Say on Pay Votes Come Back in a Big Way:
Three Failed Votes in One Week

Author(s): Andrew MacDougall

Within a week, three failed say on pay votes have put compensation practices back in the spotlight and demonstrably shown that investors still use say on pay advisory votes to voice dissatisfaction with company compensation practices.

In 2014, the level of support on Canadian say on pay votes was increasing and there were no failed votes. That trend clearly reversed last week, with failed votes at Barrick Gold Corporation (73.4% against), Yamana Gold Inc. (62.73% against) and Canadian Imperial Bank of Commerce (56.84% against). This is the second time Barrick has failed its say on pay vote, and it has the dubious distinction of having received both the lowest level of shareholder support on a say on pay vote in Canada (14.8% in 2013) as well as the second lowest level (26.6% in 2015).

Compensation practices continue to be subject to close scrutiny, so employers determining compensation levels and creating disclosure must vigilantly consider a broad range of stakeholder interests and potential reactions.

WHY WERE SHAREHOLDERS UPSET?

The circumstances triggering the say on pay vote results vary.

BARRICK GOLD CORPORATION

Barrick Gold took a number of actions in response to its failed 2013 say on pay vote, including extensive shareholder engagement and appointing six new directors to the board in 2014. In addition, salaries were frozen and bonus amounts were reduced pending the adoption of new practices, including performance scorecards for grading executive compensation, the use of share units with three-year vesting and mandatory share ownership requirements. Although these actions did not satisfy all institution shareholders, they were enough to reverse the vote in 2014, where Barrick received 80.3% approval of its say on pay vote.

The 2015 vote result appears to reflect dissatisfaction with the size of cash incentive compensation paid to Barrick executives, especially the Executive Chairman, in a year where shareholders continued to experience a decline in share price, both in absolute terms and relative to gold indices. Notwithstanding
the use of annual performance incentive scorecards for determining executive compensation, investors continued to perceive compensation decisions as being made largely on a discretionary basis. In addition, while entitlements for most executives were capped at a percentage of base salary and resulted in payouts of up to 286% of base salary, no caps on incentive awards were applied to the Executive Chairman, who received incentive awards totalling 380% of base salary.

**YAMANA GOLD INC.**

Investors criticized Yamana Gold not only for awarding incentive compensation on a largely discretionary basis, but also for not properly disclosing compensation received. Yamana completed a major transaction in 2014, being its joint acquisition with Agnico-Eagle Mines Limited of Osisko Mining Corporation. Certain of the senior executives involved in the acquisition were awarded large cash bonuses and were granted share-based incentive awards tied to the performance of the Osisko assets. These amounts were disclosed as a supplemental bonus and were not included in the summary compensation table in Yamana Gold’s information circular for its 2015 annual meeting of shareholders. Little explanation was given regarding the amount of such awards. Further, investors concluded other short-term incentive amounts were determined largely on a discretionary basis as the company’s proxy disclosure did not disclose a clear link between performance and incentive pay. Investors also criticized the company for “long-term” incentive awards which fully vest in only two years, with one third vesting on grant.

**CANADIAN IMPERIAL BANK OF COMMERCE**

Shareholders were surprised by the generous retirement compensation arrangements granted to the company’s former CEO and COO, when they were disclosed in the proxy circular for the 2015 annual meeting.

The former CEO was a party to an employment agreement with the bank signed on August 1, 2005, amended on November 2009 and renewed on May 2013. Less than one year after the renewal, on April 24, 2014 the bank held its 2014 annual meeting of shareholders and revealed that its CEO intended to retire effective April 30, 2016 – with the actual date to be finalized upon completion of a succession process. Then on July 31, 2014 the bank announced the appointment of its new CEO effective September 15, 2014. The new CEO was the existing Group Head of the bank’s Wealth Management group and, in view of his deep knowledge of the bank and the board of directors’ confidence in his leadership, the board decided to accelerate the retirement of the bank’s former CEO. In addition, the planned retirement of the COO was announced on March 27, 2014, to be effective on October 31, 2015. However, on September 15, 2014, the bank announced that it had reached an arrangement with the COO to accelerate his retirement to that day.

CIBC’s proxy circular for its 2014 annual meeting was dated and filed prior to the announcements on March 27, 2014 and April 24, 2014 of the planned retirements of the former COO and CEO, respectively, and so it reflected their arrangements before they were revised. In reviewing the proxy disclosure for the 2015 annual meeting, shareholders were surprised to discover that the revised arrangements had resulted in the two former executives receiving over $25 million in incremental compensation.

Investors also expressed concerns regarding the bank’s succession-planning process. In 2014, the bank stated that the management resources and compensation committee and board of directors annually review succession plans, including for the CEO. The board concluded at the end of April 2014 that it was desirable to enter into a two-year contract with the former CEO, only to conclude three months later...
that the former CEO’s continued service was no longer necessary.

