



INDU: Bill C-25

Brief to the House Standing Committee on Industry, Science and Technology

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Introduction

1. This brief deals exclusively with the amendments to the *Canada Business Corporations Act* (the “CBCA”)¹ proposed in Part 1 of Bill C-25,² as such amendments relate to CBCA distributing corporations.
2. Bill C-25, if enacted, will result in improvements to the governance regime for CBCA distributing corporations, will support many principles of shareholder democracy, and should help to boost Canada’s investment potential.³ Accordingly, the Canadian Coalition for Good Governance (“CCGG”) strongly recommends that the bill’s provisions enhancing corporate governance for CBCA distributing corporations be adopted.
3. Additionally, CCGG believes that further consideration should be given to how to further improve corporate governance in Canada, both through focussed consultation on key governance matters, and by subjecting the CBCA to ongoing review as informed by stakeholders that have direct experience with the realities of investing and doing business in Canada.

I. Enact Bill C-25, including its Provisions Enhancing Corporate Governance for Distributing Corporations

4. CCGG strongly urges this committee to recommend to the House that the CBCA amendments in Part 1 of Bill C-25 be adopted.

¹ *Canada Business Corporations Act*, RSC 1985, c C-44.

² Bill C-25, *An Act to amend the Canada Business Corporations Act, the Canada Cooperatives Act, the Canada Not-for-profit Corporations Act, and the Competition Act*, 1st Sess, 42nd Parl, 2017 (second reading in the House of Commons 9 December 2016).

³ See: Anita Anand, “The Value of Governance” (1 February 2013), online: <http://www.ccg.ca/site/ccgg/assets/pdf/the_value_of_governance_anand_anita.pdf>. In her report, Professor Anand remarked: “Overall, there is a strong consensus in the literature that corporate governance is linked positively to firm value, even when ‘governance’ and ‘value’ are defined and measured in various ways.”

5. Bill C-25 proposes several key enhancements to the corporate governance of CBCA distributing corporations, the most important of which is the introduction of a “majority voting system” for uncontested director elections.
6. Under the current CBCA proxy voting procedure, a “plurality voting system” is used to elect the directors of a public company. Under this system, a shareholder can either vote “for” a director nominee or “withhold” her vote. It is not possible to vote “against” a director, and “withheld” votes in effect are like abstentions and do not count. Accordingly, a director needs only one “for” vote to be elected to the board. By way of example, a nominee who owns one share could vote for herself and be elected.
7. Further, under the current system, shareholders are left with a limited number of options to change the composition of the board, and each of these options can be expensive, onerous, and time-consuming to execute.
8. By contrast, under a “majority voting system” as proposed in Bill C-25, a director nominee in an uncontested election would be elected only if that nominee receives more votes “for” than “against”. We understand that this system is used in most jurisdictions around the world, with Canada and the United States as notable outliers.
9. Since 2014, the Toronto Stock Exchange (the “TSX”) has required each listed issuer to adopt a majority voting policy if it is incorporated in a “plurality voting system” jurisdiction. Such a policy requires that any director candidate for whom more votes are “withheld” than are voted “for” must immediately tender his or her resignation to the board, which the board shall accept absent exceptional circumstances. CCGG considers this to be a workaround for the problems inherent in the plurality voting system, but a better outcome would be the adoption in the corporate statutes of a principled “majority voting system”, which would obviate the need for such a workaround in the first place. Additionally, nothing prevents this TSX listing requirement from being reversed in the future.
10. CCGG also notes that there is no comparable requirement to adopt a majority voting policy for the over 1,600 issuers listed on the TSX Venture Exchange. Each of these listed issuers has the privilege of access to the public capital markets, and CCGG’s view is that with this privilege should come the corresponding responsibility to be answerable to shareholders in a meaningful way.
11. CCGG also supports the proposed amendments concerning diversity-related disclosure, both for gender and forms of diversity other than gender. CCGG has taken the position for many years that:

While the quality of individual directors is paramount, we also expect boards as a whole to be diverse. A high performance board is comprised of directors with a wide variety of experiences, views and backgrounds which, to the extent practicable, reflects the gender, ethnic, cultural and other personal characteristics of the communities in which the corporation operates and sells its goods or services.⁴

12. CCGG also supports the amendments that provide for individual (not slate) director elections and annual terms for directors. Although these two practices are also currently listing requirements for the TSX, nothing prevents such requirements from being reversed in the

⁴ CCGG, “Building High Performance Boards” (August 2013), online: [http://www.ccg.ca/site/ccgg/assets/pdf/building_high_performance_boards_august_2013_v12_formatted_sept_19_2013_last_update .pdf](http://www.ccg.ca/site/ccgg/assets/pdf/building_high_performance_boards_august_2013_v12_formatted_sept_19_2013_last_update.pdf)> at 9.

future. Each of these rules are essential elements of good corporate governance and, accordingly, they should be entrenched into the CBCA.

