

LERNERS



LAWYERS

CORPORATE GOVERNANCE
Liability and Risk Management

A CORPORATION IS A DISTINCT LEGAL ENTITY

- Applies to Co-operative Corporations, Business Corporations and Not-For-Profit Corporations.
- Generally, directors, officers, and members/shareholders are not liable for the actions or wrongs committed by a corporation.
 - Example: Breach of contract
- However, there are some exceptions where directors, officers, and members/shareholders may be liable under statute and common law.

A DIRECTOR'S DUTY IS TO MANAGE OR SUPERVISE THE MANAGEMENT OF THE BUSINESS AND AFFAIRS OF THE CO-OPERATIVE.

IN CARRYING OUT THIS DUTY, DIRECTORS MUST EXERCISE THEIR POWERS AND DISCHARGE DUTIES HONESTLY, IN GOOD FAITH, AND IN THE BEST INTERESTS OF THE CO-OPERATIVE TO THE STANDARD OF A REASONABLY PRUDENT PERSON.

A DIRECTOR MAY BE LIABLE TO THE CO-OPERATIVE IF HE OR SHE IS IN BREACH OF THEIR DUTIES.

DIRECTOR'S ARE ALSO LIABLE UNDER A NUMBER OF STATUTES AND COMMON LAW.

LIABILITY IN TORT

- A tort is a civil wrong recognized by courts for which injured persons may claim damages.
- Director's may be liable in tort if:
 - They permitted an unsafe condition to exist on the co-operative's property which led to injury
 - They failed to monitor and safeguard the corporation's assets resulting in a loss
 - They approved an unauthorized investment that resulted in a loss to the co-operative
 - They failed to supervise the conduct of employees in their work for the co-operative, and the employees cause loss

LIABILITY IN CONTRACT

- Director's may be liable if they enter into a contract on behalf of the co-operative without authority.
 - Statutory requirements not fulfilled;
 - By-laws or other corporate documents not complied with.

LIABILITY BREACH OF FIDUCIARY DUTY

- Directors may be liable if they fail to:
 - Deal honestly with the co-operative;
 - Exercise due diligence in performance of duties;
 - Avoid conflicts of interest.

LIABILITY UNDER INCOME TAX ACT (CANADA)

- Director's may be liable if the co-operative fails to withhold and remit taxes and the co-operative does not have the ability to pay:
 - Dealing with non-resident vendors

LIABILITY UNDER EXCISE TAX ACT (CANADA)

- Director's may be liable if the co-operative fails to remit HST.

LIABILITY FOR EMPLOYMENT INSURANCE AND CANADA PENSION PLAN

- Director's may be liable if the co-operative fails to remit employee premiums.

LIABILITY UNDER EMPLOYER HEALTH TAX ACT (ONTARIO)

- Director's may be liable if the corporation fails to remit employer health tax.

OCCUPATIONAL HEALTH AND SAFETY ACT (ONTARIO)

- Director's may be liable if the co-operative fails to take steps to ensure compliance with the safety regulations.

WORKPLACE SAFETY AND INSURANCE ACT, 1997 (ONTARIO)

- Director's may be liable if the co-operative fails to remit WSIB premiums.

ENVIRONMENTAL PROTECTION ACT (ONTARIO)

- Any person may be liable if found to be in care or control of a pollutant, an operation responsible for emitting a pollutant or contaminated lands.

DO NOT ALLOW A CO-OPERATIVE TO LOAN OR PROVIDE FINANCIAL ASSISTANCE TO MEMBERS, DIRECTORS OR EMPLOYEES THAT IS NOT GENERALLY AVAILABLE TO ALL.

- Section 17.2 of the Act:
 - Directors could be liable to the co-operative and to the creditors for any loss together with interest at the rate of 6% per year.

DIRECTORS MUST DISCLOSE ALL MATERIAL CONTRACTS BETWEEN THEM AND THE CO-OPERATIVE THAT ARE NOT AVAILABLE TO ALL MEMBERS.

