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The Magazine for Canadian Listed Companies

SPECIAL REPORT

CYBER RISK AND THE BOARD

What every director needs to know—and do—about cybersecurity P.26

Deborah Rosati
Director and audit chair, Sears Canada Inc.

PLUS

DIRECTOR'S CHAIR

Ira Millstein, corporate governance giant, with David W. Anderson P.36

TOO BIG TO SELL?

Finding a buyer for the world's largest gold-copper deposit is harder than it sounds P.32

BIDDERS, BOARDS GET A RESET

The CSA proposes dramatic changes to rules on takeovers P.8

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Talking it up: Seabridge Gold CEO Rudi Fronk is in the market for a major partner

Features

"People tend to think of cyberattacks, cybersecurity and cyber risk as IT issues. But 95% of attacks are economic and the economic incentives favour the bad guys. They are cheap to launch, incredibly profitable, and easy to do."

Larry Clinton, president and CEO Internet Security Alliance
Page 28

Photograph: Theo Stroomer

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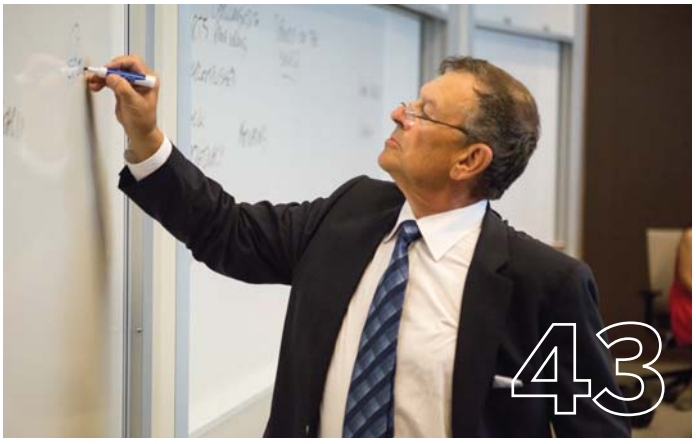

Photograph: Brendan McDermid/Reuters; Thomas Trutschel/Getty Images

New U.S. tax rules blunt "inversion" mania

Well, that didn't take long. In last issue's cover story on Valeant Pharmaceuticals (TSX:VRX), "How to build a pharma giant [and win friends and incite critics]," writer Robert Thompson noted that the corporate "inversion" strategy used by the formerly U.S.-based Valeant to become a Canadian company through its "acquisition" by Biovail, based in Laval, Que., was now under threat from U.S. regulators and government officials. Valeant, which did its deal with Biovail in 2010, was relatively early to the party. Since then, as our story said, the U.S. pharmaceutical sector, in particular, has seen a big wave of similar transactions—sparking fears of a significant erosion of that country's corporate tax base. Now, expect that wave to dissipate.

In September, the U.S. Treasury Department announced new rules, effectively immediately, that will make such tax-avoidance transactions more costly and make companies think twice before doing them. The changes aren't retroactive, so they mean little to companies that have already done an inversion. But a number of large U.S. firms in the midst of inversion-type deals immediately felt the impact, with their share prices taking big hits.

The changes target a number of different techniques and tactics, so not all inversions will be equally affected. High on the list of maneuvres in the Treasury's sights are strategies that companies were using to bring overseas profits into the U.S. with paying U.S. taxes.

It's also possible that more changes are in store. When these moves were announced, experts said they still expect further action from the Obama administration on tax inversions. Stay tuned.

Bank directors grapple with new OSFI guidelines

Back in 2012, in an exclusive interview, *Listed* spoke to Julie Dickinson, then superintendent with the Office of the Superintendent of Financial Institutions (OSFI) about the development and pending introduction by her office of new corporate governance guidelines for Canadian banks ("Banking on better boards," Spring 2012). At the time, Dickinson said the new guidelines were being developed in response to the financial crisis of 2008 and 2009, with a key aim of "empowering" boards in their oversight of management, particularly when it comes to risk management.

Those new rules were ultimately introduced and took effect at the beginning of 2014; Dickinson then stepped down this summer, when her seven-year term expired. But now, it seems, Canadian bank directors and the executives they oversee are struggling to come to terms with the changes. At a luncheon speech in Toronto in early October by Jeremy Rudin, Dickinson's successor as OSFI superintendent, several bank directors in the audience voiced concerns that new rules were putting directors in the awkward position of having to be overly involved in day-to-day operations—ordinarily the purview of management, not boards.

The key areas of conflict emanate from the same aspects of risk management oversight that Dickinson talked about in 2012. The OSFI's new rules require boards to approve detailed risk management frameworks development by the banks' management as well as overall objectives and strategy. However, directors told Rudin that doing this requires them to get too involved in operational details for either their or management's liking. According to reports from the luncheon, Rudin was sympathetic but unyielding, essentially telling the directors present that these issues are now their responsibility and they have to figure out how to deal with it. Expect to hear more on this from all parties in the coming weeks and months.

Jamie Sokalsky

Former Barrick CEOs on comeback trail

We've written features about Barrick Gold Corp. (TSX:ABX) twice in recent in recent years ("Cash flow is colour-blind," Winter 2011; "Barrick turns the page," Mining 2014), and both of the now-former Barrick CEOs featured in those pieces recently took significant steps on the career comeback trail.

In September, just one day after he officially left the top job at Barrick, Jamie Sokalsky was appointed director and tabbed as the incoming non-executive chairman of Probe Mines Ltd. (TSX-V:PRB), a Toronto-based junior gold explorer. At present, Probe's key asset is gold deposit near Chapleau, Ont. Sokalsky is expected to assume the chairman's role after Probe's annual meeting on Oct. 29.

Meanwhile, Aaron Regent, Sokalsky's predecessor as Barrick CEO, made news in early October with word that his private equity firm, Magris Resources Inc., had partnered with other Asian investors to buy the Niobec mine, a nobium mine and rare earth deposit in northern Quebec. The seller was Iamgold Corp. (TSX:IMG) of Toronto, and the price tag was US$530 million. The deal is Magris's first since Regent formed the company after he left Barrick in 2012.

In announcing the deal, Regent also said Magris and its investor partners, Temasek Holdings, of Singapore, and CEF Holdings, of Hong Kong, would continue to look to team up on other potential purchases.

Photograph: David Cooper/Global Look

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Digital-age defence

Seeing your company make news for a data breach is every director's worst nightmare. No wonder more boards are giving cyber risk the attention it deserves

By the time the news broke in early September that retailer Home Depot had suffered a catastrophic data breach, with some 56 million of its North American customers' credit and debit card accounts hacked earlier this year, we were already hard at work on this issue's cover story, "Cyber risk takes centre stage." Needless to say, the news reaffirmed both the story's core premise—that the elevation of cybersecurity oversight to the top of boardroom agendas is warranted, if not overdue—as well as our decision to make it the focus of our latest Special Report on Risk. For these reasons, I highly recommend it as essential reading.

In preparing the article, writer Jim Middlemiss spoke to company directors, board advisers and legal and technical experts while reviewing the growing body of material on the subject. The good news: a lot of boards and their advisers are waking up to the fact that data security is no longer just a matter of concern for the IT department, that the potential threats to companies' reputations, their share prices, even their viability, are too big for boards to overlook. The bad news: other boards haven't yet caught on to this fact and, in many cases, are ill-equipped to deliver the appropriate oversight even after it's brought to their attention. For those in the former category, I hope our story provides additional insight; for those in the latter, may it be the catalyst for change.

For those who require more convincing, I need only point to the headlines one more time. As this issue went to press, news had just broken about another massive data breach, involving U.S. financial services giant JPMorgan Chase. In this case, sensitive customer data—account numbers, passwords, social security numbers, user IDs and the like—from an incredible 76 million households and seven million small businesses had been compromised. We also know it won't be the last time this happens. So the best thing directors can do is work to ensure that when the next headlines hit, it will be someone else's company in the news, not theirs. Our story starts on page 26.

THERE'S PLENTY MORE in this issue, of course, including a full slate of smart, authoritative items from *Listed*'s professional columnists; a fascinating feature on Toronto-based Seabridge Gold, a company with a unique problem—trying to find a partner/buyer for what could be the largest undeveloped gold and copper deposit in the world; and lastly, a feature interview with one of the original giants of corporate governance, Ira Millstein. And don't forget: we're always eager for reader feedback. You can reach our experts via e-mail, or send me a note directly and I'll be sure to pass it along.

Brian Banks
Editorial Director
brian@listedmag.com

Next issue: Our winter issue features a pair of Special Reports. It starts with our report on M&A, a two-part package that kicks off with *Listed*'s selection of the Deal of the Year. It's been a strong year thus far for M&A, with a number of big deals—which one makes the grade? The second part of the M&A package is a review of all the year's top deals, deal trends and dealmakers. Along with that, we bring you our annual Special Report on Preparing for Proxy Season. This year, we're taking an expanded look at what is sure to be nearly every shareholder's hot-button issue at proxy/AGM time: compensation. Watch for it December 15.

No half measures: The CSA's proposal includes a minimum 50% tender condition, preventing minority-stake offers previously used by activists like Carl Icahn

M&A rules get an overhaul

The Canadian Securities Administrators, with unanimous provincial support, is proposing new rules on takeover bids. Target boards and shareholders will get more leverage, bidders will need to rethink strategy

By John Greenwood

Big changes often start imperceptibly until suddenly they become fact, part of the landscape. That's a good description for the Canadian Securities Administrators' recently proposed changes to regulations on takeover bids and shareholder rights plans which, assuming they're adopted, will dramatically reshape the way mergers and acquisitions are carried out in the public market.

Senior executives and directors still have time to take stock of the new proposals—the CSA plans to publish them as draft rules for comment in the first quarter of 2015—but they shouldn't underestimate their potentially sweeping impact. By extending the time for takeover bids and mandating a minimum tender condition, the CSA could change everything from the kinds of deals that succeed, to the use of poison-pill shareholder rights plans, to the balance of power between corporate boards and shareholders.

"This will change the strategic considerations that a bidder will have to go through when deciding how to approach a target company," says Alex Moore, a partner at Davies Ward Phillips & Vineberg LLP. For one thing, he adds, it will "dramatically reduce" the frequency with which securities regulators are called to intervene in proposed deals.

For another, it will provide incentive for bidders to come out of the gate with generous offers, according to Hooman Tabesh, executive vice-president at proxy solicitor Kingsdale Shareholder Services.

Corporate M&A has always been a dance. A potential buyer tables a bid, the target company demurs that the price is too low and, as often as not, the bid gets sweetened. It's all tightly choreographed, with regulators watching closely for errant footwork.

A central pillar of the regulation is the length of time that a bid must remain open for acceptance by shareholders. The current rule calls for a minimum of at least 35 days.

When a company is targeted by an unsolicited bid, it's the job of the board of directors to make a recommendation to shareholders whether to tender their shares, or to reject it and hold out for a higher offer. If the latter, it then falls to the board to seek alternatives, such as a better offer. The more time a board has to do its job, the greater the likelihood of success.

Now, 35 days doesn't leave a board much room to do its job, but in

Photograph: Brendan McDermid/Reuters

More time: New bid rules will make arbitrary court extensions, as with HudBay's Augusta Resource's takeover, unnecessary

the real world boards find ways around that. Regulators are nearly always called in and the period nearly always ends up getting extended, to anywhere from 60 days to 90 days, though there have been occasions when it has gone well beyond that. For example, in 2013, when HudBay Minerals Inc. (TSX:HBM) tabled an unsolicited bid for Augusta Resource Corp., the B.C. Securities Commission ultimately ruled that the bid could remain open for 156 days. Another case in point: this winter, we saw Goldcorp Inc. (TSX:G) launch a bid for Osisko Mining Corp. in January. It stretched out into more than three months of bids, court actions and counter offers before Osisko found a white knight in a larger, joint takeover offer from Agnico Eagle Mines Ltd. (TSX:AEM) and Yamana Gold Inc. (TSX:YRI).

So after a fashion, target companies are able to get the time they need. But that doesn't mean the rules work.

Like a banger car that still gets from A to B, the current system—which hasn't been significantly updated in more than two decades—ultimately does what it's supposed to. The drawback is that you never know going in quite what you're going to get from the regulators. What sort of conditions will be applied? Will the board get enough time to allow the company to prove its new technology/mineral deposit/drug?

"That inherent uncertainty isn't good for the market," says Grant McGlaughlin, a partner at Goodmans LLP. "If there's uncertainty in the marketplace, people will back off because they can't control the direction [of events]."

According to McGlaughlin, the proposals represent a "significant improvement" on the current regime, "a pragmatic solution to a very complicated issue."

The new rules would extend the minimum open-bid period from 35 days to 120 days—a more than three-fold increase. This is a big deal. From a board's perspective, time is leverage, and 120 days is a whole lot of leverage.

No more need to go before a regulator to beg for breathing room, since the new minimum is, experts say, long enough for a target board worth its salt to flush out any white knights or alternative bidders lurking in the underbrush.

The new, extended time frame also solves a rift that had existed between the CSA and Quebec's securities regulator (AMF), which last year issued divergent proposals on allowable defensive tactics for target companies, especially the adoption of so-called poison pill defences. Under this new plan, the CSA, rather than trying to regulate poison pills directly, can simply use the extended open-bid period to render the strategic, time-buying leverage that poison pills afford largely moot.

THE CSA PROPOSAL also raises the bar in terms of how much of a company's equity a bidder needs to acquire in order to have completed a takeover, another knotty issue.

Currently, bidders can choose to take up whatever proportion of tendered shares they choose—there's no minimum. Critics say that's an invitation for abuse and leaves other shareholders who don't like the offer price in a difficult spot deciding whether to tender. If they hold out, they could find themselves owning shares alongside a powerful minority investor, resulting in a smaller float and a potentially lower share price. In some situations, says Davies' Moore, "it's almost like a threat [to shareholders]: You can either sell to me now or live with me as controlling shareholder."

Consider what happened when activist investor Carl Icahn took a run at Lions Gate Entertainment Corp. back in 2010.

It started off like any other takeover struggle. After trading barbs in the press with Lions Gate for more than a year, Icahn, who had an 18% stake in the company, decided it was time to get serious and in February 2010 he swooped in with a US$6-a-share offer for the Vancouver-based film production company—a fat 10% premium over the precious day's closing price.

But here's the thing. Icahn only wanted to boost his stake to about 30%, enough to make him a major shareholder with clout to steer board decision-making.

Shareholders found themselves over a barrel: if they accepted the offer, they had no guarantee they be able to sell all their shares at the offered price. On the other hand, if they opted to hold onto their stake, they would be left as minority owners of a company with a very large activist shareholder. (The good news in this case was that Icahn eventually abandoned his pursuit, but only after a costly, bitter fight.)

Under the new rules, such situations will be a thing of the past. Bidders must agree to acquire at least 50% of the shares they don't already own, closing the door on such tactics. The CSA proposals "put some power back in the hands of shareholders and boards," says Kingsdale's Tabesh.

It's unclear exactly when these changes might come into effect, but when they do, expect to see a very different climate in the world of M&A, one with more certainty, less regulatory wrangling and, hopefully, lower legal bills.

And owing to the fact that boards will have a lot more ability to defend against offers they don't like, it's reasonable to expect a lot fewer hostile bids being tabled. In this new environment, the onus will be on potential acquirers to make a good first impression. "I think obviously it will put pressure on bidders to come out with an attractive bid," said Tabesh. "These proposals are absolutely more shareholder and target-company friendly."

Photograph: Hudbay Minerals; Chris Wattie/Reuters

Federal securities regulator in view

Draft legislation paves way for 2015 implementation, while Ottawa works to get more provinces onside

BY NEXT FALL, if the federal government continues on its present course, the proposed Cooperative Capital Markets regulatory system will be up and running—taking the country partway to meeting the Conservative government's eight-year-old effort to create a single national securities regulator to replace the current system of 13 distinct provincial and territorial overseers.

In September, the government released draft legislation for the creation of the new regulator, shortly after New Brunswick and Saskatchewan announced they'd join Ontario and British Columbia in supporting the new system. The draft bills pave the way for changes to federal and provincial legislation to bring the new system into force.


Joe Oliver

Oversight and administration for the cooperative system will rest with a single Capital Markets Regulatory Authority. The CMRA will have the power and responsibility for regulatory enforcement and adjudicative functions, management of systemic risk and to collect data to monitor capital markets. Regulation of things like trading facilities, market intermediaries and credit rating organizations also falls under this umbrella. Participating provinces, meanwhile, will lead day-to-day regulation of securities markets, based on passage of harmonized and modernized securities legislation in each jurisdiction.

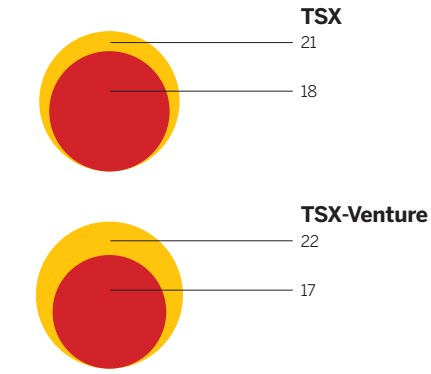
"Canada needs a cooperative system that will strengthen our capital markets, reduce red tape for businesses and attract more capital investment," said Finance Minister Joe Oliver in a statement issued when the bills were unveiled.

