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CORPORATE GOVERNANCE AND DIRECTORS' DUTIES

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Corporate governance and directors' duties in Canada: overview

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CORPORATE GOVERNANCE TRENDS

1. What are the main recent corporate governance trends and reform proposals in your jurisdiction?

Shareholder democracy

Shareholder activism continues to be an important trend in corporate governance, demonstrated by more frequent shareholder proposals and an increasing level of engagement between shareholder activists and management.

On 28 September 2016, the federal government of Canada (Federal Government) recognised this trend by introducing Bill C-25 (Bill). At the time of writing, the Bill had only received its Second Reading. If passed into law, the Bill will amend the Canada Business Corporations Act (CBCA) to adopt, among other things, a mandatory majority voting regime for public companies incorporated under the CBCA. The proposed new regime will allow shareholders that are dissatisfied with a directorship candidate to vote against their election. The currently available option is simply to abstain from voting for that candidate. The Bill contemplates exceptions to this regime, however these have yet to be articulated to be set in the corresponding regulations. The purpose behind introducing this new regime is to prevent under-supported directors (that is, directors who receive few votes in his or her favour but many abstaining votes) from being elected.

These proposed changes generally follow the changes adopted by the Toronto Stock Exchange (TSX) to its TSX Company Manual (TSX Manual) on 30 June 2014. The TSX Manual now requires all TSX-listed companies, except listed companies that are majority controlled, to implement majority voting procedures or policies for director elections at uncontested meetings. In particular, the TSX Manual requires that:

- Each individual director of a TSX-listed company must be elected by a majority of the votes cast with respect to his or her election (majority voting requirement).
- A TSX-listed company must adopt a majority voting policy if it does not otherwise satisfy the majority voting requirement in a manner acceptable to the TSX (for example, in its articles or bye-laws).

If a TSX-listed company adopts a majority voting policy, it must also include a full description of the policy in the materials provided to its shareholders in connection with its annual meeting.

For 2016, proxy advisory firm Institutional Shareholders Services (ISS), a prominent proxy advisory firm, recommended that shareholders withhold votes from all directors nominated by slate ballot. Glass Lewis, another advisory firm, recommended that shareholders withhold votes for the members of the corporate governance committee if the company in question has not adopted majority voting procedures or policies.

For the 2017 proxy season, ISS recommends, irrespective of whether the company has adopted majority voting policies or procedures, that shareholders withhold votes for an individual director if such a director is "overboarded" and has attended less than 75% of board and committee meetings in the past year, without a valid reason for such absences. ISS defines an "overboarded" director as either:

- A Chief Executive Officer (CEO) of a public company who sits on more than one outside public company board in addition to the company of which he/she is CEO.
- A director who is not a CEO of a public company and sits on more than four public company boards.

Glass Lewis' voting recommendations for "overboarding" in 2017 are based on a threshold of two total boards for a director who serves as an executive officer of a public company, and five total boards for a director who is not a public company executive. For companies listed on the TSX Venture Exchange (the emerging company exchange of the TSX), Glass Lewis applies a more lenient "overboarding" standard than the foregoing.

With the rise in shareholder activism, an increasing number of listed companies have implemented advance notice policies, which generally require that notice of director nominations and detailed information about nominees and dissident shareholders be provided to management in advance of a shareholder meeting. The advance notice policy has become an important mechanism to protect companies from activist shareholders who may otherwise attempt to ambush a shareholders' meeting by bringing a surprise motion to nominate directors. The advance notice policy mechanism has received endorsement from the Supreme Court of British Columbia, as well as limited endorsements from ISS and Glass Lewis. ISS recommends withholding votes for the election of directors where the board has adopted an advance notice policy but does not seek shareholder approval of such policy at the next shareholders' meeting. Glass Lewis recommends that shareholders only approve an advance notice policy to the extent that the policy imposes reasonable restrictions (generally 30 days) on nomination rights, and does not present excessive impediments on shareholders who wish to nominate directors under the policy.

Diversity on corporate boards

Diversity on corporate boards continues to be an important topic in today's corporate reforms. Academics and industry participants alike comment on the need for corporate boards to better reflect the makeup of their stakeholders, which can be achieved by adopting diversity measures such as a focus on improving gender diversity. As of 28 September 2016, the Canadian Securities Administrators reported that Canadian companies are making some progress in adding women to their boards, albeit slowly. A review of diversity disclosure reports filed this year by 677 TSX-listed companies shows that 21% have adopted a policy to identify and nominate women (up from 15% last year) and 18% have diversity policies that do not specifically address women. In contrast, 59% still have not adopted written policies of any kind.

The Federal Government addressed this issue by introducing amendments to the CBCA in the Bill. If passed into law, this will (among other things) require directors of "prescribed corporations" to disclose to its shareholders at every annual shareholders' meeting the prescribed diversity information in relation to the directors and members of senior management. Background information provided by the Federal Government for the proposed amendments to the CBCA suggests that the new diversity disclosure requirements will be on a "comply or explain" basis.

The adoption of this approach in the CBCA would follow the trend established by Canadian securities regulators (Regulators) in all the provinces and territories (except for Alberta, British Columbia and Prince Edward Island) who in 2014 adopted "comply or explain" diversity disclosure amendments to the existing corporate governance disclosure rules in National Instrument 58-101 - *Disclosure of Corporate Governance Practices* (NI 58-101).

After Alberta's securities regulator published for comment proposed amendments to NI 58-101 on 14 September 2016, Alberta may also adopt a "comply or explain" diversity disclosure regime. If accepted, the "comply or explain" reporting rules will require companies to disclose the following information in their proxy circular or annual information form:

- Policies regarding the representation of women on the board, if any.
- Whether the board or its nominating committee considers the representation of women in the director identification and selection process.
- Whether the company considers the representation of women in executive officer positions when making executive officer appointments.
- Targets regarding the representation of women on the board and in executive officer positions have been set by the company (if any).
- The number of women on the board and in executive officer positions.
- Director term limits or other mechanisms of board renewal.

