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AMENDMENTS TO EXECUTIVE COMPENSATION DISCLOSURE RULES FOR 2012 PROXY SEASON

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On July 22, 2011, the Canadian Securities Administrators (CSA) published amendments to the executive compensation disclosure rules, which will come into force on October 31, 2011. The principal amendments will be made to Form 51-102F6 — *Statement of Executive Compensation,* and consequential amendments will be made to National Instrument 51-102 — *Continuous Disclosure Obligations*, Form 58-101F1 — *Corporate Governance Disclosure,* and Form 58-101F2 — *Corporate Governance Disclosure (Venture Issuers)* (collectively, the "Amendments").

The Amendments are designed to provide investors with enhanced information about key risks, governance, and compensation matters, and take into account executive compensation disclosure developments in the U.S. and other foreign jurisdictions, as adapted for the Canadian marketplace. They follow a CSA staff review of executive compensation disclosure and public comments received on draft amendments published last year. In addition to introducing new disclosure requirements, the Amendments clarify certain existing requirements.

Issuers must comply with such rules for financial years beginning on or after October 31, 2011. Hence, they will want to familiarize themselves with the new disclosure requirements now to ensure they comply with them next proxy season.

New Compensation Discussion and Analysis (CD&A) Disclosure

The Amendments include the following new disclosure requirements, which must be part of an issuer's CD&A:

- *Serious Prejudice Exemption.* An issuer must explicitly disclose when it is relying on the serious prejudice exemption and explain why disclosing the relevant performance goal or similar condition would seriously prejudice its interests. The CSA is of the view that even if the disclosure of a target level itself may seriously prejudice the issuer's interests in a particular case, disclosure of the metric itself would typically not.

- *Risk Management and Compensation*. To address the concern that compensation practices and policies may result in executives taking greater risks than appropriate, the CSA has introduced enhanced disclosure requirements regarding employee compensation policies and practices that create risks reasonably likely to have a material adverse effect on the issuer. An issuer must disclose that the board (or a committee established by the board) considered the risk implications of its compensation practices. The issuer must then disclose (i) the nature and extent of the board's (or a committee of the board's) role in the risk oversight of compensation policies and practices and (ii) any practices used to identify and mitigate compensation policies and practices that could encourage a named executive officer or individual at a principal business unit or division to take inappropriate or excessive risks. The Amendments also provide commentary to clarify that if an issuer used any benchmarking in determining compensation or any element of compensation, the issuer should include the benchmark and describe why the benchmark group and selection criteria are considered relevant by the issuer.

The Amendments contain examples of situations that could encourage an executive officer to expose an issuer to inappropriate or excessive risk. Examples of compensation practices and policies the CSA cites as potentially encouraging officers to take inappropriate risks include arrangements at a principal business unit or for certain executive officers that differ from the rest of the compensation arrangements within the issuer, policies where the compensation paid to executive officers is a significant percentage of the issuer's revenues, performance goal, or conditional compensation arrangements that are heavily weighted to short-term objectives, and incentive plan awards that do not provide a maximum benefit or payout limit to executive officers. These examples are not exhaustive and the situations which may be of concern vary depending upon the nature of the issuer's business and its compensation policies and practices.

- *Hedging by Named Executive Officers and Directors*. The CSA requires the issuer to disclose if any named executive officer or director is permitted to purchase financial instruments whose purpose is to hedge the risk of a decrease in value of any equity securities held by him or her.

- *Compensation Committee and Governance*. Issuers should describe any policies and practices adopted by the board of directors to determine the compensation for the issuer's directors and executive officers. If an issuer has established a compensation committee, such issuer should describe the relevant experience of the committee members and the skills and responsibilities of the committee. The Amendments provide that issuers should also disclose the names of each compensation committee member and whether each member is independent or not. National Policy 58-201 — *Corporate Governance Guidelines,* currently provides nonmandatory guidance on governance practices and recommends a fully independent compensation committee.