The minister's office is accepting comments on the draft bills until early November. It's expected that the final legislation will be introduced in Parliament early in 2015, with the cooperative regulator scheduled to be operational in the fall—around the same time as the next federal election, which is set for Oct. 19.

Negotiations with other provinces are continuing, meanwhile, in an attempt to bring more of them onboard. Of particular note is the situation in Alberta, which has been one of the staunchest opponents of a national regulator. With the recent election of former federal Conservative cabinet minister Jim Prentice as leader of Alberta's Conservative party and his subsequent swearing in as provincial premier, there's a new dynamic in play.

While Prentice recently said that he is opposed to the current cooperative plan, in 2008, while he was in the federal cabinet, he was of a different mind. Back then he supported the government's plans for a single, national regulator and encouraged Alberta to get behind it, calling it "an idea whose time has come."

Jul. & Aug. | New listings TSX & TSX-Venture

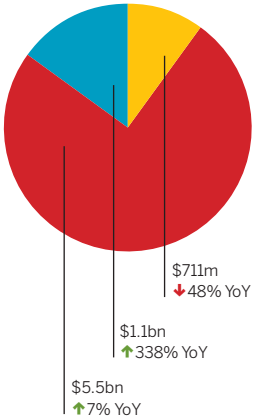


Jul.-Aug. 2014 Jul.-Aug. 2013

Source: TMX Group

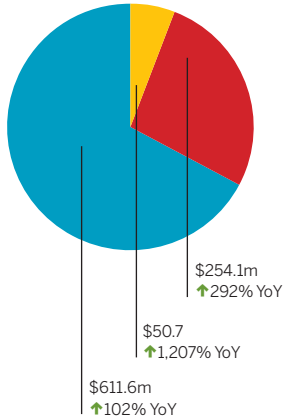
Jul. & Aug. | Capital raised TSX

Total 7.3bn
↑6.8%



Jul. & Aug. | Capital raised TSX-Venture

Total $916.4m
↑232%



IPOs Public offerings Private placements

Source: TMX Group

New listings/IPOs (Jul. 1-Sept. 15)

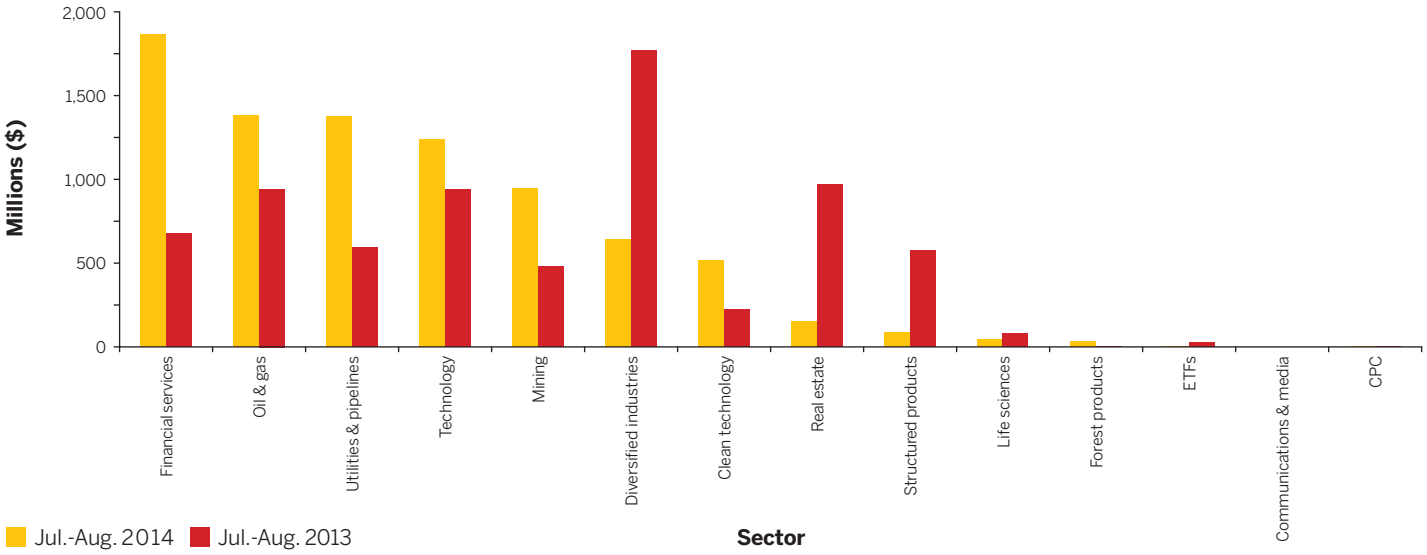
TSX		
Name*	**Type**	**IPO Price ($)**
Industrials		
Dream Hard Asset Alternatives Trust (DRA.UN)	IPO	10.00
DataWind Inc. (DW)	IPO	4.75
Manulife U.S. Regional Bank Trust (MBK.UN)	IPO	10.00
Mining		
Heron Resources Ltd. (HER)	New listing	n/a
Sulliden Mining Capital Inc. (SMC)	New listing	n/a
Oil & Gas		
Northern Blizzard Resources Inc. (NBZ)	IPO	19.00
Spartan Energy Corp. (SPE)	New listing	n/a

Source: TMX Group

*Excludes funds, preferred shares, debt, warrants. IPO price per share/unit

TSX-Venture		
Name*	**Type**	**IPO Price ($)**
Capital Pool		
Cluny Capital Corp. (CLN.P)	IPO	0.20
Maestro Capital Corp. (MCP.P)	IPO	0.10
Manera Capital Corp. (MEA.P)	IPO	0.10
Orletto Capital Inc. (OLE.P)	IPO	0.10
Rodeo Capital III Corp. (ROP.P)	IPO	0.10
Searchtech Ventures Inc. (MJN.P)	IPO	0.10
Whiteknight Acquisitions III Inc. (WKA.P)	IPO	0.20
Mining		
X-Terra Resources Inc. (XTT)	New listing	n/a
Oil & Gas		
Leucrotta Exploration Inc. (LXE)	New listing	n/a
Petro-Victory Energy Corp. (VRY)	IPO	0.40
Software Publishing		
01 Communique Laboratory Inc. (ONE)	New listing	n/a

Jul. & Aug. | Capital raised by sector TSX & TSX-Venture



Source: TMX Group

Other		
Eastwood Bio-Medical Canada Inc. (EBM)	IPO	0.25

Source: TMX Group

*Excludes funds, preferred shares, debt, warrants. IPO price per share/unit

CNSX

Name	**Type**	**IPO Price ($)**
Diversified Industries		
Grand Peak Capital Corp. (GPK)	New listing	n/a
Innovative Properties Inc. (INR)	New listing	n/a
Target Capital Inc. (TCI)	New listing	n/a
Velocity Data Inc. (VCT)	New listing	n/a
Life Sciences		
Alta Vista Ventures Ltd. (AVV)	New listing	n/a
ChroMedX Corp. (CHX)	New listing	n/a
My Marijuana Canada Inc. (MYM)	New listing	n/a
New Age Farm Inc. (NF)	New listing	n/a
Seashore Organic Medicine Inc. (SOM)	New listing	n/a

Mining		
Alchemist Mining Inc. (AMS)	New listing	n/a
Cerro Grande Mining Corp. (CEG)	New listing	n/a
Evolving Gold Corp. (EVG)	New listing	n/a
GeoNovus Minerals Corp. (GNM)	New listing	n/a
Goldrea Resources Corp. (GOR)	New listing	n/a
Grenadier Resource Corp. (GAD)	New listing	n/a
Inexco Mining Corp. (IMC)	New listing	n/a
United Coal Holdings Ltd. (UCL)	New listing	n/a
Oil & Gas		
Asean Energy Corp. (ASA)	New listing	n/a
Technology		
Eyelogic Systems Inc. (EYE.A)	New listing	n/a
Fundamental Applications Corp. (FUN)	New listing	n/a
SecureCom Mobile Inc. (SCE)	New listing	n/a

Source: Canadian National Stock Exchange

*Excludes funds, preferred shares, debt, warrants. IPO price per share/unit

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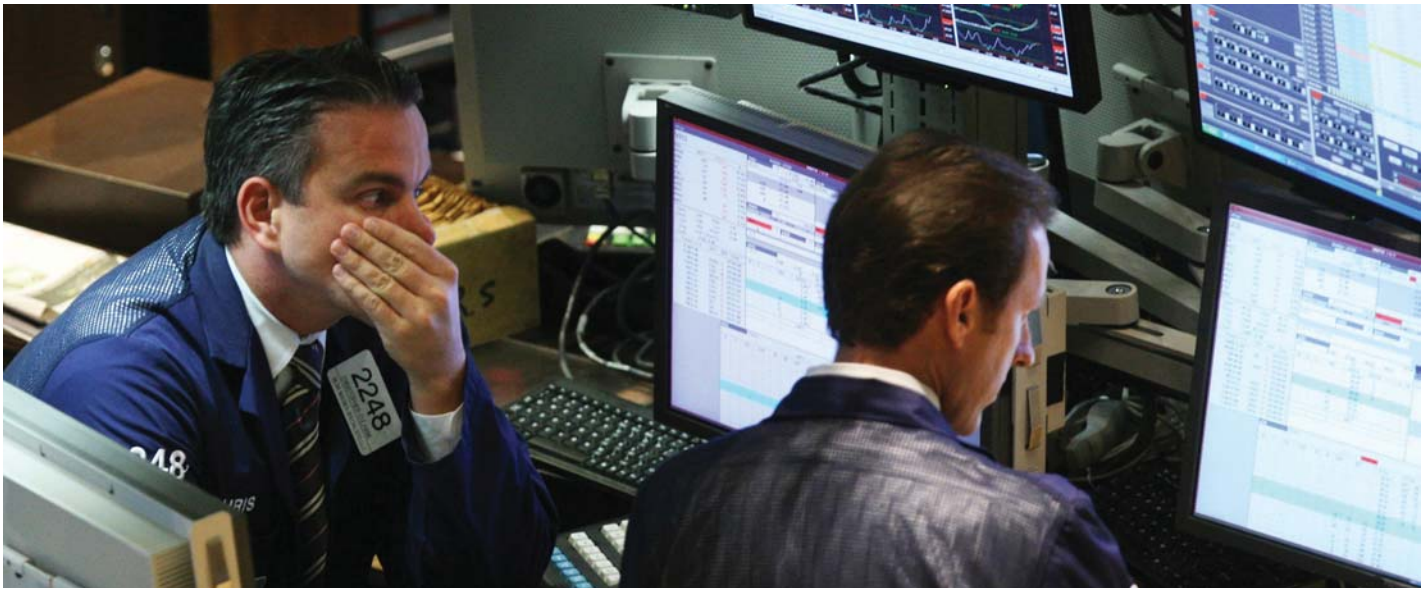

What did we learn again?

The lessons of 2008 and the consequences of loose credit and too much debt have barely been written. Yet judging by the latest leverage ratios and reemerging risky lending instruments, they're already being forgotten

By Robert Olsen with Andrew Luetchford

When I was in business school 25 years ago, most of the cases we studied were written in the early '80s and many of them featured companies that suffered financial duress from high interest rates and over-leveraging. It occurred to me then that our generation of graduates would be better equipped than previous alumni to recognize the inherent cyclicality of the economy, thus ensuring we'd approach investment opportunities in a more balanced and conservative way.

And yet we've ended up making the same mistakes. When I reflect on why, I'm inclined to say it was likely due to our getting caught up in the moment, somehow thinking the situation was unique and just plain forgetting what we learned from those cases written decades earlier.

Forgetting the fundamentals prior to the downturn of 2007-08 was somewhat plausible given the long length of time since the previous financial crisis. However, what is going on in the market today is beyond belief considering the credit crunch was just six years ago. Leverage ratios—debt as a multiple of earnings before interest, taxes and depreciation (EBITDA), basically—have now surpassed their 2007 peak of 5.6x multiple, reaching 5.7x in the second quarter of 2014.

The U.S. Federal Reserve has issued guidelines meant to reduce these overleveraged deals by requiring banks to hold higher capital requirements against these riskier assets. Although this has reduced regulated entities' appetite for the high-leverage deals (banks held approximately 3% of leveraged financings during the first half of 2014 versus 26% prior to the last financial crisis in 2007), other institutions have stepped in. This is illustrated by the recent resurgence of the collateralized loan obligation (CLO) market—this year, CLOs are forecast to exceed the record $100 billion raised in 2007.

A particular area we thought we might never see again is the use of aggressive lending instruments, such as covenant-lite loans—a type of loan whereby financing is given with limited restrictions on the debt-service capabilities of the borrower. The evolution of covenant-lite loans can generally be traced to the historical buyout power of private equity groups performing highly leveraged buyouts, which pushed for these relaxed terms. However, over time, the availability and use of covenant-lite loans has expanded to all borrowers. According to Standard & Poor's, these loans reached $96.6 billion at the heart of the financial boom in 2007, only to fall to $2.6 billion in 2008 and a low

Photographs: Jeff Kirk; Brendan McDermid/Reuters

of $0.5 billion in 2010. However, what has happened since then borders on extraordinary, with volumes rising to $57 billion in 2011, $91.4 billion in 2012 and $261.6 billion last year. What is truly scary about these loans is that if we face another big downturn in the economy, the financial institutions that hold them will be severely restricted in their ability to step in and enforce measures to protect their capital.

A concerning example of the impact of a downturn recently occurred in the UK, where Phones 4U, a private equity-backed, 720-outlet mobile phone retailer, went into receivership after being unable to renew contracts with key customers. Receivership occurred less than a year after the company issued approximately $350 million worth of subordinated, covenant-lite notes to be used to dividend out cash to the owners. (The notes increased the company's adjusted leverage in 2014 to above seven times EBITDA, according to S&P.) As it now stands, those note holders will receive little or nothing in any restructuring, given they are subordinate to approximately $1 billion of debt.

The dividend issued by the company ensured the owners recouped their investment—seemingly indicating that the risk had shifted too much toward the lenders. Time will tell if this is a one-off or a sign of things to come. For now, it is a timely reminder of the risks associated with lending, and borrowing, with high amounts of leverage.

IT IS POSSIBLE to read too much into an individual case and so it is worth noting that the current underlying dynamics are markedly different from those leading up to the credit crisis. We now live in a low-interest-rate, low-volatility environment driven by a glut of cheap liquidity pumped into the financial sector by central banks. This environment has led investors to take on greater risk in order to meet their return expectation. Pricing has now dropped below the pre-crisis levels—yield to maturity of new issuance in the middle market was 6.3% in September, compared to 8.6% in June 2007, according to S&P Capital IQ. However, are they accepting too much risk given returns are now lower than before the credit crunch? Or does the stabilization of the markets and suppression of interest rates by central banks mean that higher leverage is now inherently less risky?

Although central banks can influence the availability of funding and pricing of that debt, the performance of the borrower will fundamentally determine whether investors and lenders generate their required return. Worryingly, Lincoln International has recently noted that over 50% of companies in the U.S. are experiencing EBITDA declines. Declining performance whilst carrying higher leverage, even in the current low-interest-rate environment, is not sustainable. The aforementioned example is a case in point. Bear in mind, too, that while most of the growing debt problem is American-based, as we saw in the last crisis, any issue faced in the U.S. will surely impact Canadian companies, and swiftly.

It is easy to follow the crowd and take on more debt but given the market dynamic we are experiencing, it would be good to eat some more blueberries, wild salmon and nuts (examples of brain food according to researchers). It might help us more clearly remember the credit crisis of just six years ago and the pitfalls of not ensuring our borrowing situation is better controlled and aligned to a company's performance.

