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Good Corporate Governance

Canadian Corporate Good Governance

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Shareholder Involvement in the Director Nomination Process: **Enhanced Engagement and Proxy Access**

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OVERVIEW

- **"Proxy access"** is the ability of shareholders to have meaningful input into the director nomination process *(by being able to influence who the nominees are/by actually nominating directors)*.
- Under Canadian corporate law shareholders elect directors but shareholders have no input in the normal course in choosing any director nominees. Current best practices in Canada suggest that those nominees should be chosen by an independent nominating committee of the board.
- Corporate law recognizes this principle by providing shareholders with the ability to have direct input into board composition by giving shareholders the right to nominate directors from the floor at an annual general meeting ("AGM").
- The board and management should welcome the input of shareholders in this important area as bringing the perspective of owners and stewards. And that companies should not use advance notice bylaws or any other mechanisms to impede the proxy access policy described.
- The overarching idea behind enhanced proxy access is the view that shareholders' ability to have a meaningful say in the nomination of directors is a benefit to the corporation and a fundamental principle of shareholder democracy.
- A slate of nominee directors in non-contested director elections, where the number of nominees is equal to the number of director openings and all such nominees have been selected by the existing board, often with the input of the CEO, and which is established without any meaningful input into its composition by the voting participants, is not true shareholder democracy.
- Enhanced proxy access will increase shareholder involvement in the director nomination process. In addition to encouraging boards to engage with shareholders on board composition, a specific proxy access mechanism is supported whereby shareholders can nominate some directors directly onto the company's proxy. This mechanism will be used sparingly by shareholders most likely when company performance is poor and attempts to engage have failed.
- Relevant differences exist in capital markets around the world that will impact the appropriate form of corporate governance, including the form of proxy access.

POLICY

- Independent directors should communicate with shareholders on a regular basis to seek their input on board composition, including appropriate director candidates. Absent a formal structure for shareholder input into the nomination process, the form of this communication should be within the discretion of the particular company, provided that it leads to real dialogue between shareholders and directors about board composition.
- In addition proxy access should be available to shareholders on the following basis so that shareholders have the ability to directly nominate some directors when warranted.

- ***Meaningful Ownership Level – 3% or 5% Depending on Market Capitalization***

Shareholders holding a meaningful percentage of a company's outstanding voting shares should have the opportunity to present director nominee(s) to shareholders in the company's proxy materials. Shareholders should be permitted to coordinate and aggregate their holdings to reach the required threshold. Any higher threshold would render this form of proxy access impracticable and defeat the objective of providing shareholders with a reasonable mechanism for nominating directors directly. Shareholders must continue to hold the relevant percentage of shares up to the time of the meeting at which the director nominees will be considered. This form of proxy access is another area impacted by the problems associated with empty voting.

Proxy access should not be available to shareholders whose economic ownership interest does not reflect their voting interest with respect to the level of outstanding shares that provides the basis for their access to the proxy. Accordingly, proxy access should be available only to shareholders that represent that their economic ownership interest, being the amount of their equity in the company "at risk", is equal to their voting interest with respect to at least three or five percent of the outstanding voting shares depending on market capitalization and that such percentage will be held until the meeting at which the shareholder nominees are proposed for election.

- ***Cap on number of nominees***

In order to distinguish this normal course access to the proxy from situations where a change of control of the board is the goal, the number of shareholder nominees permitted under a proxy access mechanism should be capped. To avoid ‘creeping board control’ through the proxy access mechanism, shareholders should be restricted to nominating the lesser of three directors or 20 percent of the board. Shareholders would not be able to nominate another three directors or 20 percent of the board in following years so long as the previously nominated directors, if elected, remain on the board.

- ***Fair disclosure in the proxy circular and form of proxy***

The disclosure about shareholders’ director nominees in the company’s proxy circular and form of proxy should be set out fairly and on an equal footing with company nominees. Equal footing requires that shareholder nominees be placed in the same location as company nominees in the proxy circular, that the same opportunity to present information on nominee background and qualifications is available for all nominees and that a fair form of universal proxy is used. All relevant information about any compensation being paid to shareholder-nominees should be clearly disclosed in the proxy circular as well in order to let shareholders know of any ‘golden leash’ arrangements that may be relevant to shareholders when determining how to vote.

- ***No holding period required***

Its not believed that a holding period is necessary either to ensure that proxy access is restricted to shareholders with a long term perspective or to avoid vexatious nominations. Past behaviour is not necessarily indicative of future intention and it cannot be assumed that a shareholder that purchased shares only recently does not have a long term perspective. participants were not comfortable with the notion of identifying ‘long term shareholders’ on the basis of holding periods”. Shareholders that are not seeking to change control of the board should be able to access the company’s proxy and then let the shareholders decide at a shareholder meeting which directors they wish to elect.

SUMMARY

It is recommended that companies adopt policies and procedures that will enable shareholders to communicate with independent directors about board composition on a regular basis.
The corporate statutes are an appropriate location for proxy access provisions given that they currently provide alternative mechanisms for nominating directors.
Shareholders holding an aggregate economic and voting interest of at least five or three percent of an issuer's outstanding voting shares, depending on the company's market capitalization, should be able to nominate directors to be placed on the same form of proxy as the company's nominees.

- Shareholders must hold the prescribed percentage of shares up to the time of the meeting at which the shareholder- nominees are proposed for election.
- Disclosure about shareholder nominees should be set out fairly in the company's proxy circular, including being located in the same section of the proxy circular with the same prominence and on essentially the same terms as disclosure about the company's nominees, along with the use of a fair universal proxy' form.
- Shareholders do not need to hold their shares for a specific period of time before they are permitted to nominate a director.
- The number of directors to be nominated by shareholders cannot exceed the lesser of three directors or 20 per cent of the board.
- Shareholders nominating directors should be able to use the company's proxy circular to solicit support.
- Reasonable solicitation costs on the part of the shareholder should be paid by the company unless shareholders resolve otherwise.
- Shareholders nominating directors must make representations that they are not seeking control and that their economic ownership interest is at least five or three percent, depending on the company's market capitalization, of the issuer's outstanding voting shares.
- The adoption of a meaningful process for receiving shareholder input on a regular basis about board composition, including the director nomination process, along with the adoption of the method of enhanced proxy access outlined above, offers a practical mechanism that would make the shareholders' right to elect directors meaningful and will assist in holding boards accountable and in improving board composition and performance.

DUAL CLASS SHARE POLICY

- Overview of DCS Policy
- Advantages
- Disadvantages
- Governance Differences of Equity Controlled Corporate Policy Principles:
  1. Electing Directors
  2. Maximum Voting Ratio of MV Shares to SV Shares
  3. Non-voting common shares
  4. Coattails
  5. Collapse of the DCS structure
  6. Monetization of MV Shares
  7. Payments to an owner of MV Shares upon a collapse of the DCS structure

OVERVIEW OF DCS POLICY

- Dual Class Shares "DCS" (multiple voting shares "MV Shares" and subordinate voting shares "SV Shares").
- Currently there are 77 DCS companies (exclusive of investment funds) listed on the TSX. Google (which already is a DCS company) is planning to issue a new class of common shares with no voting rights. Notwithstanding that these principles are intended to be applied on a going forward basis to any newly created DCS company in Canada, existing DCS companies are encouraged to take these principles into account if and when appropriate.

  - Dual-class shares

    → Zuckerberg has 18% ownership but 57% of voting rights

Background

- The manner in which DCS companies are regulated in Canada today results from rules adopted by the Canadian Securities Administrators ("CSA") in the early 1980s and by the Toronto Stock Exchange ("TSX") in 1987 after years of hearings and debate. No material changes to these rules have been made in 25 years.

THE EXTRACT BELOW IS FROM A PAPER PUBLISHED IN 2005 ENTITLED “DUAL-CLASS SHARE STRUCTURES AND BEST PRACTICES IN CORPORATE GOVERNANCE”:

“Dual-class share structures emerged in [Canadian] companies for a variety of reasons. Historically, Canadian companies issued shares with multiple voting rights to preserve family control while gaining access to capital in public equity markets.

To retain voting control over the firm, the family kept the high voting stock for themselves and sold the restricted-voting shares to the public. Even today, these structures are common among family businesses that wish to go public, and often represent a transitional phase between private and full public ownership. As the company grows, controlling shareholders may opt to move to more equitable voting structures in a bid to build a larger investor base.

Past restrictions on foreign investment also served to encourage the use of dual-class share structures. While some of these restrictions have been lifted, the federal government continues to limit the level of foreign ownership of companies in various regulated sectors, including telecommunications, broadcasting, media and entertainment, and airlines. Even now, companies that use dual-class shares tend to be largely concentrated in these sectors. These companies often justify the continued use of such structures by the need to avoid violating foreign-ownership restrictions, while attracting adequate equity investment from foreigners.

An additional explanation as to why companies that favour dual class share structures are concentrated in the broadcasting and cable industries relates to the takeover protection conferred by subordinated voting. The existence of a large control block of shares makes it difficult for an investor to mount a hostile takeover of a firm. Since government regulators provide a limited number of broadcast licenses, often the only method of obtaining a license is to take over an existing company. Thus, it is argued that licensed firms have a greater incentive to protect themselves by issuing dual-class shares. Additionally, it is often the case that dominant individuals and families have played a significant role in the foundation and growth of the major cable and media firms in Canada.”