- Section 98 of the Act:
 - Directors could be liable to account for any gain unless the members approve of the contract.

**DO NOT AUTHORIZE AN ACQUISITION OF SHARES OR
PAYMENT OF ANY LOAN FROM ANY MEMBER IF CO-
OPERATIVE IS INSOLVENT**

- Section 99 of the Act:
 - Directors could be liable for any amounts paid.

DO NOT AUTHORIZE DIVIDENDS ABOVE THE PRESCRIBED RATE OR WHERE THE CO-OPERATIVE IS INSOLVENT OR WHERE ITS CAPITAL IS DIMINISHED.

- Section 100 of the Act:
 - Directors could be liable for any amounts paid.

DIRECTORS ARE LIABLE TO EMPLOYEES OF THE CO-OPERATIVE FOR UP TO SIX MONTHS OF UNPAID WAGES AND VACATION PAY IF CO-OPERATIVE IS UNABLE TO PAY.

- Section 103 of the Act:
 - Directors only liable if the co-operative is sued and cannot pay amount of judgement, or if the action is commenced and the co-operative goes into liquidation or is ordered to be wound up or makes an unauthorized assignment under the *Bankruptcy and Insolvency Act*.
 - Directors who pay the debt to employees have a preferential claim in bankruptcy against the co-operative.

DIRECTORS ARE LIABLE TO THE CO-OPERATIVE IF THEY VOTE OR CONSENT TO INDEMNIFY A PERSON CONTRARY TO SECTION 110 OF THE ACT.

- For a person to be indemnified under Section 110 of the Act:
 - Person acted on Co-operative's behalf at the Co-operative's request
 - Person acted honestly and in good faith with a view to the best interests of the Co-operative
 - If the cases is of a criminal or administrative nature, the person had reasonable grounds for believing that his or her conduct was lawful
- Directors may be liable to the amount paid under any indemnification that does not meet the above requirements

**NO PERSON SHALL OFFER FOR SALE OR SELL OR PURCHASE A
LIST OF MEMBERS OF A CO-OPERATIVE**

- Section 121 of the Act.
- May be liable for breach of privacy laws and breach of the Act.

DIRECTORS MUST COMMUNICATE MATERIAL FACTS TO AUDITORS OF CO-OPERATIVE.

- Section 127 of the Act:
 - Directors and officers must notify auditor where a director or officer becomes aware of a fact which could reasonably have been determined prior to the last annual meeting and that requires a material adjustment to the financial statements.

MEMBERS MAY BE LIABLE FOR DEBTS OF CO-OPERATIVE IF THE NUMBER OF MEMBERS FALLS BELOW THE PRESCRIBED LEVEL FOR A PERIOD EXCEEDING SIX MONTHS.

- Section 145 of the Act:
 - Minimum number of members for Workers' Co-operative: 3
 - Minimum number of members for other Co-operatives: 5
- A member can be exonerated from liability under this section if he or she protests to the co-operative in writing and provides notice by registered mail to the Minister.

DIRECTORS MAY BE GUILTY OF AN OFFENCE FOR REFUSING TO PRODUCE ANY ACCOUNT OR RECORD RELATING TO THE CO-OPERATIVE OR REFUSING TO ANSWER QUESTIONS RELATING TO AFFAIRS AND MANAGEMENT OF THE CO-OPERATIVE UNDER INVESTIGATION OR AUDIT

- Section 146 and 148 of the Act:
 - Director may be guilty of an offence under Section 176 of the Act
 - Section 176 provides that a director who authorized, permitted or acquiesced is guilty and on conviction is liable to a fine of not more than \$5,000.

A DIRECTOR MAY BE LIABLE IF HE OR SHE MAKES A FALSE OR MISLEADING STATEMENT OR OMITTS TO STATE A MATERIAL FACT WHICH MAKES A STATEMENT FALSE OR MISLEADING

- Section 173 of the Act:
 - on conviction, liable to a fine of not more than \$10,000 or imprisonment of a term of not more than 1 year, or both.
 - not liable if person did not know the statement was false or misleading and in the exercise of reasonable diligence could not have known statement was false or misleading.