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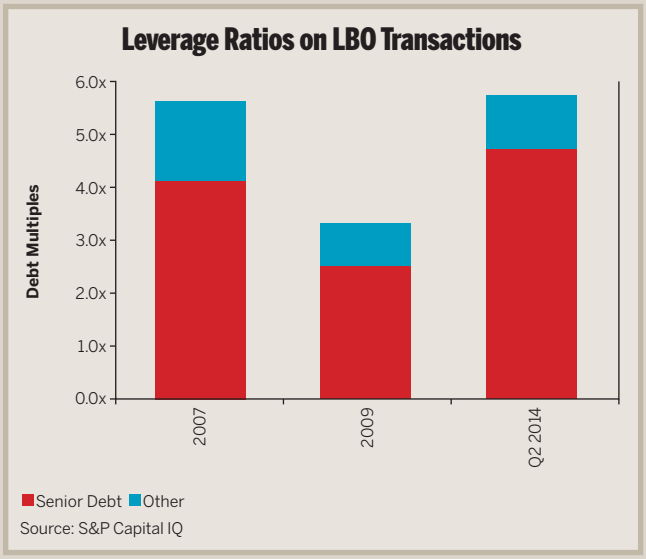
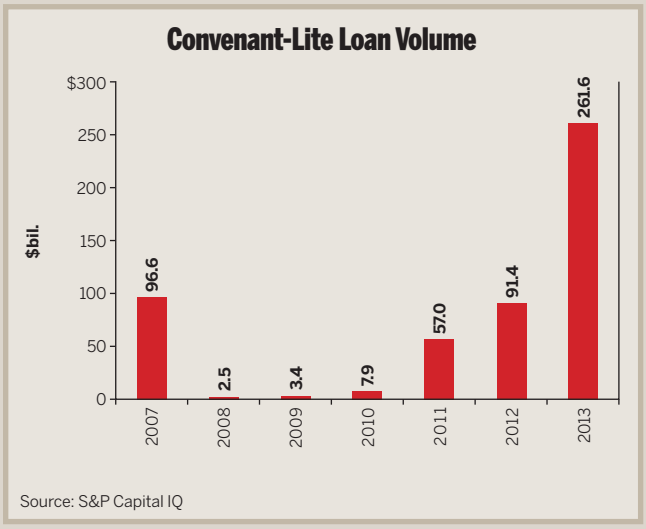
Testing our limits

How much leverage is too much leverage? After the crash, we thought we knew. But we're back there again

The charts below, which pick up on data cited in the main column, clearly reveal the extent to which higher-risk corporate lending and borrowing has not only rebounded from the crash but now exceeds peak levels seen in 2007. The first chart shows leverage ratios on transactions, with senior debt segments highlighted. In the bottom chart, we see the dramatic rise in covenant-lite loans, to the point where volumes in 2013 were more than double that of 2007. Amid all of our navel-gazing during the credit crunch, the widespread use of these loans was identified as one of the practices that precipitated the crash. Yet they're now back in favour, big time.





Own the pay-for-performance narrative

A board's best defence in the say-on-pay era? Conduct an independent pay-for-performance assessment, then communicate it to your shareholders

By Ken Hugessen with Lisa Oldridge

Shareholders are interested in ensuring compensation is aligned with performance, and they use say-on-pay votes and director elections to express concerns where this is not seen to be the case. Unfortunately, many issuers fail to provide compelling evidence of a strong link between pay and performance beyond making aspirational statements, which do little to demonstrate that pay outcomes are indeed aligned with performance

Proxy advisers have naturally moved to fill this vacuum, providing their own approaches to evaluating pay for performance (P4P). While many observers are critical of proxy advisers' methodologies, their P4P tests do address shareholders' needs for an independent assessment of whether a company is aligning pay with performance.

For boards, a practical response is to conduct their own assessments, and then engage with shareholders on the results. But to be effective, it is critical that boards take ownership of the pay-for-performance "storyline" by forming and expressing an opinion early on.

Proxy season is not the time to start building support for your approach to P4P. Reacting to a negative recommendation from a proxy adviser may be too little, too late to prevent a hit on say-on-pay voting and director elections. Even a convincing refutation of a "vote against" recommendation may be in vain if no engagement work has been done in advance, as the cumbersome machinery of the institutional investors' governance process can be too large and slow moving for the message to reach the right people in time. On the other hand, proactively engaging with shareholders well ahead of the proxy season not only allows the board to take control of the narrative, it also provides intelligence on investors' voting expectations for the upcoming season, voting guidelines and voting process, permitting a faster response to any negative sentiment.

Boards need to understand the critical issues in conducting a P4P assessment: i) choosing the performance peers and ii) considering what performance measures to use to compare performance (e.g., Total Shareholder Return, EPS growth, ROE, etc.). These two elements drive the conclusions of the P4P test, and give rise to many of the concerns about the proxy adviser recommendations.

Much of the criticism of the proxy adviser P4P tests stems from their methodologies for creating peer groups. In response, companies should take ownership of peer group creation, and provide a basis for the choices made. If compensation peers are distinct from performance peers, this should be clearly stated and why.

In assessing and presenting relative performance, metrics should be selected based on their ability to influence shareholder value. In addition to relative Total Shareholder Return (TSR), other measures, particularly those that are easily comparable among peers, can be useful. Boards should be able to explain their selections.

The next step is to conduct an independent analysis and interpretation of the results. The board should be aware it may not be entirely comfortable with the results. Some adjustment of the incentive plan performance conditions, or an application of board discretion (potentially negative), may be called for. In these cases, timely dialogue with shareholders may also be appropriate and warranted.

Even assuming the analysis shows a good alignment of pay outcomes with performance results, there is a final (and critical) step.

Proxy season is not the time to start building support for your approach to pay for performance. Reacting to a negative recommendation from a proxy adviser may be too little to prevent a hit on say-on-pay and director voting.

Clear and candid disclosure of the board's assessment in the circular is essential, especially where stock performance has suffered due to an unfavourable business or commodity cycle, and the pay-for-performance linkage may not be obvious. That the board is demonstrably concerned with this issue will not be lost on shareholders—nor on the proxy advisers, who will think twice before making a recommendation that contradicts a well-reasoned, effectively communicated demonstration of strong alignment of pay with performance.

There is no substitute for well-designed incentive plans. But unless you demonstrate their effectiveness and communicate this with shareholders, a good story can be lost...or worse.

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Photograph: Jeff Kirk

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Not yet in Canada? Pity

Proxy access is a corporate governance game changer that needs to take hold in this country. Its adoption would directly lead to better boards and better-performing companies

By Richard Leblanc

I teach my students and counsel board clients that shareholders elect directors; directors appoint managers; directors are accountable to shareholders; and managers are accountable to directors. This is largely theoretical.

Here is the reality: shareholders cannot select directors, cannot communicate with directors, and cannot remove directors, by law, without great cost and difficulty. Therefore, directors are largely homogenous groups who are selected by themselves, or, worse yet, by management.

Addressing the foregoing is the one piece of reform that will change corporate governance and performance for the better. The rest is, as they say, window dressing.

I have encouraged institutional investors and regulators to consider advocating for what is known as "proxy access." Under this process, one or more shareholders who own a modest, minimum threshold of shares, for a set period of time, can select up to 25% of proposed directors of the total board in an uncontested election in a given year. When shareholders "select" their nominees for the board, these directors would be listed in the management proxy circular alongside the management slate of directors. There would be no costly proxy battles or dissident slates. There would be no undue influence by management to marginalize shareholder-nominated directors within or outside of the proxy. Rules of the road would be set.

With proxy access, all shareholders would get to decide on the best directors from among the management-proposed and the shareholder-proposed directors. Ideally, the selection should be as neutral as possible. The focus should be solely on the qualifications, competencies and track record of the proposed directors for election at that company.

Under this new regime, there will be winners and losers. The practical effect may be that legacy or unqualified directors may withdraw from this scrutiny, as Canadian Pacific directors did at the time of shareholder Pershing Square's involvement. This is not an undesired outcome and creates a market for the most qualified directors to rise to the top.

In Canada, proxy access does not exist. It is under consideration by Industry Canada, which is looking at implementing it for larger shareholders (a 5% ownership threshold) for all federally incorporated companies. The U.S. is only slightly more advanced. When the Securities and Exchange Commission (SEC) proposed proxy access in 2010 under Dodd Frank, management and lawyers who work for management used shareholder money to fight it. They won in the U.S. Court of Appeals, on the basis of an inadequate cost-benefit analysis. The upshot is that proxy access there is now left to companies on a one-off basis and, thus far, has only occurred at a small number of firms. Regulators in both countries should revisit the topic as soon as possible.

Opponents to proxy access argue that shareholders will propose special-purpose directors or directors who lack background or experience. The evidence is the opposite. Shareholders are better at proposing directors who have the track record and industry expertise that current boards lack. Recall Canadian Pacific, where not a single director possessed rail experience prior to shareholder involvement. In this context, a director qualification dispute is welcome and will focus the lens on competencies of directors, including industry expertise.

Despite these implications, the real resistance to proxy access is with management. As a group, they are averse to independent expert directors and, the record shows, will vigorously fight proxy access. In considering its merits, then, directors should not be beholden to management, nor their advisers, nor act out of self-interest in entrenching themselves; rather, only the best interests of the company, including its shareholders, should guide them. There is evidence that the market values strong proxy access positively, leading to an increase in shareholder wealth. Independent-minded directors with the competency and skills to serve on the board should welcome it—and let shareholders and the new competitive market take over the uncomfortable task of ferreting out the underperformers.

Proxy access opponents argue that shareholders will propose directors who lack background or experience. The evidence is the opposite. Shareholders are better at proposing directors who have the expertise that current boards lack.

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Photograph: Jeff Kirk

Control in chaos

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Competition: the greatest external risk

Obtaining a deep, objective understanding of competitors' strengths and weaknesses—analyzing everything from their current strategies to ability to execute—is fundamental to assessing risk and driving your own performance

By John Caldwell

Excluding self-inflicted exposures, competition is usually an enterprise's greatest threat. Yet, ironically, management and board rigour around competitive analysis is often perfunctory at best. Quarterly board packages frequently contain cursory information on competitor activities. Even most strategic plans fall woefully short of competitive assessments.

Common flaws for boards and management in understanding and addressing competitive risk include underestimating the effectiveness of competitors' strategy and resources while at the same time overestimating their own. Assuming competitors are frozen in time is another shortcoming. These failings inevitably lead to failure to develop a truly competitive, executable strategy and, ultimately, underperformance.

To rectify this, a comprehensive competitive analysis should encompass the following: an assessment of current positioning, comparative competitive advantages and gaps, strategy, capabilities and resources and benchmarked performance.

The analysis of current positioning should include absolute and relative market shares and related margins. The market share analysis should address the fundamental issue of scale. That is, do competitors enjoy the advantage of scale? And, does this advantage result in above industry-average margins? Conversely, if the company is the largest player in the sector, is it appropriately leveraging its scale advantage to produce industry-leading results?

Competitive strategic analysis is multidimensional. It starts with understanding the six or eight things companies must excel at, such as product development, marketing and service quality, to succeed in the industry they serve. This analysis must be comparative with a degree of quantification. It is insufficient to conclude that one player is simply better. The questions are how much better and how important is that advantage? Once you understand this, it is then relatively easy to discern the most important strategies your competitors employ. For example, if innovative product development is critical and one competitor excels on this dimension, the analysis should consider in detail all aspects of its approach to product development such as how it gains insight into customer requirements, meets launch deadlines and uses technology.

The next step is to understand competitors' ability to execute. This involves examining resources and capabilities—human capital, tangible and intangible assets and financial resources. Human capital analysis includes the assessment of leadership, organizational structure, depth of talent, culture, cost of staffing and labour, core competencies and differentiated skills relevant to strategy.

Assessing competitor assets usually involves understanding capacity, the quality of assets and historical and replacement costs as well as the quality of intellectual property and reputation among customers. Financial resource analysis should look at the structure and quantum of equity and debt and the sources and cost of capital.

The final component of competitive analysis is customer performance and financial benchmarking. Customer performance should measure customer satisfaction, share of wallet, reputation, new customer intake and overall customer retention. Financial performance should involve comparative analysis of top-line growth, margins, returns, cash generation, and asset management and deployment. The art form is to understand the underlying reasons why competitors are performing better. For example, if a competitor is producing superior gross margins, is it because of relative pricing power, product/service mix, capacity utilization, materials costs or overhead expenses and cost of capital?

It is insufficient to conclude that one player is simply better. The questions are how much better and how important is that advantage? Once you understand this, it is easy to discern the most important strategies your competitors employ.

There are multiple sources to help you glean all this information. They include public disclosures, tailored competitor customer surveys, interviews with former competitor employees, discussions with vendors, industry analysts, investors as well as no shortage of web-based data. Consultancy firms, investment banks and accounting firms can also be helpful in pulling together unbiased competitive information, particularly if they have deep experience in the sectors.

John Caldwell is a veteran CEO and board member experienced in distressed situations. He recently authored the CPA Canada's A Framework for Board Oversight of Enterprise Risk. *E-mail: johncaldwell@rogers.com.*

Photograph: Jeff Kirk

CSCS

Excellence in Governance Awards Winners Announced

The Canadian Society of Corporate Secretaries (CSCS) would like to congratulate the winners of the 2nd Annual Excellence in Governance Awards (EG Awards/Prix EG):

1. **Best sustainability, ethics and environmental governance program**
   ATB Financial
2. **Best use of technology in governance, risk and compliance**
   Royal Bank of Canada
3. **Best approach to board and committee support**
   ATB Financial
4. **Best stakeholder engagement by a governance team**
   Bombardier Inc
5. **Best practices to enhance boardroom diversity**
   Hamilton Community Foundation
6. **Best practices in strategic planning, oversight and value creation by the board**
   Royal Bank of Canada
7. **Joyce Borden-Reed CSCS distinguished contribution award**
   Sylvia Groves, President and Creative Director, Governance Studio
8. **Best overall corporate governance**
   BC Cancer Foundation
   MTS Allstream
9. **CSCS Peter Dey governance achievement award**
   Stephen Jarislowsky and Claude Lamoureux (Co-Founders of the Canadian Coalition for Good Governance)

Best sustainability, ethics and environmental governance program
ATB Financial – Stuart McKellar (left), General Counsel, VP Properties and Corporate Secretary with Sponsor Richard Rohan, Vice President Corporate Sales, TMX Group

Best use of technology in governance, risk and compliance
Royal Bank of Canada – Lucille D'Souza (left), Assistant General Counsel and Head, Subsidiary Governance Office with Sponsor Renee Walton, Managing Director, North America, The Corporate Secretary Magazine

Best approach to board and committee support
ATB Financial – Stuart McKellar (left), General Counsel, VP Properties and Corporate Secretary with Sponsor Gigi Dawe, Principal, Research and Guidance and Support Leader, Corporate Oversight and Governance, Chartered Professional Accountants of Canada

Best stakeholder engagement by a governance team
Bombardier Inc – Dominique Cristall (right), Advisor, Communications and Corporate Social Responsibility with Sponsor Tony Branco, Director, Business Development, NYSE Governance Services

Best overall corporate governance
BC Cancer Foundation – Doug Nelson (left), President and CEO
MTS Allstream – Paul Beauregard (right), Chief Administrative officer and Corporate Secretary with Sponsor Jeffry Powell, Executive Vice President and Director of Sales, Diligent Board Member Services

Best practices to enhance boardroom diversity
Hamilton Community Foundation – Anne Lupkoski (right), Corporate Secretary and Executive Assistant with Sponsor Andrew MacDougall, President, Spencer Stuart Canada

Best practices in strategic planning, oversight and value creation by the board
Royal Bank of Canada – Carol McNamara (right), VP, Associate General Counsel and Secretary with Sponsor Catherine Gardiner, Director for the Directors College

Joyce Borden-Reed CSCS distinguished contribution award
Sylvia Groves (left), President and Creative Director, Governance Studio with David Masse, Chairman, CSCS

CSCS Peter Dey governance achievement award
Peter Dey (right), Chair, Paradigm Capital with Sponsor Paul Lessard, Sales Director for Western Canada, RR Donnelley accepting on behalf of Stephen Jarislowsky and Claude Lamoureux

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Business with purpose

Pending the results of an Industry Canada review, benefit corporations—for-profit businesses using the power of business to solve social and environmental problems—could soon be legally entrenched

By Sandra Odendahl

Last December, when the federal government launched a review of the *Canada Business Corporations Act (CBCA)*, topics like shareholder rights and executive compensation grabbed much of the spotlight. But among potential changes that might have the biggest lasting impact, consider its invitation for comments on rules facilitating the incorporation of benefit corporations—hybrid enterprises with both profit-making and socially responsible goals. If Industry Canada ultimately decides to add incorporation of socially responsible enterprises to the range of legal entities, it could open the door in this country to entirely new forms of profit-making enterprises that solve environmental and social problems.

In some jurisdictions, legislation has already been amended to allow for benefit corporations—a legal status distinct from incorporating as a not-for profit or a business corporation. Benefit corporations are for-profit companies that are intended to produce public benefits and operate in a socially and environmentally responsible manner. While there are already a large number of for-profit corporations that operate responsibly, this new corporate form enables for-profit companies to formally embed a corporate social responsibility mission in their articles of incorporation.

Industry Canada's review asked for comment as to whether the *CBCA*'s existing provisions are sufficient to enable these corporations, or whether amendments are needed. Among the 78 submissions it received, dozens endorsed creating a new, socially responsible-specific, legal entity. And momentum seems to be in their favour.

In 2013, the U.S. state of Delaware amended its corporate legislation to permit companies to incorporate as "public benefit corporations," for-profit corporations intended to produce a positive effect (or a reduction of negative effects) on one or more categories of persons, entities, communities or interests (other than stockholders in their capacities as stockholders), and to operate in a responsible and sustainable manner. It's especially important to have this legislation in Delaware, where: (1) there are more active public companies registered than any other jurisdiction; and (2) under Delaware law, it is very clear that the primary stakeholder of the traditional for-profit company is the shareholder and the primary purpose is profit.

In Canada, corporations are not actually prohibited from taking actions that will improve their environmental and social impact. The *CBCA* allows directors to have their corporations pursue and earn nonfinancial results that are "in the best interests of the corporation." Profit should be the primary focus, but the Supreme Court of Canada has opined that stakeholders' interests should be taken into account and treated with a minimum standard of fairness, consistent with the corporation as a "responsible corporate citizen." Chiefly, this protects corporate responsibility actions that are reasonably likely to increase profitability or enhance the brand.

