

## *Peoples, BCE, and the Good Corporate “Citizen”*

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This article considers the use of various legal instruments to advance a more expansive but well-defined view of directors' duties and discretion—a view which focuses on the longer-term interests of the corporation. We begin with an attempt to clarify the nature of directors' statutory duties under Canadian corporate law. We then consider the recent decisions of the Supreme Court of Canada in *Peoples Department Stores Inc. (Trustee of) v. Wise* and *BCE v. 1976 Debentureholders*, in which the Court took a broad view of corporate purpose, but failed to provide clear logic or operational guidance as to consequential directorial responsibilities. As a result, the Court may have afforded directors increased deference, provided they comply with prescribed procedural steps, but without a clearly stated legal rationale. We then outline various legal theories that courts might consider help advance and clarify some of the concepts averted to by the Supreme Court and discuss opportunities for complementary legislative or shareholder-initiated reform.

Cet article examine le recours à divers instruments juridiques en vue de faire progresser une perception plus expansive, mais bien définie, des devoirs et de la discrétion des administrateurs - perception qui se concentre sur les intérêts à long terme de la Société. Pour ce faire, nous commençons par essayer d'élucider la nature des devoirs statutaires des administrateurs aux termes du droit des Sociétés canadien. Ensuite, nous examinons les récents arrêts de la Cour suprême du Canada dans *Peoples Department Stores Inc. (Trustee of) c. Wise* et *BCE c. 1976 Debentureholders*, dans lesquels la Cour percevait de manière large l'objectif de la Société, mais ne donnait aucune logique claire ou orientation opérationnelle en matière de responsabilités corrélatives des administrateurs. Par conséquent, la Cour peut avoir accordé aux administrateurs une déférence accrue, tant qu'ils respectent les étapes procédurales prescrites, sans motifs légaux clairement énoncés. Nous exposons ensuite les grandes lignes de diverses théories juridiques dont les tribunaux pourraient éventuellement tenir compte pour contribuer à faire progresser et à expliciter certains des concepts que la Cour suprême évite ; enfin, nous débattons des occasions de réforme législative complémentaire ou de réforme engagée par les actionnaires.

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*being too far ahead of your time  
is indistinguishable from being wrong<sup>1</sup>*

**MANY OBSERVERS VIEW THE LAW AND LEGAL SCHOLARSHIP** as remarkably self-serving disciplines. Scholars and judges<sup>2</sup> often find a way to ensure that “the law” confirms the view they would otherwise favour for economic, social, or political reasons. There are strong incentives built into the political process for those who make laws to engage in and invite such circumlocution by, for example, being purposefully general in the language they use to express concepts.

The broad theme of this article is that judges (by choice or by default) often eschew clarity and favour ambiguity in the law in order to achieve desired outcomes.<sup>3</sup> This easily leads to confusion and unintended consequences. One area where this ambiguity is apparent is the law surrounding proper corporate purpose and the duties, discretion, and accountability of directors. Our goal in this article is not to advance a normative rationale for or against “good corporate citizenship.” Rather, our focus is on how courts and legislators have attempted

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1. Harold S. Marks, “The Value of Predictions, or Where’d All This Rain Come From?” (1993) 49 *Fin. Anal. J.* 6 at 7.
  2. See *e.g.* Richard A. Posner, *How Judges Think* (Cambridge: Harvard University Press, 2008).
  3. See *e.g.* Cass R. Sunstein, “Incompletely Theorized Agreements in Constitutional Law” (1995) 74 *Harv. L. Rev.* 1733.

to devise legal norms relating to directors' and corporate officers' duties in order to advance a modest notion of corporate social responsibility within the traditional framework of corporate governance.

At the heart of such efforts lies the continuing debate on the obligation of directors and officers to act in "the best interests of the corporation."<sup>4</sup> As discussed later in this article, translating this duty into clear, operational guidance for directors lies at the heart of one of the great unresolved debates in corporate law: whether the interests of the corporation are limited to those of its shareholders, or whether they extend to the stakeholder constituencies that contribute to, or are impacted by, the corporate enterprise. Suffice it to say at this juncture that the Dickerson Committee, which recommended including such express statutory language in the *Canada Business Corporations Act* (CBCA), specifically declined to offer guidance as to how the words "in the best interests of the corporation" should be interpreted. Instead, the Committee left this task to the courts, expressing the view that its formulation would allow the courts to escape from the constraints of the "anachronistic" view that has developed in the English courts.<sup>5</sup> The Committee was referring to Laurence Gower's complaint that the English courts viewed the best interests of the company as that of its shareholders.<sup>6</sup>

The Supreme Court of Canada's recent decision in *BCE Inc. v. 1976 Debentureholders*<sup>7</sup> illustrates the hazards of navigating this debate. In getting to a decision that confirmed the prevailing view of the law, and seeking to clarify its own reasons in *Peoples Department Stores Inc. (Trustee of) v. Wise*,<sup>8</sup> the Court managed to express some strikingly confusing views about the duties and accountability of directors. The near-term result will likely be a diminution of the latter. Likewise, the Court's casual references to good corporate "citizenship," in the absence of clear-headed analysis (or legislative norms), will likely serve primarily to add procedural costs that ensure adequate legal cover for board decisions, rather than create new norms and incentives to guide corporate conduct.

Many will welcome the *BCE* decision. Boards will take comfort in language which suggests that, in the context of change of control transactions, their duty

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4. *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 122(1)(a) [CBCA].

5. Robert W.V. Dickerson *et al.*, *Proposals for a New Business Corporations Law for Canada*, vol. 1 (Ottawa: Information Canada, 1971) at para. 241 [Dickerson Report].

6. L.C.B. Gower, *The Principles of Modern Company Law*, 3d ed. (London: Stevens, 1969) at 522.

7. [2008] 3 S.C.R. 560 [BCE].

8. [2004] 3 S.C.R. 461 [Peoples].

to act in the best interests of the corporation may be discharged by taking reasonable steps to maximize shareholder value. They will also welcome the broad discretion which *BCE* appears to confer on them to determine what is in the best interests of the corporation, should they choose to take a course other than maximizing short-term shareholder value. Because of the breadth of effect that the Court has accorded to the concept of the business judgment rule, it will be difficult for corporate stakeholders, including shareholders, to challenge directors' conduct so long as they act in a reasoned and informed manner.

Non-shareholder stakeholders and advocates of corporate social responsibility will welcome the Court's discussion of directors being required "to act in the best interests of the corporation viewed as a good corporate citizen."<sup>9</sup> They will also applaud the Court's statement that the fiduciary duty of directors is not confined to short-term profit or share value. Rather, "where the corporation is an ongoing concern, [the fiduciary duty] looks to the long-term interests of the corporation."<sup>10</sup>

*BCE* provided the Supreme Court with a rare opportunity to articulate and clarify its view with respect to proper corporate purpose and the responsibilities of directors. To do so meaningfully would have required more careful elaboration on stakeholder theory, the director-centric governance model, and attendant accountability mechanisms. Instead, unreasoned discourse, especially by the Court, is likely to be interpreted to provide something for everyone, which may mean too little for anyone.<sup>11</sup> Put another way, *BCE* can be read as stating that the best interests of the corporation are the interests of those stakeholders that a particular board deems most worthy of protection, provided that due process is adhered to in the selection of which stakeholder interests to favour. It is unlikely that this is what the Court had in mind, rendering its reasoning somewhat suspect.

Part I of this article reviews the history of ambiguity in the assessment of directors' duties and accountability. Specifically, Part I examines the extent of

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9. *BCE*, *supra* note 7 at para. 81.

10. *Ibid.* at para. 38.

11. Ronald J. Daniels & Randall Morck, *Corporate Decision-Making in Canada* (Calgary: University of Calgary Press, 1995) at 8. See also Frank H. Easterbrook & Daniel R. Fischel, *The Economic Structure of Corporate Law* (Cambridge: Harvard University Press, 1991). Easterbrook and Fischel recount that: "A manager told to serve two masters (a little for the equity holders, a little for the community) has been freed of both and is answerable to neither. Faced with a demand from either group, the manager can appeal to the interests of the other" (at 38).

uncertainty and public policy debate surrounding the duty of loyalty and good faith, the duty of care, and the business judgment rule, focusing particularly on Anglo-American law. Part II of the article focuses on judicial circumlocution as to the role and accountability of directors in *BCE*. In Part III, various well-developed legal theories are presented that a court might invoke to meaningfully elaborate the role of directors. In particular, we consider the integration of trust law principles into corporate law, the team production approach to corporate law, moral stakeholder theory as a normative principle of corporate governance, the application of the common law duty to act reasonably, and prescribing "enhanced" directors' duties in specified circumstances. In addition, statutory reform and shareholder-initiated approaches towards focusing director accountability are canvassed. We briefly review some relevant precedents, domestic and otherwise, to illustrate such approaches.

As we embark on a consideration of how such legal obligations might be framed, the factors motivating increasing pressure for companies to be good citizens are worth noting. At the simplest level, the lack of congruence between those who take a narrow view of corporate social obligations (*i.e.*, to comply strictly with law) and the actual behaviour of corporate managers has become strained. As discussed later in the article, it is obvious to any serious observer that corporate managers are highly attentive to the interests of various constituencies beyond those of current shareholders and are constantly weighing competing interests. In this context, recognizing the limitations of legal norms, corporate law has been structured to provide "managerial discretion to respond to social and moral sanctions."<sup>12</sup> This approach has become particularly relevant in a world characterized by connectedness and complexity. Globalization has eroded the power of states to regulate large, multinational corporations<sup>13</sup> and market externalities.<sup>14</sup> Likewise, the sheer complexity of contemporary social problems challenges their susceptibility to effective regulation through traditional, national legal instruments.<sup>15</sup> In this environment, corporations (and other affected institutions) must look further ahead and farther afield to achieve "sustainable" solutions.

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12. Einer Elhauge, "Sacrificing Corporate Profits in the Public Interest" (2005) 80 N.Y.U. L. Rev. 733 at 804.

13. Martin Wolf, "Will the Nation-State Survive Globalization?" (2001) 80 Foreign Aff. 178.

14. Cass R. Sunstein, "Paradoxes of the Regulatory State" (1990) 57 U. Chicago L. Rev. 407.

15. See *e.g.* Gunther Teubner, "'Global Bukowina': Legal Pluralism in the World Society" in Gunther Teubner, ed., *Global Law without a State* (Brookfield, Vt.: Dartmouth, 1997) at 3.

## I. STATUTORY DUTIES

Some of the confusion regarding the role and accountability of directors can be traced to the conflation of directors' fiduciary and statutory duties. Canadian corporate law imposes two basic duties on directors and officers: a duty of care and a duty of loyalty and good faith, both of which are shaded by the "business judgment rule." While both are often referred to collectively as "fiduciary duties," it is more typical for the "fiduciary" label to be applied only to the duty of loyalty and good faith. For example, the Court in *Peoples* specifically referred to the duty of loyalty (in contrast to the duty of care) as a "statutory fiduciary duty."<sup>16</sup>

### A. DUTY OF LOYALTY AND GOOD FAITH

The statutory duty of loyalty and good faith arises out of subsection 122(1)(a) of the CBCA, which provides that "every director and officer of a corporation in exercising their powers and discharging their duties shall act honestly and in good faith with a view to the best interests of the corporation."<sup>17</sup>

As Robert Flannigan has pointed out in a series of articles, a description of this "duty of loyalty" as a fiduciary obligation is a mistaken characterization. The functions of fiduciary duties are to control opportunism and to discipline self-interested behaviour in those arrangements in which "an actor has access to the assets of another for a defined or limited purpose."<sup>18</sup> The fiduciary accountability of corporate directors and officers is established through their preferential access to the assets of the corporation. Fiduciary duties are a narrow subset of the duty of loyalty, embracing conflicts between the corporate duties of directors and their personal interests. These typically arise in respect of corporate opportunities, compensation, contracts in which a director or officer has a material interest, and change of control transactions. The broader statutory duty of loyalty and good faith imposes on directors and officers the obligation to not exceed their authority and to exercise such authority "in the best interests of the corporation."

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16. *Peoples*, *supra* note 8 at para. 32.

17. *CBCA*, *supra* note 4.

18. Robert Flannigan, "Fiduciary Duties of Shareholders and Directors" (May 2004) *J. Bus. L.* 277 at 281. See also by Flannigan, "The Boundaries of Fiduciary Accountability" (2004) 83 *Can. Bar Rev.* 35; "The Adulteration of Fiduciary Doctrine in Corporate Law" (2006) 122 *Law Q. Rev.* 449 [Flannigan, "The Adulteration of Fiduciary Doctrine"]; "Reshaping the Duties of Directors" (2005) 84 *Can. Bar Rev.* 365; and "Book Review: A Romantic Conception of Fiduciary Obligation" (2005) 84 *Can. Bar Rev.* 391.

Considering the interests that directors must take into account in their decisions is a distinct exercise from defining the beneficiaries of their fiduciary duties. Conflating the two issues necessarily involves either the expansion of fiduciary duties or an erosion of the statutory duty of loyalty and good faith.

The mistaken description of the duty of loyalty and good faith as a "statutory fiduciary duty" is exemplified in the drafting proposals of the Dickerson Report which led to the CBCA.<sup>19</sup> In characterizing the proposed duty as "a general statutory formulation of the principles underlying the fiduciary relationship between corporations and their directors,"<sup>20</sup> the Dickerson Report referred to earlier United Kingdom (UK)<sup>21</sup> and Ontario law reform initiatives.<sup>22</sup> In fact, a reading of the Ontario reform proposals suggests that the Select Committee on Company Law (the Ontario Select Committee) may have been focusing on the narrower "fiduciary" concern of directors foregoing their personal self-interest:

The law is clear as to what duties of good faith are owed by [a] director to the company arising from [the] fiduciary relationship. ...

...

... [T]he Committee has determined that it is not the director's fiduciary relationship to the company which is unclear in the law, nor do the precise scope or nature of his duties and responsibilities need clarification.<sup>23</sup>

While this may be a charitable view of the Ontario Select Committee's analysis, there is no basis for giving the Dickerson Report a similar benefit of the doubt. Making it clear that the statutory provision was intended to embrace common law and equitable principles, the Dickerson Report identified its purpose as giving "statutory support to principles that are as difficult to apply as they are well understood."<sup>24</sup> By observing that the notion of the best interests of the corporation left "the way free for directors to take into account whatever factors they consider relevant in determining corporate policies,"<sup>25</sup> they clearly

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19. *Dickerson Report*, *supra* note 5.

20. *Ibid.* at 81.

21. U.K., Board of Trade, *Report of the Company Law Committee* (London: Her Majesty's Stationary Office, 1962).

22. Ontario, Legislative Assembly, "1967 Interim Report of the Select Committee on Company Law" by Allan F. Lawrence in *Sessional Papers*, No. 5 (1967).

23. *Ibid.* at 53.

24. *Dickerson Report*, *supra* note 5 at 81.

25. *Ibid.* at 82.

had in mind a broader agency duty—one inconsistent with traditional fiduciary obligations.

The resulting lack of clarity and accountability is not unique to Canadian corporate law. Flannigan<sup>26</sup> traces how things went astray shortly after the House of Lords' decision in *Regal (Hastings) Ltd. v. Gulliver*.<sup>27</sup> That decision confirmed that fiduciary regulation serves to control opportunism, indicating strict liability of directors where a conflict exists (or a benefit is obtained) in the absence of consent. In contrast, in the following month, the UK Court of Appeal in *Re Smith & Fawcett Ltd.*<sup>28</sup> combined the concept of fiduciary obligation with that of "the best interests of the corporation." Describing the power to register share transfers as a "fiduciary power," Lord Greene stated that directors "must exercise their discretion bona fide in what they consider—not what a court may consider—is in the interests of the company, and not for any collateral purpose."<sup>29</sup>

Likewise, in *Howard Smith Ltd. v. Ampol Petroleum Ltd.*,<sup>30</sup> in considering whether directors had properly issued shares during a control contest, the Privy Council saw fiduciary accountability as extending beyond the objective of controlling opportunism. In rejecting the argument advanced on behalf of the directors (that the issuance of shares was not motivated by self-interest and was within the authority of the board), Lord Wilberforce purported to expand the scope of fiduciary accountability:

But it does not follow from this, as the appellants assert, that the absence of any element of self-interest is enough to make an issue valid. Self-interest is only one, though no doubt the commonest, instance of improper motive: and, before one can say that a fiduciary power has been exercised for the purpose for which it was conferred, a wider investigation may have to be made.<sup>31</sup>

Nor is the confusion as to the distinction between fiduciary accountability and determining the best interests of the corporation limited to Anglo-Canadian jurisprudence. In *Credit Lyonnais Bank Nederland N.V. v. Pathe Communications Corp.*, in the context of deciding whether there was a breach of fiduciary duties,

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26. Robert Flannigan, "The Adulteration of Fiduciary Doctrine," *supra* note 18.

