

# Meridian Compensation Partners Client Update



## Canadian Regulatory and Governance Update

There have been a number of recent regulatory and governance changes affecting executive compensation and governance.

### Canadian Developments

#### **1. Canadian Securities Administrators Publish “Guidance for Proxy Advisory Firms”**

On April 24<sup>th</sup>, the CSA published for comment their proposed Policy for proxy advisory firms. The Policy sets out recommended practices that the CSA believes (but does not require) proxy advisors should adopt, designed to promote transparency and understanding by market participants about the activities of proxy advisory firms.

There are 4 main areas covered by the Policy:

#### **A) Conflicts of Interest**

The Policy states that conflicts of interest must be effectively mitigated, and cites 3 examples of conflict:

- i. Proxy advisory firm provides vote recommendations in respect of a client for whom they provide consulting services
- ii. An investor client submits a shareholder proposal that could be the subject of a favorable vote recommendation by the proxy advisory firm
- iii. A proxy advisory firm is owned by an investor client that invests in issuers where the proxy advisory firm makes recommendations (this will apply to Glass Lewis and, after the impending acquisition by Vestar, also to ISS)

The Policy does not, however, provide detailed guidance on how such conflicts could be mitigated, and potentially leaves the meaning of “mitigation” open to interpretation, in this context.

#### **B) Transparency and Accuracy of Vote Recommendations**

The CSA expects that vote recommendations of proxy advisors should be transparent, the underlying information be accurate and vote recommendations be consistent, based on proxy voting guidelines. The CSA recommends that proxy advisors:

- i. Have written policies describing their approach/methodologies
- ii. Design internal safeguards to ensure that information is accurate
- iii. Disclose their policies and safeguards

#### **C) Proxy Voting Guidelines**

Proxy voting guidelines should be developed in a consultative and comprehensive manner and proxy advisors should publish their proxy voting guidelines and explain their rationale.

#### **D) Communications with Clients, Market Participants, Media and Public**

The CSA expects proxy advisors to:

- i. Disclose to their clients: conflicts, methodologies and weighting, factual vs. analytical information, which guidelines are used, the outcome of any dialogue with the issuer, any limitations in the research or analysis, and that the recommendations are intended solely as guidance

- ii. Publicize policies on dialogue with issuers
- iii. Correct factual errors
- iv. Have a communication policy
- v. Have a contact person for communications
- vi. Describe their communication policy

The Policy is open for comment until June 23, 2014.

**Meridian Comment:** It is important to note that this policy is a recommended self-regulatory scheme, rather than a rules-based regulatory framework. Glass Lewis and ISS both have existing policies and procedures designed to address many of the issues raised by the CSA. There is little in the guidance that is likely to cause significant change in how proxy advisors operate. For proponents of proxy advisor regulation this policy may be interpreted as rather benign. It remains to be seen whether proxy advisors will adjust their practices and whether issuers will agree that such policies and procedures are adequate.

## 2. *New Majority Vote Requirements for TSX Companies*

New Toronto Stock Exchange rules will require all TSX-listed issuers to adopt majority-voting for director elections. The requirement is effective at the end of June 2014 and expands a 2012 requirement that directors stand for individual election, rather than as a slate. The rule requires companies to have policy that:

More than **95%** of the **S&P/TSX 60** already have a majority vote standard for director elections; almost **70%** also include mandatory resignation policies.

- A director must immediately tender his or her resignation if not elected by a majority of the votes cast
- The board must accept the resignation absent exceptional circumstances
- The board must decide within 90 days whether to accept the resignation
- The board's decision must be announced promptly by news release which must fully explain any decision not to accept resignation

Companies with a controlling shareholder are exempt from the new requirement, but must annually disclose their reasons for not adopting a majority vote policy.

## 3. *OTPP Publishes Updated 2014 Proxy Voting Guidelines*

Ontario Teachers' Pension Plan has changed its say-on-pay voting guidelines. OTPP will address resolutions on a case by case basis, and may vote AGAINST say-on-pay in any year, and vote AGAINST board members where there is an "extreme" disconnect between pay and performance.