Several provinces have passed or are contemplating legislation to support the dual objectives of benefit corporations. For example, British Columbia's *Business Corporations Act* now allows Community Contribution Companies (C3). According to the B.C. Ministry of Finance, "C3 status allows entrepreneurs in B.C. to pursue social goals through their businesses while still generating a profit and providing investment opportunities to like-minded investors." Meanwhile, across the country, more than 100 companies have gone a different route, seeking B Corp certification, a voluntary designation that provides third-party endorsement of a for-profit company's commitment to public good. B Corps are certified by B-Lab, a U.S.-based non-profit organization, after meeting a range of performance standards in several categories. But while their ranks are growing around the world, they are not governed by statute.

While there are already a large number of for-profit corporations that operate responsibly, this new corporate form enables for-profit companies to formally embed a corporate responsibility mission in their articles of incorporation.

That's why the changes now contemplated by the federal government are so important. Benefit corporations are not charities. They are for-profit businesses that see an opportunity to use the power of business to solve social and environmental problems. It's time we help get them going and then get out of their way.

Sandra Odendahl is director of corporate sustainability at RBC. The views expressed are her own, not necessarily those of RBC. E-mail: sandra.odendahl@rbc.com.

Photograph: Jeff Kirk

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Spare the paper, boost the engagement

Notice and access is making slow progress in Canada since it was approved in 2013. But wherever it's applied, shareholders show they are ready for new channels for proxy communication

By Chaya Cooperberg

In a recent conversation with four other investor relations officers, each representing a sizeable Canadian public company, the topic of notice and access came up. Of the five of us, only two were early adopters of the process introduced in 2013, which allows shareholders to access annual meeting materials online instead of receiving hard copies in the mail.

The adoption rate is even lower market-wide, but that could soon change. Notice and access is the kind of issue that typically resides in company backrooms, rarely hitting the radar of board members and executives. But it will become hard to ignore, as it slowly, but inexorably, becomes the norm for annual proxy communications.

Some background. For years, one of the most expensive line items in my investor relations budget was the printing and mailing of our annual meeting materials, which were distributed to all of our 12,000 shareholders. I suspected that the majority of packages quickly landed in the recycling bin, but we had no recourse. I envied our corporate neighbours in the U.S., where rules changed in 2006 to allow the delivery of meeting materials only to shareholders that requested them.

Flash forward to 2013 when the Canadian Securities Administrators (CSA) approved the use of notice and access for proxy solicitations. In that first proxy season, over 160 issuers, representing 9% of those eligible, implemented notice and access through investor communications firm Broadridge. My company was among them.

That year, we reduced the number of annual reports and information circulars that we printed and mailed by 90%. Yet our voting rates at our annual general meeting remained consistent with the prior year. We received only a handful of requests for materials, which we promptly fulfilled.

Another early adopter, Calgary oil and gas producer Baytex Energy, had a similar experience. "Based on experience in the U.S., Broadridge suggested that 3% of shareholders would call for a copy [of the information circular]," recalls vice-president, investor relations Brian Ector. "We provided our transfer agent with 500 additional copies. I believe that the number that they actually mailed out was less than 100."

My company achieved a meaningful reduction in printing costs, but postage savings were partially offset by Broadridge's fees for the notice-and-access service. Broadridge estimates that companies will save about $6.70 per shareholder, on average, in print and postage expenses.

Perhaps most encouraging is that despite concerns to the contrary, notice and access is associated with higher levels of shareholder engagement and voting turnout. In 2014, according to Broadridge, issuers that sent traditional print packages had retail investor voting rates of 39.2%, while issuers that used notice and access had a retail investor voting response rate of 46.2%.

Interestingly, voter turnout is actually higher in Canada than in the U.S. for companies using notice and access, due to a key difference in the rules. Canadian companies are required to send shareholders a voting information form along with the notice, while U.S. companies only send the notice. Theoretically then, notice and access could become more pervasive in Canada than in the U.S., where the adoption rate by public companies is greater than 30%. But so far, we're lagging. In 2014, the Canadian adoption rate rose to 13%, versus 20% in the second year of notice and access in the U.S.

Despite concerns to the contrary, notice and access is associated with higher levels of shareholder engagement and voting turnout. In 2014, voting response was 7% higher for issuers using notice and access versus traditional mail outs.

Patricia Rosch, president of Investor Communication Solutions, International at Broadridge Financial Solutions, expects it to grow as issuers see the success of others adopting it. "The fact that we have seen a higher voting rate will help," she says. "Others are still adjusting to a new way of the proxy process."

In our case, switching to notice and access did require more planning and lead time with our transfer agent and proxy firm. But the communication went smoothly, we significantly reduced our costs and had high voter turnout. It also demonstrated our commitment to using multiple means of communication to keep investors engaged in our annual proxy voting process.

Chaya Cooperberg is vice-president of investor relations and corporate communications at Progressive Waste Solutions in Vaughan, Ont. E-mail: chaya.cooperberg@progressivewaste.com.

Photograph: Jeff Kirk

Cyber risk takes centre stage

A string of high-profile cybersecurity breaches has focused attention on an emerging challenge in the boardroom: are directors doing enough to ensure their companies are adequately protecting sensitive data and technology?

BY JIM MIDDLEMISS

When Doug Hayhurst traveled on company business in the 1980s, the former IBM and PwC executive used a briefcase with no corporate logo when visiting certain jurisdictions so as not to attract attention. Fast-forward to today. Hayhurst, an independent director who sits on a number of boards, including Canexus Corp. (TSX:CUS), says the rule for executives visiting certain high-risk jurisdictions is to travel with a clean computer and a burned cell phone. "Every business has some information. You don't want to be the weak link that opens it up."

Welcome to the new world order—one where organizations of all sizes must increase security measures and lock down the precious data stored in their information vaults to protect it from prying eyes and sloppy employees.

The problem, however, is that data is not a tangible gold brick and IT systems aren't capable of being isolated like a Fort Knox.

The result is that public companies are increasingly subject to revelations about embarrassing and damaging data breaches—and their boards are being held to account for the adequacy of their oversight.

Home Depot breach

The latest to make headlines is Home Depot. On Sept. 8th, America's largest home improvement retailer confirmed that its payment data systems for the U.S. and Canada had been breached, dating back to April.

Interestingly, it wasn't the retailer that first made the information public. A week before official confirmation, cybersecurity expert Brian Krebs, of Krebs on Security, blogged that banks were seeing evidence Home Depot was the source of a batch of new stolen credit and debit card data that was for sale on the Internet.

A short time later, Home Depot confirmed that the attack involved a record 56 million accounts, carried out with custom-built malware that had "not been seen previously in other attacks. The company now estimates costs of $62 million to fix the problem, offset by $27 million in insurance.

More ripples and repercussions are sure to follow, if the experience at Target Corp., which saw 40 million credit and debit cards stolen over a three-week period in 2013, is any indication.

Target's intrusion was traced back to password credentials stolen from a heating, ventilation and air conditioning (HVAC) firm that worked for Target and had access to its systems. And the news rocked Target's board—with calls from proxy adviser Institutional Shareholder Services for director resignations (which never happened)—pummeled its share price, and led to the resignation of its CEO and CIO. So far Target has spent more than $148 million to recover (still short of the $256 million that retailer The TJX Companies, Inc. spent after 45 million of its customer debit and credit cards were stolen in 2007).

The scenarios currently playing out at Target and Home Depot are a director's worse nightmare.

"Cybercrime is very sophisticated," says Deborah Rosati, who chairs the audit committee on Sears Canada Inc.'s board (TSX:SCC) and sits on a number of other boards. "You are always on guard."

Rosati, an accountant and management consultant, says her biggest fear is waking up in the morning to a news-alert about the company that "I wasn't aware of."

Adds Rosati: "At the end of the day you want to ensure that you've got the systems, the processes and the people in place to manage your business and...that you've got monitoring to ensure you are mitigating high-risk areas."

Stakes are high

The cybersecurity stakes are high. Consulting firm McKinsey estimates that "over the next five to seven years, US$9 trillion to US$21 trillion of economic-value creation, worldwide, depends on the robustness of the cybersecurity environment."

The worrisome part is that many boards seem ill prepared for the

Biggest fear: "Cybercrime is very sophisticated," says Deborah Rosati, audit chair at Sears Canada. "You are always on guard."

Photograph: Jeff Kirk

Customers exposed: The recent data breach at Home Depot involved a record 56 million customer accounts

challenge. A 2012 CyLab report from Carnegie Mellon University found "boards are not actively addressing cyber risk management." It comes at a time when the report says "corporate data is at a higher risk of theft or misuse than ever before." While boards are focusing on risk management, the study found that "there is still a gap in understanding the linkage between information technology risks and enterprise risk management."

The cost of a breach can be staggering. A 2014 study by the research firm Ponemon Institute of 314 companies in 10 countries found that a data breach costs an average of US$3.5 million per incident, up 15% over last year. The U.S. leads with an average of $US5.85 million per incident (the study did not examine Canada). The probability of having a breach involving a minimum of 10,000 records was 22%.

Ponemon also found brand and reputation declined between 31% and 17% and that it can take more than a year for an organization to recover its corporate image. As well, a breach damages consumer confidence in the company, can lower share price and expose a company to regulatory hearings and class-action lawsuits.

Interestingly, system glitches and careless employees and contractors accounted for 59% of breaches, according to Ponemon, while malicious and criminal attacks made up the remainder. However, criminal and malicious breaches are also the most costly.

Attacks are economic

Larry Clinton, president and CEO of the Internet Security Alliance, which promotes thought leadership and education around cybersecurity, says boards need to rethink the way they approach data breaches.

"People tend to think of it as an IT issue," he says, but "95% of attacks are economic" and the "economic incentives favour the bad guys."

"They are cheap to launch, incredibly profitable, and easy to do."

Moreover, he says, they are increasingly difficult to detect. Advance persistent threats, an effective form of cyberattack usually carried out by nation states, has "moved down the chain and criminals are now doing these things," notes Clinton, who worked with the National Association of Corporate Directors (NACD) in the U.S. to create a cyber risk manual for directors that has been endorsed by the U.S. Department of Homeland Security.

"It's a huge problem and its getting worse," Clinton says of malicious and criminal attacks.

It's not just financial data that is at risk, but everything from intellectual property to business processes are under siege. Part of the problem, he says, is the increasing connectivity of the global economy.

Policies like bring-your-own-device to work, voice-over-internet-protocol phone systems, a digitally connected supply chain all bring efficiencies and lower costs to organizations, but at the same time, they increase the number of doors into an organization that need to be locked down. "It's really hard to secure all this stuff."

And it's going to get worse, he says, as society enters the next stage of the Internet evolution, known as the Internet of Things. That's the creation of a smart grid, where more and more devices, such as fridges or microwaves, will be interconnected and interact with other systems, such as a smartphone.

"It is going to massively increase the number of access points and therefore the number of vulnerabilities."

Photograph: Beck Diefenbach/Reuters

Even now, director Hayhurst is surprised at the amount of snooping that goes on. "People are trying to go into systems all the time. It happens daily," regardless of whether a company has customer lists or valuable credit card information, he says.

So what should directors do? Mark Fernandes, cybersecurity leader at Deloitte in Toronto, says there are five key messages directors need to keep in mind when it comes to cybersecurity risk: define it, address it, measure it, execute on a plan to combat it and communicate that plan. "The risk landscape is changing on an hourly, if not daily basis," he notes.

Manage cyber risk across the enterprise

Directors say the first thing boards need to understand is cybersecurity risk needs to be managed on an enterprise basis and not simply viewed through the IT lens.

"Cybersecurity is just another one of the risks an organization needs to manage," says Gary Baker, who sits on the board of financial company Libro Credit Union. "The board should be continuously challenging management to make sure what they are doing is appropriate and reasonable in circumstance."

Rosati notes "not everything is foolproof. It's about risk mitigation and reputational risk."

Hayhurst adds: "I don't put it as a new risk." Rather, he runs a multi-year calendar for the board's audit committee that addresses various risks facing the company, including cybersecurity. It usually comes up under IT security and controls or tech advancement.

Regular briefings are also key, says Clinton, since cyber threats can change quickly. But how much is enough? The NACD guide suggests quarterly committee briefings, while the full board should be briefed at least semi-annually.

Where responsibility should lie at the board for overseeing cybersecurity risk remains a bone of contention and it is all over the map.

In some companies, it falls to the audit committee, which is already overseeing financial controls. In others it falls to a full board committee, while at others a risk committee may be assigned the task.

The ISA's Clinton suggests that a full committee of the board should be in charge because it's too important to isolate to one committee.

Hayhurst, however, feels that the audit committee is appropriate because it can give the topic a "deep dive and report back intelligently to the whole board. A board can delegate, but it can't abdicate."

Challenge the IT assumptions

Mike Strople, president of telecom services provider Allstream, who also sits on the board of the Liquor Control Board of Ontario, warns boards not to be complacent when it comes to cybersecurity risk.

For example, he says, "Firewalls can give a false sense of security."

"A firewall is not a big stone concrete wall, it has all sorts of holes punched in; it is only if you get all the holes lined up the right way that it does what it is supposed to do."

He warns: "If the CIO or whoever advises the board says it's a green check mark or a red X, it doesn't come in those flavours. It is much more shades of grey."

Adds Deloitte's Fernandes: "What often gets overlooked is that insiders are being used as launch pads." Those looking to gain access will target individuals in a company who might have specific knowledge about new products, or IT systems and security. For ex-

Cyber risk oversight 101

Before directors can provide proper oversight on cyber risk, they must ask management the right questions. Here's a good list

When it comes to managing cybersecurity risk, there is no shortage of information out there for directors to tap.

"The last three years we've seen a lot of investment in cybersecurity," says Mark Fernandes, cybersecurity leader at Deloitte in Toronto. "Boards are starting to educate themselves."

One essential theme in the material is the matter of whether or not directors are asking management the right questions about their firm's exposure to a cybersecurity breach.

Here is a compendium of the top questions directors should ask management, drawn from the National Association of Corporate Directors' handbook for *Cyber-Risk Oversight*.

Situational awareness

- What are the company's cybersecurity risks and how is the company managing these risks?
- How will we know if we've been hacked or breached and what makes certain we will find out?
- Who are our likely adversaries?
- What is the biggest vulnerability in our IT systems?
- Has the company assessed the inside threat?
- Have we had a penetration test or external assessment? What were the key findings and how are we addressing them? What is our maturity level?
- Does our external auditor indicate we have deficiencies in IT? If so, where?

Corporate strategy and operations

- What are leading practices for cybersecurity and where do our practices differ?
- Where do management and our IT team disagree on cybersecurity?
- Do we have an enterprise-wide, independently budgeted cyber risk management team? Is the budget adequate?
- Do the company's outsource providers and contractors have cyber controls and policies in place and clearly monitored? Do these policies align with the company's expectations?
- Is there an ongoing company-wide awareness and training program established around cybersecurity?
- Does the company have adequate cyber insurance?

Incident response

- How will managers respond to a cyberattack? Is there a valid corporate incident response plan? Under what circumstances will law enforcement and other relevant government entities be notified?
- What constitutes a material cybersecurity breach and will those events be disclosed to investors?

ample, the advent of social media such as LinkedIn—where people post their business credentials—makes it easy for criminals to target key employees.

Also beware of third parties. One oil company was breached when hackers put malware on a downloadable menu from the local Chinese restaurant that staff often used.

As well, vendors and suppliers pose real challenges. Simply imposing your own security policy onto a vendor won't work, since they may have 10,000 clients doing the same thing, each of which has different standards. As well, the sophistication levels of a vendor's IT system may be suspect compared with your own organization. "You have to be real diligent in how you sign up third-party providers," says Rosati. Understand what your company policies are, she says.

Make sure you are benchmarking and monitoring

Hayhurst says it is also important to have benchmarking in place so the company knows where it stands in relation to its industry and competitors, which includes examining costs and making sure that the IT department is delivering value. "It may not be the mindset they (IT) bring to everything."

Rosati adds it is important for directors to understand what basic systems are in place to monitor and protect their companies. So things like policies governing internal password protections and what happens when someone leaves a company to make sure they are not walking off with the passwords and how often a company changes them. "What technologies and what security tools does a company need?" is another area that needs to be examined, she says.

Adam Kardash, a privacy lawyer with Osler Hoskin & Harcourt, urges boards to put in place an incident response protocol as part of an overall "robust network governance framework" that addresses cybersecurity risk.

"The response plan is critical when the cybersecurity incident occurs and you are in a crisis event. The plan outlines the core steps, at a very general level, that the enterprise will take to address the crisis and investigate it to contain whatever has occurred and establish immediate and long-term remediation."

He says a cross-disciplinary team needs to be established comprising senior management, information technology, legal, human resources, public relations, insurance, key vendors, forensic and people from core areas of the business. Law enforcement officials also need to be contacted.

