TOP 10 CURRENT BUSINESS AND LEGAL TRENDS AFFECTING DIRECTORS AND OFFICERS LIABILITY IN CANADA 2017

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1. SECURITIES CLASS ACTION CLAIMS

FILINGS, SETTLEMENTS & DISMISSALS

According to National Economic Research Associates' (NERA) Trends in Canadian Securities Class Actions: 2016 Update, filings of Canadian securities class actions doubled in 2016 as compared to 2015, but were lower than the numbers filed annually between 2010 through 2014. The Canadian experience contrasts with the United States, where 2016 saw the highest number of securities class actions filed since the early 2000s.

Nine new Canadian securities class actions were filed during 2016. Seven of the new nine cases filed in 2016 were statutory secondary market cases. There have now been a total of 76 statutory secondary market cases filed to date.

Only two Canadian securities class actions were settled in 2016. To date, there have been 31 settlements of statutory secondary market cases, with an average settlement of $11.7 million. Of the 31 statutory secondary market cases that been settled, 20 were Canadian-only cases and 11 were cross-border cases with claims being filed both in Canada and the U.S. The average settlement of the cross-border statutory secondary market cases was $21.9 million.

Three Canadian securities class actions were dismissed during 2016. Of the 76 statutory secondary market cases filed, eight have been dismissed so far. By comparison, dismissal rates in the United States have been substantially higher where about half of the cases filed between 2008 and 2011 (the most recent years with a substantial resolution rate) were dismissed. One Canadian securities class action was discontinued in 2016.

At the end of 2016, 54 Canadian securities class actions representing more than $55 billion in claims remained unresolved. Of the 54 unresolved cases, 34 (63%) are statutory secondary market cases representing more than $53 billion in damages claimed.

Canadian-domiciled companies continue to experience claims activity in the United States. By the end of December 2016, there were 18 pending U.S. securities class action cases against Canadian-domiciled companies, the majority of which (all of but three) were filed in the last four years.

2. CHANGING LITIGATION ENVIRONMENT IN CANADA

We continue to observe a changing and increasingly difficult litigation environment in Canada for companies and their directors and officers. This changing environment is being driven by multiple factors, including the evolving state of the law with respect to secondary market civil liability, a developing and increasingly aggressive plaintiffs' bar, institutional investors acting as lead plaintiffs, early disclosure of directors and officers liability insurance (D&O) policies and third-party funding arrangements, to name a few.

RECENT CASE LAW

In April 2015, the Supreme Court of Canada released its decision in Theratechnologies Inc. v. 121851 Canada Inc., dismissing a proposed securities class action against Montreal based pharmaceutical company Theratechnologies Inc. In this landmark case, the Supreme Court of Canada provided guidance for the first time regarding the test for leave to assert a statutory claim for secondary market misrepresentation. This case arose out of allegations that Theratechnologies had failed to properly disclose questions that the FDA had with respect to side

effects regarding a new drug. The FDA's questions were publicized and the company's stock dropped by more than 50%. The FDA later approved the drug and the share price recovered. Nevertheless, a proposed class action was brought under the Quebec Securities Act alleging that the potential side effects of the medication and the FDA's questions regarding the potential side effects constituted a material change of business that Theratechnologies had failed to disclose.

In a 7-0 decision written by Justice Rosalie Silberman, the Supreme Court of Canada in Theratechnologies weighed in on the test Canadian judges must use in deciding whether a plaintiff may obtain leave to commence a statutory secondary market liability claim under provincial securities laws. The Supreme Court ruled that a plaintiff must provide "sufficient evidence to persuade a court that there is a reasonable possibility that the action will be resolved in the claimant's favour." In so doing, the Supreme Court confirmed that the leave test is not merely a "speed bump" and that in order to show that a case has a reasonable possibility of success, the plaintiff must provide some credible evidence to support the claim. Applying the test to this case, the Supreme Court noted that the obligation of timely disclosure is limited to material changes in the operations, business or capital of the issuer and that plaintiffs had failed to establish that the FDA's questions related to a material change in Theratechnologies' business that had not been disclosed.