27. [1967] 2 A.C. 457 (H.L.).

28. [1942] 1 Ch. 304.

29. *Ibid.* at 306.

30. [1974] 1 A.C. 821.

31. *Ibid.* at 834.



then-Chancellor Allen stated that "where a corporation is operating in the vicinity of insolvency, a board of directors is not merely the agent of the residue risk bearers, but owes its duty to the corporate enterprise."<sup>32</sup> While the decision was initially interpreted to expand directors' duties to include creditors when a corporation is in the so-called zone of insolvency, subsequent case law has clarified that, rather than extending or expanding duties to creditors, it was intended to create an additional shield for directors against shareholders claiming that the company should have taken increased risks for their benefit.<sup>33</sup> In the more recent *Foundation Inc. v. Gheewalla* case, the Delaware Supreme Court made it clear that duties are not owed directly to creditors, but that directors continue to owe duties only to the corporate enterprise.<sup>34</sup>

The Supreme Court of Canada addressed the above-mentioned logic in *Peoples*. By doing so under the rubric of fiduciary obligations (as in *Credit Lyonnais*), it may have added to the confusion in Canada. In *Peoples*, Peoples Department Stores Inc. (Peoples) had been acquired by a subsidiary of Wise Stores Inc. (Wise) from Marks & Spencer Canada Inc. (M&S).<sup>35</sup> The three Wise brothers were directors of both Wise Stores Inc. and its new subsidiary. To protect amounts due to M&S on account of the purchase price, the purchase agreement restricted the amalgamation of the two corporations.<sup>36</sup> As a result, a joint procurement program was established whereby Peoples did most of the purchasing and transferred to Wise inventory purchased on its behalf.<sup>37</sup> When Peoples filed for bankruptcy, its trustee claimed that the directors had breached their statutory duties of loyalty and care to Peoples by implementing the joint procurement plan.<sup>38</sup>

While the Court determined that directors do not have a fiduciary duty to corporate creditors where the corporation is approaching insolvency,<sup>39</sup> it framed its analysis in terms of which stakeholder claims are entitled to consideration by directors in determining "the best interests of the corporation."<sup>40</sup> The Court

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32. [1991] Del. Ch. LEXIS 215 at 108 [*Credit Lyonnais*].

33. *Production Resources Group, L.L.C. v. NCT Group, Inc.*, 863 A.2d 772 (Del. Ch. 2004).

34. 930 A.2d 92 (Del. Sup. Ct. 2007).

35. *Peoples*, *supra* note 8 at para. 8.

36. *Ibid.* at para. 11.

37. *Ibid.* at para. 18.

38. *Ibid.* at para. 23.

39. *Ibid.* at paras. 43-46.

40. *Ibid.* at paras. 41-47.

rejected the notion that the best interests of the corporation means the best interests of its shareholders and stated that the positions of other stakeholders, including creditors (and not merely when a corporation approaches the zone of insolvency), are entitled to consideration by directors:

It is clear that the phrase the “best interests of the corporation” should be read not simply as the “best interests of the shareholders.” ... [I]n determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, *inter alia*, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment.<sup>41</sup>

The Court cited with approval the view of Justice Berger in *Teck Corp. v. Millar*:

I appreciate that it would be a breach of their duty for directors to disregard entirely the interests of a company’s shareholders... . But if they observe a decent respect for other interests lying beyond those of the company’s shareholders in the strict sense, that will not, in my view, leave directors open to the charge that they have failed in their fiduciary duty to the company.<sup>42</sup>

The stakeholder debate is an important and timely one but the Court may have done a disservice by characterizing it as an issue of fiduciary obligation. Having done so, the Court found that both Peoples and Wise had consented to the conflicting duties that the directors owed to each of them. The Court found that the evidence indicated no favouritism. Rather, it demonstrated that the defendant directors had been solely motivated to resolve the problem of managing inventories efficiently.<sup>43</sup> As a result, the Court concluded that there was no fiduciary breach. By treating the issue as whether directors owed a fiduciary obligation to creditors, as opposed to determining whether the directors had breached their statutory duty to the corporation, the Court managed to extricate itself from the “proper purpose” analysis by arguing that creditors (and presumably other stakeholders) had other remedies, such as oppression and negligence, available to them. Indeed, the Court found that the availability of “a broad oppression remedy undermines any perceived need to extend the fiduciary duty imposed on directors... .”<sup>44</sup>

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41. *Ibid.* at para. 42.

42. [1972] 33 D.L.R. (3d) 288 at para. 97 (B.C. S.C.) [*Teck Corp.*].

43. *Supra* note 8 at paras. 40-41.

44. *Ibid.* at para. 51.

Having mischaracterized the issue as one of fiduciary accountability, the Supreme Court might have resolved it by finding no evidence of bad faith or negligence. Instead, while observing that directors' fiduciary liability is strict,<sup>45</sup> the Court immediately stepped back from that position to assert that "all the circumstances may be scrutinized to determine whether the directors and officers have acted honestly and in good faith with a view to the best interests of the corporation."<sup>46</sup> The Court further stated that "the subjective motivation of the director ... is the central focus of the statutory fiduciary duty."<sup>47</sup>

It is not clear how the Court reconciled "subjective motivation" or scrutiny of "all the circumstances" with strict liability. Nor is it evident how wading into the stakeholder debate was relevant to the issue of fiduciary accountability. Doing so arguably imported the oppression analysis and further diluted the concept of fiduciary accountability: if complainants must produce evidence of improper motivation or culpability "in the circumstances," the likelihood of a court finding directors in breach of their "fiduciary" duty is substantially diminished.<sup>48</sup>

## B. DUTY OF CARE

A review of how the law has evolved with respect to the duty of care further highlights the hazards of ambiguity.

The statutory duty of care arises out of subsection 122(1)(b) of the CBCA, which provides that "every director and officer of a corporation, in exercising their powers and discharging their duties, shall ... exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances."

The common law standard of directorial care was subjective and, viewed in hindsight, remarkably low. Its classic articulation is found in *Re City Equitable Fire Insurance Company Limited*.<sup>49</sup> In effect, the common law standard did not

45. *Ibid.* at para. 39.

46. *Ibid.*

47. *Ibid.* at para. 63.

48. For a more detailed discussion of the frailties of *Peoples*, see Ian B. Lee, "Peoples Department Stores v. Wise and the 'Best Interests of the Corporation'" (2005) 41 Can. Bus. L.J. 212; Mohamed F. Khimji, "Peoples v. Wise – Conflating Directors' Duties, Oppression and Stakeholder Protection" (2006) 39 U.B.C. L. Rev. 209; and Darcy L. MacPherson, "Supreme Court Restates Directors' Fiduciary Duty – A Comment on *Peoples Department Stores v. Wise*" (2005) 43 Alta. L. Rev. 383.

49. (1924), [1925] 1 Ch. 407 (C.A.).

require of directors (as it did of others under the general law of negligence) the standard of the “reasonable person.” This approach was rejected by each of the Ontario Select Committee and the Dickerson Report.

The Ontario Select Committee recommended that the common law standard of care be elevated to an objective test, requiring that directors exhibit the “degree of care, diligence, and skill [of a] reasonably prudent director in comparable circumstances.”<sup>50</sup> The language ultimately adopted in the Ontario *Business Corporations Act* (OBCA) extends the test to officers, as well as directors, and measures their conduct against that of a “reasonably prudent person,” rather than that of a “reasonably prudent director,” in comparable circumstances.<sup>51</sup>

While the use of the word “person” instead of “director” might have been intended as a conforming change, given the extension of the duty to officers as well as directors, it was also viewed as a diminution of the proposed standard from that of a “director” (connoting some degree of expertise or professionalism) to that of a “reasonably prudent person.” This was the conclusion of the Federal Court of Appeal<sup>52</sup> in construing virtually identical language in subsection 227.1(3) of the *Income Tax Act*.<sup>53</sup> That court found the reference to a reasonably prudent (versus skilled) person suggested an objective standard of competence, while the inclusion of the phrase “in comparable circumstances” introduced a subjective element. Accordingly, it concluded that the language in subsection 227.1(3) created a hybrid test:

It is not enough for a director to say he or she did his or her best, for that is an invocation of the purely subjective standard. Equally clear is that honesty is not enough. However, the standard is not a professional one. Nor is it the negligence law standard that governs these cases. Rather, the Act contains both objective elements—embodied in the reasonable person language—and subjective elements, inherent in individual considerations like “skill” and the idea of “comparable circumstances.” Accordingly, the standard can be properly described as “objective subjective.”<sup>54</sup>

Like the Ontario Select Committee, the Dickerson Report sought to raise the common law standard of care in its proposed statutory codification.<sup>55</sup> As it

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50. *Supra* note 22 at para. 7.2.3.

51. *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 134(1) [OBCA].

52. *Soper v. Canada* (1998), 1 F.C. 124 at para. 38 (C.A.) [Soper].

53. *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.), s. 227.1(3).

54. *Soper*, *supra* note 52 at para. 41.

55. *Dickerson Report*, *supra* note 5 at para. 242.

noted, "it is ... cold comfort to a shareholder to know that there is a steady supply of marginally competent people available under present law to manage his investment."<sup>56</sup> Although the Dickerson Report did not propose the phrase "in comparable circumstances," it was included by the legislative drafters. At least until *Peoples*, this was viewed by many (including the Federal Court of Appeal) as preserving the common law subjectivity of the duty of care.

Arguably, such ambiguity was put to rest by the Supreme Court of Canada in *Peoples*. With respect to the specific issue, the Court made it clear that the standard had been raised to an objective contextual one:

The main difference is that the enacted version includes the words "in comparable circumstances," which modifies the statutory standard by requiring the context in which a given decision was made to be taken into account. This is not the introduction of a subjective element relating to the competence of the director, but rather the introduction of a contextual element into the statutory standard of care.<sup>57</sup>

As a result, the duty of care imposed on directors would appear to be identical to that imposed on all other persons.

In reaching that result, however, the Court may have created new uncertainty. Their reference to the introduction of a "contextual element" into the statutory standard of care is not clear. According to the Court "the contextual approach dictated by s. 122(1)(b) of the CBCA not only emphasizes the primary facts but also permits prevailing socio-economic conditions to be taken into consideration."<sup>58</sup>

The Court did not elaborate on the relevance of such socio-economic conditions, or how they might be taken into account by directors in their decision making or by judges exercising their discretion in adjusting liability standards after the fact. Nor did it reflect on the justiciability of such issues. Instead, the Court took an expansive view of the scope of directors' duty of care:

[U]nlike the statement of the fiduciary duty in s.122(1)(a) of the CBCA, which specifies that directors and officers must act with a view to the best interests of the corporation, the statement of the duty of care in s.122(1)(b) of the CBCA does not specifically refer to an identifiable party as the beneficiary of the duty. ... Thus the identity of the

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56. *Ibid.* at para. 242.

57. *Peoples*, *supra* note 8 at para. 62.

58. *Ibid.* at para. 64.

beneficiary of the duty of care is much more open-ended, and it appears obvious that it must include creditors.<sup>59</sup>

As Christopher Nicholls points out, it appears that the Court may have conflated two different concepts—the tort “duty of care,” which anticipates many beneficiaries, and the statutory duty of care. Nicholls argues that it is difficult to understand why a corporate statute would impose additional personal duties on directors other than to the corporation itself.<sup>60</sup>

It has been suggested that this reasoning of the Court was based on the civil law of Quebec.<sup>61</sup> This raises interesting issues with respect to the consistent interpretation of the CBCA, a federal statute, particularly in the context of interpretation by a civil law court.

Ontario has subsequently amended the OBCA to add the italicized words:

134(1): Every director and officer of a corporation in exercising his or her powers and discharging his or her duties *to the corporation* shall,

- a) act honestly and in good faith with a view to the best interests of the corporation; and
- b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.<sup>62</sup>

In analyzing the Court’s language in *Peoples*, it is interesting to consider whether a broader duty of care, theoretically owed to a diverse, undefined group of stakeholders, might serve to defeat the object of the duty of loyalty, thereby creating further confusion and leading to suboptimal board decision making. For example, would well-advised directors eschew risks for fear of attracting creditor liability, even when doing so sacrifices corporate opportunity? If so, *Peoples* would serve to encourage self-interested conduct (*i.e.*, the mitigation of exposure to personal liability). This concern has been specifically raised in the context of court-supervised reorganization proceedings under the *Bankruptcy and Insolvency Act* and the *Companies’ Creditor Arrangement Act*.<sup>63</sup> For this reason,

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59. *Ibid.* at para. 57.

60. Christopher C. Nicholls, *Corporate Law* (Toronto: Emond Montgomery, 2005) at 298-99.

61. Bruce L. Welling, *Corporate Law in Canada: The Governing Principles*, 3d ed. (London, ON: Scribblers Publishing, 2006) at 331, n. 115. Both *Peoples* and *BCE* were considered by the Supreme Court on appeal from the Quebec Court of Appeal.

62. *OBCA*, *supra* note 51, s. 134.

63. Stephanie Ben-Ishai & Catherine Nowak, “The Threat of the Oppression Remedy to Reorganizing Insolvent Corporations” (2008) *Ann. Insolv. Rev.* 429. The authors consider

Stephanie Ben-Ishai and Catherine Nowak recommend that the oppression remedy should not be available for use by stakeholders of a corporation once it has entered into a court-supervised reorganization proceeding.

Of late, such concerns have risen to the forefront. Increasingly, directors focus on the personal consequences of board service, both in their deliberations (which tend to be highly process driven) and in their aversion to making higher-risk decisions (which are often characteristic of longer-term strategies). The consequences for firms, as well as for systemic innovation and competitiveness, are alarming.

### C. THE BUSINESS JUDGMENT RULE

One final aspect of *Peoples* merits comment. *Peoples* was the first instance in which the Supreme Court of Canada specifically considered and validated the “business judgment rule.”

In the United States, courts have formalized the “business judgment rule” as a standard of conduct which, if adhered to, insulates the board from judicial review of their actions. A classic US case is *Shlensky v. Wrigley*, in which the plaintiff challenged the Wrigley board’s refusal to install lights at Wrigley Field when every other major league baseball team played night games.<sup>64</sup> The board defended its actions based on the preferences of Wrigley’s majority owner—that baseball is a day game and that lighting the stadium would damage the surrounding community. The court granted the board’s motion to dismiss, relying on the “business judgment rule” to preclude the plaintiffs from even inquiring into the basis for the board’s decision.

Assuming a board acts in good faith, on an informed basis, in a manner in which it believes is in the best interest of the corporation, and is neither wasteful (in the narrow sense of an activity amounting to “corporate waste”) nor engaged in self-interested conduct, it is afforded wide latitude by the US courts under the shield of the business judgment rule.<sup>65</sup> The presumption of judicial deference to the judgment of directors may be rebutted if any of the above-noted

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*Bankruptcy and Insolvency Act*, R.S., 1985, c. B-3; *Companies’ Creditors Arrangement Act*, R.S., 1985, c. C-36.

64. *Shlensky v. Wrigley*, 237 N.E.2d 776 (Ill. App. 1968).

65. *Aronson v. Lewis*, 473 A.2d 805 (Del. Sup. Ct. 1984); *Kaplan v. Centex Corp.*, 284 A.2d 119 (Del. Ch. 1971); *Robinson v. Pittsburgh Oil Refinery Corp.*, 126 A.2d 46 (Del. Ch. 1924); *Puma v. Marriot*, 283 A.2d 693 (Del. Ch. 1971).

conditions are not satisfied, in which case the burden shifts to the directors to show that their actions were rational and taken in good faith. Self-interested conduct in the context of control transactions results in the application of a more stringent “entire fairness” test.<sup>66</sup>

Former Chancellor William T. Allen finds the business judgment rule justified, within the overall context of liability provisions, as intending to protect shareholders by encouraging boards to take risks for their benefit.<sup>67</sup> Einer Elhauge provides a more socially-focused rationale, suggesting that allowing managerial discretion may serve to subject corporate decisions to the same social and moral processes that apply to sole proprietors.<sup>68</sup>

In practice, the business judgment rule has provided a broad shield. Well-advised boards should always have a carefully-prepared record to ensure that the rule’s protection trumps any statutory duty claim. For example, boards have been protected in taking actions that deliberately benefit creditors at the expense of shareholders, so long as the decision was based in facts, well considered, in good faith, and not conflicted by any personal interests of a majority of directors.<sup>69</sup>

Canadian jurisprudential deference to the business judgment rule is less developed. In *CW Shareholdings v. WIC Western International Communications Ltd.*, the Ontario Superior Court of Justice explained that the rule:

[O]perates to shield from court intervention business decisions which have been made honestly, prudently, in good faith and on reasonable grounds. In such cases, the board’s decision will not be subject to microscopic examination and the court will be reluctant to interfere and usurp the board of directors’ function in managing the corporation.<sup>70</sup>

The rule was referred to by the Supreme Court in *Peoples* as follows:

Business decisions must sometimes be made, with high stakes and under considerable time pressure, in circumstances in which detailed information is not available. It might

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66. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. Sup. Ct. 1985) [*Unocal*].