He adds that the plan needs to be tested in advance of a real event. Little things can stymie it, such as the inability to reach a key person because of lack of contact information. "Once you're in a crisis, all bets are off. You have to have information at your fingertips."

Understand legal ramifications

Ross McKee, a corporate lawyer at Blake, Cassels & Graydon in Toronto, says directors also need to understand the legal ramifications of cybersecurity risk.

Regulators in Canada and the U.S. are approaching cyber disclosures differently. The U.S. has been much more prescriptive and in 2011, the SEC issued guidelines on disclosure of cyber risk. For example, companies "should disclose the risk of cyber incidents if these issues are among the most significant factors that make an investment in the company speculative or risky."

In Canada, the Canadian Securities Administrators issued notice 11-326 in September 2013 warning companies about cybercrime and advising them to "take the appropriate protective and security hygiene measures necessary to safeguard themselves."

"Issuers should consider whether the cybercrime risks to them, any cybercrime incidents they may experience, and any controls they have in place to address these risks, are matters they need to disclose in a prospectus or a continuous disclosure filing."

Repercussions: Target's 2013 breach rocked the board and cost the CEO and CIO their jobs

Ross McKee says while the SEC guidance is "helpful," the reality is that "people don't like to talk about security measures very much."

"The SEC recognizes the challenge public companies face describing risk factors with respect to cybersecurity disclosure without giving away the keys to hackers at the same time."

Kardash, however, warns that more disclosure is on the Canadian horizon. The next round of amendments to Canada's *Personal Information Protection and Electronic Documents Act* will include a security breach notice provision, requiring companies to advise the public if their personal information has been compromised. "There will be more reporting," he says.

Get the right expertise on board

As cyber risk issues become higher priorities for boards, directors say it's increasingly important that boards have adequate IT expertise. Unfortunately, it's a subject that can glaze over the eyes of the most adept director.

What constitutes the right skill set is still a matter of some debate. "You need diversity around the board," Rosati says, and given the profile that IT issues are taking, "there might be an emerging trend to see more competence around that."

Baker, however, believes that "you need people on boards that understand the business issues associated with IT. They have to understand the business implications of technology and the business risk of the technology. It's an important distinction."

Boards would also be wise to seek third-party advice about the vulnerability of their systems, says Hayhurst.

Above and beyond any specific action, however, Hayhurst stresses that the time for boards to act is now. "The hackers are going everywhere. It's doesn't matter what business you are in, you are going to be attacked and may be a through point. You cannot afford to be the weak link."

Photograph: Geoff Robins/Reuters

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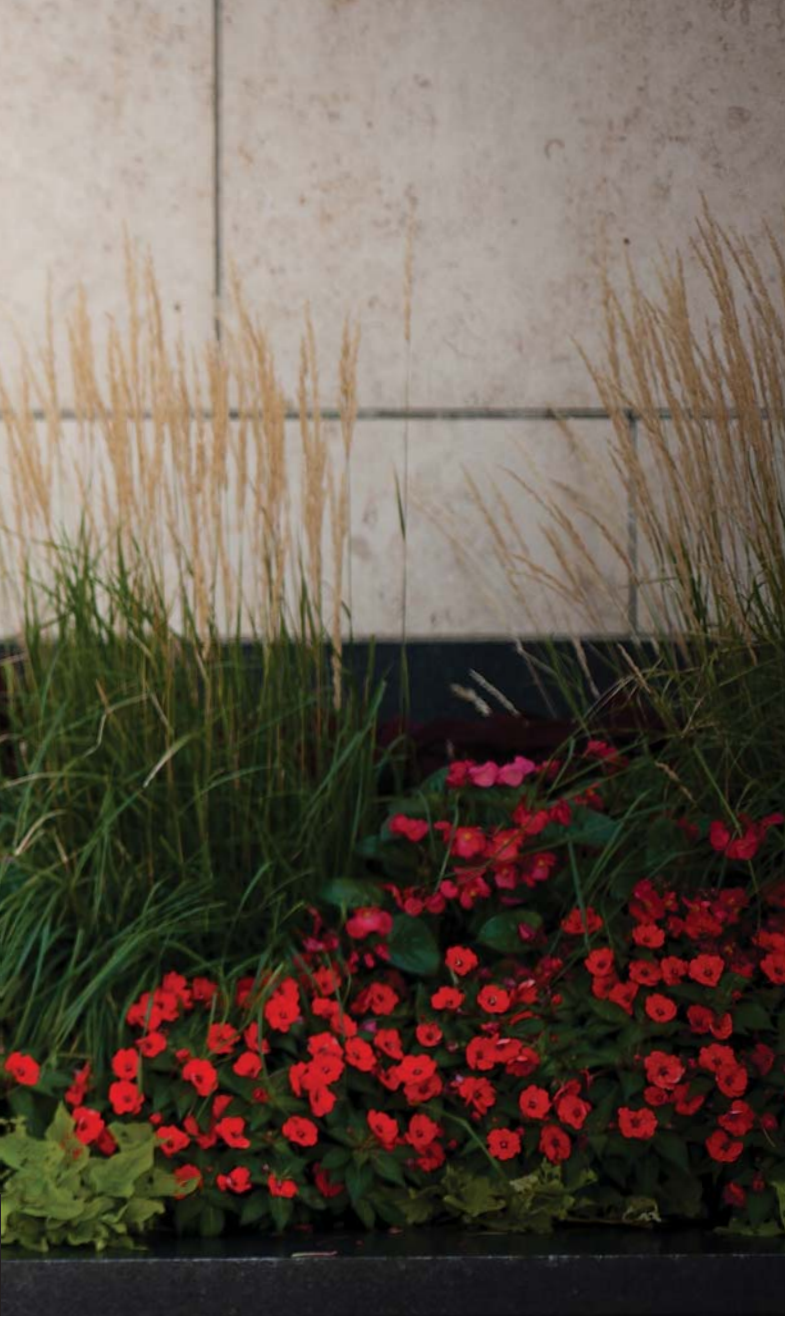
The elephant in the room

Mining veteran Rudi Fronk, CEO of Seabridge Gold, has hit the mother lode—the largest undeveloped gold-copper project in the world. Now comes the hard part: finding a major partner to buy him out

BY KERRY BANKS

Photograph: Theo Stroomer



Boundless reserves, limited market: Seabridge's KSM deposit in northern B.C. is so immense, Rudi Fronk (photo, left) says it's out of reach for all but a handful of the world's biggest gold and base metal miners

Rudi Fronk is back on the road. The smooth-talking 56-year-old CEO and chairman of Toronto-based Seabridge Gold Inc. (TSX:SEA) is in the midst of a month-long travel itinerary that will take him to various mining conferences and industry showcases in the U.S. and Europe. Today, Fronk is in Denver, Col., to give a presentation at the Denver Gold Forum, the world's most prestigious gathering of precious metal companies. Held every September, the invitation-only event is attended by leading precious metal investors and analysts. It's an ideal venue for Fronk to tout the potential of his company's massive Kerr–Sulphurets-Mitchell (KSM) gold and copper deposit in northwestern British Columbia and establish connections with potential investors.

With a modest corporate headquarters in Toronto and fewer than 20 full-time employees, Seabridge may not be one of the bigger players in the mining business, but its KSM enterprise is a bona fide heavyweight. Fronk describes it as "the largest undeveloped gold-copper project in the world today in terms of reserves. Contained within four separate deposits we have 38.5 million ounces of proven and probable gold reserves and 10 billion pounds of copper reserves," he says in a phone interview. That's enough reserves to produce a staggering 130,000 tonnes of ore a day for up to 52 years. Imagine the weight of the world's largest cruise ships and you have an approximation of the daily tonnage that would be carted away. It's estimated that the mine would create 1,800 jobs during construction and more than 1,000 permanent jobs once it is up and running.

At this point, however, all this vast promise remains unfulfilled. Seabridge is a mine finder, not a mine builder. In order to move the project into production the company needs to join forces with a senior partner with the capital and resources to handle the venture's intimidating $5.3-billion estimated price tag. Ironically, KSM's most obvious selling point—its immense size—is also one of the greatest obstacles to its realization. Because of the project's logistics, it really can only be successfully built and operated by one of the world's largest gold companies. "There are probably less than 10 companies in the world able to operate a mine this size," admits Fronk.

When Fronk founded Seabridge with venture capitalist James Anthony and geologist William Threlkeld in 1999, he could not have realistically imagined he would be in the position he finds himself today—heading up a company that owns 100% of such a massive find. It may be just as difficult to believe that after carefully cultivating this bonanza for 15 years he has not been able to advance the project into its final stages. Instead, with the mining industry in a prolonged slump and the majors now retreating from big acquisitions and the construction of new mines, Fronk finds his company having to work to improve the attractiveness of what, in better days, would be a can't-miss proposition. The good news there is that Seabridge has been adept in clearing environmental assessment hurdles and earning local First Nations' support. But until it lands a major partner, there won't be any payoff.

FROM THE BEGINNING Seabridge's operating philosophy was quite specific: purchase North American gold projects with proven resources that have large exploration potential, fund work to expand those resources and upgrade them to reserves, and then sell or partner the ventures when they reach the production stage.

It's a philosophy that Fronk says he established after his calamitous experiences with Greenstone Resources Ltd., a Toronto-based mining company for which he served as CEO and president from 1993 to 1998. Greenstone operated gold properties in Central America that Fronk exuberantly promoted, raising $300 million in financing on promises of seven million ounces of gold reserves and 600,000 ounces in annual production. But in 1998, rather than reaping handsome profits, Greenstone abruptly collapsed. Critics contend the cause was poor administration and runaway expenses, but Fronk blames the debacle on a rapid drop in gold prices, conflicts with local communities and the devastating effects of Hurricane Mitch.

A key lesson that Fronk learned during this ill-fated adventure was to avoid the risky business of building or operating mines. Instead, he and his partners at Seabridge opted to go on a shopping spree. As Fronk recalls, "Due to the decline of the gold market, there were hundreds of projects for sale at distressed prices as producers struggled to stay in business." Between 1999 and 2002, Seabridge

purchased nine properties with estimated gold reserves of 15 million ounces for a bargain-basement price of $15 million.

The KSM property in northwestern B.C. was acquired in 2000 from Placer Dome. At the time, the site was known to have just two ore deposits—the Sulphurets and Kerr—and Placer estimated the yield at 3.4 million ounces of gold and 2.7 billion pounds of copper. But because gold was only trading at about $260 per ounce and copper at about 65¢ per pound, Placer had concluded that the project wasn't economically viable.

A few years later, when gold prices began to rise, Seabridge shifted its focus from acquiring properties to expanding its resource base through carefully targeted exploration. Drilling began on the KSM site in 2006, and not long afterwards, the company found the enormous Mitchell deposit, which is now regarded as the largest gold deposit ever discovered in Canada. Interestingly, an unlikely process has aided access to the ore here. Aerial photographs show the Mitchell glacier has retreated one kilometre laterally and hundreds of metres vertically since 1991. "You can easily see the difference from year to year," says Fronk. "Global warming is our friend."

High and mighty: Seabridge's Mitchell deposit, named for the adjacent Mitchell glacier, is the largest gold deposit ever found in Canada. Melting ice is aiding access to the site

In 2010, Seabridge drill bits unearthed the Iron Cap deposit, which added a fourth ore body to the project. As well, in 2010 the company continued to expand the Sulphurets and Kerr deposits. In tandem with the drilling, Seabridge also devised a plan for extraction. It calls for the Kerr, Sulphurets and Mitchell deposits to be mined as open pits using earth-moving equipment. Mitchell would then be mined as an underground operation later in the mine life, while Iron Cap would only be mined as an underground operation.

Seabridge has spent about $200 million developing the KSM site to the point where the bulk of its resources are now classified as reserves. While that no doubt helps support Seabridge's share price and affirms the giant deposit's legitimacy, it only heightens the need for a partner with serious capital—never an easy sell, and one made that much tougher by the depressed state of the market. "Since 2009 there has been a general drift of capital out of the mining sector. It started with the institutions and soon was followed by others," says Jeremy South, global leader for mining M&A at Deloitte.

It's a familiar spiral to everyone in the industry, one that's deepened since 2011. As South explains, a combination of escalating costs coupled with downward trending of commodity prices has slashed profit margins in mining and caused investors to put their capital elsewhere. As a result, instead of acquiring new properties as they had been doing, mining firms have been cutting costs and focusing on means of enhancing profitability. The switch in direction was articulated in 2013 by Jamie Sokalsky, then chief executive of Barrick Gold Corp. (TSX:ABX), the world's largest gold company, who bluntly announced, "We have no plans to build any new mines."

Fronk, for his part, insists that the KSM mine would be economically feasible at today's gold prices (just below $1,200 an ounce as of early October). He notes that while the initial capital costs for the KSM mine are considerable, the operating costs are projected to be low—only $141 per ounce of gold. According to a 2012 feasibility study, the total production cost, including capital, is $603 per ounce of gold, a very favourable number. The initial payback period is pegged at six years.

Even so, many analysts believe that gold prices will have to climb significantly to stimulate new mining activity. "Uncertainty around the price of gold and the potential of it drifting lower is preventing companies from investing in new mines," says Stephen Mullowney, managing director and national deals leader in mining at PwC. "It's a volatile industry and even slight decreases in the price of gold can have a huge impact on margins. If gold prices were to rise $100 or $200 it would give more certainty to the industry."

WHILE SEABRIDGE MAY have no control over the vagaries of the metals marketplace, it has been able to advance the project in other respects, most notably in the complex "de-risking" process. To that end, on July 31 the company received its environmental assessment certificate from the province of B.C., clearing a key hurdle on the path towards construction.

KSM is only the second metal mine in the past five years in B.C. to secure an environmental assessment certificate, and according to Fronk, it's not simply because few companies are applying. Rather, it's because the process "is exhaustive and expensive." In Seabridge's case, Fronk estimates the procedure involved some 40 meetings with federal and provincial officials and local stakeholders over a period of six years. The mining application itself ran to 33,000 pages.

In order to fulfill the certificate's terms, Seabridge must comply with 41 legally binding requirements. The provisions include constructing water treatment facilities prior to the mining of any ore, building a selenium treatment plant by year five of operations, and switching to underground block caving for parts of the Mitchell and Iron Cap deposits, which will reduce the amount of waste rock moved by more than two billion tonnes. The conditions were developed following input from First Nations groups, government agencies and local communities. Because the KSM property lies a mere

Photograph: Seabridge Gold

30 kilometres from the Alaskan border, the company also consulted government officials from Alaska.

To ease the concerns of First Nations communities about the project's environmental impact, Fronk says that Seabridge made a number of design changes to its original plan, including moving its proposed production and tailings facilities to a less sensitive watershed 23 kilometres away from the mine. As a result, the company will have to bore a 20-kilometre-long tunnel through a mountain to allow transfer of rock from the mine to the processing plant.

"One smart thing that Seabridge has done was to get the First Nations involved early in the permitting process," says Raj Ray, an analyst in metals and mining at National Bank Financial. "A lot of companies have learned the hard way that you can expect long delays if you don't involve First Nations groups early in the process."

The proposed KSM mine sits on the traditional territory of the Nisga'a Nation. Earlier this year, the Nisga'a signed a benefits agreement with Seabridge that includes the promise of financial payments and commitments to train and employ members of the band. On the occasion of the signing, Mitchell Stevens, president of Nisga'a Nation, stated: "We appreciate Seabridge's open and direct approach to working with the Nisga'a Nation. They began consulting with us very early on in the development of the KSM Project design. They listened to our concerns and took them seriously."

The company has also earned the support of other First Nations in the area. It's inked an agreement with the nearby Gitanyow First Nation to fund programs to monitor wildlife, fish and water quality; the Gitxsan First Nation has given its endorsement; and the company is working towards an accord with the Tahltan First Nation. As Fronk explains: "We're going into land that these people have inhabited for generations, and we need to make sure that we're a responsible neighbour. Getting them on side is the only way to advance a project through the approval process."

The next step will be receiving the go-ahead from the federal watchdogs at the Canadian Environmental Assessment Agency, whose verdict is expected later this fall. With final federal and provincial environmental approval in hand, Seabridge can then apply for permits covering the specific requirements for construction.

Moving forward with the actual work will require a buyer ready to tackle some significant construction challenges. The KSM deposits are situated in a remote, mountainous area. The terrain is rugged, the winters severe (one of Seabridge's surveyors was killed by an avalanche in 2012) and the closest town—Stewart, B.C., located 65 kilometres to the southeast—boasts a population of 494. At the moment there is no road into the site, so everything must be transported by helicopter. Infrastructure is lacking, as is an easily available labour pool, but Fronk insists that concerns about the location's remoteness are overblown. He points out that the site is close to an existing road network and that Stewart, influenced by a marine climate, boasts the most northerly year-round, ice-free port in Canada.

Another logistical plus is easy access to cheap power. The KSM property will be able to connect to the newly installed $746-million Northwest Transmission Line that stretches 344 kilometres from Terrace to a substation near Bob Quinn Lake. "It will allow us to buy power for about 5¢ per kilowatt hour off the grid," says Fronk.

