The Corporate Governance Review

Sixth Edition

Editor
Willem J L Calkoen

Law Business Research

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EDITOR'S PREFACE

I am proud to present this new edition of *The Corporate Governance Review* to you.

In this sixth edition, we can see that corporate governance is becoming a more vital and all-encompassing topic with each year that passes. We all realise that the modern corporation is one of the most ingenious concepts ever devised. Our lives are dominated by corporations. We eat and breathe through them, we travel with them, we are entertained by them, most of us work for them. Most corporations aim to add value to society and they very often do. Some, however, are exploiting, polluting, poisoning and impoverishing us. A lot depends on the commitment, direction and aims of a corporation's founders, shareholders, boards and management and employees. Do they show commitment to all stakeholders and to long-term shareholders, or mainly to short-term shareholders? There are many variations on the structure of corporations and boards within each country and between countries. All will agree that much depends on the personalities and commitment of the persons of influence in the corporation.

We see that everyone wants to be involved in 'better corporate governance': parliaments, governments, the European Commission, the US Securities and Exchange Commission (SEC), the Organisation for Economic Co-operation and Development (OECD), the UN's Ruggie reports, the media, supervising national banks, shareholder activists and other stakeholders. The business world is getting more complex and overregulated, and there are more black swans, while good strategies can quite quickly become outdated. Most directors are working diligently, many with even more diligence. Nevertheless, there have been failures in some sectors, so trust has to be regained. How can directors do all their increasingly complex work and communicate with all the parties mentioned above?

What should executive directors know? What should non-executive directors know? What systems should they set up for better enterprise risk management? How can chairs create a balance against imperial CEOs? Can lead or senior directors create sufficient balance? Should most non-executive directors understand the business? How much time should they spend on their function? How independent must they be? What about diversity? Should their pay be lower? What are the stewardship responsibilities of shareholders? What are the pros and cons of shareholder rights plans?

Governments, the European Commission and the SEC are all pressing for more formal inflexible legislative acts, especially in the area of remuneration. Acts set minimum standards, while codes of best practice set aspirational standards.

More international investors, voting advisory associations and shareholder activists want to be involved in dialogue with boards about strategy, succession and income. Indeed, far-sighted boards have 'selected engagements' with stewardship shareholders to create trust. What more can they do to show all stakeholders that they are improving their enterprises other than through setting a better 'tone from the top'? Should they put big signs on their buildings emphasising integrity, stewardship and respect?

Interest in corporate governance has been increasing since 1992, when shareholder activists forced out the CEO at General Motors and the first corporate governance code – the Cadbury Code – was written. The OECD produced a model code and many countries produced national versions along the lines of the Cadbury 'comply or explain' model. This has generally led to more transparency, accountability, fairness and responsibility. However, there have been instances where CEOs gradually amassed too much power or companies have not developed new strategies and have produced bad results – and sometimes even failure. More are failing since the global financial crisis than previously, hence the increased outside interest in legislation, further supervision and new corporate governance codes for boards, and stewardship codes for shareholders and shareholder activists. The European Commission is developing a regulation for this area as well.

This all implies that executive and non-executive directors should work harder and more as a team on policy, strategy and entrepreneurship. More money is lost through lax or poor directorship than through mistakes. On the other hand, corporate risk management is an essential part of directors' responsibilities, and sets the tone from the top.

Each country has its own measures; however, the chapters of this book also show a convergence. The concept underlying the book is of a one-volume text containing a series of reasonably short, but sufficiently detailed, jurisdictional overviews that permit convenient comparisons, where a quick 'first look' at key issues would be helpful to general counsel and their clients.

My aim as editor has been to achieve a high quality of content so that *The Corporate Governance Review* will be seen, in time, as an essential reference work in our field. To meet the all-important content quality objective, it was a condition *sine qua non* to attract as contributors colleagues who are among the recognised leaders in the field of corporate governance law from each jurisdiction.

I thank all the contributors who helped with this project. I hope that this book will give the reader food for thought; you always learn about your own law and best practice by reading about the laws and practices of others. Further editions of this work will obviously benefit from the thoughts and suggestions of our readers. We will be extremely grateful to receive comments and proposals on how we might improve the next edition.

