies in place. There is a significant legal issue as to whether or not a company can legally indemnify its directors from a claim made in a derivative action. (See the discussion in *Lions Gate* at paras. 175-193.) As set out in *Lions Gate*, s. 163(2) of the BCA prohibits indemnification for derivative claims. While s. 164 of the BCA appears to give the court the power to override s. 163(2) and order indemnity, the circumstances in which such an order would be made are far from clear.
- [223] In my respectful view, the possibility that there may be an obligation some time in the future to pay legal fees or indemnify the directors is not sufficient reason, given the amounts in issue in this litigation, to deny leave. In my opinion it appears to be in the best interest of EPL to grant leave.

B. Good Faith

- [224] I turn now to the question of good faith. In his initial affidavit of October 31, 2018, Mr. Hong deposed:
3. The petitioner is bringing this application because it believes that the proposed defendant directors of [EPL] breached their duties to the company in connection with transactions with Union Goal Offshore Solutions Limited.
88. I am pursuing leave to commence this action as a derivative action for the purpose of pursuing remedies on behalf of [EPL] against the proposed defendants, and for no other or improper purpose.
- [225] In his second affidavit of May 6, 2018, Mr. Hong deposed as follows:
62. Mr. Dentoom has suggested in his affidavit that I am not acting in good faith, large because I did not disclose in my first affidavit that I am a plaintiff in another lawsuit against Fasken Martineau DuMoulin LLP (Fasken) and others relating to [EPL] (the Fasken Claim).
63. I did not disclose that in my first affidavit because I did not believe the fact that I commenced the Fasken Claim was relevant to this proceeding (although, as described below, there is some factual overlap in the two proceedings). I was not attempting to hide my involvement in the Fasken Claim. In fact, I advised Mr. Wallenius and Miss Hu of the Fasken Claim on May 8, 2018. A copy of my email to Mr. Wallenius and Miss Hu advising them of the Fasken Claim is attached to my affidavit as Exhibit M.

69. In any event, in the course of my and Beijing Hehe's attempt to acquire a controlling interest in [EPL], I acquired a substantial number of shares in [EPL], including through the petitioner. I am now through the petitioner, concerned that the Union Goal Transactions have improperly deprived and are going to continue to improperly deprive me of the value of the shares held through the petitioner. Accordingly, I was appointed Chief Executive Officer of the petitioner on October 18, 2018 so I could advance the petition in order to protect my and the petitioner's interest in the share of [EPL].
70. I confirm that I am the petitioner's sole economic interest in [EPL] is in our capacity as (direct or indirect) shareholders. I also confirm that none of the other officers, directors or beneficial owners of the petitioner has any economic interest other than in their capacity as (indirect) shareholders.
- [226] EPL did not apply to cross-examine Mr. Hong on his affidavit.
- [227] In his good faith analysis, the chambers judge indicated that the onus of proving good faith is "substantial". He then acknowledged that Mr. Hong's statements that he believed the derivative action would be in the interest of EPL because the proposed defendant's conduct had been detrimental to the company and that his and 253's sole economic interest was in their capacity as shareholders, could be prima facie evidence of good faith. He went on to find, however, that other evidence called those bald assertions into question. This evidence concerned Mr. Hong's prior dealings with EPL.
- [228] In particular, the trial judge referred to Mr. Hong's effort in 2016 to gain control of EPL in a proxy battle and his own proposal to buy chrome produced from EPL tailings. In finding that 253 had failed to satisfy the onus of proving good faith, the chambers judge reasoned as follows:
- [57] In short, the CEO of the corporate petitioner, who 2538520 puts forward to give evidence on its behalf, clearly has or has had personal interests separate from whatever concern he may have for the best interests of EPL. He was involved in a failed bid to take over the company. He subsequently was rebuffed or ignored when he sought to enter into a transaction with the company. His efforts were rejected in favour of the very transaction that 2538520 now complains of.
- [58] Those facts clearly suggest that Mr. Hong's personal interests, as opposed to the interests of EPL, are a significant motive for this proposed action. The most likely inference to be drawn from the evidence before me is that the proposed action is an attempt to continue Mr. Hong's unsuccessful takeover bid by other means or to obtain retribution for that bid's failure.
- [59] Evidence of a personal interest may not be fatal to a leave application if it is outweighed by other evidence of good faith. But in the presence of clear evidence that suggests 2538520, through its CEO, is motivated by other interests, a mere assertion of belief in the merits of the claim accompanied by a bald profession of good faith is not sufficient.