II. Engage in Focussed Consultations on Improvements to Corporate Governance

13. CCGG recommends that this committee, or the appropriate government body, conduct focussed consultations with provincial securities regulators and other key stakeholders, such as interest groups representing industry and shareholders, and professionals in the areas of law and finance, on additional amendments to be made to the CBCA in order to improve the corporate governance of CBCA distributing corporations.
14. Three particular measures for consideration during such consultations are set out below. CCGG does not believe that Bill C-25 should be held up to provide for these measures at this time, however, as these items will take some time to fully consider and draft.

Consultation Item (A): Facilitate the ability of shareholders to nominate directors (aka “Proxy Access”)

15. Consideration should be given to amending the CBCA, and in particular section 137(4) thereof, in order to facilitate the ability of shareholders to nominate directors. The principles set out in CCGG’s published policy on this topic should guide the consultation.⁵
16. Current methods by which shareholders can nominate director candidates are, quite simply, not effective, and they also can be unequal, onerous, and/or prohibitively expensive in their application. In part due to this ineffectiveness, director nominees are almost always chosen by the incumbent directors and/or company management. Further, in CCGG’s experience, companies very seldom seek input from shareholders when selecting board nominees.
17. Canada is becoming a laggard in this area of governance. In the United States, 39% of S&P 500 companies have adopted a meaningful method for shareholders to nominate director candidates.⁶ We also understand that direct shareholder input into the director nomination process is permitted in many other countries.⁷

Consultation Item (B): Mandate periodic shareholder votes to approve a public company’s approach to executive compensation (aka “Say on Pay”)

18. Consideration should be given to amending the CBCA to require distributing corporations to hold periodic advisory “Say on Pay” votes by means of an ordinary resolution at each annual meeting of shareholders. The text of the resolution should be substantively similar to:

Resolved, on an advisory basis and not to diminish the role and responsibilities of the board of directors, that the shareholders accept the approach to executive compensation disclosed in

⁵ CCGG, “Shareholder Involvement in the Director Nomination Process: Enhanced Engagement and Proxy Access” (May 2015), online: http://www.ccg.ca/site/ccgg/assets/pdf/proxy_access_finalv.35.docx_edited_on_june_18,_2015.pdf [CCGG Shareholder Nomination Policy].

⁶ Peter Kimball and Alexandra Higgins, “The Finer Points of Proxy Access Bylaws Come Under the Microscope”, Harvard Law School Forum on Corporate Governance and Financial Regulation (12 September 2016), online: <https://corpgov.law.harvard.edu/2016/09/12/the-finer-points-of-proxy-access-bylaws-come-under-the-microscope/>.

⁷ See, for example, CCGG Shareholder Nomination Policy, *supra* note 5, at 7–8.

the Company's information circular delivered in advance of the [insert year] annual meeting of shareholders.

19. Currently, neither corporate law nor securities law in Canada provides any direct role for shareholders in monitoring executive compensation.⁸ Compensation of executives is one of the most critical roles carried out by directors, and shareholders should have the right to signal, in general terms, their support, or lack thereof, for a board's approach to executive compensation.
20. Such advisory votes have the benefit of requiring directors to turn their attention to executive compensation. Directors anticipating an annual "Say on Pay" vote are incentivized to thoroughly understand their company's compensation arrangements and meaningfully explain them to shareholders in the company's information circular.
21. Further, such advisory votes are another area where Canada is an international outlier. Periodic "Say on Pay" votes are mandatory in various countries around the world, including the USA, Australia, and Western European countries such as the United Kingdom, France, Germany, the Netherlands, and Belgium.⁹

Consultation Item (C): Require the Board Chair to be independent of company management

22. Consideration should be given to amending the CBCA to require that, as a general rule, the Board Chair be independent of management.
23. The Board Chair plays a critical role in leading or coordinating the other directors, both during and outside of meetings, in support of the board's obligation to supervise the senior executive team's performance.
24. When the Board Chair is not independent of management, it results in a serious conflict of interest, and it obscures the lines of accountability. For example, the oversight of the senior executive team, in particular of the CEO, is one of the board's key responsibilities. A combined Board Chair/CEO would thus be responsible for leading the body that oversees herself.
25. Many other key responsibilities of the Board Chair also are compromised when the role is shared: setting the agenda for board meetings; ensuring directors remain apprised of key company developments; and ensuring that board meetings are conducted with open discussion and permit an independent assessment of management's performance and views.
26. Similar problems arise with any Board Chair who is not wholly independent of management.
27. A general rule such as this would also require exceptions to be carved out, where appropriate.