DIRECTORS MAY BE LIABLE THEY FAIL TO FILE ANY DOCUMENT THE ACT REQUIRES TO BE FILED

- Section 174 of the Act:
 - on conviction, liable to a fine of not more than \$10,000 or imprisonment for a term of not more than 1 year, or both.

DIRECTORS MAY BE LIABLE IF THEY FAIL TO COMPLY WITH ACT, ARTICLES OR BY-LAWS OF A CO-OPERATIVE

- Section 178 of the Act:
 - the Superintendent or member or a creditor of the co-operative may apply to the Court for an order directing the director to comply with such provision and upon application, the Court may make such order as the Court thinks fit

LIMITING DIRECTOR'S LIABILITY

1. Exercise due diligence
2. Indemnity
3. Insurance

Resigning as a director of a co-operative will not absolve you from liability for actions taken during the term you were a director.

However, the Limitations Act generally restricts a claim being brought against persons after a period of two (2) years when the action giving rise to a claim was first discovered or reasonably should have been discovered.

HOW TO EXERCISE DUE DILIGENCE:

- **The Big Three:**
 - Deal honestly with the co-operative
 - Exercise due diligence in performance of duties
 - Avoid conflicts of interest

HOW TO EXERCISE DUE DILIGENCE:

- **When first appointed as a director:**
 - Review articles, by-laws, policies and financial statements of the co-operative
 - Attend training seminars to understand your duties and liabilities
 - Meet with management and members to discuss operations and any concerns

HOW TO EXERCISE DUE DILIGENCE:

- **While acting as a director:**
 - Prepare for and attend all meetings of directors:
 - Ask questions and think critically about information being presented or decisions to be made
 - Voice opinion and opposition to any decisions made
 - Declare conflicts of interest
 - Ensure minutes of meeting are kept and meetings proceed in an orderly fashion
 - Keep your own records of materials
 - Frequently examine and inspect co-operative property and assets and observe operations and conduct of employees
 - Review all contracts the co-operative is entering

HOW TO EXERCISE DUE DILIGENCE:

- **Obtain professional advise:**
 - Auditors to complete financial statements
 - Accountants to review financial policies, remittances, budgeting
 - Lawyers to review transactional matters, liability concerns, and employment issues
 - Engineers/building inspectors to review property and safety concerns

HOW TO EXERCISE DUE DILIGENCE:

- **Follow Corporate Governance Procedures:**
 - Act, By-laws, and policies
 - Directors meetings and member meetings

HOW TO EXERCISE DUE DILIGENCE:

- **Financial Management:**

- Review co-operative's financial statements frequently
- Approve and monitor budget
- Rely on independent auditor
- Implement financial procedure safeguards:
 - Signing authority and banking
 - Ensure management and employees have a list of reporting requirements

HOW TO EXERCISE DUE DILIGENCE:

- **Policies and Procedures:**
 - Commit resources to develop co-operative policies:
 - health and safety procedures
 - employee policies
 - organizational structure and job descriptions
 - technology
 - confidentiality and privacy

INDEMNITIES

- **Review By-laws of Co-operative for Indemnity Provisions**
- **Must comply with Section 110 of the Act:**
 - acted on Co-operative's behalf at the Co-operative's request
 - acted honestly and in good faith with a view to the best interests of the Co-operative
 - If the cases is of a criminal or administrative nature, had reasonable grounds for believing that his or her conduct was lawful

DIRECTORS AND OFFICERS INSURANCE

- **Review policy to ensure it provides adequate coverage and limits**
- **Must comply with Section 110 of the Act:**
 - acted on Co-operative's behalf at the Co-operative's request
 - acted honestly and in good faith with a view to the best interests of the Co-operative

CORPORATE GOVERNANCE

THANK YOU