Willem J L Calkoen
NautaDutilh
Rotterdam
March 2016

Chapter 6

CANADA

Andrew MacDougall, Robert Yalden and John Valley[1]

I OVERVIEW OF GOVERNANCE REGIME

Canada's system of corporate governance is derived from the British common law model and strongly influenced by developments in the United States. While corporate governance practices in the United Kingdom and the United States are similar in many respects, where there are differences Canadian practice usually falls somewhere in between. For example, a Canadian corporation is more likely than a US corporation to have a chair who is not the CEO, and typically has fewer executives on the board than a UK corporation.[2]

Under Canada's Constitution, provincial governments have exclusive power over property and civil rights within the province. As a result, corporations may choose to incorporate under federal corporate law or under the corporate laws of any of the 10 provinces in Canada. In addition, securities law in Canada is regulated by securities administrators in Canada's 10 provinces and three territories. However, the federal governments and five provincial governments are collaborating on a cooperative capital markets regulatory system.[3] Regulation of Canada's national stock exchange is

1 Andrew MacDougall and Robert Yalden are partners at Osler, Hoskin & Harcourt LLP. John Valley is an associate at the same firm.

2 According to reports by Spencer Stuart, in Canada 88 per cent of corporations have a chair who is not the CEO and 80 per cent of directors are independent; in the UK the CEO rarely serves as chair but only 71.5 per cent of the directors (excluding the chair) are non-executives; and in the United States only 48 per cent of corporations have a chair who is not the CEO, but 84 per cent of directors are independent. See the 2015 Spencer Stuart Board Index, the 2015 Canadian Spencer Stuart Board Index and the Spencer Stuart 2015 UK Board Index.

3 The cooperative capital markets regulatory system would involve uniform provincial capital markets legislation of participating provinces and complementary federal legislation. The

divided between the Province of Ontario for the senior exchange, the Provinces of British Columbia and Alberta for the venture exchange and the Province of Quebec for the derivatives exchange.

Corporate governance practices in Canada are shaped by legal rules and best practices promoted by institutional shareholder groups, the media and professional director associations such as the Institute of Corporate Directors (ICD). Sources of legal rules include provincial corporate statutes, securities laws and rules, stock exchange requirements and the common law, as well as a wide variety of other regulatory statutes, regulations and policies. The 10 provincial securities commissions are very active in corporate governance matters, which often overlap corporate law areas of concern. Canadian corporate governance has also been influenced by the high proportion of public corporations in Canada that have a dominant or controlling shareholder, either through equity ownership or the ownership of multiple voting rights.

Canadian institutional investors have a profound influence on Canadian corporate governance practices and Canada may be unique in that has a national institutional investor organisation formed to promote good governance practices in corporations whose shares members own. The Canadian Coalition for Good Governance (CCGG) comprises 49 members, including many of Canada's largest institutional investors, collectively managing nearly C$3 trillion in assets, and has pursued an organised programme of articulating its views and encouraging best practices generally without resorting to proxy battles.

i Recent developments

In February 2016 the CSA announced fundamental amendments to the takeover bid regime in Canada that are expected to come into force on 9 May 2016. Among other things, the amendments provide a company that is the subject of a hostile takeover bid with up to 105 days to respond to the hostile bid (instead of the 35 days that previously governed). These changes are expected to affect the market practice in connection with shareholder rights plans (which should play a more limited role going forward), the structure of white knight transactions and the ways in which boards of directors in Canada respond to hostile bids.

In October 2015, the staff at the Ontario Securities Commission (OSC) released a policy for a proposed whistle-blowing programme for the payment of financial incentives of up to C$1.5 million to individuals who provide the OSC with information that meaningfully assists the OSC in a securities law enforcement investigation which results in monetary sanctions or settlement amounts. The comment period for this policy closed in January 2016 and it is expected to come into force in the spring of 2016. The proposed policy is the first of its kind in Canada and is modelled on the Securities and

comment period on draft legislation closed in December 2015 and the jurisdictions participating in this initiative are working towards implementation in the autumn of 2016. The participating provinces are Ontario, British Columbia, Saskatchewan, New Brunswick and Prince Edward Island.

Exchange Commission's programme in the United States, although it seeks to avoid some of the more egregious aspects of that programme by imposing a proportionally smaller reward scale and establishing a maximum award cap.

The Canadian Securities Administrators (CSA) announced amendments to the continuous disclosure obligations of 'venture issuers' in Canada. 'Venture issuers' are predominantly issuers listed on the TSX Venture Exchange and generally tend to be smaller issuers. The amendments came into force in April 2015 and are intended to streamline and tailor the disclosure required to be made by 'venture issuers', including by reducing the extent of financial reporting and of required corporate governance, audit committee and executive compensation disclosure.

On 1 June 2015, the Canadian Extractive Sector Transparency Measures Act was proclaimed into force. The legislation's stated purpose is to 'implement Canada's international commitments to participate in the fight against corruption through the imposition of measures applicable to the extractive sector', and it requires Canadian businesses involved in resource extraction to file and make publicly available reports on certain types of payments made to both domestic and foreign governments.