- [229] Having concluded that 253 had failed to satisfy the onus of good faith, the chambers judge then commented on Mr. Hong's evidence that 253 was seeking to protect its interest as a shareholder. In this regard he said:
- [61] Further, Mr. Hong's own evidence suggests that 2538520 is seeking to protect its interest as a shareholder rather than advance the interests of the company. His affidavit says that in the course of the takeover bid "I acquired a substantial number of shares in [EPL], including through the Petitioner" and that his goals include "to protect my and the petitioner's interest in the shares of [EPL]".
- [62] It is entirely proper for a shareholder to be concerned about its position and the value of its shares. But that is not a matter that is properly raised in a derivative action. If 2538520 is alleging unfair treatment and damages suffered in its capacity as a minority shareholder, that is a matter to be raised in an oppression claim under s. 227 of the BCA.
- [230] In my view, in his good faith analysis, the chambers judge applied the wrong onus of proof. He held that the onus to prove good faith is substantial. As set out above, good faith only needs to be proved on the balance of probabilities. The application of the wrong legal standard is an error of law subject to a standard of correctness: *Housen v. Nikolaisen*, 2002 SCC 33 at para. 36.
- [231] While my colleague and I agree that good faith only needs to be proved on the balance of probabilities, we differ on whether the chambers judge applied the correct standard. Whether he did so is of critical importance. If he applied the correct test, then his decision, as my colleague correctly notes, is entitled to deference. If, however, he applied the wrong standard, this Court must revisit his findings.
- [232] Prior to the decision in *F.H.*, the standard of proof in civil cases had long been a matter of controversy: see paras. 26-49 of *F.H.* While there was general agreement that the standard in civil cases was proof on a balance of probabilities, many cases reflected the view of Lord Denning that "there may be degrees of probability within that standard" that "require a degree of probability which is commensurate with the occasion": *Bater v. Bater*, [1950] 2 All E.R. 458 (C.A.) at 459.
- [233] *Tremblett v. S.C.B. Fisheries Ltd.* (1993), 116 Nfld. & P.E.I.R. 139 (NLSCTD), to which my colleague referred, is an example of a case in which a higher standard was imposed. While Justice Puddester stated that the burden was that of the civil balance of probabilities, he required the case to be proved on a clearly established balance or preponderance of the evidence. In that regard, he said:
- [58] However, in my view the history of the development of statutory provisions such as s. 369 shows that for statutory relief against the strict common law position of non-intervention in majority decisions internal to corporations, in light of the extraordinary power vested in a shareholder or director applicant to use the corporate resources and to create a position of legal conflict between the corporation and others, it is necessary that an applicant bring

cogent evidence establishing clearly on a preponderance of evidence that the application is in fact brought in good faith. ...

[78] The very existence of a separate dispute between the applicant and the corporation is obviously of concern as part of the totality of evidence to be considered as to whether the applicant has met the substantial burden of establishing his good faith in bringing an application for leave.

[82] Nevertheless as noted above, in an application such as this there is a substantial onus on an applicant-complainant himself to positively establish "good faith". Even though this matter is assessed on an application, as opposed to a trial, in my view there is a substantial onus to be met by any applicant, including the applicant here, with respect to the establishment of good faith.

[83] In my view, while the burden is that of the civil balance of probabilities, it is appropriate to require that there be a clearly established balance or preponderance shown.

[Emphasis added.]

