Cruelty and Corporate Reputation: An argument for reverse piercing of the corporate veil

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(i) Introduction

In *Québec (Attorney General) v. 9147-0732 Québec inc.*, the Supreme Court of Canada unanimously agreed that s. 12 of the *Canadian Charter of Rights and Freedoms* does not protect corporations from cruel and unusual punishment or treatment. The crux of the matter centered on whether the word “cruel” could apply beyond human beings to corporations. The Court ruled that “cruel” denotes human pain and suffering, either physical or mental. A corporation, as a non-human entity, cannot be subject to human pain or suffering. In other words, the legal fiction of a corporation benefitting from legal personhood does not mean that the corporation can be subject to cruelty. Therefore, the Court ruled that cruel and unusual punishment cannot apply to corporations given their inability to feel human pain or suffering.

We agree with the Supreme Court. In this paper, we make two arguments in relation to the evolution of the law. First, we argue that there may be exceptions where it is appropriate to pierce the corporate veil to ensure just treatment. Secondly, from a philosophical perspective, corporate reputations are the “new new” of corporate governance. For example, scholars argue that corporations should attempt to secure strong reputations in diversity in order to help lower their cost of capital, secure top talent, and grow revenue. While our courts recognize the new role of corporate reputation in governance, in the same breath, the courts say that corporations cannot suffer. As corporations evolve and develop a social conscience recognized in governance, perhaps corporate law needs to evolve as well.

(ii) Background

In this case, at first instance 9147-0732 Québec inc. was found guilty before the Court of Québec for carrying out construction work without a proper licence, contrary to the provisions of the *Building Act*. The Court of Québec imposed a mandatory minimum fine, as mandated under the *Building Act*, against 9147-0732 Québec inc. totalling $30,843. The corporation appealed,

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2 *Québec (Attorney General) v 9147-0732 Québec inc*, 2020 SCC 32 at para 14 [9147-0732 Québec inc].
4 *Building Act*, CQLR 2020, c B-1.1.
5 9147-0732 Québec inc, supra note 1 at para 54.
challenging the mandatory minimum fine as unconstitutional under s. 12 of the Charter, which protects against cruel and unusual punishment.\(^6\)

In ordinary circumstances, a corporation cannot suffer or be subject to treatment amounting to cruel and unusual, as such suffering is a very human notion. Sylvia Rich, for example, argues that it is impossible for a state to criminally punish corporations because “1) suffering is a component of successfully imposed punishment; 2) corporations cannot suffer; 3) ergo, corporations cannot be punished.”\(^7\) Rich writes that part of punishment is to impose suffering, as otherwise there would be no justification to impose “hard treatment” under either a retributive or deterrence theory of punishment, as such punishment applies to individuals.\(^8\) She further argues that though emotional states generally can be imputed onto corporations through those individual members of the corporation, imputation is not possible in the realm of punishment. This is because while the corporation can be fined, and fines may cause suffering to those individuals behind the corporation, “the suffering of individuals who are not named in the punishment cannot be used as evidence that the punishment worked…[it] cannot suffer directly, prior to the involvement of individual agents.”\(^9\) Since Rich argues that punishment must be experienced directly, and cannot flow from others’ suffering, its members’ suffering is not connected to punishing the specific corporation itself for its transgressions.\(^10\) Thus, corporations are not subject to suffering and thus cannot be themselves subject to cruel and unusual punishment based on such suffering.

However, Justices Brown and Rowe, writing for the majority in Quebec (Attorney General) v. 9147-0732, seem to leave the door open when they write that under s. 12 of the Charter, “excessive fines (which a corporation can sustain), without more, are not unconstitutional.”\(^11\) While Justices Brown and Rowe go on to rely on the R. v. Boudreault standard that for s. 12 to be triggered, fines must be incredibly excessive so as to be indecent and “abhorrent or intolerable”, and that each are anchored in human dignity,\(^12\) their language begs the question about whether there could be any circumstance in which excessive fines against a corporation may violate human dignity.

Of course, we agree that corporations cannot be themselves subject to cruel and unusual punishment, because a legal person is a legal fiction - an inanimate entity incapable of suffering itself. However, it is worth exploring specifically whether an excessive fine can ever rise to the level of cruel and unusual punishment to those behind the corporation, who are indeed physical human persons capable of suffering due to cruel and unusual treatment.

