Governance issues front and centre as 2018 proxy season gears up

Diversity, pay are givens, but "over-boarding" may be newest discussion on the table next year

Barry Critchley, Financial Post, October 27, 2017

The 2018 proxy season is months away but issuers can expect no let up on a host of governance matters that concern institutional investors.

That's the view of Dexter John, executive vice-president of D.F. King Canada, an AST Company. This week the proxy solicitation firm, which released its 2017 post proxy season review.

"For next year there will be more focus on say on pay, a lot more scrutiny from the large institutions in ensuring that pay for performance is aligned across the board," said John, whose report noted that TransAlta Corp. and Eldorado Gold failed to receive at least 50 per cent say on pay approval in 2017.

The report indicated that five other issuers (Valeant Pharmaceuticals, Iamgold, Encana Corp., Alacer Gold and Aralez Pharmaceuticals) all received less than 70 per cent support for non-binding proposals.

Those seven issuers received significantly less support than the 91 per cent average garnered by issuers in the S&P/TSX 60 index. That average occurred even though for 2017, ISS and Glass Lewis, two proxy advisory firms, recommended against a small number of say-on-pay proposals for TSX60 companies.

But D.F. King believes current levels of support for say-on-pay "will continue to decrease as more stringent criteria are put forward by institutional holders," a trend that may be mitigated by "more frequent shareholder engagement practices."

John also expects diversity will be another theme for 2018, in part because many large institutions have modified their guidelines allowing them to vote against directors if "certain actions in respect to diversity" haven't been taken. That heightened focus is not good news for members of the issuer's governance committee.

D.F King's report shows there has been some improvement. For instance, women directors now represent 25 per cent of total directors (the banks were the outliers with a 35 per cent average).

As well, while the average board size has shrunk (to 12.2 directors from 12.5) the number of women per board has increased to 3.1 from 2.2.

One matter, currently brewing beneath the surface, may become a bigger theme in 2018, John believes. That matter relates to an ISS proposal concerning over-boarding (when a director is on more than four public boards) and attendance (at least 75 per cent threshold is required). Currently if an over-boarded director misses more than one quarter of the meetings, a withhold vote is recommended.

“There’s some talk the attendance component will be dismissed. But it’s very early talk,” noted John, who doesn’t support the planned change. “Over-boarding should be viewed on a case-by-case basis, as not all boards are created equally,” he said. “The 75 per cent criteria should not be removed as it is an indicator if a director has the time or not.”

John mused about the one-size-fits-all approach taken by ISS and Glass Lewis, the firms whose recommendations are considered important for institutional shareholders. John said the approach taken by those two proxy advisory firms often disregards the situations faced by smaller issuers. “It needs to be recognized that each industry needs to be looked at differently in terms of retaining talent, and ultimately there should be some alignment,” he said. ‘They should be more flexible.”

This week, the pressure on issuers was notched up when more than 40 institutional investors, mostly from Quebec, demanded that Canadian issuers “commit to disclose more information on their exposure to climate change risks and the measures they adopt to manage these risks.” In a release, Finance Montreal, the body that coordinated the demand, said the information is essential to allow investors to “better assess the non-financial risks to which investment portfolios are exposed.”