[234] In *Primex*, Justice Tysoe cited from the respondent's submissions, which quoted some of the above passages from *Tremblett*. While Justice Tysoe noted the respondent's submission that the onus to prove good faith is a substantial one, he did not himself comment on the legal standard: *Primex* at para. 30.

[235] In *Tkatch v. Dr. Heide Dr. Tkatch Dr. Climenhaga Dr. Fietz Inc.* (1996), 29 B.L.R. (2d) 266 (B.C.S.C.) at para. 24, Justice Hutchinson, citing *Primex*, said there was a substantial onus on a petitioner to show positively that the application was brought in good faith.

[236] In *Discovery*, the respondent, citing *Tkatch*, submitted the burden of proving good faith was substantial. Chief Justice Williams specifically rejected the submission of a higher standard and held that good faith only needed to be proved on a balance of probabilities: *Discovery* at para. 118.

[237] Notwithstanding that *Discovery* would appear to have conclusively determined the issue, the question of the onus was resurrected in *LaRoche v. HARS Systems Inc.*, 2001 BCSC 140, where Justice Hood, in a passage quoted by my colleague, said:

[95] These factors, and others, go to the issue of good faith. In *Primex*, Tysoe, J. seemingly agreed that the onus on the Petitioner to establish good faith is a substantial one. In any event, on the basis of Mr. LaRoche's conduct, as well as the evidence pertaining to the merits of the two actions, and to their settlement, although in conflict in some areas, Mr. LaRoche has not satisfied me that it is more likely than not that his primary purpose is the recovery by HARS of fairly substantial sums in the actions, and that he is acting in good faith.

[238] My colleague reads these reasons as confirmation that the reference to the requirement being substantial does not change the burden of proof on a balance of probabilities. With respect, I read the decision otherwise. It must be remembered that *LaRoche* was decided

some seven years before F.H. As I read Justice Hood's decision, he clearly recognized that a higher standard of proof might apply regarding bad faith. He said that in *Primex*, Justice Tysoe had seemingly agreed that the onus on the petitioner to establish good faith is a substantial one. (I pause to note that Justice Tysoe made no such finding.) Justice Hood then went on to find, "in any event," the petitioner had failed to satisfy him on a simple balance of probabilities that he was acting in good faith. In other words, Justice Hood did not have to determine whether there was a higher onus because, in his case, the petitioner did not reach even the balance of probabilities.

- [239] All of the above cases were decided before F.H., which made clear that there was only one civil standard of proof at common law: proof on a balance of probabilities. The Court in F.H. specifically rejected the idea that a higher standard might apply in certain cases: F.H. at para. 40.
- [240] The issue did not arise again until *Lions Gate*. In *Lions Gate*, the chambers judge stated at para. 157 that in *LaRoche*, the court opined the onus of proving good faith is "substantial." That statement, which was relied upon by the chambers judge in this case, was, unfortunately, a complete misreading of *LaRoche* and led the chambers judge into error.
- [241] In my respectful opinion, when the chambers judge stated that the onus of proving good faith was substantial, he was applying an onus higher than the balance of probabilities. If the chambers judge intended to decide the case on the balance of probabilities, there was no reason for him to mention any other standard of proof. For these reasons, I am of the view that the chambers judge erred and applied the wrong standard of proof.
- [242] In my view, in addition to the question of onus, there are, with respect, other errors in the chambers judge's good faith analysis. In his good faith analysis, the chambers judge referenced Mr. Hong's sworn evidence as to the merits of the case, but did not consider his own finding that the proposed proceeding was in the best interest of the corporation. As set out at para. 52 above, such evidence is a relevant consideration in assessing the issue of good faith.
- [243] The chambers judge gave no consideration to Mr. Hong's evidence that 253 was seeking to protect the value of his shares, holding that is not a matter that is properly raised in a derivative action because if 2538520 is alleging unfair treatment and damages suffered in its capacity as a minority shareholder, that is a matter to be raised in an oppression claim under s. 227 of the BCA. With respect, that is not an accurate statement of the law. A shareholder may only bring an action for oppression where the shareholder has suffered particular prejudice or damage apart from the prejudice suffered by all shareholders. Where the shareholder's damage is the same as that suffered by all shareholders, the action must be brought on behalf of the company, as a derivative action: *Dubois v. Milne*, 2020 BCCA 216 at para. 106; *Jaguar Financial Corporation v. Alternative Earth Resources Inc.*, 2016 BCCA 193 at para. 177.