Whether similar changes will be adopted in British Columbia remains to be seen.

In addition to the pressures to Canadian companies from Regulators and governments to adopt diversity mandates for their corporate boards, companies are also facing increasing pressures from outside stakeholder organisations. An example of an organisation that promotes diversity on boards is the Canadian Board Diversity Council. It has initiatives like:

- Diversity 50, which identifies board-ready candidates that meet their diversity criteria.
- The 30% Club which promotes gender diversity, mainly through the efforts of its Chair and CEO members in Canada.

Altogether, these various initiatives and developments make it clear that diversity on corporate boards will remain a prevalent issue in corporate reform. The lobby to impose gender quotas appears to be gaining momentum.

National securities regulator

Since the Supreme Court of Canada held in 2011 that the proposal to create a unified national securities regulator to replace the current system of provincial and territorial regulators was unconstitutional, the Federal Government has continued its efforts to work with the provinces and territories toward establishing a unified national securities regulator under a model of co-operative federalism.

In September 2013, the Federal Government announced that it reached an agreement in principle with the provinces of Ontario and British Columbia that would see the creation of a Cooperative Capital Markets Regulator (CCMR). Under the agreement, the participating provinces would no longer retain their own provincial securities regulators and would fall under the oversight of a single regulator, the CCMR. Since then, several other provinces and one territory have announced their intention to join the contemplated CCMR. Consultation drafts of both the uniform provincial securities legislation, to be introduced in participating provinces and the single territory, in addition to the overarching federal systemic risk legislation, were first published for comment in September 2014. More recently, CCMR published the latest revisions of the legislation on 5 May 2016. In a statement on 22 July 2016, federal and participating provincial finance ministers indicated that they expect to enact the legislation by 30 June 2018, and that the CCMR would be operational that year. However, despite these statements, certain Canadian provinces have historically been strongly opposed to the creation of a single regulator. It is therefore still unclear whether the CCMR will harbour the political will required to succeed.

Board renewal

The December 2014 amendments to NI 58-101 provide that a TSX-listed company must disclose whether it imposes term limits on its directors, or otherwise employs mechanisms intended to promote board renewal. While there have been some calls for the implementation of term limits on directors holding office, to date, proxy advisory firms (such as ISS and Glass Lewis) and organisations (such as the Institute of Corporate Directors and the Canadian Coalition for Good Governance) have continued to prefer assessment mechanisms over term limits. However, most recently, the Federal Government introduced proposed amendments to the CBCA in the Bill. If passed into law, this will (among other things) impose on any CBCA incorporated public company a one-year term limit on directors holding office before a re-election is required and will remove the option for slate voting by requiring individual director voting. Despite these proposed changes, it remains to be seen whether directorship term limits will become a requirement for Canadian public companies incorporated under other corporate statutes.

Takeover bid regime

On 9 May 2016, Regulators adopted changes to the policies that regulate takeover bids in Canada, which are:

- Multilateral Instrument 62-104 - Take-Over Bids and Issuer Bids (MI 62-104).
- National Policy 62-203 - Take-Over Bids and Issuer Bids (NP 62-203).

The amendments seek to address the issue of shareholder coercion in the context of an unsolicited takeover bid and to provide a target board with additional time to respond to such a bid.

The amendments require that:

- To be successful, a takeover bid must meet a minimum tender requirement of 50% of the outstanding securities of a company which are subject to the bid (minimum tender requirement).
- A bid must remain open for a minimum of 105 days.
- A bid must also be extended for a period of an additional ten days upon the satisfaction of the Minimum Tender Requirement and all other terms and conditions outlined in the bid.

Overall, commentators consider these changes to provide target boards and target company shareholders with a greater opportunity to assess the merits of an unsolicited takeover bid while also facilitating auction processes by giving additional time to identify and court other potential deal suitors. Altogether, commentators conclude that these changes should lead to greater value creation for shareholders.

Say-on-pay

A say-on-pay vote is a non-binding, advisory vote requesting shareholder approval of proposed executive compensation. The number of public companies that put a say-on-pay vote to their shareholders has grown significantly over the years to include a large majority of companies listed on the S&P/TSX 60 (an index of 60 large TSX-listed companies). In 2016, four S&P 500 companies had their advisory say-on-pay resolutions rejected by shareholders. Certain proxy advisory services, including ISS and Glass Lewis, are strongly supportive of say-on-pay votes and in connection, are increasingly scrutinising companies' compensation practices. While say-on-pay has become mandatory in many jurisdictions, it remains to be seen whether Canadian jurisdictions will do the same.

Enforcement of anti-bribery legislation

While Canada has had anti-corruption legislation in place since the late 1990s, the Corruption of Foreign Public Officials Act (Canada) (CFPOA), it was limited in scope and rarely enforced by Canadian authorities. In June 2013, the Canadian Government enacted amendments to the CFPOA, which implemented a variety of changes aimed at strengthening both the scope and application of the legislation. These changes included, among others:

- The introduction of several new offences targeting the falsifying of accounting books and records for the purpose of bribing a foreign public official.
- The eventual elimination of the exception for facilitation payments made to foreign public officials in connection with non-discretionary decisions that cover acts of a routine nature.
- The increase of the maximum prison sentence for an individual convicted of a foreign bribery offence from five to 14 years (the CFPOA does not provide a maximum fine amount).

