Corporate Governance Developments Set to Be Codified into the CBCA

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As 2019 comes to an end, we provide a lookback at corporate governance related amendments to the CBCA that have come into force this year and look forward to those slated to come into force in 2020 and beyond.

- Fiduciary duty guidance is codified.
- A new focus on diversity, employee well-being and clawback policy reporting.
- Non-binding annual say-on-pay resolutions mandated.

In an attempt to enhance retirement security, the Federal Government has adopted amendments to the *Canada Business Corporations Act* (CBCA) through Bill C-97, *Budget Implementation Act, 019, No. 1* (Bill C-97). Initially proposed on April 8, 2019, the Bill C-97 amendments may represent a significant addition to the Canadian corporate governance landscape despite some of the new requirements being familiar to Canadian public companies.

Codifying BCE Best Interests of the Corporation

The CBCA requires directors and officers to "act honestly and in good faith with a view to the best interests of the corporation". Known as the fiduciary duty, directors and officers are required to promote the corporation's interests above those of their own, including other business or personal interests they may have. Despite the historically held view that generally acting in the best interests of the corporation equated to acting in the best interests of the shareholders, in 2008 the Supreme Court of Canada held in *BCE Inc. v. 1976 Debenture Holders* that the fiduciary duty is owed to the corporation and not to any other particular constituency. While promotion of the corporation's interests will typically align with shareholder interests, where these interests conflict, "the directors' duty is clear – it is to the corporation". Notwithstanding the duty being owed to the corporation, the Court provided guidance in *BCE* that directors may look to the interests of "shareholders, employees, creditors, consumers, governments and the environment to inform their decisions".

With the adoption of Bill C-97, effective June 21, 2019, the CBCA was amended to essentially codify the *BCE* decision by including factors that directors and officers may consider when acting with a view to the best interests of the corporation. These factors are the interests of shareholders, employees, retirees and pensioners, creditors, consumers and governments, the environment and the long-term interests of the corporation. Interestingly, these factors mirror those identified in *BCE* with the addition of retirees and pensioners, evidencing the Canadian government's increased focus on this growing subset of the Canadian population. The CBCA factors also include a mention of the environment, which may create

some of the most interesting issues for boards and executives over the coming years as the spotlight on environmental issues continues to grow. As we have recently discussed, the environment, and more particularly climate change, has become the focus of interest for many Canadian investors, with the Canadian securities regulators publishing guidance with regard to related disclosure matters.

As these amendments largely mirror the prevailing legal interpretation since BCE, it remains to be seen whether the codification of these interests will materially affect the current governance landscape.

Additional Diversity and Well-Being Disclosure Also Set to Come Into Force

As we have discussed, enhanced diversity disclosure with regard to women, visible minorities, persons with disabilities and Indigenous peoples will come into force for CBCA incorporated public companies on January 1, 2020 pursuant to recent amendments to the CBCA under 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* (Bill C-25). Bill C-97 also includes amendments to the CBCA which will require enhanced diversity disclosure for "prescribed corporations" with the specific disclosure requirements to be determined by yet to be published regulations. It is, however, expected that such regulations will be similar to those set to come into force on January 1, 2020 under Bill C-25, given the coordinating provisions of Bill C-97.

As previously discussed , since 2014 Canadian public companies have been required to disclose certain information regarding women in corporate leadership roles on a "comply or explain" basis and, according to CSA Multilateral Staff Notice 58-311 Report on Fifth Staff Review of Disclosure regarding Women on Boards and in Executive Officer Positions (October 2, 2019), there have been modest increases in the representation of women in corporate leadership roles since the implementation of the disclosure requirements. Once again, it will remain to be seen whether the enhanced diversity disclosure requirements found in the CBCA will change the landscape of board composition for CBCA incorporated issuers. In addition, proxy advisory firms and institutional investors have yet to update their voting guidelines to reflect the diversity amendments but some (for example, Glass Lewis) have noted that the new expanded disclosure will be monitored and reflected in their analysis with regard to director elections.

Bill C-97 also proposes some novel annual disclosure on the "well-being of employees, retirees and pensioners", with the terms retirees and pensioners to be defined at a later date. The exact disclosure requirements have yet to be published but may lead to disclosure about the solvency of pension plans, post-retirement benefits and the like.