In fact, the power line has sparked a flurry of new mining activity in the region, which has been dubbed "the Golden Triangle" because of its wealth of buried riches. Both Seabridge and its next-door neighbour, Pretium Resources Inc. (TSX:PVG), are working on ore deposits that were initially explored and then abandoned by major companies. The adjacent claims of the two companies boast a total of 130 million ounces of gold plus vast amounts of silver, copper and other metals. The combined metal value on those two properties, calculated at today's prices, is an astounding $300 billion, and all of that value is concentrated within a 12-kilometre circle.

FRONK'S INVOLVEMENT with the KSM property has been an all-consuming pursuit for the past 15 years. "Almost all of my net worth is tied up in this company," he admits. Although the natural impulse is to push for fast results, he realizes that patience is necessary. "I've read studies that say the average time to develop a mine from initial exploration to the point where you are taking ore out of the ground is 19 years."

As Stephen Mullowney of PwC notes, "Rudi has been working on this project for a long time and I think he's gone about it the right way. He hasn't made any obvious missteps."

Fronk remains confident that gold prices will soon climb and that gold miners will once again ramp up operations. But even if they don't, Seabridge now has other options. In 2013, the company added a fifth deposit—Deep Kerr—that has produced markedly higher copper grades than seen before. The discovery of these new, richer copper zones is significant because it expands Seabridge's horizons.

"What's changed recently for this company is the discovery of high-grade copper at Deep Kerr. That has attracted the attention of some big, base metal companies," says Raj Ray. "I know that there have been expressions of interest. You can never tell for sure what might happen, but in terms of potential partners, the playing field has certainly widened."

Ray also believes that the style of mining that is likely to be used at Deep Kerr—underground block cave mining—makes it less likely that Seabridge will find a partner from the gold realm. "There are not a lot of gold companies that have the expertise to do block cave mining. But big base metal companies have that knowledge."

Whatever lies ahead, Ray says he would not expect any joint-venture partners to emerge before 2015 once all the environmental assessments are complete. "Permitting is such a big issue today, any potential partners would want to wait for all the approvals to come through."

In the meantime, drilling, surveying and assaying will continue on the KSM site, along with, Fronk notes, visits by potential partners. "Our geologists are very excited about the prospects and we have four drills turning right now to extend the Deep Kerr deposit, as well as to look for other high-grade core zones beneath our existing deposits. We think the best is yet to come," he says.

Why governance is our best defence

Ira Millstein, a man whose name is practically synonymous with corporate governance, issues a passionate reminder: it's the people's money that funds corporations and governance exists to protect it

Photography by Joe Leavenworth

If you're looking to build a list of the giants of corporate governance, you'd be hard pressed not to put Ira Millstein at the top. A lawyer, professor at Columbia law and business schools, and chair of the epynonymous Millstein Center for Global Markets and Corporate Ownership, Millstein has had an illustrious and influential career. As the bio below indicates, he's lent his ideas, opinions and authority on governance to many top U.S. corporations, commissions and non-profit organizations. Here, in conversation with governance and leadership adviser David W. Anderson, Millstein explains why he believes governance is so fundamental to business integrity and corporate success.

Ira Millstein

Primary role
Senior partner, Weil, Gotshal & Manges LLP

Additional roles
Adjunct professor, Columbia Law School and Columbia Business School; chair, Millstein Center for Global Markets and Corporate Ownership; chair, Governor's Task Force on the implementation of the *Public Authorities Reform Act* (New York State); member of the bar, U.S. Supreme Court, U.S. Court of Appeals (1st, 2nd, 3rd, 4th, 9th and Federal Circuits) and New York State

Former counsel on corporate governance to the board
General Motors Corp., Westinghouse, Bethlehem Steel, CalPERS, Tyco International, The Walt Disney Co., The Ford Foundation, The Nature Conservancy and Planned Parenthood Federation of America

Former roles
Senior associate dean for corporate governance, Yale School of Management; co-chair, Governor's NYS Ready Commission (New York State); chair, New York State Commission on Public Authority Reform; chair, Private Sector Advisory Group to the Global Corporate Governance Forum; chair, OECD Business Sector Advisory Group on Corporate Governance; chair, New York State Pension Investment Task Force; chair, Central Park Conservancy; adjunct professor, New York University School of Law; fellow of the Faculty of Government, JFK School of Government, Harvard University

Education
B.S. (Engineering), Columbia University (1947); J.D., Columbia Law School (1949)

Honours
- Named "Best Lawyer" for antitrust, corporate compliance, corporate governance, corporate and securities/capital markets law (Best Lawyers in America)
- 2012 International Who's Who of corporate governance lawyers
- New Yorkers for Parks 2012 Legacy Award for role in revitalizing Central Park
- Elected fellow, American Academy of Arts & Sciences
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David W. Anderson **Your name is synonymous with corporate governance around the world. It's defined your career as much as you've defined it. Why does governance mean so much to you?**
Ira Millstein Let me say up front, I respect and admire the corporation and oppose anything that interferes with the productive exercise of capitalism. Corporations are the best means we've invented to provide value to everyone—goods and services for all of us as consumers, returns to investors, taxes to the government and jobs for people—which provide them with money to invest, pay taxes and spend in the economy. Not only do corporations provide such value now, they hold our future welfare in their share capital—the wealth we will rely on to sustain us. It's not hyperbole to say everything is a stake here. I think corporations protect us, so we have to protect them. The mechanism of governance offers the best protection for us all—employees, consumers, investors and government.

David W. Anderson **What does governance protect us from?**
Ira Millstein Governance is a necessary defence against entrenched interests, greed, corruption, incompetence and indifference. With so much money in play in our remarkable capitalist system, there's an open invitation for abuse. I see significant risks to our future well-being, a future made possible by our money that's invested in corporations. This is the key insight I want to share—that it is *our* money that powers the corporate world and which corporate governance must protect. That money doesn't belong to the banks or the hedge funds or the pension funds; it belongs to the people it comes from—working people. The appalling thing is that most interested parties forget that—the institutional investors, the intermediaries, the proxy advisers, the directors and the executives all seem to have forgotten whose money it really is. They have grown accustomed to using our money for their benefit. Most troubling, though, is that the public forgets that it's their money. Consequently, there's little sense of ownership, stewardship and accountability because most people aren't sufficiently aware enough to care.

David W. Anderson **What is the message you want people to understand about the nature of capitalism and corporate governance?**
Ira Millstein It's simple. Corporations and our system of capitalism exist for our benefit. It's through our investments that we provide the fuel for the whole system. Whatever happens after we invest our money, we will be forced to live with the outcome, because we are the intended beneficiaries of this system. This is so important for our population to understand that I'm writing a book on it now. We can't lose sight of the fact that working people are the actual owners of capital and the very people who are relying on corporations to create value for the long run. I think this is the critical link in the story of capitalism and corporate governance.

David W. Anderson **What's your assessment of how well working people currently understand the system?**
Ira Millstein The public isn't sufficiently aware. People don't truly understand what's at stake. They don't understand what corporate governance is supposed to do, nor the capitalist system of which corporate governance is a part. The public's view of the issues is clouded by self-serving intermediaries. While the working people are in fact supposed to be the intended beneficiaries of the system, too few of the intermediaries in the system treat working people as the prime beneficiaries. How is it that so many people invest so much in mutual funds, with their huge fees and lacklustre results? Not everyone is going to read John Bogle—though they should because he's got it right. Moreover, do these mutual and hedge funds all care about the corporations in which they invest, or are some simply playing with stock certificates? The public should understand enough to make better decisions themselves and support corporate governance practices that exist for their protection. A lot of people get hurt when corporate governance doesn't work right.

David W. Anderson **How then does corporate governance offer protection?**
Ira Millstein I want people to understand this in personal terms. The fundamental purpose of corporate governance is to see to it that *my money* is handled properly—that it flows to the right place. We have to get this right because if we screw it up, we're in big trouble. Corporate governance is the machinery that protects me. I don't know in every sense where my money is going, but I expect that the people who handle my money will keep in mind that it's mine, not theirs. To put a human face on this accountability, corporate governance provides the means by which shareholders pick boards who pick managers who provide value. I'm relying on governance decisions to get money to the corporations on whom I'm going to depend for my security down the road, and that my money within those corporations is being used to invest wisely for the future. I need that money to grow if I'm going to get a benefit. So I need corporate governance to funnel my money into the hands of corporations that are investing for the future growth of stocks and bonds, by producing goods and services. The only way I will benefit in the future is if those companies use my money to create long-term growth. This means I need to be sure the corporation has a board that knows it's my money they are using. That's how the whole system is intended to work—for us to be the long-term beneficiaries of growth through the investment of our capital. Anyone who interferes with this, I have to question.

We can't lose sight of the fact that working people are the actual owners of capital and the ones relying on corporations to create value for the long run. This is the critical link in the story of capitalism and corporate governance.

David W. Anderson **Over the decades, in your role as counsel to hundreds of corporations and adviser to governments and regulators, what are some of the failures of governance or interference you've seen?**
Ira Millstein A few things really frustrate me. Pension funds should be the bulwark of society; most working people look to their pension fund for accumulation of capital over time. So why does a pension fund invest in a hedge fund? Yes, their goal is to increase its return so the state doesn't have to contribute as much, but what the pension fund is often doing is investing in something that doesn't match the S&P. This is counter-productive to what the pension fund wants to achieve. Certainly

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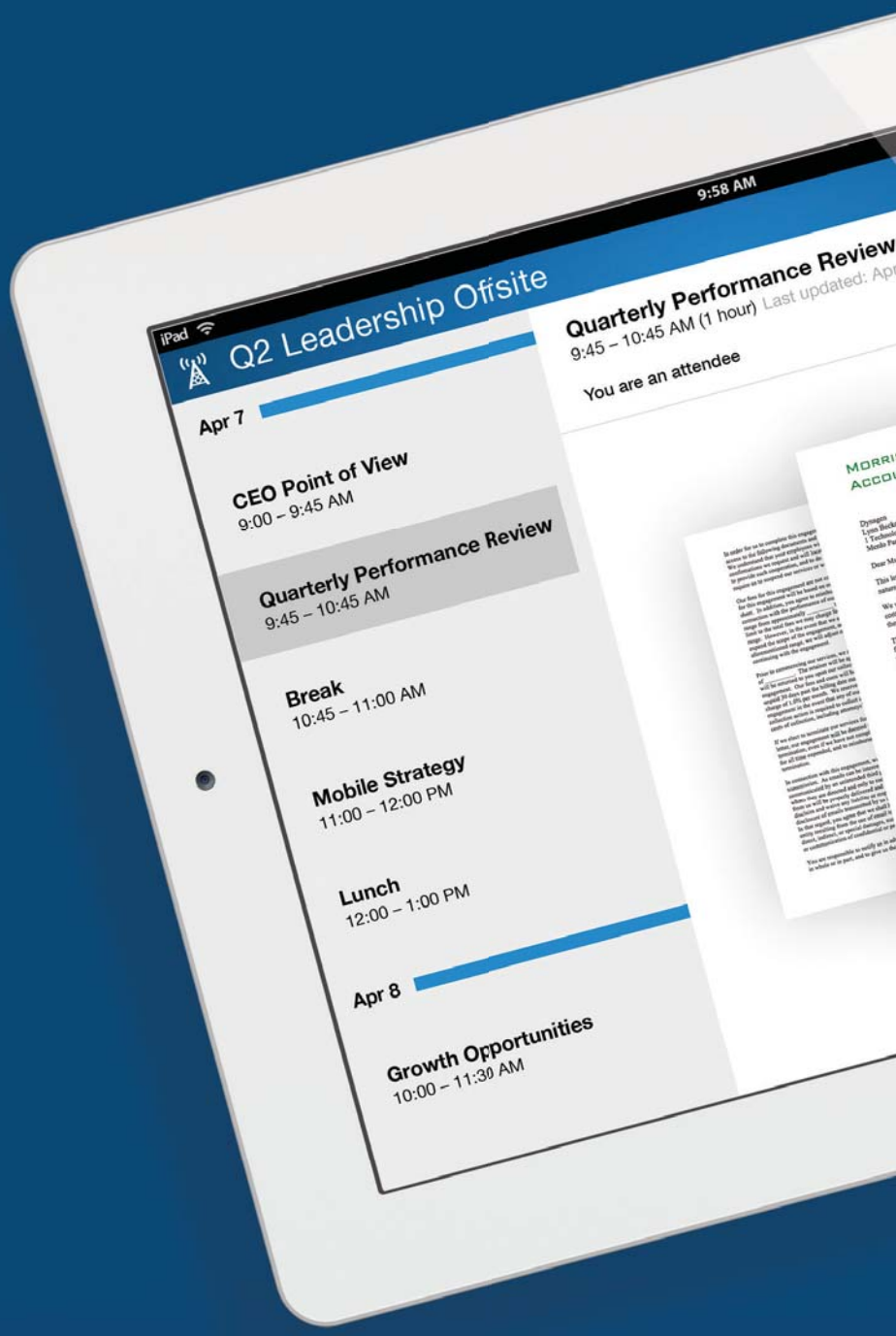

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some hedge funds are value investors but others are playing the market. I don't understand why pension funds don't see this and pick out the right hedge funds. I think a pension fund ought to be able to discern what the hedge fund is doing and invest only in those that are using money to improve the board and management, not just gambling.

On the other side of the equation, I'd also hope that corporations would be able to discern who, as investors, are coming in to upset them or improve their management. I don't like seeing corporations throw up walls and unnecessarily create staggered boards or poison pills to keep ideas and people away. I can see that a corporation may want some leverage in dealing with investors, but more often these tools are used to block genuine performance improvement.

Finally, I'm tired of seeing boards be so frightened of missing a quarterly earnings expectation that they won't invest in the future. We've got to get past the mantra of quarterly returns. Why don't boards stand up for a long-term, growth-oriented model and convince shareholders of what is right? I've known large companies such as IBM and Verizon that missed many quarters to change themselves into something that would endure. It cost them during the transition but they had shareholders who believed in their strategy and were patient through the transition. Those boards and their shareholders prioritized long-term over short-term considerations. I fault corporations that are fearful of doing this. I see it as a message when they can't demonstrate they're on the right tack.

David W. Anderson **You've been legal counsel to major boards as they've charted new courses in corporate governance and reshaped the field. What contributions to the evolution in corporate governance are you most proud of?**

Ira Millstein I'd choose two: the practice of independent directors meeting alone in executive sessions and the establishment of board leadership independent of the CEO. When John Smale and Harry Pearce turned GM around years ago, the idea of independent directors meeting alone was unheard of. It was seen as treason against the CEO. GM's board had never met alone as just the independent directors to discuss GM's business performance and its leadership, as they were afraid of what management would say. Smale recognized that the directors were not open and candid with management present and said we're not going to be an effective board unless we meet without management. I helped him craft the rules for meetings of the independent directors. Similarly, we created independent board leadership—either in the form of the board chair or lead director—to run the business of the board. The person who runs the board should sit at the head of the table separate from the CEO and set the agenda. These initiatives, which transformed the practice of governance, were not invented in a law school. They came from inside a boardroom created by business people who understood what they had to do to get it right. Business people came up with these ideas and they spread like wildfire.

David W. Anderson **The professional basis of your work with business people is the practice of law. What's the unique contribution to corporate governance that legal minds bring?**

Ira Millstein Nothing unique. You are highlighting one of the problems with the system. Very few business schools teach corporate governance, but many law schools do. How did corporate governance wind up in the hands of those who don't run corporations? Corporate governance should be controlled by business people, not lawyers. Directors tell me all the mega rules that today are "corporate governance" have little to do with a good board. Quality governance has to do with the quality of directors: Do they know the business? Do they work together to take risks and operate transparently?

When I look at a board, I ask myself, "Is this a group that will work together to make the corporation better?" I don't like outsiders interfering in business decisions. Who knows better than the directors and executives? Boards shouldn't get caught up in rules and external dictates. Let the directors talk to their management and get on with the business of business—understanding their business model and market, managing finances and raising capital. Would you have to give business people a rulebook to run their company? Of course not. Yet we have detailed rules and regulations that proxy advisers focus on that are too often inventions of the legal community. Lawyers aren't trained to understand the essence of how business works. Their focus should be on human qualities, because that's what matters.

I'm tired of seeing boards be so frightened of missing a quarterly earnings expectation that they won't invest in the future. Why don't boards stand up for what is in the long-term interest of growth-oriented businesses?

Now let me be fair to the legal community. There are borders that ought to be created by the legal community for directors to work within—defining concepts like loyalty and care. The legal rules ought to assure the application of these concepts makes sense. But as a lawyer, I'm not going to tell you anything about how to run your board.

David W. Anderson **What do you tell boards, then?**

Ira Millstein Recently I was before a well-qualified board that wanted me to talk about good governance and remind them of what rules to follow. I said, "No, you don't need to hear that from me because you're a really good board. I can see it. You are talking and arguing the points and you know this business. By virtue of the fact you asked me to come in and you take minutes you are exercising due care, and you are not operating for your own interest, so you are doing exactly what you should be doing." They had a staggered board and it's working fine for them. My advice was that if some proxy adviser says vote against this practice, say "no" and explain why you do what you do. Similarly, a poison pill isn't always bad, especially if the wrong guy comes knocking. My only advice would be to keep it as simple as possible, so it's not a dead hand. The bottom line is this: legal advice is good if directed at the principles involved. Duty of care and loyalty are about what's happening in the market, and I have confidence that business people know that.