The legislative initiative outlined in these changes is consistent with the increased vigour Canadian enforcement authorities have recently shown towards pursuing anti-corruption-related matters, as evidenced by:

- Two significant convictions resulting in penalties in the range of Can$10 million for each liable company.
- The first conviction of an individual under the CFPOA.

Canadian authorities indicated in February 2013 that they had over 35 active investigations related to potential CFPOA charges. In February 2015, CFPOA charges were brought against a large Canada-based multinational consulting and engineering company. A pre-trial hearing is set for 2018.

Influenced by these events, Canadian companies have started to either establish or strengthen their own anti-corruption compliance programmes. These policies are typically aimed at preventing the commission of an offence at the outset and include appropriate procedures if breaches of the applicable legislation occur.

Risk management

Recent highly visible domestic and international risk management failures (for example, instances of cyber security privacy breaches, regulatory (including, environmental and health and safety) non-compliance, financial fraud and resulting litigation and exposures) have thrust risk management into the spotlight. In January 2013, the Office of the Superintendent of Financial Institutions Canada released revised Corporate Governance Guidelines for federally regulated financial institutions. These guidelines identified risk management as a main theme and contemplate enterprise-wide risk identification and focused management.

Corporate social responsibility (CSR)

Today, most large companies in Canada employ CSR personnel that are specifically dedicated to developing socially responsible corporate practices. Among other things, boards have identified the need to engage stakeholders through a variety of different means, which include creating and maintaining an ongoing dialogue. In many cases, companies have voluntarily committed to international CSR standards, such as sustainability reporting. Various factors (including economic volatility and underperformance among many listed companies) have led to growing public scrutiny of corporate boards, including a renewed emphasis on the role of boards in promoting socially responsible corporate practices.

In response to an emerging demand for socially focused investment options (such as health, environmental, cultural and educational goals) investors can now pursue social goals while seeking to make a profit through new hybrid corporate models such as community contribution companies in British Columbia and community interest companies in Nova Scotia. For a federal alternative, see the Canada Not-For-Profit Corporations Act. Overall, these models supplement the traditional role of societies, associations and clubs.

CORPORATE ENTITIES

2. What are the main forms of corporate entity used in your jurisdiction?

This overview of Canadian corporate governance matters and directors' duties applies to the main corporate entities existing under corporate legislation, as described below, and does not address matters applicable to other entities, such as statutory corporations or financial institutions.

The main corporate entities used for business in Canada are federally or provincially incorporated corporations and increasingly, in certain provinces, unlimited liability corporations. The following answers focus on public companies, with the intention that private companies will find it useful in structuring and measuring their own governance frameworks.

LEGAL FRAMEWORK

3. Outline the main corporate governance legislation and authorities that enforce it. How influential are institutional investors and other shareholder groups in monitoring and enforcing good corporate governance? List any such groups with significant influence in this area.

The principal sources of corporate governance requirements in Canada are:

- Corporate legislation.
- Securities legislation.
- Stock exchange rules.
- The common law.

In addition, shareholder advocacy groups and proxy advisory services, including the Canadian Coalition for Good Governance (comprised primarily of institutional investors such as pension funds, mutual funds and third party money managers), Institutional Shareholders Services (ISS), Glass Lewis and the Institute of Corporate Directors, are influential through shareholder

engagement and their publications of policy statements and guidelines. These organisations have become a reference point on best practices for corporate governance. Companies also often refer to the concepts of, and commentary on:

- Corporate social responsibility.
- General business ethics.
- Basic tenets of strategic planning.
- Risk management.
- Engagement.
- Accountability.
- Transparency.
- Efficiency and effectiveness.

Corporate legislation

Generally, a company in Canada is incorporated by filing articles of incorporation (or similar charter documents) with the appropriate federal or provincial government authority. The articles of incorporation specify certain corporate governance matters, which can include:

- The maximum and minimum number of directors.
- Any restrictions on the business that the company can carry on.
- Any rights attaching to each class of shares.

Usually, corporations also enact bye-laws (or similar documents), which address more procedural issues, such as quorum at meetings and the authority of corporate officers.

Additionally, in certain jurisdictions, such as under the CBCA, unanimous shareholder agreements or sole shareholder declarations can limit the role of directors and transfer the responsibility (and liability) for certain matters to the shareholders.

Securities legislation

National Policy 58-201 - Corporate Governance Guidelines (NP 58-201) sets guidelines for most public companies in Canada in respect of governance matters, including:

- Composition and mandate of the board of directors.
- Directors' independence.
- Development of position descriptions for directors and officers.
- Codes of conduct.
- Nomination and remuneration of directors.
- Performance assessment of the board and individual directors.

Companies must disclose information about their corporate governance practices in accordance with National Instrument 58-101 - Disclosure of Corporate Governance Practices (NI 58-101). Generally, Regulators require that companies comply with the guidelines in NP 58-201 or explain their lack of compliance in their public disclosure.

Stock exchange rules

Public companies listed on the Toronto Stock Exchange (TSX) must:

- Comply with the provisions in the TSX Manual related to corporate governance.
- Seek shareholder approval for certain transactions (in particular those that represent a fundamental change to the business or will result in extraordinary dilution).

Generally, the requirements of the TSX Manual align with both NI 58-101 and NP 58-201. Companies listed on the TSX Venture Exchange must comply with Policy 3.1 – Directors, Officers, Other Insiders & Personnel and Corporate Governance of the TSX Venture Exchange's Corporate Finance Manual.

Common law

Directors' and officers' duties and conduct, shareholder rights and obligations, fiduciary duties and other corporate governance matters are subject to the common law, which in Canada is increasingly interpreted through a "made in Canada" approach to case law.

