WHAT DOES THE MARKET SAY ABOUT SAY-ON-PAY? A LOOK AT THE CANADIAN BANK EXPERIENCE

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Abstract

This paper explores the share price reaction to a recent news announcement that Canadian banks were adopting say-on-pay, a policy that gives shareholders an annual non-binding vote on executive compensation. Using event study methodology, the effect of adopting this new policy is explored and found to be associated with a significant increase in share price. This result suggests that giving shareholders a voice on executive compensation is expected to generate economic benefits, which adds to the paucity of knowledge currently available to shareholders and legislators as they consider the consequences of say-on-pay.

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1. Introduction

Say-on-pay is a corporate policy that gives shareholders an advisory vote on executive compensation. The use of say-on-pay is increasing in Europe as more countries mandate it, and in other parts of the world as more shareholders demand it. The United States (U.S.) became the most recent nation to embrace this governance initiative when it enacted the Dodd-Frank Financial Reform law in 2010, requiring U.S. firms to hold a say-on-pay vote at least once every three years. However, the economic benefit of adopting say-on-pay has not been clearly established in the extant literature. Say-on-pay could be beneficial if it safeguards against excessive executive compensation. Yet it could be detrimental if the compensation contract is already optimal but say-on-pay adds an additional governance constraint. Finally, since the vote is not binding, adopting a say-on-pay policy could potentially have no impact whatsoever on the value of the firm. A recent development on say-on-pay is examined in this paper to explore whether the policy is expected to be beneficial. On the morning of February 26 2009, shareholders of Royal Bank of Canada adopted say-on-pay through a majority vote at their annual general meeting. About an hour later, the shareholders of Canadian Imperial Bank of Commerce did the same. Later that day, the board of directors at National Bank of Canada declared the adoption of say-on-pay in anticipation of its annual general meeting scheduled for the following day. These three became the first Canadian banks to adopt say-on-pay. The action quickly spread to the other four large Canadian banks, either through successful shareholder resolutions, or as banks voluntarily adopted say-on-pay to preempt its approval at their annual general meetings. This paper is an event study of the impact that say-on-pay had on the share price of the Canadian banks that adopted it. The analysis provides regulators and corporate governance interest groups with information regarding whether say-on-pay creates, destroys, or has no effect on firm value.

Much of the current literature on say-on-pay explores whether it leads to improvements in the firm's subsequent financial performance or to changes in executive compensation, but a few papers explore the share price reaction of firms adopting say-on-pay. This approach assumes an efficient capital market such that at the moment a firm announces its adoption of say-on-pay, the capital market estimates the economic effect of the new policy and bids share price up or down accordingly. This is the approach in Cai and Walkling (2011) who test whether the passage of a say-on-pay bill in the House of Representatives had an effect on the value of firms in the U.S., and find that the subset of firms they identified as likely to adopt it under shareholder pressure experienced a significant positive share price reaction. Wagner and Wenk (2011) explore whether the announcement of a public referendum on say-on-pay reform had an impact on the value of Swiss firms, and find a negative share price reaction.[1] The analysis

[1] The proposed legislation would have made say-on-pay votes binding for Swiss firms rather than being advisory in

in this paper responds to the policy paper by Magnan and Mangen (2009) who outline the potential costs and benefits of say-on-pay, and suggest that the economic effect of implementing this policy is important but not fully understood.

The setting for this paper is limited and specific, which has advantages and drawbacks. While the uniqueness of the setting reduces the generalizability of the results, there are four reasons to expect a share price reaction to be more readily established in this small sample of Canadian banks than in countrywide studies such as the ones cited above. First, say-on-pay is relatively new in Canada and is driven by shareholder activism rather than by regulation. One would therefore expect the firms specifically targeted for say-on-pay resolutions to be the ones for which adopting the policy would yield the greatest benefits, which should generate a stronger share price reaction. Second, the say-on-pay adoption occurred at the tail end of the financial crisis of 2008-2009. Although the crisis was less severe in Canada than in many countries, shareholders were likely to be concerned about the effectiveness of executive compensation contracts in the banking industry when the policy was adopted. If there were perceived benefits to say-on-pay, one would expect them to emerge in a sample of banks at this point in time. Third, the sequence of events that led to the adoption of say-on-pay by Canadian banks was specific, unanticipated, and well publicized, therefore the firms affected and the event dates are easy to establish, which should theoretically reduce the noisiness of the tests. Finally, testing firms that are relatively homogeneous with respect to industry, size, operations, price informativeness, and corporate governance characteristics reduces the need to control for a myriad firm-specific factors that would be required if the sample comprised the 80 Canadian firms that had adopted say-on-pay by May 2011.[2]

The capital market reaction to the banks' adoption of say-on-pay is assessed using event study methodology. In order to isolate the share price movement attributable to say-on-pay, other factors that affect share price are included as control variables in the event study model. The share price effect is estimated separately for each bank, and overall for the seven banks based on the dates each one adopted say-on-pay, as well as overall for the seven banks on the day the first three banks were forced to adopt the policy. This analysis treats the mechanism between policy adoption and share price movement as a "black box" since no attempt is made to explain why the markets expect say-on-pay to change the value of the firm. However, establishing that say-on-pay causes a change in share price adds to the paucity of knowledge about its economic effect, and is a first step in understanding the consequences of implementing this policy.