In May 2015, CCGG issued a proposal on 'proxy access' for Canadian corporations which would permit shareholders to submit nominees for director to be included in the company's proxy circular if the submitting shareholders hold at least 5 per cent of the outstanding shares (3 per cent if the issuer's market capitalisation is C$1 billion or more). The shareholders need not have held the shares for a period prior to making the nominations and they would be permitted to solicit votes for their nominees without filing a separate proxy circular. The benefit of pursuing the CCGG's proposal compared with other alternatives has been questioned, especially in light of existing shareholder proxy access rights under long-standing statutory provisions in Canada.

The CSA announced a national policy providing guidance on recommended practices and disclosure for proxy advisory firms on 30 April 2015 that is intended to promote transparency in the processes leading to vote recommendations and the development of proxy voting guidelines. Relatedly, in January 2015, the CSA provided an update on its continuing review of the effectiveness of the proxy voting system in Canada, noting that its research indicates that overvoting does appear to occur on a regular basis, although without any substantive impact on the result of the meeting. The CSA stated that for the 2016 proxy season it would direct key entities that engage in vote reconciliation to work collectively to develop appropriate industry protocols for meeting vote reconciliation.

During the 2015 proxy season, three significant TSX-listed issuers, including one of the five largest Canadian banks, lost their advisory 'say-on-pay' votes. One of these issuers had a vote of approximately 73.4 per cent against, representing the second-lowest ever level of shareholder support on a say-on-pay vote in Canada. These votes followed say-on-pay votes in 2014 that showed increasing levels of support and no failed votes, and demonstrate that investors in Canada still use say-on-pay advisory votes to voice dissatisfaction with company compensation practices.

II CORPORATE LEADERSHIP

i Board structure and practices

Responsibility for the governance of a corporation is vested in the corporation's board of directors (the board). The board is a single-tier body elected by the shareholders that supervises the management of the corporation. If shareholders are not satisfied with the performance of the board, they may remove the directors or refuse to re-elect them.

The role of directors is one of stewardship and oversight. Directors have complete discretion to exercise their powers as they deem appropriate, subject to the constraints imposed by law. The board discharges its responsibilities through majority approval of the directors at board meetings.

Directors are neither required nor expected to devote their full time and attention to the corporation's affairs. Instead, responsibility for the day-to-day management of a corporation's affairs is delegated to the CEO and other senior executives who are responsible to, and report back to, the board. Appointing these senior executives and evaluating their performance are among the most important functions of the board. Notwithstanding such delegation, the board retains the ability to intervene in management's decisions and must exercise final judgement on matters that are material to the corporation. National Policy 58-201 Corporate Governance Guidelines (NP 58-201), issued by the CSA, a group composed of the 10 provincial regulators, recommends that a board adopt a written mandate in which it acknowledges responsibility for stewardship of the corporation.

Committees

The board may delegate certain of its responsibilities to committees of directors. Certain responsibilities may not be delegated to a committee of the board, including (under the Canada Business Corporations Act):

a making changes to the by-laws;
b approving the annual financial statements, a management proxy circular, a takeover bid circular or directors' circular;
c issuing securities (except on terms already approved by the board);
d declaring dividends; and
e purchasing or redeeming shares of the corporation.

In practice, the committees of many boards do not formally approve the matters before them but return the matter to the full board with their recommendation.

All public corporations are required by statute to have an audit committee. Private corporations frequently choose to have an audit committee as a matter of good practice. Most public corporations also have separate committees to deal with compensation matters and director nominations and corporate governance. Corporations with larger boards may also have an executive committee. Boards also strike *ad hoc* or special committees from time to time to address specific issues or transactions.

Under the corporate statutes, the audit committee of a public corporation must be composed of at least three directors, a majority of whom must not be employees of the corporation or any of its affiliates. However, National Instrument 52-110 Audit Committees (NI 52-110) of the CSA requires that public corporation audit committees be composed of at least three members, all of whom must be 'independent' directors,

as defined in that instrument. NI 52-110 also requires that all members of the audit committee be 'financially literate' – that is, that they have the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the issues that can reasonably be expected to be raised by the corporation's financial statements. Furthermore, corporations must disclose the education and experience of each audit committee member that is relevant to the performance of his or her responsibilities as an audit committee member.

Public corporations are required to disclose publicly on an annual basis the processes by which a board determines compensation for the corporation's directors and officers, including the responsibilities, powers, experience and operation of the compensation committee of the board, if any, and the identity, mandate and compensation paid to any advisers retained by the committee in the past financial year. The overwhelming majority of Canadian public corporations establish a board committee that has responsibility for overseeing compensation matters. NP 58-201 recommends that a board appoint a compensation committee composed entirely of independent directors with responsibilities for oversight of the compensation payable to senior executives. The members of the compensation committee are not required to be independent or to have any particular expertise. However, if the compensation committee is not comprised solely of 'independent' directors as defined in Section 1.4 of NI 52-110, the corporation must disclose what steps the board takes to ensure an objective process for determining executive compensation.