- [244] That is the situation in this case. 253's loss of share value is the same as suffered by all shareholders. 253's desire to protect the value of its shares supports a finding of good faith because 253's interests coincide with those of EPL. It was a factor the chambers judge should have considered in his good faith analysis.
- [245] As set out at para. 12 above, good faith is a question of fact to be determined on all of the evidence. The failure of the chambers judge to consider relevant evidence is an error of law and a basis for appellate intervention: *Holdyk* at para. 35.
- [246] In this case the chambers judge applied the wrong legal standard and failed to consider relevant evidence. His finding that 253 was not acting in good faith must be revisited.
- [247] Good faith is a question of fact to be determined on all the evidence on a balance of probabilities. The onus of proving good faith lies on 253. Mr. Hong has sworn he believes in the merit of the action. He has also sworn that the petitioner is pursuing leave to commence this action as a derivative action for the purpose of pursuing remedies on behalf of EPL against the proposed defendants, and for no improper purpose. He has further deposed that his sole economic interest in EPL is as a shareholder. He acknowledges a self-interest in protecting the value of his shares.
- [248] Mr. Hong was not cross-examined on his affidavit. There is no direct evidence before the court that challenges his sworn statements.
- [249] In addition to Mr. Hong's sworn evidence, the chambers judge found the derivative action was in the best interest of EPL. That finding is a relevant consideration in assessing the issue of good faith and supports a determination that the petition is brought in good faith.
- [250] The chambers judge drew the inference that Mr. Hong was driven by ulterior motives. In particular, he drew the inference that the purpose of the action was an attempt to continue Mr. Hong's unsuccessful takeover bid by other means or to obtain retribution for that bid's failure. While existing disputes between the parties are relevant to the question of a petitioner's good faith, as noted at para. 14 above, an inference of bad faith is not warranted merely because the petitioner is involved in a shareholder's dispute or related litigation.
- [251] Appellate courts may interfere with the drawing of an inference that does not flow logically and reasonably from established facts. The court's power was explained by Justice D. Smith in *ICBC v. Atwal*, 2012 BCCA 12:
- [40] In addressing this ground of appeal it is important to note the distinction between the drawing of inferences from proven facts and the inference-drawing process. This distinction was helpfully described by Mr. Justice Doherty, for the court, in *R. v. Morrissey* (1995), 97 C.C.C. (3d) 193 (Ont. C.A.) at page 209:

A trier of fact may draw factual inferences from the evidence. The inferences must, however, be ones which can be reasonably and logically drawn from a fact or group of facts established by the evidence. An inference which does not flow logically and reasonably from established facts cannot be made and is condemned as conjecture and speculation. As Chipman J.A. put it in *R. v. White* (1994), 89 C.C.C. (3d) 336 at p. 351, 28 C.R. (4th) 160, 3 M.V.R. (3d) 283 (N.S.C.A.):

These cases establish that there is a distinction between conjecture and speculation on the one hand and rational conclusions from the whole of the evidence on the other. The failure to observe the distinction involves an error on a question of law.

[Emphasis added.]

