BANKING ON CORPORATE

BY NEILL MAY

Do you like say on pay?

I am May. May I am. Do you like say on pay? Do you like greenbacks and spam? There has been much discussion of say on pay recently, most of it focused on elements other than how much the catchy phrase sounds like something invented by Dr. Seuss.

Say on pay is a term used for resolutions, which can be either binding or simply advisory, voted upon by a publicly traded issuer's security holders concerning the compensation of the issuer's senior executives. In the enduring wave of governance reforms, and in the wake of a series of controversies about disproportionate executive pay, regulators in many countries have begun to require non-binding advisory say-on-pay resolutions; others have moved to, or are moving toward, mandatory binding resolutions.

In Canada, while say-on-pay resolutions are not mandatory, a significant number of the larger, publicly traded companies have adopted say on pay, and many governance and shareholder watchdog organizations strongly support it (though in both the large-cap-issuer and watchdog communities there are high-profile dissenters). Canadian say-on-pay resolutions have not generated dramatic results, such as the toppling of senior executives, that have occurred elsewhere. However, the recent rejection of the say-on-pay advisory resolution by the shareholders of Barrick Gold Corp., a rare outcome in Canada, may increase focus on the subject.

Clearly there is more to the inertia behind say on pay than its catchy name, though that doesn't hurt (I am rushing to trademark "rock your stock," "air your share," and "voice your choice" for upcoming governance initiatives). So should Canada require say on pay now, and if so, then how, how, how? Would that work here, to be clear? Is the time to do it now, or near?

The say-on-pay question raises the age-old issue of agency theory in corporations, based on the potential misalignment of interests between the owners and managers of an enterprise. Those supportive of mandatory say on pay argue it imposes a useful discipline on executive compensation, and increases security holder engagement by improving disclosure (by giving issuers an incentive to explain the reasoning behind their compensation decisions) and encouraging dialogue between issuers and security holders. They also point to global trends (in say on pay specifically, and in the governance field generally), and to the number of countries adopting mandatory votes.

Opponents of mandatory say on pay argue it improperly usurps the role of the board, which may be better situated than public security holders (through the board's access to corporate information) to develop a compensation framework that best serves the interests of the issuer. There are many disciplines on board conduct, the argument goes, in an era of widespread governance reforms, growing disclosure requirements, increasing regulatory scrutiny, the daunting threat of legal action, and the acceleration of shareholder activism. Restricting the board's flexibility to act (and where say-on-pay resolutions are binding, taking the matter right out of the board's hands), raises questions as to where security holder oversight of corporate decisions should end, and whether security holders are better positioned than boards to make these decisions. (I guess I should reserve rights to "the board ignored" while I'm at it.)

There are other concerns about mandatory say on pay. For one, it is a one-size-fits-all approach that may not be appropriate for issuers of different sizes and in different circumstances (for example, Power Corp. has questioned whether mandatory shareholder votes on executive compensation are appropriate for companies, such as itself, which have a controlling shareholder that has an ongoing relationship with the issuer and is able to express its perspectives on executive compensation other than at the annual shareholder meeting). Another issue is say-on-pay resolutions can yield ambiguous results; a negative vote does not make clear what element(s) of the compensation framework are considered unfavourable, and for what reason. Where shareholders communicate publicly about the elements of executive compensation that they dislike, as some shareholders did with Barrick, there is no ambiguity, but shareholders do not need mandatory say on pay to communicate disapproval, and even in the case of Barrick the directors were all voted back into office so the message was mixed.

Finally, there is the "if it ain't broke" argument. In a regulatory framework with reasonably robust governance, disclosure requirements, and security holder protections, issuers can choose to adopt say on pay or, if they choose not to, defend that approach.

It may be there is less pressure to impose a mandatory requirement in Canada because we did not experience the financial convulsions of the past few years to the same degree as other economies, or witness executives receiving super-size pay packages in publicly bailed-out firms. Even still, the debate can be expected to continue. With further profound apologies to Dr. Seuss, from there to here, and here to there, governance related issues are everywhere. CL

Neill May is a partner at Goodmans LLP in Toronto. His practice focuses on all aspects of securities law, with an emphasis on M&A and corporate finance. E-mail him at nmay@goodmans.ca. *The opinions expressed in this article are his own.*