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ARTICLE

What public companies should expect in 2017

With the 2017 proxy season just around the corner, many Canadian public companies may be wondering what lies ahead. On Jan. 17, 2017, the TMX Group (the TMX) and BLG hosted an event "What Public Companies Should Expect in 2017," which included a panel discussion about 2017 proxy season updates and recent regulatory developments, as well as a lively discussion about shareholder activism in Canada.

Speakers included Ungad Chadda, Julie Shin and Tim Babcock of the TMX, Poonam Puri of Osgoode Hall Law School, Amy Freedman of Kingsdale Advisors, David Surat of the Ontario Securities Commission and Gordon Raman, Manoj Pundit and Philippe Tardif of BLG. See below for a summary of the 2017 proxy season updates and recent regulatory developments discussed.

Proxy season updates

- Say-on-pay resolutions are voluntary resolutions that issuers may put before shareholders and which enable such shareholders to cast advisory (non-binding) votes on executive compensation. Say-on-pay votes are becoming increasingly popular among Canadian issuers, and according to "2016 Best Practices for Proxy Circular Disclosure" by the Canadian Coalition for Good Governance, more than 50 per cent of the issuers in the S&P/TSX composite index offer their shareholders a say-on-pay vote. Companies that have had their say-on-pay votes fail to pass have generally been companies whose shareholders may have perceived that executive compensation was inconsistent with shareholder returns.
- On July 18, 2016, the Canadian Securities Administrators (CSA) published CSA Staff Notice 51-346 – *Continuous Disclosure Review Program Activities for the fiscal year ended March 31, 2016*, which discusses the results of its continuous disclosure reviews in fiscal 2016. 62% of the 902 reviews required issuers to improve or amend their disclosure (compared to 59% of the 1,058 reviews conducted in 2015). Certain key comments from the CSA are set out below:
    - Financial Statements. In their financial statements, issuers should (i) disclose sensitivity analysis for each type of market risk to which the issuer is exposed; (ii) recognize contingent consideration received in transactions at fair value on the acquisition date; (iii) with respect to purchase prices received in business transactions, ensure that purchase prices are properly allocated among the assets and that all applicable assets are recognized; (iv) not change their functional currency at a time that does not correspond to the time of the change in underlying circumstances; (v) ensure that they meet the aggregation criteria and disclose judgements made by management in applying the criteria if they intend to aggregate several operating segments into a single operating segment; and (vi) ensure that they include adequate disclosure with respect to credit risk.
    - MD&A. In their MD&A, issuers should (i) discuss the issuer's ability to meet obligations as they become due and how the issuer expects to resolve the deficiency or default if they have or expect to have a working capital deficiency or if they have debt covenants that they have breached or may soon breach; (ii) provide adequate forward-looking information disclosure and (iii) base their discussion of operating segments on the operating segments disclosed in their financial statements.
- In November 2016, Institutional Shareholder Services ("ISS") and Glass Lewis updated their respective Proxy Voting Guidelines for meetings on or after Feb. 1, 2017. Certain key recommendations are set out below.
    - Auditors' fees. ISS currently recommends (i) voting for proposals to ratify auditors unless non-audit related fees paid to the auditor exceed audit and audit-related fees and (ii) withholding votes for individual directors who are members of an audit committee if non-audit fees paid to the external audit firm exceed audit and audit-related fees. Going forward, ISS will recommend (i) voting for proposals to ratify auditors unless non-audit fees are greater than the sum of audit fees, audit-related fees and tax compliance/preparation fees and (ii) withholding votes for individual directors who are members of the audit committee if non-audit fees exceed the sum of audit fees, audit-related fees and tax compliance/preparation fees. ISS will consider tax fees not directly related to tax compliance services to be non-audit fees.
    - Director compensation. On a case-by-case basis, ISS will generally recommend a vote withhold for a member of a director compensation committee (or where there is no such committee, the chair of the board or the entire board) where director compensation practices could compromise a non-employee director's independence or could otherwise be problematic from a shareholder's perspective.
    - Overboarding. The 2017 Glass Lewis "overboarding" guidelines codify the policies set out in its 2016 guidelines. Glass Lewis will generally recommend voting against (i) a director who serves as an executive officer of any public company while serving on more than two public company boards and (ii) a non-executive director who serves on more than five public company boards. ISS will only consider a director to be "overboarded" if he or she (i) sits on an excessive number of boards and (ii) has a poor attendance record. It is therefore possible that Glass Lewis could recommend voting against a particular director while ISS recommends voting in favour.
    - Full value awards. Glass Lewis clarified its approach to equity compensation plans that provide "full value" awards such as RSUs or DSUs. Glass Lewis will generally recommend voting against full value award plans that have a limit set at a rolling maximum in excess of five per cent of the applicable company's share capital.
    - Shareholder rights plans. ISS and Glass Lewis both amended their voting guidelines to reflect the new requirement imposed by NI 62-104 *Take-Over Bids and Issuer Bids* that take-over bids must have a minimum deposit period of 105 days. Both firms will recommend that shareholders vote against plans where the minimum period for a permitted bid exceeds 105 days.
- On March 31, 2016, the CSA issued CSA Multilateral Staff Notice 54-304 — *Final Report on Review of the Proxy Voting Infrastructure and Request for Comments on Proposed Meeting Vote Reconciliation Protocols (March 31, 2016)* and on Jan. 26, 2017, the CSA issued CSA Staff Notice 54-305 — *Meeting Vote Reconciliation Protocols*. The Protocols stemmed from investors' concerns that the proxy voting infrastructure and meeting vote reconciliation processes are unreliable and non-transparent. The Protocols are voluntary and set out in detail the roles and responsibilities for the key parties involved in meeting vote reconciliation and describe the procedures such entities should implement to ensure such roles and responsibilities are fulfilled. The Protocols provide for a feedback process from meeting tabulators to intermediaries to beneficial owners when beneficial owners' voting entitlements are rejected or prorated. In events where tabulators reject or prorate proxies, they will be obligated to advise the intermediary, who will be required to report the same to the applicable beneficial owner. The Protocols also include guidance with respect to how involved parties can establish end-to-end voting entitlements, to confirm whether votes will be accepted by the tabulator.