2. Data

Event studies involve estimating a regression model that has changes in share price as the dependent variable, and an explanatory variable that represents the date the event took place (in this case, the adoption of say-on-pay), as well as a set of control variables. The first critical task in any event study is to pinpoint the date that the event became public information. Shareholders in the banking industry had been proposing say-on-pay for some time before it was initially adopted by the first set of Canadian banks in February of 2009. However, in accordance with the Board of Directors' recommendations, the majority of shareholders had been voting against adopting the policy at their Annual General Meetings (AGMs). The Boards generally reasoned that executive compensation was already transparent and that the existing governance mechanism appropriately addresses compensation issues; that compensation decisions should remain with the Board to exploit their knowledge and experience instead of trying to accommodate the diverse views of shareholders; and that there were better avenues than say-on-pay for shareholders to express concerns about compensation issues.[3]

However, on the morning of February 26th, 2009, three Canadian banks unexpectedly announced they would adopt say-on-pay. Say-on-pay was forcibly adopted by Royal Bank of Canada and Canadian Imperial Bank of Canada as shareholder resolutions proposing the policy were voted in by majority support at their respective AGMs. Within a few hours of this event, National Bank of Canada voluntarily adopted say-on-pay in anticipation of it being instituted at its upcoming AGM. By late afternoon, the media was broadcasting news that three large Canadian banks had adopted say-on-pay. The impact of this event was not trivial. In an attempt to appease its shareholder, the CEO of Toronto-Dominion Bank agreed to forgo his $10 million golden parachute a few days later; and within a week, the CEO of the Bank of Montreal volunteered to reduce his pay by $4.1 million. The shareholders of three more large banks followed suit by voting for say-on-pay at their AGMs. Bank of Montreal and Bank of Nova Scotia voted for say-on-pay on March 3, 2009, while Laurentian Bank adopted it at its AGM on March 10, 2009. On March 18, Toronto-Dominion bank preempted its say-on-pay resolution by voluntarily adopting it ahead of its AGM, which was scheduled to take place two weeks later.[4]

nature. This is different from most say-on-pay programs, therefore the Wagner and Wenk (2011) results do not necessarily extend to other settings.

[2] Source: Report from the Canadian Coalition for Good Governance, available at: http://www.ccgg.ca/site/ccgg/assets/pdf/Shareholder_Democracy_Study_June_2011.pdf.

[3] See excerpts from AGM reports in Appendix A.

[4] See Appendix B for excerpts of the news releases discussed in this paragraph.

The second critical task in an event study is to control for other factors that could affect share price movement on the event date in order to isolate the price reaction that is attributable to the event. A firm's share price is primarily affected by macroeconomic events, therefore as with prior event studies, my model incorporate a market index to capture the effect of daily overall market fluctuations. In addition, a preliminary analysis of the data shows that the banks in my sample released some or all of the following information on the dates their say-on-pay was announced: dividend declaration on common stock, first quarterly financial results, and the issuance of a series of preferred shares. There are also a few occurrences of the banks concurrently releasing a press release about a change in interest rates on the same day that say-on-pay was announced. These news events could generate changes in share price that may be falsely attributed to say-on-pay unless the model factors out their influence, therefore variables are included in my model to control for the effect of these announcements. Finally, archived news releases were obtained from Lexis Nexis and scrutinized to verify that no other significant news event occurred in the weeks surrounding the banks' say-on-pay announcements. Except for Toronto-Dominion being associated with Bernard Madoff's Ponzi scheme in March of 2009, no noteworthy events occurred.

3. Methodology

Due to the multiple event dates and the need to control for concurrent news release, the event study model used in this paper is a market model augmented with indicator variables. This is an acceptable alternative to the standard event study methodology, which calculates excess returns as the prediction errors from a market model (see Campbell, 1997). The length of the data series is from January 2004 to December 2010 to ensure that several instances of each type of announcement listed above is included, allowing the say-on-pay effect to be more accurately estimated. The following model is estimated by ordinary least squares:

$$RET_t = \alpha + \beta_1 MKT_t + \beta_2 SAYPAY_t + \beta_3 DIV_t + \beta_4 PREF_t + \beta_5 BINCR_t + \beta_6 BDECR_t + \beta_7 CINCR_t + \beta_8 CDECR_t + \beta_9 UE1_t + \beta_{10} UE2_t + \beta_{11} DIVCHG_t + \beta_{12} PREFNUM_t + \varepsilon_t \quad (1)$$

where the dependent variable is the daily returns data (RET) collected from the CRSP database, which reflects changes in share price.[5] The first explanatory variable is the daily market index return (MKT), also available from CRSP. The coefficient on the MKT variable (β_1) represents the normal returns-generating process of the firm, and is commonly known as the firm's market beta. Returns in excess of this process are captured by the coefficients on the indicator variables that represent the dates of announcements explored in this paper. The say-on-pay indicator variable (SAYPAY) is set equal to one on the dates the banks declared adoption of the policy. A significant coefficient on the SAYPAY variable (β_2) indicates that the banks' adoption of say-on-pay had an effect on their share price. The direction of the coefficient tells us whether share price increased (positive coefficient) or decreased (negative coefficient) as a result of this governance initiative. Note that this paper explores several constructs for the SAYPAY variable. First, the SAYPAY variable is set equal to one on the date each respective bank announced the adoption of the policy (see Table 1 for a list of these dates), and estimated individually by bank to explore firm effects. The adoption of say-on-pay is also analyzed collectively by "stacking" all the bank observations into one matrix to estimate the mean effect. A third method of constructing the SAYPAY variable is devised in order to consider spillover effects. The extant literature (e.g., Connor, 1995 and Barberis et al., 2005) shows that when a firm releases information, there is a co movement of daily returns for similar firms in the industry. It is likely that when the first three banks adopted say-on-pay, the capital market expected other large Canadian banks to also be affected, and adjusted the share price of these other banks accordingly. Therefore the overall response when say-on-pay was initially announced is estimated by setting the SAYPAY indicator variable equal to one on February 26th, 2009 for all banks in the sample.