Most Canadian public corporations also have a board committee that has responsibility for overseeing the process for nominating directors for election by shareholders. NP 58-201 recommends that, before an individual is nominated as a director, the board, with advice and input from the nominating committee, should consider the competencies and skills that the board, as a whole, should possess; the competencies and skills of each existing director and of each new nominee; and whether the new nominee can devote sufficient time and resources to serving as a director. Public corporations are required to disclose publicly on an annual basis the process by which the board identifies new candidates for nomination and the responsibilities, powers and operation of the nominating committee. The members of the nominating committee are not required to be independent or to have any particular expertise. However, if the nomination committee is not comprised solely of 'independent' directors as defined in Section 1.4 of NI 52-110, the corporation must disclose what steps the board takes to ensure an objective nominating process.

Board chair

Boards appoint a chair from among the directors with responsibility to provide leadership to the board to enhance board effectiveness. The chair is responsible for, among other things, managing the board, setting the agenda, ensuring that directors are kept informed, presiding at director and shareholder meetings, and acting as a key liaison between the board and senior management.

Canadian boards typically do not appoint the CEO as board chair. Concerns about board accountability and process and the desire to provide independent leadership to the board have led most larger public corporation boards in Canada to appoint an

independent director as board chair. NP 58-201 recommends that the chair of the board should be an independent director and, where this is not appropriate, an independent director be appointed as lead director. Public corporations are required to disclose whether or not the chair is an independent director and, if not, to disclose whether the board has a lead director. If there is no independent chair or independent lead director, a corporation must then disclose what the board does to provide leadership for its independent directors.

ii Directors

Directors are fiduciaries of the corporation they serve. This obligation and duty arises under common law and is codified in the corporate statutes in the requirement that directors act honestly and in good faith with a view to the best interests of the corporation, and must exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. This fiduciary relationship requires a strict standard of conduct that includes loyalty and good faith and requires directors to avoid putting themselves in a position where their duty to act in the best interests of the corporation conflicts with their other obligations.

Directors are required by corporate statutes to discharge their fiduciary duty 'with a view to the best interests of the corporation'. The Supreme Court of Canada has stated that directors owe their fiduciary duty to the corporation and that the best interests of the corporation must not be confused with the interests of the corporation's shareholders or any other stakeholders of the corporation.

Director qualifications

Canadian corporate statutes impose minimal qualifications for directors. Any individual who is 18 or over and of sound mind and who is not bankrupt may serve as a director. Some Canadian corporate statutes also require that a certain percentage of directors of the board and committees be resident Canadians.

The ability of the board to exercise independent judgement is of fundamental importance to the governance of public corporations. As a result, most public corporation boards have a number of 'independent' directors. Independent directors and the role they play in ensuring the board is able to exercise independent judgement have been a focus for those concerned with accountability in corporate governance. Rules for the determination of who may be considered to be an independent director are set out in both corporate and securities legislation in Canada. In addition, some Canadian institutional shareholders set their own standards for assessing director independence.

The corporate statutes define an independent director as any director who is not employed by the corporation or one of its affiliates. Under this definition, recently retired employees of the corporation and representatives of a controlling shareholder of the corporation would qualify as 'independent'. Further, as the term 'affiliates' involves the concept of control, directors or employees of a major, but not controlling, shareholder are technically independent under the corporate statutes.

The TSX requires a listed corporation to have at least two independent directors. For this purpose, an independent director is a person who:

a is not a member of management and is free from any interest and any business or other relationship that could reasonably be perceived to materially interfere with the director's ability to act in the best interest of the corporation; and

b is a beneficial holder, directly or indirectly, or is a nominee or associate of a beneficial holder, collectively of 10 per cent or less of the votes attaching to all issued and outstanding securities of the corporation.

However, the TSX does not consider a person to be independent if within the past three years they have served as an employee or service provider to the listed corporation or its affiliates or they currently serve as an employee or controlling shareholder of a company that has a material business relationship with the listed corporation.

For publicly traded corporations, there is yet another definition of 'independent director'. The definition is set out in Section 1.4 of NI 52-110 of the CSA and requires the board to consider whether there is a material relationship between the director and the corporation that could, in the board's view, be reasonably expected to interfere with the exercise of that director's independent judgement. In making its determination, the board must consider all direct and indirect relationships between a director and the corporation – past, present and anticipated – both individually and collectively. The board's determination is subject to certain 'bright-line' tests that are similar to the director independence tests under the New York Stock Exchange's corporate governance listing requirements. Under such tests, recently retired employees and employees of a parent of the corporation are not independent. Public corporations are required to disclose annually which of the directors on the board are independent and which are not, and describe the basis for determining that a director was not independent. For audit committee purposes, there are additional bright-line director independence tests set out in Section 1.5 of NI 52-110 that correspond to requirements under the Securities Exchange Act of 1934 in the United States.

