

new director election requirements for TSX companies

Earlier this month, the Toronto Stock Exchange adopted new rules relating to the election of directors and at the same time, proposed for public comment a rule requiring companies to adopt majority voting for the election of directors.

the new TSX rules

Effective December 31, 2012, companies listed on the TSX will be required to:

- elect directors individually (as opposed to by 'slate');
- hold annual elections for all directors (as opposed to overlapping, multi-year/staggered terms);
- disclose annually in the company's management information circular whether the company has adopted a majority voting policy for uncontested director elections and, if not, explain its election practices and its reasons for not adopting such a policy; and
- after each meeting at which directors have been elected:
 - (i) notify the TSX if a director has received a majority of 'withhold' votes
(if the company has not adopted a majority voting policy); and

(ii) promptly issue a press release disclosing the voting results.

individual vs slate director elections

While the prevalence of slate elections (electing directors of a company as a group or 'slate') has declined significantly over time in favour of individual director elections, neither securities nor corporate law in Canada requires individual director voting. Individual director elections are now mandated for TSX companies allowing shareholders to cast votes on director nominees on an individual basis, thereby providing shareholders with the opportunity to express disapproval regarding an individual director by withholding support for such director.

annual director elections

Although both the *Canada Business Corporations Act* and the *Business Corporations Act* (Ontario) permit director terms of up to three years¹ and staggered terms,² the TSX has mandated that its listed companies hold annual elections for all members of the company's board of directors. Annual elections are seen as being an essential part of best practices corporate governance, permitting shareholders the opportunity to evaluate the performance of board members on an annual basis. Most companies in Canada already hold annual director elections, so this provision should impact a relatively small number of companies.

majority voting

In Canada, corporate statutes currently provide for the election of directors by plurality voting. In a plurality voting scheme, shareholders are given the choice to vote either 'for' a nominee director, or to 'withhold' their vote for such nominee. In

¹ *Canada Business Corporations Act*, RSC 1985, c C-44, s 106(3) [CBCA]; *Business Corporations Act* (Ontario), RSO 1990, c B.16, s 119(4) [OBCA].

² CBCA, s 106(4); OBCA, s 119(5).

uncontested elections, a plurality voting scheme allows an individual to be elected with less than a majority of the votes cast in favour of his or her election, regardless of the number of votes 'withheld' from the individual's election. In contrast, for companies that have adopted a typical majority voting policy, any nominee for director who receives a greater number of votes 'withheld' from than 'for' his or her election, would be required to tender his or her resignation as a director. The remaining board members would, absent unusual circumstances, generally accept such resignation.

It is important to note that, at this time, the TSX has not mandated that companies adopt a majority voting policy, instead it has chosen to implement a 'disclosure and explain' model, concluding that a company's adoption or non-adoption of a majority voting policy is valuable information for shareholders which will ensure that boards of directors consider director election practices. However, as discussed under "The Proposed Majority Voting Rule" below, concurrent with its announcement of the new rules, the TSX has proposed a further new rule which, if adopted, will *require* its listed companies to adopt a majority voting policy.

effective date

The new rules take effect on December 31, 2012 and are not retroactive, so shareholder meetings that have already been set and for which proxy materials have received approval are unaffected by the new rules until their next shareholder meeting at which directors will be elected. By December 31, 2013, all TSX listed companies are expected to be in compliance with the new rules, however, the TSX has made provision for companies that must amend their articles or by-laws to accommodate the new requirements.

the proposed majority voting rule

As referenced above, concurrent with the adoption of the new rules, the TSX has published a proposed rule for public comment that would *require* its listed companies to have majority voting for directors at uncontested meetings. The proposed rule would allow a company to discharge its obligation to have majority voting by adopting a majority voting *policy* rather than a majority voting standard. A majority voting standard could result in too few directors being elected to achieve quorum or committee requirements. With a majority voting policy, directors that do not receive sufficient support are still elected, however, they would be required to resign at a later time, giving the board time to reconstitute and reorganize the board if necessary without being offside any laws or creating governance issues.

The TSX has stated that the 'disclose and explain' approach to majority voting it took in drafting the new rules was its view of Canada's current level of education and awareness on the issue. However, upon receiving numerous comments supportive of mandatory majority voting, the TSX has reconsidered its position and published the proposed rule for comment. The TSX also noted that according to the Canadian Coalition for Good Governance, 61% of S&P/TSX Composite Index listed companies already have majority voting. The comment period on the proposed rule expires on November 5, 2012.

conclusion

The TSX believes Canada's director election practices are lagging other major international jurisdictions. Both the new rules and the proposed rule are aimed toward enhancing Canada's reputation for stronger governance standards, and bringing Canada closer to the practices of other major jurisdictions. One would expect that the above rules are but the latest (and not the last) initiatives of securities regulatory authorities in this environment of increasing shareholder rights and empowerment.

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a cautionary note

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