67. See William T. Allen, “Modern Corporate Governance and the Erosion of the Business Judgement Rule in Delaware Corporate Law” (Osgoode Hall Law School, Comparative Research in Law and Political Economy (CLPE), Research Paper No. 06/2008), online: <<http://www.ssrn.com/abstract=1105591>>. Allen was Chancellor of the Court of Chancery of the State of Delaware.

68. Elhauge, *supra* note 12 at 844.

69. See Stephen M. Bainbridge, *Corporation Law and Economics* (New York: Foundation Press, 2002) at 414-15.

70. [1998] 39 O.R. (3d) 755 at para. 57.



be tempting for some to see unsuccessful business decisions as unreasonable or imprudent in light of information that becomes available *ex post facto*. Because of this risk of hindsight bias, Canadian courts have developed a rule of deference to business decisions called the "business judgment rule," adopting the American name for the rule.<sup>71</sup>

Since at least *Teck Corp.*,<sup>72</sup> Canadian courts, in the absence of conflicts of interest or patently flawed process, have been reluctant to second-guess or impose liability on directors. This may have been an acknowledgement that setting the standard of review too low would discourage board service and risk-taking. For reasons discussed below, *BCE* may serve either to enshrine an overly broad formulation of the business judgment rule, or cast doubt on its relevance and utility. Neither of these outcomes is desirable.

## II. THE *BCE* DECISION

Those who follow Canadian corporate law eagerly awaited the Supreme Court of Canada's reasons in *BCE*. Given the uncertainty surrounding directors' duties (exacerbated by the Court in *Peoples*) there was a general expectation that the Court might use the opportunity to revisit and distinguish (or otherwise clarify) its earlier reasoning. Instead, it created additional uncertainty with respect to the manner in which the "fairness" test for a Plan of Arrangement and the oppression remedy will be applied, as well as adding to the confusion surrounding directors' duties and the indeterminate nature and scope of their agency obligations.

The facts in *BCE* involved a leveraged buyout—which, at the time, would have been the largest of its kind—that was to have been effected by a Plan of Arrangement under the CBCA (the Arrangement). While it did not purport to arrange the legal rights of bondholders of Bell Canada (a wholly-owned subsidiary of BCE), certain bondholders contested the fairness of the Arrangement and brought an oppression claim. The trial judge dismissed such claims, finding the Arrangement to be in the best interests of BCE and Bell Canada.<sup>73</sup>

The Quebec Court of Appeal unanimously overturned the trial decision, finding that the Arrangement had not been shown to be fair and that it should not have been approved.<sup>74</sup> The Court of Appeal found that the BCE board of

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71. *Peoples*, *supra* note 8 at para. 64.

72. *Supra* note 42.

73. *BCE Inc., Re*, [2008] R.J.Q. 1097, 43 B.L.R. (4th) 1 (Q.C.S.).

74. *BCE Inc., Re*, [2008] 43 B.L.R. (4th) 157, 2008 QCCA 935.

directors (the Board) was under a duty to consider whether the Arrangement could have been structured in a way that provided a satisfactory price for shareholders, while avoiding, or at least mitigating, the adverse effect on bondholders. In the absence of such efforts, the Court of Appeal determined that BCE had not discharged its onus of showing that the Arrangement was fair and reasonable. In doing so, the Court of Appeal ignored the trial judge's specific findings that the Board had, in fact, considered the interests of bondholders. Given its tenuous connection to the factual record, the Court of Appeal's decision was troubling because it suggested a substantive objection that it was not sufficient merely to have considered extra-contractual interests. Rather, the Board should have done something about them. Absent a legal entitlement that could be clearly articulated, the Quebec Court of Appeal left unanswered how a board might go about striking a satisfactory and legally justifiable balance.

On a remarkably expedited basis, the Supreme Court of Canada heard the appeal and unanimously reversed the decision of the Quebec Court of Appeal. In its reasons, the Court reinstated key findings of the trial judge, rejecting the bondholder claims that the transaction was oppressive, and confirming that BCE had satisfied the fairness test required for court approval of the Arrangement.

In analyzing the manner in which the "fairness" test for a Plan of Arrangement will be applied, the Court noted that the scope of judicial inquiry is generally confined to legal rights. The Court rejected the "fair and reasonable" test by which courts previously reserved the discretion to rule against an arrangement, notwithstanding shareholder approval thereof.<sup>75</sup> Instead, and absent extraordinary circumstances (not found in this case and, therefore, presumably not simply a diminution in the market value of a complainant's securities), the Court articulated a narrower test for approval, *i.e.*, whether (i) the arrangement has a valid business purpose and (ii) the objections of those whose legal rights are being arranged have been resolved in a fair and balanced way. The Court recognized that "there is no such thing as a perfect arrangement," and that, "although Board decisions are not subject to microscopic examination with the perfect vision of hindsight, they are subject to examination."<sup>76</sup> The valid business purpose prong of the test suggests an inquiry by the Court into specific facts and the degree of

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75. BCE's common shareholders approved the Arrangement by a vote of over 97 per cent. See *BCE*, *supra* note 7 at para. 161.

76. *UPM-Kymmene Corp. v. UPM-Kymmene Miramichi Inc.*, [2002] 214 D.L.R. (4th) 496 at para. 153, cited in *BCE*, *supra* note 7 at para. 155.

necessity of the arrangement. The fair balancing prong looks at a number of factors, including requisite shareholder approval.

It remains to be seen whether this two-part test will facilitate arrangements or be used by courts as a mechanism to second-guess shareholder votes, when they are so inclined, for equitable reasons. Moreover, as noted, the Court's reasons imply a "necessity test" in order to effect a transaction by way of an arrangement. In this case, the Court determined, without any elaboration, that such necessity was established.

The Court also set out a two-pronged test for its analysis of the oppression remedy. A complainant is required to establish that (i) it had a reasonable expectation, (ii) which was unfairly disregarded.<sup>77</sup> The Court found the concept of reasonable expectations to be objective and contextual, in that "the question is whether the expectation is reasonable having regard to the facts of the specific case, the relationships at issue, and the entire context, including the fact that there may be conflicting claims and expectations."<sup>78</sup> It went on to suggest that, where there is a conflict between the views of stakeholders, each is entitled to reasonably expect fair treatment. In resolving conflicts, the Court found that a board owes a duty to the corporation, not to a particular group of stakeholders, and that the reasonable expectations of stakeholders dictate that the directors act in a disinterested and impartial manner, free from conflict of interest, and in the best interests of the corporation.

The Court elaborated various useful factors for determining whether reasonable expectations exist, including general commercial practice, the nature of the corporation, the relationship between the parties, past practice, steps the claimant could have taken to protect itself, representations and agreements, and the fair resolution of the conflicting interests of different stakeholders.<sup>79</sup> With respect to the last factor, while the Court noted that directors can resolve conflicts between different stakeholder groups in a way that favours one group at the expense of another, it articulated a cornerstone of fair treatment, stating that "the corporation and shareholders are entitled to maximize profit and share value, to be sure, but not by treating individual stakeholders unfairly."<sup>80</sup> *BCE* fails to provide guid-

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77. *BCE, ibid.* at para. 56.

78. *Ibid.* at para. 62.

79. *Ibid.* at paras. 69-84.

80. *Ibid.* at para. 64.

ance as to when permissible favouritism crosses the line into unfairness.

The Court's approach to the oppression remedy illustrates the circular logic of its reasoning. Reasonable expectations arguments are, by their nature, somewhat circular, insofar as expectations are likely to reflect extant legal norms. To compound (or confound) the problem, the Court, in effect, suggests that reasonable expectations can be breached, so long as doing so is not unfair. This challenges the law since *Ebrahimi v. Westbourne Galleries Ltd.*,<sup>81</sup> under which "reasonable expectations" have defined fairness. Moreover, in setting out several factors for determining the reasonableness of expectations, the Court may have changed their relative significance. For example, did the Court, in listing the existence of a contract alongside other factors, intend to diminish its relative importance? More generally, by touching on various theories of what might form the basis of a judicially recognized "reasonable expectation," the Court created uncertainty as to the assessment of such claims.<sup>82</sup>

The Court's analysis of how a board should weigh "the fair resolution of conflicting interests between corporate stakeholders" appears to link oppression to the duty of loyalty owed by directors, and notes that "reasonable expectations" are now relevant to such duty.<sup>83</sup> It stated that "directors, acting in the best interests of the corporation, may be obliged to consider the impact of their decisions on corporate stakeholders... . However, the directors owe a fiduciary duty to the corporation, and only to the corporation."<sup>84</sup> Earlier in its reasons, the Court asserted that "this case does involve the fiduciary duty of the directors to the corporation, and particularly the 'fair treatment' component of that duty, which ... is fundamental to the reasonable expectations of stakeholders claiming an oppression remedy."<sup>85</sup> However, merging the duty of loyalty (owed to the corporation) with the oppression remedy (intended to redress personal harm to a security holder, creditor, director, or officer of a corporation) has resulted in uncertainty as to both.

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81. [1973] A.C. 360 (H.L.).

82. Jeffrey G. MacIntosh, "Unsafe at Any Speed: BCE and the Peoples' Corporate Law" *The National Post Financial Post* (9 June 2008), online: <<http://network.nationalpost.com/np/blogs/fpcomment/archive/2008/06/09/unsafe-at-any-speed-bce-and-the-peoples-corporate-law.aspx>>.

83. *BCE*, *supra* note 7.

84. *Ibid.* at para. 66.

85. *Ibid.* at para. 36.

In effect, *BCE* appears to denote that fair treatment in respect of alleged corporate or personal harms is whatever stakeholder groups are entitled to reasonably expect, without further elaboration on the nature (or reasonableness) of such expectations or the distinction among various remedies.<sup>86</sup> The Court appears to designate the board as a referee and—so long as it is not conflicted and observes appropriate process—to afford it the protection of an extraordinarily expansive business judgment rule.

The Court's fiduciary duty analysis is the most problematic aspect of the case. The Court stated that "the content of the duty varies with the situation at hand."<sup>87</sup> It relegated the duty of loyalty to one of the listed factors to be considered in the context of considering oppression relief, *i.e.*, entailing a factual "fairness" determination rather than a determination of whether a decision was made on a good faith basis. In this context, the Court had held in *Peoples* that the fiduciary duty is a duty to act in the best interests of the corporation, which may include considering the impact of corporate decisions on particular stakeholders. In *BCE*, reaffirming *Peoples*, the Court went on to speak of an affirmative "fiduciary duty to act in the best interests of the corporation, viewed as a good corporate citizen."<sup>88</sup> In resolving conflicting interests, the Court held that there is "no principle that one set of interests ... should prevail over another set of interests. Everything depends on the particular situation faced by the directors and whether ... they exercise business judgment in a responsible way."<sup>89</sup> Such observations are unhelpful in clarifying norms of directorial conduct. The Supreme Court also noted that the "fiduciary duty" of the directors to the corporation is not confined to short-term profit or share value: "Where the corporation is an ongoing concern, it looks to the long-term interests of the corporation."<sup>90</sup>

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86. For an interesting and somewhat prescient contextual analysis that was written after the Supreme Court's decision and in anticipation of its reasons, see Peer Zumbansen & Simon Archer, "The BCE Decision: Reflections on the Firm as a Contractual Organization" (Osgoode Hall Law School, Comparative Research in Law and Political Economy (CLPE), Research Paper No. 17/2008), online: <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1160094](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1160094)>. For a discussion of how *BCE* further confuses derivative and personal actions, see MacIntosh, *supra* note 82.

87. *BCE*, *supra* note 7 at para. 38.

88. *Ibid.* at para. 81. The concept of corporate "citizenship" is a non-sequitur which the Court did not explain or elaborate on.

89. *Ibid.* at para. 84.

90. *Ibid.* at para. 38.

Although the stakeholder debate is an important and timely one, the Court may have done it a disservice by characterizing its premise as an issue of fiduciary obligation. The challenge of judicial monitoring of competing stakeholder interests is even more daunting than that of monitoring shareholder value maximization. Judges are ill-suited to either task.

*BCE* also adds uncertainty to the nature and scope of directors' agency obligations. Looking to the facts of the case, the Court vindicated the trial judge. The Court found that the evidence both supported a reasonable expectation that the Board would consider the position of the bondholders and that it did, in fact, consider their interests in an appropriate manner, given the circumstances. The repeated references to the interests and fair treatment of stakeholders, and to long-term good corporate citizenship, suggest a rejection of the Delaware model. The Delaware model expressly recognizes and explicitly resolves the conflict that directors face in a change of control context, establishing, as principles, that, once a board of directors makes a decision to sell a company, they (i) have a duty to maximize the value that shareholders receive, and (ii) are subject to an intermediate standard of review. The consequence of this standard is that directorial decisions receive less deference than under the normal business judgment rule.<sup>91</sup> That said, having framed the issue in terms of stakeholder theory (in contrast to a duty to maximize value for shareholders while respecting obligations to other stakeholders), the Court in *BCE* provided no guidance as to the priority of any constituency claims, other than to suggest that boards must focus on the best interests of the corporation. For example, the Court did not address the treatment of preferred shareholders because it was not called upon to do so. In *Palmer v. Carling O'Keefe Breweries of Canada Ltd.*,<sup>92</sup> the Ontario Divisional

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91. *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. Sup. Ct. 1986). Subsequent Delaware cases have addressed fact-specific issues concerning how directors should approach value maximization when selling a company. In each of *Maple Leaf Foods Inc. v. Schneider Corp.*, [1998] 42 O.R. (3d) 177 and *Ventas Inc. v. Sunrise Senior Living Real Estate Investment Trust* (2007), 85 O.R. (3d) 254, the Ontario Court of Appeal held that, when there is a change of control, directors should take reasonable steps to maximize shareholder value. Other Canadian courts have taken a similar view. This principle is also reflected in Canadian Securities Administrators, "Notice of National Policy 62-202," online: <[http://www.osc.gov.on.ca/en/SecuritiesLaw\\_pol\\_19970704\\_62-202\\_fnp.jsp](http://www.osc.gov.on.ca/en/SecuritiesLaw_pol_19970704_62-202_fnp.jsp)> (stating that: "The primary objective of the take-over provisions of Canadian securities legislation is the protection of the bona fide interests of the shareholders of the target company").
92. (1989), 67 O.R. (2d) 161.

Court effectively protected such shareholders by holding that the directors' duty is to act in the best interests of shareholders as a whole, including holders of preferred shares. *BCE*, on the other hand, posits preferred shareholders as just another stakeholder group whose interests (arguably more akin to debt than to common equity) must be balanced.

Even the questions of whether directors may consider, should consider, or are obliged to consider stakeholder interests, and, if so, at what point, were not addressed clearly by the Court. Early in its reasons, it noted that, in *Peoples*, "this Court found that although directors *must* consider the best interests of the corporation, it may also be appropriate, although *not mandatory*, to consider the impact of corporate decisions on shareholders or particular groups of stakeholders."<sup>93</sup> Later, the Court stated that "the duty of directors to act in the best interests of the corporation comprehends a duty to treat individual stakeholders ... equitably and fairly."<sup>94</sup> Is this duty mandatory?

Having waded into stakeholder theory, the Court retreated, without so acknowledging. In searching for an accountability mechanism, it recognized as a practical matter that, with a change of control being imminent, the Board had a duty to maximize value for shareholders. At the same time, it stated that the US *Revlon* duty does not displace the fundamental rule that the duty of directors cannot be confined to particular priority rules. This reasoning was buttressed by the Court's holding that the buy-out would have a beneficial impact on BCE. Absent any finding of conflict of interest or bad faith, and providing that the Board's decisions were within a range of reasonable choices it could have made, the Court was not prepared to exercise hindsight as to whether the Board's decision was the perfect one.