4. Has your jurisdiction adopted a corporate governance code?

No jurisdiction in Canada has adopted a corporate governance code in its corporate legislation. However, public companies in Canada must comply with securities legislation and applicable stock exchange rules, which contain corporate governance guidelines and related disclosure requirements (*see Question 3*). For example, financial institutions and members of the S&P 500 or the TSX Composite Index are frequent targets of governance and action groups that insist on good governance practices.

CORPORATE SOCIAL RESPONSIBILITY AND REPORTING

5. Is it common for companies to report on social, environmental and ethical issues? Highlight, where relevant, any legal requirements or non-binding guidance/best practice on corporate social responsibility.

Despite the continuing increase in public attention to corporate social responsibility (CSR) practices by companies in Canada, Canadian corporate and securities laws do not generally regulate expectations for CSR, and attempts in recent years to pass such legislation have failed.

However, specific continuous disclosure obligations are triggered in certain circumstances where the company has undertaken particular initiatives. For example:

- Public companies that have implemented any social or environmental sustainability policies that are fundamental to their operations (such as policies regarding the environment, communities in which they operate or human rights) must describe these policies and the steps taken to implement them in their annual public disclosure, the annual information form.
- Companies must also outline the financial and operational effects of environmental protection requirements on their current and future capital expenditures, earnings and competitive position in their annual information form and/or their periodic management discussion and analysis.
- Companies that violate federal environmental legislation can be ordered by a court to disclose these violations to their shareholders.

The Federal Government and various Canadian industry associations promote several widely recognised, but not mandatory, international CSR performance guidelines, such as the Global Reporting Initiative.

In addition, the Federal Government has established the Office of the Extractive Sector Corporate Social Responsibility Counsellor to perform both an advisory role and a dispute resolution role in managing issues related to CSR in Canada's extractive sector. In December 2013, the Federal Government launched consultations with civil society organisations to review the CSR strategy for the extractive sector. As a result of these consultations, the Federal

Government passed legislation in December 2014 that requires Canadian extractive companies to disclose certain categories of payments made to government entities above a certain threshold, and to publicly report such information. The Extractive Sector Transparency Measures Act came into force in June 2015, and generally requires mining, oil and gas, and other extractive companies to report all cumulative payments of Can$100,000 or more under specific categories made to governments in Canada or abroad in a given year. Payments made to aboriginal governments in Canada do not need to be reported until 1 June 2017.

BOARD COMPOSITION AND RESTRICTIONS

6. What is the management/board structure of a company?

Structure

Companies in Canada have a unitary board structure.

Management

A company is managed by a board of directors. The board of directors is generally required to manage, or supervise the management of the company's business and affairs, subject to any unanimous shareholder agreement or transfer of such powers in the company's constating documents. There are also specific duties imposed on directors, including:

- Issuing periodic shareholder reports.
- Declaring dividends.
- Reviewing financial statements.
- Setting remuneration for senior management.
- Approving the issuance of shares.

Generally, except possibly for early stage businesses, directors are not actively involved in the day-to-day business and activities of the company, with a trend towards monitoring and oversight. Delegation to senior officers and other management and board committees for public companies and large private companies is common practice. For example, all public companies must have at least an audit committee. Regardless of any delegation, directors remain responsible for the supervision of the management of the company, except for any transfer of responsibility to shareholders by unanimous shareholder agreement or in the company's constating documents, where permitted.

Board members

Individuals are elected by shareholders to sit on the board of directors. In the case of public companies, these individuals are typically nominated for election by the officers or by a nominating committee of the board. Shareholders can also nominate directors. However, for public companies, the adoption of advance notice policies and the company's disclosure obligations can make shareholder nominations a relatively rare occurrence.

Employees' representation

Corporate legislation does not provide employees with a right to representation on the board of directors.

Number of directors or members

A private company must have at least one director, while a public company must have at least three directors.

7. Are there any general restrictions or requirements on the identity of directors?

Age

In Canada, anyone who is less than 18 years of age cannot be a director.

Nationality

There are no nationality requirements for being a director. However, there are requirements regarding Canadian residency. These vary across Canada, and although certain provinces' corporate laws do not contain residency requirements for directors, such as British Columbia, a number of other jurisdictions require that at least 25% of the directors of a company must be resident in Canada.

Gender

There are no gender quotas for board composition in Canada. However, Regulators in all of the provinces and territories (except for British Columbia, Prince Edward Island and Alberta – though Alberta is in the process of adopting its own diversity disclosure rules) require the disclosure of board composition as part of a public company's corporate governance disclosure. As mentioned, amendments to the CBCA have been tabled that would require, among other things, proscribed CBCA companies to produce diversity disclosure. Additionally, the TSX Manual requires, among other things, diversity disclosure for TSX-listed companies, which includes disclosing:

- The level of representation of women on the board of directors.
- Whether the company has a policy for identifying female candidates for executive office and board positions.
- If the company does not have such a policy, the company must disclose the reasons for not adopting a policy.

8. Are non-executive, supervisory or independent directors recognised or required?

Recognition

In Canada, independent directors are recognised and have equal standing in comparison to other directors. Publicly traded companies must disclose the identity of independent directors in their annual corporate governance disclosure.

Board composition

There is no corporate legislation that requires Canadian companies to have independent directors. However, both the TSX and the TSX Venture Exchange require listed companies to have at least two independent directors. Similarly, the audit committee of the board of directors of publicly traded companies must have at least three directors and, subject to certain specified exemptions, the members of the audit committee must be independent directors.

Independence

Non-executive or supervisory directors are not required to be independent of the company.

9. Are the roles of individual board members restricted?

There are no restrictions on the roles of individual board members in Canada.

10. How are directors appointed and removed? Is shareholder approval required?

Appointment of directors

Typically, directors are nominated by management of the company and are elected by the shareholders of the company at the company's annual general meeting. In some instances, the governing corporate legislation or the charter documents of the company can provide that, between annual meetings, the current directors can appoint additional directors up to a certain percentage of the current size of the board (typically one third) to fill any board vacancies.