- *Disclosure of Fees Paid to Compensation Advisers*. An issuer must disclose which compensation advisers (other than legal, accounting, and tax advisers) have been retained by the issuer and describe their mandates and any other work they have performed for the issuer (including a breakdown of all fees paid to the compensation adviser for each service provided). The Amendments require the description of any other nonexecutive compensation services provided by the compensation adviser to not only the issuer, but also to its affiliated or subsidiary entities or to any of its directors or members of management. Finally, disclosure is required as to whether the board or the compensation committee must preapprove such services.

Currencies

- *Currencies*. Generally, amounts required by the forms and tables must be in Canadian dollars or the currency used in the issuer's financial statements. The Amendments provide some flexibility if the issuer's performance goals and similar conditions disclosed in the CD&A are in a currency different from the currency presented in the prescribed tables, which may be for the purposes of consistency with financial reporting obligations. In addition, the Amendments specifically provide that for the share-based awards and the option-based awards table, if the option was granted in a different currency than that reported in the table, issuers should include a footnote specifying the currency and the exercise or base price.

Summary Compensation Table

- *Format of the Summary Compensation Table (SCT)*. Issuers must make disclosure in accordance with the form and must not alter the presentation of the SCT by adding columns or other information. However, the CSA reiterates that issuers are allowed to provide additional tables and information, as a supplement to the SCT, if necessary to achieve the objective of executive compensation disclosure.

- *Reconciliation of Grant Date Fair Value and Accounting Fair Value for Share-based and Option-based Awards*. Issuers must disclose the fair value of the award on the grant date for share-based awards and option-based awards in the appropriate columns of the SCT. The fair value of the award on the grant date for these types of awards must be reported in the SCT in the year of grant irrespective of whether part or all of the award relates to multiple financial years, and payout is subject to performance goals and similar conditions, including vesting, to be applied in future financial years.

Pension Plans

- *Defined Benefit Plans Table*. The Amendments include a new requirement to the effect that, for purposes of calculating the annual lifetime benefit payable at the end of the most recently completed financial year, issuers must assume that the NEO is eligible to receive payments or benefits at year end. The CSA also clarified that issuers may calculate the annual lifetime benefit payable in accordance with a formula included as commentary or in accordance with another formula if the issuer reasonably believes that the other formula produces a more meaningful calculation of the annual lifetime benefit payable at year end.

- *Defined Contribution Plans Table*. The amendments proposed in 2010 requested public comment on a requirement to disclose the noncompensatory amount for defined contribution plans, including employee contributions and regular investment earnings on employer and employee contributions. In response to public comment, this proposal has not been included in the Amendments.

LEGISLATION UPDATE

Federal

The *National Security Review of Investments Regulations,* SOR/2009-271, effective September 17, 2009, were added.

The *Corruption of Foreign Public Officials Act,* S.C. 1998, c. 34, was added.

The *Canada Not-for-profit Corporations Act,* S.C. 2009, c. 23, was added.

Bill C-10, the *Safe Streets and Communities Act,* received first reading September 20, 2011. Bill C-10 proposes amendments to the *Criminal Code*.

These changes have been incorporated into the *Canada Corporations Law Reporter*.

Alberta

The *Rules of Court Statutes Amendment Act,* 2011, S.A. 2011, c. 14, received first reading February 23, 2011, second reading April 12, 2011, third reading May 9, 2011, Royal Assent May 13, 2011, and is proclaimed to be in force October 1, 2011. This Act amends the *Cooperatives Act,* the *Engineering, Geological and Geophysical Professions Act,* the *Legal Professions Act,* and the *Partnership Act*.

RECENT CASES

Derivative Action

Court of Queen's Bench of Alberta, August 12, 2011

The plaintiffs, Raymond C.S. Liu ("Liu") and 1199918 Alberta Ltd. ("1199918"), which was Liu's holding company, owned 25% of the shares of TRL Holdings Inc. ("TRL"). The defendants were the majority shareholders of TRL, Terry Regenwetter ("Regenwetter") and his holding company, 1199935 Alberta Ltd. ("1199935"). A third company, Right Time Investments Inc. ("Right Time"), was also owned and controlled by Regenwetter.

