

Reform of the Canada Corporations Act and Directors' Liability

Final Report

March 2003

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Foreword

In June 2000, the federal government announced the Voluntary Sector Initiative (VSI), a joint initiative between the voluntary sector and the Government of Canada to build a new relationship with Canada's voluntary sector. The federal government committed \$94.6 million over a five-year period toward the goal of building a new relationship with Canada's voluntary sector. Under the VSI, Industry Canada's Corporate and Insolvency Law Policy Directorate was tasked with expediting the development of a new, modern federal not-for-profit statute and to study specific areas of directors' liability, including: approaches taken to address directors' liability by other jurisdictions and the issue of a cap on directors' liabilities; the types of exposure for directors, officers and not-for-profit organizations; and the availability, cost, and effectiveness of existing remedies such as directors' and officers' insurance.

The following is the final report on Reform of the *Canada Corporations Act* and Directors' Liability. It contains a synopsis of the project's activities, which included cross-country consultations with the voluntary sector, to meet the twin goals of examining the issue of directors' liability and expediting the development of a new federal law governing not-for-profit corporations. It also contains a list of publications and products resulting from the project's work and the next steps that will be undertaken toward meeting our objectives.

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Mandate

In June 2000, the government announced the Voluntary Sector Initiative and a commitment of \$94.6 million for building a new relationship with Canada's voluntary sector. Of this, \$1.6 million was allocated to Industry Canada to examine the issue of directors' liability and to expedite the development of a new federal law governing not-for-profit corporations.

Industry Canada's Corporate and Insolvency Law Policy Directorate set the following objectives related to this project:

- To expedite the development of a new, modern federal not-for-profit statute;
- To undertake studies in specific areas of directors' liability, including:
 - The approaches taken to address directors' liability by other jurisdictions and the issue of a cap on directors' liabilities;
 - The types of exposure for directors, officers and not-for-profit organizations; and
 - The availability, cost, and effectiveness of existing remedies such as directors' and officers' insurance.
- To share the results of this research with the voluntary sector by posting them on the Web site of the Corporate and Insolvency Law Policy Directorate.

In order to assist in achieving these objectives, Industry Canada established and met with an Experts Group on Not-for-profit Law and Directors' Liability. The Experts Group was comprised of 12 individuals from across Canada and it met on May 25, October 10, and November 26, 2001. Its mandate was to:

- Promote collaboration between Industry Canada and the nonprofit sector on corporate governance and directors' liability; and
- Provide expert advice to Industry Canada on a wide range of issues related to options for reforming the Act and for addressing directors' liability.

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Workplan and Work Completed

The activities completed under this project include:

Undertake and contract out research studies to assess corporate and directors' liability issues in the not-for-profit sector, including:

- The types of exposure for directors and officers of not-for-profit organizations;
- The approaches taken to address directors' liability by other jurisdictions and the issue of a cap on directors' liabilities;
- The issue of corporate liability for wrongful acts of employees; and
- The availability, cost and effectiveness of directors' and officers' insurance.

The studies that resulted were, respectively:

- [*A Study of the Liabilities Facing Directors and Officers of Nonprofit Corporations in Canada*](#) (March 2001) prepared by Gowling Lafleur Henderson LLP;
- [*Virginia's Liability Caps for Nonprofit Directors and Officers*](#) (October 2001) and [*The New York and Texas Non-profit Director Liability Caps*](#) (January 2002) prepared by Kevin A. Kordana, Professor of Law, University of Virginia;
- [*Vicarious Liability in the Non-profit Sector*](#) (December 2001) prepared by Cassels Brock & Blackwell LLP; and

- *A Study on Existing Costs, Availability and Coverage for Directors' and Officers' Liability Insurance* (June 2001) prepared by Marsh Canada.

Prepare a preliminary discussion paper on reforming the *Canada Corporations Act* (the Act) and on directors' and officers' liability issues related to the Act: the discussion paper, *Reform of the Canada Corporations Act: the Federal Nonprofit Framework Law* was published in July 2000.

Conduct consultations with the voluntary sector on this preliminary discussion paper. During the fall and winter of 2000–01, roundtable discussion groups were held in St. John's, Halifax, Ottawa, Montreal, Toronto, Edmonton and Vancouver.

Draft framework for a new federal not-for-profit statute in clear and simple language. In March 2002, Industry Canada published two documents related to reforming the Act and directors' liability:

- [*Reform of the Canada Corporations Act: Draft Framework for a New Not-for-Profit Corporations Act*](#); and a supplement
- [*Reform of the Canada Corporations Act: Discussion Issues for a New Not-for-Profit Corporations Act*](#).