The remaining indicator variables are included to control for the concurrent release of potentially confounding information. The dividend declaration dates (DIV) are obtained from the CRSP database; the dates when banks announced they would be issuing preferred shares (PREF) are collected from each bank's Investor Relation website. Indicator variables are constructed to represent dates when an increase (BINCR) or decrease (BDECR) in the bank's interest rate is announced, as well as announcements of increases and decreases in the prime interest rate (CINCR and CDECR) based on news releases from the Bank of Canada. The remaining variables in the model are continuous variables, rather than indicator variables. The effect from news of the quarterly financial results is captured by "unexpected" earnings variables (UE1 and UE2), which are constructed as differences between the banks' reported Earnings Per Share (EPS) and analyst predictions of EPS. The proxies capture the difference between reported EPS

[5] Two banks (National Bank of Canada and Laurentian Bank) are not listed on any stock exchange in the U.S. therefore their returns data were not available in CRSP. Returns for these firms are collected from the Toronto Stock Exchange through the CFMRC (Canadian Financial Markets Research Centre) database. As a sensitivity check, regression models for all banks were estimated using both CRSP and CFMRC (in conjunction with the CFMRC Value Weighted Index Returns as a proxy for market returns) and no significant differences were found.

and the analyst forecast that most recently precedes the earnings announcement (UE1), and the difference between reported EPS and the average analyst forecast over the relevant fiscal quarter (UE2). The two unexpected earnings variables are constructed from data available in IBES. The model also incorporates a quantitative dimension of the dividend and preferred share news announcements by including variables that represent the change in dividends-per-share (DIVCHG) and the number (in millions) of preferred shares issued (PREFNUM). The intercept (α) captures the mean effect of all uncorrelated variables not modeled in this paper. Based on extant accounting research, the coefficients on variables UE1 and UE2 are expected to be positive, but the prior literature does not provide any indication for the significance or direction for parameters on the remaining variables in this model.

Microstructure analysis shows that public information is incorporated into share price within minutes of its release (see Chordia et al., 2005). Announcements in this event study were made public by mid-day therefore the full share price reaction to say-on-pay is expected to occur on the day of the announcement. Consequently, the analysis in this paper is done with a one-day event window. Most event studies use a three-day window to allow for leakage of the news on the day before the announcement and for the possibility that the news was released after the stock market was closed. However, this larger window is utilized because researchers seldom know the exact time of the event. The downside to including adjacent days is that they may contaminate the results with the effect of other news announcements. Therefore, the main tests in this paper are performed by setting SAYPAY equal to one on the date of the event, but results are corroborated with an estimation of the model with a three-day window surrounding the event.

4. Results

Some descriptive statistics of the returns variable are presented in Table 1. The first column shows the name of the bank, followed by the date the bank adopted say-on-pay. The remaining columns provide a comparison of the bank's returns to the market returns, first on the dates each bank respectively adopted say-on-pay and then on Feb 26th when the first set of banks adopted it. The last set of columns (comparing returns on Feb 26th) show that the bank returns (which are all positive) are all larger than the market return on that date (which is -0.0123). Consequently it is apparent that each of the seven banks experienced a positive share price reaction on Feb 26th that was unrelated to macroeconomic factors affecting other firms in the market on that day. The first set of columns show weaker results when comparing returns on the date each bank respectively adopted say-on-pay, since the last banks listed in the table (Laurentian Bank and Toronto-Dominion Bank) had worse returns than the market, and the banks that announced say-on-pay on March 3rd, 2009 (Bank of Montreal and Bank of Nova Scotia) experienced returns that may not be significantly different from the market. In order to remove the market effect and the share price reaction to other concurrent news releases, the say-on-pay effect is estimated with regression Equation 1, and results are reported in Table 2.

Model 1 in Table 2 reports the coefficients obtained in a regression of Equation 1 when the indicator variable (SAYPAY) is set equal to one for each bank on the respective date that it announced its adoption of say-on-pay. Model 2 shows the coefficients when SAYPAY is set equal to one on Feb 26th for all banks. Results suggest that the adoption of say-on-pay had a positive impact on the share price of the banks. Both models produce significant and positive coefficients on SAYPAY, with a parameter estimate of 0.025 in Model 1 and of 0.072 in Model 2. These results are consistent with capital market expecting say-on-pay to be economically beneficial to shareholders of the banks that adopted it. The difference in SAYPAY coefficients between the two models suggests a stronger share price reaction on Feb 26th based on the coefficient of 0.072, than on their respective adoption dates with a coefficient of 0.025.

The stronger response in Model 2 is consistent with information transfer among banks. Information transfer occurs when disclosure made by one firm contemporaneously affects the returns of other firms in the same industry. Researchers have found evidence of information transfer with the announcement of earnings (Foster, 1981), reorganizations (Chi, 2008), management forecasts (Kim, 2008), credit defaults (Jorion and Zhang, 2007), dividend declarations (Laux et al., 1998), and many other types of disclosed events. It appears that the adoption of say-on-pay is information that also transfers to firms in the same industry as the announcing firm(s). This is explored further by estimating Equation 1 by bank.

For brevity, only the coefficients on the SAYPAY variable are reported by bank in Table 3. As in Table 2, the first model (Model 1) is estimated with SAYPAY set to one on each respective bank's date of adoption, while Model 2 reports the coefficients obtained if SAYPAY is equal to one on February 26th for all banks. The first three banks listed are the ones that announced their event on February 26th therefore they have the same coefficient in both models. The remaining four banks announced say-on-pay later, and Model 1 shows that, aside from a negative return for Laurentian Bank, there was no reaction when these announcements were made. However, Model 2 shows that these four firms experienced a consistent share price reaction when the first set of banks adopted say-on-pay, on February

26th. This is in accordance with information transfer and the notion that once the first set of banks adopted say-on-pay, the market expected the benefit of this initiative to extend to the four banks that would soon adopt it.

The clustering of event dates is a common econometric concern in event studies. There is a high chance of committing a Type I error (falsely rejecting the null hypothesis of no effect) when many firms experience the event on the same date, which is the case for the firms tested in this paper. The issue arises because the error terms from the regression model are correlated, which understates the variance of returns, and therefore inflates the test statistic that is used to evaluate the null hypothesis. The problem can be mitigated with this data set by using the standard error from the coefficient on the market variable (MKT), since this variable captures the normal variation in returns. The standard error on MKT is a conservative estimate of the standard deviation on the event date, and can be used to test the coefficient on SAYPAY more rigorously.