ADVANTAGES

DCS structures allow controlling shareholders which hold the MV Shares, the board of directors and management to focus on the long term success and profitability of the DCS company, thereby permitting long term investment decisions to be made instead of having to satisfy short term expectations which can be detrimental to building long term value

- DCS structures encourage entrepreneur-controlled companies to access the public capital markets and thereby provide investors the opportunity to purchase shares in companies that otherwise might not have been available to them
- DCS structures are an effective takeover defense which protects DCS companies from opportunistic acquirers
- DCS structures are helpful in those sectors which still have legislated Canadian ownership or control restrictions
- Some studies show that, over time, companies which have DCS structures outperform companies which do not have DCS structures
- DCS structures, if combined with meaningful equity ownership by the controlling shareholders, can align the interests of controlling shareholders with those of minority shareholders

DISADVANTAGES

- DCS structures confer voting power on the holders of the MV Shares well beyond the economic interest of those holders, thus providing shareholders that take a DCS company public the ability to access public capital (generally at a cost which is less expensive than private capital) and to continue to control the DCS company yet pass off the majority of the financial risk to the public owners of the SV Shares
- DCS structures may result in a non-assertive board of directors in light of the fact that only the holders of MV Shares have the actual ability to elect or replace the board
- DCS structures can entrench poorly performing management, can result in nepotism or cronyism in management succession and can insulate management from accountability for their actions
- Situations have arisen where holders of MV Shares have been able to extract funds and other assets from a DCS company through unreasonable compensation plans or self dealing
- Situations have arisen where a DCS company's cash flow has been diverted to personal projects championed by the holders of MV Shares which are unrelated to the company's core business and strategy
- Some studies show that, over time, companies which have DCS structures underperform companies which do not have DCS structures

PRINCIPLES

1. ELECTING DIRECTORS

- **Principle:** Holders of MV Shares should be entitled to nominate to the board of the DCS company a number of directors equal to the least of
  - i. two-thirds of the board,
  - ii. the number obtained when the board size is multiplied by the percentage of total voting rights held by the MV Shares (rounded up to the nearest whole number), and
  - iii. if the holders of MV Shares are related to management of the controlled corporation, then one-third of the board. When a DCS company reports the results of director elections, in addition to disclosing the aggregate voting results the DCS company also should disclose the voting results for the MV Shares and the SV Shares separately.

Note: Its recommended that two-thirds of the board of every non-controlled corporation should be independent of management. However its recognized that it would be appropriate for a controlling shareholder which controls a company through its ownership of common shares (and not through MV Shares) to have directors related to it on the board in proportion to the controlling shareholder's ownership of common shares, to a maximum of two-thirds of the board. If the controlling shareholder is related to management of the controlled corporation.

A controlling shareholder which controls the company through MV Shares also should be entitled to have directors on the board in proportion to its voting rights, to a maximum of two thirds of the board. However, as with a controlling shareholder that controls a company through ownership of common shares, if the holder of MV Shares is related to management of the controlled corporation then at least two-thirds of the board should be independent of both management of the controlled corporation and the controlling shareholder.

In any event, irrespective of which shareholders nominate a director, under Canadian corporate law every director owes duties to the corporation rather than to the shareholders that nominated the director.

This principle does not require the SV Shares to have a separate class vote in director elections. Each DCS company can determine in its particular circumstances how best to achieve the outcome set out in this principle.

2. MAXIMUM VOTING RATIO OF MV SHARES TO SV SHARES

- **Principle:**
- Any DCS structure which is adopted should require holders of MV Shares to have a meaningful equity ownership stake in the DCS company.
- While the import of a "meaningful equity ownership stake" may vary depending on context, a ratio of voting rights of a MV Share to a SV Share of no more than 4 to 1 generally would constitute a "meaningful equity ownership stake".
- **Note:**
- What constitutes a "meaningful equity ownership stake" is not simply an arbitrary computation. A MV Share to SV Share voting ratio of 4 to 1 assures that the holders of all the outstanding MV Shares own 20% of the equity of the DCS company in order to have voting control of the company. A 20% equity ownership stake is "meaningful", but also recognize that a lower percentage could be meaningful if the dollar amount of the ownership stake represents a significant economic interest in the DCS company's equity.

3. NON-VOTING COMMON SHARES

- **Principle:** Companies which are reporting issuers should not have non-voting common shares.
- **Note:** A fundamental right of a common share is the right to vote at a shareholder meeting. By requiring common shares to have a vote, all holders of common shares will be entitled to attend an annual shareholder meeting in order to exercise the fundamental right to vote for directors and to address management and the board once a year.

4. COATTAILS

- **Principle:** In order to ensure that owners of SV Shares and owners of MV Shares are treated equally when there is a change of control of a DCS company, all DCS companies which are reporting issuers, even if not listed on the TSX, should have coattails.
- The TSX should standardize the form of coattail provisions for TSX listed DCS companies rather than leave the form of coattail to the discretion of the TSX to approve. DCS companies which are reporting issuers, even if not listed on the TSX, should adopt the same standardized coattails.
- **Note:** The owners of MV Shares and the owners of SV Shares should be treated equally in the event that there is a change of control of the DCS company. The listing requirements of the TSX currently require DCS companies to have coattail provisions in place, the terms of which must be pre-cleared with the TSX. Rather than relying on the TSX's discretion to approve the form of coattail drafted by the DCS company, DCS companies should have standardized coattail provisions in place to protect holders of SV Shares. Furthermore, these standardized coattails should apply to DCS companies which are reporting issuers even if the DCS companies are not listed on the TSX.

5. COLLAPSE OF THE DCS STRUCTURE

Principle: The DCS structure should collapse at an appropriate time as determined by the board of the DCS company and, if practicable, as set out in the DCS company's articles, unless a majority of the outstanding SV Shares voting separately as a class approve the continuation of the DCS structure. Any approval by the holders of the SV Shares to continue the DCS structure should remain in effect for five years or such shorter period of time as is approved at the shareholder meeting by majority vote of the outstanding SV Shares voting separately as a class. Prior to the expiry date, another separate class vote of the outstanding SV Shares should be required in order to continue the DCS structure for another period of up to five years and so on thereafter. If the DCS structure is not then all MV Shares outstanding on the MV Share Termination Date should convert automatically into SV Shares on a one-for-one basis.

On an ongoing basis, the board of a DCS company should consider the reasons why a DCS structure was established and whether those reasons remain valid and should explain to shareholders annually in the DCS company's proxy circular (or if the DCS company does not issue a proxy circular because the public owns non-voting common shares, then in another public document which is filed with the securities regulatory authorities) the reasons why the continued existence of the DCS structure is appropriate.

- **Note:** Because there are many types of DCS companies, it is difficult to have a "one size fits all" definition of MV Share Termination Date. Some DCS companies are controlled by entrepreneur founders or immediate family, some are controlled by private equity groups and some are established to comply with legislated Canadian ownership or control restrictions.

Accordingly, boards of newly created DCS companies, as well as the underwriters and legal advisers assisting newly created DCS companies in future initial public offerings, should consider the following matters when contemplating how to define the MV Share Termination Date in a DCS company's particular circumstances:

1. *should the definition tie into the date when the DCS company's founders are no longer directors or senior officers of the company?*
2. *should the definition tie into the date when the DCS company's founders together with permitted transferees no longer own, directly or indirectly, at least a specified percentage of the total number of the company's outstanding MV Shares and SV Shares (counted as if such shares were of the same class)?*
3. *is there a specific outside date when the DCS structure should collapse?*
4. *should the definition tie into the date when legislated Canadian ownership or control restrictions no longer apply to the DCS company?*

6. MONETIZATION OF MV SHARES

- **Principle**: A holder of MV Shares should not be allowed to monetize the holder's MV Shares by entering into a derivative transaction.
- A holder of MV Shares may sell some or all of the holder's MV Shares, if the holder wishes. Such sold MV Shares should convert automatically into SV Shares on a one-for-one basis unless sold to a permitted transferee (as such term is defined by the particular DCS company).
- **Note:** Owners of MV Shares already are able to exercise control over a DCS company that is not proportional to their equity interest. If a shareholder with MV Shares is allowed to monetize such holder's economic interest in the MV Shares, then the proportion of control to equity will be further skewed or the equity interest of the holder of the MV Shares may be eliminated entirely. Shareholder control with little or no equity investment can lead to non-alignment of the interests of the controlling shareholder with the interests of the other shareholders.

7. PAYMENTS TO AN OWNER OF MV SHARES UPON A COLLAPSE OF THE DCS STRUCTURE

- **Principle:** No premium should be paid to the owner of MV Shares upon a collapse of the DCS structure.
- **Note:** Just as owners of MV Shares and SV Shares should be treated equally pursuant to coattail provisions upon a change of control of a DCS company, owners of MV Shares should not be entitled to receive any premium when a DCS structure is collapsed. Accordingly, on the MV Share Termination Date all outstanding MV Shares should convert automatically into SV Shares on a one-for-one basis.

3. BUILDING HIGH PERFORMANCE BOARDS

- Introduction
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  - Facilitate shareholder democracy
  - Ensure at least two thirds of directors are independent of management
  - Separate the roles of Board Chair and Chief Executive Officer
- EXPERIENCED, KNOWLEDGEABLE AND EFFECTIVE DIRECTORS WITH THE HIGHEST LEVEL OF INTEGRITY
  - Ensure that directors are highly competent and bring the requisite knowledge and experience to the board
  - Ensure that the goal of every director is to make integrity the hallmark of the corporation
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- A HIGH PERFORMANCE BOARD HAS CLEAR ROLES AND RESPONSIBILITIES
  - Establish mandates for board committees and ensure committee independence
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  - Oversee Strategy
  - Oversee risk management
  - Assess the Chief Executive Officer and plan for succession
  - Develop and oversee executive compensation plans
- A HIGH PERFORMANCE BOARD ENGAGES WITH SHAREHOLDERS
  - Report governance policies and initiatives to shareholders
  - Engage with shareholders

INTRODUCTION

"Strengthening board independence and fixing board oversight, particularly of risk management, is the essential starting point for corporate governance reform … There is no way detailed regulation can mandate how to make every critical discretionary decision in a private enterprise. The minds of men and women generally never stop being ingenious and entrepreneurial in finding open spaces in regulations. This is why we need to rely on the independent mindedness of directors – as the agents of shareholders, under a fiduciary responsibility to direct strategy, monitor performance, control risk, and generally 'do the right thing' for the company and society."

- **<u>The role of directors</u>**

Shareholders of public companies elect directors to oversee the business and affairs of the companies in which the shareholders are invested. Directors have a fiduciary duty to act in the best interests of the corporation. Directors also should consider, where appropriate, the interests of all stakeholders. Directors must be (and be seen to be) independent of the management they hire and oversee in order to give shareholders confidence that the board can carry out these responsibilities effectively.