III. Establish and Seek Advice from a Stakeholder Advisory Council

28. CCGG recommends that an advisory council populated with key stakeholders and professionals be established and charged with providing periodic reports on ways to improve the regulatory environment for CBCA distributing corporations.

⁸ As of mid-2015, 163 Canadian public companies have voluntarily agreed to have annual advisory Say on Pay resolutions, with larger public companies leading the way, with approximately 80% of the S&P/TSX 60 Index and 48% of the S&P/TSX Composite companies having adopted Say on Pay; see Meridian Compensation Partners, LLC, "Canadian Companies Continue to Voluntarily Adopt Say on Pay" (4 August 2015), online: <<https://www.meridiancp.com/insights/news/canadian-companies-continue-to-voluntarily-adopt-say-on-pay/>>.

⁹ Randall S Thomas and Christoph Van der Elst, "Say on Pay Around the World" (2015) 92:3 Washington UL Rev 653, online: <https://papers.ssrn.com/sol3/papers2.cfm?abstract_id=2401761>.

29. CCGG agrees with the government that “[m]odern and well-crafted economic framework laws are the foundation upon which Canadian companies can innovate and grow to scale in the modern economy on a more regular basis.”¹⁰ A stakeholder advisory council with direct knowledge of the opportunities and challenges faced by Canadian investors and businesses can provide invaluable advice to the government as it seeks to bring Canada’s corporate laws into line with international best practices, while also ensuring Canada remains a popular jurisdiction for economic growth and investment.
30. Such a council would also provide external stimulus to government to ensure that more regular reviews of the CBCA are conducted. Despite the statutory requirement to review the CBCA every ten years,¹¹ such reviews have not occurred on schedule. Indeed, the CBCA has been substantially amended only twice in the past forty years.
31. Further, such a council could provide helpful feedback regarding the manner in which the provisions in Bill C-25 related to diversity are being interpreted and adopted by distributing corporations.

Summary Table of Recommendations

I	Enact the CBCA amendments in Part 1 of Bill C-25 which will enhance corporate governance for distributing corporations
II	Engage in focussed consultations on additional improvements to corporate governance for CBCA distributing corporations, in particular on the three matters specified
III	Establish and seek advice from a stakeholder advisory council

About CCGG

32. CCGG was founded in 2002 to promote good governance practices in the Canadian public companies whose shares are owned by our members. CCGG members include a wide range of institutional investors – primarily pension funds and third party money managers – that have in aggregate approximately \$3 trillion in assets under management. Millions of Canadians rely on returns from these investments to fund their retirements. A list of CCGG members is available on our website at www.ccg.ca.
33. CCGG is widely recognized as a thought leader in corporate governance. CCGG is regularly consulted on governance matters by governments, regulators, and reporting issuers, and has published many widely-read policy papers on governance topics.¹² CCGG has also been granted intervenor status in certain critical cases before the Supreme Court of Canada that raise corporate governance issues, most recently in the case of *Livent v Deloitte*, which was heard by the court on February 15, 2017.¹³

¹⁰ Canada, “Backgrounder: An Act to amend the Canada Business Corporations Act, the Canada Cooperatives Act, the Canada Not-for-profit Corporations Act and the Competition Act” (28 September 2016), online: <<http://news.gc.ca/web/article-en.do?nid=1130719>>.

¹¹ *An Act to amend the Canada Business Corporations Act and the Canada Cooperatives Act and to amend other Acts in consequence*, SC 2001, c 14, s 136.

¹² CCGG, “Policies & Principles”, online: <<http://www.ccg.ca/index.cfm?pagepath=Policies&id=17581>>.

¹³ Supreme Court of Canada, “Factums on Appeal – *Deloitte & Touche v. Livent Inc., Through its Special Receiver and Manager Roman Doroniuk*”, online: <<http://www.scc-csc.ca/case-dossier/info/af-ma-eng.aspx?cas=36875>>.