David W. Anderson, MBA, PhD, ICD.D is president of The Anderson Governance Group in Toronto, an independent advisory firm dedicated to assisting boards and management teams enhance leadership performance. He advises directors, executives, investors and regulators based on his international research and practice. E-mail: david.anderson@taggra.com. Web: www.taggra.com

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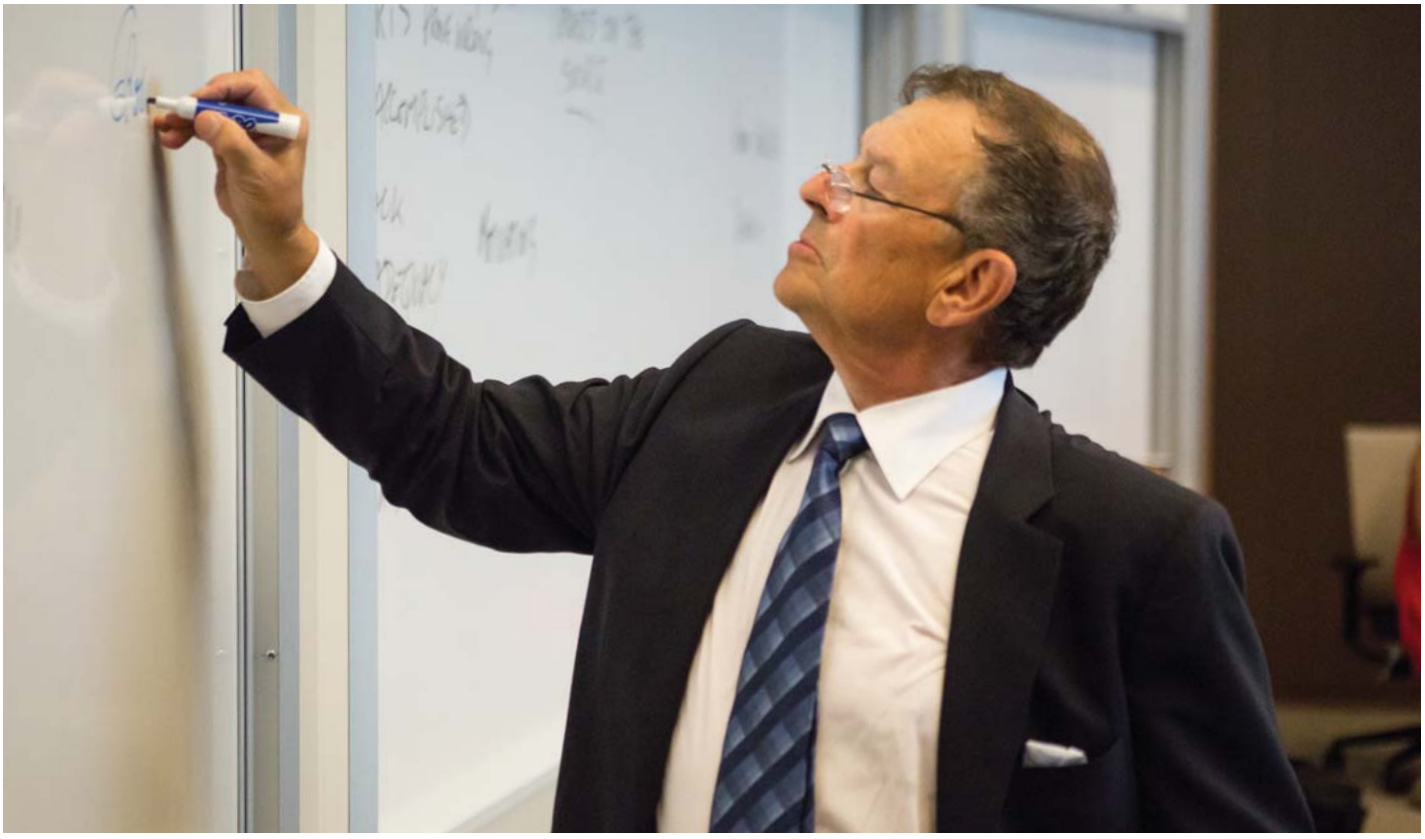


Essential but elusive: "Character is the basis of effective decision making," says Jeffrey Gandz, professor emeritus at Ivey Business School

Test of character

It seems obvious that good directors and top executives be individuals of good character. But is it possible to measure and screen for it when recruiting?

By Ken Mark

It's been six years since the rock-bottom depths of the financial crisis, yet that period remains a constant point of reference when business people, economists, academics and even social commentators assess root causes of failure at companies and in the economy overall. Typically, they focus on such elements as risk, dependence on debt, lax regulation and structural flaws, and consider ways to reduce exposure to them in the future.

For Jeffrey Gandz, however, a professor emeritus in strategic leadership at the Ivey Business School at Western University and a director on the board of Maple Leaf Foods Inc. (TSX:MFI), research into the crash and its aftermath has helped shed light on another element in the successful functioning of companies and boards that is widely recognized but rarely analyzed: the role of individual character in business leadership and governance.

"Leadership character is the least understood and most difficult [attribute] to talk about. Yet it is the basis of effective decision making," says Gandz. "That's because, of all governance tasks, character is key to influencing what information executives seek out and consider, how they interpret it, how they report findings and how they implement board directives."

Gandz began to hone in on this topic after he and other members of an Ivey research team surveyed more than 300 business leaders about the 2008 meltdown and found that many of them identified character weaknesses as a central factor in the overleveraging of the financial system and its subsequent collapse.

The next logical steps for Gandz and his team: to look more closely at what character actually is, why it's hard to talk about, and to examine the extent to which it's possible to screen directors and senior executives during the hiring/selection process for their character attributes in the same way they can be screened for their business acumen, sectoral experience, commitment to hard work, engagement and so on.

Whether or not it can be isolated, there's widespread agreement that character today plays a key role in the makeup of a good company director. When the question is put to Peter Dey, chairman of Paradigm Capital Inc. in Toronto and author of the influential Dey Report in the 1990s, a major catalyst for the advancement of corporate governance in this country, he lists character alongside good

business acumen and the independence of mind to express a point of view that differs from the majority as three essential criteria that make a good corporate director. "When you ask me about character, I think about personal values and I think a director's ability to judge what's right, so the corporation is doing what's right," says Dey.

Historically, character may have played a less significant role in director selection, notes Chris Bart, recently retired professor at the DeGroote School Business at McMaster University and a cofounder and lead faculty member of The Directors College. In the past, "it was all about who you knew and was often based on belonging to the same social circle and wearing the 'old school tie.' But now organizations are worried about 'snakes in suits'—people who have great reputations, talk about personal integrity but don't live up to their reputations.

"Selection committees are developing criteria for evaluating candidates' skills and competencies to protect their organizations from such risks. But trying to define character together with integrity is a brutal monster."

To try to tame that monster, Gandz and his research team have bundled up the relevant, crucial leadership qualities into the three Cs. These include *character*, consisting of personal traits, values, virtues; *competence* related to dealing with people, organizations, business, and strategy and finally, *commitment* involving an individual's aspirations, engagement and sacrifice.

Supporting the three character traits are 11 dimensions (see diagram, below). These are integrity, humility, courage, humanity, drive, accountability, temperance, justice, collaboration, transcendence and judgment. Gandz estimates that a candidate's reputation only reflects three or four of the dimensions.

The last named—judgment—is the centerpiece around which the other 10 dimensions revolve. "It enables executives to adapt to circumstances. It tells you when to speak up or keep quiet, when to 'hold 'em and when to fold 'em," says Gandz.

Although Gandz has gained widespread support for establishing the vocabulary of leadership character in business discussions, his job is far from over. In a recent follow-up survey asking how well corporate selection committees are implementing leadership character criteria in choosing directors, respondents told him that the methodology is viable but organizations are not carrying it out.

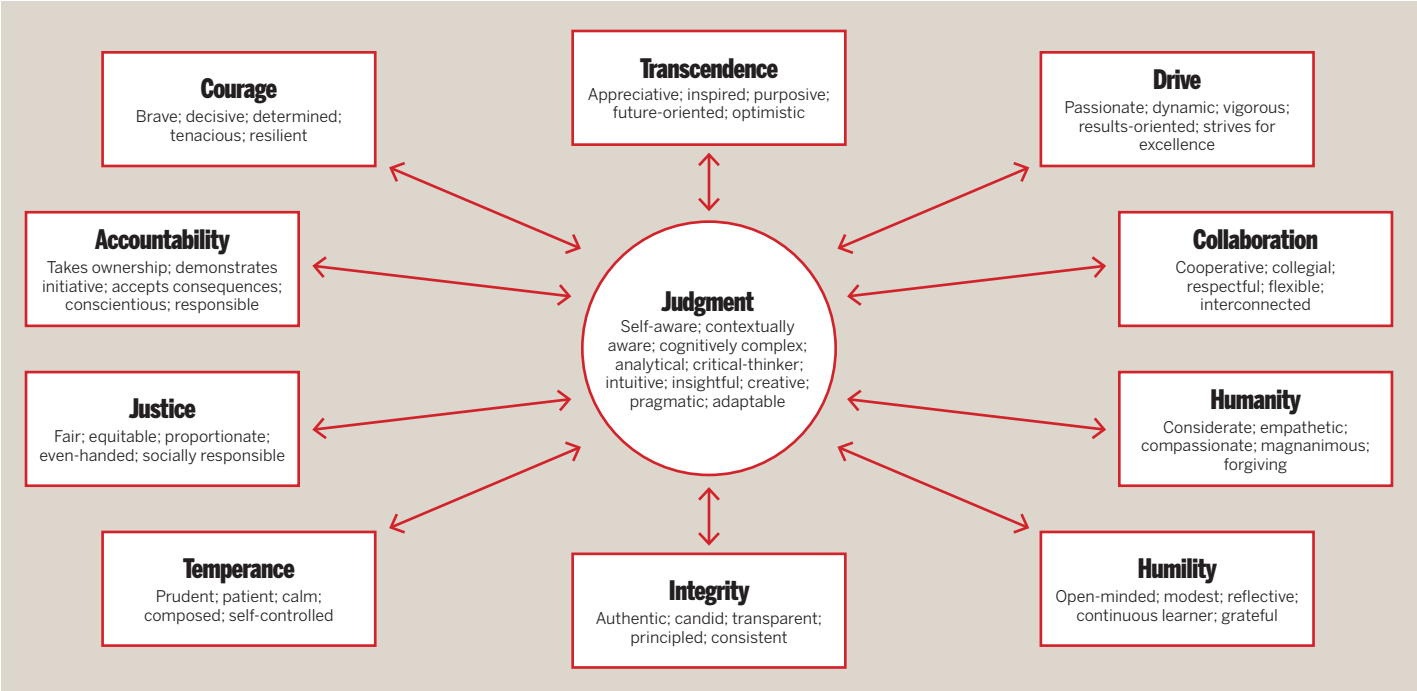
As a result, he and his researchers now face the new task of trying to put into play ways of getting at the character of candidates. "We know what we're looking at," he says. "But in practice it can be difficult to subject high-powered, successful individuals to such close scrutiny."

The ideal approach is to pose well constructed, probing questions about how candidates have behaved in similar situations in the past, or how they believe they would behave in specific situations in the future. But Gandz concedes that he would personally feel awkward asking candidates such questions for each of the 11 dimensions.

As well, as an academic he notes that there is no lack of opinion on how to fill the information gap. However as a new field of study, business leadership character has yet to establish a research base that generates sufficient, reliable data on how to assess and measure the impact of the various character elements in terms of gradation and scale. In other words, there is a lack of Moneyball-type statistics on candidates' past performances that selectors can analyze so they can estimate the range and impact of a candidate's future contributions to a board.

One possible solution Gandz is working on involves developing a character-dimension, self-assessment test. In the same vein, Bart proposes that all prospective candidates for CEO and board membership should be asked to fill out such a character-assessment questionnaire.

In the real world, putting together a board based simply on individuals who scored highest on an 11-point dimension scale or any other such system may not be a winning approach. But in the wake of Gandz's research, the governance community must realize that while competencies matter and commitment is critical, it's character that really counts.



Character mapped: Gandz's 11 dimensions of leadership character, with judgment at the centre

Hallmarks of a great board chair

Excelling as chairman of a public company board is a complicated task—but you'll never lift your game from good to great without embracing three key attributes

By Beverly Behan

Being chairman of the board is an honour. But it's also an important job that can make all the difference in terms of the board's overall effectiveness. Three things distinguish truly great board chairs—and relatively few actually step up to these challenges. Ready to raise your boardroom game as chairman? Here are the steps you need to take:

1. Step up to director performance issues. PwC's 2013 Annual Corporate Directors Survey of over 900 public company directors found that 35% felt someone on their board should be replaced. 35%!! That's a pretty big number. When the PwC survey went on to ask, "What are the impediments to replacing an underperforming director?" the No. 1 answer was, "Board leadership is uncomfortable addressing the issue."

If you're the chair of the board and you've got someone on your board that really isn't making the type of contribution they should, you need to address the problem rather than ignore it. Retirement ages and term limits are the easy way out—and often they extend rather than resolve the situation. Real boardroom leaders understand the importance of stepping up to these awkward issues and have the courage to do so.

A good example is a chairman that I worked with in the northeastern U.S.—a female chair who was also the CEO of a major company. She incorporated robust individual director assessments into her board evaluation every three years and then, most importantly, took action on them. She explained that she was frustrated by her own chair's failure to address director performance issues at the company where she served as CEO; she wasn't going to behave the same way in her chairman's role. Three years later, when the individual director assessments came around again, she expected recriminations. Instead, it was evident that the board's respect for her had grown tremendously. In fact, she had raving fans.

2. Step in to stop micro-management. A board's tendency to "get down in the weeds" rather than stay at a governance level is the bane of many board meetings for CEOs. Yet the solution to this problem should be sitting at the head of the board table—it's the chairman who steps in and reminds the board, "I think we're overstepping into management's turf at this point." It's this type of ongoing board leadership that actually solves micro-management problems. But for this to work, the chair needs to have a solid understanding of the management/governance line in the first place.

I was recently working with a U.S. bank that had this problem. Its frustrated CEO had brought in a lawyer noted for his expertise in governance to speak about this topic at a board dinner. When that had little impact, he created a handout with two columns: Governance on one side, Management on the other. But again, the problem persisted. I asked him, "Shouldn't your chair be playing a role in addressing this issue?" To this, he replied: "Our chair? He's the worst offender!"

3. Step away from the temptation of driving an agenda. Great board chairs are great listeners. They also realize that if they've earned the board's respect, what they have to say carries a lot of weight. Because of this, they hesitate to weigh in too early on critical issues so as to foster a robust debate.

A classic example is a chairman from Chicago who I had the privilege of working with on a CEO succession plan. He had me interview all of his board members on this issue but said, "Leave me out for now. I want to see what they have to say." We discovered that the board was sharply divided on two issues: First, whether an external search was even necessary, and second, if it was, whether it should be limited to candidates from the company's industry or broadened into related sectors.

We discussed these issues at a board dinner—and a spirited debate ensued. Finally the chairman weighed in: "I'm persuaded. We need to look outside but we need to limit it to our sector. Now, if you had asked me about this at the outset, I'd have said that we don't need to waste our time with an outside search given the calibre of our bullpen. And if I'd said that, you probably would have all gone along with me. But I wanted to hear your views on this issue and it's changed my mind." To which one of the board members called out, "And that's what makes you a great chairman!"

Beverly Behan is a New York-based board consultant who has worked with more than 100 boards of directors in the U.S., Canada and internationally in the past 17 years. E-mail: beverly.behan@boardadvisor.net.

Be safe, not sorry

As the RCMP targets offshore bribery, companies should prepare for a knock on their door

EARLIER THIS YEAR, Canadian courts handed down the first prison sentence to someone convicted of conspiracy to bribe a foreign public official under the *Corruption of Foreign Public Officials Act*. Legal experts immediately flagged the decision for their corporate clients operating in international markets. Why?

In 2013, the federal government beefed up the *CFPOA*, chiefly in response to international criticism that Canada wasn't treating Canadian complicity in overseas corruption as a serious issue. In tandem, the Royal Canadian Mounted Police began devoting more resources to corruption investigations. The prison sentence, a three-year term, indicated the courts were in sync with this effort.

While the majority of Canadian companies operate within the law, Maggy Wilkinson, head of the anti-bribery and corruption division at CKR Global, a Toronto-based risk mitigation and investigation services company, says more firms can expect to be investigated as a result of these changes—and that some companies and boards, at least, are getting the message. "There is more willingness to become informed," says Wilkinson. "They want to know what their risks are in the particular jurisdictions where they operate and also what their personal risks are as members of boards."

