



Disclosure Reviews and Recommended Governance Practices

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As the 2010 proxy season approaches, reporting issuers should be reviewing the content of their management information circulars and annual filings in the light of disclosure reviews by the Canadian Securities Administrators (“CSA”) and the Ontario Securities Commission (“OSC”). In addition, the Canadian Coalition for Good Governance (“CCGG”) and RiskMetrics Group (“RiskMetrics”) have published guidance and recommendations for public issuers relevant to their annual meetings.

Disclosure Reviews

Staff Notice 51-331 - Report on Staff’s Review of Executive Compensation Disclosure

In November 2009, the CSA published Notice 51-331, setting out the results of its review of compliance by issuers with the executive compensation disclosure requirements which took effect at the end of 2008. The most common deficiencies identified were those relating to disclosure of performance goals and the use of benchmarking.

With respect to disclosure of performance goals, the CSA advised issuers to: (i) explicitly link the discussion about performance goals to compensation that is actually reported; (ii) describe the relative importance between issuer goals and individual performance objectives when making executive compensation decisions; (iii) explain the importance of board discretion in determining bonuses; and (iv) quantify any objective measures used (e.g. use of earnings per share or EBIDTA) in formulating compensation awards. With respect to disclosure of benchmarks, the CSA advised that an issuer should explain its compensation benchmarking methodology and the composition of the benchmark group.

Issuers can expect that the CSA will continue to closely monitor executive compensation disclosure.

Staff Notice 51-330 - Guidance Regarding the Application of Forward-Looking Information Requirements under National Instrument 51-102

In November 2009, the CSA published Notice 51-330, setting out the results of its review of various continuous disclosure documents and the use of forward-looking

information therein. The CSA advised that in circumstances where issuers alert readers to material forward-looking information in a cautionary paragraph, the issuer should state the nature of the material forward-looking information in the paragraph, thereby assisting investors to more readily identify the information. The CSA also advised that in addition to disclosing material risk factors that could cause actual results to differ from forward-looking information, issuers should also disclose material factors or assumptions used to develop the forward-looking information.

OSC Notice 51-717 - Corporate Governance and Environmental Disclosure

In 2009, the OSC undertook an initiative to recognize best practices in reporting standards relating to corporate social responsibility and environmental, social and governance matters. As part of that initiative, the OSC has advised, in OSC Notice 51-717, that it intends to issue a staff notice in 2010 which will provide guidance on compliance with existing environmental disclosure requirements under National Instrument 51-102 - *Continuous Disclosure Obligations*. The OSC expects to publish the notice in time for issuers to consider the guidance when preparing their annual continuous disclosure documents. Concurrently with the publication of Notice 51-717, the OSC published a report to the Minister of Finance (Ontario) reviewing the adequacy of the current materiality-based environment disclosure rules. The report indicated that although environmental disclosure requirements in Canada are adequate, compliance with those requirements has not been consistent. One of the OSC’s recommendations in the report is to provide additional guidance to issuers by building on recommendations made in OSC Staff Notice 51-716 *Environmental Reporting*, published in February 2008. The guidance is expected to steer issuers towards using more meaningful qualitative and quantitative language in producing disclosure regarding environmental matters.

In the United States, the SEC has also committed to review environmental impact disclosure. In January 2010, the SEC voted to provide guidance to publicly listed companies regarding the level and quality of their disclosures on climate change and its material impact on their businesses. While the SEC vote does not change existing disclosure requirements, it may influence companies to increase the quality and quantity of their environmental impact disclosure.

Recommended Governance Practices

The following recommendations of the CCGG and RiskMetrics provide issuers with insight as to governance matters that are potentially of concern to their securityholders.

“Say on Pay”

The CCGG is encouraging issuers to give securityholders a non-binding, advisory “say on pay” vote in order for them to express their satisfaction with the issuer’s approach to compensation in the previous year. For the 2010 proxy season, more than one dozen Canadian public issuers have decided to provide securityholders with a “say on pay” vote to date. In the United States, a “say on pay” vote is mandatory for companies receiving federal bailout funds and legislation has been introduced to extend the requirement to all U.S. companies.