- **<u>The role of shareholders</u>**

Pension funds, mutual funds and other institutional money managers have acquired significant equity stakes in publicly traded corporations. Today, as much as 40% to 45% of the equity of major Canadian public companies is owned by institutional shareholders. At the same time, clearer expectations of how public companies should be governed have emerged, and shareholders and their representatives are actively engaging with boards of directors to discuss these expectations. There is also increasing focus on the responsibilities of shareholders in exercising their stewardship role.

A HIGH PERFORMANCE BOARD IS ACCOUNTABLE AND INDEPENDENT

Guideline 1: Facilitate shareholder democracy

The right to vote is critically important for shareholders and fundamental to shareholder democracy. Every public corporation must have a voting system that supports shareholder democracy. Following a shareholder vote, the corporation should disclose the detailed voting results immediately, irrespective of the manner in which the vote is held.

A Note on Majority Voting

Current Canadian corporate and securities regulations limit shareholder democracy by enshrining a plurality voting system. Under that system, shareholders can only vote "for" or "withhold" their vote for directors. The effect of the plurality system is that a director can be elected with only a single vote "for", even if an overwhelming number of shareholders withhold their vote.

Expected best practices

- Adopt a majority voting policy for uncontested director elections
- Obtain shareholder approval before issuing 25% or more of the shares of the corporation as part of a transformational transaction.
- Report detailed voting results on SEDAR immediately, indicating the actual number and percentage of votes cast for, against and/or withheld for each resolution.
- Issue promptly a news release describing the results of director elections
- The Board should give serious consideration to the voting results for shareholder proposals even if the resolutions are only advisory in nature.

<u>Guideline 2: Ensure at least two thirds of directors are independent of management</u>

In order to ensure directors' interests are aligned with shareholders, at least two thirds of every board should be independent of management.

"Independence" means a director is independent of management, does not have a material relationship with the corporation and, except for director fees and share ownership, does not financially benefit from his or her relationship with the corporation. A material relationship is any relationship that could interfere with a director's ability to exercise independent judgment or inhibit his or her ability to make difficult decisions about management and the business. Examples of people with material relationships with the corporation include: employees of a corporation; paid advisors or consultants to the corporation such as lawyers, accountants and bankers; employees of a significant customer or supplier; anyone with a personal services contract with the corporation; anyone affiliated with a foundation, university or other non-profit organization that receives significant grants or endowments from the corporation; relatives of the CEO or of other executives of the corporation; and those who are part of an interlocking directorate (where the CEO or other executive serves on the board of the corporation that employs the director). Boards also should assess the "independent mindedness" of prospective and current directors. Every member of a well-governed board should be willing to challenge management and, if necessary, other members of the board.

Expected best practices

- Ensure at least two-thirds of directors are "independent".
- Have a formal board policy which is publicly disclosed that limits the number of board and committee director interlocks on the board.
- Report clearly all board and committee interlocks to shareholders

Guideline 3: Separate the roles of Board Chair and Chief Executive Officer

The board chair and CEO have different responsibilities and a different focus.

- The chair is responsible for leading the board and ensuring that it is acting in the long-term best interests of the corporation.
- The CEO is responsible for leading management, developing and implementing the corporation's business strategy over the short and longer term, and reporting to the board.
- The chair is accountable to shareholders and the CEO is accountable to the board. Combining the two positions creates inherent conflicts of interest and obscures accountability. A chair cannot effectively oversee senior management when he or she is the CEO and a member of the management team.

Accordingly, the two positions should be separated. As a transition, companies may consider appointing an independent lead director for a short period of time.

Expected best practices

- The independent members of the board should appoint an independent board chair to function in a non-executive capacity with a defined mandate and role. The board chair should be prepared to invest considerable time and effort in the role and should have sufficient availability to do so.
- The independent chair (or independent lead director) should set board agendas with the CEO and other directors, be responsible for the quality of the information sent to directors and lead in camera meetings of independent directors.
- The CEO should be required to leave the board when he or she retires.

EXPERIENCED, KNOWLEDGEABLE AND EFFECTIVE DIRECTORS WITH THE HIGHEST LEVEL OF INTEGRITY

- **Guideline 4. Ensure that directors are highly competent and bring the requisite knowledge and experience to the board**

The character and effectiveness of a board is driven by its directors. Its believed the single most important corporate governance requirement is to have directors of quality. To facilitate this, all boards should put in place a director succession plan and ensure that they utilize a formal recruitment process to identify and recruit potential new directors. Boards may develop and manage that process internally or may choose to engage an independent third party; whatever method is used, boards should ensure that the involvement of the CEO in the director recruitment process is limited and appropriate.

Quality directors must also be curious. They must be willing to ask the questions of management that will provide them with a complete understanding of the risks and rewards of any proposed plan of action and how it will affect the long term viability of the corporation. While the quality of individual directors is paramount, we also expect boards as a whole to be diverse. A high performance board is comprised of directors with a wide variety of experiences, views and backgrounds which, to the extent practicable, reflects the gender, ethnic, cultural and other personal characteristics of the communities in which the corporations operate and sells its goods or services.

Director education creates boards with ever-increasing professionalism and enhances the effectiveness of directors, boards and board committees. At a minimum, a director education program should include an initial orientation along with ongoing educational programs and guidelines, such as formal education courses, in-house sessions and conferences.

Expected best practices

For individual directors:

- A significant number of directors on a board should have career experience and expertise relevant to the corporation’s industry, financial responsibilities and risk profile. Other directors will bring specific expertise, like human resources, accounting, law or other relevant professional knowledge. Each director’s career experience and qualifications should be described in the proxy circular.
- In addition to members of the Audit Committee, some directors should have financial accreditation and all directors should be financially literate as that term is defined in National Instrument 52-110, that is, able to understand a breadth and level of complexity of accounting issues that is reasonably expected to be raised by the corporation’s financial statements.

All directors should demonstrate excellent listening, communicating and persuasion skills so they can actively and constructively participate in board discussions and debate.

All directors should make a commitment to devote the time, effort and energy necessary to serve effectively as a director of the company. We believe that directors who hold a full-time executive position should hold at most two outside public company directorships and that directors who are not employed full time should generally hold no more than four additional outside public company directorships. Time commitments related to not-for profit organizations, private companies and government agencies also should be taken into account when directors' availability is considered.

Expected best practices

For the board as a whole:

- Utilize a formal process for identifying and recruiting new directors and describe that process in detail in the proxy circular. Ensure that the role of the CEO in that process is limited and appropriate.
- Maintain and disclose in the proxy circular a 'matrix' of director talents and board requirements that shows the corporation's needs and also identifies skill strengths of directors and any gaps on the board.
- Ensure that the board is diverse, or set reasonable and measurable targets to build a more diverse board.
- Build and maintain an "ever-green" list of suitable candidates to fill planned or unplanned vacancies.
- Have a plan in place for the orderly succession of directors to maintain an appropriate balance between directors with experience and those who bring a fresh perspective.
- Create a board of an appropriate size – large enough to include the requisite expertise and to allocate the various board and committee duties among the directors, but small enough to allow open, cohesive and responsible discussion and debate and to ensure individual accountability and responsibility for board decisions.
- Create an orientation and continuing education program for directors to establish and update their skills and knowledge of the corporation, its businesses and key executives, and to address ongoing and emerging issues in the functional areas of the board and disclose the program details in the proxy circular.
- Disclose in the proxy circular the education programs and events in which directors have participated in the past year.

Guideline 5: Ensure that the goal of every director is to make integrity the hallmark of the corporation

To have integrity is to be principled, moral, honest and responsible. A public company's reputation for integrity is fundamental in creating and maintaining value for shareholders and other stakeholders. Every director on the board should be a person with demonstrated integrity. The importance of integrity should be at the forefront in the boardroom and in every board committee discussion. The board also must make every effort to ensure that the CEO and other senior officers are individuals of integrity who are creating or building on a culture of integrity throughout the organization.

Expected best practices

For individual directors:

Each director should carefully examine the ethical implications of the corporation's strategies, policies, initiatives and activities. In order to empower directors to identify ethical issues and to deepen their understanding of them, directors should participate in educational activities relating to ethical issues for directors generally, as well as those that are specific to the industry or sector in which the corporation operates.

- When meeting with corporate employees (including the CEO and other senior officers), directors should take the opportunity, whenever possible, to emphasize the importance of integrity.
- Directors should demonstrate a proven understanding of fiduciary duty and the implications of their role as fiduciaries.

Expected best practices

For the board as a whole:

- Emphasize the importance of integrity during in camera sessions. Consider whether the CEO and other senior officers demonstrate the right "tone at the top" to ensure a culture of integrity throughout the organization.
- Include questions about integrity in board, committee and director performance reviews.
- Include integrity issues in continuing education programs for directors.
- Make sure the CEO and other senior officers have programs in place that build a culture of integrity. These should be led by the CEO and normally will include:
  - a statement of the corporation's values, emphasizing integrity as a fundamental value
  - sessions with employees that include discussions of integrity and reputation
  - codes of conduct, surveys of compliance and whistle blowing procedures, all in plain language so that they can be easily understood by all employees
  - the appointment of an officer who has responsibility for integrity at the corporation. The officer should work with the board and the CEO to make sure integrity issues are taken seriously and dealt with effectively
  - zero tolerance for breaches of integrity, taking into account employees who voluntarily report their transgression(s) and show remorse
  - a process for reporting all significant breaches of the code of conduct to the board.
  - Ensure that the integrity of candidates is a key consideration in the process of board and management recruitment.

Guideline 6:Establish reasonable compensation and share ownership guidelines for directors

Directors should be paid fees for their services at a level that is reasonable and will attract qualified and experienced candidates. Director compensation should not, however, be so high or structured in such a way that it interferes with a director's ability to be independent, forthright in his or her views or willing to challenge management or the status quo. Moreover, directors should recognize that when they determine their own compensation, they are in an inherent conflict of interest.

