

## **Section 9**                      **Protection of Directors**

Although directors are required to perform their duties with an appropriate standard of care, a number of protective measures are also available. These are individually and collectively designed to minimize the exposure of directors of non-profits to legal liability.

### **Indemnification**

Indemnification means that Owl will compensate the directors for any loss incurred for the liabilities arising from the performance of the director's duties, within their scope of authority, except for those arising from wilfully negligent actions. It is important to note that a director can be indemnified when there has been negligence, provided they were acting in good faith.

The purpose of indemnification is to encourage skilled directors to participate in non-profit governance.

### **Insurance**

Indemnity does not eliminate the risk of all liabilities, such as breaches of standard of care, or of certain statutes, or where the corporation is suing the director.

Directors' liability insurance can be maintained in 2 ways: through the corporation, with premiums paid by the corporation; or by the director personally, with premiums paid either by the corporation or by the director.

Not all types of liability are covered, including acts that are *ultra vires* (i.e. beyond the authority of the corporation) and where conflict of interest results in personal profits for directors.

### **Independent Advice**

Directors must act within the scope of their authority and in the best interest of Owl. At times, this may require directors to seek independent advice (e.g. regarding the investment of funds).

Where independent advice is sought, directors should ensure that properly qualified individuals are asked for their expertise.

## Disclosure of Competing Interests

The easiest way to avoid personal liability is to disclose to the board at the earliest opportunity all situations in which a conflict of interest may arise.

The Canada Corporations Act sets out certain provisions for the disclosure of conflicts of interest. These state that the conflict must be declared at the first opportunity and at the meeting of the Board of Directors. Furthermore, the director is then precluded from voting on any contract, transaction or matter - no matter how remote the conflict of interest is.

## Impact of Ratification

Directors can be protected from personal liability where members of the organization ratify their actions. For example, where a director fully discloses a personal interest in a contract, the members may ratify the contract and thus move liability to the corporation or its creditors and away from the personal liability of the director. The members have exerted control of the issue and this ratification provides protection from liability.

## Due Diligence

Reducing the risk of liability before problems arise is the most effective form of protection. This comes in the form of due diligence.

A director must exercise due diligence by attending meetings and reviewing materials, knowing what transactions and activities are happening, discussing issues with other members of the board, making decisions, and ensuring compliance with applicable legislation.



On the next page you will find a brief self-test, covering material from this section.

(Answers will be found on the page afterwards.)

Use this self-test to evaluate for yourself how well you grasped the material covered. Go back and review any areas you need to.



## Self-Test

### Protection of Directors

1. Which of the following is not an example of an Owl director exercising due diligence:
  - a) reviewing materials and attending meetings
  - b) being aware of current transactions and activities
  - c) ensuring compliance with applicable laws and requirements
  - d) discussing issues with other board members
  - e) regularly consulting with outside experts
  
2. What is the most effective form of protection:
  - a) avoiding contentious and controversial topics
  - b) exercising due diligence to minimize the probability of problems arising
  - c) purchasing an insurance policy
  - d) abstaining from voting
  
3. True or False. Indemnification means that Owl will compensate the directors for any loss incurred for the liabilities arising from the performance of the director's duties.

## Self-Test Answers

### Protection of Directors

1. e) regularly consulting with outside experts
2. b) exercising due diligence to minimize the probability of problems arising
3. False. Directors are not indemnified if they act outside of their scope of authority or are wilfully negligent.