In effect, by deferring to directors' determinations on resolving conflicts between stakeholder groups in a fair manner that reflects the best interests of the corporation, the Court appears to have broadened the jurisprudential relevance and protection that is afforded by the business judgment rule. What previously afforded protection from directorial negligence now extends, arguably, to the determination of directors' statutory duties and whose interests should, may, or must be considered in resolving conflicts in a "fair manner."<sup>95</sup> Taking the Court's

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93. *BCE*, *supra* note 7 at para. 39 [emphasis in original].

94. *Ibid.* at para. 82.

95. Alternately, the context may have supported a conclusion that shareholders had a reasonable expectation in a sale of control that the board would act to maximize value for them.

logic to its extreme, boards would be accorded broader deference than administrative tribunals. In the case of the Ontario Securities Commission, this was recently held to include “the right to be wrong”<sup>96</sup> (but, in the case of boards, this would presumably not include the right to be “unfair,” whatever that may mean).

This development may reflect a fundamental divergence of Canadian and US legal norms with respect to judicial review of directors’ conduct. For example, in contrast to the “entire fairness test,”<sup>97</sup> which informs judicial review of directors’ conduct in the United States (at least when self-interest is alleged), Canadian courts have tended to defer to process-oriented requirements<sup>98</sup> imposed by securities regulators, largely in response to the historical prevalence of controlled public companies in Canada. Securities regulation, in effect, has occupied the field, leaving the courts less inclined to invoke the extraordinary breadth of the oppression remedy in the face of self-interested or change of control transactions.

Conversely, the Court’s reasoning may allow for a contrary position to be argued as well. By engaging in a detailed review of the factual circumstances, the Court may be interpreted to be paying lip-service to the business judgment rule or to be using it as a device to extricate itself from the analytical swamp it had waded into. Such a lack of deference, and an implied willingness to second-guess director decisions made with care and in good faith, suggests a radical narrowing of the business judgment rule!

While many had hoped that *BCE* would be the Supreme Court’s opportunity to clarify and narrow some of the open-ended pronouncements in *Peoples*, one can speculate about a range of fact situations in respect of which the law may now be highly uncertain. How does a board of directors deal with a bidder whose stated intentions may be prejudicial to non-shareholder constituencies when the offer is the best value for shareholders? All other things being equal, should a board be prepared to accept a lower bid to ensure a better capitalized acquiror (at least at the time when the acquisition is effected)? In a broader context, how would one advise a board of directors that decides to relocate opera-

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96. *Sears Holdings Corp. v. Ontario Securities Commission*, [2006] 84 O.R. (3d) 61 at para. 13 (Sup. Ct. J.).

97. See e.g. *Weinberger v. UOP, Inc.*, 457 A.2d. 701 (Del. Sup. Ct. 1983). Defendants are required to demonstrate the “entire fairness” of an impugned transaction to the corporation.

98. *Insider Bids, Issuer Bids, Business Combinations and Related Party Transactions*, O.S.C. Rule 61-501.



tions offshore with a view to ensuring the corporation's long-term commercial viability, given the conflicting effects on creditor, employee, shareholder, and other constituencies? Traditional notions of fiduciary duties, oppression, and the business judgment rule have been confused in the Court's casual discourse on corporate citizenship and directorial accountability, which is remarkable both for its lack of analytical rigour and for its necessity to reach the Court's ultimate decision.

Ironically, the oppression claim—in respect of which relief only extends to conduct that is prejudicial to the interests of security holders, creditors, directors, or officers—was abandoned by the bondholders and not argued by their counsel before the Supreme Court. This renders the effect of the Court's discussion of these issues even more uncertain.

### III. ALTERNATIVE PATHS TO CORPORATE CITIZENSHIP

While not an excuse for casual reasoning by the Supreme Court of Canada in *Peoples* and *BCE*, the debate about imposing corporate citizenship or social responsibility obligations through corporate law is long-standing. It is fair to say that courts and legislators have, overall, tended to follow and respond to heightened societal expectations over time. The following section of this article considers ways in which this process might be accelerated and clarified.

No one disputes the proposition that corporations may only pursue their economic mission through lawful means.<sup>99</sup> However, legal and political debates about the role of the corporation in society extend back close to a century, as discussed further below. The political debate has intensified with the success of the corporation as a vehicle for mobilizing capital and with its increasing social impact. As noted by US President Obama in his inaugural address:

Nor is the question before us whether the market is a force for good or ill. Its power to generate wealth and expand freedom is unmatched, but this crisis has reminded us that without a watchful eye, the market can spin out of control—that a nation cannot prosper long when it favours only the prosperous.<sup>100</sup>

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99. Robert C. Clark, *Corporate Law* (Boston: Little, Brown & Co., 1986) at 18 (a corporation's purpose is to "maximize the value of the company's shares, subject to the constraint that the corporation must meet all its legal obligations to others who are related to or affected by it").

100. Barack Obama, "Inaugural Address" (Delivered at the US Capitol Building, Washington, 20 January 2009), online: <<http://www.america.gov/st/usg-english/2009/January/20090120130302abretnuh0.2991602.html>>.

Debates on improving the market's "watchful eye" tend to run aground when they are disconnected from effective legal frameworks. Robert Reich characterizes these phenomena as a kind of "faux democracy," suggesting that the message that companies have social responsibilities tends to divert public attention from the task of establishing such laws and rules in the first place.<sup>101</sup> This, in turn, feeds into the legal debate over corporate social responsibility, which is generally characterized by competing theories as to the duties of directors and managers to owners or to a wider range of stakeholders. While, as discussed below, there have been occasional law reform initiatives to address this issue, the debate has been highly theoretical and repetitive.

Advocates of corporate social responsibility have embraced *Peoples* as recognizing "as an accurate statement of law" the legal proposition that it may be legitimate for "directors to consider, *inter alia*, the interests of shareholders, employees, suppliers, creditors, consumers, governments, and the environment" in determining whether they are acting with a view to the "best interests of the corporation."<sup>102</sup> There was little Canadian law on this issue prior to *Peoples*.<sup>103</sup> Rather than providing clarification, *BCE* simply reaffirmed *Peoples*:

The fiduciary duty of the directors to the corporation is a broad, contextual concept. It is not confined to short-term profit or share value.

...

In considering what is in the best interests of the corporation, directors may look to the interests of, *inter alia*, shareholders, employees, creditors, consumers, governments and the environment to inform their decisions. Courts should give appropriate deference to the business judgment of directors who take into account these ancillary interests, as reflected by the business judgment rule.<sup>104</sup>

As discussed, such statements add little to the law other than to conflate concepts and provide cover for directorial discretion, assuming appropriate process is adhered to. The resulting uncertainty concerning proper corporate purpose could lead to a diminution in directorial accountability and potential liability. There are a range of alternate legal theories that courts may choose to focus on

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101. Robert B. Reich, "The Case Against Corporate Social Responsibility" (Goldman School of Public Policy, University of California, Berkeley, Working Paper No. GSPP08-003, 2008), online: <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1213129](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1213129)>.

102. *BCE*, *supra* note 7 at para. 39.

103. See *Teck Corp.*, *supra* note 42 and accompanying text.

104. *BCE*, *supra* note 7 at paras. 38, 40.

to elaborate more meaningfully on the social- or stakeholder-related duties of directors. Some are canvassed below. In addition, we briefly note several opportunities for legislative or shareholder-initiated reform.

#### A. TRUST LAW

The Court's language, particularly in *BCE*, is somewhat suggestive of theories of corporate responsibility advanced by A.A. Berle and E. Merrick Dodd in the nascent stage of the corporate responsibility and accountability debates. In 1931, Berle advanced the notion that corporate directors would become subject to the implied oversight of a court's equitable jurisdiction and that, in the future, corporate law would become "in substance, a branch of the law of trust."<sup>105</sup> He argued that directors' powers are subject to equitable limitations to ensure that their grant of power is used "for the rateable benefit of all the shareholders as their interest appears."<sup>106</sup> Berle was reacting to the broad powers that directors exercised on behalf of owners. In effect, he engaged in the same sort of aspirational logic as the Supreme Court, concluding:

In every case, corporate action must be twice tested: first, by the technical rules having to do with the existence and proper exercise of the power; second, by equitable rules somewhat analogous to those which apply in favor of a *cestui que* trust to the trustee's exercise of wide powers granted to him in the instrument making him a fiduciary.<sup>107</sup>

The Court might have embraced and expanded on Berle's proposal to incorporate trust law principles into corporate law.

Berle's argument was taken to its logical conclusion by Dodd the following year.<sup>108</sup> Dodd treated the corporation as a separate legal person and characterized directors as trustees, not for the shareholders but for the separate legal entity. He then argued that directors could "employ [corporate] funds in a manner appropriate to a person ... with a sense of social responsibility without thereby being guilty of a breach of trust."<sup>109</sup> Put otherwise, Dodd suggested that any

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105. A.A. Berle, Jr., "Corporate Powers as Powers in Trust" (1931) 44 Harv. L. Rev. 1049 at 1074.

106. *Ibid.* at 1049.

107. *Ibid.*

108. E. Merrick Dodd, Jr., "For Whom Are Corporate Managers Trustees?" (1932) 45 Harv. L. Rev. 1145.

109. *Ibid.* at 1161.

notion of social responsibility by directors, on behalf of corporations, is voluntary but permissible.

Berle quickly responded,<sup>110</sup> arguing that Dodd's proposal effectively replaced the notion of shareholder primacy with nothing but the discretion of management, doing away with any legal accountability mechanisms. He characterized this as simply handing power over to management "with a pious wish that something nice will come out of it."<sup>111</sup> He went on to note that:

[Lawyers] must meet a series of practical situations from day to day. They are not ... in a position to relinquish one position—here, the idea of corporate trusteeship for security holdings—leaving the situation in flux until a new order shall emerge. Legal technique does not contemplate intervening periods of chaos; it can only follow out new theories as they become established and accepted by the community at large.<sup>112</sup>

However, as Berle became more concerned about corporate power, he became more enamoured with the stakeholder theory of corporate governance, as evidenced by his directive to lawyers to "provide for the new interests as they successively appear."<sup>113</sup> In his best known work, he suggested "that the 'control' of the great corporations should develop into a purely neutral technocracy, balancing a variety of claims by various groups in the community and assigning to each a portion of the income stream on the basis of public policy rather than private cupidity."<sup>114</sup>

Dodd continued to provide the counterpoint as his thinking evolved. In reviewing *The Modern Corporation and Private Property*, he seized on the hazard Berle had initially focused on in their exchange: that duties to the corporation weakened duties to shareholders without putting anything effective in their place. He argued that "[i]f corporations generally are to be conducted in such manner as to give due regard to the interests of all classes in society ... it is primarily through legislation that the change can be brought about."<sup>115</sup>

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110. A.A. Berle, Jr., "For Whom Corporate Managers are Trustees: A Note" (1932) 45 Harv. L. Rev. 1366.

111. *Ibid.* at 1368.

112. *Ibid.* at 1371.

113. *Ibid.* at 1372.

114. Adolf A. Berle, Jr. & Gardiner C. Means, *The Modern Corporation and Private Property* (New York: MacMillan, 1932) at 356.

115. E. Merrick Dodd, Jr., Book Review of *The Modern Corporation and Private Property* by A.A. Berle, Jr. & Gardiner C. Means (1933) 81 U. Pa. L. Rev. 782 at 785.

The conclusions of both Berle and Dodd are not as incompatible as they may at first seem. Berle suggested that the stakeholder debate should be incorporated into corporate law through trust law principles. Dodd argued that it should only be recognized through legislation. In contrast, the Court's analysis in *BCE* fails even to suggest a workable framework.

Before leaving the trust law characterization, we should note that courts have meaningfully wrestled with the extent to which non-shareholder interests should be considered by directors. For example, several years before the *Credit Lyonnais* decision, in *Re Central Ice Cream Co.*,<sup>116</sup> a bankrupt company's only asset was a \$52 million judgment it had obtained against McDonald's. In response, McDonald's offered to settle for \$16 million, which would have satisfied all of the creditor claims and left \$4 million for the shareholders. The creditors favoured the settlement while the shareholders opposed it. Stopping short of the suggestion in *Credit Lyonnais* that, in the zone of insolvency, directors may need to make choices other than those that shareholders would make, Justice Easterbrook held that bankruptcy law requires the trustee to maximize the value of the estate. Based on this logic, directors' duties might be analogized to the trust law principle of "impartiality": the duty of trustees to consider the trust as a whole, with due regard for the diverse beneficial interests created by the terms of the trust.<sup>117</sup>

As with Berle and Dodd, Judge Easterbrook's thinking evolved. Viewing the corporation as a "nexus of contracts" between various stakeholders relegates corporate law to a set of default rules<sup>118</sup> that are designed to reduce transaction costs by obviating the need for individual contracts. Such a construct considerably diminishes, if not eliminates, the notion of the corporation as a distinct entity. Easterbrook and Fischel argue that if the corporation is simply a web of contracts, it becomes "a financing device and is not otherwise distinctive."<sup>119</sup>

The limits of this conceptualization were highlighted in the bid by Rupert Murdoch's News Corporation for Dow Jones, Inc. About 64 per cent of Dow

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116. *Re Central Ice Cream Co.*, 836 F.2d 1068 (7th Cir. 1987).

117. Where the interests of beneficiaries conflict, the trust should try to maximize the value of the trust as a whole and to "act impartially and with due regard for the diverse beneficial interests created by the terms of the trust." *Restatement of the Law: Trusts*, 3d ed. (St. Paul, MN: American Law Institute Publishers, 2003), § 79(1)(a).

118. Easterbrook & Fischel, *supra* note 11 at 75.

119. *Ibid.* at 10.

Jones was held in various trusts for descendants of the Bancroft family. Some family members preferred the premium cash offer, while others were prepared to sacrifice monetary value to ensure continued journalistic integrity. According to press reports, in considering the various interests involved, the first several months of negotiations were spent arguing over principles, resulting in various commitments to protect and invest in the quality of the Dow Jones publications and news services, while the last several days were spent negotiating price. The final sweetener was News Corporation and Dow Jones agreeing to pay the family's advisors' fees, estimated at US\$40 million (equal to an additional US\$2 per share for family members on top of the US\$60 per share final bid price).<sup>120</sup> Faced with a conflict between money and idiosyncratic preferences, the outcome was not surprising (and the law was not particularly relevant). To the extent that fiduciary duties serve as a proscription on self-interest, they tend to be obscured by the contractual approach to corporate law.

A contrasting contractual analogy to trustee powers in a corporate law context was illustrated in the merger of Reuters PLC and the Thomson Corporation. As a part of a business combination that gave the controlling shareholder of the Thomson Corporation control over the combined entity, Thomson and its controlling shareholder undertook to support the Reuters Trust Principles in relation to the combined entity. These principles include the preservation of integrity, the reliability of news, and the development of the news business, and they are enforced by the Reuters Founders Share Company Limited. In the merger, this company was to hold a special "founders share" in each of the dual listed entities, Thomson Reuters Corporation and Thomson Reuters PLC, enabling it to exercise an overriding vote where a third party had obtained prescribed holdings of voting shares in excess of specified limits.

Kelli Alces has recently argued that efforts to define and enforce corporate fiduciary duties, where the relationship is not a fiduciary one, has led to the atrophy of such duties to the point of obsolescence.<sup>121</sup> Instead, she recommends contractually-based disciplinary regimes, including provision for an "equity trustee," which might serve a similar function for shareholders as does an indenture

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120. Andrew Ross Sorkin, "Murdoch and Dow Jones: How The Deal Got Done" *The New York Times* (1 August 2007), online: <<http://dealbook.blogs.nytimes.com/2007/08/01/murdoch-and-dow-jones-how-the-deal-got-done>>.

121. Kelli A. Alces, "Debunking the Corporate Fiduciary Myth" (2009) 35 J. Corp. L. [forthcoming], online: <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1352595](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1352595)>.

trustee for bondholders. Perhaps there is some basis in such mechanisms for enshrining the "long-term" focus averted to by the Court in *BCE*, should a board and/or a corporation's shareholders so choose. The notion of enshrining overriding principles into the corporation's constituting documents merits more careful review, and is discussed below.