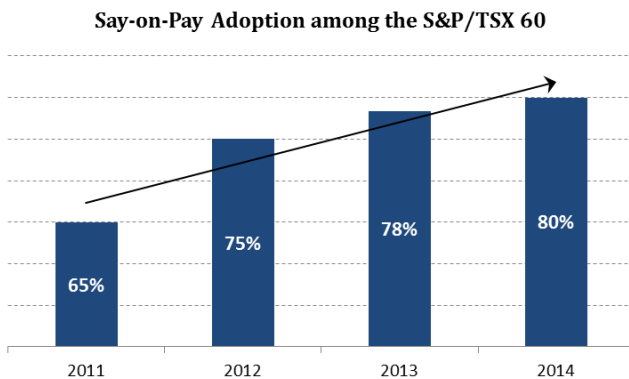
Previously, OTPP had an escalating approach which called for:

- supporting the resolution in the first year of say-on-pay (and follow-up with concerns);
- voting FOR or AGAINST say-on-pay in the second year, and
- voting FOR or AGAINST compensation committee members in the third year (depending on the board's actions to address concerns brought forward by the OTPP)

OTPP has made a number of other changes to its proxy voting guidelines, including a stated expectation that boards demonstrate a "commitment to diversity".

#### 4. Still No Requirements for Say-on-Pay Vote

In January 2011, the OSC issued a staff notice seeking comments on shareholder democracy issues, including say-on-pay. Investors and issuers were divided on the issue of adopting mandatory say-on-pay votes. To date, there has been no word from the OSC as to whether it will require advisory say-on-pay resolutions.



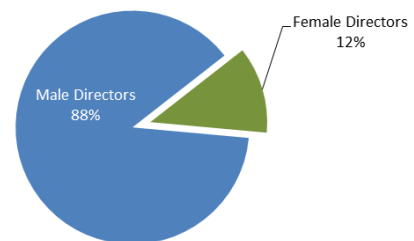
Meanwhile, the number of Canadian companies voluntarily adopting say-on-pay continues to increase, with 80% of the S&P/TSX 60 companies having adopted advisory votes. More broadly, however, only about 3% of Canada's public companies have adopted say-on-pay, so practice at Canadian companies has not made regulation moot.

#### 5. Proposed Disclosure for Board Gender Diversity and Term Limits

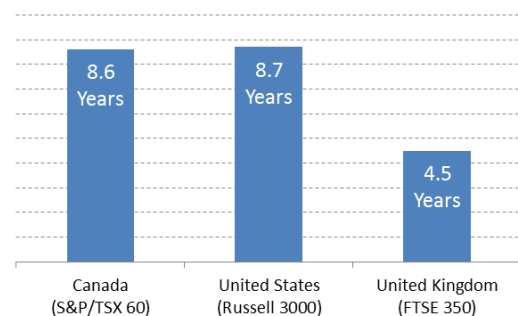
The Ontario Securities Commission has proposed disclosure of director term limits and gender diversity. The proposed “comply or explain” regime could require TSX-listed issuers in Ontario to disclose:

- Director term limits, and if the company has not adopted term limits, to disclose why it has not
- Policies regarding women on the board
- The board's consideration of the representation of women in the director identification and selection process
- The company's consideration of the representation of women in executive officer positions when making executive officer appointments
- Targets regarding the representation of women on the board and in executive officer positions
- The number of women on the board and in executive officer positions

**Director Gender Diversity at Large Canadian Companies**



**Average Director Tenure at Large Public Companies**



These proposals are ahead of those in place in other countries. The comment period for the proposed amendments closed April 16, 2014, but an effective date has not yet been announced.

### International Developments

#### 6. United States: SEC Rulemaking

The Securities and Exchange Commission still expects to adopt final rules in 2014 for disclosure of the ratio of CEO pay to median employee pay. The SEC has received over 127,000 comment letters. Concerns continue about inclusion of non-U.S. employees in the pay ratio calculation, the cost to calculate

the ratio, and data privacy. Even if the new rules were finalized soon, most companies will not need to disclose the CEO pay ratio until the **2016** proxy season.

The SEC has confirmed its intention to propose rules during 2014 for all other outstanding Dodd-Frank mandates, including:

- Pay-for-performance proxy disclosure (disclosure of compensation “actually paid”)
- Mandatory (no-fault) executive compensation “clawback” policies
- Disclosure of stock hedging/pledging policies

### ***7. European Union: EU Commissioner Proposes Greater Pay Transparency***

The European Commission will propose new measures designed to strengthen corporate governance and disclosure of executive pay at 10,000 companies listed on Europe’s stock exchanges. The planned changes include:

- A requirement to disclose clear, comparable and comprehensive information on remuneration policies and how they were put into practice. Policies must include an explanation of how they contribute to the long-term interests and sustainability of the company, and a maximum level for executive pay. Companies would have to explain the ratio between average employees and executive pay, but there would be no binding cap on remuneration
- Companies must put their remuneration policy to a binding shareholder (say-on-pay) vote
- Transparent disclosure on the methodologies used by proxy advisors for their voting recommendation and on how they manage conflicts of interests
- Companies would have to disclose more details of dealings between a company and its management, i.e., related party transactions, and some would require shareholder approval

The proposals are not likely to be settled until late 2015 at the earliest.

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