The Student's test statistic provides a means to verify of the robustness of the results. The statistic obtained by dividing a regression coefficient by its standard error follows a Student's t distribution, which leads to the rejection of the null hypothesis when the test statistic is greater than 2.32 (at the 1% level of significance), 1.64 (at the 5% level of significance), or 1.28 (at the 10% level of significance). The standard errors for the MKT and SAYPAY coefficients are reported in Table 4 for this analysis. An examination of the statistics for Model 1 shows that the standard error is smaller on the SAYPAY coefficient (.00550) than on the MKT coefficient (.00921), which is consistent with a higher correlation of error terms on the event date. To the extent that the correlation of error terms is caused by the event itself, dividing the SAYPAY coefficient (0.025) by the understated standard error (.00550) results in an overstated test statistic of 4.55. A more conservative test statistic is obtained by using the larger standard error from the MKT coefficient as a proxy for the true standard error on the event date. For Model 1, this changes the test statistic of the coefficient on SAYPAY from 4.55 (based on 0.025/.00550) to a value of 2.71 (based on 0.025/.00921). This new value is well within the rejection area for a 5% level of significance, and also exceeds the cutoff for a rejection of the null hypothesis at the 1% level. For Model 2, applying the larger standard error from the MKT coefficient changes the test statistic on the coefficient on SAYPAY from a value of 13.19 (based on 0.072/.00546) to a value of 7.87 (based on 0.072/.00914), which causes the null hypothesis to be rejected at the 1% level. Consequently, the clustering of event dates does not appear to change any inference from the results in Table 2.

5. Conclusion

On February 26, 2009 three major Canadian banks adopted say-on-pay policies. Two of the banks espoused the policy as a result of a majority vote on a shareholder resolution, while one of the banks adopted it voluntarily. Over the next few weeks, the remaining four large Canadian banks also adopted say-on-pay. This paper is an event study of the capital market response to the news announcements that Canadian banks were adopting say-on-pay. Say-on-pay is a policy that provides shareholders with a non-binding vote on the firm's executive compensation package. If say-on-pay is considered to be beneficial in terms of reducing agency problems, the announcements should generate a positive share price reaction.

The share price reaction to say-on-pay is estimated with a regression that has the daily change in share price as the dependent variable, and explanatory variables that are comprised of an indicator variable set equal to one on the date the banks adopted the policy, and variables that control for other factors expected to systematically affect share price. The result is a positive and statistically significant estimate of a share price reaction on the day banks announced their adoption of say-on-pay. This suggests that the capital market expected this governance tool to provide significant economic benefits, as suggested by proponents of the policy.

The findings in this paper are relevant to the say-on-pay literature, which has remained largely inconclusive about the effect of its adoption on the value of a firm. However, they must be interpreted with caution. The setting is unique to the banking industry in Canada and may not generalize readily to other firms. In addition, say-on-pay was adopted by Canadian banks mainly as a result of shareholder activism, and the benefits of adopting it may not extend to firms that are mandated to change their governance practices regardless of whether shareholders are satisfied with them. Nevertheless, the finding in this paper should be of interest to regulators and advocates of say-on-pay as it provides new information about the value of the policy, and helps us ascertain whether its adoption could be beneficial.

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Table 1. Dates of say-on-pay adoption and corresponding returns

		On respective say-on-pay date		On Feb 26/09	
	Say-on-pay date	Bank return	Market return	Bank return	Market return
National Bank of Canada	Feb 26, 2009	0.0887	-0.0123	0.0887	-0.0123
Royal Bank of Canada	Feb 26, 2009	0.5813	-0.0123	0.5813	-0.0123
Canadian Imperial Bank of Commerce	Feb 26, 2009	0.0609	-0.0123	0.0609	-0.0123
Bank of Montreal	March 3, 2009	0.0421	0.0260	0.0802	-0.0123
Bank of Nova Scotia	March 3, 2009	0.0301	0.0260	0.0631	-0.0123
Laurentian Bank	March 10, 2009	-0.0320	-0.0049	0.0864	-0.0123
Toronto-Dominion Bank	March 18, 2009	-0.0235	-0.0081	0.0530	-0.0123

Table 2. Estimate of the effect of say-on-pay on returns.

	Model 1 (with SAYPAY equal to one on each bank's respective date of adoption)			Model 2 (with SAYPAY equal to one on Feb 26/09 for all banks)		
	coefficient	*p-value*		*coefficient*	*p-value*	
MKT	0.891	***	.00	0.893	***	.00
SAYPAY	0.025	***	.00	0.072	***	.00
DIV	-0.004	*	.06	-0.005	**	.03
PREF	0.024	***	.00	0.021	***	.00
BINCR	-0.005	*	.07	-0.005	*	.07
BDECR	-0.002		.28	-0.002		.26
CINCR	0.001	**	.05	0.001	**	.05
CDECR	0.000		.34	0.000		.29
UE1	0.034	***	.00	0.022	***	.00
UE2	0.003		.12	0.006		.12
DIVCHG	0.002		.47	0.002		.46
PREFNUM	-0.002	***	.00	-0.002	***	.00
INTERCEPT	0.000	***	.00	0.000	***	.00
N	12,337			12,337		
ADJ-R^2	44%			44%		

* indicates significance at the 10% level
** indicates significance at the 5% level
*** indicates significance at the 1% level

Table 3. Coefficient on SAYPAY variable by bank

	Estimated with Model 1 (with SAYPAY equal to one on each bank's respective date of adoption)			Estimated with Model 2 (with SAYPAY equal to one on Feb 26/09 for all banks)		
National Bank of Canada	0.085	***	.00	0.085	***	.00
Royal Bank of Canada	0.053	***	.00	0.053	***	.00
Canadian Imperial Bank of Commerce	0.045	*	.10	0.045	*	.10
Bank of Montreal	0.016		.24	0.092	***	.00
Bank of Nova Scotia	0.005		.73	0.072	***	.00
Laurentian Bank	-0.030	*	.08	0.091	***	.00
Toronto-Dominion Bank	-0.016		.20	0.065	***	.00