Election and term

Directors are usually elected by shareholders at the corporation's annual meeting. Most Canadian corporations provide shareholders with the opportunity to vote on each director individually, instead of en bloc for a slate of directors. Slate voting for directors is rare in Canada since the TSX senior exchange requires all its listed companies to provide for individual voting for directors. Shareholders may vote for directors or withhold their vote but cannot vote 'against' a director. A corporation's articles may provide for cumulative voting for directors, whereby each shareholder may cast one vote for each share held multiplied by the number of directors to be elected. However, this is very rare. The articles of a corporation may also permit a particular class of security holders, such as preferred shareholders, to elect one or more directors, or may permit a particular class of security holders to hold multiple voting rights, such as 10 votes per share.

Since 30 June 2014, companies listed on the TSX, other than majority-controlled companies, have been required to have adopted majority voting for the election of directors, either as a board policy or as an amendment to their constating documents. Under majority voting, if in an uncontested election more votes are withheld from the election of a director than are voted in favour of the director's election, the director must immediately tender a resignation for consideration by the board. The board must accept

the resignation absent exceptional circumstances and it must make its determination as to whether to accept the resignation within 90 days and announce it via press release it promptly thereafter. A copy of this press release must also be provided to the TSX.

Directors are generally elected annually. Although corporate statutes permit directors to be elected for terms of up to three years and on a staggered basis, such practices are rare since most Canadian corporate statutes permit shareholders to remove one or more directors from office mid-term and elect their replacements. In addition, the TSX senior exchange requires all its listed companies to elect directors annually.

Board diversity requirements

Virtually all Canadian issuers subject to public reporting requirements in Canada, other than 'venture issuers' and investment funds, are subject to disclosure requirements respecting the representation of women on the board and in senior management and respecting board renewal mechanisms. All provinces and territories other than Alberta, British Columbia, Yukon and Prince Edward Island implemented amendments to a national instrument on disclosure of corporate governance practices effective as of 31st December 2014 that requires issuers to disclose annually in the proxy circular for the annual meeting (or the annual information form if the issuer does not send a proxy circular to its investors) the number and percentage of women directors and women who are executive officers. Such issuers must disclose whether:

a the issuer has adopted term limits for board service or other mechanisms for board renewal, and if so to describe them and, if not, to explain why;

b the issuer has a written policy for the identification and nomination of women directors and, if not, to explain why;

c the board considers the level of representation of women on the board in identifying and nominating candidates for director and how it does so, and if it does not, to explain why;

d the issuer considers the level of representation of women in executive officer positions when making executive officer appointments and how it does so, and if it does not, to explain why; and

e the issuer has adopted targets respecting the number or percentage of women on the board and in executive officer positions, and if not, to explain why.

If an issuer has adopted a written policy for the identification and nomination of women directors, the issuer must summarise the policy and its objectives, the measures taken to implement it, the annual and cumulative progress made on achieving the objectives and whether, and if so how, the board or nominating committee measures the policy's effectiveness. If targets regarding women on the board or in executive officer positions have been adopted, the issuer must disclose the annual and cumulative progress made on achieving the targets.

III DISCLOSURE

All Canadian corporations are subject to periodic reporting to shareholders. In the case of a private corporation, periodic reporting may consist solely of the delivery of annual

financial statements and a notice of an annual shareholder meeting. Public corporations are also subject to continuous disclosure reporting requirements under Canadian securities laws.

Periodic disclosure requirements require public corporations to file publicly certain documents on the System for Electronic Document Analysis and Retrieval (SEDAR) including:

a annual and quarterly financial statements, and related management's discussion and analysis;

b an annual information form describing the corporation and its business; and

c information circulars in respect of shareholder meetings, including disclosure respecting compensation paid or payable to the directors and certain named executive officers.

Canadian public corporations are also subject to timely disclosure obligations. Under Canadian securities laws, public corporations must issue and file on SEDAR a press release as soon as there has been a material change in the business, operations or capital of the corporation that would reasonably be expected to have a significant effect on the market price or value of any of the corporation's securities. They must also file a material change report on SEDAR within 10 days of the date of such material change. TSX rules also require listed corporations to promptly disclose by press release any fact that would reasonably be expected to have a significant effect on the market price or value of any of the corporation's securities.