## B. TEAM PRODUCTION THEORY

Margaret Blair and Lynn Stout significantly advance Dodd's trustee analogy in proposing the "team production" approach to corporate law as the basis for describing the existing legal duties of directors (rather than arguing, as have Dodd and Berle at various stages in their thinking, about what the board's responsibilities should be in the future).<sup>122</sup> They argue that the board's economic and legal role is to balance competing interests of certain (but not all) stakeholders, which are essential to team production and the success of the enterprise. Blair and Stout argue that, like shareholders, these stakeholders make firm-specific investments, allowing them to extract economic value (including residual entitlements) from the corporation. In describing that role as a "mediating hierarch" between competing constituencies within the corporation, Blair and Stout see stakeholders as voluntarily ceding control to the board, which, in promoting a team enterprise, is then obliged to and responsible for balancing competing interests.<sup>123</sup>

One can read much of this reasoning into *BCE*. The Supreme Court of Canada stated that the duty of directors to act in the best interests of the corporation:

[C]omprehends a duty to treat individual stakeholders affected by corporate actions equitably and fairly. There are no absolute rules. In each case, the question is whether, in all the circumstances, the directors acted in the best interests of the corporation, having regard to all relevant considerations, including, but not confined to, the need to treat affected stakeholders in a fair manner, commensurate with the corporation's duties as a responsible corporate citizen.<sup>124</sup>

Until recently, such notions rarely caused legal confusion. Indeed, ambiguity in statutory duties allowed for constructive tension and responsive judicial interpretation in egregious cases. Any dissonance between the legal duties of

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122. Margaret M. Blair & Lynn A. Stout, "A Team Production Theory of Corporate Law" (1999) 85 Va. L. Rev. 247.

123. *Ibid.*

124. *BCE*, *supra* note 7 at para. 82.

directors to owners and their broader obligations has tended to be that of theory and behaviour. In practice, the day-to-day conduct of effective managers generally reflects an implicit view of corporate obligations to a variety of constituents as being more immediate, if not more important, to the enterprise than its obligations to shareholders. Convergence is achieved, as the Court implied, by taking a longer-term view of value and wealth maximization.

The difficulty has arisen in the face of systemic behaviour that challenges the incumbency of management and rewards the immediate realization of shareholder value, often to the detriment of other constituents. As is generally the case, market forces (including the short-term focus of incentive structures, the opportunity for deception arising from financial innovation, the limited attention span of politicians, and the overwhelming urge to manage public expectations) trumped legal theory. At such a juncture, a legal construct which professes to balance multiple interests breaks down insofar as it provides neither coherence, consistency, nor organizational focus.

Those who advocate team production (or other-than-shareholder primacy) recognize this limitation. For example, Richard Ellsworth argues in favour of customer primacy as providing the most effective discipline on corporate management.<sup>125</sup> Blair and Stout do not address this challenge of keeping accountability focused; nor did the Court. While reaffirming the stakeholder model of directors' duties that it had endorsed in *Peoples* (and, hence, largely accepting the bondholders' argument as to directors' duties) the Court ruled against the bondholders in *BCE*, concluding that they had no reasonable expectation to anything more than the contractual rights provided to them in the trust indentures pursuant to which their bonds were issued.

Examples of new stakeholder-based governance models (in addition to more traditional models, such as cooperatives and employee-owned firms) are rapidly emerging. A recent survey of such experiments in substituting social benefit for profit maximization as the dominant organizational principle around which ownership, governance, capitalization, and compensation structures are designed identified three dominant models.<sup>126</sup> The first is the stakeholder-owned company, such as the Rabobank Group in the Netherlands, the Vanguard group

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125. Richard R. Ellsworth, *Leading with Purpose: The New Corporate Realities* (Stanford: Stanford University Press, 2002). This would have been an ironic test to apply to *BCE*, which, until relatively recently, enjoyed monopoly status in Canada.

126. Marjorie Kelly, "Not Just for Profit" *Strategy & Business* 2009:54 (24 February 2009) 49.



of mutual funds, or John Lewis Partnership PLC. The latter is the largest department store chain in the United Kingdom, currently wholly-owned by some 69,000 employees. It is overseen by a traditional board as well as by an employee-elected governing body (which, in turn, elects five of the twelve board members and has the power to dismiss the chairman). The second is the mission-controlled company, such as Thomson Reuters PLC and Upstream 21 Corporation. Upstream 21 is a holding company established in Oregon to buy local companies that are focused on building social and economic capital within the region and facilitated by recent reforms to Oregon's corporate law, which are described below. Finally, there is the public-private hybrid, which deliberately blurs the lines between for-profit and non-profit modes of operation. Google.org, which manages Google's annual philanthropic budget of about US\$2 billion,<sup>127</sup> terms itself "for-profit philanthropy," and operates as a division of Google, eschewing the traditional, tax-exempt, foundation organizational structure in order to embed itself within, and fully draw upon, Google's resources.

### C. MORAL STAKEHOLDER THEORY

The team production approach to corporate law fails to address the issue of immediate accountability. Most directors are anxious to meet all prescribed legal norms and are reluctant to stray much further. The proliferation of new governance standards (and consequential liability) has exacerbated their proclivity to risk-averse behaviour.

It has been argued that moral stakeholder theory (MST) may "hold the key to giving the board a more useful, comprehensive framework of the firm's utility and purpose to society."<sup>128</sup> MST can be summarized as upholding the beliefs that "fiduciary obligations go beyond short-term profit and are in any case subject to moral criteria in their execution; and ... mere compliance with the law can be unduly limited and even unjust."<sup>129</sup> Like the team production approach,

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127. See Dana B. Reiser, "For-Profit Philanthropy" (2008), online: The Berkley Electronic Press <[http://works.bepress.com/dana\\_brakman\\_reiser/14](http://works.bepress.com/dana_brakman_reiser/14)> [unpublished]. In Google's initial public offering (IPO), discussed later in this article, the company announced its intention to contribute 1 per cent of equity and 1 per cent of profits to charity.

128. Rookmin Maharaj, "Critiquing and Contrasting 'Moral' Stakeholder Theory and 'Strategic' Stakeholder: Implications for the Board of Directors" (2008) 8 Corp. Gov. 2 at 115 (Abstract).

129. Kenneth E. Goodpaster, "Business Ethics and Stakeholder Analysis" (1991) 1 Bus. Ethics Q. 53 at 70.

MST implies that a board's role is to balance the competing interests of various stakeholders. While the team production approach fails to provide a workable framework for stakeholder identification and how their interests should be balanced, MST, through the identification of relational attributes, seeks to provide insight on that point. For example, Mitchell, Agle, and Wood narrow the definition of stakeholder on the basis of "power to influence the firm, legitimacy of the stakeholder relationship with the firm, and the urgency of the stakeholder claim on the firm."<sup>130</sup> Using such criteria to map stakeholders might better enable directors to recognize, prioritize, and thereby manage various stakeholder interests more efficiently and move away from market-induced, short-term incentives.

In response to Milton Friedman's concern that "few trends could so thoroughly undermine the very foundations of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible,"<sup>131</sup> MST mapping arguably benefits corporations financially, even though directors may not have anticipated financial gain at the time of stakeholder identification. For example, in an interview regarding an energy company that suffered financial loss and long-term costs because of its inability to identify and prioritize stakeholders' interests, a company executive stated, "I think that the stakeholder risks that developed ... were not ones that we could have seen before, perhaps because of our lack of knowledge and understanding about a bunch of church groups."<sup>132</sup>

It is often the case that stakeholders will have unique insights to contribute to the success of an enterprise. For that reason—and a desire to promote effective stakeholder engagement—corporate reporting is increasingly viewed as a process through which stakeholders can be meaningfully engaged. It is viewed as more than simply an outcome required by regulation. Put otherwise, the identification of stakeholder interests, according to MST, may provide more focused accountability.

A similar mapping exercise might be beneficial at a societal (*i.e.*, national or regional) level. While the "virtues" of responsibility, accountability, fairness,

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130. Ronald K. Mitchell, Bradley R. Agle & Donna J. Wood, "Toward a Theory of Stakeholder Identification and Salience: Defining the Principle of Who and What Really Counts" (1997) 22 *Acad. Mgmt. Rev.* 853 at 854.

131. Milton Friedman, *Capitalism and Freedom* (Chicago: University of Chicago Press, 1962) at 133-34.

132. Maharaj, *supra* note 128 at 119.

and transparency are widely accepted and implicit in most corporate governance frameworks,<sup>133</sup> their application is highly contextual. There is debate as to how far and to whom such virtues should be applied. Andrew West recently proposed a research agenda to address the question of whether corporate governance convergence between various jurisdictions is appropriate.<sup>134</sup> He noted that, irrespective of the answer to the question he posed, such an inquiry might inform governance frameworks, including accounting practice, managerial approaches, and business education.<sup>135</sup>

#### D. OBLIGATION TO ACT REASONABLY

We have previously noted how, in an early effort to defer to the business judgment of directors, courts exempted directors from general tort law principles, increasing the threshold for liability under statutory duties of care and loyalty to one of gross negligence. Canadian jurisprudence was further muddled following the Federal Court of Canada's decision in *Mentmore Manufacturing Co. Ltd. v. National Merchandise Manufacturing Co.*,<sup>136</sup> where Justice LeDain asserted a conflict between the principles of tort law and corporate law.<sup>137</sup> Leaving aside confusion regarding the argument that directors should be subject to the same application of tort law as others are,<sup>138</sup> there is a broader argument that, in all basic areas of law governing market conduct (including tort, contract, and property law), there is a fundamental duty to act reasonably.

Joseph Singer characterizes this as an "obligation of attentiveness,"<sup>139</sup> arguing that directors, in their oversight of corporate conduct, are subject to the same

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133. See e.g. Ira M. Millstein et. al, *Corporate Governance: Improving Competitiveness and Access to Capital in Global Markets: Report to the OECD by the Business Sector Advisory Group on Corporate Governance* (Paris: OECD Publications, 1998).

134. Andrew West, "Corporate Governance Convergence and Moral Relativism" (2009) 17 Corp. Gov.: Int'l Rev. 107.

135. *Ibid.* at 117.

136. (1978), 89 D.L.R. (3d) 195 (F.C.A.).

137. See Robert Flannigan, "The Personal Tort Liability of Directors" (2002) 81 Can. Bar Rev. 247.

138. There are currently operating in Canada a number of arguably inconsistent judicial approaches to the question of when directors may be found liable to third parties for tortious corporate acts. See e.g. Nicolas Juzda, *The Tort Liability of Directors to Parties Outside the Corporation* (LL.M. Thesis, Osgoode Hall Law School, 2007) [unpublished].

139. Joseph William Singer, "Corporate Responsibility in a Free and Democratic Society" (2008) 58 Case W. Res. L. Rev. 1.

equitable obligations as others to attend to the effects of their actions on others. These obligations apply to those with whom the corporation has continuing relationships (*i.e.*, stakeholders) as well as to the interests of strangers. Beyond specific laws that create clear limits on corporate conduct, Singer suggests that this obligation to attend to the interests of others is based in the common law duty to act reasonably: “We are not free to cause significant harm to others... . We have an obligation to balance their interests against our own to determine whether we can justify the harm we may cause them.”<sup>140</sup>

The environmental law precautionary principle may also serve to elaborate on directors’ duty of care. The principle, mandating precautionary measures in the face of threats of serious or irreversible environmental harm, has now been widely embraced in international law, as well as domestic Canadian and US statutes and jurisprudence.<sup>141</sup> A similar concept has been advanced by John Ruggie in his efforts to operationalize a “protect, respect, and remedy” framework regarding the issue of human rights and transnational corporations.<sup>142</sup> He argues for a “corporate responsibility to respect human rights” or, put simply, “not to infringe on the rights of others.”<sup>143</sup> Likewise, trust scholars have suggested that financial fiduciaries might be subjected to a statutory duty to consult with their beneficiaries when formulating investment policies.<sup>144</sup> The concept of a “duty to consult and accommodate” has been developed extensively by the Court in the context of the Crown’s obligations to Aboriginal peoples. It has held that such a duty arises when the Crown contemplates conduct that might adversely affect Aboriginal rights or title.<sup>145</sup>

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140. *Ibid.* at 6.

141. For a full discussion of the development and extended relevance of the precautionary principles, see Michael Kerr, Richard Janda & Chip Pitts, *Corporate Social Responsibility: A Legal Analysis* (Toronto: LexisNexis, 2009).

142. John Ruggie, Special Representative of the Secretary-General, *Business and Human Rights: Towards Operationalizing the “Protect, Respect, and Remedy” Framework*, UNHRCOR, 11th Sess., UN Doc. A/HRC/11/13 (1999).

143. *Ibid.* at paras. 23, 24. See also paras. 45-55.

144. Gary Watt, *Trusts and Equity*, 2d ed. (New York: Oxford University Press, 2006) at 437. This proposal raises interesting issues as to how the views of contingent beneficiaries are to be taken into account.

145. See Kent McNeil, “The Crown’s Fiduciary Obligations in the Era of Aboriginal Self-Government” *Can. Bar Rev.* [forthcoming]; Sonia Lawrence & Patrick Macklem, “From Consultation to Reconciliation: Aboriginal Rights and the Crown’s Duty to Consult” (2000) 79 *Can. Bar Rev.* 252.

Given this judicial history, it would not have been a significant leap for the Court in *BCE* to develop an explicit directorial "duty to consider," as has been suggested by Judd Sneirson.<sup>146</sup> Under such a theory, fulfilling the statutory duty of care would require directors to consider all reasonably available material information. A broad view of materiality would include the consideration of potential impacts on various stakeholders. Failure to do so could lead to decisions being invalidated by the courts.<sup>147</sup> Such a notion comports with the Court's reasoning that, once stakeholder interests have been considered, directors can reach whatever decision they believe is in the best interests of the corporation. It would also be consistent with management literature, which suggests that a broader stakeholder assessment framework will lead to better corporate decision-making.<sup>148</sup>

Here, again, the challenge is one of accountability. While the duty of loyalty can be utilized to limit the pursuit of self-interest by individual directors or managers, there is no equivalent construct for the corporation itself. Without the elaboration of clear standards by the courts or legislators, it is unrealistic to hold directors accountable to the level of moral reasoning that is implicit in a "duty of attentiveness" for the "reasonableness" of corporate actions.

#### E. ENHANCED DUTIES

Another approach to director duties and accountability would be to articulate "enhanced duties" analogous to, but broader than, the *Revlon* duty in US jurisprudence. In *BCE* the Court purported to reject such a duty (but, as a practical matter, appeared to embrace it). For example, Bernard Sharfman recently proposed a standard of conduct for public company boards when dealing with excessively risky decisions. In such circumstances, he would require that boards specifically consider the company's liquidity, capital adequacy, and funding risk, et cetera, before determining whether it is in the best interests of the corporation to proceed with such a decision.<sup>149</sup>

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146. Judd F. Sneirson, "Doing Well by Doing Good: Leveraging Due Care for Better, More Socially Responsible Decision-Making" (2007) 3 Corp. Gov. L. Rev. 438.

147. However, absent gross negligence, directors would generally remain effectively immune from personal liability as a result of indemnification provisions.

148. Michael C. Jensen, "Value Maximization, Stakeholder Theory, and the Corporate Objective Function" (2001) 14 J. App. Corp. Fin. 8.

149. Bernard S. Sharfman, "Enhancing the Efficiency of Board Decision Making: Lessons

Sharfman's standard of conduct would interact with the existing standard of review and be consistent with the recent Delaware Supreme Court decision in *Lyondell* as well as the approach to board oversight taken by then-Chancellor Allen in *Caremark*.<sup>150</sup> *Caremark* identified a new affirmative duty to monitor corporate compliance with "applicable legal standards," whether or not the board had been given any notice of the wrongdoing on the part of the company's employees. It should be noted that Allen has recently expressed reservations about the effect of directorial liability on risk-taking in the absence of a conflict of interest.<sup>151</sup> He describes how shareholders seek to shift risk to directors whenever things go wrong, thereby discouraging subsequent risk-taking. Providing guidance (rather than prescribing punishment) might best serve to clarify the manner in which directors fulfill their duties of care and loyalty in the context of specified decisions. The Delaware Supreme Court noted in *Stone v. Ritter* that "[w]here directors fail to act in the face of a known duty to act, thereby demonstrating a conscious disregard for their responsibilities, they breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith."<sup>152</sup> While this judicial observation was made in the context of a board accused of not having a system in place to monitor violations of law, it might be applied to an articulation of other fact situations.