Liu and Regenwetter formed TRL to invest in real estate. Although the parties had entered into a unanimous shareholders' agreement entitling Liu to be a director, Regenwetter was the sole director of TRL. TRL became a shareholder in a number of real estate projects and the accounting on those projects was carried out by Liu's professional corporation. However, in 2008, the professional corporation was fired and Liu alleged that outstanding invoices remained unpaid. Liu also alleged that all of TRL's trade creditors had been paid in full. Liu also alleged that TRL had earned significant profits on its real estate ventures, but that more than $2 million had been diverted from TRL to Regenwetter or entities related to him. Liu and 1199918 sought leave to bring a derivative action on behalf of TRL against Regenwetter and his companies, and sought an order providing that the costs of the action should be funded by the shareholders of TRL in proportion to their respective shareholdings.

The application for leave to bring a derivative action was allowed. The application with respect to the funding of the derivative action was denied. The Court first reviewed the statutory preconditions for the granting of leave to bring a derivative action: the applicant is required to give reasonable notice to the directors of his intention to make the application and is required to act in good faith. In addition, the Court must be satisfied that it is in the best interests of the corporation to bring the action.

It was clear to the Court that the applicants, as minority shareholders of the company, had standing to bring the application. The Court held that the applicants had given reasonable notice to TRL, Regenwetter, and 1199935, and that notice to any other party was not required. The Court then considered whether the applicant was acting in good faith in seeking to bring the derivative action and held that Liu's acting in his own interests was compatible with acting in good faith. The Court further held that, while there were other actions pending between the parties, a derivative action was the only way that Liu, as a shareholder, could obtain an effective remedy against the director of the corporation as none of the other actions would resolve the issues that Liu sought to put forward in the proposed derivative action. The Court then reviewed the allegations made by Liu and concluded that some of them had a reasonable prospect of success and that, to the extent that Liu's interests were to ensure that revenues and assets of the corporation not be improperly diverted to others, an action to recover such assets would be in the best interests of the corporation. The Court concluded that Liu had met all the criteria for obtaining leave to bring a derivative action, and the application was allowed.

The Court then considered whether the derivative action should be funded by the shareholders of TRL as requested by Liu, and concluded that it should not. In the Court's view, Liu's request was akin to an application requiring Regenwetter to pay advance costs to him, and Liu had not met the requirements for advance costs. The Court also held that requiring shareholders to personally fund litigation on behalf of the corporation was contrary to basic principles of corporate jurisprudence and represented an extraordinary remedy that was not justified under the circumstances of the case.

1199918 Alberta Ltd. v. TRL Holdings Inc., 2011 ACLG ¶79,411
2011 BCLG ¶78,835
2011 CCLR ¶200,992
2011 CCSG ¶51,272
2011 OCLG ¶51,648

Piercing the Corporate Veil

Supreme Court of British Columbia, August 8, 2011

A lease containing a "radius clause" was entered into in respect of a property in Vancouver. Under the terms of the radius clause, the tenant agreed not to operate a business similar to that carried on at the leased premises within a specified radius of that location. Upon breach of the clause, the tenant was required to include in the tenant's gross revenue the gross revenue from the competing business, for purposes of calculating the percentage rent payable to the landlord.

The original tenant of the property was Cineplex Odeon Canada ("COC"). COC assigned its lease to one of the defendants, Cineplex (Western Canada) Inc. ("Cineplex Western"), a wholly owned single purpose company. COC, which had entered into proceedings under the *Companies' Creditors Arrangement Act* and therefore had no continuing liability under the lease, subsequently sold its assets (including the sole share in Cineplex Western) to the other defendant, Cineplex Entertainment Limited Partnership ("CELP"). CELP later acquired ownership of a theatre that was located within the radius specified within the radius clause of the original lease agreement.

