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Personal Liability of Directors and Officers under the Forest and Range Practices Act –

The Case of *Smurthwaite v. Government of British Columbia et al.*

Introduction

Late last November the Forest Appeals Commission (the “Commission”) released its decision in the case of *Smurthwaite v. Government of British Columbia et al* (Appeal No. 2005-FOR-015(a)). At issue was the personal liability of a corporation’s directors and officers under s-s.71(4) of the *Forest and Range Practices Act* (“FRPA”):

If a corporation contravenes a provision of the Acts, a director or an officer of the corporation who authorized, permitted or acquiesced in the contravention also contravenes the provision.

This case is interesting both for its factual context and legal discussion.

Background

The licensee was a corporate participant in the British Columbia Timber Sales program, and held timber harvesting rights under a timber sale license. Numerous “karst” features were in the vicinity of the licensee’s road construction activities, and the licensee was required to protect those features. The licensee retained a contractor to perform harvesting and road construction operations on the licensee’s behalf. Before road construction commenced, representatives of the licensee, the contractor, and Ministry of Forests and Range (“MoF”) attended a pre-work meeting and, among other things, discussed the need to protect the karst features. In spite of this, many of the karst features were either severely damaged or destroyed during the course of the contractor’s road construction activities.

The MoF investigated the incident for noncompliance with s-s.62(1) of the *Forest Practices Code of British Columbia Act*. The correspondence and inspection reports referenced the names of the licensee and the sole officer and director of the licensee (the “Appellant”) in the address. Similarly, the MoF’s compliance and enforcement investigation report named the licensee but also referenced the Appellant’s name. The delegated decision maker (the “District Manager”) offered an opportunity to be heard in respect of the matter, and the

This article provides a general overview and does not constitute legal advice. Persons requiring further information or advice should contact Jeff Waatainen at 250.758.9485 or jeff@bcforestrylaw.com.

Appellant presented a submission on behalf of the licensee to the District Manager. The Appellant acted throughout as though the proceedings related to a garden variety case of a licensee's vicarious liability for the contraventions of its contractor.

Very much to the Appellant's surprise, the District Manager found that the Appellant was, himself, personally liable in his capacity as a director and officer of the licensee for the contravention, and imposed a \$45,000 administrative penalty against him (90% of the maximum available under the circumstances). This was notwithstanding that:

- at no time before the determination did the MoF explicitly or implicitly indicate that the Appellant, in his personal capacity, was the MoF's target;
- at no time did the MoF so much as reference s-s.71(4) of FRPA;
- the MoF presented no evidence that the Appellant "authorized, permitted, or acquiesced" in any contravention as required under s-s.71(4) of FRPA;
- the submissions of both parties at the opportunity to be heard were entirely focused on the licensee's liability, and the Appellant was obviously under the impression that the licensee's potential liability was the issue, rather than his own.

The Appellant appealed the determination to the Forest Appeals Commission. Not only did the MoF decide to defend the determination in spite of its obvious legal defects, the Forest Practices Board (the "Board") also decided to join in and make a test case out of it.

The MoF and the Board relied upon a variety of arguments in their efforts to overcome the defects in the determination:

- given that the salutations and addresses on the correspondence and documentation associated with the MoF's investigation included the Appellant's name along with that of the licensee, the MoF and Board argued that the Appellant should have known that he was personally the subject of the proceedings even though nothing in the documentation or correspondence mentioned this, or included a simple reference to the provision in FRPA that provides for director and officer liability;
- the Board and the MoF argued that the Appellant did get to participate in an opportunity to be heard, even though the focus of that opportunity was entirely on the question of the licensee's liability and had nothing to do with the potential liability of the Appellant;
- even if the Appellant did not get an opportunity to be heard before the District Manager to defend himself against personal liability as required under FRPA, the Board and the MoF argued that the appeal now afforded him the opportunity to do so, and the Commission could thereby cure any defects associated with the determination.

This latter argument was particularly troublesome from the Appellant's perspective: if the MoF wanted to assess a penalty under FRPA against the Appellant personally, it was required to do so within a three year limitation period. But before the MoF could impose an administrative penalty, the Appellant was entitled to receive an opportunity to be heard regarding his personal liability, also within that limitation period. By the time of the appeal, the limitation period had expired. To simply forego the statutory requirement for an opportunity to be heard on the basis that the Commission could allow the Appellant to defend himself

against personal liability on appeal and thereby cure that omission would deny the Appellant the benefit of the statutory limitation period altogether.

The Decision

There is not much more to add to the Commission's words:

There is no discussion of any evidence establishing that Mr. Smurthwaite authorized, permitted or acquiesced in the Company's alleged contravention. Consequently, it is unclear as to how the District Manager arrived at his conclusion that Mr. Smurthwaite was liable in his capacity of president of the Company, or whether the District Manager even considered the second stage of the test set out in s-s.71(4) of the Act [whether the Appellant authorized, permitted or acquiesced in a contravention]. ...

Accordingly, there is no evidentiary basis for the determination against Mr. Smurthwaite in his capacity as an officer and director of the Company, nor is there a basis upon which the Commission could evaluate the case against him. On this basis alone, the Commission would allow the appeal.