A HIGH PERFORMANCE BOARD HAS CLEAR ROLES AND RESPONSIBILITIES

Guideline 7: Evaluate board, committee and individual director performance

A board needs processes in place to evaluate and improve the performance of individual directors, board committees and the performance of the board as a whole. Annual performance reviews help directors assess their personal strengths and weaknesses, make decisions about the need for further education, and decide when it might be appropriate to step down. Directors should be assessed on the basis of their ability to continue to make an effective contribution. A robust assessment process whereby results of the assessment are acted upon is superior to establishing term limits or a retirement age as a method for removing under-performing directors. In order to assess the quality of current directors and board committees and processes, many boards confidentially survey directors once a year and have the board chair, lead director or nominating/governance committee or its chair review the results. Other boards prefer to hire an independent third party to perform board evaluations.

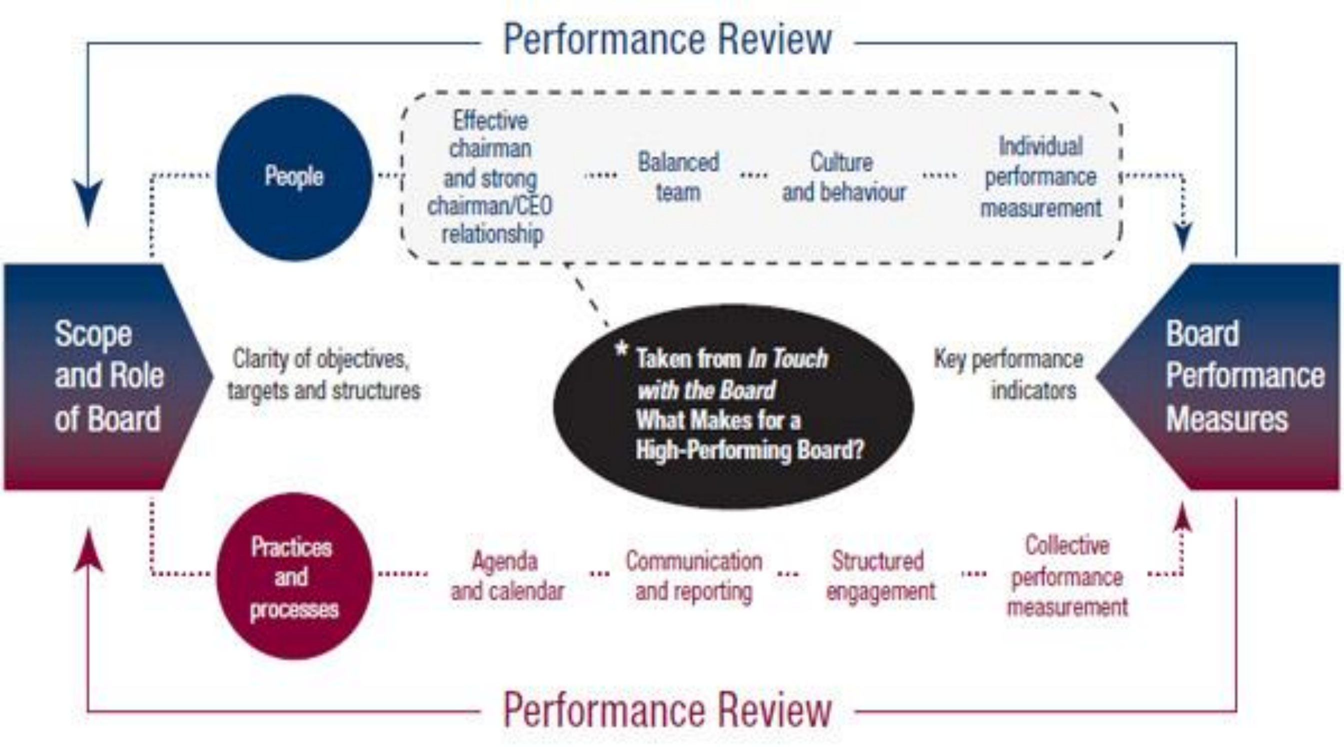
Expected best practices

For individual directors:

- Prepare a detailed list of expectations for individual directors and publish it in the proxy circular.
- Ensure the performance review process assesses a director's skill set and other expertise against the company's strategic plan and current skills required and other needs of the board.
- Publish the record of individual director attendance at board and committee meetings every year in the proxy circular and include directors who attended committee meetings on an ex officio or non-voting basis. Directors are expected to attend every board and applicable committee meeting, absent exceptional circumstances.
- Determine and document the kinds of events that will prompt an expectation that a director would resign from the board.
- Evaluate the performance of individual directors every year using a confidential peer-review survey. The board chair or independent lead director, chair of the nominating/governance committee or independent third party should conduct the survey and provide feedback to each director. The survey should include open-ended questions to allow directors to suggest improvements
- Establish an annual review process for the chair and disclose the details of that process to shareholders.
- Disclose the performance review process in the proxy circular in enough detail to demonstrate to shareholders that there is a robust system in place that is capable of identifying individual performance issues and effectively responding to them.

For the board and its committees:

- Evaluate the overall effectiveness of the board and its committees every year using a confidential survey or one-on-one meetings between the independent chair or lead director (for committees it should be the committee chair) and each director.
- Review the board and respective committee mandates every year and evaluate the performance of the board and committee chairs and members against their respective mandates annually.
- Disclose the board performance review process in the proxy circular in enough detail to demonstrate to shareholders that there is a robust system in place capable of identifying board or committee level performance issues and effectively responding to them. Where appropriate, disclose in the proxy circular conclusions drawn and improvement opportunities identified from the process.
- Ensure that the nominating/governance committee closely monitors emerging best practices in board and committee structure and processes as well as in how to evaluate board and committee performance.



Guideline 8: Establish mandates for board committees and ensure committee Independence

Committee charters should be adopted by the board and reviewed annually. Such charters should include requirements concerning the composition of the committees, responsibilities of the committees and procedures for committee meetings. Board committees often do a large part of the work of a board and then present their recommendations to the entire board for approval. As a result, conflicts of interest between management and shareholders are most likely to arise at the committee level first. Moreover, the work done by committees typically involves the detailed oversight and assessment of management.

Expected best practices

For all committees:

- Review committee charters every year and amend or confirm the mandate and procedures based on information received from the board and committee evaluation processes.
- Ensure that all committee meetings include in camera sessions with independent directors only.
- Ensure every committee includes directors of diverse backgrounds and at least one director with significant expertise relevant to the committee's role.

For the audit committee:

- Committee members must all be independent (as required under NI 52-110 Audit Committees).

For the nominating/governance committee:

- Committee members should all be independent, and the CEO should not participate in their selection.

For the compensation committee:

- Committee members should all be independent with an objective and knowledgeable view of compensation, formed independently of management, and the CEO should not participate in their selection.
- Ensure that no more than one in three members of the committee is currently the CEO of another corporation.
- Do not include management in committee meetings when their compensation is being deliberated.

Guideline 9: Adopt well defined board processes and procedures that support board independence

Board independence must be supported by the establishment of robust and well-defined board processes and procedures that will assist directors in meeting their oversight responsibilities. Board processes and procedures should ensure that directors are provided with sufficient information, time and independent advice to be able to make meaningful decisions in an independent manner.

Expected best practices

Meetings materials provided to boards by management must be sufficiently detailed, comprehensive and succinct to support meaningful decisions by directors. Meeting materials must be provided to the board far enough in advance of board meetings to allow directors to make considered decisions. Board meeting schedules must allocate sufficient time for major decisions to be considered/discussed/reviewed, with decisions reached over the course of more than one meeting if appropriate.

The independent chair should have approval over meeting agendas and the flow of information to the board. All board meetings should include in camera sessions with independent directors only. Procedures should be in place to ensure proper access to, and funding of, independent advisors to the board or its committees when the board or its committees deems it appropriate.

Guideline 10: Oversee Strategy

Directors are responsible for oversight of the corporation's strategy and ultimately approving the overall vision, objectives and long-term strategy of the corporation. Management, on the other hand, is responsible for developing and implementing an appropriate detailed strategy that is designed to realize the corporation's vision and achieve its objectives while managing the associated risks.

The board reviews, discusses, challenges and ultimately approves a strategic plan for the business and oversees management's implementation of the plan, ensuring it is consistent with the approved vision, long-term objectives and strategy. The board also monitors the corporation's performance against the strategic plan. The board should have a heightened interest in its oversight role of strategy because of its importance and impact on shareholder value.

Expected best practices

- At a formative stage of strategic plan development, review with management the format and planned content of the comprehensive strategic plan. The content of the strategic plan would include competitive analysis as well as resource requirements – both financial and human resources.
- Allocate sufficient time to review the strategic plan. Such review would involve discussion with and without management presence, challenging underlying assumptions and insisting upon modifications to the strategic plan as required.
- Approve the final strategic plan.
- Oversee the implementation of the strategic plan, including the linkage to the annual business plan.
- Monitor the corporation's performance against the strategic plan using appropriate metrics and milestones.
- Conduct periodic reviews of strategy during the strategic plan period.
- At least annually, require management to provide an update or a revised strategic plan.

Guideline 11. Oversee risk management

Directors are responsible for risk oversight, including overseeing management's systems and processes for identifying, evaluating, prioritizing, mitigating and monitoring risks. Directors are also responsible for approving the corporation's risk parameters including risk tolerance and appetite. Such parameters are designed to prevent the destruction of asset and shareholder value and to reduce the likelihood of underperformance over the long term. Directors should consider taking a heightened interest in assessing risks associated with strategy and leadership since management should not be expected to objectively assess its own performance, capabilities and strategy from a risk perspective.

- *Risk management is a core function of the board*

The global financial crisis has revealed that many directors, including directors of large, sophisticated corporations, did not have a full understanding of all of the risks facing their corporations and failed in effective risk oversight. Every organization is exposed to multiple risks. While strategic risk in terms of both strategy formulation and implementation effectiveness can pose a major threat, there are numerous other types of risks such as external, operational, financial, organizational, regulatory, environmental, reputational, etc., which can significantly impact a corporation's value in the short and long term. The board should understand how these various risks are interrelated and the resultant compounding effect. The effective oversight of all relevant types of risk is a core function of the board and a process in which every director should be actively involved. As part of its oversight role, the board should establish appropriate financial and non-financial incentives for management to operate within the board approved risk parameters.