If anything has been learned from the most current financial crisis, it relates to the interconnectedness that characterizes global policy making and enterprise.<sup>153</sup> Leaders in the private and public sphere now realize (although they may still resist) the need to extend their horizons temporally, sectorally, and geographically. With the growing recognition that social issues have profound

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Learned from the Financial Crisis of 2008" (2009) 34 Del. J. Corp. L. 813.

150. *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 239 (2009) (holding that board liability may be found only if the board utterly failed to perform its duties); *Re Caremark International Inc. Derivative Litigation*, 698 A.2d 959 (Del Ch. 1996).

151. *Supra* note 67.

152. 911 A.2d 362 at 370 (Del S.C. 2006).

153. See e.g. John M. Broder, "Climate Change Seen as Threat to U.S. Security" *The New York Times* (9 August 2009), online: <<http://www.nytimes.com/2009/08/09/science/earth/09climate.html>>. In commenting on the geo-political impacts of climate change, General Anthony Zinni, former head of the US Central Command, is quoted, "We will pay to reduce greenhouse emissions today, and we'll have to take an economic hit of some kind. Or we will pay the price later in military terms and that will involve human lives."

effects on long-term business prospects, notions of corporate citizenship become more consonant with traditional fiduciary norms.<sup>154</sup>

## F. STATUTORY REFORM

Prescribing standards for corporate responsibility may not lend itself to the narrowness (and shallowness) that characterizes the evolution of common law in small, incremental steps. It behooves us also to canvass legislative initiatives to develop and clarify such norms. Recent efforts have tended to focus on more expansive conceptions of directors' duties and on reporting standards aimed at encouraging more responsible corporate conduct.

### 1. DIRECTORS' DUTIES REDEFINED

As noted above, the ambiguity inherent in statutory directorial duties began to break down in the 1980s, when hostile, leveraged control transactions challenged the incumbency of managers and rewarded the immediate realization of shareholder value, often to the detriment of other constituents. The ensuing "corporate constituency statutes," adopted by many US states from the 1980s onwards, empower (but generally do not require) directors to consider a wide range of interests in their decision-making, including those of employees, customers, creditors, and local communities.<sup>155</sup> While such statutes have proven challenging for practitioners advising boards (because, like the decision in *BCE*, they are so open-ended), most are permissive and do not expose directors to liability if they choose to disregard non-shareholder interests.<sup>156</sup> So, too, with the Delaware case

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154. Benjamin J. Richardson, "Putting Ethics into Environmental Law: Fiduciary Duties for Ethical Investment" (2008) 46 *Osgoode Hall L.J.* 243 at 271. For analogous arguments concerning the fiduciary obligations of institutional investors, see Asset Management Working Group, United Nations Environment Programme Finance Initiative, *Fiduciary Responsibility: Legal and Practical Aspects of Integrating Environmental, Social and Governance Issues Into Institutional Investment: A Follow Up to the AMWG's 'Freshfields Report'*, UNEP FI, 2009, UNEP Job No. DTI/1204/GE, online: <<http://www.unepfi.org/fileadmin/documents/fiduciaryII.pdf>>.

155. See e.g. Eric W. Orts, "Beyond Shareholders: Interpreting Corporate Constituency Statutes" (1992) 61 *Geo. Wash. L. Rev.* 14.

156. An exception is the constituency statute of Connecticut, which only applies in respect of control transactions and requires (rather than permits) directors to consider stakeholder interests in determining the best interests of the corporation. See Conn. Gen. Stat. Ann. § 33-313(e) (West 1992). The Indiana and Pennsylvania statutes state that directors need not focus solely on the interest of shareholders as determinative, but may consider other stakeholder interests. See Ind. Code Ann. § 23-1-35-1(f) (West 2009); Pa. Stat. Ann. tit. 15, § 1715 (West 2009).

law permitting directors to consider the interests of non-shareholder constituents in the context of hostile takeovers.<sup>157</sup> In this respect, they differ from the arguments of Blair and Stout (and possibly the theory of *BCE*), which suggest that a board must, or at least should, take such non-shareholder interests into account.

The impetus for such legislative reform was takeover protection, based on the popular sentiment of ensuring that local (*i.e.*, state) interests would not be adversely affected as a consequence of such transactions (and the cost-cutting and asset-disposals which often follow). The conflict between these objectives and shareholder wealth maximization, as well as the obvious conflict of interest in incumbent directors using such statutory provisions to secure their own positions, may be the reason why the “corporate citizenship” goals that are suggested in these statutes have not been realized.<sup>158</sup> It should be noted that most such statutes are not limited in their application to control transactions.<sup>159</sup>

This conflict was belied in the 1990s, as compensation schemes responded to, and exacerbated, the increasingly short-term focus of market participants. The transformation was profound and overwhelming. For example, the US Business Roundtable—which had stressed the social role that corporations play in their communities with the advent of hostile takeovers—revised its position in 1997 to refocus on the paramount duty of management to shareholders.<sup>160</sup> Corporate executives who had portrayed raiders as vandals now embraced the very same values—a process of reinvention which characterizes (and is often both a strength and Achilles’ heel of) our enterprise system. Yet, even without constituency statutes, broad managerial discretion has been recognized in US corporate law.<sup>161</sup>

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157. See *Unocal*, *supra* note 66; *Paramount Communications v. Time Inc.*, 571 A.2d 1140 (Del. Sup. Ct. 1990).

158. Alternatively, it is widely viewed that these laws simply confirm, in change of control situations, the broad discretion conferred upon directors under the business judgment rule.

159. Orts, *supra* note 155.

160. The Business Roundtable, “Statement on Corporate Governance” (September 1997), online: European Corporate Governance Institute <<http://www.ecgi.org/codes/documents/businessroundtable.pdf>>.

161. See *e.g.* American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations*, vol. 1 (St. Paul, MN.: American Law Institute Publishers, 1994), § 2.01(b).

Even if corporate profit and shareholder gain are not thereby enhanced, the corporation, in the conduct of its business:

(1) Is obliged, to the same extent as a natural person, to act within the boundaries set by law;



Law reform initiatives in Canada and Australia have, in recent years, considered and rejected as unnecessary proposals to amend corporate law to permit or require directors to take into account the interests of non-shareholder constituencies in their actions. In the process leading to the most recent amendments to the CBCA, in 2001, Industry Canada published a discussion paper on directors' liability.<sup>162</sup> While noting that the term "best interests of the corporation" is far from clear, and citing a survey of previous case law suggesting that "where [the] relationship between the short-term and longer-term or broader-based interests is incapable of precise definition ... Canadian directors have few guidelines,"<sup>163</sup> the paper suggested that "[the] circumstances are not prevalent, and thus, the absence of guidelines in these cases is not a major issue."<sup>164</sup> While considering various options, particularly in response to control transactions, the report recommended that no legislative changes be made in this area and that the courts be left to develop the concept of the "best interest of the corporation."<sup>165</sup>

In Australia, both the Parliamentary Joint Committee on Corporations and Financial Services<sup>166</sup> and the federal governmental Corporations and Markets Advisory Committee<sup>167</sup> concluded that Australian corporate law already affords sufficient basis for directors to consider the interests of stakeholders, including shareholders. Both rejected the desirability of legislative reform. The latter com-

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(2) May take into account ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business; and

(3) May devote a reasonable amount of resources to public welfare, humanitarian, educational, and philanthropic purposes.

162. Industry Canada, "Canada Business Corporations Act: Discussion Paper: Directors' Liability" (November 1995), online: Depository Services Program <<http://dsp-psd.pwgsc.gc.ca/Collection/C2-280-7-1995E.pdf>>.

163. Mindy Paskell-Mede & John Nicholl, "Directors' Liability from Private Rights of Action" (May 25, 1994) [unpublished], cited in *ibid.* at 15-16.

164. Industry Canada, *ibid.* at 16.

165. *Ibid.* at 18.

166. Austl., Commonwealth, Parliamentary Joint Committee on Corporations and Financial Services (PJCCFS), *Corporate Responsibility: Managing Risk and Creating Value* (Canberra: Senate Printing Unit, Parliament House, 2006), online: Parliament of Australia <[http://www.aph.gov.au/Senate/committee/corporations\\_ctte/completed\\_inquiries/2004-07/corporate\\_responsibility/report/report.pdf](http://www.aph.gov.au/Senate/committee/corporations_ctte/completed_inquiries/2004-07/corporate_responsibility/report/report.pdf)>.

167. Austl., Commonwealth, Corporations and Markets Advisory Committee (CAMAC), *The Social Responsibility of Corporations* (Sydney: CAMAC, 2006), online: <[http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFFinal+Reports+2006/\\$file/CSR\\_Report.pdf](http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFFinal+Reports+2006/$file/CSR_Report.pdf)>.

mittee noted that including a non-exhaustive list of interests to be taken into account, in the absence of guidance as to how such interests are to be prioritized and reconciled, could “make directors less accountable to shareholders without significantly enhancing the rights of other parties.”<sup>168</sup>

In contrast, the UK *Companies Act 2006* introduced a new statutory duty of loyalty that requires directors to “promote the success of the company for the benefit of its members as a whole” and, in doing so, take account of a range of statutorily prescribed considerations, including:

- (a) the likely consequences of any decision in the long term,
- (b) the interests of the company’s employees,
- (c) the need to foster the company’s business relationships with suppliers, customers and others,
- (d) the impact of the company’s operations on the community and the environment,
- (e) the desirability of the company maintaining a reputation for high standards of business conduct, and
- (f) the need to act fairly as between members of the company.<sup>169</sup>

There has been little judicial consideration of state constituency statutes. We are only aware of one instance in which such a statute has been referred to in finding in favour of a decision by an incumbent board.<sup>170</sup> It is not surprising that courts have shied away from the juridification of stakeholder interests; *BCE* illustrates the challenge. The UK statutory standard, while requiring (rather than permitting) directors to consider stakeholder interests, ultimately adjudges their deliberations based on whether their decisions “promote the success of the company for the benefit of its members [*i.e.*, shareholders] as a whole.”<sup>171</sup> The most one can reasonably expect of such a standard is to see judicial validation for long-term wealth creation, rather than a new locus for directorial accountability. Even those firmly wedded to shareholder value would concede this point.<sup>172</sup>

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168. *Ibid.* at 112.

169. *Companies Act 2006* (U.K.), 2006, c. 46, s. 172(1).

170. *Georgia Pacific Corp. v. Great Northern Nakoosa Corp.*, 727 F. Supp. 31 (N.D. Me. 1989), referred to in Richard Marens & Andrew Wicks, “Getting Real: Stakeholder Theory, Managerial Practice, and the General Irrelevance of Fiduciary Duties Owed to Shareholders” (1999) 9 *Bus. Ethics Q.* 273 at 284.

171. *Companies Act 2006* (U.K.), *supra* note 169, s. 172(1).

172. See *e.g.* Henry Hansmann & Reinier Kraakman, “The End of History for Corporate Law” (2001) 89 *Geo. L.J.* 439. Hansmann and Kraakman state that there is “no longer any serious competitor to the view that corporate law should principally strive to increase long-

In 2007, Oregon amended its *Business Corporations Act* to expressly permit an Oregon corporation's Articles of Incorporation to include a provision "authorizing or directing the corporation to conduct the business of the corporation in a manner which is environmentally and socially responsible."<sup>173</sup> While apparently intended to address "sustainability" concerns, the amending legislation does not purport to define "environmentally and socially responsible" conduct. Presumably, those utilizing this provision will take care in doing so, to avoid uncertainty or conflict with other corporate objectives.

## 2. REPORTING REQUIREMENTS

An expected corollary of the new statutory duty in the UK *Companies Act* was to have substantially enhanced social transparency through an annual Operating and Financial Review (OFR) requirement.<sup>174</sup> The OFR would be required of all "major companies" and would require directors to consider including material relevant to the interests of stakeholders, such as the company's policies relating to employment, environmental issues, and social and community issues relevant to the company's business.<sup>175</sup> However, as the bill went through parliamentary debates, the OFR requirement was withdrawn, leaving only the requirement to include in a public company's Annual Business Review "information about environmental matters ..., the company's employees, and social and community matters."<sup>176</sup> According to the statute, the purpose of the business review is "to inform members of the company and help them assess how the directors have performed their duty under s. 172."<sup>177</sup> Information about environmental, employee, and community matters is not required if, in the view of the directors, it does not assist in understanding the business of the company. Nor must directors state why such disclosure is not provided. The deletion of the OFR requirement

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term shareholder value" (at 439). See also Michael Jensen, "Value Maximization, Stakeholder Theory and Corporate Objective Function" (2001) 7 *Eur. Fin. Mgmt.* 297 at 309.

173. Or. Rev. Stat. § 60.047(2)(e) (2007). See also Perkins Coie, News, "Recent Oregon Legislation Addresses Corporate Social Responsibility" (8 January 2008), online: <[http://www.perkinscoie.com/news/pubs\\_detail.aspx?publication=1553&op=updates](http://www.perkinscoie.com/news/pubs_detail.aspx?publication=1553&op=updates)>.

174. U.K., Department of Trade and Industry, *Modernising Company Law* (Government White Paper, Cm 5553-1) (London: The Stationery Office, 2002).

175. *Ibid.* at 149, cls. 77, 78.

176. *Companies Act 2006* (U.K.), *supra* note 169, s. 417(5).

177. *Ibid.*, s. 417(2).

in the UK *Companies Act* was a disappointment to those who view social transparency as a way to influence norms of corporate conduct.<sup>178</sup>

There remains, however, ample ground for optimism, both as to the imposition of new social transparency requirements and their effect on corporate conduct. For example, the European Parliament's recent resolution on corporate social responsibility anticipates more expansive social transparency, "so that social and environmental reporting" are included alongside financial reporting requirements.<sup>179</sup> This observation was made having regard to the shortcomings of voluntary social reporting in which "only a minority [of the reports] use internationally accepted standards and principles, cover the company's full supply chain or involve independent monitoring and verification."<sup>180</sup>

In South Africa, the King Report (a voluntary governance code that was first published in 1994, revised in 2002, and revised again in 2009) advocates an integrated approach that takes into account the "triple bottom line": people, profits, and planet.<sup>181</sup> The King Report recommends that companies move away from profit maximization, and, in developing business strategies, focus on a broad range of stakeholders.<sup>182</sup> It recommends disclosure of the nature and extent of a company's commitment to social, ethical, safety, health, and environmental practices, as well as organizational integrity. While compliance is voluntary, most South African public companies follow the King Report's recommendations as a result of initiatives by various external sources to track and publish performance. For example, the Johannesburg Stock Exchange launched a Socially Responsible Investment (SRI) market index in May 2004, based on proprietary criteria, in keeping with the framework promoted by the UN *Principles for Responsible Investment*.<sup>183</sup> Major South African companies, including SAB

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178. See e.g. Cynthia A. Williams, "The Securities and Exchange Commission and Corporate Social Transparency" (1999) 112 Harv. L. Rev. 1197; Cynthia A. Williams & John M. Conley, "An Emerging Third Way? The Erosion of the Anglo-American Shareholder Value Construct" (2005) 38 Cornell Int'l L.J. 493.

179. EC, Committee on Employment and Social Affairs, *Report on Corporate Social Responsibility: A New Partnership* (Luxembourg: EC, 2006) at 10.

180. *Ibid.* at 9-10.

181. Institute of Directors in Southern Africa (IOD), *King Report on Governance for South Africa* (Cape Town: IOD, 2009), online: <<http://african.ipapercms.dk/IOD/KINGIII/kingiiiireport>>.

182. *Ibid.*

183. Principles for Responsible Investment (PRI) Secretariat, *Principles for Responsible Investment*, online: <<http://www.unpri.org/>>; Johannesburg Stock Exchange (JSE), *Social Responsibility*

Miller, AngloGold Ashanti, and Mondi actively report social responsibility initiatives on their websites. The King Report was also referred to by a South African court in finding that directors had breached environmental orders. The court specifically noted that the corporate community within South Africa has widely accepted the recommendations of the King Report, stressing that one of the characteristics of good corporate governance is social responsibility.<sup>184</sup>

The French *Code de Commerce* (*Commercial Code*) was amended in 2001 to require all French corporations listed on its primary stock exchange to report annually on social and environmental impacts.<sup>185</sup> This requirement was elaborated upon the following year by a decree which specifies categories of social, community-related, and environmental information that must be disclosed.<sup>186</sup>

Under the new *Social Responsibility for Large Businesses* law, which amended the Danish *Financial Statements Act*<sup>187</sup> as of 1 January 2009, an estimated 11,000 of the largest Danish companies (whether listed, private, or state-owned) are now required to include information on their corporate responsibility policies and practices in their annual financial reports. An absence of such corporate responsibility policies must also be reported. A stated objective of the legislation is to encourage large businesses "to work actively on ways they can contribute to solving social challenges."<sup>188</sup> This links to a longer-term governmental strategy, outlined in the May 2008 government "Action Plan on Corporate Social Responsibility."<sup>189</sup> The Action Plan stated the government's intention "to promote social responsibility and help Danish businesses reap more benefits from being at the global vanguard of corporate social responsibility."

