



THE LEGAL INSIDER

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CANADIAN CORPORATE LAW

Directors' clash of interests

The **Canadian Business Corporations Act** (Federal) and the **Companies Act** (Quebec) both foresee that a corporation's director, contrary to shareholders, must act in the corporation's best interest. In fact, a corporation's director must avoid placing himself in a conflicting position with regard to the corporation's interests. Such obligation to act in the corporation's best interest is easily reconcilable for a director only attending to one Board of Directors. However, when a director attends to several Boards of Directors, he may be placed at deadlock.

By example, a corporation may want to appoint a specific person to its Board of Directors. The said specific person could, because of his business capacities and knowledge, bring a major advantage to the company. However, could it be possible for this person to attend to several Boards of Directors and still comply with his obligation to act in the best interests of the corporations he represents? What would happen if two (2) of the corporations this person represents have conflicting relationships? There are an infinite number of examples on that matter.

A company may, for several reasons, want to appoint a lawyer as director. How would this lawyer manage with the decisions he has to take as director with regards to the clients he represents or counsels in his private practice as a lawyer?

1. Preventing possible conflicts – *due diligence*

Before accepting to be elected as a director of a corporation, one must proceed to a due diligence of the business' activities, signed contracts and accounts receivable in order to evaluate the possibility to be placed in interests' conflict. The decision to accept or not a position of director must be taken carefully. It is strongly suggested to avoid a situation where there is apparent conflict of interests even though the law only sanction existing clash of interests situations.

2. Obligation to declare possible conflicts

If a director notices, during his mandate and despite his previous due diligence, a situation where a conflict of interests could eventually occur, he has the obligation to denounce this possible conflict to the Board of Directors. If such possible conflict is related to a specific decision the Board of Directors has to take (by example: the conclusion of a contract in which a director has an interest), this director must abstain from voting.

The **Canadian Business Corporations Act** provides that any director or officer has the obligation to denounce his interest as a direct party of a projected contract or as an indirect party when he is a director or officer (or if he owns important interest) of another corporation which is part of such contract. In addition to the provisions set forth in the **Canadian Business Corporations Act**, a director appointed in the Province of Quebec also has to comply with the requirements of the Civil Code of Quebec, which are greatly more restrictive. In fact, the Civil Code of Quebec formally forbids directors to engage themselves in a conflicting situation regarding their own interests and those of the corporation they represent. In accordance with the Civil Code of Quebec, a director must, in any circumstances whatsoever act in the best interest of the corporation he represents.

Even though the **Canadian Business Corporations Act** and the Civil Code of Quebec do not provide any penalty for a director who fails to comply with the above-mentioned disclosure obligation, any shareholder or interested person may request for the annulment of a decision taken in breach of such obligation.

Conclusion

In Quebec and Canada, a director is considered as being a trustee or proxy of the corporation he represents and is therefore invested with all duties and obligations pertaining to such position. A director may easily expose himself (knowingly or not) to a possible conflicting situation, therefore placing himself and the corporation in a delicate position. Thus, it is of major importance for a director to have great knowledge of the corporation's activities in order to avoid and foresee such possible conflicts. Before accepting to join a corporation as a director, it would be to one's advantage to proceed to a due diligence of the business. If doubts arise, it would be appropriate to obtain the advice of a corporative legal counsel.

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