IN FACT AND IN LAW

Competition

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Competition Law: Directors' and Officers' Liability

By Serge Bourque, Patrick Buchholz and Larry Markowitz

In this era of Enron, the notion of directors' and officers' liability is on everybody's mind. Greater accountability is expected of directors and officers by shareholders, the media and the general public.

The theory behind imposing a greater level of personal liability on directors and officers is that, if they may be found liable, directors will be more attentive to their legal obligations to properly manage a corporation.

General Principles

The Common Law and the *Civil Code of Québec* impose a variety of obligations on corporate directors. In addition, corporate directors may be held personally liable under provincial and federal statutes, such as the *Competition Act*.

It is also important to study case law with respect to directors' liability. For instance, in a leading U.S. case, *Smith* v. *Van Gorkom*[1], the Supreme Court of Delaware held that the board of directors' conduct in considering a merger was grossly negligent and therefore found the directors to be personally liable. In this case, the directors had failed to deliberate adequately about how the merger price had been determined or about the intrinsic value of the corporation. Moreover, the directors had not sought legal advice or a fairness opinion.

The various forms of liability imposed on corporate directors and officers under the *Competition Act* may generally be avoided through a due diligence defence.

With a due diligence defence, directors or officers may protect themselves by demonstrating that they have put in place appropriate controls and systems to monitor and ensure that proper policies are being implemented, that periodic reports are produced and reviewed in a proper fashion and that appropriate action is taken when a problem is brought to their attention.

When applying a standard of due care to corporate directors, the Courts are concerned about the process that the board of directors has followed, rather than the result. If directors make a decision which is debatable from a business perspective or if it turns out badly, the Courts will not hold the directors personally liable. This principle is referred to as the "Business Judgment Rule".

Directors must discharge their duties with the same level of diligence as a reasonably prudent person in comparable circumstances.

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[1] *Smith* v. *Van Gorkum*, 488 A. 2d 858 (Del. Supr. 1985).

Serge Bourque has been a member of the Quebec Bar since 1962 and specializes in Business Law, with a focus on Competition Law

In *UPM-Kymmene Corporation v. UPM-Kymmene Miramichi* Inc.[2], the Ontario Superior Court of Justice held that the Business Judgment Rule should not apply to the decision by the Board of Directors of Repap Enterprises Inc. to approve an employment agreement with the corporation's senior executive that provided for excessive levels of compensation, since the directors had breached their duty of care by not making the proper inquiries or investigations that would have enabled them to conduct a proper analysis of the situation. Thus, the Business Judgment Rule only applies to the extent that the directors meet a proper standard of due diligence in reaching their decisions.

Liability under the *Competition Act*

There are a number of examples under the *Competition Act* where the law imposes personal liability on corporate directors and/or officers:

- Section 45(1): Conspiracy — Imprisonment for a term not exceeding five years or a fine not exceeding $10 million, or both, for conspiracy to restrain or injure competition unduly.
- Section 47(2): Bid-rigging — A fine in the discretion of the court or imprisonment for a term not exceeding five years, or both.
- Section 52(5): False or Misleading Representation — Depending on the circumstances, a fine either at the discretion of the court or of an amount not exceeding $200,000 or imprisonment for a term not exceeding either one year or five years, or both a fine and imprisonment.
- Section 52.1(8): Deceptive Telemarketing — Liability of officers and directors who are in a position to direct or influence the policies of a corporation that engages in deceptive telemarketing.
- Section 53(5): Deceptive Notice — Liability of officers and directors who are in a position to direct or influence the policies of a corporation that sends a deceptive notice of winning a prize.
- Section 65(4): Contravention of Section 11 Order — Directors and officers of a corporation that contravenes an order for oral examination or the production of documents under section 11 of the *Competition Act* may be found liable, where such director or officer directed, authorized, assented to, acquiesced in or participated in the commission of the offence.
- Section 74.10: Deceptive Marketing Practices — An administrative monetary penalty of up to $50,000 for a first offence and up to $100,000 for each subsequent offence.

In Canada, beginning in the late 1990s, the Competition Bureau shifted towards securing convictions against individual executives and not just their corporations. In fact, it is the stated intention of the Competition Bureau to prosecute directors and officers personally.

For example:

- In 1999, the Competition Bureau imposed a fine of $250,000 against an executive from F. Hoffman-La Roche Ltd. for his part in an international conspiracy to fix bulk vitamin prices and allocate sales. Another former executive was fined $250,000 for his part in two international cartels to fix prices and allocate markets in the bulk vitamin and citric acid industries.
- In *Her Majesty* v. *Cormie*[3], Donald Cormie, the former president of the Principal Group Ltd., which offered financial products, was charged personally and pleaded guilty. He was fined $500,000 under the misleading advertising provisions of the *Competition Act.*
- In September 1999, a former vice-president of Chinook Group Limited was sentenced to nine months in prison for his part in an international conspiracy to fix prices and share markets for choline chloride, an additive used in the animal feed industry. He was also ordered to perform 50 hours of community service. This was the first jail term imposed for a breach of the Conspiracy provisions of the *Competition Act.*

[2] Ont. S.C. No. 99-CL-3536, June 20, 2002.

