

## Before You Say Yes, Understand The Risk

Family members must understand the responsibilities and risks associated with becoming directors of a family-owned corporation.

### Know What You're Getting Into

Incorporation of an owner-managed business requires shareholders to elect a board of directors to assist in managing the affairs of the company. The owner-manager will almost certainly be elected, as well as a member of their family. In many instances family members allow themselves to be elected director simply because they want to help keep family control of the business. Unfortunately, all too often these

family members have little business experience and only a minimal understanding of the onerous responsibility and contingent risk that the position of director carries with it.

Excerpts from the *Canada Business Corporations Act* (R.S.C. 1985, c. C-44) are typical of regulations in the provincial Corporations Acts, in that they indicate the overall substance of responsibility of a director:

102.(1) Subject to any unanimous share holder agreement, the directors shall manage, or supervise the management of, the business and affairs of a corporation.

### Duty of care of directors and officers

122.(1) Every director and officer of a corporation in exercising their powers and discharging their duties shall:

- (a) act honestly and in good faith with a view to the best interests of the corporation; and
- (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances

### Duty to comply

(2) Every director and officer of a corporation shall comply with this Act, the regulations, articles, by-laws and any unanimous shareholder agreement.

### No exculpation

(3) Subject to subsection 146(5), no provision in a contract, the articles, the by-laws or a resolution relieves a director or officer from the duty to act in accordance with this Act or the regulations or relieves them from liability for a breach thereof.

### Be Aware of Personal Liability

Perhaps the most important area for inexperienced directors of an owner-managed business is Section 122. For instance, directors may be held accountable if they fail to ensure that a corporation maintains proper books and records or fails to file required forms or make payment to regulatory authorities (all of which would be done by a reasonable and prudent individual).

It may come as a surprise to many that directors can be held personally liable for breaches of duty in such areas as mismanagement of corporate assets, financial losses, wrongful dismissal, employee discrimination or failure to address environmental issues for which the company could reasonably be held responsible.



The legal cost of a director's defence when named in a statement of claim against the company may be

advanced or reimbursed by the corporation as long as it is determined that the director:

124.(3)...

- (a) acted honestly and in good faith with a view to the best interests of the corporation, or, as the case may be, to the best interests of the other entity for which the individual acted as director or officer or in a similar capacity at the corporation's request; and
- (b) in the case of a criminal or administrative action or proceeding that is enforced by a monetary penalty, the individual had reasonable grounds for believing that the individual's conduct was lawful.

The federal Act provides that the company can carry insurance to protect the director against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgment, reasonably incurred by the individual in respect of any civil, criminal, administrative, investigative or other proceeding in which the individual is involved because of that association with the corporation or other entity.

### Acquire Insurance

124.(6) A corporation may purchase and maintain insurance for the benefit of an individual referred to in subsection (1) against any liability incurred by the individual

- (a) in the individual's capacity as a director or officer of the corporation; or
- (b) in the individual's capacity as a director or officer, or similar capacity, of another entity, if the individual acts or acted in that capacity at the corporation's request.

The role of director in a company, regardless of its size or province of incorporation, places a burden of responsibility that most owner-managers are not aware of. It is incumbent upon directors to be aware of:

- the risk of negligence and the potential liability of all directors or other officers of the corporation;
- the need to insist that they are provided with all pertinent information they require to oversee the operations of the corporation;
- the statutes and regulations that the company is obligated to follow;

- the financial condition of the corporation at all times;
- the need to avoid any conflict of interest. A director should have no task outside their responsibility as director that could interfere with their responsibility to the company;
- the need for rules and guidelines within the corporation to ensure confidentiality of not only all corporate documentation but all information concerning employees;
- the need to document the information used and the process of how major decisions were arrived at;
- the need to use corporate legal counsel in contentious situations to demonstrate that due care and diligence were exercised before the decision was made; and
- their obligation to understand the operations of the corporation and to participate and communicate with management on all matters of corporate significance regardless of whether a director agrees or disagrees with the activities of management.

### Get Legal Advice

The ownership and the directors and officers of family-owned businesses are usually one and the same. As such there is minimal risk of disgruntled shareholders taking the directors to task. However, outside entities, whether regulatory bodies or third parties, may not be so obliging. When family members are directors, the corporation may have trouble convincing authorities that objectivity, confidentiality and corporate governance are not tainted by non-arm's length relationships among family members. If you are invited to become a director of a corporation owned by members of your family, get legal advice before agreeing to stand for election. In the long run, it is in the best interests of both you and the company to meet with your lawyer and discuss the best means of protecting the business and the family from both corporate and personal loss.

### This'n That at Logan Katz

#### Logan Katz Celebrates the UFE Results

The Partners and Staff of Logan Katz would like to extend our most sincere congratulations to fellow team members, Samuel Levine and Yusuf Abdi who have recently passed the Uniform Final Exam (UFE).

The UFE is the final milestone in completing the academic requirements leading to the CA designation.

Please join us in congratulating them on this outstanding accomplishment.

#### November On-Line Poll

The Logan Katz October on-line poll asked "Did you attend a Remembrance Day ceremony this November?" Our non-scientific results were 30% YES and 70% NO. Visit our website to participate in our monthly polls.