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Meridian Client Update

Regulatory and Governance Update—Canadian Developments

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

Mandatory Say on Pay Remains Unlikely

The Canadian voluntary Say on Pay regime appears unlikely to change soon, although voluntary adoption continues to increase with 127 companies and 82% of the TSX 60 adopting say on pay. Early in 2011, the OSC issued a staff notice seeking comments on shareholder democracy issues, including the development of regulatory proposals relating to Say on Pay. Investors and issuers appear divided on mandatory Say on Pay votes and the OSC has yet to publish any results or clarify whether a change is expected.

Increasing Pressure on Public Companies to Appoint More Women to Boards

The Ontario Securities Commission (OSC) issued a consultation paper on disclosure designed to advance the representation of women on boards and in senior management. Disclosure would include issuers' policies regarding female representation on boards and in senior management, representation of women in the director selection process and quantitative information regarding the representation of women in the organization. The model disclosure requirements will be open for public comment until September 27, 2013 and applies to large TSX traded companies.

Meridian comment: The OSC's proposal does not call for quotas, but would be part of the Corporate Governance Disclosure rules "comply or explain" regime with no target levels set, similar to the Australian model. The U.K. has issued guidelines urging large companies to aim for 25% women on their boards.

CSA's Priorities Include Shareholder Democracy

The Canadian Securities Administrators (CSA) released its Three-Year Business Plan, which sets out the priorities of the CSA over the next three years, including shareholder democracy and protection. This includes reviewing Canadian proxy infrastructure and assessing whether regulatory intervention is required with respect to activities of proxy advisory firms. This stated focus is interesting given that the CSA has not yet published results from its last year's consultation paper concerning the regulation of proxy advisory firms.

Guidance on Director Election Requirements

The TSX provided some guidance on its new rules for the election of directors. The rules require that shareholders elect directors individually on an annual basis and that issuers disclose the voting results. The TSX suggests that issuers disclose the following in a news release: (i) the percentages of votes received "for" and "withheld" for each director; (ii) the total votes cast by proxy and ballot, together with the number that each director received "for"; or (iii) the percentages and total number of votes received "for" each director.

CCGG's Upcoming Initiatives

At its annual general meeting held in June 2013, the Canadian Coalition for Good Governance (CCGG) outlined its current initiatives: a policy on dual class share structures, and an updated version of Building High Performance Boards.

Results of Continuous Disclosure Review Program

The results of the CSA's continuous disclosure review program for 2013 have:

- 47% of issuers reviewed required to take some action to improve disclosure.
- 26% of issuers reviewed expected to provide enhanced disclosure in future filings, including on executive compensation

International Developments

SEC may Adopt Rule on CEO Pay Ratio Disclosure "in the Next Month or Two"

The Securities and Exchange Commission (SEC) may be voting on a proposed rule on the CEO pay ratio disclosure required under the Dodd-Frank Act later this month, according to comments by SEC Chair Mary Jo White. However, a bill to repeal this disclosure requirement is pending in Congress.

Meridian comment**:** The controversy around CEO pay ratio disclosure continues. Businesses and trade groups have criticized the disclosure and urged its repeal, but the new SEC Chair has stated that the Commission has no "higher priority" than to complete rulemaking under Dodd-Frank. Any proposed rule would be subject to a public comment period, so it seems unlikely that disclosure will be effective for the 2014 proxy season given the complexities that many companies will face in complying with the CEO pay ratio disclosure requirements.

SEC Commissioner Raises Concerns about Institutional Shareholders "Blindly" Following Proxy Advisory Firms' Vote Recommendation

In remarks before a professional trade group on July 11, 2013, SEC Commissioner Daniel Gallagher criticized institutional shareholders' over-reliance on vote recommendations by proxy advisory firms and called for "Commission-level guidance" on institutional shareholders' proxy voting responsibilities and a review of the "role and regulation" of proxy advisory firms.

Meridian comment: The role of the proxy advisory firms in corporate governance has been on the SEC's radar screen for several years, but the SEC has not taken any regulatory action. Perhaps Commissioner Gallagher's comments will re-ignite the discussion on oversight of proxy advisory firms.

ISS Recommends Against Four McKesson Board Members Due to Pay Issues

Institutional Shareholder Services (ISS) rarely recommends that shareholders vote AGAINST members of a compensation committee because of executive pay issues, but did recommend that shareholders vote against the compensation committee of McKesson Corporation based on a number of continuing problematic pay practices.

Meridian comment: The McKesson vote reminds companies that problematic pay practices that go unattended or are inadequately addressed over multiple years will likely lead to a loss of ISS support for compensation committee members.

U.K .Government Proposes Binding Say on Pay

On June 24, 2013, the U.K. government presented "final draft" regulations requiring that shareholders have a **binding** vote on a listed company's remuneration policy, focusing primarily on the compensation of directors who serve as executive officers of the issuer. The regulations would apply to all U.K. incorporated companies listed with the U.K. Listing Authority, a European Economic Area member-state, NYSE or NASDAQ. The regulations would apply to any remuneration report presented for approval at a shareholders meeting held in fiscal years beginning on or after October 1, 2013.

Meridian comment: The U.K. has long been a leader in the development and evolution of Say on Pay. The proposed legislation takes a significant evolutionary step by introducing "binding" Say on Pay. In essence, the proposed legislation would give shareholders a veto over prospective executive pay policies. If enacted, the U.K. would be one of the first major countries to adopt binding Say on Pay.

Swiss Government Proposes Ordinance Implementing the Minder Initiative

More than two-thirds of Swiss voters approved an executive pay referendum (the "Minder Initiative") seeking new legislation to improve corporate governance and curb executive compensation. In June 2013 the Swiss Federal Council released, for public consultation, a draft ordinance to implement Minder Initiative reforms. Similar to the UK proposal, the key element of the Swiss proposal is a binding Say on Pay vote.

The proposal would prohibit certain forms of compensation, including severance payments, golden parachute payments and advance payments. The proposal would also expand shareholder voting rights by requiring annual shareholder elections of supervisory board members (the functional equivalent of a corporate board in North America) and elections of key board leadership positions (e.g., board chair and compensation committee members).

Swiss regulators expect to release final legislation in late November. If approved, the final regulations will generally take effect on January 1, 2014 and will apply to Swiss incorporated public companies whether listed on a Swiss or non-Swiss stock exchange.

Meridian comment: The proposed Swiss legislation reflects a European trend to rein in executive pay and to enact corporate governance reforms. However, Switzerland is the first country we are aware of to propose criminal penalties in this context.

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