This possibility was explored by Justice Bélanger, writing for the majority at the Court of Appeal of Québec in the appellate level case, 9147-0732 Québec inc. c. Directeur des poursuites

\(^6\) Ibid at para 55.
\(^8\) Ibid at 10.
\(^9\) Ibid.
\(^10\) Ibid at 11.
\(^11\) 9147-0732 Québec inc, supra note 1 at para 17 [emphasis added].
\(^12\) Ibid.
criminelles et pénales. Justice Bélanger pointed out that there could be circumstances where the legal person is not affected by the excessive fines in a cruel and unusual way, but the people behind the organization are affected in a cruel and unusual way. Justice Bélanger writes that for physical persons who do not benefit from a distinct legal personality from the corporation when the corporation is fined, but are directly affected by a disproportionately high fine which has been imposed on their organization, the juridical guarantee of s. 12 should apply.\textsuperscript{13}

Drawing upon Rich’s argument, if a corporation is being fined and the people behind the corporation are suffering acutely by a punishment that is not even meant to target them or cause them suffering, then such punishment may be found cruel and unusual against those behind the corporation. The question then becomes whether, and how, cruel and unusual punishment can be attributed to those behind the corporation in such a circumstance, since corporations and the human persons behind it are legally considered separate entities. In other words, a fine levied upon a corporation is not a fine levied on the people behind the corporation, which bars standing to those behind the corporate veil.

The type of situation that Justice Bélanger described, one where the fine was cruel and unusual to the people behind the corporation, was not the specific question put before the Supreme Court in Quebec (Attorney General) v. 9147-0732 Québec inc. The corporation 9147-0732 Québec inc. was fined a relatively modest fine of $30,843, making it extremely unlikely that such a fee would rise to the level of cruel and unusual to the people behind the corporation or rise to the level of harming public interest. However, to build upon Justice Bélanger’s observation, a blanket statement barring s. 12’s applicability to corporations might be ill-advised. Such a bright-line rule would preclude all physical persons, in every circumstance, from the standing required to vindicate their claims under s. 12 when they suffer because of a disproportionately high criminal fine levied on the corporation for which they work. Such situations may include when the corporate veil is pierced to find personal liability. There ought to be some room left for s. 12 to apply to corporations, specifically the people behind them, in certain, narrow circumstances.

(iii) Reverse Piercing of the Corporate Veil

What type of treatment affecting the individuals behind the corporation would rise to such a level as to merit the benefit of s. 12 protection? We propose that s. 12 should apply to smaller, closely held corporations where an excessive fine might have severe consequences for the physical persons behind the corporation. These persons would not have any recourse under such a situation, since after the Supreme Court’s ruling the company would rightly not be able to raise a cruel and unusual punishment argument, and the physical persons are not themselves charged. Each factor results in these physical persons not having proper standing to pursue recourse.

\textsuperscript{13} 9147-0732 Québec inc c Directeur des poursuites criminelles et pénales, 2019 QCCA 373 at para 120, [2019] JQ no 1443.
One might protest, asking how this would work given it is a well-established principle that a corporation is a moral person, legally distinct from those physical persons who are behind the corporate veil. We draw upon our courts’ ability to pierce the corporate veil, and suggest that in certain cases where a punishment levied on a corporation might as well be a punishment levied on the people behind the corporation - because the corporation and the people behind it are so tightly entwined in terms of size, management, and funding - then courts should pierce the corporate veil to determine whether the punishment was cruel and unusual to those behind the corporation. As Justice Carole J. Brown wrote in Choc v. Hudbay Minerals Inc.,

Ontario courts have recognized three circumstances in which separate legal personality can be disregarded and the corporate veil can be pierced: (a) where the corporation is ‘completely dominated and controlled and being used as a shield for fraudulent or improper conduct; ...(b) where the corporation has acted as the authorized agent of its controllers, corporate or human... and (c) where a statute or contract requires it.¹⁴

In Yaiguaje v. Chevron Corporation,¹⁵ the Ontario Court of Appeal affirmed that corporate separateness is the governing rule subject to the exception where the corporate form is being abused to the point that the corporation is not a truly separate corporation and is being used to facilitate fraudulent or improper conduct. The Supreme Court of Canada denied leave to appeal in Chevron.¹⁶

Nichols and Khimji conducted empirical analysis of the veil-piercing cases in an article entitled “Piercing the Corporate Veil in the Canadian Common Law Courts: An Empirical Study”.¹⁷ The article divides the veil-piercing cases into types and then analyses the results in terms of relative success. Important for white collar crime and regulatory violations is the empirical finding that there was a statistically significant relationship between the identity of the party seeking to pierce the corporate veil and whether the veil was actually pierced. Government entities were the most successful with their claims (with a success rate of 45.76%) whereas shareholder, corporation, and related corporation piercing claims were the least successful.