The Commission went on to state:

In light of the complete failure to notify Mr. Smurthwaite of the possible determination under section 71(4), the complete failure to comply with a statutory requirement to give Mr. Smurthwaite an opportunity to be heard on his role in the alleged contravention(s) ... the Commission finds that the determination cannot be corrected by the Commission, nor would it be appropriate, or even possible in this situation, for the Commission to decide whether Mr. Smurthwaite is liable under section 71(4) of the Code [G]iven the nature of the errors in this case, the Commission is of the view that it does not have the jurisdiction to correct the errors or to send the determination back to the decision-maker. The determination is fundamentally flawed.

Essentially, the Commission found that the MoF had made such a mess of things that the Commission could not possibly fix the determination. Accordingly, the Commission rescinded the determination and the \$45,000 penalty levied against the Appellant personally.

Why It's Important

While the Commission's decision confirms some basic principles (for example, the need to actually tell someone whether his or her personal liability is the subject of a pre-determination hearing, or the idea that the statutory prerequisites of an administrative penalty are actually important), this is not why the decision is significant. These sorts of errors were not the result of any meaningful uncertainty in the law; they simply reflected a disregard for the law.

However, there are still a couple of important points that come out of this decision.

The Nature of Director and Officer Liability

First, the Commission clarified that under s-s.71(4) of FRPA the liability of a director or officer for the contraventions of a corporation is different than the liability of a licensee for the acts of its contractor under s-s.71(3):

[T]he Commission finds that the Legislature intended that there must be some factual basis [under s-s.71(4)] for concluding that a corporate director or officer “authorized, permitted or acquiesced in” the corporation’s contravention. Under section 71(3), liability is direct: as long as the contractor, employee or agent contravened the Acts while acting in the course of carrying out the contract, employment or agency, the person (in this case a corporation) also contravenes the Acts. In contrast, section 71(4) does not impose liability on corporate directors or officers simply by virtue of the corporation contravening the Acts in the course of its operations; rather, a director or officer must have authorized, permitted or acquiesced in the contravention. The onus is on the Ministry ... to establish that the director or officer “authorized, permitted or acquiesced in” the corporation’s contravention.

The MoF must do more than simply prove that a corporation contravened the legislation to impose liability on a director or officer of the corporation, unlike the case of a licensee’s liability for the contraventions of its contractor where proof of the contractor’s contravention is proof of the licensee’s contravention. The Ministry must provide additional evidence that the director or officer actually “authorized, permitted or acquiesced in” the contravention. Moreover, the MoF must make a formal finding that the corporation, itself, actually contravened the legislation: “mere assertions” or a “casual finding” are not sufficient. In this case, the MoF did not bother with either requirement.

Director and Officer Due Diligence

The most important aspect of this decision is the Commission’s commentary on the application of the phrase “authorized, permitted or acquiesced” under s-s.71(4) of FRPA. While the Commission did not have to apply the phrase under the circumstances given the complete absence of evidence in relation to the appellant’s personal culpability, the Commission nevertheless set out a test with respect to the application of s-s.71(4) of FRPA:

[T]he Commission concludes that the words “authorized, permitted or acquiesced in the contravention” include both positive acts and omissions such as a failure to prevent a **foreseeable** occurrence that leads to a contravention. In particular, “permit” includes a “passive lack of interference,” through inaction or omissions, on the part of a director or officer who **should have foreseen** an occurrence leading to a contravention. The statutory language does not import a mental element in terms of an intention to commit the contravention or knowledge that the contravention would actually occur, but it does require that the director or officer had the power to control whether the contravention occurred. ... [S]ection 71(4) requires ... that a corporate director or officer failed to prevent an occurrence which he or she **ought to have foreseen**. [Emphasis added.]

The significance of the Commission’s approach is that it casts a broader net than directors and officers may have expected. The Commission indicated that s-s.71(4) will not only apply in circumstances where a director or officer expressly authorized or permitted a contravention, or was willfully blind with respect to contravention, but may also apply where the director did not, in fact, have any real knowledge of a potential contravention but “should” or “ought” to have known about it. The test of whether a director or officer “authorized, permitted or acquiesced” is not only based upon actual, subjective knowledge, but is also based upon objective knowledge – what a director or officer ought to have known in the circumstances. In other words, the standard is akin to liability under the law of negligence.

Closing Comment

If the Commission does follow this approach, the consequence is that directors and officers of a corporation will, effectively, have to establish due diligence with respect to their own, personal conduct to ensure that they are not personally liable under s-s.71(4) for any noncompliance of the corporation. Further refinements to the Commission's comments are still necessary to determine what this will involve in any particular circumstances. For example, the question of what a director or officer of a major licensee with a million cubic metres of annual allowable cut "ought" to know is probably something different than the knowledge expected of the sole director and officer of a small numbered company that is merely that person's corporate persona. In any event, though, due diligence on the part of the director or officer appears necessary.

Finally, I cannot help but suggest that this is another example of the problems with the Commission's restrictive approach towards costs. Given the Commission's policy against awarding costs other than in the most egregious circumstances, the MoF and the Board were able to defend this appeal without any fear of an adverse costs award even though, based on the Commission's decision, the determination was "fundamentally flawed" and clearly indefensible. While the MoF and the Board would likely argue that it is in the public interest for them to test the application of a provision of FRPA such as s-s.71(4) that has received little attention to date, the problem is that they did so at the expense of a private person in circumstances where they had no case. This is not to say that the Commission should award costs to all successful parties as a matter of course; but some credible threat of an adverse costs award should exist to discourage the MoF and the Board from forcing an appellant to incur the costs of an appeal in circumstances where the MoF and the Board have no real prospect of success.