Failure to comply with periodic filing requirements and timely disclosure obligations may lead to enforcement proceedings by securities administrators. In addition, investors in most jurisdictions in Canada may have a statutory right of action against the corporation and its directors and officers for damages in the event that written or oral disclosure by the corporation is misleading or untimely. Although there are statutory limits on such liability, class action proceedings alleging misleading or untimely disclosure are becoming increasingly prevalent in Canada.

Directors, certain officers, 10 per cent shareholders and certain others are required to file on the System for Electronic Disclosure by Insiders (SEDI) insider reports detailing their holdings of securities and related financial instruments, including equity-based compensation holdings, and other arrangements involving, directly or indirectly, a security of the public corporation or related financial instrument. Persons acquiring more than 10 per cent of any class of securities of the public corporation are required to issue a press release and file a report disclosing their holdings.

Many Canadian corporations also provide a range of supplemental voluntary disclosures that they publish on their corporate websites. Public corporation websites typically include links to documents filed on SEDAR and press releases issued by the corporation, as well as supplemental information provided to analysts, recordings or transcripts of analyst or investor calls, and key corporate governance documents (such as the board and committee charters and code of conduct).

IV CORPORATE RESPONSIBILITY

Directors are permitted to consider various stakeholder interests in determining whether they are acting in the best interests of the corporation. In the Supreme Court of Canada's decision in *BCE Inc v. 1976 Debentureholders*, the Court stated that where there are conflicting stakeholder interests, it falls to the directors to resolve them in accordance with their fiduciary duty to act in the best interests of the corporation, viewed as a 'good corporate citizen'. By this reference, together with the Court's focus on what is in the corporation's best interests, the Supreme Court of Canada has rejected a purely shareholder-centric understanding of the duties of a board. Rather, there is recognition that corporations have a responsibility to consider the community in which they operate and boards have to balance many competing factors and interests when making decisions.

Many Canadian corporations seek to enhance stakeholder trust including through voluntary participation in initiatives such as the Global Reporting Initiative's Sustainability Reporting Guidelines.

Boards are responsible for setting the tone at the top by approving codes of conduct for employees and directors that set out the board's expectations regarding compliance with laws, handling of conflicts of interest and use of resources and stakeholder relations. NP 58-201 states that the board is responsible for satisfying itself as to the integrity of the CEO and other executive officers of the corporation and that the CEO and other executive officers create a culture of integrity throughout the organisation. The audit committee is required under NI 52-110 to establish procedures for the receipt, retention and treatment of complaints received by the corporation regarding accounting, internal accounting controls or auditing matters and the confidential, anonymous submission by employees of the corporation of concerns regarding questionable accounting or auditing matters. Most corporations satisfy this requirement by adopting a whistle-blowing policy that addresses not only reporting of such matters, but also reporting of potential violations of the corporation's code of conduct.

V SHAREHOLDERS

Although directors owe a duty to the corporation and not its individual shareholders, shareholders are accorded a special role in the governance of Canadian corporations. Increasingly, shareholders in Canada are taking steps to make their views known to the board and are exercising their rights when the board's response or corporate performance is not satisfactory.

i Shareholder rights and powers

Under Canadian corporate statutes, shareholders elect the directors and appoint the external auditors of the corporation. Certain matters of fundamental importance are also required to be approved by shareholders, including changes to the articles and by-laws, amalgamations, reorganisations, the sale of all or substantially all of the corporation's assets and the continuance of the corporation to the laws of another jurisdiction. In

addition, TSX rules require listed corporations to obtain shareholder approval of certain dilutive transactions and for share-based compensation arrangements involving new issuances of shares.

If a shareholder believes that the actions of the corporation have been unfairly prejudicial to its interests, the corporate statutes provide several ways for the shareholder to take action against directors. First, a shareholder may apply to the court for an order compelling the directors to comply with the corporation's articles, by-laws or governing statute. Second, a shareholder can pursue a derivative action, which allows the shareholder to require the corporation to take action against the directors in the name and on behalf of the corporation. Third, a shareholder may take advantage of the oppression remedy. The oppression remedy is a very broad remedy available to a complainant where the corporation, the board or the corporation's affiliate has acted in a manner that was oppressive or unfairly prejudicial to, or that unfairly disregarded, the complainant's interests. The remedy gives a court 'broad, equitable jurisdiction to enforce not just what is legal but what is fair' to protect the reasonable expectations of the shareholders.

In addition, shareholders have available to them a range of tools in Canada to exert pressure on corporations they feel are underperforming, all of which are intended to force a reluctant management or board to engage in a dialogue.

Canadian corporate statutes allow shareholders holding at least 5 per cent of the issued shares of a corporation to require directors to convene a shareholder meeting for a broad range of purposes relating to the business of the corporation so long as they respect certain prescribed criteria.