* indicates significance at the 10% level
** indicates significance at the 5% level
*** indicates significance at the 1% level

Table 4. Statistics on the MKT and SAYPAY coefficients from Table 2

From Model 1:	*coefficient*	*standard error*	*t-statistic*	*p-value*
MKT	0.891	.00921	96.74	<.01
SAYPAY	0.025	.00550	4.55	<.01
From Model 2:	*coefficient*	*standard error*	*t-statistic*	*p-value*
MKT	0.893	.00914	97.70	<.01
SAYPAY	0.072	.00546	13.19	<.01

Note that *t-statistic* is obtained by dividing *coefficient* by *standard error*. This statistic has the Student's t distribution, which leads to the rejection of the null hypothesis (which is that the coefficient is equal to zero, or has no effect) if it is greater than 1.28, 1.64, and 2.32 for a significance of 10%, 5%, and 1%, respectively.

APPENDIX A
Excerpts from Notices of Annual General Meetings of Shareholders

A.1.1. *Excerpt from CIBC's 2008 Annual General Meeting and Management Proxy Circular*[6]
PROPOSAL NO. 1: It is proposed that shareholders of Canadian Imperial Bank of Commerce urge the board of directors to adopt a policy that Canadian Imperial Bank of Commerce's shareholders be given the opportunity at each annual meeting of the shareholders to vote on an advisory resolution, to be proposed by Canadian Imperial Bank of Commerce's management, to ratify the report of the Management Resources and Compensation Committee set forth in the proxy statement. The proposal submitted to shareholders should ensure that shareholders understand that the vote is non-binding and would not affect any compensation paid or awarded to any Named Executive Officer.

The Board recommends that shareholders vote AGAINST this proposal.

The Board and management have been monitoring developments in Europe, Australia and the U.S. on annual shareholder advisory votes relating to executive compensation, also known as "say-on-pay". The Board has determined that, at this time, it would not be in the best interests of CIBC to institute a say-on-pay vote. Based on discussions with the Chairman of the Board has had with various shareholders and leading governance organizations in Canada, the Board believes there are strong and diverse views regarding the merits of a say-on-pay vote."

A.1.2. *Excerpt from the Voting Results of the CIBC 2008 Notice of Annual Meeting of Shareholders:*[7]
PROPOSAL NO. 1// FOR: 44.96% AGAINST: 55.04%

A.2.1. *Excerpt from CIBC's 2009 Annual General Meeting and Management Proxy Circular*[8]
"PROPOSAL NO. 1: It is proposed that the Board of Directors adopt a governance rule stipulating that the executive compensation policy be subject to an advisory shareholder vote."
The proposal was followed by text provided by MÉDAC:
"Shareholders cannot currently express their opinions on executive compensation policies (in particular, the proportion of the variable salary and its value based on different scenarios relating to increased share prices, sales or profits, as the case may be). Moreover, executive compensation has reached heights that even the most experienced observers find surprising. According to a survey conducted by McKinsey/HRI/CCGG in Canada, some 40% of directors believe that the compensation of chief executive officers is too high and 65% of investors agree. The members of the Mouvement and many citizens find it unacceptable that the salaries of senior executives continue to increase at an exponential rate, while those of average employees have hardly kept up with inflation. The results of a study by the Canadian Centre for Policy Alternatives on the compensation of the 100 highest paid chief executive officers of public corporations, published in early 2008, show that these chief executive officers now make 218 times as much as an average employee, while ten years ago they made only 104 times as much. Nothing can justify such a huge discrepancy, and everything militates in favour of changing this trend of recent years. We recognize that senior executive salaries should be determined by the Board of Directors. That is why we advocate an advisory vote ("say-on-pay") so that the Board can hear shareholders' view on its policy. Our business intelligence activities in this regard have allowed us to note that several countries have adopted rules to give shareholders the right to have a say on the fundamental policies and mechanisms of corporate executive compensation. Since 2003 in the United Kingdom and since 2004 in Australia, the compensation policies of public corporations are subject to an advisory vote. The Netherlands (2004), Sweden (2005) and Norway (2007) have gone even as far as making such a vote binding. This acknowledgment of shareholder competence over compensation policies has also been discussed in the OECD's Principles of Corporate Governance. In Canada, the proposal has been supported on average by 40.3% of shareholders at the last annual general meetings of the banks in 2008. This is a great opportunity for the Corporation to show its sensitivity to shareholders' concerns before such a policy is required of it by regulatory authorities."

The Board recommends that shareholders vote AGAINST this proposal.

[6] Available at http://www.cibc.com/ca/pdf/investor/
[7] Available at http://www.cibc.com/ca/pdf/investor-relations/annual-meetings/
[8] Available at http://www.cibc.com/ca/pdf/investor/

Board and Management Statement:

Over the course of the year, the Board spent considerable time monitoring developments on shareholder voting on executive compensation policies, and believes the objectives underlying such a vote – demonstrated alignment of pay to performance, transparency of Board decision-making through disclosure, and effective shareholder communications – are addressed by the governance framework and practices the Board and management have adopted and continue to enhance. In addition, the Board believes that it is important to maintain clarity regarding the role of the Board and the role of shareholders and it is critical for the Board to strike the right balance of open communication with shareholders while maintaining its accountability. These objectives are best achieved through ongoing dialogue on governance issues between the Board and its stakeholders. The Board will continue its discussions with stakeholders to assess the value of say-on-pay to shareholders. In the meantime, the Board does not believe that adoption of a shareholder vote on compensation policy is necessary at this time."

