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DIRECTORS' AND OFFICERS' LIABILITY

The Rapid Transit Public/Private Partnership Steering Committee recommends the adoption of the recommendation contained in the following report, May 10, 2007, from the Regional Solicitor:

1. RECOMMENDATION

It is recommended that:

1. This report be received for information.

2. PURPOSE

This report considers the potential liability to a Regional Councillor arising from the position of director or officer of the Region's rapid transit corporation, York Region Rapid Transit Corporation (Rapidco).

3. BACKGROUND

On July 2, 2003, Rapidco was incorporated under the *Municipal Act*, 2001. On that same day, a Unanimous Shareholder Declaration was executed by the Region which instrument vested most of the powers of the directors of Rapidco in the sole shareholder, the Region, through Regional Council. Pursuant to Regional Council's authorization, the board of directors of Rapidco is to be comprised of the members of the Rapid Transit Steering Committee. By a companion report of today's date, Regional Council must appoint the new board of directors because of the change in composition of the Rapid Transit Steering Committee arising from the 2006 municipal election. In the April 2007 Rapid Transit Steering Committee meeting, the committee members sought further information about their duties and responsibilities, as well as their potential liabilities, arising from their position as directors of Rapidco.

4. ANALYSIS AND OPTIONS

4.1 Unanimous Shareholder Declaration

Rapidco is an incorporated corporation under and governed by the provisions of the *Business Corporations Act* (Ontario) *(OBCA)*. The *OBCA* specifies the powers of a corporation that must or may be exercised by its directors, its officers and its shareholders. Since the date of Rapidco's incorporation, the Region restricted the powers of its directors and officers to an interim mandate which did not include operational responsibilities, and through a Unanimous Shareholder Declaration, reserved virtually all strategic and operational decisions to the Region, as sole shareholder. Thus, a Regional

Councillor, who consents to act as a director of Rapidco, has no actual authority to make any decisions on Rapidco's behalf without specific authorization from Regional Council to do so. Accordingly, the risk of potential claims against a council member arising from acts or omissions in his or her capacity as a director is minimal.

4.2 Directors and Officers Liability Insurance

Section 136(4) of the *OBCA* permits a corporation to purchase and maintain insurance for the benefit of directors and officers, or former directors or officers, against any liability incurred by the person in that capacity except where the person fails to act honestly and in good faith with a view to the best interests of the corporation. Since the date of incorporation, the directors and officers of Rapidco have had liability coverage under the Region's Errors and Omissions (E & O) Liability Policy with the Ontario Municipal Insurance Exchange (OMEX), the Region's main insurer. The E & O Policy covers financial losses suffered by a third party arising as a result of an actual or an alleged wrongful act of a director or officer. Specific exclusions under the E & O Policy include losses for bodily injury, property damage and personal injury, as these would be covered under the Region's Commercial General Liability insurance policy. Other exclusions under the E & O Policy include (i) claims arising out of the failure to maintain adequate insurance, bonds or financial guarantees on assets, construction or employee benefits; (ii) claims arising out of breach of contract; (iii) criminal, dishonest or fraudulent wrongful acts; and (iv) improper investment of funds. As discussed above, since Regional Council has retained control of Rapidco's business and operations and wholly restricted the decision-making powers of the board of directors, the potential risk of incurring third party claims which can be properly maintainable against a director is negligible.

4.3 Rapidco's Indemnification of Directors and Officers

Under Rapidco's General By-law, the corporation has, subject to the limitations contained in the *OBCA*, indemnified the directors and officers of Rapidco, in respect of all costs, charges and expenses reasonably incurred by such person in connection with any suit or proceeding to which the person is made a party by virtue of being or having been a director or officer of Rapidco, so long as (i) he or she acted honestly and in good faith with a view to the best interests of Rapidco and, (ii) in the case of a criminal or administrative action that is enforced by a monetary penalty, he or she had reasonable grounds for believing that his or her conduct was lawful. Failing this test having been satisfied, the director will be personally liable for any costs awarded against such director in the proceeding or charges or expenses incurred by the director therefrom. Thus to minimize the potential for personal liability in a proceeding, a director or officer should ensure that he or she, when carrying out his or her duties for Rapidco, acts honestly, and in good faith with a view to the best interests of Rapidco, and believes, on reasonable grounds, that his or her conduct was lawful.

4.4 Other Obligations and Liabilities under OBCA and Other Statutes

The *OBCA* imposes upon directors and officers two general types of obligations in connection with their management of a corporation's business and affairs. The first is the fiduciary duty to act honestly, in good faith and in the best interests of the corporation. A typical situation in which the fiduciary obligation applies is where a director or officer is a party to a material contract or proposed material contract. Section 132 of the *OBCA* permits such contracts if the director or officer discloses in writing to the corporation or has entered into the minutes of the meeting of directors the nature or extent of his or her interest. Generally the obligation of a director or officer of Rapidco is analogous to that of a Regional Councillor when a conflict situation arises. The second general type of obligation imposed by the *OBCA* is that in carrying out his or her duties, a director or officer must exercise the standard of care that a reasonably prudent person would exercise in comparable circumstances. Since the business and affairs of Rapidco has been the responsibility of the Region under the Unanimous Shareholder Declaration since incorporation, Rapidco's directors have not exercised any decision-making powers, so in fact, a director would have needed only to ensure that conflicts of interest have been dealt with appropriately.

5. FINANCIAL IMPLICATIONS

The E & O Policy has a limit of liability of $50,000,000 per claim and a deductible of $100,000 per claim.

6. LOCAL MUNICIPAL IMPACT

Rapidco, through the Region, is making public transit accessible to residents of York Region, with positive environmental impact.

7. CONCLUSION

A director or officer of Rapidco has potential liability arising from his or her position. However, given that the board's powers have been superseded by Regional Council by virtue of the Unanimous Shareholder Declaration, there is a much reduced risk of potential liability arising from a board member's position. Further, the Region, through its Errors and Omissions policy insures against various insurance claims to reduce a director's or officer's potential risk of loss occasioned by holding his or her position in Rapidco.

For more information on this report contact Janis Vanderburgh, Senior Counsel, Corporate Services Department.