For directors, risk oversight should go beyond quantitative risk assessments in order to focus on challenging the facts and assumptions management has used in identifying and evaluating risk. Experience has shown that assumptions such as these are not always valid, so boards should keep in mind and plan for unusual and unexpected occurrences and for systemic risks.

Expected best practices

- Clearly assign board responsibility for risk oversight as set out in board and committee mandates.
- Ensure breadth of capability on the board to understand and oversee all critical risks and, if appropriate, utilize independent advisors to advise the board with respect to critical risks.
- Ensure directors are engaged in discussions of risk and bring constructive criticism.
- Ensure independent verification of facts and assumptions relied on by management in its identification, evaluation, mitigation and monitoring of risks.
- Adopt an appropriate framework for the board's oversight of risk.
- Allocate sufficient time and resources in the board's agenda to consider risk.
- Clearly set out risk parameters including tolerance and appetite for risk.
- Understand interrelationship of risks and any pre-existing conditions or vulnerabilities that could have a compounding impact on the corporation.
- Adopt robust risk management systems and processes including active involvement by the chief executive officer with clear assignment of accountability to specific members of management.
- Adopt appropriate and effective management compensation arrangements aligned with risk parameters.
- Ensure full and complete disclosure of how the board oversees risk.

Guideline 12. Assess the Chief Executive Officer and plan for succession

The board is responsible for hiring, retaining and if necessary terminating the CEO, reviewing his or her performance every year and establishing an executive succession plan to ensure a pipeline of leadership talent is being developed. Succession planning should anticipate both orderly succession and unexpected scenarios.

Expected best practices

- Develop position descriptions for the CEO and other senior management that are updated as appropriate.
- Develop an annual review process for the CEO, including establishing CEO performance targets and objectives at the start of each fiscal year.
- Ensure the CEO has a talent development plan in place for senior executives.
- Review succession plans for the CEO and other senior executives at least annually.
- Review progress being made against succession plans to identify 'talent gaps' and take steps to fill those gaps through executive development or recruitment.
- Ensure the board develops an independent perspective on succession and the pipeline of talent.
- Review with the CEO the performance of his or her direct reports.
- Ensure the board has the opportunity to interact, both formally and informally, with high potential senior executives.

Guideline 13. Develop and oversee executive compensation plans

Senior executives should be compensated fairly and reasonably, with a large component of compensation being performance-based. Executives also should have meaningful shareholdings in the company to more closely align their interests with shareholders and the long term sustainable value of the company.

A HIGH PERFORMANCE BOARD ENGAGES WITH SHAREHOLDERS

Guideline 14. Report governance policies and initiatives to shareholders

Boards need to make every effort to help shareholders understand the board's governance policies and how the board fulfills its responsibilities to effectively oversee management.

Expected best practices

- Ensure that the proxy circular describes the corporation's governance practices in sufficient detail for shareholders to ascertain whether the corporation complies with the guidelines in this document.
- Include a discussion of the corporation's governance philosophy, policies, practices and monitoring processes in the proxy circular and indicate whether its standards meet or exceed regulatory requirements.
- Disclose in the chair's section of the annual report any substantive issues, changes and developments in governance practices at the corporation that could affect shareholder interests.
- Ensure the chair of each committee is available to answer questions at the annual general meeting and any other significant shareholder meetings.
- Ensure that the name and contact information of a director that shareholders and other stakeholders can contact is made available in the proxy circular and on the corporation's website.

Guideline 15. Engage with shareholders

Shareholders and boards should have regular, constructive engagement meetings. Engagement between shareholders and boards allows each group to explain its perspectives on governance and disclosure practices. It also allows boards to obtain feedback on their governance practices directly from the shareholders to whom they are accountable and allows boards to explain the reasoning behind their chosen governance practices to shareholders.

Expected best practices

- Provide opportunities for shareholders to have access to directors outside of the annual meeting in order to discuss issues that concern either party.
- Provide the name and contact information of a director for shareholders and other stakeholders to contact in the proxy circular and on the corporation's website.

4. EXECUTIVE COMPENSATION PRINCIPLES

- Introduction / Overview
- Principles Explained
  - PRINCIPLE 1: Executive compensation should be “at risk” and based on performance
  - PRINCIPLE 2: Performance should be based on key business metrics
  - PRINCIPLE 3: Executives should build equity
  - PRINCIPLE 4: Ensure benefit entitlements are not excessive
  - PRINCIPLE 5: Compensation structure should be simple
  - PRINCIPLE 6: Boards and shareholders – actively engage

OVERVIEW OF EXECUTIVE COMPENSATION

These principles are set to provide enhanced guidance to boards and to promote compensation decisions that are aligned with long-term company and shareholder success. Determining and structuring long-term compensation plans is a complex, multi-year process for boards that is constantly evolving. Compensation plans have many objectives measured over a multi-year time horizon, including:

- Ensuring that compensation decisions are highly correlated to long-term performance
- Enhancing the alignment of interests between executives and shareholders
- Mitigating the risk of unintended outcomes or the creation of inappropriate incentives
- Attracting, motivating and retaining top talent

The focus of the following principles is on “pay for performance” and the integration of risk management functions into the executive compensation philosophy and structure.

While proxy disclosure is limited to the top five executives, boards are expected to ensure these principles are used in determining compensation practices throughout the company. The compensation programs for senior executives set the tone and should reflect a company’s overall compensation philosophy and risk profile.

The board and the compensation committee of every public company are responsible for, and accordingly must be actively involved in, establishing and independently verifying compensation philosophy, setting performance measures and assessing performance.

PRINCIPLE 1

A significant component of executive compensation should be "at risk" and based on performance

- A large percentage of the total compensation of senior executives should be a reflection of business performance achieved and should be linked to the risks taken during the relevant time period. Performance should be measured on an absolute basis and relative to a fully-considered list of company peers. The pay for performance component should be truly variable and dependent on performance and not be deferred base salary. Performance awards should be based on intrinsically risk-adjusted financial and non-financial measures and should include share-based awards such as Performance Share Units (PSUs) or a mixture of PSUs and time-vesting Restricted Share Units (RSUs), with a greater emphasis on performance as the primary vesting mechanism.

Use of Stock Options

- Shareholders generally are discouraging the use of time-vested-only stock options as a significant component of executive compensation, arguing that options may encourage inappropriate risk-taking and lead to unintended reward outcomes that are not well aligned with long-term performance. Another criticism levied at stock options is that they allow management to participate in share performance upside while not suffering any consequences on the downside. In addition, recent research has highlighted the fact that the value of stock options may be quite volatile and often reflective of market-specific rather than company-specific factors.
- Where stock options are used, they should be de-emphasized in favour of other forms of equity-linked compensation and serious consideration should be given to introducing performance-vesting provisions. Performance-vesting provisions are a means of mitigating the risk of rewarding executives for share performance clearly driven by factors beyond management's control. Boards also should be mindful of minimizing the dilutive impact of a stock option program.

PRINCIPLE 2

"Performance" should be based on key business metrics that are aligned with corporate strategy and the period during which risks are being assumed.

- Performance-based compensation should be based on successfully achieving strategic goals over the short, medium and long term. These goals should be identified in advance, and the board should be allowed to use its informed judgment to alter payouts to ensure that compensation reflects the performance of the business, both in absolute terms and relative to a fully-considered peer group. Payments of performance-based compensation should be aligned with the period of time over which results are achieved and the related risks are assumed.

Performance Metrics

- The board should determine a number of relevant performance metrics and develop a compensation plan that is linked to achieving those metrics. The board should be actively engaged in setting performance goals, determining the appropriate level of stretch and assessing performance against the company's goals. The metrics should include broad corporate financial metrics as well as individual and/or corporate measures key to managing risk. Chosen performance metrics should also reflect the key strategic goals of the business as determined by the board, capturing a range of dimensions of long-term corporate performance. Companies should disclose these larger strategic goals and explicitly show the linkage between strategy and the chosen performance metrics. Care must be taken to weight the metrics appropriately to avoid unintended payouts when the company performs poorly but meets some of the metrics. Executives, directors and shareholders must be able to clearly understand the corporate goals that management is being incented to achieve.

Link Compensation and Management of Business Risks

- The board should integrate the company's enterprise risk management program into its compensation plans. Compensation plans should reward appropriate risk-taking consistent with the risk profile of the company as presented to shareholders. Compensation plans should also focus on maintaining the quality and sustainability of earnings over the long term. The time period over which compensation is paid should be aligned with the period in which performance is achieved and the associated risks are assumed.
- Variable compensation components should include caps to ensure an appropriate sharing of value between management and shareholders and to limit the incentive to take excessive risks in order to achieve short term, unsustainable performance.

PRINCIPLE 2

Scenario Analysis

- Boards should formally "stress test" compensation plans to ensure that rewards are appropriate in different scenarios and that there are no windfalls for unsustainable performance. The board should ensure that there is an ongoing link between compensation and business performance, and that there is significant leverage in the compensation package to reward exceptional performance. Stress testing allows the board to determine the reasonableness of compensation if unexpected or unintended positive or negative events occur and to adjust the design of compensation plans to avoid extreme results.

Quantum

- In determining the overall quantum of compensation to award, boards often place significant emphasis on the relative positioning of total compensation against a list of industry peers on the basis that talent retention is the primary concern. While these external considerations are important, overreliance on these factors can lead to ever-increasing compensation levels unrelated to performance, particularly where total compensation is specifically targeted at percentile ranges beyond the median of the peer group. Similar concerns also have led some boards to grant substantial awards even during periods when corporate performance has not met expectations. Absent extenuating circumstances, quantum of compensation awarded should be determined within the context of the organization as a whole and justified primarily by performance. Consideration also should be given to the realized value of previous award grants in determining current compensation levels. Boards should reassess regularly how effective the compensation program has been at achieving the company's strategic objectives.