CONSEQUENCES OF A FAILED SAY ON PAY VOTE

Results are non-binding – In Canada, say on pay votes are provided on a voluntary basis and are advisory and not binding. While every Canadian company that provides a say on pay vote states that its board of directors and compensation committee considers the outcome of the vote as part of its review of executive compensation, the company is under no legal obligation to take any steps in response to the failed vote.

Withhold votes on election of compensation committee chair – A significant number of shareholders of each company also express their dissatisfaction by withholding their votes from the election of certain directors. In Barrick’s case, 25.9% of the votes were withheld on the election of its compensation committee chair. In Yamana Gold’s case, 23.22% of votes were withheld from voting on its compensation committee chair. In the case of CIBC, 14.98% of the votes were withheld from voting on the chair of the management resources and compensation committee, even though she became chair only after the compensation decisions respecting the former CEO and COO had been made.

Implications for future say on pay and director election votes – Although not legally required to take any action in response to the failed say on pay vote, there are several reasons why it would be prudent for a company to consult with its shareholders and consider whether changes to its compensation practices are warranted, including the fact that if proxy advisory firms are dissatisfied with the company’s response as disclosed in the next annual meeting circular, they will recommend withhold votes on the election of directors who are members of the compensation committee. MDC Partners Inc., for example, received less than 70% approval on its say on pay resolution in 2013. Dissatisfied with the company’s response to that vote result, in 2014 proxy advisory firms Institutional Shareholder Services and Glass Lewis not only recommended against MDC Partners’ say on pay vote in 2014, but also recommended that shareholders withhold from voting for directors on the compensation committee. In the case of Barrick, as 2015 was the second time Barrick had failed a say on pay vote, a significant percentage of votes were withheld on the election of each of the members of the compensation committee, ranging from 24% to 25.9%.

Shareholder litigation – Failed say on pay votes in the United States prompted multiple shareholder lawsuits, seeking compensation from executives and boards for breach of fiduciary duties and from executives for unjust enrichment, as well as from the compensation consultants who advised the directors. Most have ultimately proven unsuccessful, although a few have settled, resulting in payment of the plaintiffs’ legal fees. In 2012, Citibank became the first U.S. bank to fail a say on pay vote, with 65% of votes cast against the say on pay resolution. Citibank and its board were promptly sued by multiple shareholder groups seeking damages, alleging, among other things, that the board had breached its fiduciary duties of candor, good faith and loyalty by awarding excessive and unwarranted compensation. Two of the Citibank executives whose compensation sparked the vote result resigned within six months of the vote. The shareholder actions were ultimately unsuccessful as the plaintiffs voluntarily dismissed their action in 2013 and a subsequent action to recover US$6 million in attorney fees was also dismissed. Plaintiffs’ lawyers are likely to be discouraged by the relatively poor success rate of such claims, although the possibility of litigation remains. Two Ontario cases have found that directors breached their fiduciary duty in awarding excessive compensation.¹

Regulatory scrutiny – Compensation practices are also subject to scrutiny by regulators. Criticism of
Yamana Gold’s compensation disclosure could prompt further inquiry from securities regulators. Financial institutions are required by the Office of the Superintendent of Financial Institutions (OSFI) to align their compensation arrangements with the Financial Stability Board’s Principles for Sound Compensation Practices, which seek to align compensation with prudent risk taking. For example, CIBC would need to be ready to respond should it receive an inquiry as to how the arrangements for the former CEO and CFO align with such principles.

CONCLUSION

Executive compensation disclosure these days is subject to close examination by shareholders and regulators, and attracts substantial media interest. Criticism of a company’s pay practices in the media can affect employee morale, customer perceptions and corporate reputation. In today’s environment, disclosure implications must be carefully considered when making compensation decisions, and the rationale for decisions should be disclosed on a transparent basis, especially when making decisions that may be unpopular, to avoid surprising stakeholders.

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1 “‘This can raise outrage’: CIBC’s CEO retirement pay surprises many,” Tim Kaldaze The Globe and Mail, April 1, 2015.

2 The former CEO is entitled to an additional $16,666,646 payable over time in respect of continued salary and bonus from September 15, 2014 to April 30, 2016 plus the increased compensatory value of his pension. The former COO is entitled to an additional $8,527,469 payable over time in respect of continued salary and bonus from September 15, 2014 to October 31, 2015 plus the increased compensatory value of his pension.

CONTACT US

For more information, please visit osler.com or contact the following individual(s):

TORONTO
Andrew MacDougall, Partner,
Corporate
416.862.4732
amacdougall@osler.com

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