The Theratechnologies case is significant because it raises the threshold that had been established in previous lower court decisions, which had been criticized for years for being too low and insufficiently rigorous. Now the fundamental merits of a case will have to be proven at an initial stage of the proceeding before a case will be granted leave to proceed as a secondary market civil liability class action, which is a positive development for publicly traded companies in Canada and their directors and officers. As the test for leave for certification is consistent in Canadian securities laws, this decision is important not only in Quebec where it was originally commenced, but across Canada. It will be interesting to see whether this more robust test acts as a deterrent to potential litigants, as it could make it harder for plaintiffs to advance this kind of litigation, and if it will result in more dismissals of potential secondary market civil liability class actions, as courts take a harder look at the merits of potential cases.

In December 2015 in one of the most anticipated cases of the year, the Supreme Court of Canada released its decision in Canadian Imperial Bank of Commerce v. Green. The Green case involved appeals from three different cases (CIBC, IMAX and Celestica) and addressed three issues: 1) the limitation period applicable to class actions for claims for secondary market misrepresentations under Part XXIII.1 of the Ontario Securities Act ("OSA"); 2) the standard for leave to proceed under Part XXIII.2 of the OSA; and 3) whether both a statutory cause of action and a common law claim for misrepresentation can be certified as the same class proceeding.

With respect to the limitation issue, the Supreme Court of Canada in Green disagreed with the Ontario Court of Appeal and found that the limitation period applicable to a class proceeding is suspended when leave is granted. The Supreme Court of Canada's decision on the three year limitation period will have limited applicability as the OSA was amended in 2014 to provide that the limitation period is suspended on the date the plaintiff files a motion to seek leave.

With respect to the standard for leave, the Supreme Court of Canada in Green unanimously confirmed the leave test set out in Theratechnologies applies under the OSA.

In terms of certification of common law claims, the Supreme Court of Canada in Green, confirmed the Ontario Court of Appeal's ruling that reliance cannot be certified as a common issue, however, in some circumstances where statutory claims are certified, other elements of a common law misrepresentation claim, such as conduct and intent, could be certified as common issues and proceed as part of a class action. Therefore, while both statutory and common law claims could be certified together in a class action, plaintiffs may have to prove issues relating to reliance and damages through separate trials, which could be both costly and onerous.

In July 2015, Coffin v. Atlantic Power was the first case to consider the more robust test for leave following the Supreme Court's decision in Theratechnologies. In that case, Justice Belobaba found that the plaintiffs had no reasonable possibility of success at trial and declined to certify parallel common law claims.

In 2016, lower courts continued to adopt the standard for leave established by the Supreme Court of Canada. In Bradley v. Eastern Platinum Ltd., the Ontario Superior Court of Justice dismissed a proposed class action on the basis that there was no reasonable possibility that the proposed plaintiff would succeed on his alleged claims and stated that "the leave test as now understood requires a robust, meaningful examination and critical evaluation of the evidence (or absence of evidence)." In Mask v. Silvercorp, the Ontario Court of Appeal unanimously dismissed an appeal from a refusal to grant leave to proceed to a secondary market class action and confirmed that the judge is "entitled to undertake a critical evaluation of all of the evidence and that this necessarily requires some weighing of the evidence, drawing of appropriate inferences and the finding of facts established by the record."

CARRIAGE MOTIONS

Multiple class actions may be filed by different plaintiffs and law firms. When this occurs, plaintiffs will file a carriage motion and the court will have to decide which action will proceed. Carriage motions, in which competing plaintiffs' law firms bring an application to the court to act as lead plaintiff, have been commenced in Canada in respect of statutory secondary market cases. In the course of the application, plaintiffs' law firms argue why they would be the best counsel to conduct the litigation. Areas of focus include the scope of the pleadings and the proposed class, as well as, the experience and expertise of the plaintiffs' law firms. Although carriage fights are not uncommon in the litigation context in the United States, they are a relatively newer phenomenon in Canada. While the costs associated with carriage motions are typically borne by plaintiffs' counsel, such motions can delay the advancement of the action in Canada, a consideration that can complicate matters in terms of managing and settling cross-border securities claims in Canada and the United States, as the two pieces of litigation can progress at very different rates.