The plaintiff, Emtwo Properties Inc. ("Emtwo"), brought an action that sought to require Cineplex Western, as tenant, to include revenue from the competing theatre business in its gross revenue for the purpose of calculating rent payable. It also sought to hold CELP liable for any rent payable on the basis that Cineplex Western, if liable, was the mere alter ego of CELP (that is, the control by the parent was so profound that the subsidiary had no separate independent functioning) and that it was therefore appropriate to pierce the corporate veil and hold CELP liable.

The action was dismissed. There were two issues for determination by the Court. The first was the proper interpretation of the radius clause in the lease to determine whether Cineplex Western was required to include revenue from the competing theatre business in its gross revenue for the purpose of calculating rent payable. The second was whether CELP could be held liable for any rent amounts payable on the basis that Cineplex Western was a mere alter ego of CELP.

The Court first reviewed the history of dealings between the parties and the terms of the lease agreement, as well as whether Cineplex Western was liable under the radius clause by reason of CELP's operation of a competing business. The Court concluded proper interpretation of the provision provided that, for the radius clause to be triggered, the tenant would need to control the entity operating the competing theatre. In this case, Cineplex Western did not control CELP, but the reverse. Therefore, the operation of the competing theatre by CELP did not trigger liability under the radius clause.

The Court then considered whether CELP should be found responsible for Cineplex Western's liability, if Cineplex Western was found liable under the radius clause. The Court reviewed British Columbia, Ontario, and English jurisprudence on the subject of when a parent company could be held liable for the contractual obligations of a subsidiary under the alter ego doctrine. It held that B.C. appellate jurisprudence supported the proposition that the separate existence of parent and subsidiary corporations must be respected. The parent does not acquire the subsidiary's liability simply through its profound control of the subsidiary. The circumstances in which the corporate veil will be pierced to impose such liability require conduct akin to fraud; mere unfairness will not suffice. There was no suggestion of any wrongdoing or fraud in this case.

The Court noted that, whatever the scope of the alter ego doctrine, it did not apply in this case. Notwithstanding the fact of profound control by CELP of Cineplex Western, the two companies were separate legal entities and any contractual obligation was that of Cineplex Western alone.

Emtwo Properties Inc. v. Cineplex (Western Canada) Inc., 2011 ACLG ¶79,412
2011 BCLG ¶78,836
2011 CCLR ¶200,993
2011 CCSG ¶51,273
2011 OCLG ¶51,649

Dissolution

Ontario Superior Court of Justice, August 17, 2011

The plaintiff company carried on an auction business. In November 2002, a significant amount of inventory disappeared from the business premises. The defendant insurer refused coverage of the $700,000 loss on the basis that the alleged theft of the inventory had been staged. The plaintiff company brought an action to compel coverage of the loss; however, when that action came up for trial in fall of 2010, it was determined that the plaintiff company had, in fact, been dissolved by the Ministry of Consumer and Business Services in January 2008 as a result of the company's failure to pay the required $50 annual fee. The plaintiff company was then revived and the plaintiff brought a motion for an order to grant it leave to maintain the action.

The motion was granted and leave given to maintain the action. The Court reviewed the requirements of section 18 of the *Corporations Information Act* pursuant to which a corporation that is in default of a requirement to file a return or that has unpaid fees or penalties is not capable of maintaining a proceeding in a court in Ontario, except by leave of the court. Such leave shall be granted by the court where it is satisfied that the failure to file the return or pay the fees or penalties was inadvertent, that there was no evidence that the public had been misled, and that, at the time the application for leave was made, the corporation was in full compliance with all of its filing and payment obligations. However, the Court also noted that section 242 of the *Business Corporations Act* provides that, despite the dissolution of a corporation under that Act, an action or proceeding commenced by or against the corporation prior to dissolution may be continued as if the corporation had not been dissolved. While there was, therefore, some question about whether the plaintiff corporation actually required leave to continue its action, the Court held that it was not necessary to resolve that question, as it was prepared to grant the leave.