- [252] To consider this question, it is necessary to review in further detail the underlying evidence that the chambers judge relied on to draw the inference that Mr. Hong was driven by ulterior motives.
- [253] The pleadings filed in the Fasken action set out that in 2016, the plaintiffs Mr. Hong and his partner, Beijing Hehe Fengye Investment Co., attempted to buy a controlling interest in EPL to take control of its board of directors. They retained Fasken as their legal counsel. The lawsuit alleges that Fasken, while representing the plaintiffs in connection with their attempts to gain control of EPL, was also acting for Ka An in connection with its attempt to achieve the same ends. Both groups were attempting to replace the existing directors and gain control of EPL.
- [254] The main thrust of the claim is against Fasken. The lawsuit alleges that Fasken breached its fiduciary duties by acting for Ka An. It further alleged that Fasken disclosed confidential information to Ka An. In the result, the plaintiffs' claim against Fasken is for negligence, breach of fiduciary duty and misuse of confidential information. The claim against Ka An is for knowing assistance in breach of the fiduciary duty and misuse of confidential information.
- [255] The litigation does not involve 253, EPL, or the Union Goal Transaction. It is an action for damages for alleged misdeeds of a solicitor and its client.
- [256] I should note that in submissions, 253's counsel acknowledged that the lawsuit in isolation was not sufficient to draw an inference of ulterior purpose but the inference could be supported when coupled with evidence of other activities of Mr. Hong in late 2017 and early 2018.
- [257] In late 2017 Mr. Hong sought a shareholders list. On January 31, 2018 he met with Mr. Wallenius. Mr. Wallenius in his first affidavit set out what happened at the meeting:
- [68] Mr. Hong told me that, through a company, he had purchased a block of shares previously owned by K2, a former large shareholder of EPL. He told me he wanted to benefit from those shares, whether through purchasing more shares, selling the K2 block of shares, or investing in another way. Mr. Hong also told me he wanted to speak directly to Ka An

Development Co., the large shareholder of EPL. Regarding his request for a shareholders list, Mr. Hong informed me that his and Mr. Hung's interest in the list was to assist his effort to contact significant shareholders.

[258] I note that the chambers judge did not refer to this evidence in his reasons.

[259] There is no evidence that Mr. Hong or 253 have taken steps since the end of the proxy battle to seek control of 253. Nothing in the evidence, I suggest, could lead to an inference that Mr. Hong was carrying on a proxy battle or vendetta against Ka An or that the derivative action is an attempt to continue Mr. Hong's unsuccessful takeover bid by other means. At its highest, the evidence indicates that Mr. Hong was exploring possible ways upon which he could benefit from his investment. There is nothing wrong in his desire to do so. One would expect no less.

[260] An inference must flow logically and reasonably from established facts. There is a distinction between conjecture and speculation on the one hand, and rational conclusions from the whole of the evidence on the other. In my respectful view, an inference cannot be reasonably and logically drawn from the established facts that the derivative action is an attempt to continue Mr. Hong's unsuccessful takeover bid by other means. Such an inference would be based on speculation and conjecture and cannot be sustained.

[261] The second piece of evidence referenced by the chambers judge was Mr. Hong's expressed interest in purchasing the chrome tailings. By the time Mr. Hong had raised that issue with EPL, EPL was already committed to the Union Goal Transaction. As I read Mr. Hong's affidavit, his reference to his proposed offer to purchase the tailings was made in the context of the directors' failure to consider options other than Union Goal. It does not lead to an inference of an ulterior motive.

[262] The chambers judge relied on DeCotiis for the proposition that a previous involvement in an unsuccessful attempt to take over the company was a relevant factor in finding a party had failed to satisfy the onus of demonstrating good faith. DeCotiis, with respect, is clearly distinguishable. In that case there was a long documented history of an ongoing attempt to secure control of the company. In earlier proceedings a judge had found the petitioner's intention was "to cause havoc to the management of Petromin and its ability to focus on Petromin's business" (DeCotiis at para. 40). That is not the evidence in this case. In my respectful opinion there is no foundation for the inference that 253 is motivated by improper ulterior motives.