Conduct public, *cross-country consultations* on the proposals for a new federal not-for-profit statute. Public consultations were held in St. John's, Halifax, Ottawa, Montreal, Toronto, Winnipeg, Regina, Edmonton and Vancouver in the spring of 2002. Summaries of these consultations were prepared and distributed to participants. The views and inputs of stakeholders who participated and any written submissions received by the department were reviewed and analyzed.

And finally, in partnership with the Canadian Centre for Philanthropy, Industry Canada produced a handbook for directors of not-for-profit organizations. [*The Handbook on Directors' Liability*](#) provides directors with guidance about their basic legal rights and obligations, and with some simple tools to help them exercise those rights and meet those obligations.

It also provides prospective directors with a good understanding of their potential responsibility should they agree to serve on the governing body of a not-for-profit organization, and advice on what to ask in order to make an informed decision on whether or not to take on that responsibility.

Next Steps

- Undertake further research on issues that arose out of the public consultations and the written submissions to the department, and hold targeted consultations with specific stakeholders, as required.
- Finalize departmental policy proposals for reforming the *Canada Corporations Act*.

- Present the departmental policy proposals to the Minister of Industry.
- Consult with, and seek the views of, other federal departments on the detailed proposals for a new federal statute governing not-for-profit corporations.
- Prepare final proposals to modernize the current federal legislation governing not-for-profit corporations.

The new *Canada Corporations Act* will be based on the principles of flexibility, transparency and accountability, efficiency and fairness. These principles are explained as follows.

- **Flexibility.** The Act should be flexible and permissive rather than unduly regulatory. To ensure that the individual needs of each corporation can easily be met, many of the proposals can be adapted to particular circumstances.
- **Transparency and accountability.** The public requires that not-for-profit organizations, particularly publicly funded organizations, be well run and accountable. There must be public trust that they are performing their intended functions in a scrupulous, well-run manner.
- **Efficiency.** The proposals would allow incorporation as a right. This will reduce the level of pre-incorporation scrutiny that not-for-profit corporations currently face, and eliminate the current system of ministerial discretion in granting, or not, corporate status. As a result, organizations would have the ability to incorporate more quickly, reducing costs both to the corporation itself and to government.
- **Fairness.** Directors of not-for-profit organizations have increasingly faced fears of liability. The proposals will contain several provisions that would help to protect directors and officers from unfair and unwarranted liability. They will set out a clearly defined duty of care, and the standard by which it should be measured. The proposals will also provide directors with a due-diligence defence to help them to avoid unwarranted liability, and a right to dissent from decisions that they feel are not in the best interest of the corporation.

Relevant Documents List

A Study of the Liabilities Facing Directors and Officers of Nonprofit Corporations in Canada (March 2001) prepared by Gowling Lafleur Henderson LLP.

http://strategis.ic.gc.ca/epic/internet/incilp-pdci.nsf/vwGeneratedInterE/h_cl00422e.html

Virginia's Liability Caps for Nonprofit Directors and Officers (October 2001) prepared by Kevin A. Kordana, Professor of Law, University of Virginia.

http://strategis.ic.gc.ca/epic/internet/incilp-pdci.nsf/vwGeneratedInterE/h_cl00423e.html

Vicarious Liability in the Non-profit Sector (December 2001) prepared by Cassels Brock & Blackwell LLP.

http://strategis.ic.gc.ca/epic/internet/incilp-pdci.nsf/vwGeneratedInterE/h_cl00424e.html

Industry Canada's Corporate and Insolvency Law Policy Directorate publication: *Reform of the Canada Corporations Act: Draft Framework for a New Not-for-Profit Corporations Act* (March 2002).

http://strategis.ic.gc.ca/epic/internet/incilp-pdci.nsf/vwGeneratedInterE/h_cl00030e.html

Industry Canada's Corporate and Insolvency Law Policy Directorate publication: *Reform of the Canada Corporations Act: Discussion Issues for a New Not-for-Profit Corporations Act* (A supplement to the *Draft Framework for a New Not-for-Profit Corporations Act*.) (March 2002).

http://strategis.ic.gc.ca/epic/internet/incilp-pdci.nsf/vwGeneratedInterE/h_cl00031e.html

Handbook on Directors' Liability (Primer for Directors of Not-for-Profit Corporations (Rights, Duties and Practices) <http://strategis.ic.gc.ca/cilpd/primer>