Payments When Targets are Exceeded or Missed

- If performance targets are significantly exceeded, compensation above target levels may be warranted, provided that compensation is similarly reduced in the event that performance is below target. In other words, there should be symmetry or balance between the upside and the downside of performance based compensation. In some cases, the negative impact to the company of failing to achieve a performance target may be greater than the positive impact of exceeding it. If so, consideration should be given to more severe compensation consequences for failure to meet the target relative to the benefit of exceeding it

PRINCIPLE 2

Recoupment Policies

If a company pays a bonus to an executive on the apparent achievement of performance metrics in a particular year, and it later becomes clear that the metrics were not achieved, the company should ensure it has a specific right to require the return of the bonus and to cancel unvested compensation awards. This result typically is affected through a formal recoupment or "claw back" policy in the company's code of business conduct.

It also may be appropriate for boards to require the return of compensation previously awarded to an executive in the event of a material earnings restatement or other company-specific change that significantly reduces shareholder value. It generally is preferable to align payouts with the period in which risks are realized and to use intrinsically risk-adjusted economic efficiency measures and equity based compensation, rather than to rely on a recoupment policy.

Consider Realized or Current Value of Past Compensation Awards

In determining annual equity-based awards, boards should be aware of the current or realized value of past equity-based compensation granted to the executives and should disclose this information annually in the company's proxy circular. Particular consideration should be given to instances where extraordinary events unrelated to the performance of the executives have led to unintended pay outcomes. Companies should also include a "lookback" table in the circular that compares the disclosed value of compensation awarded in past years with the realized and current value of those same awards.

Allow for Board Discretion

When performance metrics are used to determine the degree of vesting or the amount of an award, the board should be very hesitant to provide "exemptions" or substitute other forms of compensation when one or more metrics are not met in a particular year. In cases where performance metrics used indicate that a substantial payout is warranted, boards should consider the extent to which the performance may have been favourably impacted by factors outside of management's control and in such instances boards should not hesitate to consider downward adjustments to award levels. The board should maintain the ability to use informed judgment to alter awards in unusual or unanticipated situations. If such discretion is used, the board should fully disclose in the company's proxy circular the fact that it has exercised its discretion and the reasons why it has done so.

PRINCIPLE 3

Executives should build equity in the company to align their interests with those of long-term shareholders

- In order to align the interests of long-term shareholders and management, executives should be required to hold a significant portion of their net worth in shares of the company while employed and ideally for a period of time after cessation of employment. Consideration also should be given to requiring an executive to hold some or all shares issued on the exercise of stock options. The requirement to build equity is often stated as a multiple of base pay or total compensation, with both the multiple and absolute value increasing with the level of an individual's seniority within the organization.
- If there is a significant sustained drop in the company's share price, the board should not directly or indirectly "re-price" stock options. Option exercise prices are not increased when share prices rise, and they should not be reduced when share prices drop – this tenet is considered fundamental to aligning the interests of management with the interests of long-term shareholders.

Hedging and Monetization

- Companies should prohibit directors and executives from directly or indirectly hedging or monetizing the value of shares held in the company, as such actions reduce the alignment with shareholder interests that these programs are intended to create. In instances where the board allows an individual to hedge or monetize some portion of his or her holdings on an exception basis, the rationale for granting the exception and the financial impact on the individual's overall share holdings in the company should be fully explained in the proxy circular and in the appropriate regulatory filings.

PRINCIPLE 4

A company may choose to offer pensions, benefits and severance and change-of-control entitlements. When such perquisites are offered, the company should ensure that the benefit entitlements are not excessive.

Pensions

- Some companies provide retirement allowances to their executives above statutory pension maximums (usually called Supplementary Executive Retirement Plans or SERPs) based, for example, on average cash compensation in the five years before retirement and on the number of years worked at the company. Boards should impose an annual limit on SERP payments on retirement to ensure that the total pension entitlement is reasonable in the context of the business and does not amount to additional non-performance linked compensation. If "bonus years worked" are awarded, the board should disclose this fact and the reasons why it has done so in the company's proxy circular.

Termination Payments

- In Canada, if there is no specific contractual provision, employment can be terminated by an employer "without cause" by providing "reasonable" notice to the employee or the payment of "compensation in lieu of notice" (so called "severance"). "Cause" has been very narrowly defined by the courts. The amount of compensation in lieu of notice a court will award for a termination without cause varies within a range depending on factors such as length of service, position, compensation level and age. If a company has a written employment agreement with an executive, it should ensure that the termination provisions are reasonable and are not overly generous in order to avoid "pay for failure". Companies should ensure that employment arrangements with executives provide only reasonable payments on termination and that unvested deferred compensation is forfeited on termination.

Change of Control Provisions

- It is common for the employment contracts of senior executives to include financial provisions intended to ensure that executives are neutral on a change of control and motivated to act in the best interests of shareholders.
- Any change of control provision should have a "double trigger" requirement, meaning that an actual legal change of control has occurred, and the executive has been terminated by the company during a specified time period following the change of control. Severance payments on a termination after a change of control should be substantially the same as are payable on a normal dismissal without cause, although it may be appropriate to provide for accelerated vesting of deferred compensation in this circumstance.

PRINCIPLE 5

Compensation structure should be simple and easily understood by management, the board and shareholders

- Compensation plans have become very complicated: they often have multiple components incorporating different time horizons, objectives and metrics. A variety of programs may be needed to pay for performance over the appropriate risk time horizons and that tax constraints are a relevant consideration. While a certain level of complexity may be unavoidable, the compensation structure should be simple and easily understood by the board and management, and the board must in turn clearly explain the key elements of the compensation structure and the process for determining variable compensation awards in sufficient detail in order that shareholders can understand it and can consider whether the approach to compensation is appropriate.

Use of External Consultants

- Boards often will engage the services of an external consultant to assist in designing compensation programs or to identify an appropriate peer group for compensation benchmarking purposes. When external consultants are retained by the board, the board, as a governance best practice, should ensure that the consultant is independent of management. In any event, while the input received from independent compensation consultants may provide valuable assistance to the board, it does not necessarily validate the approach to executive compensation nor does it reduce the board's responsibility to ensure that compensation decisions are appropriate and closely aligned with performance.

PRINCIPLE 6

Boards and shareholders should actively engage with each other and consider each other's perspective on executive compensation matters

- Regular shareholder engagement provides the opportunity for boards to hear the perspectives of investors on a range of matters. It is recommended that companies hold an annual 'Say on Pay' advisory vote, which is an effective means of soliciting direct feedback from shareholders on the company's approach to executive compensation. While the vote is non-binding, the board should take the results of the vote into account, as appropriate, when considering future compensation policies, procedures and decisions and in determining whether there is a need to significantly increase their engagement with shareholders on compensation and related matters. The board also should ensure that detailed voting results on the 'Say on Pay' advisory vote are fully disclosed, for the benefit of all shareholders.
- In the event that a significant number of shareholders oppose the 'Say on Pay' resolution, the board should consult with opposing shareholders in order to understand their concerns and review the company's approach to compensation in the context of those concerns. Boards also should follow up with shareholders on any significant year-over-year declines in support for its 'Say on Pay' resolution, regardless of the overall level of support achieved. Shareholders who intend to vote against a 'Say on Pay' resolution or have major issues with the company's approach to executive compensation should contact the board to discuss their concerns. The board should disclose to shareholders as soon as is practicable a summary of the significant comments relating to compensation received from shareholders in the engagement process and an explanation of any changes to the compensation plans made or to be made by the board or why no changes will be made.

5. GOVERNANCE DIFFERENCES OF EQUITY CONTROLLED CORPORATIONS

- Overview of Equity controlled Corporations
- Definitions used
- Guidelines 1-7

EQUITY CONTROLLED CORPORATIONS

Guidelines to help ensure that the board of a public company:

- is accountable and independent
- has experienced, knowledgeable and effective directors committed to the highest level of integrity
- has clear roles and responsibilities, and
- engages with its shareholders.

Many large Canadian corporations are controlled by a family, a parent company or a group of shareholders through their holdings of common shares. Effective equity control can come from holding as little as 20% of the common shares of a widely held company.

These guidelines relate only to those corporations which are controlled through the ownership of common shares, and not to corporations which are controlled by virtue of multiple-voting or dual class share structures.

In general, a controlling shareholder may have a legitimate interest in being actively involved in the board of directors of the corporation. In fact, many institutional investors expect shareholders that control a corporation by virtue of their equity holdings to have substantial influence over the strategic direction of the company, the election of some of the directors, the appointment of executives, the financial affairs of the business and executive compensation. While the representation of the controlling shareholder on the board and its influence over the corporation is often valuable, representation generally should be proportional to the controlling shareholder's equity holdings. A board always should have a meaningful number of independent directors who are not related to the controlling shareholder or management.

All public companies should strive to have their governance practices go beyond legal minima to ensure excellence.

REVISED GUIDELINES

Guideline #1 - Shareholder Democracy

- Controlled Corporations should allow shareholders to vote "for" or "against" each individual director nominee and promptly disclose the detailed vote results following each election. The board of a Controlled Corporation should commit publicly to adopt immediately the Majority Voting Policy if the Controlling Shareholder ceases to control 50% or more of the common shares.
- The nominating committee of a Controlled Corporation should have a process to receive and discuss suggestions from shareholders for potential director nominees.
- Boards of all public companies should facilitate shareholders' ability to effectively vote their shares "for" or "against" individual directors by adopting the Majority Voting Policy. Only directors who receive a majority of votes in their favour will be elected to a board.

The Majority Voting Policy commits a board to hold director- by-director elections, promptly disclose the detailed results of each election, and require a director who receives more votes "withheld" than "for" to tender his or her resignation to the board.

Generally, Controlled Corporations should allow shareholders to vote "for" or "against" each individual director nominee. However, if a Controlling Shareholder holds 50% or more of the common shares, it is highly unlikely that more votes for an individual director will be "withheld" than are voted "for" and therefore adopting the Majority Voting Policy would rarely lead to the resignation of a director. Accordingly, its believed that the board of a Controlled Corporation should adopt a board policy that commits the Controlled Corporation to:

  - allow shareholders to vote for each individual director
  - disclose the results of director elections promptly after each annual meeting, and
  - immediately adopt the Majority Voting Policy if at any time the Controlling Shareholder controls less than 50% of the common shares.