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*Investment (SRI) Index*, online: <<http://www.jse.co.za/sri>>.

184. *Minister of Water Affairs and Forestry v. Stilfontein Gold Mining Co.*, [2006] ZAGPHC 47 (S. Afr. H.C. (Wit. Local Div.)).

185. *Code de Commerce*, Art. L225-102, as amended by *Loi n° 2001-420 du 15 mai 2001*, J.O., 16 May 2001, 7776.

186. See Lucien J. Dhooge, "Beyond Voluntarism: Social Disclosure and France's *Nouvelles Régulations Économiques*" (2004) 21 *Ariz. J. Int'l & Comp. L.* 441.

187. See The Danish Commerce and Companies Agency, *Proposal for an Act Amending the Danish Financial Statements Act (Report on Social Responsibility for Large Businesses)*, online: <[http://www.eogs.dk/graphics/Samfundsansvar.dk/Dokumenter/Proposal\\_Report\\_On\\_Social\\_Resp.pdf](http://www.eogs.dk/graphics/Samfundsansvar.dk/Dokumenter/Proposal_Report_On_Social_Resp.pdf)>.

188. *Ibid.* at 4.

189. Denmark, *Action Plan on Corporate Social Responsibility* (2008), online: <[http://www.eogs.dk/graphics/Samfundsansvar.dk/Dokumenter/Action\\_plan\\_CSR.pdf](http://www.eogs.dk/graphics/Samfundsansvar.dk/Dokumenter/Action_plan_CSR.pdf)>.

In 2008, the Australian Stock Exchange (ASX) adopted a new set of corporate governance principles that frame corporate citizenship issues within the notion of “material business risks.” Such risks are defined as follows:

Material business risks have the potential to create value and protect established value. The following examples of material business risk categories are identified in Principle 7: operational, environmental, sustainability, compliance, strategic, ethical conduct, reputation or brand, technological, product or service quality, human capital, financial reporting, [and] market-related risks.<sup>190</sup>

Listed companies must establish policies concerning “material business risk management” and disclose a summary thereof. According to the Corporate Governance Council, “[w]here a company has risks relating to sustainability or corporate social responsibility that are material to its business they should be considered in the context of [the revised reporting requirement].”<sup>191</sup>

In 2009, Australian authorities announced support for the establishment of the Responsible Investment Academy, designed to mount education and training programs to enable the investment community to better assess “environmental, social, and governance” (ESG) considerations.<sup>192</sup> A senior Australian Treasury official has also been appointed to the Global Reporting Initiative Governmental Advisory Group, with the Minister for Superannuation and Corporate Law noting: “it’s clear to me that the true value of corporate responsibility crystallizes around effective reporting.”<sup>193</sup>

Another recent example of a similar approach was that proposed by the Canadian Securities Administrators (CSA) in their request for comments on pro-

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190. ASX Corporate Governance Council, “Review of the Principles of Good Corporate Governance and Best Practice Recommendations” (2 August 2007) at 4, online: Chartered Secretaries Australia <[http://www.csaust.com/AM/Template.cfm?Section=ASX\\_Corporate\\_Governance\\_Council\\_guidelines&Template=/CM/ContentDisplay.cfm&ContentID=9231](http://www.csaust.com/AM/Template.cfm?Section=ASX_Corporate_Governance_Council_guidelines&Template=/CM/ContentDisplay.cfm&ContentID=9231)>.

191. ASX Corporate Governance Council, News Release, “Revised Corporate Governance Principles Released” (25 September 2008), online: CPA Australia <[http://www.cpaaustralia.com.au/cps/rde/xchg/SID-3F57FECA-1DFF2D2D/cpa/hs.xml/1017\\_23703\\_ENA\\_HTML.htm](http://www.cpaaustralia.com.au/cps/rde/xchg/SID-3F57FECA-1DFF2D2D/cpa/hs.xml/1017_23703_ENA_HTML.htm)>.

192. Australian Minister for Superannuation & Corporate Law, Media Release No. 009, “Government to provide assistance for establishment of responsible investment academy” (2 February 2009), online: Treasury Portfolio Ministers <<http://minscl.treasurer.gov.au/DisplayDocs.aspx?doc=ppressrelease/2009/009.htm&pageID=&min=njs&Year=&DocType=0>>.

193. Australian Minister for Superannuation & Corporate Law, Media Release No. 008, “Australian representative to join global reporting initiative” (5 February 2009), online: Treasury Portfolio Ministers <<http://minscl.treasurer.gov.au/DisplayDocs.aspx?doc=ppressrelease/2009/008.htm&pageID=&min=njs&Year=&DocType=0>>.

posals to replace their existing corporate governance regulatory regime.<sup>194</sup> The proposed, but recently abandoned, CSA National Policy 58-201: *Corporate Governance Guidelines*, articulated nine core "high-level corporate governance principles and [would have] provide[d] guidance to issuers on their corporate governance structures and practices."<sup>195</sup> In connection with the draft commentary to "Principle 5 – Promote Integrity," the CSA provided examples of generally recommended practices, including adoption of a code of conduct.<sup>196</sup> The CSA suggested that, in connection with the adoption of such a code of conduct, issues to be addressed should include "the issuer's responsibilities to security holders, employees, those with whom it has a contractual relationship and the broader community."<sup>197</sup>

Increasingly, public companies and their counsel are facing difficult judgment calls as to whether non-financial information concerning a company's environmental policies or social practices might be viewed as "material" under relevant securities laws.<sup>198</sup> For example, over the last several years, a number of investor groups, lead by CERES,<sup>199</sup> have sought to pressure the US Securities and Exchange Commission (SEC) to mandate climate change disclosure in public filings. CERES, along with the New York Attorney General, a number of state treasurers, pension fund managers, and others, petitioned the SEC on

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194. Canadian Securities Administrators, Ontario Securities Commission Bulletin, "Request for Comment – Proposed Repeal and Replacement of NP 58-201 *Corporate Governance Guidelines*, NI 58-101 *Disclosure of Corporate Governance Practices*, and NI 52-110 *Audit Committees* and Companion Policy 52-110CP *Audit Committees*" (2008) 31 OSCB 12158 (19 December 2008) [CSA, "Request for Comment"]. On 13 November 2009, the CSA announced their determination to not implement the proposals. Canadian Securities Administrators, Staff Notice 58-305, "Status Report on the Proposed Changes to the Corporate Governance Regime" (2009) 32 OSCB 9347.

195. CSA, "Request for Comment," *ibid.*, 58-201, App. B, Part I, 1.2.

196. *Ibid.*

197. *Ibid.* Curiously, CSA National Policy 62-202, *Take-Over Bids – Defensive Tactics* purports to remove many of the tools that a self-entrenching board might seek to invoke to favour non-shareholder constituencies.

198. See *e.g.* David Monsma & Timothy Olson, "Muddling Through Counterfactual Materiality and Divergent Disclosure: The Necessary Search for a Duty to Disclose Material Non-financial Information" (2007) 26 *Stan. Envtl L.J.* 137.

199. CERES (Coalition for Environmentally Responsible Economies) is a coalition of investors and public interest groups focused on improving corporate, environmental, and social performance. See online: <<http://www.ceres.org>>.

18 September 2007 to provide interpretive guidance on climate risk disclosure.<sup>200</sup> A supplemental filing on 12 June 2008 described subsequent developments from the date of the original petition.<sup>201</sup> The request was reiterated in a 28 October 2008 submission to the SEC in connection with its “21st Century Disclosure Initiative.”<sup>202</sup>

As of January 2010, the SEC has not officially responded to these submissions. However, the New York Attorney General (who was a signatory to the original CERES petition) issued subpoenas to five energy companies on 14 September 2007, questioning the adequacy of their climate change disclosure under New York securities law.<sup>203</sup> The subpoenas and subsequent investigations resulted in settlements with two of the companies, Xcel and Dynegy, in August and October 2008, respectively. Each company agreed to provide more detailed climate disclosure in their future SEC annual reports, including descriptions on present financial risks and probable regulation of greenhouse gas emissions, litigation, physical impact associated with climate change, and strategies to reduce climate change risks.<sup>204</sup>

Pressure on the SEC continues.<sup>205</sup> Most recently, the SEC’s Investor Advisory Committee has indicated its intention to establish a subcommittee to focus on disclosure of environmental, social, and governance (ESG) factors.<sup>206</sup>

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200. Petition to the US Securities and Exchange Commission for Interpretive Guidance on Climate Risk Disclosure (18 September 2007), online: <<http://www.incr.com//Document.Doc?id=187>>.
201. Letter from California Public Employees’ Retirement System *et al.* to Nancy M. Morris, US Securities and Exchange Commission Secretary (12 June 2008).
202. Letter from California Public Employees’ Retirement System *et al.* to Florence E. Harmon, U.S. Securities and Exchange Commission Acting Secretary (22 October 2008) (calling on the SEC to consider how material environmental, social, and corporate governance data can be integrated into public filings).
203. *Martin Act*, N.Y. Gen. Bus. Law §§ 352-c, 353 (allowing investigation of any “fraudulent practice” related to investments).
204. See *Re Xcel Energy Inc.: Assurance of Discontinuance Pursuant to Executive Law § 63(15)*, AOD #08-012 (N.Y. Att’y Gen., Envtl. Prot. Bureau 2008); *Re Dynegy Inc.: Assurance of Discontinuance Pursuant to Executive Law § 63(15)*, AOD #08-132 (N.Y. Att’y Gen., Envtl. Prot. Bureau 2008).
205. See *e.g.* Letter from Lisa Woll, CEO of Social Investment Forum, to Honorable Mary L. Schapiro, Chairman of United States Securities and Exchange Commission (21 July 2009), online: Social Investment Forum <[http://www.socialinvest.org/documents/ESG\\_letter\\_to\\_SEC.pdf](http://www.socialinvest.org/documents/ESG_letter_to_SEC.pdf)> (requesting increased ESG disclosure); Letter from Ceres’ Investor Network on Climate Risk to Honorable Mary L. Schapiro (12 June 2009), online: Investor Network on Climate Risk <<http://www.incr.com/Page.aspx?pid=1107>> (requesting improved disclosure



While the SEC has yet to issue guidance, the Canadian Institute of Chartered Accountants did so in late 2008.<sup>207</sup> This was followed by an Ontario Securities Commission (OSC) Staff Notice on environmental reporting which, based on a review of the continuous disclosure documents of thirty-five issuers, found a number of common deficiencies and issued guidance in respect thereof. The Staff Notice explicitly considers the materiality of environmental matters both from a financial statement and continuous disclosure perspective.<sup>208</sup> This approach may signal a convergence of legal and aspirational requirements, focusing on the "materiality" of non-financial information. Further, on 9 April 2009 the Ontario Legislature voted unanimously to support a private member's resolution calling for the OSC to consult and report back to the Minister of Finance on best practices on corporate social responsibility and ESG reporting standards.<sup>209</sup>

At the federal level in Canada, a private member's bill that is currently before the Standing Committee on Foreign Affairs and International Development would require companies in the resource sector that are receiving federal government support to "act in a manner consistent with international environmental best practices and with Canada's commitments to international human rights standards."<sup>210</sup> Already, the *Public Accountability Statements Regulations*,<sup>211</sup> which apply to Canadian banks, insurance companies, and trust and loan companies with equity of \$1 billion or more,<sup>212</sup> require the annual filing of a public account-

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of climate change and other risks); and Michael J. Kane, *Global Survey of Environmental, Social and Governance Policies with National Governments, International Organizations and Institutional Investors*, online: Association for Sustainable & Responsible Investment in Asia (ASrIA) <<http://www.asria.org/news/press/lib/>> (a useful survey of ESG policies recently compiled by the US Environmental Protection Agency).

206. *Global Proxy Watch* (31 July 2009), online: David Global Advisors, Inc. <<http://www.davisglobal.com/publications/gpw/index.html>>.

207. Canadian Institute of Chartered Accountants, *Building a Better MD&A – Climate Change Disclosures* (October 2008), online: Chartered Accountants of Canada <<http://www.cica.ca/research-and-guidance/mda-and-business-reporting/mda-publications/item12846.pdf>>.

208. Ontario Securities Commission (OSC), Staff Notice 51-716, "Environmental Reporting" (2008) 31 OSCB 2223 (29 February 2008).

209. Ontario, Legislative Assembly, *Official Report of Debates (Hansard)*, 39th Parl. 1st sess., No. 135 (9 April 2009) at 6051 (Laurel Broten raising a motion regarding corporate reporting).

210. Bill C-300, *An Act respecting Corporate Accountability for the Activities of Mining, Oil or Gas in Developing Countries*, 2d Sess., 40th Parl., 2009, cl. 3.

211. S.O.R. 2002-133 [PASR].

212. See *Bank Act*, S.C. 1991, c. 46, s. 459.3(4); *Insurance Companies Act*, S.C. 1991, c. 47, s.

ability statement. The statement must describe the entity's contribution to Canada's economy and society, including:

- 3(1) ...  
 ...  
 (c) detailed examples ...  
 (i) of their participation ... in activities for the purpose of community development ...,  
 (ii) of activities undertaken on their behalf during the period by their employees on a voluntary basis for the purpose of community development,  
 ...  
 (iv) of their philanthropic activities ...,  
 ...  
 (f) and an overview of initiatives undertaken ... to improve access to financial services for low-income individuals, senior citizens and disabled persons, ...<sup>213</sup>

In each of the above-noted instances, demands for disclosure reflect broader efforts to influence corporate conduct and governance. This approach is exemplified in a 2008 PricewaterhouseCoopers report, *Recasting the Reporting Model – How to Simplify and Enhance Communications*.<sup>214</sup> In advancing the case for “making sustainability mainstream,” the report suggests that “the interdependent relationship between existing financial data and other data (including social, customer, supplier and environmental indicators)” must be made clear, and that doing so “could have a transformational impact on reporting by ensuring that companies’ decision-making and strategy and investors’ valuations are based firmly on a more complete picture of performance.”<sup>215</sup>

### 3. REFORMING REGULATORY PARADIGMS

While beyond the scope of this article, it is worth noting the shifting role of what have traditionally been viewed as “economic” or “market” regulators in proactively advancing social goals. For example, Ontario’s *Green Energy Act*<sup>216</sup> adds to

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489.1(4); and *Trust and Loan Companies Act*, S.C. 1991, c. 45, s. 444.2(4).

213. *PASR*, *supra* note 211, s. 3(1).

214. PricewaterhouseCoopers, *Recasting the Reporting Model – How to Simplify and Enhance Communications: Opportunities for Discussion*, (2008) online: <<http://pwc.blogs.com/files/recasting-the-reporting-model---publication.pdf>>.

215. *Ibid.* at 5.

216. Bill 150, *An Act to enact the Green Energy Act, 2009 and to build a green economy, to repeal the Energy Conservation Leadership Act, 2006 and the Energy Efficiency Act and to amend other statutes*, 1st Sess., 39th Leg., Ontario, 2009 (assented to 14 May 2009), S.O. 2009, c. 12.

the mandate of the Ontario Energy Board the objectives of promoting conservation and renewable energy. By focusing on advancing environmental and social values and outcomes, the Act fundamentally shifts the focus of regulation from ensuring cost- and environmentally-efficient supply to regulating the energy sector as a contributor to the green economy.

### G. SHAREHOLDER-INITIATED APPROACHES

As public norms and expectations shift, corporations may choose to proactively clarify directors' duties, thereby conditioning the reasonable expectations of stakeholders. One Canadian example of such an exercise is Magna International Corporation. In 1984, its shareholders ratified a "Corporate Constitution," which set out certain principles, including guidelines for the allocation of profits between employees, shareholders, and management; the allocation of at least 7 per cent of pre-tax profit for research and development "to ensure [Magna's] long-term viability"; and the allocation of not more than 2 per cent of pre-tax profit for "charitable, cultural, educational and political purposes to support the basic fabric of society."<sup>217</sup> The constitution also provides that any amendments thereto require shareholder approval with each class of shares (Magna is controlled through three hundred vote shares) voting separately. Arguably in an effort to mitigate attempts to unionize plants, Magna also adopted an *Employee's Charter*, which focuses on job security, workplace safety, competitive compensation, and equity/profit participation.<sup>218</sup>

Such initiatives are not unique to Magna. For example, Casio Computer Co. Ltd. has established a "Charter of Creativity for Casio" and the "Casio Common Commitment," as described in Casio's 2008 Corporate Report.<sup>219</sup> This Charter embraces a number of norms, including corporate social responsibility, which is "said to be a matter of a company fulfilling its responsibility to all of its stakeholders in all important economic, environmental and social respects."<sup>220</sup>

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217. Magna International Inc., *Magna's Corporate Constitution*, online: <<http://www.magna.com/magna/en/responsibility/constitution/default.aspx>>.

