

# Memorandum

**From:** Paul Barbeau  
**Date:** March 3, 2000  
**Re:** Director's Duties Pursuant to the British Columbia *Company Act*

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## DUTIES AND OBLIGATIONS OF DIRECTORS

Directors are responsible for managing the affairs of a corporation, but the complexity of the tasks involved in managing a corporation may require the delegation of certain management functions to the officers; however, the directors may not delegate all of the authority of management of the corporation to the officers. At a minimum, the directors must retain the power to recall the delegated powers.

Conceptually, the power to manage the company resides in the members of that company, but historically the power to manage was delegated to the directors. Pursuant to the current provisions of the *British Columbia Company Act* (the "Act"), section 117(1) provides that:

"Subject to this Act in the Articles of the Company, the directors must manage or supervise the management of the affairs of the business."

Notwithstanding this section of the Act, the directors inherent right to manage the affairs of the company, is derived from the underlying rights of the members of the company, which in turn gives rise to the fiduciary duty imposed on the directors to act in the best interests of the members.

The fiduciary duties of directors at common law have been generally found to include the following:

- (a) Directors are strictly liable to account for conflict of interest situations, making secret profits or taking corporate opportunities;
- (b) Directors must exercise powers only for the purposes for which they were intended and if powers are exceeded only the shareholders can ratify such conduct;
- (c) Directors fiduciary duties continue even though a director resigns or the corporation is struck from the register of companies; and

- (d) Directors' fiduciary duties to act honestly and fairly are extended in some circumstances to shareholders and fellow directors.

#### **A. General Statement of Duty of Care**

Section 118(1) of the Act states that every director of a company, in exercising in director's powers and performing the director's functions, must:

- (a) Act honestly and in good faith and in the best interest of the company; and
- (b) Exercise the care, diligence and skill of a reasonably prudent person.

(Note: This duty of care is imposed on officers of the company, by section 135.)

The case law has expressed the concept of directors acting in the best interests of the company as follows:

“If today directors of a company were to consider the interests of its employees, no one would argue that in doing so they were not acting in the best interests of the company itself. Similarly, if the directors were to consider the consequences to the community on any policy that the company intended to pursue and were deflected in their commitment to that policy as a result, it could not be said that they had not considered bona fide the interests of the shareholders.”<sup>1</sup>

Further, the courts recognize that directors must be guided by what amounts to a business judgement rule. Directors, in the absence of self dealing or fraud, are presumed to have acted properly in making a business decision if they acted on an informed basis, in good faith, and in an honest belief that the actions taken were in the best interests of the company.

In determining what constitutes negligence on the part of a director in exercising his duties and obligation established case law provides the following general guidelines:

- (a) Directors are not liable for mere errors of judgement;
- (b) Directors are not bound to give continuous attention to the affairs of the company;
- (c) Directors have duties of an intermittent nature to be performed at periodic board and committee meetings;
- (d) Directors need not attend all meetings, although they ought to attend whenever reasonable to do so;

- (e) Directors are justified in entrusting certain matters of business to officers of the corporation; and
- (f) Directors are justified, in the absence of grounds for suspicion, in trusting that officers of the company will perform in their duties honestly.<sup>2</sup>

However, in deciding whether the director has acted negligently, the courts have often focused on the director as an individual, judging him in relation to the type of business and company involved and having regard to his personal background and ability.

### **B. Conflict of Interest**

Section 123 of the Act requires every director who holds any office or possesses any property that either directly or indirectly might create a conflict of interest with his duty as a director of the company to declare the nature and extent of the conflict at a directors' meeting.

Further, section 120 of the Act requires directors to disclose any interest in a proposed contract or transaction with the company. A general written notice by a director to the other directors to the effect that he is a member, director or officer of a specified corporate, or that he is a partner in, or owner of, a specified firm, and that he has an interest in a specified corporation or firm, is sufficient disclosure to comply with the Act.