[3] *Her Majesty* v. *Cormie*, Alta. Q.B., January 22, 1992 (unreported).

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Larry Markowitz has been a member of the Quebec Bar since 1996 and specializes in Business Law, with a focus on Competition Law

- On June 20, 2002, three Toronto chemical suppliers were charged with bid-rigging and conspiracy with respect to the sale and supply of liquid chlorine used by the City of Toronto. In addition to the corporate charges, two individuals, namely, a former marketing vice-president and a manager of another accused corporation were also charged personally.
- In November 2002, criminal charges were laid against a number of corporations, as well as some of their executives personally, for deceptive telemarketing, in which non-profit organizations were contacted by telemarketers who allegedly misrepresented themselves as their regular suppliers of business directories or office supplies.

A case where a successful due diligence defence was mounted was that of *Stroh Brewery*:

- In October 2002, The Stroh Brewery Company (Quebec) Ltd. was fined for engaging in price maintenance, but management was not held personally liable since the behaviour in question did not represent the general policy of the company, but was merely an isolated occurrence. The company instituted a competition law compliance program and held information sessions on the *Competition Act* for its employees.

The United States

In the areas of directors' and officers' liability and in matters of competition and antitrust law, generally, the trends in Canada tend to follow those that are initially established in the United States. It is therefore useful to consider important American decisions, such as the 1999 case of *Archer Daniels Midland Company*, where two senior executives of the American agribusiness giant that had conspired with its rivals to fix prices, were sentenced to two years in jail and fined US $350,000 each.

Trends under Canadian Competition Law

We foresee an increase in the volume of personal liability litigation against directors and officers under Canadian competition law for a number of reasons:

- A private recourse is now allowed for a refusal to deal and market restriction and thus, it is not only the Competition Bureau that may prosecute cases under these provisions. We expect that, in coming years, private actions will be permitted under other provisions of the *Competition Act*, with abuse of a dominant position being a distinct possibility.
- Under section 36 of the *Competition Act*, any person who has suffered a loss or damage as result of anti-competitive conduct may sue for damages. The current trend is for class action recourses to be taken on the basis of this section.
- There is a trend towards co-operation among the antitrust agencies in Canada, the United States and Europe which has led to a greater number of prosecutions and more effective competition law enforcement (e.g., international cartels for fixing prices and allocating markets in the bulk vitamins industry).

Conclusion

Under those offences in competition law where directors and officers can avoid liability through the establishment of a due diligence defence, instituting a corporate compliance program is the best way to avoid such liability. Such a program would be tailored to the specific needs of the corporation and cover both the criminal and civil provisions of the *Competition Act*. For further information regarding the contents of a competition compliance manual, as well as the issues to be addressed under a competition compliance program, we invite you to consult our bulletin entitled "*Competition Law: The Need for Compliance Programs*", which we published in July 2002, available on our firm's website at www.laverydebilly.com.

These bulletins are intended solely to provide general guidance with respect to the potential liability of corporate directors and officers, in order to avoid such a liability. For an analysis of your company's particular situation or the formulation of a competition law compliance program, including the preparation of an employee compliance manual, please contact Serge Bourque at (514) 877-2997, Patrick Buchholz at (514) 877-2931 or Larry Markowitz at (514) 877-3048.

The *Competition Law* team at *Lavery, de Billy* can also conduct seminars for your employees to inform and guide them with respect to competition law compliance.

In addition, if a complaint has been filed against you or if there is a possibility that one may be filed, *Lavery, de Billy*'s Criminal and Penal Law Group, led by Raphaël H. Schachter, Q.C. and Marc Cigana can assist you.

Messrs. Bourque, Buchholz and Markowitz are the co-authors of *Loi sur la concurrence annotée* (Les Éditions Yvon Blais inc., 2000), an annotated version of the *Competition Act* (Canada).

You may contact any of the following members of the Competition Law group with regard to this bulletin.

at our Montréal office
Patrick Bourbeau
Serge Bourque
Patrick Buchholz
Marc Cigana
David Eramian
Benjamin Gross
Guy Lemay
Corinne Lemire
Larry Markowitz
Jean Saint-Onge
Raphaël H. Schachter, Q.C.

Montréal
Suite 4000
1 Place Ville Marie
Montréal, Quebec
H3B 4M4

Telephone:
(514) 871-1522
Fax:
(514) 871-8977

Québec City
Suite 500
925 chemin Saint-Louis
Québec City, Quebec
G1S 1C1

Telephone:
(418) 688-5000
Fax:
(418) 688-3458

Laval
Suite 500
3080 boul. Le Carrefour
Laval, Quebec
H7T 2R5

Telephone:
(450) 978-8100
Fax:
(450) 978-8111

Ottawa
Suite 1810
360 Albert Street
Ottawa, Ontario
K1R 7X7

Telephone:
(613) 594-4936
Fax:
(613) 594-8783

Web Site
www.laverydebilly.com