- The board of a Controlled Corporation also should ensure that it has processes in place to allow interested minority shareholders to nominate directors and that those nominations are formally considered by the board's nominating committee.

Guideline #2 - Board Composition

The number of Related Directors of a Controlled Corporation should not exceed the proportion of the common shares controlled by the Controlling Shareholder, to a maximum of two thirds. However, if the CEO is related to the Controlling Shareholder, then at least two thirds of the directors of a Controlled Corporation should be Independent Directors.

- For Controlled Corporations, it can be valuable to the company for Related Directors to sit on the board, but the number of Related Directors should be proportional to the common share ownership of the Controlling Shareholder, to a maximum of two thirds.
- However, if the CEO of the Controlled Corporation is Related to the Controlling Shareholder, the other Related Directors also are not independent of management. In those circumstances, in order to ensure the independent oversight of management, proper management of conflicts of interest and the protection of the interests of minority shareholders, two thirds of the board of the Controlled Corporation should be Independent Directors.

Guideline #3 - Independent Chair

- The Chair of the Board and CEO of every public company that is not a Controlled Corporation should be separate roles held by different people, as these roles have different responsibilities and functions.
- If a Controlling Shareholder controls at least 50% of the common shares of a Controlled Corporation, the CEO and Chair roles may be combined, or the CEO may be the Controlling Shareholder or related to it, provided that there is a lead director who is an Independent Director and the board has an effective and transparent process to deal with any conflicts of interest between the Controlled Corporation, minority shareholders and the Controlling Shareholder.
- In every public company that is not a Controlled Corporation, the roles of board Chair and CEO are fundamentally different and should be held by different individuals. The Chair should always be independent of management and should not participate in management or have a material relationship with management or the corporation that would lead a reasonable person to believe that he or she is not truly independent. In a widely held public company, an independent Chair plays an integral role in providing the necessary impartial oversight of management.
- If a Controlling Shareholder controls at least 50% of the common shares of a Controlled Corporation, the influence of the Controlling Shareholder may make the appointment of an independent Chair impracticable. In such Controlled Corporations, the roles of CEO and Chair may be combined or the Chair may be a Related Director who is also actively involved in management of the business (sometimes called an “Executive Chair”).

The lead director should be appointed by the Independent Directors. The lead director's role should be to set board agendas with the Chair and CEO, be responsible for the quality of information sent to the directors, chair in camera meetings when needed and be the liaison between the Controlling Shareholder and the Independent Directors. The lead director should also be a conduit for shareholders to raise issues of concern and should be available to engage with shareholders appropriately. The lead director should be the person responsible for ensuring that there are appropriate procedures in place to identify and manage conflicts of interest between the Controlled Corporation, minority shareholders and the Controlling Shareholder.

- If the CEO and Chair roles have been combined or if the CEO is related to the Controlling Shareholder, the board should disclose to shareholders why it has adopted that structure and why it believes that it is in the best interests of the corporation and all of its shareholders. The board should continually monitor the effectiveness of that structure and the role of the lead director and consider modifying it if necessary.

Guideline #4 - Related Directors on Board Committees

- At least one member of each board committee of a Controlled Corporation should be an Independent Director.
- All members of the compensation committee should be independent of management of the Controlled Corporation. In addition, if the CEO is related to the Controlling Shareholder, no more than one member of the compensation committee should be a Related Director.
- National Instrument 52-110 Audit Committees generally provides that no member of the audit committee may be a Related Director. Given their connection to the Controlling Shareholder, Related Directors can bring an important perspective to the audit committee which may add value to the Controlled Corporation.
- Similarly, boards of public companies that are not Controlled Corporations usually have compensation and nominating committees comprised entirely of Independent Directors. It is appropriate for Related Directors who are independent of management to sit on the compensation or nominating committees of a Controlled Corporation to bring the knowledge and perspective of the Controlling Shareholder to executive compensation, appointments and board nominations. However, if the CEO is related to the Controlling Shareholder, the compensation committee should include no more than one Related Director, and he or she should not participate in discussions about the CEO. This procedure will ensure that the compensation of the CEO is determined by Independent Directors.
- The participation of Related Directors on board committees could give rise to conflicts of interest between the Controlled Corporation and the Controlling Shareholder which may require Related Directors to recuse themselves. As a result, boards should consider carefully each committee's quorum requirements to ensure that a single director is never asked to approve a conflict of interest transaction. If conflicts arise frequently the board should consider creating a conflict of interest committee made up entirely of Independent Directors to address conflicts on behalf of the board.

Guideline #5 –Assess the CEO and Plan for Succession

- If the CEO is Related to the Controlling Shareholder, the board's process to evaluate the performance, leadership, compensation and succession of management should be led by Independent Directors.
- Where the CEO is Related to the Controlling Shareholder, the board of a Controlled Corporation should put in place an objective and independent process to consider executive appointments, performance evaluations, compensation and succession planning that is led by Independent Directors. This procedure will ensure that those decisions are not unduly influenced by the Controlling Shareholder and reflect the views of the entire board.

Guideline #6 - Shareholder Engagement

- The board of a Controlled Corporation should encourage Independent Directors and Related Directors to engage with the company's shareholders to discuss relevant governance issues.
- In the case of a Controlled Corporation, minority shareholders should be able to engage both with the Independent Directors as well as the Related Directors, either together or separately as may be appropriate for the issues to be discussed.

Guideline #7 - Say on Pay

- Every public company, including Controlled Corporations, should hold an annual shareholder advisory vote on compensation and publicly disclose the detailed vote results.
- A board's approach to executive compensation is an important indication of the board's governance of the company. As a result, its believed that every public company, including Controlled Corporations, should hold an annual 'say on pay' advisory vote and publicly disclose the detailed vote results. Although for some Controlled Corporations the result of that vote may be dictated by the Controlling Shareholder, it is an important vehicle through which minority shareholders can express their view on the board's approach to executive compensation.

6. MAJORITY VOTING

- Guidelines
  - "Plurality" Voting Required by Law
  - What is "Majority Voting"?
  - Company Examples
  - Board Majority Voting Policy
  - Filling a Vacancy
  - Terms of a "Majority Voting" Policy
- Suggested Form of Majority Voting Policy

GUIDELINES

The adoption of majority voting is a three-step process:

1. List individual directors on the Registered Form of Proxy or the Voting Instruction form.
2. The Board adopts an internal policy which states that for any director receiving 50% + 1 withheld votes, those votes would be considered votes "against" the director.
3. Once a resignation is submitted, the Corporate Governance Committee (or equivalent) reviews any extra circumstances surrounding the voting results and makes a decision whether or not to accept the resignation. The Committee's decision is made public.

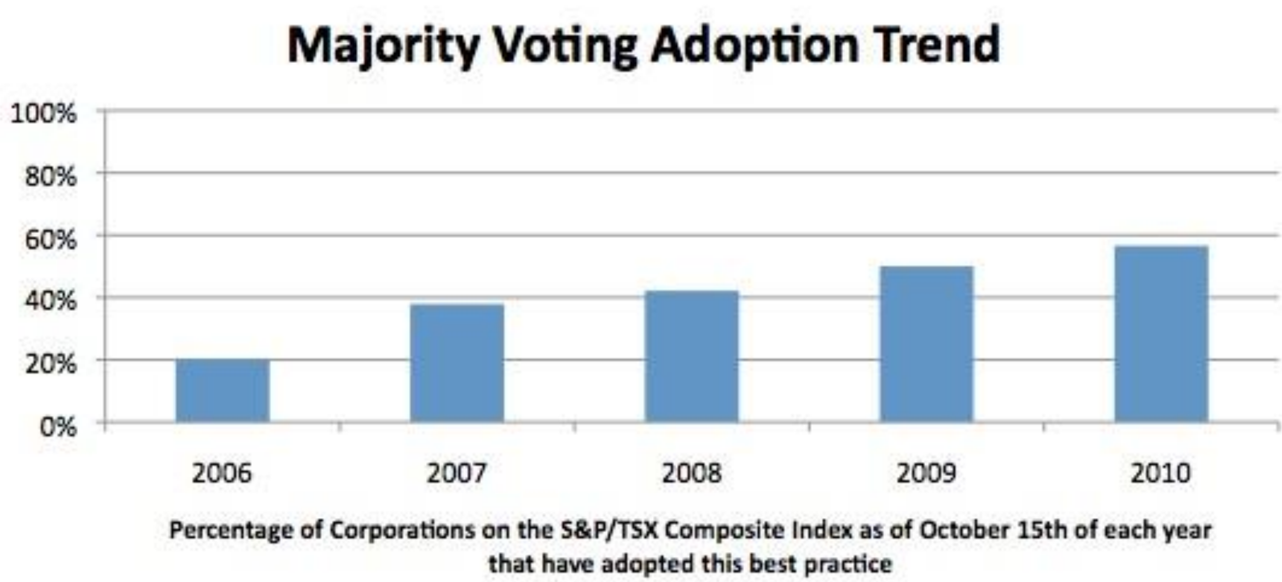
“Plurality” Voting Required by Law

- Under Canadian law, voting for directors by shareholders of a public corporation is based on a "plurality system" under which a shareholder can either vote "for" a director nominee or "withhold" his or her vote. “Withhold” votes do not count and a director needs only one "for" vote to be elected to the board, even if all other votes are “withheld”. If a director nominee is a shareholder, in theory the only “for” vote needed for the nominee to be duly elected to the board is his or her own vote.
- The plurality system for the election of directors is not in the best interests of shareholders as it does not permit shareholders to vote against an underperforming director and allows an entrenched board to continue to be in charge of the company, even if they are opposed by a majority of the owners of the company. The only option for shareholders who wish to effectively vote against one or more directors is to undertake a costly and confrontational public proxy fight.
- The board of directors of a public issuer has a responsibility to ensure that shareholders have the opportunity to vote for each director on an annual basis and that the vote is conducted fairly.
- In most cases, the individuals nominated by the board (often called “management nominees”) receive substantial support from shareholders. Prior consultation or engagement by the board with investors before putting forward management nominees can minimize the possibility of shareholders withholding votes for one or more management nominees.
- While this policy is focused on issuers formed as corporations, it should also be applied to other forms of issuers (such as trusts) to ensure that the persons representing the equity holders have the confidence of a majority of the owners of the issuer.