This provision has been held to absolve a director from liability and that the Act replace the common law in this regard.<sup>3</sup>

Section 122 provides that a contract or transaction without meeting the disclosure requirements does not invalidate the contract or transaction, but the courts may grant relief, including injunctive relief, to the company or any interested person, with respect to the proposed or existing contract or transaction.

Section 121 allows the members of the company to ratify conflicts of interest but approval must be by special resolution and even then it may only ratify if the contract or transaction in issue was reasonable and fair to the company at the time into which it was entered.

### **C. Further Duties Imposed on Directors under the Act**

In addition to the broad duties imposed on the directors to act in the best interest of the members, the following is a partial listing of the further duties, which are specifically imposed on directors by the Act:

- (a) Section 40(1) provides that the directors may change the location of the registered and records office by passing a Resolution and filing the required Notice with the Registrar of Companies;

- (b) Section 171(2) requires that the accounting records of a company shall be kept at a place determined by the directors;
- (c) Section 126(1) provides that the director shall not sell, lease, or otherwise dispose of the whole or substantially the whole of the undertaking of the company unless they have the approval of the members, given by a Special Resolution;
- (d) Section 73 provides that the directors shall be entitled to set, in advance, a date as the "record date"; and,
- (e) Section 41 sets out the provisions for the allotment of treasury shares and provides that the directors of every company, before allotting treasury shares, must offer those shares proportionally to its members.

In each of the above instances, it is only the directors who may exercise the powers involved. Furthermore, in the absence of articles of the company to the contrary, each of the powers will lie solely within the scope of the director's duties.

#### **D. Miscellaneous Liabilities under the Act**

Further miscellaneous director's liabilities include the following:

- (a) If at any time a company carries on business for more than 6 months without a member, every director and officer of the company during that time is jointly and severally liable for debts contracted (N.B. Section 14 of the Act);
- (b) If a company issues shares which are not fully paid, the directors are jointly and severally liable to compensate the company and any member for any loss, damage and costs sustained by the company or the member by reason of the allotment or issue of any share in violation of the relevant sections (N.B. Sections 43 and 45 of the Act);
- (c) If the company fails to deliver a share certificate to a member in the time and manner provided in sections 48 and 49 of the Act, the director or officer responsible for this default may be liable for the members' cost of an application to the court to force delivery;
- (d) a director or officer who knowingly permits the company not to display or use its name at its place of business or on all notices, contracts, invoices, bills of exchange and other documents, or to issue any instrument that does

not display its name, can be held liable for damages (N.B. section 106 of the Act);

- (e) Section 290, which sets out the powers given to the court on a winding-up, is also relevant to a consideration of the liabilities of a director. That section provides that when a company is being wound up, the court may inquire into the past conduct of any past or present director, officer, receiver, receiver-manager, liquidator or member of the company or any promoter of the company regarding misappropriation of company funds or breach of trust and may compel restitution or compensation;
- (f) Where a general meeting is called by requisitionists, every director or officer who authorized, permitted or acquiesced in the failure of the company to give notice of the meeting is liable to pay rateably to the company the amount paid by the company to reimburse the requisitionists (N.B. section 147(5)(b) of the Act);
- (g) If a company or extraprovincial company has failed to file any document required to be filed with the Registrar and the Registrar has, after due notice, ordered the filing of the document, any person, director or officer of the company or extraprovincial company may be directed to pay the costs of and incidental to the application (N.B. section 339 of the Act); and,
- (h) Section 342 provides that it is an offence, punishable by a fine not exceeding \$2,000.00 or a term of imprisonment not exceeding one year, or both, for any person to make or assist in making a statement in any document required to be made by or for the purposes of the Act or the regulations that, at the time and in the light of the circumstances under which it was made, is false or misleading in respect of any material fact, or that omits to state any material fact., the omission of which makes the statement false or misleading.

