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Chair of the Compensation Committee: *Evolution of the Role*

Introduction

Shareholders and regulators are continuing to demand more of corporate boards, calling for their active and direct involvement in corporate governance. In response, boards and their committees have been re-examining their mandates, membership, internal processes and alignment with best practices. With compensation remaining a top concern for investors, regulatory bodies and the public, compensation committees in particular are being affected, with a strong call for direct involvement and accountability on executive compensation decisions. One of the greatest changes taking place is in the evolution of the role of compensation committee chair, triggering a need to rethink and document the changes, as has generally been done for the committee itself by way of its written mandate from the board.

A Changing Style for a Changing Governance Environment

Central to the evolution of the chair role is a gradually changing leadership style - a move from a generally reactive, dependent and accommodating style to a more proactive, independent and challenging style when dealing with executive compensation and performance issues. Today's committee chairs are being asked to control the committee work plan and agenda, with input from the board and its chair at the outset of the year, and be prepared to initiate various pay and performance analysis with input from, but independent of, management. Perhaps most important, the chair must be prepared and able to challenge management recommendations and analysis when the committee and / or board believe it is warranted.

Today's chairs are being asked to juggle these increasingly hands-on demands while at the same time maintain high-level oversight. And all this while maintaining a constructive working relationship with the CEO and management team!

Compensation Committees: the Core Responsibilities

Traditionally, the compensation committee has been responsible for overseeing human resource and compensation policies on behalf of the board; duties include the following, as typically noted in the committee charter:

- Develop recommendations to the full board in the following areas:
 - compensation policy for the CEO and executives
 - compensation plan design including appropriate performance metrics
 - target pay and corresponding performance levels for the CEO and other top executives
 - cash, equity and any other incentive awards
 - pension and benefits as applicable
- Review plans for talent management including retention and succession of key executives and career development of employees, with a focus on building and maintaining a strong internal talent pool
- Support the board and its chair with regards to negotiating the CEO's employment agreement
- Oversee the preparation of executive compensation disclosure and recommend to the full Board for inclusion in the proxy circular

As pressure for improved governance continues, so do innovations in compensation committee duties, processes and practices. Consequently, changes to the chair's role are not

limited to style alone - they also reflect an expansion in the committee's core responsibilities.

Role of Committee Chair in CEO Employment Contract Negotiation

A new CEO appointment presents opportunities for the committee chair to:

- Eliminate, as appropriate, legacy compensation practices and align with "best practices" in executive compensation
- Support the board chair (who is typically the key point of contact with the CEO through contract negotiations), by providing input and ensuring final arrangements are aligned with executive compensation philosophy as set by the committee

Expanding Role of Compensation Committee Chair

Key responsibilities of the chair role, above and beyond those of the committee and its members, include an increasingly active and therefore time-consuming role outside of committee meetings. The expanding role includes reviewing committee materials and liaising with the

board, management and external advisors, to ensure a meaningful level of understanding and exchange of views before the compensation committee meeting. These activities are listed in more detail at the end of this briefing; areas of focus include amongst others:

- Lead the pre-review of mailing materials with appropriate parties, having a sufficient level of comfort with quantitative aspects of pay and performance measurement to lead the committee to develop an informed view on proposals
- Provide active leadership in the hiring and direction of advisors to the committee
- Oversee the executive compensation process, outcomes and disclosure, with awareness and consideration of public relations and corporate reputation; to this end, some chairs have taken direct ownership of compensation disclosure by drafting core messages themselves
- Ensure open dialogue and the timely exchange of relevant information between the Compensation, Audit and Risk Committees, and the full Board, not just at year end, but on a routine basis
- Engage with the full board on compensation matters so that directors are aligned with respect to the objectives and inherent risks of compensation programs, and have line of sight to upcoming compensation decisions
- Keep abreast of key issues and developments; ensure programs, such as director education sessions, are offered to members of the compensation committee, and the board, so that they be kept up to date on the changing environment
- Where warranted, coordinate with the board chair to establish and conduct a regular and appropriate process of shareholder engagement regarding executive compensation matters

Audit Committee versus Compensation Committee

It is generally accepted that audit committee represents the most demanding committee duty; however, as demands increase, the compensation committee faces a workload with unique challenges; in contrast to the audit committee, the compensation committee is:

- operating within a significantly less prescriptive regulatory framework (disclosure is regulated, but content is generally not)
- responsible for significant personal judgment in decision making, and the ultimate accountability that goes with it
- navigating comparatively uncharted waters, whereas audit committees benefit from a model that has stabilized over time
- not currently required to retain an expert external advisor, whereas audit committees are required to retain an auditor

In response to these changes, boards are moving to document the higher expectations of the role of the compensation committee and its chair, in order to enhance the committee's effectiveness and demonstrate good governance to shareholders.

