10. Directors' and Officers' Liability

Directors' Duties and Liabilities

This chapter provides a brief summary overview of the statutory and common law duties of directors and officers of corporations incorporated under the federal *Canada Business Corporations Act* (CBCA). Although the liability of corporate directors and officers varies with the jurisdiction of incorporation, the statutory duties found in provincial legislation are generally similar to those set out in the CBCA.

Duty of Care and Duty of Loyalty

Under the CBCA, directors and officers have two principal duties: a duty of care and a fiduciary duty of loyalty.

The duty of care imposed by CBCA requires that each director and officer of a corporation, in exercising their powers and discharging their duties, must exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. The duty of care requires that directors and officers make sufficient inquiries to inform themselves and consider all material information available to them prior to acting.

The CBCA also imposes a fiduciary duty of loyalty that directors and officers act honestly and in good faith with a view to the best interests of the corporation. Under the fiduciary duty of loyalty, directors and officers are to act impartially and place the interests of the corporation first, not allowing their decisions to be tainted by self-interest or self-dealing. The duty requires directors and officers to avoid conflicts between the interests of the corporation and any opposing interests, including their own.

The Supreme Court of Canada has ruled that the fiduciary duty is owed at all times to the corporation. The Court has also stated that acting in the best interests of the corporation is not synonymous with acting in the best interests of shareholders:

> "The fiduciary duty of the directors to the corporation is a broad, contextual concept. It is not confined to short-term profit or share value. Where the corporation is an ongoing concern, it looks to the long-term interests of the corporation. The content of this duty varies with the situation at hand. [...]
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> "In considering what is in the best interests of the corporation, directors may look to the interests of, [among other things], shareholders, employees, creditors, consumers, governments and the environment to inform their decisions. [...]
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> "There is no principle that one set of interests—for example the interests of shareholders—should prevail over another set of interests. Everything depends on the particular situation faced by the directors and whether, having regard to that situation, they exercised business judgment in a responsible way." *(BCE v 1976 Debentureholders, 2008 SCC 69)*

The *BCE* decision has, however, created ambiguity regarding the nature and extent of such duties. The Court held that where conflicts arise between the interests of the corporation and its stakeholders, "...it falls to the directors to resolve them in accordance with their fiduciary duty to act in the best interests of the corporation, viewed as a good corporate citizen." The Court did not provide guidance as to how to give effect to this concept, but the reference to "good corporate citizen" suggests some degree of accountability to stakeholders.

On June 21, 2019, Bill C-97, *An Act to implement certain provisions of the budget tabled in Parliament on March 19, 2019* and other measures, received Royal Assent. The Bill, among other things, codified elements of the BCE decision and amended the CBCA to provided that, when acting with a view to the best interests of the corporation, one may consider, but are not limited to, the interests of shareholders, employees, retirees and pensioners, creditors, consumers, governments, the environment and the long-term interests of the corporation.

Required Disclosure of Conflicts of Interest

The CBCA further attempts to minimize conflicts of interest between directors and corporations on which boards they serve by requiring directors to disclose such conflicts to the corporation. Under the CBCA, a director who discloses a conflict of interest must refrain from voting on any resolution to approve the contract or transaction giving rise to such conflict of interest, subject to certain exceptions. Prudence may also dictate, and some provincial statutes require, that such directors also not attend any part of a meeting at which such contracts or transactions are discussed.

The Oppression Remedy and Derivative Actions

While directors do not have a fiduciary duty to stakeholders, shareholders and other interested parties have the ability under Canadian corporate statutes to seek redress against a corporation or its directors under the oppression remedy. This statutory right is available to a complainant in circumstances where their reasonable expectations were violated by conduct that was oppressive to, unfairly prejudicial to, or unfairly disregarded the claimant's interest. The Supreme Court of Canada has also recently affirmed that directors can be held personally liable under the oppression remedy where the impugned conduct is attributable to directors because of their action or inaction.

Additionally, shareholders may commence a derivative action on behalf of the corporation if directors breach their fiduciary duty to the corporation or engage in a self-interested transaction. These provisions act as a restraint on directors' actions and help to control directors' opportunism.

Business Judgment Rule

Under the business judgment rule, if a board acts in good faith and on an informed basis, it is afforded wide latitude under the shield of the business judgment rule and is presumed to have acted in the best interests of the corporation and its shareholders. While a high degree of diligence is required, courts do not require perfection. Where a director's decision is a reasonable one in light of all the circumstances about which the director knew or ought to have known, courts will not interfere with that decision.

The court's inquiry will generally focus on whether the directors applied an appropriate degree of prudence and diligence in reaching their decisions. So long as a decision is within the range of reasonableness, a court will not substitute its opinion for that of the board, regardless of what subsequent events may have transpired. The business judgment rule reflects the reality that directors are generally better suited than courts to determine what is in a corporation's best interest. However, the business judgment rule is not a complete defence – business judgment must actually be shown in order for directors to be able to rely on it.

Limiting Liability

The CBCA provides that the corporation may indemnify directors and officers against liabilities incurred in the course of their duties and may purchase and maintain insurance against any liability incurred by the individual in their capacity as a director or officer. Provided that the director or officer has acted honestly and in good faith with a view to the best interests of the corporation, such indemnity is generally available.

Although there is no legal obligation to establish a special committee, except in certain limited circumstances, the creation of a special committee is a way to protect directors from liability by ensuring that a board's decision-making process is free from the influence of a director who may have a conflicting interest with that of the corporation. Establishing a special committee will protect the board from allegations of wrongdoing and, where the board acts on the recommendation of a special committee, the decision should be respected under the business judgment rule, provided the special committee acted independently and in good faith.

A director may also limit their liability by having their dissent entered into the minutes in respect of a decision or, ultimately, by resigning from the board. The CBCA provides a right to resigning directors to submit to the corporation a written statement giving reasons for resigning, and corporations are in turn required to circulate such statement to shareholders. Resignation will not absolve a director from liabilities incurred while serving as a director.