The corporate statutes also permit a shareholder to circulate a proposal to shareholders with a supporting paragraph containing not more than 500 words describing the topic the shareholder wishes to raise at an upcoming shareholder meeting. If the proposal meets time parameters and certain other limited criteria, it must be included in the management information circular sent to shareholders of the corporation. A shareholder proposal submitted by shareholders representing more than 5 per cent of the outstanding shares may include proposed director nominees. Although there continues to be considerable debate regarding 'proxy access' in the United States, and although 'proxy access' is the subject of a recent CCGG proposal, the ability of shareholders to submit a shareholder proposal including director nominees has been a long-standing provision of Canadian corporate law.

Once a shareholder meeting has been called, any shareholder can solicit proxies either for or against any matter properly before the meeting, including the election of one or more directors, by providing a dissident proxy circular containing prescribed information to the person solicited prior to or contemporaneously with the solicitation. In recent years, rules respecting what constitutes solicitation and exempting certain practices from the proxy solicitation rules have been relaxed in favour of shareholders. For example, Canadian securities laws now allow a shareholder to solicit proxies by way of public broadcast or speech, or by way of publication, without having to incur the costs associated with preparing and mailing a dissident proxy circular, provided certain conditions are met.

ii Shareholder activism

Shareholders of Canadian corporations now seem to be increasingly prepared to exercise voting rights and submit shareholder proposals as a means of encouraging change at corporations. In part, this reflects increased activity in Canada from a number of US-based funds that have traditionally been active in trying to influence the governance of US corporations and have come to realise that the Canadian environment is comparatively favourable to shareholder activist activity. For example, some Canadian companies have tangled with Carl Icahn (Fairmont Hotels, Lions Gate Entertainment, Talisman Energy), Crescendo Partners (Cott Corporation), Jana Partners (Agrium) and Pershing Capital (CP Rail). In addition, although Canadian fund managers have historically been more than comfortable making their views known to corporate boards and the public, they have periodically demonstrated an increased appetite for formally opposing corporate activity. In 2010, the Canada Pension Plan Investment Board and the Ontario Teachers' Pension Plan Board were highly vocal opponents of the terms on which Magna International proposed to eliminate its dual-class share structure (and launched an ultimately unsuccessful court challenge).

Some of the reasons the Canadian environment is more favourable to shareholder activists are:

a the use of staggered boards is ineffective as most Canadian corporations' directors may be removed at any time by a simple majority vote of shareholders;

b there are clear rights to requisition meetings with a 5 per cent ownership interest and a clear entitlement to a shareholder list;

c it is easier for shareholders to include proposals on the election of directors in management proxy circulars;

d the threshold for giving notice that a shareholder has accumulated a significant ownership position is higher at 10 per cent and the reporting regime after hitting that threshold is less onerous; and

e the TSX requires any listed issuer adopting a shareholder rights plan (i.e., poison pill) to obtain shareholder approval of the plan within six months of its adoption, which gives institutional shareholders the ability to influence the terms of these plans. Moreover, unlike the Delaware courts in the United States, Canadian securities regulators have consistently been prepared to terminate rights plans once they have given a board time to pursue alternatives to a hostile bid (typically 50–70 days). In February 2016 the CSA announced amendments to the takeover bid regime in Canada that are expected to come into force in May 2016. These amendments afford a target company up to 105 days to respond to a hostile bid and are discussed in more detail under 'Takeover Defences' below.

Shareholder activism has prompted a large number of Canadian corporations in recent years to amend their by-laws to require advance notice in respect of nominations for director, resulting in increased scrutiny of such provisions by proxy advisory services. Corporations have also looked at adopting shareholder rights plans that may be triggered by shareholders entering into voting agreements or conducting a proxy solicitation, although such provisions are controversial.

iii Contact with shareholders

Shareholder communication is a fundamental and long-standing aspect of the board's fiduciary oversight responsibility. Boards must take shareholder interests into consideration, and so they have an interest in understanding shareholder views about the corporation, its governance and its operations. Accordingly, Canadian corporations have a long-standing practice of consulting with their principal shareholders on matters that may be of interest to them. The importance of shareholder communications is recognised in NP 58-201, which states that the board is responsible for adopting a communication policy for the corporation.

All Canadian corporations have some form of shareholder communications programme through which the corporation communicates material information to shareholders. Typically, the corporation's disclosure practices are summarised in a disclosure policy and a management disclosure committee is tasked with responsibility for ensuring compliance with the disclosure policy and the corporation's disclosure controls and procedures.