Removal of directors

Directors can be removed from office during their term by the company's shareholders. A majority of the shareholders must vote for a director's removal at a special meeting. Such a meeting can be called by the directors at any time.

11. Are there any restrictions on a director's term of appointment?

Directors commonly serve for one-year terms, although the shareholders can elect directors for terms of up to three years (subject to term limit requirements under applicable corporate or securities laws, such as the proposed changes to the CBCA). Lately, more and more companies are adopting director term limits (*see Question 1, Board renewal*). However, there are no statutory limits on the number of terms that a director can serve.

DIRECTORS' REMUNERATION

12. Do directors have to be employees of the company? Can shareholders inspect directors' service contracts?

Directors employed by the company

Directors do not have to be employees of the company.

Shareholders' inspection

Unless otherwise specified in the company's charter documents or in a unanimous shareholders' agreement, the shareholders of a company cannot inspect directors' service contracts. However, publicly traded companies must disclose the quantum of fees and other benefits paid to the directors of the company.

13. Are directors allowed or required to own shares in the company?

Directors can own shares in the company they manage. Although there are no legal obligations for directors to own shares in the company they manage, minimum shareholding requirements for directors are commonly adopted into director remuneration programmes in an effort to align the directors' interests with those of the company's shareholders.

14. How is directors' remuneration determined? Is its disclosure necessary? Is shareholder approval required?

Determination of directors' remuneration

Corporate statutes contain provisions relating to contracts with, and the remuneration of, directors. Generally, the directors of the company are responsible for determining directors' remuneration. In most public companies, remuneration is set by the compensation committee of the board of directors, in consultation with senior management. The charter documents or any unanimous shareholder agreement can limit this power.

Disclosure

Public companies must disclose annually the reasons for and amount of remuneration provided to their directors and certain senior executive officers, in accordance with the requirements of securities laws.

Shareholder approval

The remuneration of directors does not have to be approved by the shareholders of a company. However, public companies are increasingly incorporating advisory, non-binding say-on-pay shareholder resolutions into their corporate governance regime. The TSX requires listed companies to receive approval from the majority of its directors and security holders for plans to provide certain security-based compensation arrangements (such as stock option plans) to its directors and officers.

General issues and trends

While there are no legal restrictions on the quantum of directors' or executives' compensation, proxy advisory firms such as Glass Lewis and Institutional Shareholders Services are increasingly focusing on the nexus between shareholder value and executive compensation (pay-for-performance) for public companies. This nexus includes, among other things, the:

- Appropriate weighting of executive compensation between salary, short-term incentives and long-term incentives.
- Use of performance goals as a metric for determining executive compensation.

As directors set the compensation paid to executives, certain proxy advisory firms will recommend withholding voting for the election of the director who serves as the chair of the compensation committee.

However, as independent directors are not involved in the day-to-day business and activities of the company, many shareholder advocacy groups and proxy advisory services often differentiate between executive and independent directors' compensation. For independent directors, tying compensation to performance can be seen as creating incentives that diminish the independent director's role in taking a longer-term view of the welfare of the company.

MANAGEMENT RULES AND AUTHORITY

15. How is a company's internal management regulated? For example, what is the length of notice and quorum for board meetings, and the voting requirements to pass resolutions at them?

The operation of internal management is generally regulated by the company's articles of incorporation and bye-laws, subject to any unanimous shareholder agreements and the applicable corporate statute.

A company has some flexibility when determining the process for its meetings, subject to any applicable corporate laws that require meetings to be held in Canada. The company typically sets out in its articles or bye-laws the:

- Location and notice requirements for the meeting.
- Quorum requirements for the meeting.

In jurisdictions with Canadian residency requirements for directors, similar residency requirements may also apply to attendance at meetings. When residency requirements apply, directors must attend meetings in person – proxies or representatives are not permitted. However, attendance at meetings can be performed by telephonic or other electronic means, provided that all participants can communicate adequately with each other.

Directors' resolutions can be passed by majority vote. Any dissenting positions regarding a proposed directors' resolution will be acknowledged and recorded in the company's minutes. Generally, resolutions can also be passed by a written consent resolution signed by all the directors.

16. Can directors exercise all the powers of the company or are some powers reserved to the supervisory board (if any) or a general meeting? Can the powers of directors be restricted and are such restrictions enforceable against third parties?

The operation and management of a company is primarily the responsibility of the directors, although certain fundamental matters require shareholder approval. Corporate legislation in Canada typically requires shareholder approval for, among others things:

- Amendments to a company's articles or other charter documents.
- Selling all or substantially all of the company's assets.
- The amalgamation of a company with one or more other companies.

In some Canadian jurisdictions, shareholders can enter into a unanimous shareholder agreement that restricts or transfers directors' usual powers of management and supervision to the shareholders. In other Canadian jurisdictions, the constating documents of the company can transfer these powers to one or more other persons. If this occurs, the individuals to whom those powers are transferred will have the same duties and obligations as directors, and any action that could normally be brought against directors can be enforced against these individuals.

17. Can the board delegate responsibility for specific issues to individual directors or a committee of directors? Is the board required to delegate some responsibilities, for example for audit, appointment or directors' remuneration?

Boards typically delegate some of their more specialised functions to committees of directors. Boards of publicly traded companies must form audit committees and delegate to them the responsibility to:

- Oversee the company's auditor.
- Resolve any disputes between management and the auditor.
- Recommend the auditor to shareholders.

However, in most cases, delegation does not relieve non-committee board members of their responsibility. Certain matters cannot be delegated to a director or a committee of directors, such as the power to issue securities, declare dividends or fill a vacancy among the directors.

