Summer 2010

Listed

RATE HIKES: How High, How Fast?

www.listedmag.com

The Magazine for Canadian Listed Companies

BETTER BOARDS
Why compliance alone won't cut it

HIGH-YIELD DEBT
Are you in yet?

RAIDING AMERICA
Canadian banks on a hiring assault

Lessons of the fall

HudBay's legacy: CEO churn, new rules on M&A–and still, all that cash

Allen Palmiere
CEO HudBay Minerals
2008-09

Publication Agreement No. 41983030

Premier Issue

Trusts: A Conversion How-To

Say What?

The first shareholders have spoken. After a smooth start, say-on-pay still stirs the pot

By Dan Bortolotti

Bank shareholder meetings aren't typically known for high drama, and the Royal Bank's annual gathering in early March was as sober as you'd expect. But as ballot collectors darted through rows of chairs at the Metro Toronto Convention Centre, there was more at stake than simply rubber-stamping the board's choice of auditor. Canada's largest publicly traded company had just held its first advisory vote on executive compensation. The say-on-pay era had arrived.

The UK has required an annual, non-binding advisory vote on compensation since 2003, and Australia made it mandatory in 2005. In the U.S., final legislation is still taking shape, but a number of firms have taken the plunge. Canadian companies, meanwhile, had been slower to embrace the idea—indeed many, including RBC, actively opposed a vote until a majority of shareholders demanded it. But all of the Big Five banks introduced say-on-pay for their 2010 meetings. In late February, CIBC went first. Its proposed pay package received 93% support. The following week, just over 91% of RBC shareholders approved that bank's approach to compensating its executives in the year ahead.


Topic Photo/Global Look Press

Look for dozens of say-on-pay votes in 2011

With more than 90% in favour, the votes lacked a certain drama. Yet no doubt boards and compensation committees across the country have been watching the results of these, and subsequent advisory votes, very closely. Beyond the banks, the list of participating companies includes BCE, Potash Corp., Manulife Financial and TMX Group. "We've had a number of other companies say they want to wait and see how the banks change their compensation structures," says Stephen Griggs, executive director of the Canadian Coalition for Good Governance, which represents institutional investors and formally endorsed the say-on-pay process in 2009 after more than two years of consultation. Griggs says several firms will wait until 2011, including Suncor,

RBC

RBC's O'Brien: Studying the vote

Enbridge, EnCana, Telus and several insurance companies. "They want to learn from the experience of the banks."

It's all sweetly satisfying for Gary Hawton, CEO of Winnipeg-based Meritas Mutual Funds. No one has worked harder to bring say-on-pay to Canada. Four years ago, Hawton approached banks and other companies and asked them to be more transparent in disclosing executive pay packages. He was hoping to avoid having to submit a shareholder resolution at the corporations' annual meetings. "The resolutions came later," he says, "after the companies completely ignored us, or politely told us, 'Go away, we are not the least bit interested.' "

Hawton forced the issue by bringing say-on-pay resolutions forward at all the Big Five banks' shareholder meetings in 2008, flying around the country to do so personally. He wasn't expecting more than token support. "Right up until the first vote, no one called us from within the industry to say, 'Great idea, we're with you.' When CIBC came in at around 45%, it completely blew me away." Results were similarly enthusiastic at the other banks, with an average of 40.5% of shareholders supporting an advisory vote on compensation.

Shareholder resolutions almost never receive that kind of support, and Hawton expected at least one bank would voluntarily introduce say-on-pay in 2009. But none did. "I'm surprised nobody said, 'We're already a governance leader, so why don't we be the first mover on this?' They all stood back and said, 'We don't want to be the first.' " (For its part, RBC says it was waiting for the Canadian Securities Administrators to announce its new rules for executive compensation disclosure.)

So Hawton again introduced his resolution at the banks' annual meetings in early 2009. A lot had changed by then, of course: namely, the worst financial crisis and stock market crash since the Depression. The widespread outrage of investors helped turn a healthy minority into a majority: Hawton's say-on-pay resolution passed at the first four bank shareholder meetings. The last to hold its meeting was TD and, seeing the writing on the wall, its board accepted the resolution without even putting it to a vote.

As the banks prepared their proxy circulars for 2010, it was clear the game had changed. Not only have they outlined their pay packages in (more or less) plain English, they appear to be making an effort to tie compensation to mid- and long-term performance. At RBC, executives will now wait three to four years for their stock options to be vested; previously the vesting schedule kicked in after only one year. CIBC has introduced so-called "book value units," which the bank says "better ties pay to the creation of real and sustainable value over time, rather than being unduly influenced by short-term market movements." Meanwhile, at the Bank of Montreal's AGM in late March, shareholders endorsed a plan that will see a third party conduct a review and make recommendations on executive pay. The plan, including potential bonus clawbacks, aims to improve the linkage between pay and performance.

A big question remains: how companies will respond to shareholders who vote against the compensation plans. "The difficulty is knowing the reasons why people vote for or against," RBC Chairman David O'Brien told *Listed* after the bank's AGM. "We will over the next year be spending more time discussing with institutions and other shareholders, and they are always invited to write to me with their suggestions. Of course, you can't satisfy everyone."

Going forward, the CCGG plans to meet with about 35 companies this year, and Griggs says most now understand that an advisory vote on compensation is inevitable. "Boards are now talking about when they will implement say-on-pay, not whether they will."

SAY-ON-PAY SPARKS REACTION

The arrival of shareholder advisory votes on compensation is forcing more groups to take sides

Now that say-on-pay has taken root in this country, it's prompting all kinds of response—some positive, some negative—beyond the dozen or so companies that have had or will have shareholder advisory votes on executive compensation at their 2010 annual meetings.

YEA Following the largely painless first round of say-on-pay votes at Canada's major banks, more Canadian companies have agreed to introduce similar non-binding votes at their annual general meetings in 2011. Some of the recent high-profile joiners include TransAlta, Barrick Gold, Agrium, Biovail and Canadian Pacific Railway. According to Gary Hawton, CEO of Meritas Mutual Funds, about 25 Canadian companies have now adopted the practice.

NAY Although shareholder rights organizations are attempting to get say-on-pay resolutions implemented at a growing number of companies, not every firm is cooperating. Take Methanex, for example. In the lead-up to its April 29 AGM and scheduled shareholder vote to adopt say-on-pay in 2011, the Vancouver-based methanol producer and marketer continued to resist. Instead, it asked shareholders to fill out an online executive compensation survey, promising to forward comments to the chair of its human resources committee.

Methanex has a powerful ally. In March, the Ontario Teachers' Pension Plan issued a letter stating that it is generally opposed to shareholder proposals for say-on-pay advisory votes. According to Teachers, executive compensation decisions are sufficiently complex that they are best left to expert board committees rather than general shareholders. Instead, Teachers said it would deal directly with compensation committee chairs when pay packages don't conform to its internal guidelines.

Meanwhile, the Institute for Governance of Private and Public Organizations, a joint initiative of the Concordia University's John Molson School of Business and Montreal's École des haute études commerciales, published a paper opposing say-on-pay votes, arguing that they represent a small, but significant, shift in governance responsibilities from boards to shareholders.