In reaching this conclusion, the Court reviewed the actions taken by the plaintiff company, which included multiple changes in its corporate structure, a failure to keep the Ministry informed of its current address, a failure to file annual returns, and a failure to file corporate tax returns. The Court concluded, on a balance of probabilities, that a decision had been made to allow the plaintiff corporation to fall into disuse and, ultimately, dissolution. In other words, the failure to comply with its regulatory obligations had not been inadvertent. Despite the plaintiff company not having met the requirements of section 18 of the *Corporations Information Act,* the Court held that it retained a residual discretion to grant leave. Supported by the jurisprudence, the Court's view was that it was mandatory to grant leave where the conditions in section 18 had been met, but otherwise the Court still had the discretion to grant leave in other "just and appropriate circumstances". In this case, the Court concluded that it would be unjust to terminate the plaintiff's lawsuit on the basis of an unpaid $50 fee without a hearing on the merits, and that such a punishment would be "grossly out of proportion" with the acts and omissions of the plaintiff company. All fees and filings were now up-to-date, the plaintiff company was properly constituted, and leave to continue the action to a full hearing was granted.

Bloomsbury & Butterfield Ltd. v. Economical Mutual Insurance Group, 2011 ACLG ¶79,413
2011 BCLG ¶78,837
2011 CCLR ¶200,994
2011 CCSG ¶51,274
2011 OCLG ¶51,650

Derivative Actions

Court of Queen's Bench of Alberta, August 11, 2011

The plaintiff, Yousra Jaber ("Jaber"), was one of the investors in a condominium building project. A company planned to acquire a 36-unit condominium building and resell the units in that building for a profit. To that end, it secured funds from investors for the purchase of the building. Jaber brought a court application to require disclosure of information from the company's solicitors and alleged that this information showed that monies advanced to the company had in fact been paid out to one of the defendants, Nageb Ammache ("Ammache"). Jaber also alleged that Ammache, who denied the allegations, had no right to receive the funds, that Ammache attempted to hide the fact that he had done so, and that he made false representations to Jaber with respect to the profitability of the company. Jaber brought an

application for leave to commence a derivative action against Ammache and the other defendants in the name of the condominium corporation.

The application was allowed. The 51% shareholding in the company held by Jaber was held under an arrangement in which the defendant, Ammache, held the shares in trust for Jaber. Notwithstanding the fact that the shares were held in trust, the Court was prepared to exercise its discretion to find that Jaber was a "complainant" within the meaning of subparagraph 239(*b*)(iv) of the *Business Corporations Act* (the "Act").

In order to obtain leave to bring a derivative action, an applicant must, under subsection 240(2) of the Act, give notice to the directors of the corporation on whose behalf the action will be brought and must be acting in good faith. The court must also be satisfied that bringing the action would appear to be in the interests of the corporation.

The parties agreed that Jaber had given the required notice to the directors of the condominium corporation. The defendants argued, however, that Jaber was not acting in good faith but was pursuing a "personal vendetta" against Ammache. The Court agreed that there was considerable "bad blood" between the parties, but this did not justify a conclusion that Jaber was acting in bad faith. Rather, the materials filed with the Court sufficed to show that there was reason to determine the legitimacy of recorded payments out of the company. As well, Ammache's apparent reluctance to allow Jaber to explore those issues on an informal basis justified the Court's conclusion that Jaber's attempt to explore the issues through a derivative action was in good faith.

Finally, the Court held that it was satisfied that the proposed action was in the best interests of the company and leave to bring that action was granted. The Court required, however, that Jaber file an undertaking to pay any costs awarded against the company in the action personally.