A.2.2. *Excerpt from the Voting Results of the CIBC 2009 Notice of Annual Meeting of Shareholders:*[9]
PROPOSAL NO. 1// FOR: 53.07% AGAINST: 46.93%
A.3.1 *Excerpt from the Royal Bank's 2009 Annual General Meeting and Management Proxy Circular*[10]

Proposal No. 1: Consultative vote by the shareholders on the compensation policy for executive officers
It is proposed that the Board of Directors adopt a rule of governance stipulating that the compensation policy of their executive officers be submitted to a consultative vote by the shareholders.

The proposal was followed by a rationale provided by MÉDAC. It is very similar to the statement printed in the CIBC report (see subsection A.2.1)

THE BOARD OF DIRECTORS RECOMMENDS SHAREHOLDERS VOTE AGAINST THE PROPOSAL FOR THE FOLLOWING REASONS:

Our governance approach is one of continuous improvement and we monitor emerging best practices aimed at further aligning executive compensation with the interests of shareholders. In carefully considering this proposal, the Board of Directors has taken into account several factors, including finalization by the Canadian Securities Administrators in September 2008 of new rules regarding executive compensation disclosure. As disclosure of Canadian issuers becomes more consistent under these new rules, the Board of Directors will continue to assess appropriate practices including shareholder advisory votes. The Board of Directors is committed to providing shareholders with clear, comprehensive and transparent disclosure that demonstrates the strong link between compensation and individual and corporate performance. Starting on page 22 of this Circular, this disclosure describes in detail the disciplined and prudent approach for setting compensation implemented by the board and its Human Resources Committee, which is composed exclusively of independent and experienced directors and works in consultation with an independent expert. We are also committed to open and responsive communications with shareholders. We actively engage in dialogues with investors and governance advocates and adopt policies responsive to their concerns when it is in the best interests of all shareholders. In addition, shareholders have the opportunity to communicate with the board concerning executive compensation or other matters by contacting the board's independent Chairman as provided on page 46 of this Circular.
The Board of Directors believes that the mechanisms in place for shareholder engagement provide meaningful opportunities for shareholders to effectively express their views concerning executive compensation, unlike the shareholder vote proposed, which would not specify which aspects of executive compensation policy have raised shareholder concerns.

A.3.2. *Excerpt from the Voting Results of the Royal Bank's 2009 Notice of Annual Meeting of Shareholders:*[11]
PROPOSAL NO. 1// FOR: 56.9% AGAINST: 43.1%

[9] Available at http://www.cibc.com/ca/pdf/investor-relations/annual-meetings/
[10] Available at http://www.cibc.com/ca/pdf/investor/
[11] Available at http://www.cibc.com/ca/pdf/investor-relations/annual-meetings/

APPENDIX B
News Announcements about Say-on-Pay

"National Bank to give shareholders advisory vote on the compensation policy for executive officers beginning in 2010"
Source: National Bank Investors Relation website, Montreal, February 26, 2009.

National Bank of Canada today announced that, beginning next year, it would submit the compensation policy for its executive officers to its shareholders for an advisory vote. In so doing, the Bank is acknowledging the developments of the past few weeks relating to this matter and fulfilling a wish expressed by many of its shareholders.
The vote on the compensation policy will be non-binding, as had been requested in the related proposal submitted by a shareholder, the *Mouvement d'éducation et de défense des actionnaires* (MEDAC), for tomorrow's Annual Meeting.
National Bank therefore becomes the first major bank in Canada to agree to submit its compensation policy for executive officers to shareholders for an advisory vote.

"RBC, National, CIBC Shareholders get say-on-pay"
Source: Globe and Mail, Published Thursday, Feb 26, 2009 at 2:31 EST.
Three of Canada's biggest banks will submit to shareholder demands for a say on executive compensation plans, reacting to investor anger that bank bosses are taking home millions even as profits shrink. A majority of Canadian Imperial Bank of Commerce and Royal Bank of Canada shareholders voted at annual meetings to pass motions to have non-binding "say-on-pay" advisory votes on executive compensation.
National Bank of Canada announced Thursday morning that it too would hold non-binding shareholder votes on executive compensation, starting next year. National was facing a shareholder motion on the idea at its annual meeting, which is scheduled for Friday.
All Canada's big banks are facing say-on-pay motions put forward from shareholders. The banks opposed the motions but the tide of investor anger over multi-million-dollar pay cheques during the current downturn appears to be overwhelming.There is growing support among major Canadian investors for say-on-pay programs at major companies, especially where compensation seems to be growing despite poor financial results, said Stephen Griggs, managing director of the Canadian Coalition for Good Governance (CCGG), which represents large institutional shareholders.
"Attitudes are change very quickly on say-on-pay," he said in an interview.
Royal Bank and CIBC officials both said they would respect the results of the votes on the shareholder motions.
"The board will now be considering how best to give shareholders a vote on this important issue, and we commend those who brought the say-on-pay proposals forward," Royal Bank chairman David O'Brien said, adding that RBC Asset Management actually voted in favour of idea.
National may have moved in anticipation that investors would demand the right to have a say-on-pay. With a shareholder vote on the issue looming at its annual meeting Friday, National dropped its opposition and said it would allow investors to vote on pay starting in 2010. The vote will be non-binding.
"In so doing, the bank is acknowledging the developments of the past few weeks relating to this matter and fulfilling a wish expressed by many of its shareholders," National said in a statement.
The CCGG issued a statement early last year saying it did not support say-on-pay proposals because its members felt such votes were a "blunt instrument" to send a message to companies, and they preferred to use direct consultations with companies to communicate concerns about specific elements of compensation plans.
But things have changed over the past year, Mr. Griggs said, because members have grown frustrated that some companies have not responded despite consultations.
Mr. Griggs said one issue fanning the flames is the recent revelation that Canadian Imperial Bank of Commerce has increased the maximum possible pension that can be collected by chief executive officer Gerry McCaughey.
Mr. Griggs said some of his coalition's largest members were planning to vote in favour of a say-on-pay resolution that has been submitted to CIBC for a vote at its annual meeting.
"I'm getting e-mails and phone calls from our members saying, 'We thought we had very good engagement with them, but they didn't get it,'" he said.
Some bank CEOs, including Royal's Gordon Nixon and CIBC's Mr. McGaughey, have tried to fight anger about their compensation by giving back bonuses.
However, Louis Vachon, head of National, had come under fire because even as his bank's involvement in the asset-backed commercial paper mess hampered profit growth, he took home a bonus for last year.
National Bank said Thursday that Mr. Vachon would donate to charity $1-million he received from the bank for his personal holdings of ABCP.