218. Magna International Inc., *Magna International Inc. Employee's Charter*, online: <<http://www.magna.com/magna/en/responsibility/charter/default.aspx>>.

219. Casio Computer Co., Ltd., *Casio Corporate Report 2008* (N.p. 2008) at 5, online: <[http://world.casio.com/env/pdf/report\\_2008/Casio\\_05\\_ENG.pdf](http://world.casio.com/env/pdf/report_2008/Casio_05_ENG.pdf)>.

220. *Ibid.* at 5.

A more recent (and widely publicized) example was the initial public offering of Google. The prospectus included a letter from the founding shareholders which articulated a number of principles on which Google was based and which would continue to be maintained after the public offering (through a dual class share structure, under which the board and executive management team would control 61.4 per cent of the voting power). Commitments to serving end users, a long-term focus, and “making the world a better place” were set out in some detail in an effort to ensure that prospective investors would understand that “Google is not a conventional company [and it does] not intend to become one.”<sup>221</sup> The Google vision was expressed succinctly as follows: “We believe strongly that in the long term, we will be better served—as shareholders and in all other ways—by a company that does good things for the world even if we forego some short-term gains.”<sup>222</sup>

Such disclosure (arguably reinforced by shareholder approval or other validation) has proven to be consequential in determining director liability. In *Greenlight Capital Inc. v. Stronach*,<sup>223</sup> a case involving the conduct of Magna’s controlling shareholder in respect of a Magna spin-off company under identical control, the trial judge found such disclosure to be directly relevant to a determination of the subjective expectations of the shareholder plaintiff in the context of an oppression claim.<sup>224</sup> Given *BCE*, boards are likely to be advised to deliberately condition stakeholder expectations in order to insulate themselves in respect of oppression (and other) claims.

In recent years, shareholder activists have tested the limits of corporate law with by-law proposals that attempt to constrain the authority of boards of directors. Some commentators have argued that, to the extent that such proposals attempt to usurp authority for shareholders (who do not owe duties to advance the interests of the corporation) they should not be allowed.<sup>225</sup> Conversely, one law firm recently proposed that corporations amend advance notice by-laws governing shareholder proposals to include new, continuous disclosure obliga-

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221. Larry Page & Sergey Brin, “An Owner’s Manual for Google Shareholders” (2009), online: <[http://investor.google.com/ipo\\_letter.html](http://investor.google.com/ipo_letter.html)>.

222. *Ibid.* at 6.

223. (2008), 47 B.L.R. (4th) 215.

224. *Greenlight Capital Inc. v. Stronach* (2006) 22 B.L.R. (4th) 11 at para. 23.

225. Frederick H. Alexander & James D. Honiker, “Power to the Franchise of Fiduciaries” (2008) 33 Del. J. Corp. L. 749.

tions (beyond those contained under US securities laws) relating to beneficial ownership interests (intended to prevent activist shareholders from secretly accumulating a significant interest without disclosure).<sup>226</sup> The Dutch Parliament is currently considering legislation that would codify the recommendations of a Corporate Governance Code Monitoring Committee appointed by the Minister of Finance. The bill would impose substantive responsibilities on institutional shareholders, such as a requirement on holders of at least 3 per cent of a public company's voting shares to notify the regulatory authority on whether they agree with the firm's strategy.<sup>227</sup>

Lord Myners, the UK Finance Secretary, recently argued that voting rights might vary in proportion to the length of time that shares are held by the voting shareholder.<sup>228</sup> Such a proposal would follow the French model, under which ordinary shares double their voting rights if they are held by the same owner for a period of time specified in the company's charter (typically several years).<sup>229</sup> While the focus (attacking "short-termism") is laudable, we are not aware of evidence that such measures have been effective. The risk, again, is a diminution in board accountability.

Another approach to extending authority to shareholders would be through the use of unanimous shareholder agreements (USAs). Though, at common law, the discretion of directors in respect of their duties cannot be fettered,<sup>230</sup> a USA is a statutory exception to that common law principle. Arguments have been raised as to whether USAs can be used in public companies. This issue was

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226. Cravath, Swaine & Moore LLP, Bulletin, "Beneficial Ownership – By-law Disclosure Proposal" by Phillip A. Gelston & James C. Woolery (8 September 2008), online: Harvard Law School Forum on Corporate Governance and Financial Regulation <<http://blogs.law.harvard.edu/corpgov/files/2008/09/beneficial-ownership-by-law-disclosure-proposal.pdf>>; Michael J. de la Merced, "Shedding Light on Hidden Activists" *New York Times* (9 September 2008), online: <<http://dealbook.blogs.nytimes.com/2008/09/09/shedding-light-on-hidden-activists/>>.

227. See *Global Proxy Watch*, *supra* note 206.

228. "Short of Ideas – The Rights of Shareholders and the Wrong Done to Clients" *The Economist* (6 August 2009), online: <[http://www.economist.com/businessfinance/displaystory.cfm?story\\_id=14174485](http://www.economist.com/businessfinance/displaystory.cfm?story_id=14174485)>.

229. Tatiana Nenova, "How to Dominate a Firm with Valuable Control? Dual Class Firms Around the World: Regulation, Security-Voting Structure and Ownership Patterns" (SSRN Working Paper Series, April 2001), online: <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1017603](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1017603)>.

230. *Kennerson v. Burbank Amusement Co.*, 260 P.2d 823 (Calif. C.A. 1953); *Sherman & Ellis, Inc. v. Indiana Mutual Casualty Co. et al.*, 41 F.2d 588 (7th Cir. 1930).

analyzed in a 1996 discussion paper, which concluded that there is nothing in the Canadian statute that says USAs cannot be used in the context of a public corporation.<sup>231</sup> Section 146(1) of the CBCA states:

An otherwise lawful *written* agreement among *all the shareholders* of a corporation, or among all the shareholders and one or more persons who are not shareholders, that restricts, in whole or in part, the powers of the directors to manage, or supervise the management of, the business and affairs of the corporation is valid.<sup>232</sup>

As noted, there is no restriction with respect to the number of shareholders or type of corporation; if shareholders can reach a sufficient agreement, why should legislation interfere? Further, section 146(5) of the CBCA states:

To the extent that a unanimous shareholder agreement restricts the powers of the directors to manage, or supervise the management of, the business and affairs of the corporation, parties to the unanimous shareholder agreement who are given that power to manage or supervise the management of the business and affairs of the corporation have all the rights, powers, duties and liabilities of a director of the corporation, whether they arise under this Act or otherwise, including any defences available to the directors, and the directors are relieved of their rights, powers, duties and liabilities, including their liabilities under section 119, to the same extent.<sup>233</sup>

The USA would likely have to be created when a company is first set up and would have to be in place at the time of the initial public offering. The prospectus would provide full disclosure and state that the shares are subject to the USA, which prescribes a different governance framework than the statute. Share certificates would have to be legended accordingly. Section 146(4) of the CBCA provides that transferees of shares subject to a USA are deemed to be parties to the USA if they have notice of the agreement or a “reference to it is noted conspicuously on the security certificate.”<sup>234</sup> Thus, as a matter of corporate law, if the agreement is written, otherwise lawful, and unanimous, the aforementioned sections should be effective in creating a limited access arrangement between the corporation, directors, and shareholders. It is interesting to consider whether shareholders exercising some or all of the powers of directors through

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231. Parliamentary Information and Research Service, *Canada Business Corporations Act: Unanimous Shareholder Agreements* by Penny Becklumb (Ottawa: Library of Parliament, 2008), online: <<http://www.parl.gc.ca/information/library/PRBpubs/prb9932-e.pdf>>.

232. *CBCA*, *supra* note 4, s. 146(1) [emphasis added].

233. *Ibid.*, s. 146(5).

234. *Ibid.*, ss. 49(8), 146(4).

such an agreement would then be subject to statutory duties, as traditionally understood.<sup>235</sup>

Shareholders might also impose their will *ab initio* (or, arguably, at any time) by including provisions in a company's articles of incorporation that provide guidance to directors in the exercise of their duties. While, under the CBCA, this would not serve to relieve directors of their statutory obligations and potential liability, it might at least colour "reasonable expectations." In contrast, Delaware law generally allows corporate charters to contain "any provision ... for the conduct of the affairs of the corporation, and any provision creating, defining, limiting and regulating the powers of the corporation, the directors, and the stockholders ... if such provisions are not contrary to the laws of this State."<sup>236</sup> Moreover, Delaware allows charter provisions that eliminate managerial duty of care liability in damages.<sup>237</sup>

Each of the Australia and New Zealand corporation statutes contain a provision providing for a corporate constitution of a wholly-owned subsidiary to permit its directors to act in the best interests of the parent company.<sup>238</sup> It is questionable whether this represents a sanctioned departure from shareholder primacy or simply clarifies the identity of interests.

There is also growing evidence of the potency of shareholder advisory votes, particularly in respect of executive compensation practices. This is but one manifestation of the seminal and growing role of institutional investors in campaigning for improvements in corporate governance and conduct.<sup>239</sup> Various voluntary codes of conduct and business self-regulation have emanated from and are directed towards such investors.<sup>240</sup> John Bogle recently referred to the challenge

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235. It is difficult to reconcile a duty of directors to consider stakeholders' interests with the ability of shareholders to restrict the powers of directors.

236. Del. Code Ann. tit. 8, § 102(b)(1) (2009).

237. *Ibid.*, § 102(b)(7).

238. *Corporations Act 2001* (Cth.) (Australia), s. 187; *Companies Act 1993* (N.Z.), 1993/105, s. 131(2).

239. See e.g. Gordon L. Clark & Tessa Hebb, "Why Should They Care? The Role of Institutional Investors in the Market for Corporate Global Responsibility" (2005) 37 *Env't. Plan. A* 2015; Gordon L. Clark & Darius Wójcik, *The Geography of Finance: Corporate Governance in the Global Marketplace* (New York: Oxford University Press, 2007); and Stephen Davis, Jon Lukomnik & David Pitt-Watson, *The New Capitalists: How Citizen Investors are Reshaping the Corporate Agenda* (Boston: Harvard Business School Press, 2006).

240. See e.g. International Corporate Governance Network, *Global Corporate Governance Principles* (2005), online: <[http://www.icgn.org/files/icgn\\_main/pdfs/best\\_practice/global\\_principles/](http://www.icgn.org/files/icgn_main/pdfs/best_practice/global_principles/)

of establishing a “fiduciary society” based on statutory duties to focus on long-term investment, appropriate due diligence, and ensuring that “managers/agents ... act in a way that reflects their ethical obligations to society.”<sup>241</sup> Indeed, such manifestations of shareholder and popular sentiment are now informing legislative processes.<sup>242</sup>

#### IV. CONCLUSION

William T. Allen suggested long ago that “anyone trying to understand how our law deals with corporations must have in mind that they are the locus of many conflicting claims, and not all of those claims are wholly economic.”<sup>243</sup> He noted how the long-term/short-term distinction preserved the norm of shareholder oriented property theory, while affording directors considerable latitude to deal with other groups or institutions that have an interest in, or are affected by, the corporation. He concluded:

[I]n defining what we suppose a public corporation to be, we implicitly express our view of the nature and purpose of our social life. Since we do disagree on that, our law of corporate entities is bound itself to be contentious and controversial. It will be worked out, not deduced. In this process, efficiency concerns, ideology, and interest group politics will commingle with history (including our semi-autonomous corporation law) to produce an answer that will hold for here and now, only to be torn by some future stress and to be reformulated once more. And so on, and so on, evermore.<sup>244</sup>

In other words, the legal and economic frameworks of corporate governance are embedded in more basic values, attitudes, and beliefs. As former US Supreme Court Justice Earl Warren noted, “the law floats on a sea of ethics.”<sup>245</sup>

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2005\_global\_corporate\_governance\_principles.pdf>; UNEP FI, *Fiduciary Responsibility*, *supra* note 154.

241. John C. Bogle, “A Crisis of Ethic Proportions” *The Wall Street Journal* (20 April 2009) A19.

242. For example, the Australian Treasurer recently announced his government’s intention to amend the Australian *Corporations Act* to require shareholder approval for termination payments that exceed average annual base salary. See Rachel Pannett, “Australia to Rein in Executive Pay; Salaries, ‘Golden Handshakes’ Would be Put to Shareholders; Overregulation?” *The Wall Street Journal* (19 March 2009) C2.

243. William T. Allen, “Our Schizophrenic Conception of the Business Corporation” (1992) 14 *Cardozo L. Rev.* 261 at 280.

244. *Ibid.* at 281.

245. Noel Preston, *Understanding Ethics*, 3d ed. (Sydney: The Federation Press, 1996) at 21.



Likewise, Elhauge has forcefully argued that corporate law does and should confer managerial discretion to consider and, within reason, respond to social and moral sanctions because "there are residual areas beyond the reach of even optimally framed legal duties..."<sup>246</sup> Once framed in this manner, the challenge shifts to one of determining when, absent self-interested conduct, courts should constrain the exercise of such discretion.<sup>247</sup>

It has been argued that, in both *Peoples* and *BCE*, the Court may have reached to achieve a desired outcome—one arguably consonant with societal norms—without carefully articulating the underlying legal reasoning, and this has led to a diminution both in judicial clarity<sup>248</sup> and directorial accountability. In this article, some of the existing legal theories that the Court might have focused on to elaborate the responsibilities of directors have been presented, along with a consideration of potential legislative and shareholder-initiated reforms—any of which might add clarity to the law.

A reader of this article may reasonably assume that clarification of the law with respect to the role and accountability of directors necessarily involves a shift towards greater scrutiny of the interests that directors should consider and also towards directors' commitment to long-term value maximization. While this reflects the authors' bias, it need not be the case. For example, clarity with respect to the role and accountability of directors could involve establishing that the role of directors should be a singular focus on maximizing wealth creation for the benefit of the current shareholders, with the safeguarding of other interests left to political and social forces.<sup>249</sup>

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246. Elhauge, *supra* note 12 at 743.

247. For example, the American Law Institute suggests that courts should sustain decisions to sacrifice profits for ethical principles when such principles are reasonable because they "have significant support although less-than-universal acceptance." American Law Institute, *supra* note 161 at s. 2.01 (comment (h)). David Engel, however, suggests a more stringent standard, based on broad social consensus. David L. Engel, "An Approach to Corporate Social Responsibility" (1979) 32 *Stan. L. Rev.* 1 at 27-34.

248. Ian Lee points out that the Court's approach in *Peoples* "obscures the choice actually faced by the court and the normative considerations relevant to that choice," adding that, "[i]n this way, it is an example of the kind of reasoning that realist scholars persuasively criticized in the last century." Lee, *supra* note 48 at 220, n. 37. See also Felix S. Cohen "Transcendental Nonsense and the Functional Approach" (1935) 35 *Col. L. Rev.* 809.

249. See *e.g.* Reich, *supra* note 101.

Ultimately, the determination of proper corporate purpose, duties of directors, and directors' discretion and accountability depends on an understanding of the role of the corporation in our society. Is a legal construct that has and continues to hold the potential to transform our world really one that we want to hinder? If not, how best can we focus the role of directors (or others assigned with legal duties and accountability) on ensuring that corporations generate wealth within the context of broader societal values? Equally, how do we focus the "watchful eye," referred to by President Obama, to ensure an effective oversight role and ultimate responsibility for wealth distribution?

Never before have the duties owed by directors attracted such political currency. Sadly, the Supreme Court of Canada has now missed two opportunities to address these issues in the context of corporate law. Perhaps, in venturing into the realm of social responsibility, it was "being too far ahead" of its time—if so, only by not going deep. The theoretical basis for a shift to directors taking a broader and longer-term view of corporate responsibilities is compelling. There is no shortage of legal theories by which such conduct could be encouraged or required. Hopefully, others will soon provide greater clarity.