If it is appropriate to pierce the corporate veil to do justice on behalf of a government regulator, the mirror situation should also be considered by way of a reverse piercing argument. Imagine, for example, a large corporation which has created shell companies to hide assets offshore to evade taxes, hide incoming funds, pay bribes, or for other purposes contrary to criminal or regulatory law. If the corporation is being used to facilitate fraudulent or improper conduct, the Chevron test gives regulators the ability to pierce the corporate veil in order to associate shell companies with the parent company.

¹⁴ Choc v Hudbay Minerals, 2013 ONSC 1414 at para 45, 116 OR (3d) 674 [Hudbay].
¹⁵ Yaiguaje v. Chevron Corporation, 2018 ONCA 472, 423 DLR (4th) 68 [Yaiguaje].
Now, imagine a family-run construction business comprised of three people. The family has poured all their life savings into ensuring the business gets off the ground and becomes viable. As newcomers to the construction and business worlds, the family members are relatively unsophisticated businesspeople. The company becomes caught up in a quasi-criminal or regulatory offense and gets fined $1,000,000, a fine which represents the loss of life savings that each family member poured into the corporation for its launch.

If there is a bright-line rule that bars the physical persons behind corporations from bringing a claim under s. 12 for this fine levied against the corporation, then these physical persons may not have an ability to challenge the fine in court - despite the fact that the fine may be disproportionate to the regulatory offense committed and may in fact rise to the level of cruel and unusual punishment against those few persons who closely hold the family-run corporation. Unlike what the Supreme Court asserts, a corporation cannot always sustain such excessive fines when they are smaller and closely held - indeed, the people behind a corporation sometimes certainly cannot.

This situation is not a theoretical one; similar cases have been contemplated by courts in Canada, which have exposed the complexity of corporate sentencing when the corporation, as a legal fiction, is treated separately from the people behind it. In the recent case of R. v. D&J Insley & Sons Contracting Ltd., Justice Nick Devlin reviewed a trial judge’s sentencing decision in a case where a family-held and family-run lumber company, after a freak accident and for the first time in a century of operation, found itself guilty of charges under the Occupational Health & Safety Act. The sentencing judge granted the Crown’s recommended sentence of a $105,000 fine (which was understood as a symbolic fine the corporation could not afford to pay), victim fine surcharge, and a 12-month probation order. The trial judge asserted that she was sentencing D&J Insley, the company, and not Mr. Insley, the physical person and the CEO of the corporation at the time of the accident. However, the trial judge appointed Mr. Insley as the representative of the corporation mandated to carry out the probationary terms sentenced; in doing so, she recognized that the effect “is akin to piercing the corporate veil”, while making Mr. Insley personally liable for the sentence imposed on the company.

Justice Devlin, on his review of the trial judge’s decision, writes that “this is a classic piercing of the corporate veil...functionally bind[ing] Mr. Insley to probation, despite him never having been charged, tried, or convicted.”

This case is a good illustration of our argument: D&J Insley was a closely held corporation, and the trial judge effectively pierced the corporate veil to make Mr. Insley responsible, in his personal capacity, for the probation penalty given to the corporation. While Justice Devlin overturns the decision in this case, he also finds that a trial judge, under common law, may

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18 9147-0732 Québec inc, supra note 1 at para 17.
21 Ibid at para 16.
22 Ibid at para 18.
23 Ibid at para 28 [emphasis added].
pierce the corporate veil when determining a sentence or a regulatory penalty. This leaves open the possibility that the corporate veil may be pierced in certain situations which mirror Mr. Insley’s situation. If there is a circumstance where Mr. Insley or someone like him could be personally responsible for a regulatory penalty imposed on a corporation, when they themselves have never been charged or stood trial, should he or she not have standing to challenge that penalty as cruel and unusual as it applies to him or her?

Allowing a reverse-pierce would allow the physical persons to go to court, so that the persons can argue that even though the business operates in a corporate form, the composition is really only the three people who cannot sustain such a disproportionate fine. This reverse-pierce of the corporate veil would allow the physical persons behind the corporation to have standing to make the argument that the fine is cruel and unusual treatment for them, the physical persons, even as the fine was directed towards the corporation.

A counter argument to explore is that economic harm resulting from punishment never rises to the level of cruel and unusual. Yet, economic harm can rise to the level of cruel and unusual punishment to an individual. If a punishment is so disproportionate that it rises to the level of destroying a person’s life savings such that they are literally destitute, that punishment arguably has vast harmful effects on that person’s mental health, physical health, and family well-being - thus, extending to levy punishment on persons past the offending individual.

