

June 21, 1996

**Canadian Centre for Ethics & Corporate Policy Response**  
**to the Request for Comments Re: Amendments**  
**to the *Canadian Business Corporations Act***

The Canadian Centre for Ethics & Corporate Policy (the “Centre”) is pleased to submit its proposal for an amendment to the *Canada Business Corporations Act* (the “CBCA”). This submission is being made in response to the Discussion Paper on Directors’ Liability released in November 1995 (the “Discussion Paper”). It deals specifically with the issues raised in Part B of the Discussion Paper, relating to directors’ fiduciary duties.

**The Centre and Its Mandate**

The Centre was founded in 1988 to promote the ethical dimension of corporate and organizational decision-making in the private and public sectors. The Centre is not an advocacy group for any particular interest or cause, but encourages corporations to take into account the impact of their actions on those who have a stake in those actions, in particular those whose interests are not already protected by contract or statute. These “stakeholders” may include a corporation’s customers, employees, lenders, shareholders and suppliers, the community in which it operates or society as a whole. We refer to corporate behaviour which takes into account the interests of all of the corporation’s stakeholders as “ethical” behaviour.

In 1994, the Centre made a submission to The Toronto Stock Exchange Committee on Corporate Governance in Canada which we have attached to this submission for your information.

**Analysis**

It has long been recognized that corporations have stakeholders other than their shareholders and steps have been taken to provide legislative protection for some of those stakeholders. Legislatures and regulators seek to protect the interests of those affected by the corporation through a variety of statutes such as environmental and employee protection statutes and through policy-based regulation such as securities legislation. These statutes and regulations require the corporation to take or refrain from taking certain action and impose penalties on the corporation - and often on the officers and directors - if that action is or is not taken. In addition, the oppression remedy in the CBCA and many other Canadian corporate statutes offers recourse to certain of the corporation’s stakeholders in the event of “conduct that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer”.

Legislation and regulation generally respond to specific problems. A more flexible approach is required in order to encourage corporations to be proactive in their consideration of the corporation’s stakeholders and responsive to the changing identity of those stakeholders. Boards of directors and

management must be encouraged to consider the interests of stakeholders as a regular part of their decision-making, rather than only when they are required by law to do so. Many corporations today recognize their obligations to a variety of constituents through various manifestations of good corporate citizenship. In some cases, boards of directors and senior management provide guidance to others in their organization through codes of corporate conduct. These codes typically articulate the corporation's goals and principles in its relationships with its stakeholders and the corporation's commitment to operate with integrity in these relationships. This is, however, far from a uniform practice. Moreover, relevant codes of conduct, where they do exist, are not uniformly applied - nor do they address all the issues relevant to other stakeholders which a board or management might reasonably take into account.

There are several possible reasons that boards of directors and management may not take into account the interests of stakeholders in making decisions for the corporation. In many cases, they may simply not be aware that the interests of certain stakeholders are being affected. In other cases, directors may be aware of the impact of their decisions on the corporation's stakeholders, but may not recognize that the corporation depends on the continued support of its various stakeholders and, accordingly, that the interests of those stakeholders are generally consistent with the long-term best interests of the corporation. Finally, directors and officers may be concerned that they will be open to criticism, even liability, if they base corporate decisions on considerations that do not directly and demonstrably relate only to the best interests of the corporation. We therefore believe that it would promote ethical corporate conduct if the CBCA expressly stated that directors and management are permitted to take the interests of the corporation's stakeholders into account. It would also provide directors and officers with the necessary comfort that they will not be subject to liability by reason only that they have taken the interests of certain stakeholders into account, provided that they have otherwise satisfied their fiduciary and other duties.

An amendment to the CBCA of the nature being proposed would not represent a change in the law or, for many corporations, even a change in practice. We do not propose that any change be made to the relationship of the board and management to the corporation. It would simply represent a codification of what the Court in *Teck* held to be the law in Canada and what many corporate leaders already hold to be their responsibility.

The August 1995 discussion paper on Directors' and Other Corporate Residency Issues expresses a concern that a "community interest" clause would diminish shareholder protection or affect many other aspects of the CBCA. An amendment which permits, but does not require directors to take the interests of other stakeholders into account, as they are currently permitted to do, would not raise this type of concern. It would also not expose the board or management to materially greater risk of liability or litigation, since a purely permissive provision would not impose any duty on directors or officers that does not already exist.

We would also like to emphasize the role of management in promoting an ethical corporate culture. A corporation acts through its board of directors, which in turn typically appoints senior management to manage the business and affairs of the corporation. The CBCA currently establishes a duty of care for both the directors and officers of a corporation, but imposes no specific obligations on the officers. It is the board that establishes the areas of responsibility for the officers. While the Centre does not propose that this should be changed, we are concerned that the focus on the role of boards of directors in the 1990s diverts attention from those who have day-to-day responsibility for the corporation and its actions. Accordingly, we propose that any amendment to the CBCA of the type we are suggesting state that officers are also permitted to take the interests of the stakeholders into account.