Slate Voting

RiskMetrics now advocates the election of directors on an individual basis (supporting this view with the fact that a majority of the largest capitalized issuers on the TSX adhere to this practice). As such, RiskMetrics has updated its voting recommendation policies and has indicated that where director nominees of TSX-listed issuers are presented to shareholders as a slate in combination with other deficient governance practices, RiskMetrics may issue a recommendation to withhold votes from the entire slate of directors. Deficient practices include: (i) lack of separation of the roles of chairman of the board and chief executive officer (or no independent lead director); (ii) less than a majority of the board being “independent”; (iii) lack of disclosure of audit fees broken down by category; and (iv) lack of separate nominating and compensation committees of the board.

Majority Voting

The CCGG recommends that issuers adopt a “majority voting policy” whereby a nominee director receiving greater than 50% “withheld” votes would have such votes regarded as an “against” vote with respect to the nominee. In such an event, the individual would withdraw his or her name as a nominee for election. Currently, Canadian corporate law provides for the election of directors through a “plurality system” whereby shareholders vote either “for” a nominee or “withhold” their vote with respect to the nominee. In the plurality system, withheld votes effectively do not count, so a director needs only one “for” vote to be elected (in the absence of other nominees standing for election).

Access to Proxies

The CCGG has recommended to the CSA that a securityholder, or group of securityholders, holding at least 5% of the issuer’s relevant securities, should be

permitted to require an issuer to include in its management proxy circular alternative nominees for directors (along with a description of their backgrounds and why they should be elected), and allow the securityholder (or securityholders) to solicit other securityholders without the need to file a dissident information circular. The CCGG has further recommended that this access to and use of the management information circular should be at no cost to the securityholder (or securityholders), and that the securityholder (or securityholders) should be reimbursed by the issuer for reasonable solicitation costs, unless the issuer’s other securityholders vote that there should be no reimbursement.

The SEC is also proposing proxy access rules for shareholders of US public companies.

Best Practices in Disclosure of Executive Compensation Related Information

The CCGG has made the following recommendations to improve the quality of executive compensation disclosure in management information circulars: (i) disclosure regarding the compensation committee’s specific expertise in compensation matters; (ii) disclosure of the name of any engaged consultant and fees paid to the consultant; (iii) discussion of various metrics used to link pay to performance (including rationale behind the choice of metrics) and how relevant metrics translated to actual compensation; (iv) discussion of ownership guidelines for executives upon leaving the issuer.

In December 2009, the SEC adopted new rules to enhance compensation and corporate governance disclosure, including requiring companies to provide an explanation of their pay practices if they create risks that are reasonably likely to have a material adverse effect on the company.

Five Year Review of the Canada Business Corporations Act

The CCGG is advocating that certain governance practices and recommendations be codified in the *Canada Business Corporations Act* (the “CBCA”). In February 2010, the CCGG made a submission to the Standing Committee on Industry, Science and Technology in which it recommended the following amendments to the CBCA: (i) the prohibition of slate voting and the requirement for director election on an individual basis; (ii) the requirement for majority voting for electing directors; (iii) the requirement for annual director elections for all CBCA public companies; (iv) the requirement for public companies to disclose detailed results of shareholder votes; (v) allowing significant shareholders access to and use of the management information circular; and (vi) the requirement for the separation of the roles of chief executive officer and chair of the board.

The CCGG has also recommended that the Standing Committee broaden its legislation review consultation process and consider ways in which shareholders can have better access to and use of the oppression remedy.

This update is intended as a summary only and should not be regarded or relied upon as advice to any specific client or regarding any specific situation.

If you would like further information regarding the issues discussed in this update or if you wish to discuss any aspect of this commentary, please feel free to contact us.

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