The Supreme Court seems to agree with this line of reasoning: in Boudreault, the Supreme Court specified that if a surcharge or fine could be rightly classified as “punishment,” or that the state action “(1) . . . is a consequence of conviction that forms part of the arsenal of sanctions to which an accused may be liable in respect of a particular offence, and either (2) . . . is imposed in furtherance of the purpose and principles of sentencing, or (3) . . . has a significant impact on an offender’s liberty or security interests”;24 and that the punishment rose to the level of being abhorrent or intolerable or offensive to societal standards of decency, then economic sanctions may rise to the level of cruel and unusual.25 The Court is careful to specify that the “cruel and unusual” element is a high bar to meet. If the person can show that the punishment is disproportionate such that it wipes out their savings in response to a relatively innocuous crime, then this punishment may be found cruel and unusual as applied to that person.

Quebec (Attorney General) v. 9147-0732 should be interpreted as leaving the door open to harsh economic treatment rising to the level of triggering s. 12 protection. While the Court does specify that s. 12 does not apply to corporations and thus cannot protect corporations from high economic penalties,26 the Court also draws on Boudreault to clarify that surcharge punishments can violate s. 12 of the Charter when that penalty causes certain harms to

25 Ibid at para 45.
26 9147-0732 Québec inc, supra note 1 at para 67.
individuals. Specifically, *Boudreault* identifies four economic harms which could trigger s. 12 protections, including “disproportionate financial consequences suffered by the indigent; threat of detention and/or imprisonment; threat of provincial collections efforts; and *de facto* indefinite criminal sanctions.” In the situation of penalties levied against small and closely held corporations, which stand to negatively affect those individuals behind the corporation, it is possible that a penalty which depletes an individual’s savings could rise to the level of disproportionate financial consequences suffered by an indigent person, and thus attract s. 12 protection.

(iv) **Corporate Governance and Reputation**

Corporate reputations are the “new new” of corporate governance. While courts recognize the new role of corporate reputation in governance, in the same breath courts say that corporations cannot suffer. As corporations evolve and develop a social conscience recognized in governance, perhaps corporate sentencing law needs to evolve as well.

Earlier we cited Brummer and Strine’s opinion that “it is plausible that a third business case for diversity—that of reputational enhancement in light of an increasingly diverse world—is most compelling for corporate directors and managers. According to this view, many investors, customers, and employees value diversity greatly, so much so that it informs their behaviors. Corporations should thus attempt to secure strong reputations in diversity in order to help lower their cost of capital, secure top talent, and grow revenue.”

We share this view as applied to Canadian jurisprudence.

We propose that the Supreme Court in *Peoples Department Stores Inc. (Trustee of) v. Wise* was simply recognizing the new reality that the best interests of the corporation must take into account reputational effects and the costs of litigation. The Supreme Court decision of *BCE Inc. v. 1976 Debentureholders* confirmed that interpretation of *Peoples*. For that reason, although directors *must* consider the best interests of the corporation, it may also be appropriate, although *not mandatory*, to consider the impact of corporate decisions on shareholders or particular groups of stakeholders such as employees, suppliers, creditors, consumers, governments, and the environment.

This is not a new paradigm of governance, but rather a recognition within the governance paradigm of the importance of corporate reputation to the long-term best interests of the corporation. There are multiple examples of reputational harm to companies ensnared in corporate wrongdoing. Enron, VW, Wells Fargo, Loblaws, Lac-Megantic, British Petroleum, Boeing 737 Max 8, Facebook. The list goes on.

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30 Archibald & Jull, *supra* note 3, Chapter 4 “Governance of the Corporation”.
In recent business history, especially since the global financial crisis of the 2000s, there have been cases of corporate decline and failure. The cases of Enron and Worldcom, for example, failed due to factors ranging from sheer lack of managerial or leadership competence to poor management and other issues. Scholars have drawn a link between a lack of emotional intelligence and corporate decline:

Some of these issues hinge squarely on critical lack of emotional intelligence with regard to individuals’ behavior and performance detrimental to corporate excellence. In this changing world, characterized by advancements in information and communications technology (ICT), marketing competitiveness, and narrow profit margins, elements of trustworthiness, passion, empathy, discipline, vision and service-orientation are skills seriously lacking in some people put in positions of corporate responsibility which often leaves the doors and windows open for corporate decline.\(^{31}\)

The recognition of corporate reputation in some ways paints a picture of corporations as almost human. Indeed, the advertising of many companies draws on human like comparisons to evoke a bonding process with consumers. Sixteen years ago, Spike Jonze directed a quirky little ad for Ikea that quickly became a classic of modern advertising. “Lamp 1” played on your heartstrings, while amping up the melodrama of an old lamp being tossed onto the street by its owner. By the end of the spot, you actually felt sorry for the lamp—until Swedish actor Jonas Fornander wanders onscreen and admonishes the viewer for being so easily manipulated.