DIRECTORS' DUTIES AND LIABILITIES

18. What is the scope of a director's general duties and liability to the company, shareholders and third parties?

Directors have a duty to comply with:

- The governing corporate laws and regulations;
- Relevant securities laws and regulations.
- Stock exchange rules.
- Industry or activity regulations.
- Employment-related, environmental and taxation regulations.
- The common law.
- Charter documents of the company.
- Any unanimous shareholder agreement.

Two overarching corporate duties imposed on directors are that directors must:

- Act honestly and in good faith, with a view to the best interests of the company; and
- Exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

Directors can be held personally liable for breaching these duties.

19. Briefly outline the regulatory framework for theft, fraud, and bribery that can apply to directors.

Theft and fraud are both governed by the *Criminal Code of Canada*. A director found guilty of theft or fraud is liable to imprisonment and restitution. There are also civil law remedies for persons seeking damages for loss suffered from theft or fraud.

The Corruption of Foreign Public Officials Act (Canada) (CFPOA) prohibits the bribery or corruption of foreign public officials to obtain an improper advantage in business. A director of a company found in breach of the CFPOA can be personally liable and face fines and/or imprisonment.

20. Briefly outline the potential liability for directors under securities laws.

Securities legislation is a provincial matter in Canada. The exact offences and potential liabilities for directors will depend on the specific securities legislation of the jurisdiction in question. However, the provincial securities statutes are similar to one another, and the following potential liabilities for directors apply under every provincial securities statutes:

- Directors are liable for losses suffered by a purchaser of the securities of a company as a result of a misrepresentation made by the company in an offering document, although certain statutory defences are available.
- Directors can be found liable for losses suffered by a person who purchases securities in the secondary market due to:
  - a misrepresentation made by the company in its public disclosure documents or public oral statements; or
  - the company's failure to make timely disclosure of a material change.

- A director can be found liable for insider trading if:
  - he or she buys or sells the securities of the company with knowledge of a material fact or material change that has not been generally disclosed; or
  - he or she knowingly provides insider information to a third party other than in the necessary course of business.
- Directors can be found liable for market manipulation if engaging in any conduct relating to securities that he or she knows, or reasonably ought to know, would result in a misleading appearance of trading activity in, or an artificial price for, a security or derivative of a security.

21. What is the scope of a director's duties and liability under insolvency laws?

Directors must ensure that the company only carries on business if it can meet its liabilities. Directors can be personally liable if the company conducts business while insolvent. When a company is insolvent, in addition to the basic fiduciary duty owed to the company, directors owe special duties towards different stakeholders such as employees, creditors and the environment.

22. Briefly outline the potential liability for directors under environment and health and safety laws.

The *Canadian Environmental Protection Act* and certain provincial environmental legislation provide that directors must take all reasonable care to prevent the company they serve from contravening environmental laws. Reasonable care generally includes the:

- Establishment of an environmental policy.
- Implementation of a proper system for preventing breaches of environmental laws.
- Establishment of an effective internal compliance and reporting system.

Directors are personally liable for participating in, or acquiescing to, conduct that contravenes environmental laws, regardless of whether the company is charged or convicted. In addition, directors can be liable for failing to prevent environmental contraventions through reasonable care.

Provincial occupational health and safety legislation, such as the British Columbia *Workers Compensation Act*, provide that directors must take reasonable care to ensure that the company they serve complies with the legislation and that the employees work in an environment that is safe and free of hazards and liability. A company's failure to comply with the applicable health and safety legislation can result in the directors being personally liable.

23. Briefly outline the potential liability for directors under anti-trust laws.

Anti-trust matters are governed by the federal *Competition Act*, which contains criminal and civil provisions proscribing a variety of anti-competitive conduct, including:

- Price-fixing.
- Bid-rigging.
- Deceptive marketing.
- Abuse of a dominant position.

A director in a position to direct or influence the policies of a company in relation to a prohibited conduct can be considered guilty of the offence, unless the director exercised proper due diligence. If found guilty, the director can receive a prison term of up to 14 years, fines at the discretion of the court of up to Can$750,000 for first-time offences or, in the alternative, the director's company could receive administrative monetary penalties of up to Can$10 million.

24. Briefly outline any other liability that directors can incur under other specific laws.

Directors can be personally liable under the *Income Tax Act* if the company fails to deduct or remit to the Canada Revenue Agency the prescribed amounts for certain payments by the company, including salaries, wages, and pension benefits, among others.

In certain jurisdictions, corporate legislation also imposes liability on directors for unpaid employee wages, including accrued vacation pay and termination pay, and various source deductions. In jurisdictions where corporate statutes do not impose such liability, employment standards legislation generally does.

Canada's Anti-Spam Legislation (CASL) expressly extends legal responsibility to directors of a company if the company contravenes CASL, regardless of whether there are proceedings against the offending company. A director can be personally liable if he or she directed, authorised, assented to, acquiesced in, or otherwise participated in the violation, unless the director exercised proper due diligence. If a director is found liable, he or she can face monetary penalties of up to Can$1 million.

At this time, only the Canada Radio-television and Telecommunication Commission (CRTC) can bring claims under CASL. On 26 October 2016, the first penalties under CASL were issued by the CRTC for a total of Can$50,000. However, from 1 July 2017, private claims under CASL will be allowed, which is likely to take the form of class action litigation.

25. Can a director's liability be restricted or limited? Is it possible for the company to indemnify a director against liabilities?

Directors' liability is limited to the extent that directors' powers have been transferred to another person, whether by a unanimous shareholder agreement or otherwise.