However, traditional shareholder communication and investor relations practices no longer satisfy shareholder demands for increased transparency, more frequent communications and more opportunities to express their views on how the corporation should be run, as evidenced by shareholder-led initiatives on majority voting for directors and say on pay. Some investors have actively sought the opportunity to meet with directors in addition to, or in lieu of, management. The CCGG has a regular annual programme through which its representatives meet with directors of almost 50 Canadian corporations each year to share perspectives on the corporation, its strategies, performance and management. Generally, management is not present for these meetings.

iv Takeover defences

In February 2016 the CSA announced fundamental amendments to the takeover bid regime in Canada which are expected to come into force on 9 May 2016. These amendments afford a target company up to 105 days to respond to a hostile bid. Although shorter periods may apply in the event the target company's board of directors agrees or in the event an 'alternative transaction' is entered into by the target company, the amendments afford a target company significantly more time to respond to the bid than is typically provided under the current regime.

The amendments do not specifically address how shareholder rights plans will be treated after the new regime comes into force, though the CSA have indicated that the existing takeover bid defence regime will continue to apply. Therefore, given the increased time afforded to a target company to respond to a hostile bid under the amendments, absent unusual circumstances, it is expected that shareholder rights plans will not be permitted to remain in effect after the 105-day period expires.

This new 105-day mandatory minimum bid period may also decrease the incentive for issuers to adopt shareholder rights plans either 'strategically' at their annual general meetings or 'tactically' in the face of a hostile bid. However, because the amendments do not apply to exempt takeover bids, there will likely continue to be a role for shareholder rights plans in protecting a target company from a 'creeping bid' made through normal course purchases and private agreement exemptions and to prevent hard 'lock-up'

agreements, and for tactical 'voting pills' in the context of proxy contests (in order to stop a dissident group from representing more than a given percentage (e.g., 20 per cent) of the outstanding shares).

The amendments may also affect the structure of white knight transactions in Canada. The amendments require the initial hostile bid to remain open for at least 105 days, but this period may be shortened if the target company enters into a white knight transaction. If the white knight transaction is structured as a takeover bid, the hostile bid will be entitled to the same bid period as the white knight. However, if the white knight transaction is structured in another fashion, such as an arrangement or amalgamation transaction, the hostile bid may be shortened to a minimum of 35 days from the original commencement date of the hostile bid. As this would leave the white knight at a timing disadvantage, the new regime creates an incentive for white knight transactions to be structured as bids rather than 'alternative transactions'.

The amendments also mandate a minimum tender requirement of more than 50 per cent of the outstanding securities that are the subject of the takeover bid (other than those owned, or over which control or direction is exercised, by the bidder and any joint actors). Among other things, this will eliminate the ability to make 'any-or-all' takeover bids in Canada and will make takeover bids for target companies with significant minority shareholders more difficult to complete.

VI OUTLOOK

Shareholders, whether activist shareholders or active institutional shareholders, have increasingly influenced both regulatory developments and best practices in Canada on corporate governance. Their influence has prompted boards to become more involved in engaging with the corporation's shareholders on corporate governance matters, and this has been aided by a growing focus not only by boards but also long-term active institutional shareholders on the importance of taking a longer-term perspective and avoiding decisions motivated solely by short-term results. In addition, continued scrutiny by shareholders, regulators, other stakeholders and the media have substantially increased the complexity of board oversight of Canadian companies.

Appendix 1

ABOUT THE AUTHORS

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Andrew MacDougall is a partner in Osler's Toronto office and practises corporate and securities law, with a particular focus on mergers and acquisitions and corporate governance. In his corporate governance practice, he advises boards and management on a broad spectrum of corporate governance issues, including directors' duties, executive compensation, shareholder engagement and shareholder meeting matters, and he has written and spoken extensively on these topics. He has also advised Canadian securities regulators and various professional bodies in Canada that are active in the governance area. Mr MacDougall is an inaugural fellow of the American College of Governance Counsel.

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Robert Yalden is a partner in Osler's Montreal office. He is co-chair of the firm's national mergers and acquisitions group and head of the Montreal office's corporate group. His career with Osler spans 25 years, during which he has been involved with some of Canada's most innovative and ground-breaking transactions. Mr Yalden has advised boards of directors and senior management in connection with a wide range of corporate governance and M&A mandates. He was part of the Osler team that implemented the first poison pill in Canada. He led the Osler legal teams involved in Canada's largest-ever completed leveraged buyout, as well as the largest private equity deals in Quebec in 2014 and 2015. He has recently been involved with a significant proxy fight that has seen the problems of 'empty voting' on the part of hedge funds receive considerable public scrutiny in Canada. He is the co-author of *Business Organizations, Policies and Practices* (2008) and teaches a course in comparative corporate governance at McGill University's faculty of law.

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