Regulatory developments

- New exempt market filings are now available to issuers, including the *Investment Dealer Exemption* available in British Columbia, Alberta, Saskatchewan, Manitoba and New Brunswick, which will permit issuers listed on a Canadian exchange to raise capital by distributing securities to investors who obtain advice from a registered investment dealer; the *Offering Memorandum Exemption* available in Ontario through the use of a prescribed-form offering memorandum; and the *Crowd Funding Exemption* available in Manitoba, Ontario, Québec, New Brunswick and Nova Scotia, which is designed to facilitate capital raising activities for start-ups and small businesses through a crowd funding prospectus exemption and online

funding portal.

- The harmonized Take-Over Bid regime for non-exempt take-over bids has been implemented through the adoption of NI 62-104 *Take-Over Bids and Issuer Bids*, which now requires that a minimum of 50 per cent of all target securities be tendered to a bidder. If the 50 per cent minimum tender is met, the bid must be extended for 10 days to give security holders who have not tendered an opportunity to tender. Lastly, the minimum period that a take-over bid must be open for is 105 days, which may be reduced to 35 days by the target company.
- The Ontario Securities Commission adopted a Whistleblower Policy (OSC Policy 15-601). The policy establishes a whistleblower program which introduces monetary awards for "whistleblowers" — individuals who provide voluntary, original information regarding a violation of Ontario securities law that has occurred, is ongoing or is about to occur.
- The Insider Trading prohibition under Ontario's *Securities Act* has been expanded, and now prohibits "recommending" or "encouraging" the purchase or sale of securities of an issuer where the person or company recommending or encouraging the purchase or sale is in a "special relationship" with the issuer and is in possession of material information that has not been generally disclosed to the public.
- CSA Staff Notice 11-332 regarding Cybersecurity provides direction on cybersecurity risk management and encourages issuers to consider their disclosure obligations with respect to cyber risks and incidents. More recently, the CSA issued Multilateral Staff Notice 51-347 — *Disclosure of cyber security risks and incidents*, which supplements CSA Staff Notice 11-332 and provides further guidance to assist issuers in complying with their legal obligations to ensure that investors have timely, material information to make informed investment decisions.
- Several amendments to the *Canada Business Corporations Act* have been tabled by Parliament in Bill C-25. Of particular interest to issuers incorporated under the *Canada Business Corporations Act* are amendments that may require changes to voting on the election of directors and the disclosure of gender diversity among their directors and senior managers.
- On Sept. 28, 2016, the CSA published CSA Multilateral Staff Notice 58-308 – *Staff Review of Women on Boards and in Executive Officer Positions*, which summarizes a sample of non-venture issuers' compliance with NI 58-101 — *Disclosure of Corporate Governance Practices*. The results of the 2016 review in comparison to the results of the 2015 review suggest that, overall, there were more women on boards in 2016 than in 2015 and that 12 per cent of the total board seats in the sample were held by women, compared to 11 per cent in 2015.
- In 2016, the Toronto Stock Exchange (the TSX) conducted a review of issuers' Majority Voting policies. All TSX-listed issuers must implement majority voting policies, which must require that if a majority of shareholders do not vote in favour of a director, such director must tender his or her resignation. In "exceptional circumstances," issuers may reject such resignations. The TSX 2016 review found that approximately half were non-compliant. Specifically, certain issuers are interpreting the term "exceptional circumstances" too broadly. "Exceptional circumstances" should only include circumstances wherein, if the company did not accept the resignation of a director who did not receive a majority vote, the company would breach either (i) corporate law or (ii) a covenant in a contract.
- There are new implementation milestones in connection with the Cooperative Capital Markets Regulatory System. Specifically, the aim is to now have the *Capital Markets Act* — the principal legislation setting the Canadian capital markets regulatory framework — enacted by June 30, 2018, with the Capital Markets Regulatory Authority — the common regulator responsible for administering securities laws — to be operational by 2018.
- The TSX Venture Exchange is engaged in ongoing efforts to revitalize Canada's public venture market, building off commitments outlined in its 'Whitepaper' (published December 2015). Specifically, the TSX Venture Exchange remains committed to effecting the following positive changes to the TSX Venture Exchange market: (i) reducing issuers' administrative and compliance costs without compromising investor and (ii) diversifying and growing its stock list to make the market more attractive.

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