"Many of you feel bad for this lamp,” he says in one of the great rug-pulls in ad history. “That is because you’re crazy. It has no feelings, and the new one is much better.”\(^{32}\) The genius was in how it so quickly was able to establish an emotional connection between the viewer and a lamp, then hilariously douse it all, with actor Jonas Fornander dropping a truth bomb.\(^{33}\)

Ikea Canada decided to resurrect the story for a sequel, while putting a modern twist on the sad little lamp’s end. Made with agency Rethink Canada and directed by Mark Zibert, “Lamp 2” picks up where the original left off, but instead of the landfill, we get a serving of responsible consumerism when a little girl finds another use for our hero. Earnest optimism replaces the original wisecrack, but we still get Fornander dropping back in, this time to remind us that it is not crazy to reuse things. The change in tone and messaging reflects how our attitudes and behavior have evolved over the last decade and a half. Responsible consumerism has gone far beyond companies such as Patagonia to major corporations like P&amp;G, Unilever, and Ikea which have begun talking more about waste. This focus on smart consumption is moving from the


\(^{32}\) Tim Nudd, “Ikea’s Excellent Sequel to ‘Lamp’ Flips the Script on an Ad That Didn’t Age Well” (10 September 2018), online: Muse by Clio <https://musebycl.io/advertising/ikea-made-sequel-lamp-flipping-script-ad-didnt-age-well>.

fringes to a more significant part of how brands and people think about their ongoing relationships with. All that, and the little red lamp finally had a happy ending.34

Corporate image advertising is sometimes used to counter negative perceptions, but also to bolster a company’s existing positive image. For example, British Petroleum (BP) was found to use corporate image advertising to make the case that the company operates in a safe way. Such ads counter the horrendously negative publicity received by the company after the 2010 Gulf of Mexico oil spill.35

If a corporation can have emotional intelligence, and if corporate images can evoke powerful emotional reactions, is it not a logical extension that those same corporations could “suffer” from a cruel and unusual sentence that would damage that very corporate reputation? This is an issue that goes far beyond the narrow constitutional argument about whether a corporation can argue that it has been subjected to cruel and unusual punishment. We need to start thinking about new corporate roles, and maybe even new corporate paradigms.

The model enshrined in s. 122(1.1) of the Canada Business Corporations Act36 does not create voting or other rights in the various stakeholders identified in BCE. Some reformers have suggested that this corporate democratic model ought to be followed. U.S. Senator Elizabeth Warren identified other stakeholders, including consumers, workers, creditors, neighbors, students and introduced legislation that would empower corporate employees to elect at least 40% of the directors on their corporation’s board.37 Others conceptualize the corporation as a separate legal entity that itself serves as a nexus of contracts.38 It is time to start an academic and political debate about new models of governance.

(v) Conclusion

In this paper, we have explored the scope of how s. 12 of the Charter, protecting against cruel and unusual punishment, may apply to corporations in certain narrow circumstances. Our analysis follows recent jurisprudence from the Supreme Court of Canada which specified that corporations cannot benefit from s. 12 protection because corporations cannot suffer. Only humans are capable of suffering. We agree with the Supreme Court that, under the current legal paradigm, corporations are incapable of suffering; but we also argue that humans behind small and closely held corporations are capable of suffering due to disproportionate corporate criminal or regulatory penalties. To deny humans standing under s. 12 in such cases would be unjust.

34 Ibid.
35 Karen A Loveland, Katherine Taken Smith & Murphy Smith, “An Examination of Corporate Image Advertising in the Oil and Gas Industry” (9 July 2019). Oil, Gas & Energy Quarterly, online: https://ssrn.com/abstract=3415750.
36 RSC 1985, c. C-44.
To this end, we have argued that in certain exceptional situations, courts should pierce the corporate veil to ensure that criminal or regulatory sanctions against corporations are not disproportionate in their effects to those behind the corporation. We have argued that this is just from a philosophical perspective. Since Peoples and BCE, corporate reputations have emerged as the “new new” of corporate governance. Society now expects more social awareness from our corporations, and, indeed, imputes human responsibility on corporations towards a variety of stakeholders. Since punishment stands to affect corporate reputation and thus potentially the livelihood of those behind the corporate veil, corporations (and specifically, those behind them in closely held corporations) are capable of suffering due to corporate criminal and regulatory sanctions.