[263] This is not to say of course that 253 is not motivated by self-interest. The fact that a party is acting out of self-interest in wanting to prosecute a derivative action is not evidence of bad faith: Richardson Greenshields; and Primex. As noted by Justice Tysoe, as he then was, in Primex:

[34] I have no doubt that the Petitioner is acting out of self-interest in wanting to prosecute the derivative action. The self-interest is to maximize the value of its shares in Northwest by pursuing causes of action which it may have against Mr. Griffiths and the other directors. The Petitioner's self-interest coincides with the interests of Northwest. This does not mean the Petitioner is acting in bad faith: see *Richardson Greenshields v. Kalmacoff*. Anything that benefits a company will indirectly benefit its shareholders by increasing the share value and it is hard to imagine a situation where a shareholder will not have a self-interest in wanting the company to prosecute an action which is in its interests to prosecute.

[Emphasis added.]

[264] That is the situation in this case. The Union Goal Transaction has jeopardized EPL's financial future. Litigation against the directors may be the only way to save the company and the shareholders' investment. 253's self-interest coincides with the interest of EPL.

[265] Good faith is a question of fact to be determined on all of the evidence and the particular circumstances of the case. The applicant's belief in the merits of a proposed claim, if accepted by the court, is a proper factor and cogent evidence of good faith and a prima facie indication that the petitioner is acting with proper motives. Other factors include existing disputes between the parties and alleged ulterior motives. In my respectful opinion, the chambers judge's conclusion on bad faith cannot be sustained. Mr. Hong's belief in the merits and the chambers judge's finding that the proceedings was in the best interest of the company are cogent evidence of good faith and a prima facie indication that the petitioner is acting with proper motives. I find no evidence of ulterior motives. 253 has met the onus of proving it was acting in good faith.

C. Reasonable Notice

[266] EPL argues that 253 did not make reasonable efforts to cause the directors to prosecute the legal proceedings, and that their failure to do so is fatal to their application for leave. The evidence indicates that 253 gave notice on September 23, 2018 that it would bring a derivative action unless the Board took steps to prosecute the proposed action. The Special Committee was formed on September 28. On October 23, 2018, 253's counsel sent a draft notice of civil claim. EPL responded on November 1 seeking an extension of time for the Special Committee to consider the proposed action. 253 was not prepared to wait and commenced the petition the following day. The Special Committee continued its deliberations and on December 17, 2018, it made its report to the Board.

[267] In the circumstances of this case, EPL had five weeks' notice to consider the proposed claim. Further, it considered and rejected the claim long before the hearing of the application. In *IPM*, the petitioners commenced proceedings 5 days after giving notice. Justice Tysoe held that the notice of requirement did not mean that proceedings could not be commenced until the expiry of a reasonable notice. In *IPM*, as in this case, the hearing did not take place until several months after the Board had considered their position and

decided that a proceeding would not be commenced. I find that 253 has met the reasonable notice criteria.

CONCLUSION

- [268] In the result, I find that 253 has met all the criteria for commencing a derivative action in negligence against the named directors and officers. EPL submits that notwithstanding all criteria are met, there remains a residual discretion in the court to deny leave. It submits that the proceeding should be returned to the chambers judge to determine whether in light of our findings that leave should be granted.
- [269] I have some difficulty imagining circumstances in which a court would deny leave after having found that all the criteria are met, including that the action appears to be in the best interest of the company. Assuming such a residual power does exist, it is not necessary to return this matter to the trial court. This Court can and has made such decisions: see *Holdyk*.
- [270] Any residual exercise of discretion must take into account the general principles that govern all derivative actions. As set out above, derivative actions allow shareholders to enforce the rights of a corporation if the directors refuse to do so and provides some degree of accountability and control over the board of directors by allowing shareholders the right to bring an action against the directors if they have breached their duty to the company. The legislation should be given a liberal interpretation in favour of the applicant.
- [271] In this case I have found that 253 has met all the criteria for commencing a derivative action. I find there is no overriding basis to deny leave. I would grant leave to commence a derivative action in negligence in the name of EPL against the named directors and officers of EPL.

"The Honourable Mr. Justice Goepel"

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