National bought out the ABCP holdings of individual clients in 2007 at full face value, including paper held by bank executives. Mr. Vachon was one of those clients, and the $2.5-million he received was put in trust pending the resolution of the ABCP workout.
Now that it's done, Mr. Vachon is getting his $2.5-million back, but he decided to donate 40 per cent to charity. The percentage was chosen to match the hit that National has taken on its own ABCP holdings, said bank spokesman Denis Dubé.

“Three Canadian banks give shareholders say-on-pay National to hold advisory vote on pay in 2010 RBC, CIBC investors vote for similar move”

Source: Reuters (Toronto), Published Thursday, Feb 26, 2009 at 4:03 EST.
Three of Canada's major banks have agreed to give shareholders a say in determining what top executives get paid, a move that comes amid growing global anger about big pay for bankers as the financial crisis rages.
National Bank of Canada (NA.TO: Quote, Profile, Research, Stock Buzz) was first out of the gate, announcing ahead of its shareholder meeting on Friday that it would give its shareholders an advisory and nonbinding vote on the executive pay packages when the program starts in 2010.
"The bank is acknowledging the developments of the past few weeks relating to this matter and fulfilling a wish expressed by many of its shareholders," National Bank of Canada, the country's sixth largest bank, said in a statement.
Royal Bank of Canada (RY.TO: Quote, Profile, Research, Stock Buzz) and Canadian Imperial Bank of Commerce (CM.TO: Quote, Profile, Research, Stock Buzz) shareholders voted in favor of introducing similar measures at their annual general meetings in Vancouver on Thursday, a decision the chairmen of both banks said they would respect.
"This is an issue that the board has continued to discuss over the past year. We understand the importance of this issue to our shareholders," said David O'Brien, RBC's chairman, at the close of the general shareholder meeting.
He noted that RBC Asset Management, the wealth management arm of the bank and a significant shareholder, voted in favor of the motion.
"The board will now be considering how best to give shareholders a vote on this important issue and we commend those who brought the say-on-pay proposals forward," O'Brien added.
The moves come after U.S. President Barack Obama took on bailed-out Wall Street firms earlier this month, setting a $500,000 annual cap on pay for top executives at companies receiving taxpayer funds and tapping popular anger over financial sector excesses.
New York officials have reported that Wall Street companies paid $18.4 billion in bonuses to employees last year even though the government had to intervene to save the sector from collapse.
Mounting fury in Europe over executive bonuses was also seen by some experts as likely to spark measures to crack down on executive pay and bonuses.
Popular anger is less intense in Canada, where pay packages are smaller and conservative lending practices have helped the industry avoid the massive writedowns and losses that have driven U.S. and European banks into insolvency. The World Economic Forum last year ranked Canada's banking system as the world's soundest.
Still, multimillion-dollar pay packages for chief executives at Canada's big banks have been criticized for years by shareholder activists. Banks have defended their compensation policies, citing the need to be competitive and retain talent.
The criticism gained momentum as bank profits have fallen, hit by the global financial crisis. All three banks reported quarterly profits that topped forecasts despite charges.

Canadian banks recently announced that their chief executives were taking smaller compensation packages this year, giving up pay at a time of global economic recession. Some heads of Canadian banks gave back their bonuses or requested that some of their pay go to charity.

“TD's Clark to forgo golden parachute; Say-on-pay impact”

Source: Financial Post, Pg. FP7, Published Thursday, Feb 28, 2009.

Ed Clark has agreed to forgo a golden parachute when the time comes to leave his post at Toronto-Dominion Bank. The chief executive has waived his claim to severance pay worth up to $10-million when he departs, and agreed to freeze his pension next year, as part of a deal extending his employment until 2013.

The move comes amid a broad-based shareholder insurrection over executive pay on Bay Street as hefty bonuses ignite public scorn in the midst of a market crash. The TD board is expected to come under pressure to give investors a voice on compensation when it holds its annual general meeting next week. Shareholders staged a revolt in recent days demanding a say on pay at three of the country's biggest banks, Royal Bank of Canada, Canadian Imperial Bank of Commerce and National Bank of Canada.

The insurrections seemed to mark a turning point for shareholder activism in the country and forced bank boards back to the drawing board when designing compensation. In foreswearing a golden handshake, Mr. Clark and the board of TD are addressing one of the most contentious sticking points between banks and institutional investors.
Generous severance packages and pension payouts are often used to resolve boardroom bust-ups at troubled companies and lead to what shareholders have dubbed pay for failure. Also, the pension payouts Mr. Clark was due to receive when his existing contract expires next year will instead be paid in stock, with the cash disbursement converted into $4.7-million of shares that he cannot divest until two years after retirement.

TD said the steps would "align Mr. Clark's interests with those of shareholders." John Thompson, chairman of the board, said, "Unlike many of its peers around the world, some of which are struggling to survive, TD remains one of the most reliably profitable banks in the world. Ed's strategic vision and leadership have a lot to do with that."
The new contract will extend the executive's tenure to 13 years at the head of TD and give him time to show if he can deliver on his strategy of expanding into the United States.

Mr. Clark is often cited on Bay Street as the bank executive most likely to be head-hunted by a major U. S. bank, and his commitment to stay on follows board deliberations over the need to develop a succession plan.
It is unclear if the concessions to institutional investors will avert a majority vote next week that would allow shareholders a non-binding vote on executive pay.

“BMO pay for CEO gets failing mark from Teachers”

Source: Globe and Mail, Published Tuesday, Mar 3, 2009.