One common piece of advice is to have a plan in place in the event of an RCMP raid. "It can make a tremendous difference in the course of an investigation," she says. To that end, here are five steps that CKR Global tells companies to follow should the police come calling:

1. Activate the action plan. Personnel should be trained so they understand their rights and know what to do. A policy as simple as having the receptionist tell police to wait in the boardroom or a conference room until the general counsel or chief compliance officer is notified could make a huge difference down the road.

2. Keep detailed notes. Document in detail what transpires during the raid. Make note of what appears to be of interest to law enforcement agents and what documents were taken. Note any attempts to seize privileged information or speak with employees.

3. Preserve documents. Make sure everyone knows not to throw anything away. Do not delete files or e-mails, erase messages or shred documents.

4. Get your communications right. Research suggests that the stock price of a listed company will drop after an investigation becomes public. Swift and clear communication to the press, staff and shareholders is essential.

5. Restore and manage data. As soon as possible, get an experienced data expert to assist you to identify and reconstruct what was taken. This step will be particularly important to prepare and defend against allegations.

Fit and finish: Mexico has moved ahead of Canada in the race for automotive jobs and investment

Canada: the third amigo

Mexico's surging manufacturing sector and growing economy mean its influence in NAFTA will soon supersede our own. But that doesn't have to be a bad thing

By Ian McGugan

Welcome, economics fans, to the 2014 version of Name that Country.

Today's clue: This nation, which shares a border with the United States, has large oil and gas reserves, is headed by a pro-business leader intent on shaking up the country's cozy telecommunications industry, and is enjoying a boom in its auto industry.

Canada, you say? Sorry, the right answer is Mexico.

The country most Canadians tend to ignore except when it's time to book a February vacation is emerging as a surprisingly muscular force in the global economy. It's doing so as Canada finds its own competitiveness under threat.

A recent report from Boston Consulting surveyed the world's top 25 export economies and concluded it is now cheaper to manufacture goods in Mexico than in China—a dramatic shift from a decade ago, when the Asian nation was the undoubted bargain basement of the global economy.

The report showered praise on Mexico and labeled it a rising global star. In sharp contrast, the consulting firm's numbers showed that Canadian factories have slipped badly in terms of cost competitiveness since 2004, and are now far more expensive than those of the U.S. or Mexico.

The shift is most clearly seen in the auto industry, where Mexico has moved ahead of Canada in the race for jobs and investments, according to a report issued last year by the Canadian Automotive Partnership Council. While the United States is still the preferred location among global automakers for North American investment, Mexico sits solidly in second place while Canada has fallen to third.

Mexico's attractions extend well beyond cheap labour. It also enjoys free trade agreements with more than 45 countries and boasts ports on both the Atlantic and Pacific oceans that can operate in all months, without any disruption from ice or snow. The proximity of those ports to the huge U.S. market position give Mexico a big advantage over China or southeast Asia especially for shipping heavy goods such as cars and car parts.

All of that is leading to the realignment of the North American auto industry. A study earlier this year by the Office of Automotive and Vehicle Research at the University of Windsor found that automakers have spent $6.3 billion in Mexico over the past four years to build new plants or expand production at existing plants. By comparison, a mere $180 million was spent to expand production in Canada during the same period.

Photograph: Thomas Trutschel/Getty Images

What may be most remarkable is that Mexico has attracted the flood of new investment while suffering from obvious problems. Drug wars among rival cartels have resulted in horrific scenes of murder and violence. On a less spectacular level, the country struggles with corruption and poverty as well as oppressive oligopolies in many areas of business.

But Mexico is finally addressing some of its issues. President Enrique Pena Nieto, who took office in 2012, has introduced measures to boost competition in the telecommunications sector. He's also passed reforms to the country's miserable education system, an overhaul that has pitted him against the country's famously militant teachers union.

Even more notably, Mr. Pena Nieto has succeeded in opening up parts of Mexico's oil and gas sector to foreign investment after decades in which the industry was off limits to non-Mexicans. In addition, he's breaking the stranglehold of the country's electricity generation and distribution monopoly in a move that has the potential to eventually cut Mexican electricity costs by nearly half. Couple that with moves to increase natural gas imports from Texas, and Mexican industry is likely to see its energy bill tumble over the coming years.

For Canadians, the rise of Mexico is likely to mean a shift of power within the North American Free Trade area. After years of regarding itself as the No. 2 player in the continental partnership, Canada is now likely to see its priorities increasingly superseded by Mexico's.

This continental shift will bruise our egos, but it could eventually carry encouraging news for our companies' bottom lines. With a population three times the size of Canada's, Mexico has the potential to become a huge export market for Canadian goods and services, as well as a steady consumer of Canadian know-how.

Surprisingly, though, Canadian businesses have largely ignored the opportunity. Mexico accounts for only a 3.5% sliver of this country's global trade—but the potential profits are becoming increasingly hard to ignore, especially given the size and relative youthfulness of Mexico's population. By 2030, Mexico will rank as the world's eighth largest economy while Canada will be only 16th, according to a report prepared for the Canadian Council of Chief Executives.

Only a handful of Canadian companies have positioned themselves for that shift. Bank of Nova Scotia entered the country in 1967 and now operates the seventh largest bank in Mexico. Bombardier has been manufacturing subway cars at Mexican factories since 1981 and in 2005 opened a $200-million plant to make aerospace components in Queretaro, north of Mexico City. Linamar of Guelph, Ont., began making auto parts in Mexico in 1998, while Palliser of Winnipeg employs more than 1,000 workers at its Mexican furniture plants.

Their examples demonstrate that Mexican expansion can make sense for Canadian companies despite the country's many problems. Assuming that Mexico can brings its violence under control—a reasonable bet given the resources being poured into the fight—the decade ahead will only add to the country's attraction as Mexico's youthful population enters its prime consumption and working years, while Canada's working force ages.

Rather than bemoaning the competition from this low-wage competitor, Canadian companies should look for ways to cash in on the opportunities that will accompany Mexico's rise. Only if they do so can Canada dominate the 2030 version of Name that Country.

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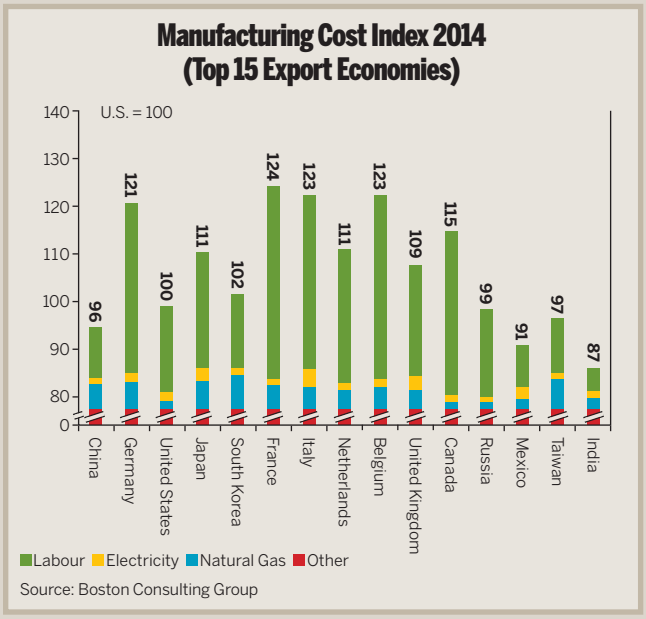
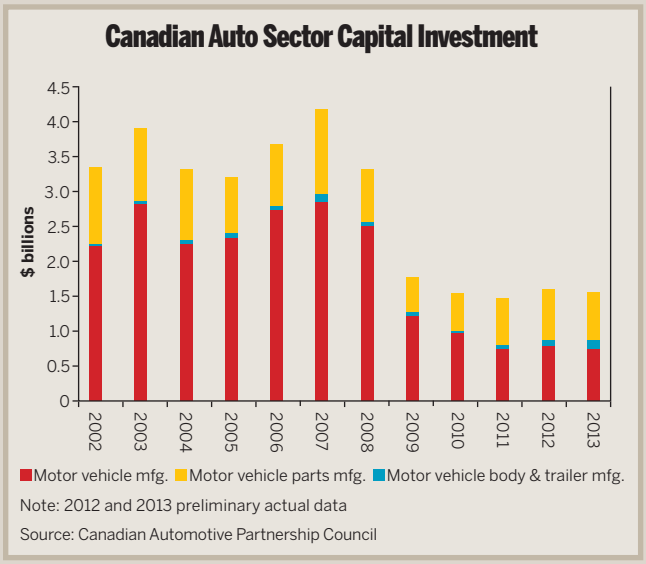
Advantage, Mexico

After making big gains in manufacturing competitiveness, Mexico is reaping the rewards

In the Boston Consulting Group study of the world's top 25 export economies cited in the main column, Mexico ranked No. 1 in terms of its improved manufacturing competitiveness in the past decade. The first chart below, taken from that study, shows the relative standing of the top 15 export economies. Canada, by comparison, is 23 points higher than Mexico, and is losing ground relative to many other economies. One consequence of our widening cost gap with Mexico is reduced investment in Canada's auto sector, as the second chart below reveals. Since 2009, average capital spending has declined more than 50% compared to the seven years prior.





Summit host: World leaders will join Australia's PM Tony Abbott at the G20 in Brisbane

Photograph: POOL New/Reuters

Oct. 29-30 Toronto

Corporate Social Responsibility Summit 2014

This inaugural event features keynotes and panels with leading professionals and practitioners in CSR, sustainability, community relations and volunteerism from across Canada. Key themes include: engaging stakeholder groups to maximize your company's impact on society and corporate reputation; getting the C-suite on board and engaged; using social media to raise awareness, connect and foster positive action. *www.conferenceboard.ca/conf/14-0167/default.aspx*

Oct. 30, 31 Washington, DC; Toronto

U.S. Q3 Gross Domestic Product (advance estimate); Statistics Canada's Gross Domestic Product by Industry/Real GDP (for August)

It's been a whipsaw year thus far for U.S. economic growth. A terrible first quarter was followed by a second quarter that was the best in four years. What will Q3 bring? With the U.S. mid-term Congressional elections taking place a few days later, even this advance estimate may have important political significance. In Canada, at the same time, we'll find out how the economy rounded out the summer. *www.bea.gov; www.stancan.gc.ca*

Nov. 12-14 Toronto

World Water-Tech North America

In Canada, we take water for granted. But as a finite resource under increasing pressure from over-consumption, pollution and climate change, water is forcing its way onto the agenda in social, political, economic and business policy-making and planning—around the world and here at home. This event, featuring key Canadian and international stakeholders and technology partners from every part of the water value chain, brings the issues to the centre of the conversation. For water industry leaders, it's a no-brainer. For all other business leaders, it's time to catch up. *http://watertechtoronto.rethinkevents.com*

Nov. 15-16 Brisbane, Australia

G20 Leaders Summit

The goal for this year's annual meeting of leaders from the world's biggest advanced and emerging economies is to set an agenda for "economic growth and resilience." In the run-up to the main event, there will also be summits for labour leaders, corporate leaders and finance ministers from the G20 countries. *www.g20.org*

Nov. 20 Vancouver

Vancouver Corporate Governance Exchange

A substantial half-day event with panel sessions on four pivotal topics in corporate governance: trends in executive and director compensation; perspectives on shareholder activism; crafting best-in-class proxy statements; leveraging big data. Hosted jointly by the Canadian Society of Corporate Secretaries and the Illawong Group, the sessions are expected to draw an audience of directors, corporate secretaries, general counsel, institutional investors and corporate advisers. *www.cscs.org/VCGEx*

Dec. 3 Toronto

2014 Corporate Reporting Awards

This annual event honours the best in corporate disclosure and reporting practices among TSX-listed issuers and federal and provincial crown corporations. Hosted by the Chartered Professional Accountants of Canada, the awards recognize winners by sector, in four performance categories—financial reporting, corporate governance disclosure, electronic disclosure and sustainable development reporting—and for best in show. *www.cica.ca/about-cica/corporate-reporting-awards/index.aspx*

Dec. 3 New York

Leading Minds of Governance/NACD Directorship 100 Awards Gala

This is a unique, two-part event, hosted by the National Association of Corporate Directors. By day, directors will meet with boardroom experts and governance gurus in an informal idea exchange. Topics on the table include: compensation, talent management and retention, audit, cyber risk, litigation and board dynamics. In the evening, it's the NACD's annual celebration of the year's top directors and most influential members of the North American governance community. *www.nacdonline.org/directorship100/index.cfm*

Dec. 5 Ottawa; Washington, DC

Statistics Canada's Labour Force Survey; Employment and Unemployment (for November); U.S. Employment Situation (for November)

The last jobs reports before the end of 2014 arrive today both here and in the U.S. Canada's unemployment rate has hovered around 7% for the past year; the U.S., in contrast, has seen the jobless rate fall quite a bit this year. Expect as much attention here on part-time job levels and numbers of workers leaving and/or returning to the workforce, as much as the primary employment figures. *www.statcan.gc.ca; www.bls.gov*

Dec. 16-17 Washington, DC

Target Range for the Federal Funds Rate/Federal Open Market Committee meeting

This last meeting of the U.S. Federal Reserve's Open Market Committee for 2014 will be watched closely for indications as to when the Fed's key lending rate might eventually be increased. Also on tap: an important outlook on the U.S. economy for 2015. *www.federalreserve.gov*

A deeper bench

Interview by *Listed* Staff

Who Mark Healy, president and CEO, Canadian Stock Transfer Co. Inc. (CST) and American Stock Transfer & Trust Co. (AST), part of the Australian-based Link Group.

Involvement This spring, AST bought D.F. King & Co. Inc., of New York, one of the most prestigious issuer and shareholder services firm in the world. For Healy, who joined AST in 2009, the deal ups the ante on a string of acquisitions that have helped the company grow from 325 to 1,800 employees while expanding its client base from 2,500 to 4,700 publicly traded companies. CST was founded in 2010 when AST bought the issuer services business of CIBC Mellon.

Listed Why is this purchase important to your company?
Mark Healy The D.F. King transaction was very important for us because it really brings a very long, institutional, deep knowledge base to our firm. We already had a presence within the Canadian markets servicing companies but, the reality here is, you have a very deep bench with D.F. King, you have a very broad diversity in terms of their knowledge base and the kind of relevance that they've had in the markets and their credibility is unparalleled.

Listed We've seen a lot of consolidation among transfer agents, proxy solicitors and other service providers. You've been at the centre of that. What's the thinking behind it?
Mark Healy If you look at the market, the rationale for what's driving this is the continued pressure on issuers as they look out at what's being put at them, not only from potential shareholder or activist situations, but also regulatory environments, the need for technology investment, the need for a more integrated service model. And that's really what we've now put together for these companies. We can service their integrated needs, both from a records administration perspective and all the things that happen from a transfer perspective, but also all of their shareholder needs, and now all the way through to the boardroom.

Listed Is that consolidation largely behind us?
Mark Healy You still have a few disparate areas that may become available at some point in time, but I think for financial services and the areas we service, you've seen most of the dance partners move around. Now it's really about vertical growth, and bringing all these services to your clients.

Listed Is D.F. King well known in Canada?
Mark Healy It's actually very well known globally in the industry. Instant recognition. That's why we really don't want to change that name, even though it's part of AST*One* [the company's integrated services brand], because there's instant recognition, there's instant credibility with that brand and what it brings.

Listed What does this deal mean to the Canadian market?
Mark Healy A couple of things. They've been supportive on a number of transactions in Canada in the past, for other solo providers. We are now clearly bringing them into the Canadian market in a more protracted way, so we're going to actually have feet on the street, folks in Canada, as part of the King team, offering out our services, on a full-time basis now. Of course, D.F. King also has a European business. And those assets will be available as well for Canadian companies as they get involved in any kind of over-the-Atlantic transactions.

Listed Speaking in Toronto this January, you said you had been meeting with a number of companies, looking at possible deals. Was this one of them?
Mark Healy Yes, it was. D.F. King has many product lines; they also have a bankruptcy administration business. And they also have a couple of outsourcing businesses. So kind of pulling all those pieces together, including Europe, took a bit to get through.

Listed Are you currently working on any other deals?
Mark Healy We just acquired a small transfer agent out of Chicago, Illinois Stock Transfer, and we're working on three other transactions that are hopefully culminating in the next few months, in the U.S. and Canada.

Listed Activity in the markets, IPOs, M&A and so on, hasn't yet recovered to pre-crash levels. Do you see it coming back?
Mark Healy In the U.S., there are 40% fewer publicly traded companies than there were six years ago. They've either been acquired, gone bankrupt or privatized. We've yet to see the transcendence of those private companies back into the markets, and not all of them will. But some will come back through other venues, other private types of exchanges. I think in Canada you have similar demographics, albeit you didn't have such a delisting issue, but you had kind of a pause in your capital market issuance and IPOs and I think you're starting to see that pass. So I think over the next year or two you will have a lot of activity in the market and deeper activity.

Photograph: Michael LoBiondo

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- **Dir. of Cybersecurity Critical Infrastructure Protection,** National Security Council
- **Senior Information Technology Policy Advisor,** National Institute of Standards and Technology

To learn more, contact Steve Walker, General Counsel and Director of Board Advisory Services: steve_walker@NACDonline.org or 202-572-2101

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