Non-Binding Say-On-Pay Votes and Clawback Disclosure

The Bill C-97 amendments will require that "prescribed corporations" develop an approach with respect to the remuneration of the directors and employees of the corporation who are "members of senior management" (a term to be defined at a later date) and that the corporation hold an annual non-binding vote on such approach (generally referred to as a "say-on-pay" resolution). The results of the vote are required to be disclosed but are not to be binding on the corporation.

Say-on-pay resolutions should not be unfamiliar to Canadian public companies. This type of non-binding vote is already mandated in some jurisdictions, including the United States, United Kingdom and Australia, and Canadian governance advocacy groups have promoted the use of these types of advisory votes for a number of years, with the Canadian Coalition for Good Governance (CCGG) publishing their Model 'Say on Pay' Policy for Issuers in September 2010, stating that "an annual … shareholder advisory vote on a board's approach to compensation is an important part of an ongoing integrated engagement process

between shareholders and boards". Indeed, our research shows that the majority of Canadian TSX/S&P 60 issuers held say-on-pay votes in the 2019 proxy season.

In some cases, a say-on-pay vote will be of benefit to a company by providing investors with an outlet to express their views on executive pay practices in a relatively risk-free environment. For example, Institutional Shareholder Services (ISS) notes in its Canada Proxy Voting Guidelines for TSX-Listed Companies (December 12, 2018) that "dissatisfaction with compensation practices can be expressed by voting against a [management say-on-pay proposal] rather than withholding or voting against the compensation committee." This allows companies to realign their approach to remuneration in response to shareholder views and concerns without risk to board seats.

Clawback Disclosure

Disclosure of "the recovery of incentive benefits or other benefits", more commonly referred to as a clawback, on an annual basis also forms a part of the Bill C-97 requirements. An important part of executive pay practices, clawback policies serve to discourage excessive risk taking.

Once again, this type of disclosure should not be novel to Canadian public companies. Form 51-102F6 *Statement of Executive Compensation* requires issuers to disclose significant elements of compensation in the compensation discussion and analysis and provides that "policies and decisions about the adjustment or recovery of awards, earnings, payments, or payables if the performance goal or similar condition on which they are based are restated to reduce the award, earning, payment or payable" are an example of this type of element. As such, to the extent that a public company has adopted a clawback policy, disclosure would generally already be provided.

In addition, clawback policies have been required in the United States since the implementation of the *Sarbanes Oxley Act of 2002* which requires the CEO and CFO of an issuer to repay any and all incentive payments and profits from the sale of stock that were received in a year prior to an accounting restatement that was the result of "misconduct". In Canada, our recent study of S&P/TSX 60 issuers shows that despite not being mandatory under any legal or stock exchange requirement in Canada, almost all such issuers have adopted clawback policies with the majority of those being applicable where there has been a financial restatement accompanied by some form of misconduct on the part of the executive. The remainder of the policies are triggered by a financial misstatement alone. This level of policy adoption marks a significant increase in the use of clawback policies since 2007, when CCGG reported that a survey of Canadian issuers revealed only three companies with disgorgement (or reimbursement) policies.

Other Bill C-25 Amendments

Not to be forgotten, in addition to the diversity amendments to come into force on January 1, 2020, Bill C-25 will also implement the following amendments to the CBCA with an aim of aligning the CBCA with Canadian securities law and stock exchange requirements:

- **Majority voting**. Public companies will be required to implement a majority voting standard in uncontested director elections for all public CBCA incorporated companies (including those listed on the TSX Venture Exchange).
- **Notice-and-Access**. Bill C-25 and the proposed related regulations would allow CBCA distributing corporations to provide meeting materials to their shareholders through the internet by way of notice-and-access, a process which has not been available to CBCA corporations due to technical provisions of the act.
- **Document retention**. The Bill C-25 amendments will change the retention periods related to documents that were received and accepted by the Director appointed under the CBCA.

None of these amendments are yet in force and timing of implementation has yet to be established.

Implementation and Coming Into Force

The best interests amendments came into force on June 21, 2019, being the date Bill C-97 was granted royal assent. The Bill C-25 diversity disclosure amendments will come into force on January 1, 2020. The proposed Bill C-97 disclosure amendments (diversity, well-being, clawbacks and say-on-pay) will come into force on a day to be fixed by order of the Governor in Council, presumably once the associated regulations have been published. As noted above, the Bill C-25 amendments other than the diversity amendments have yet to come into force and timing of implementation has yet to be established.