Jaber v. Ammache, 2011 ACLG ¶79,414
2011 BCLG ¶78,838
2011 CCLR ¶200,995
2011 CCSG ¶51,275
2011 OCLG ¶51,651

Winding Up

Ontario Superior Court of Justice, July 29, 2011

In 1991, Leon Saltsov, acting through his company Saltsov Holdings Inc. ("Saltsov"), and Valery and Iosif Levitan (the "Levitans"), acting through their company, Levitan Corporation ("Levitan"), incorporated Cashcode, which manufactured currency validator machines. Saltsov and Levitan each owned 50% of the shares in the company. Saltsov was responsible for engineering and manufacturing, while the Levitans managed the day-to-day operations of the company. Salaries were paid to Saltsov and to the Levitans, but the amount of salary paid to the Levitans was greater than that paid to Saltsov. Profit remaining after the payment of salaries was divided evenly between them; however, Saltsov chose to receive his share of the profits by way of a bonus, while the Levitans elected to take their share of profits by way of dividends.

Although Cashcode was successful, relations between Saltsov and the Levitans deteriorated until they were unable to work together. An attempt to hire a third party to manage the business was unsuccessful. The Levitans brought a successful oppression action against Saltsov on the basis that Saltsov was interfering with the business and the prospect of selling the business. In that action, Saltsov was ordered to comply with the shareholders' agreement. Eventually, the parties agreed on the appointment of a receiver in June 2004 for the purpose of managing Cashcode's ongoing business and continuing the plan to sell the business.

In May 2011, Levitan brought an application for the winding up of Cashcode. Saltsov brought his own application for a winding up, but sought two adjustments to the company's financial holdings prior to distribution of its assets between the parties: first, Saltsov alleged that he should receive compensation for the unequal payment of salaries; second, he sought an adjustment to reflect the fact that, when the Levitans elected to receive their share of the profits as dividends, that payment structure created a tax liability for the company. Saltsov asked that the amount distributed to Levitan on winding up be reduced to reflect that tax liability.

The winding-up application was allowed, with one adjustment. The Court began by noting that it possessed the discretion to wind up a corporation where it was "just and equitable to do so" under section 207 of the *Business Corporations Act* (the "Act"). That section also empowered the Court to make any order that it thought fit on a winding up. Section 248 also provides the Court with broad remedial powers to make any order it thinks fit to rectify unfairness.

The Court held, first that the company should be wound up, as agreed by the parties. The Court then considered whether the two adjustments requested by Saltsov should be made before the division of Cashcode's assets. The Court determined that the adjustment with respect to the salary differential was unwarranted. The corporation's practice for many years had been to distribute executive salaries on an asymmetrical basis and Saltsov had signed off as a director of Cashcode to those distributions. It was not, in the Court's view, now open to Saltsov to dispute those distributions.

On the issue of the second adjustment, the Court was satisfied from the evidentiary record that the Levitan shareholders were to be responsible for the tax liability incurred as a result of their taking of dividends. The Court also agreed with expert evidence indicating that the amount of the tax liability had originally been underestimated and that a further adjustment was required to correctly reflect the tax liability associated with the dividend payments.

Levitan had argued that Saltsov's claim for the adjustments was statute-barred by reason of the expiry of a limitation period. The Court was willing to assume, without making a decision on the point, that, had the relief being sought been advanced as an oppression claim, it would have been statute-barred. However, neither party was bringing an oppression remedy claim. Both parties were asking the Court to exercise its statutory and equitable jurisdiction to wind up the company and make ancillary orders as it deemed just. The Court also noted that it was not necessary for the court on a winding-up application to make a finding of oppression in order to make whatever order it deemed just and equitable. Under the circumstances, the Court concluded that it was fair and equitable that an adjustment be made to reflect the tax liability of Cashcode in relation to the payment of dividends to Levitan.

2011680 Ontario Inc. v. 968831 Ontario Inc., 2011 ACLG ¶79,415
2011 BCLG ¶78,839
2011 CCLR ¶200,996
2011 CCSG ¶51,276
2011 OCLG ¶51,652

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