A company can indemnify its directors against liabilities and expenses they reasonably incur as directors in respect of any civil, criminal, administrative, investigative or other proceedings. However, to be eligible for an indemnification, a director must satisfy his or her duty to act honestly and in good faith with a view to promoting the best interest of the company. Where a monetary penalty is imposed, the director must also prove that he or she had reasonable grounds for believing that his or her conduct was lawful.

26. Can a director obtain insurance against personal liability? If so, can the company pay the insurance premium?

A director can purchase insurance to protect against personal liability. Companies often pay the insurance premium for this type of insurance.

27. Can a third party (such as a parent company or controlling shareholder) be liable as a de facto director (even though such person has not been formally appointed as a director)?

A person can be a de facto director and be liable as a director (although not formally appointed as such) in the following cases:

- The powers of the directors have been conferred to him or her.
- He or she represents himself or herself as a director.
- He or she exercises the role of director.

TRANSACTIONS WITH DIRECTORS AND CONFLICTS

28. Are there general rules relating to conflicts of interest between a director and the company?

At common law and under statute, directors have the fiduciary duty to act in the best interest of the company. In doing so, directors must:

- Avoid conflicts of interest.
- When unavoidable, disclose a conflict of interest pursuant to the specific conflict of interest rules under the common law, corporate statute or securities legislation.

The disclosure of a conflict of interest generally entails the disclosure of the nature and the extent of the conflict of interest. As a general rule, a conflicted director must not vote or influence the vote of non-conflicted directors, subject to specific exceptions.

In most jurisdictions, if a director does not disclose the conflict of interest in the specified manner, this director will be liable to the company for any profits realised from such conflict. Directors are generally not liable for profits realised if a sufficient disclosure was made to, and the transaction giving rise to the conflict was approved by a special resolution of, the shareholders.

Additionally, courts in Canada are generally less inclined to defer to board decisions in conflict situations, where the decision was not otherwise patently reasonable.

29. Are there restrictions on particular transactions between a company and its directors?

Generally, there are no formal restrictions on transactions between a director and the company. However, a director cannot be appointed as the auditor of a company.

30. Are there restrictions on the purchase or sale by a director of the shares and other securities of the company he is a director of?

Insider trading rules in securities legislation generally restrict a director from purchasing or selling shares or other securities of the company he or she serves, if, at that time of the sale or purchase, the director is in possession or has knowledge of a material fact, which has not yet been disclosed publicly.

DISCLOSURE OF INFORMATION

31. Do directors have to disclose information about the company to shareholders, the public or regulatory bodies?

The directors of a company are ultimately responsible for corporate disclosure and transparency. However, routine compliance with continuous disclosure obligations is typically overseen by the management team that is accountable to the board of directors. Many companies have taken steps to formalise the process of meeting their disclosure obligations. Typically, the board will adopt a disclosure policy to guide members of management on issues of disclosure. Additionally, some companies establish a disclosure committee in order to consider and review the company's disclosure and ensure that all disclosure requirements have been met fully and accurately.

Many senior listed companies, either voluntarily or under formalised requirements, now participate in shareholder engagement on issues of interest to shareholders, such as executive compensation, diversity and board renewal, among others.

SHAREHOLDER RIGHTS

Company meetings

32. Does a company have to hold an annual shareholders' meeting? If so, when? What issues must be discussed and approved?

Corporate law generally requires annual meetings of shareholders, including for the election of directors and the appointment of auditors. Shareholders of public companies must also appoint an auditor at each annual meeting.

Directors can also call a special meeting at any time, and shareholders can call a meeting as described in *Question 35*.

33. What are the notice, quorum and voting requirements for holding meetings and passing resolutions?

Shareholders' meetings must be attended personally or by proxy. Typically, shareholders tender proxies to either management or other representatives to vote their shares as indicated in their proxies.

Generally, notice, quorum and voting requirements are governed by the relevant corporate and securities laws and a corporation's articles or bye-laws.

Directors must provide notice to shareholders of each meeting. Public companies and certain widely-held private corporations must also either:

- Send a management proxy circular and related materials to shareholders.
- Make use of "notice-and-access" provisions to provide shareholders with access to such materials. "Notice-and-access" provisions allow companies to disseminate meeting materials by posting the relevant materials online and delivering a notice informing shareholders that these materials have been posted electronically, and advising shareholders how to access them.

Certain shareholders can submit proposals to be included in the materials. Given how rigid the notice requirements under corporate and securities laws are, companies are limited in their ability to address matters put forward at a meeting for consideration by shareholders, which were not previously outlined in the notice of meeting.

34. Are specific voting majorities required by statute for certain corporate actions?

Certain corporate actions must be approved by a special resolution of the shareholders, which generally requires at least two-thirds or 66% of the votes cast in favour by the shareholders entitled to vote on the resolution. These actions include, among others:

- Amending the company's articles or bye-laws.
- Approving an amalgamation.
- Approving the sale or lease of all or substantially all of the company's assets.

35. Can shareholders call a meeting or propose a specific resolution for a meeting? If so, what level of shareholding is required to do this?

In most Canadian jurisdictions, to be eligible to call a shareholders' meeting, a shareholder must hold at least 5% of the outstanding voting shares of the company. To submit proposals at a meeting already scheduled, the eligibility threshold is lowered to 1% of the outstanding voting shares of the company.

Minority shareholder action

36. What action, if any, can a minority shareholder take if it believes the company is being mismanaged and what level of shareholding is required to do this?

Shareholders can call a meeting or submit a proposal to a previously called meeting, provided that they hold at least the required percentage of outstanding voting shares in the company (*see Question 35*).

Shareholders can also propose a different slate of directors (or one director) to be elected at the meeting than those nominated by management.