## **E. Liability of Directors under Other Statutes**

Set out below is only a partial list of other statutes in which a director may be found to be liable.

### **1. Income Tax Act**

Directors are strictly liable jointly and severally under the Income tax Act for failure to withhold on behalf of employees' income tax and employment insurance and Canada pension plan contributions. Directors may assert a due diligence defense that they exercised appropriate care, made appropriate investigations or otherwise acted with due diligence.

## **2. Employment Standards Act**

Directors are absolutely liable for up to two months outstanding wages of the company's employees. Accordingly, there is no due diligence defense available to directors.

## **3. Builders Lien Act**

If directors knowingly assent to or acquiesce in an appropriation or conversion of trusts funds set aside under the *Builders Lien Act* they are liable for the offence in addition to the company.

## **4. Bills of Exchange Act**

Directors may be held liable for any bills containing their signature if the director fails to add words to his signature indicating that he is signing in the capacity of an agent or representative of the company.

## **5. Criminal Code**

Section 21 of the Code sets criminal liability for persons who do or omit to do anything for the purpose of aiding or abetting any person to commit an offence under the Code. Directors may be subject to this provision but there must be an element of intention in a director's act or omission constituting aiding and abetting a person to commit an offence. It appears that it is not enough that the act or omission of a director simply had the effect of doing so.

## **F. Directors Avoiding Liability**

### **1. Dissent**

Under section 127 of the Act a director may invoke a procedure whereby he registers his dissent from a decision of the board of directors. It should be noted that failure to register a dissent a director is deemed to have consented to the breaches of certain provisions of the Act and the directors are joint and severally liable to make good any loss or damage suffered by the company.

### **2. Exoneration**

Section 127 of the Act sets out that directors are not liable for the losses or damages with respect to duties imposed under the Act if they can prove:

- (a) They did not know or could not reasonably know that the act authorized by the resolution was contrary to the Act;
- (b) They relied and acted in good faith on statements of fact represented to them by an officer of the company to be correct or on statements contained in a written report of an auditor of the company.

Section 202 of the Act sets out that the court may grant relief to directors of the company from any default or breach of duty pursuant to the Act, where they acted honestly and reasonably and where they ought fairly to be excused from the default or breach. However, the courts are in general reluctant to employ this section and it appears to be restricted in its application by case law.

### **3. Indemnification**

Pursuant to section 119 directors can not be indemnified in advance against any potential claims the company may have against a director for negligence, default, breach of duty or breach of trust.

However under section 128 of the Act the company, with the courts approval, may indemnify directors for all costs and expenses to settle an action or satisfy a civil, criminal or administrative action if:

- (a) the director acted honestly and in good faith with a view to the best interests of the company of which the person is a director; and
- (b) in the case of a criminal or administrative action or proceeding, the director had reasonable grounds for believing that his conduct was lawful.

### **4. Insurance**

Section 128 of the Act sets out that a company may purchase and maintain insurance for the benefit of a person referred to in this section against any liability incurred by him as a director. There appear to be no limits as to the extent of liabilities that may be insured in British Columbia.

### **5. Resignation**

Resignation by a director has little value for responsibility for events that occurred while the director remained in his position. Its only benefit is to limit future liabilities.

A resignation must be in writing and is effective at the time it is delivered to the registered office of the company or at a time specified in the resignation, which ever is later.

### **ENDNOTES:**

1. *Teck Corporation Ltd. v. Millar* (1972) 33 DLR (3D) 288 (BCSC);

2. *Re City Equitable Fire Insurance Company Limited* [1925] 40 ChD 41; and
3. *Rhyolite Resources Inc. v CanQuest Resource Corp* [1990] BLR 275 (BCSC).

## SOURCES

1. British Columbia Corporation Manual  
(updated to August 1998)
2. Directors Liability in Canada  
(updated to January 1999)
3. Continuing Legal Education – 1990, 1996, 1999  
Directors Liability

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