### **The Centre's Proposal**

As a result of the foregoing analysis, the Centre recommends that the CBCA confirm in some way that the directors and officers are not precluded from taking account of the interests of those who may be affected by the actions of the corporation. As discussed above, any provision added to the CBCA for this purpose should be clear that it does not impose additional duties on directors, does not create an obligation to take any particular interests into account and is subject to the directors' duty to act with a view to the best interests of the corporation. We suggest for discussion purposes, the following type of provision be added to section 122 of the CBCA:

Subject to subsection 122(1), in discharging his or her duties pursuant to this Act, every director or officer of the corporation shall be entitled to give consideration to the interests of those who are affected by the corporation's actions (including the corporation's customers, employees, lenders, shareholders, suppliers and the communities in which it operates) in assessing any action or activity of the corporation. Such entitlement does not create any duties owed by any such director or officer to any person or entity to consider or afford any particular weight to any such interest.

This proposed provision has been developed from and is similar to certain provisions of section 717 of New York state's corporate statute, the text of which is set out for your information in Schedule A to this submission. As you are aware, a number of other American jurisdictions have adopted this type of provision.

### **Response to Certain Recommendations**

Our responses to certain of the recommendations set out in Part B of the Discussion Paper are set out below. These comments are made in addition to the proposal set out above that a provision be added to section 122 of the CBCA permitting (and hopefully encouraging) directors to take ethical considerations into account in their deliberations.

***Issue 4: Whether the CBCA should be amended to define the phrase “best interests of the corporation”.***

We agree with the recommendation that no legislative changes should be made to define the phrase “best interests of the corporation”. In our view, it is almost always in the long-term best interests of the corporation for it to take into account the interests of its various stakeholders. Accordingly, paragraph 122(1)(a) of the CBCA as currently drafted is broad enough to address the Centre’s concerns. However, we also believe that it would promote ethical corporate conduct if the CBCA expressly stated that directors and management are permitted to take the interests of the corporation’s stakeholders into account, as proposed at the outset of this submission.

***Issue 5: Whether the CBCA should be amended to narrow the content and object of fiduciary duties (par. 122(1)(a)).***

We agree that the courts should be left to develop fiduciary duties and limits on their applicability. We do not advocate the creation of any fiduciary duty between the directors and any particular stakeholders of the corporation.

***Issue 6: Whether to allow nominee directors to give special but not exclusive attention to the interests of those who elected or appointed them.***

The Centre is concerned not with nominee directors, but with providing statutory permission and encouragement for directors and officers to take into account the interests of the corporation’s various stakeholders. We do not believe, as the Discussion Paper suggests, that permitting the directors to take the interests of a particular constituency into account will dilute the directors’ duty to act with a view to the best interests of the corporation. There will be many situations in which the best interests of the corporation are served - or are at least not compromised - by action taken in the interests of certain stakeholders. If the directors’ fiduciary duty to the corporation remains paramount, no confusion or conflict will result from a statutory provision permitting the board to take the interests of other stakeholders into account.

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We thank you for the opportunity to participate in this process and hope that you will find our comments useful.

## SCHEDULE A

### PROVISION FROM NEW YORK BUSINESS CORPORATION LAW

#### **717 DUTY OF DIRECTORS.--**

(a) A director shall perform his duties as a director, including his duties as a member of any committee of the board upon which he may serve, in good faith and with that degree of care which an ordinarily prudent person in a like position would use under similar circumstances. In performing his duties, a director shall be entitled to rely on information, opinions, reports or statements including financial statements and other financial data, in each case prepared or presented by:

(1) one or more officers or employees of the corporation or of any other corporation of which at least fifty percentum of the outstanding shares of stock entitling the holder thereof to vote for the election of directors is owned directly or indirectly by the corporation, whom the director believes to be reliable and competent in the matters presented,

(2) counsel, public accountants or other persons as to matters which the director believes to be within such person's professional or expert competence, or

(3) a committee of the board upon which he does not serve, duly designated in accordance with a provision of the certificate of incorporation or the by-laws, as to matters within its designated authority, which committee the director believes to merit confidence, so long as in so relying he shall be acting in good faith and with such degree of care, but he shall not be considered to be acting in good faith if he has knowledge concerning the matter in question that would cause such reliance to be unwarranted. A person who so performs his duties shall have no liability by reason of being or having been a director of the corporation.

(b) In taking action, including, without limitation, action which may involve or relate to a change or potential change in the control of the corporation, a director shall be entitled to consider, without limitation,

(1) both the long-term and the short-term interests of the corporation and its shareholders and

(2) the effects that the corporation's actions may have in the short-term or in the long-term depending upon any of the following:

(i) the prospects for potential growth, development, productivity and profitability of the corporation;

(ii) the corporation's current employees;

(iii) the corporation's retired employees and other beneficiaries receiving or entitled to receive retirement, welfare or similar benefits from or pursuant to any plan sponsored, or agreement entered into, by the corporation;

(iv) the corporation's customers and creditors; and

(v) the ability of the corporation to provide, as a going concern, goods, services, employment opportunities and employment benefits and otherwise to contribute to the communities in which it does business.

Nothing in this paragraph shall create any duties owed by any director to any person or entity to consider or afford any particular weight to any of the foregoing or abrogate any duty of the directors, either statutory or recognized by common law or court decisions.

For purposes of this paragraph, "control" shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of the corporation, whether through the ownership of voting stock, by contract, or otherwise.