

March 29, 2021

Corporations Canada
Innovation, Science, and Economic Development Canada
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Via email: ic.corporationscanada.ic@canada.ca

To whom it may concern;

We are writing to comment on the development of regulations related to amendments to the *Canada Business Corporations Act (CBCA)* enacted under Bill C-97 *An Act to implement certain provisions of the budget tabled in Parliament on March 19, 2019 and other measures*, concerning executive compensation and the well-being of employees, retirees and pensioners.

The Investors for Opioid and Pharmaceutical Accountability (IOPA) is a diverse coalition of global institutional investors with **67 members representing over \$4.2 trillion in assets under management**, including members in Canada. More about the IOPA is available [here](#).

We offer the following comments in response to the specific questions that ISED has raised regarding clawback policies and related disclosures. While the other questions raised in the current consultation are of interest to institutional investors, our coalition has specific expertise in the area of misconduct clawback policies including disclosure of the use or non-use of the clawback policy, and disclosure of adjustments to compensation metrics to remove legal costs. In recent years we have fostered the adoption of misconduct clawback policies at 18 companies and worked with fifteen major pharmaceutical industry companies to develop an agreed set of principles for bonus deferrals. Examples of these policies can be seen [here](#).

Issue D: prescribing the information that needs to be disclosed to shareholders about the recovery of incentive and other benefits.

We support the inclusion of the required information on the presence and substance of a clawback policy at the company's annual meeting (and, in the case of distributing corporations, this material should be disclosed in the company's Management Information Circular/proxy circular well in advance of the annual meeting). A clawback policy should a) recover incentive

compensation in the event of a violation of a company policy relating to non-compliance with a law or regulation that causes significant financial or reputational harm to a company, including supervisory failures, and b) require disclosure to shareholders in the proxy statement about such recoveries without violating privacy laws.

We therefore suggest the following amendments to the proposed disclosures:

- 1. The disclosures should clarify whether the clawback policy applies solely to conduct that results in material financial restatements, or includes other misconduct (e.g. related to violations of the Company's Code of Conduct or other policy governing employee conduct which results in significant reputational or financial harm related to non-compliance), or to other legal or regulatory liability.*

The scope of action should be determined by each board's policy but identifying this as a criterion for disclosure may help to guide boards in developing a policy that is sufficiently broad so as to capture misconduct that, while not necessarily resulting in restatements, is seriously damaging to the company and its shareholders.

- 2. The required disclosures should include a) whether legal and/or compliance costs are explicitly excluded from financial performance metrics used in the corporation's compensation framework, and if they are excluded, why such exclusion is warranted, and b) a breakdown of the legal and compliance costs, including any settlements made.*

Non-GAAP performance metrics like "Adjusted Earnings Per Share" are being used more and more frequently by corporations to re-define financial performance in a manner that is more beneficial to executives than standard accounting metrics might be. While the current consultation does not address this issue specifically, it is worth addressing the question of legal compliance and accountability in the context of a clawback policy specifically. Compensation metrics communicate behavioral expectations to employees and adjusting metrics for items that are related to the company's core business can suggest a lack of accountability. Even worse, insulating executives from accountability for fines and legal settlements that resulted from their decisions works in direct opposition to the purpose of a clawback policy, which is meant to ensure accountability for one's actions.

Although boards remain responsible for the choice of metrics used to define performance and may choose to exclude some items from performance metrics for specific reasons, the board should be required to explain to shareholders why fines and legal costs are being excluded in each instance.

3. *The required disclosures should also include information about incentive deferral policies, if any, their scope and application.*

Bonus deferrals allow accurate assessment of risks taken during a particular performance measurement period that could have affected performance on the financial metric(s) employed to calculate bonuses, and implementation of appropriate bonus deferrals allows a company to recoup incentive-based pay pursuant to its clawback policy. In this sense bonus deferral policies are a natural complement to an effective clawback policy, simplifying the process of retrieving pay that should not, ultimately, have been awarded. It is particularly useful in the context of insolvencies that may affect employees' retirement savings, as recouping pay that has already been awarded is very difficult after the fact and usually requires litigation (thus reducing the amount available to pay retirees).

Bonus deferral is widely used in the banking industry, where overly risky behavior generating short-term profits, but longer-term losses was widely viewed as contributing to the financial crisis. In 2009, the Financial Stability Board, which coordinates national financial authorities in developing strong financial sector policies, adopted *Principles for Sound Compensation Practices* and implementation standards for those principles, including bonus deferral. Deferral is “particularly important” because it allows “late-arriving information about risk-taking and outcomes” to alter payouts and reduces the need to claw back compensation already paid out, which may “fac[e] legal barriers,” in the event of misconduct. Banking supervisors in 16 jurisdictions, including Canada, have requirements or expectations regarding bonus deferral.¹

Deferral policies were also the subject of a recent working group of institutional investors and fifteen major pharmaceutical industry companies which developed a set of principles for bonus deferrals. After the *Incentive Principles* were developed, compensation committees of three companies, Bristol Myers Squibb, CVS Health, and Walgreens, voluntarily took steps to align their plans with the intent of the Principles, and others are in the process of doing so. [Incentive Deferral | ICCR \(Interfaith Center on Corporate Responsibility\)](#)

4. *ISED has proposed that corporations be required to disclose information on recoveries made, if any, in the previous fiscal year. This should be amended to include information on the reasons for said recoveries (consistent with the clawback policy) and the amount of the recovery made. While information may be given on the amount recouped or the number of incidents in the aggregate to avoid privacy violations, reasons linking back to*

¹ <https://www.fsb.org/wp-content/uploads/P170619-1.pdf>

violations of a company's code of conduct or regulatory or legal rules would benefit investors.

We welcome ISED's consultation on these measures and look forward to embedding accountability measures in CBCA regulations to improve outcomes for workers, retirees and pensioners, as well as shareholders.

If you would like to discuss any of these proposals in more detail, please contact the co-chair of the IOPA; Donna Meyer (dmeyer@mercyinvestments.org).

Sincerely,



Donna Meyer, Ph.D.
Director of Shareholder Advocacy
Mercy Investment Services, Inc