What is "Majority Voting"?

- Each director of a corporation should have the confidence and support of a majority of its shareholders and that this should be a legal requirement for every public issuer in Canada.
- Until the law is amended in Canada to require true majority voting for directors, the practice that has developed at many leading issuers of effectively implementing majority voting through a board "majority voting policy" is supported. A majority voting policy ensures that shareholders can vote separately for each nominee and that, if a director nominee has more "withhold" votes than votes in favour, the nominee will be considered not to have received the support of a majority of shareholders, even though duly elected as a matter of corporate law. Such a nominee would immediately tender his or her resignation to the board, which the board would be expected to accept absent extraordinary circumstances.

https://clarksoncentre.wordpress.com/2010/10/20/trend-watch-how-are-directors-elected/



Board Majority Voting Policy

- Many boards have implemented majority voting by adopting a board policy that applies to all current directors and future nominees to the board which provides flexibility for the board to deal with problematic situations. For example, if a director who does not get the support of shareholders is a corporate executive or chair of the board or of a significant board committee, time might be required for the board to make appropriate transitional arrangements. As well, there may be rare circumstances where accepting a resignation immediately would result in a lack of quorum of directors in office.

Filling a Vacancy

- If a director resigns because he or she receives more votes "withheld" than "for", the board has several options as to how the resigning director is replaced. For example, the board can leave the vacancy open until the following annual meeting, fill the vacancy with a suitable candidate or call a special shareholder meeting to elect a new director.

Terms of a "Majority Voting" Policy

To ensure effective shareholder democracy in the election of directors, It is recommended that the board of every public company adopt a majority voting bylaw or board policy that applies to the board and to all future director nominees. The bylaw or policy should include the following key provisions:

1. The company will list each individual director separately on the Form of Proxy or the Voting Instruction Form to allow shareholders to vote for each director individually.
2. The company will promptly disclose the results of the vote director by director. If the vote is by a show of hands rather than by ballot, the company will disclose the number of shares voted by proxy in favour or withheld for each director and the outcome of the vote by a show of hands.
3. If a director has 50% + 1 of the total votes "withheld" from him or her, the withheld votes will be considered "No" votes and the director will be expected to immediately tender his or her resignation to the board, which will be referred to the board or its nominating/corporate governance committee (or equivalent) for consideration.
4. The board will promptly accept the resignation unless it is determined that there are extraordinary circumstances relating to the composition of the board or the voting results that should delay the acceptance of the resignation or (in very rare cases) justify rejecting it.
5. The board will make its decision and reasons available to the public.

SUGGESTED FORM OF MAJORITY VOTING POLICY

Majority Voting Policy

- The board believes that each director should have the confidence and support of the shareholders of the corporation. To this end, the board has unanimously adopted this policy and future nominees for election to the board will be required to confirm that they will abide by this policy.
- Forms of proxy for the election of directors will permit a shareholder to vote in favour of, or to withhold from voting, separately for each director nominee. The Chair of the Board will ensure that the number of shares voted in favour or withheld from voting for each director nominee is recorded and promptly made public after the meeting. If the vote was by a show of hands, the company will disclose the number of shares voted by proxy in favour or withheld for each director.
- If a director nominee has more votes withheld than are voted in favour of him or her, the nominee will be considered by the board not to have received the support of the shareholders, even though duly elected as a matter of corporate law. Such a nominee will be expected to forthwith submit his or her resignation to the board of directors, effective on acceptance by the board. The board will refer the resignation to the nominating/corporate governance committee (or equivalent) for consideration.
- The board will promptly accept the resignation unless the committee determines that there are extraordinary circumstances relating to the composition of the board or the voting results that should delay the acceptance of the resignation or justify rejecting it. In any event, it is expected that the resignation will be accepted (or in rare cases rejected) within 90 days of the meeting.
- Subject to any corporate law restrictions, the board of directors may
    1. Leave a vacancy in the board unfilled until the next annual general meeting,
    2. fill the vacancy by appointing a new director whom the board considers to merit the confidence of the shareholders, or
    3. call a special meeting of shareholders to consider new board nominee(s) to fill the vacant position(s).
- This policy does not apply where an election involves a proxy battle.

7. DIRECTOR COMPENSATION

- DIRECTOR COMPENSATION POLICY
  - Principle One – Independence and Alignment with Shareholders
  - Principle Two – Reflect Expertise and Time Commitment
  - Principle Three – Compensation may vary for different Director Roles
  - Principle Four – Shareholding by Directors
  - Principle Five - Minimize Complexity and Ensure Transparency
  - Principle Six - Consider Shareholder Approval of Aggregate Director Compensation Limit

DIRECTOR COMPENSATION POLICY

Principle One – Independence and Alignment with Shareholders

Director compensation should be designed to promote a high degree of objectivity, independent thinking and a direct alignment with the interests of the shareholders and other stakeholders of the company. While director compensation should be sufficient to adequately reward directors for their expertise and experience and the time devoted to the company, it should not be so high as to potentially compromise the independence of directors, their ability to take a controversial stand on an important issue or their preparedness to resign on a matter of principle.

Principle Two – Reflect Expertise and Time Commitment

Aggregate director compensation and the structure of director compensation plans will vary, depending upon company-specific factors such as company size and complexity. Individual director compensation should reflect the time expected of the director as well as the overall expertise and experience required.

Annual grants of compensation to a director may vary from year to year based on the director's actual time commitment to the Board (often reflected in per meeting fees). In instances where there is an equity-based component of compensation, the amount should not be determined based on corporate performance, as that may compromise the objectivity of directors as stewards of the company on behalf of shareholders.

Director compensation should include appropriate director indemnity and insurance coverage and the reimbursement of reasonable out-of-pocket expenses (such as travel and educational costs), but should not include retirement benefits, change of control or severance provisions, health care coverage, charitable donations, vehicles, clubs, pensions, or other such perquisites.

Principle Three – Compensation may vary for different Director Roles

There should be no distinction in pay for directors performing similar roles. Some differentiation of compensation levels among directors based on relative time commitment and responsibilities may be appropriate. For example, independent chairs, lead directors and committee chairs typically entail a greater time commitment and may warrant additional compensation. In addition, particularly time consuming committees such as the Audit Committee and, increasingly, the Human Resources Committee may justify higher per meeting fees. Participation in ad hoc committees would also usually warrant additional compensation for a director.

Principle Four – Shareholding by Directors

`Minimum shareholding requirements for directors (achievable over a predetermined time frame) establish and maintain an alignment of interests between directors and shareholders by requiring directors to have a meaningful investment in the company. Directors should ideally acquire an equity stake in the company upon joining the board and add to that stake over time. Boards should consider requiring a minimum shareholding for directors based on a multiple of their annual compensation, until their retirement from the board.

Director compensation plans can facilitate the achievement of minimum director shareholding requirements and encourage directors to continue to invest in the company beyond the minimum level. Share grants or units with the same economic interest as shares (often called "Deferred Stock Units", or "DSU's") are appropriate forms of equity-based compensation for directors in lieu of cash as they directly align the interests of directors with those of shareholders. Equity-based remuneration should not be subject to vesting periods or performance conditions, other than, for example, Deferred Stock Units which require for Canadian tax purposes that the units be held until retirement from the board.

Principle Five - Minimize Complexity and Ensure Transparency

Boards should minimize the complexity of director compensation structures to ensure that the incentives being created are well understood by directors and shareholders. The process used by a board in setting its compensation should be transparent to shareholders and communicated as a part of the annual reporting process.

Principle Six - Consider Shareholder Approval of Aggregate Director Compensation Limit

Directors, as fiduciaries, should consider periodically seeking approval from their shareholders for directors' compensation. As is currently the case for financial institutions subject to the Bank Act, this could be achieved by the approval from time to time of an annual aggregate limit for director compensation.

8. BOARD ENGAGEMENT PROGRAM

- Engagement between Boards and Shareholders
  - Engagement by Boards with Shareholders
  - Board Policy on Shareholder Engagement
  - Model Board Policy

ENGAGEMENT BETWEEN BOARDS AND SHAREHOLDERS

Regular and constructive engagement between an issuer's shareholders and its board of directors is of primary importance. Responsibility lies with both shareholders and boards.

Engagement by Boards with Shareholders

Institutional shareholders should have regular, constructive engagement with the boards and compensation committees of public companies to explain their perspectives on governance, compensation and disclosure matters, and to discuss the company's practices in these areas.

It was found that boards have welcomed this direct, constructive interaction with large shareholders and agree that it leads to a better alignment of the interests of shareholders, the board and management. Where engagement meetings focus on executive compensation or other matters directly relating to management, these meetings will normally be held without management present.

Board Policy on Shareholder Engagement

It is recommended that each board of directors adopt a written policy on how they intend to engage with their shareholders and disclose the policy to its shareholders. Shareholder engagement can be done in a variety of ways and boards will likely implement a mix of approaches.

Model Board Policy

- Set out below is a sample board policy for consideration by boards and their advisers

Policy of the Board of Directors on Engagement with Shareholders on Governance Matters

- The board of directors believes that it is important to have regular and constructive engagement directly with its shareholders to allow and encourage shareholders to express their views on governance matters directly to the board outside of the annual meeting. These discussions are intended to be an interchange of views about governance and disclosure matters that are within the public domain and will not include a discussion of undisclosed material facts or material changes.
- The board will develop practices to increase engagement with its shareholders as is appropriate for its shareholder base and size.
- The board recognizes that shareholder engagement is an evolving practice in Canada and globally, and will review this policy annually to ensure that it is effective in achieving its objectives.

LINK NATURAL RESOURCES FZC

SAM MCKAY
PRESIDENT, CEO
LINK NATURAL RESOURCES (FZC)
C1 – 619
PO BOX – 21101
AJMAN FREE ZONE
AJMAN, UAE

+971 502615839 (MOBILE)
+971 6 7477588 (OFFICE)

SAMMCKAY@LINK-NATURAL-RESOURCES.COM
WWW.LINK-NATURAL-RESOURCES.COM