INTERNAL CONTROLS, ACCOUNTS AND AUDIT

37. Are there any formal requirements or guidelines relating to the internal control of business risks?

Under National Instrument 52-109 - *Certification of Disclosure in Issuers' Annual and Interim Filings*, the CEO and chief financial officer of a reporting company must implement and annually certify their responsibility for establishing and maintaining disclosure controls and procedures, and internal controls over financial reporting. To date, there is no legal requirement in Canada to have an internal auditor in either private or public companies.

38. What are the responsibilities and potential liabilities of directors in relation to the company's accounts?

Directors can be held liable for breaching their fiduciary duty if they fail to ensure that the company they serve maintains proper books, records and accounts. A defence is available if a director reasonably relied on the financial statements provided by officials or auditors of the company, and would reasonably do so if managing his or her own affairs.

39. Do a company's accounts have to be audited?

Generally in Canada, a company's annual financial statements must be audited unless the company's shareholders resolve to waive the requirement to appoint an auditor for that year. However, shareholders of publicly traded companies cannot waive the auditor requirement. Subject to certain limited exceptions, there is no requirement for a company's interim financial statements to be audited,

40. How are the company's auditors appointed? Is there a limit on the length of their appointment?

A company's auditors are appointed for a one-year term at the annual general meeting of shareholders. The auditors' term comes to an end at the next annual general meeting of shareholders. For publicly traded companies, potential candidates are generally identified by the company's audit committee.

41. Are there restrictions on who can be the company's auditors?

Only auditors that are registered with provincial regulatory bodies can act as auditors for a company. In addition, they must be independent of the company that they audit.

42. Are there restrictions on non-audit work that auditors can do for the company that they audit accounts for?

There are no restrictions on the non-audit work that auditors can perform for a company under corporate or securities laws. However, all non-audit services for a public company and its subsidiaries must be specifically pre-approved by the audit committee of the company. This pre-approval requirement can be satisfied by the adoption of specific policies and procedures for the engagement of non-audit services.

43. What is the potential liability of auditors to the company, its shareholders and third parties if the audited accounts are inaccurate? Can their liability be limited or excluded?

As an expert, an auditor can be liable for professional negligence to a company if its report is inaccurate. For publicly traded companies, an auditor can also be found liable in damages to a person who purchased or disposed of a security of the company in secondary markets during the period between the time when the document was released and the time when the misrepresentation

contained in the document was publicly corrected, regardless of whether the person relied on the misrepresentation. This secondary market liability is capped at the greater of Can$1 million or the revenue that the auditor earned from the company in the 12 months preceding the misrepresentation. If the auditor knew of the misrepresentation, there is no cap on the auditor's liability.

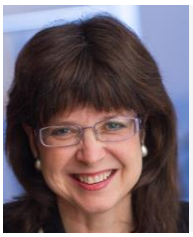
44. What is the role of the company secretary (or equivalent) in corporate governance?

The corporate secretary's role has expanded over the years and, at a minimum, generally consists of overseeing the company's corporate governance regime, which typically involves:

- Organising and maintaining the company's corporate records.
- Participating in and managing the requirements of formal meetings.

Additionally, the role of corporate secretary usually entails some reporting responsibilities to the company's directors and shareholders. Some provinces identify certain aspects of the corporate secretary's role as falling within the practice of law.

Practical Law **Contributor profiles**



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Professional qualifications. British Columbia, called to the bar, 1989; named Queen's Counsel, British Columbia, 2011

Areas of practice. Corporate governance; commercial law; administration, pension governance and investment; private equity and venture capital.

Recent activities

- Holds or has held director, committee chair (including audit committee) and corporate secretary roles for numerous entities.
- Designing or co-designing, advising, educating and orienting on and implementing corporate governance principles, strategic planning and risk management processes and frameworks for private and public entities, including government, quasi-government and not-for-profit entities.
- Working with other service providers or advisers (such as auditors and compensation consultants).

Professional associations/memberships. Certified director, Institute of Corporate Directors (ICD), completed the ICD's governance programme, 2014.

Publications

- Published articles and participated in media interviews, including on matters of corporate governance, business ethics, legal practice and regulation.
- Board-ready per the Canadian Board Diversity Council 2014 Diversity 50 national listing.
- Consistently peer-review top-listed for Corporate Governance and Private Funds/Equity by Best Lawyers in Canada®.
- Best Lawyers in Canada: recognised for Corporate Governance Practice and Private Funds law.
- 2016 YWCA Women of Distinction Awards: nominated in the Business & the Professions category.
- Best Lawyers in Canada: recognised for Corporate Governance Practice and Private Funds law.
- Best Lawyers in Canada: recognised for Private Funds law.
- 2011 Lexpert Zenith national award winner for corporate social responsibility and governance.
- Appointed Queen's Counsel in 2011.

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Professional qualifications. British Columbia, called to the bar, 1997

Areas of practice. Corporate governance; commercial law; corporate finance and securities; energy; mergers and acquisitions; mining.

Recent activities

- Represented and worked with clients in a broad range of transactions, including public and private financings of equity and debt, acquisitions and divestitures, arrangements and corporate reorganisations.
- Advising public and private company clients and their boards of directors on corporate governance, directors' duties and responsibilities and regulatory compliance.
- Acting as counsel to special committees of boards of directors in related party transactions and other corporate transactions.
- Has served as corporate secretary to a major electric utility and acted as general counsel to the utility's subsidiary.

Professional associations/memberships. Certified director, ICD, completed the ICD's governance programme, 2009.

Publications

- 2011 Lexpert Zenith national award winner for corporate social responsibility and governance.
- Best Lawyers in Canada: recognised for Corporate Governance Practice and Corporate Law.
- *Corporate Governance Report, September 2016.*
- *Canadian Securities Law News, October 2016.*
- *Directors' Briefing, September 2016.*
- *Commercial Times, October 2016.*