Amid growing concerns about executive compensation, one of Canada's most powerful investment funds, the Ontario Teachers' Pension Plan, is singling out Bank of Montreal for paying its chief executive officer too much for a lagging performance. Teachers is voicing its displeasure by withholding its vote for the directors who sit on the board committee that sets pay for BMO CEO Bill Downe, and which wanted to pay him $6.5-million in a year when shareholders lost 27 per cent on the bank's stock.

Mr. Downe eventually declined most of the money, taking home $2.4-million, but Teachers argues the board got it wrong by offering the money in the first place. Teachers was also upset with the committee's decision to remove some ties between compensation and future performance.
"We don't think shareholders or the board of directors should have to depend on the charitable acts of the CEO," said Wayne Kozun, senior vice-president of public equity at Teachers. "If the CEO thought it was not right for him to own this compensation, then why did the board think it's okay for him to earn this compensation?"
The move adds to a wave of activism on compensation for bank CEOs. Last week, shareholders of Canadian Imperial Bank of Commerce, National Bank of Canada and Royal Bank of Canada won the right to vote on pay practices at those firms. Shareholders of BMO and Bank of Nova Scotia are to vote today on "say-on-pay" motions demanding the same right.

Teachers do not support those demands, preferring instead to try to work with boards directly and to chastise them through withheld votes when necessary. The fund owned 556,600 shares of BMO as of Dec. 31, according to a regulatory filing. That's about 0.1 per cent of the bank's stock, making the pension fund's protest mostly symbolic. Still, by taking on the compensation committee, Teachers is taking a public swipe at the judgment of some of country's best-known executives.
The committee includes Robert Astley, a former Sun Life executive; TransCanada Corp. CEO Hal Kvisle; and former Torstar Corp. head David Galloway, who has been chairman of the board of BMO since 2004.

"In 2008, the management team performed well in challenging times," Mr. Galloway said.
"Their actions resulted in close to $2-billion in net income with improved customer loyalty and market share in key areas.”

"In addition, BMO's CEO compensation is substantially lower than other Canadian bank CEOs. We welcome hearing the views of shareholders and are open to a dialogue with Teachers on this matter."

Teachers met with board chairs and the heads of the compensation-setting committees at major banks at the end of 2008 to raise its concerns, Mr. Kozun said.

"At some of the banks, obviously they did a better job in terms of rewarding or structuring their compensation so that it is pay for performance, but at Bank of Montreal in particular we think that they erred in terms of giving too much pay for not enough performance," he said.

Some advocates say shareholders would be better off if Teachers would support say-on-pay motions because a direct vote on pay sends a clearer message to a board. "Why not vote directly on it? We don't quite understand the reticence," said Laura O'Neill, director of law and policy at the Vancouver-based Shareholder Association for Research and Education, which helped to craft the motions. Toronto-Dominion Bank will be the final bank to hold its annual meeting, on April 2. Mr. Kozun said Teachers is still looking at its voting plans for TD, but noted "their performance has been better than some of the other banks."

“TD Bank to implement 'say on pay' vote in 2010”

Published The Canadian Press Wednesday March 18th, 2009

TORONTO - TD Bank (TSX:TD) says its shareholders will get a so-called "say on pay" vote on compensation for its executives starting in 2010.
TD is the latest bank to bow to shareholder pressure on the issue. Shareholder resolutions calling for non-binding votes were passed or accepted at the recent annual meetings of the Royal Bank (TSX:RBC), CIBC (TSX:CM), Bank of Nova Scotia (TSX:BNS) and Bank of Montreal (TSX:BMO).
As well, TMX Group Inc. (TSX:X) recently became Canada's first major non-bank corporation to establish say on pay.
The same resolution was slated for TD's annual meeting on April 2 in Saint John, N.B. However, the bank said Wednesday that shareholder groups will no longer be presenting their proposals on the issue at the event.
"TD promotes open and proactive dialogue with shareholders, ensuring their feedback on compensation and other important issues is heard and carefully considered by the board," TD chairman John Thompson said in a release Wednesday.
"It's now clear from the votes held this year at the other major Canadian banks' meetings that the opinion of the investment community, while still divided, has moved in favour of an advisory vote, and so we've acted accordingly."
Bosses of Canada's big banks took pay cuts in 2008 in view of last year's steep share-price declines.
TD said recently that its CEO Ed Clark took a 41 per cent pay cut to $8 million last year, after declining to accept $3 million and turning this amount over to charity. Clark was awarded $11 million in total compensation for 2008, down 19 per cent from $13.5 million in 2007, the bank said last month.
TD said the CEO's cash bonus was reduced by $1 million to $1.25 million. His $11-million total award also included $4.5 million in shares, down from $6 million, and options valued at $3.75 million, the same as in 2007.
Clark's decision to refuse part of his compensation followed similar moves by other big-bank bosses.
Gordon Nixon, chief executive of the Royal Bank of Canada (TSX:RY), declined to accept $4.95 million in stock, while taking a 30 per cent cut in his cash pay. That left the boss of Canada's largest bank with an unchanged base salary of $1.4 million plus a bonus of $2.4 million, down from $4 million, and Nixon said he would invest the bonus in RBC shares.
CIBC chief executive Gerald McCaughey received $5.3 million, down from $9.1 million, although he could have been eligible for almost $13 million because of a one-year lag in setting bonuses at CIBC (TSX:CM).
Bank of Montreal (TSX:BMO) initially disclosed that CEO Bill Downe received just under $6 million in direct compensation, up from $5.5 million in 2007 as BMO "performed well in challenging times." However, after other bankers scaled back their packages, Downe decided to forgo $4.1 million.
Rick Waugh, head of the Bank of Nova Scotia (TSX:BNS) took a 20 per cent cut in his compensation to $7.5 million.
The say on pay issue has come to the forefront in North America in the past few years. Annual votes are already required by law in Britain and Australia, while in the Netherlands and Sweden the votes are binding on boards of directors.