Conclusion

As companies and their Boards continue to adjust to the reality of the changing governance environment, we will continue to see an increasing burden on a number of key director roles, including the chair of the compensation committee. The heavier work load resulting from higher expectations on the part of regulators and shareholders is expanding the duties of the chair role, leading some firms to define and document the full expectations of the role. By defining the role, firms are moving to formalize many of the activities already completed by experienced committee chairs, and establish expectations for less experienced committee chairs, resulting - in both cases - in improved efficiency and effectiveness of the committee.

The “Overview: Compensation Committee Chair Role and Responsibilities” on the following pages reflects Hugessen’s perspective on the emerging “best practice”, with respect to the role and responsibilities of the Chair of the Compensation Committee

Overview: Compensation Committee Chair Role and Responsibilities

In addition to the broad duties and responsibilities set out for the compensation committee in the board's charter, responsibilities of the chair of the compensation committee typically include the following:

1) Core Activities

Committee direction and leadership

- Provide overall leadership to the board's compensation committee with the objective of ensuring that the committee discharges its responsibilities, as outlined in the committee's charter, to the board and to shareholders in a timely and effective manner
 - In conjunction with the board chair and members of the committee, and with input from management and advisors, as appropriate:
 - Review annually and update as required the committee charter to ensure that it is accurate and up-to-date with best practices and external expectations
 - Establish, with management's support, and with input from the board chair as required, the committee's meeting schedule and associated key agenda items for the year (ideally providing members with a year's notice of meeting dates)
 - Ensure necessary information sharing between the Compensation, Audit, and Risk Committees early and often on matters pertaining to executive compensation
 - Facilitate open communication between the committee and management on compensation matters
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Committee organization, resources and development

- Supervise the structure, composition, membership and activities delegated to the committee
- Oversee the hiring, ongoing direction, performance assessment, payment and termination of the compensation committee's advisors (i.e., compensation consultants, lawyers, etc.) recognizing

the need to limit delegation of this work to management in order to preserve advisor independence

- Assess performance and provide feedback to members of the committee, management and external advisors as appropriate
- Organize the board evaluation of the committee, and the committee self-evaluation and de-brief
- Lead the annual evaluation and feedback to the committee's external advisors

Tasks leading up to each compensation committee meeting (over 4 – 6 week period)

- Review and approve detailed agenda with management, including necessary and appropriate resources / attendees, ensuring that sufficient time is scheduled to thoughtfully address the agenda items
- Review and approve for distribution to the committee materials (i.e., substantive proposals / materials for consideration) prior to mailing to committee members, ensuring that materials include appropriate analysis of proposed changes, and independent perspectives
- Meet with management and the committee's advisors, together and/or separately as required
- Ensure the timely, accurate and appropriate exchange of information among the committee, management and the committee's advisor

2) Board Interaction and Support

Board interaction and support

- Maintain a working knowledge of current events, emerging issues, management and shareholders concerns, etc., as they pertain to the compensation committee's mandate
- Keep the board chair, and the board, abreast of key issues and trends (e.g., say on pay, shareholder issues, performance conditioning of long-term incentives)
- Solicit input from the board with respect to areas where additional education would be beneficial; organize development sessions as

appropriate in light of emerging issues and committee knowledge and interests

- Report to the board with respect to the committee's activities, findings and recommendations

3) Shareholder Communications and Engagement

Shareholder communications & engagement

- In conjunction with the board chair, lead on behalf of the board any agreed engagement process with the company's shareholders on matters involving compensation and, as appropriate, with the institutional shareholder and regulatory community generally (e.g., CCGG, RiskMetrics Group, OSC, OSFI (where applicable, etc.))
- Alongside the board chair, initiate a dialogue at the board level to establish a consistent corporate message to shareholders and regulatory groups with regards to pay and performance
- Set the direction for communication with shareholders on executive compensation, including each year positioning and overseeing the preparation of executive compensation disclosure and related communications (i.e., proxy circular)

For further information or to schedule a discussion about this topic, please contact any one of the following consultants:

Toronto

Ken Hugessen at 416-868-4422, khugessen@hugessen.com

Georges Soaré at 416-868-4416, gsoare@hugessen.com

Paul Hooper at 416-847-4629, phooper@hugessen.com

Allison Lockett at 416-868-4428, alockett@hugessen.com

Calgary

Scott Munn (Calgary) at 403-444-5485, smunn@hugessen.com

Hugessen Consulting is an independent consulting firm dedicated to meeting the executive compensation consulting requirements of boards and their compensation committees. With offices in Toronto and Calgary, the firm's mission is to be the leading provider of advice on executive compensation, performance measurement and assessment, and related governance to the compensation committees of medium and large companies in Canada, the U.S., and the U.K.

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