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Meridian Client Update

Board Leadership at Canadian Companies

Board Leadership Structures

There are four types of Board leadership structures at Canadian public companies:

- **CEO Chair**—The CEO also serves as the Chair of the Board, generally for no additional compensation. This combination of roles is uncommon among large Canadian companies, but still very prevalent in the U.S. and at small to mid-size Canadian public companies.
- **Executive Chair**—The former CEO may serve as Chair of the Board, with a special/transitional role. Executive Chairs are paid similar to officers and their compensation may be included in the summary compensation table. In Canada, Executive Chairs are generally transitional, rather than permanent appointments. Typically they facilitate the transition of a departing CEO, provide developmental assistance to an incoming CEO or provide recognition to a founding CEO.
- **Independent (Non-executive) Chair**—An independent member of the board serves as the Chair. Independent Chairs are paid as outside directors, and generally receive a substantial additional retainer. This is the most common form of Board leadership at large Canadian companies. This is supported by the Canadian Coalition for Good Governance and is viewed as a good practice by proxy advisors.
- **Lead Director**—If the Chair is not independent, an independent director is often appointed as lead director. Lead directors generally focus on issues of governance and process to provide a level of independence that an executive or CEO Chair does not. Lead directors are paid as directors, but generally receive a small additional retainer reflective of the role, not unlike Committee Chairs.

Compensation of Chairs

An Executive Chair is an officer of the company. Former CEOs often have modest changes to their compensation during this transition. In general:

- Executive Chairs are paid significantly more than Independent Chairs. In fact, median Executive Chair pay is about 9x the median Independent Chair pay at S&P/TSX 60 companies.
- Compensation for Executive Chairs is specific to the role and varies significantly across companies. Similar to CEO compensation, company size and the particular incumbent influence compensation.
- Independent Chairs receive a significant pay premium. The median annual pay for an Independent Chair, in addition to regular director compensation, is \$225,000, at S&P/TSX 60 companies.

Lead Directors receive a small pay premium, even at larger companies where those roles are becoming more like Independent Chairs. S&P/TSX 60 Lead Director premiums vary significantly and are approximately 30% of the premiums paid to Independent Chairs. Median incremental pay is \$60,000.

Governance Issues

Some of the concerns with combining the roles of CEO and Chair are:

- A CEO Chair is in the position to control the board agenda, review the performance of directors and influence nominations to the board. This may give the CEO substantial influence over the board to whom the CEO reports.
- The role of the CEO is to supervise management and the role of the Board (and the Board Chair in particular) is to supervise the CEO. Having the CEO as the Chair of the Board can compromise this fiduciary oversight role.
- A CEO Chair's role and accountability shift, depending on the capacity in which the CEO Chair acts, which may not be clear to third parties, particularly in the context of mergers and acquisitions.

The Canadian Coalition for Good Governance, in their 2010 policy "Building High Performance Boards" recommends that the role of CEO and Chair of the board be **separate** and that the CEO be asked to resign from the board at the end of his or her CEO tenure.

The prevalence of combined CEO/Chair roles at S&P/TSX 60 companies is substantially lower than leading companies in the US. However, at least anecdotally, we see that at Canadian companies below S&P/TSX 60 the prevalence of combined roles tends to be higher.

Proxy Advisor Views on Board Leadership

Both ISS and Glass-Lewis favour a separate Chair and CEO, and will generally vote in favor of shareholder-led proposals in Canada and the U.S. calling for a separation of the CEO and Chair roles, with the Chair being an independent director.

Meridian Comment

There are a number of board leadership models each of which may be suitable in different circumstance, each with a different compensation structure. Companies should explain to shareholders the business rationale for their choice of Board leadership and the related compensation.

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