

THE ADVISOR

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A SEAT ON THE BOARD OF DIRECTORS: NOT AS CUSHY AS IT SOUNDS



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Many business people are familiar with the corporate director role and the powers granted to someone in the role. What is not always so commonly understood are the obligations and personal liability that accompany the role.

'Personal liability' is a serious risk, and one that all directors should understand. Personal liability means that your personal assets – not corporate assets – may be used to satisfy a judgment. While this is in opposition to the concept of limited liability associated with the corporate structure, our laws provide that directors are personally accountable for some corporate wrongs.

Liability for wrongs of a corporation

The most common personal risk that directors face relate to employees of the corporation. Directors can be held personally liable for failure to deduct and remit source deductions, *Employment Insurance Act* insurance premiums, and Canadian Pension Plan payments. Directors can also be held personally liable for unpaid employee wages (under the *Employment Standards Code*).

Another class of personal risk that directors face concerns the corporation's engagements with third parties. Under the *Excise Tax Act*, directors face personal liability for failing to collect and remit Goods and Services Tax. The *Bankruptcy and Insolvency Act* places a personal obligation on directors to not pay dividends or approve a redemption of shares in the 12 months prior to a bankruptcy, as directors should know that their company is in trouble and must not make payments to related entities in priority to creditors. Directors can also be held personally liable under the *Canadian Environmental Protection Act* for environmental contamination by a corporation.

Importantly, most of the legislation imposes 'joint and several' liability on the directors of

the corporation. Therefore, if there are multiple directors and liability is established, there is no requirement to impose liability equally amongst directors: a judgement can be satisfied in its entirety from the personal assets of the director with the deepest pockets, irrespective of which director was to blame.

Liability for wrongs to a corporation

The foregoing is only a brief overview of some of the laws that impose personal liability on directors for the wrongs of a corporation, but there is a whole other class of liability that imposes personal liability for a director's wrongs to a corporation. A director must be cautious when conducting his or her personal or other business interests, as he or she can incur liability for any acts against the best interests of the corporation. The recent case of *681210 Alberta Ltd v. Hunter*, 2011 ABQB 320, is a cautionary tale for all directors that have other business interests.

The issue in *681210 Alberta Ltd v. Hunter* was misappropriation of a corporate opportunity. The director, Hunter, formed the plaintiff company (681210 Alberta Ltd.), of which he was the sole director, and took on investors for the purpose of setting up and operating a movie theatre in Okotoks, Alberta. After establishing this business, Hunter came across another movie theatre opportunity in Calgary and incorporated a new company to operate this new business to the exclusion of the shareholders of 681210 Alberta Ltd.. After a number of years of running the Calgary movie theatre, the shareholders of 681210 Alberta Ltd. concluded that the Calgary movie theatre was an opportunity that came to Hunter and was a success due to Hunter's involvement in the Okotoks project. In considering whether Hunter had breached his fiduciary duty to 681210 Alberta Ltd to ensure that his personal interests did not conflict with those of the corporation, the Court considered that the Calgary movie theatre opportunity was in line with the general business pursuits of 681210 Alberta

Ltd. and that Hunter's success in and knowledge of the Calgary opportunity was due to his relationship with 681210 Alberta Ltd.. The Court held that Hunter had breached his fiduciary duty to 681210 Alberta Ltd., and judgement in the amount of \$2,774,073 was ordered against Hunter and the new company to account for the profits.

Practical suggestions

The director role is not a ceremonial position.

- If you agree to act as a director you should be prepared to acquaint yourself with the activities of the corporation. Specifically, review the corporation's financial records to ensure that government remittances are being made on time and in full.
- Secondly, sound financial management is the responsibility of the directors, and can reduce the risk of liability in the case of bankruptcy.
- Thirdly, certain businesses hold greater risk of director liability. Companies with numerous employees and those that conduct environmentally sensitive activities hold more risk. As part of the agreement to act as director, you should consider requiring the corporation to purchase directors' insurance when the business activities pose risk.
- Fourthly, be cautious in conducting personal or other business activities. Knowledge obtained while acting as a director cannot be used for personal gain to the detriment of the corporation. As the noted case illustrates, directors need to be careful where personal business interests have the potential to compete with the interests of the corporation they are under a duty to protect.
- Finally, understand your obligations and your specific risks. If you are a director or considering accepting such an appointment, our Business Law Group is able to provide you with an understanding of your duties and offer practical advice as to how to reduce risk to your personal resources. ▲

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