INSTITUTIONAL PLAINTIFFS

Having institutional investors, like pension funds, acting as lead plaintiffs in securities class action litigation is relatively new to the Canadian litigation landscape. As evidenced in the United States, institutional investors bring sophistication and financial means to prosecute actions. In the United States, there has been a strong correlation between the involvement of institutional investors and higher settlements. Although still new to Canada, we are seeing a similar experience.

THIRD-PARTY FUNDING

Canadian courts have confirmed arrangements where third parties to the litigation, such as Irish company Claims Funding International, have agreed to indemnify plaintiffs against costs in return for a percentage of recovery of settlement funds. The plaintiffs argued in these cases that the potential for adverse costs awards, whereby the loser pays a portion of the winners' defence costs, may act as a disincentive for plaintiffs to litigate meritorious claims and that by mitigating this downside, third-party funding arrangements provide greater access to justice. What this means for Canadian companies and their directors and officers is that an action that may not otherwise have been able to be advanced, may now proceed forward. There are also implications in terms of settlement negotiations, as settlement amounts have been increased to take into account the third party funder.

EARLY DISCLOSURE OF D&O POLICIES

Canadian courts have permitted potential plaintiffs to view the companies' D&O policies at very early stages in the proceedings. Plaintiffs' firms understand that D&O policy limits are important considerations in evaluating litigation. The problem with early policy production is that it arguably sets a "floor" for settlement negotiations, before any evaluation of the merits of the case.

3. ENVIRONMENTAL AND CLIMATE EXPOSURES

The implications of the 2013 case, Baker et. al. v. Director, Ministry of the Environment (Northstar), are an ongoing source of anxiety for directors and officers of companies with operations in Ontario, as well as other provinces. The Ontario Ministry of the Environment and Climate Change (MOECC) has since issued similar contamination related orders against companies and their directors and officers and indications are they plan to continue along this path. Based on the outcome of the recent Redwater Energy Corporation (re), 2016 ABQB 278 case in Alberta (Redwater), it would appear that other provincial regulators are planning on following Ontario on this front.

Redwater Energy Corporation was an Alberta based junior energy producer that filed for bankruptcy in May of 2015. The court appointed receiver took possession of some of Redwater's oil and gas assets but renounced others as having little or no value, as permitted under the Bankruptcy and Insolvency Act (BIA). The renounced assets, which included almost 70 inoperative wells, had unfunded environmental liabilities in excess of $5 million. The Alberta Energy Regulator (AER), in a position very similar to the MOECC's in the Northstar case, argued that to permit the receiver to abandon uneconomic wells and sell the others improperly prioritized the interests of secured creditors over environmental remediation. The Alberta Court of Queen's Bench disagreed. Relying on the long standing rule of federal paramountcy, the court held that, where the receiver's duties under the BIA conflicted with provincial environmental regulation, the BIA prevailed. This decision was released in May 2016, and the AER has appealed.

The implications for directors and officers stem not from the court case itself but the AER's reaction to the ongoing proceedings. On April 8th, 2016, the AER released Bulletin 2016-10, which included the following statements:

"The purpose of this bulletin is to remind licensees and their directors and officers of their statutory responsibilities when ceasing operations because of insolvency or for any other reason...

Failure to comply with statutory responsibilities relating to environmental liabilities or any other AER requirement may result in an investigation and the AER pursuing available enforcement against the licensee and/or its directors and officers. This may include naming individual directors and/or officers of AER licensees under section 106 of the Oil and Gas Conservation Act."

In Ontario, Alberta and other provinces, regulators have long had the ability to bring orders and proceedings against directors and officers of corporations in relation to environmental liabilities. There is limited history, however, of either doing so. The MOECC has taken just such action and AER clearly signalled its intent to do so. Incongruously, neither the Northstar nor the Redwater decisions relied upon a substantive analysis of personal environmental obligations. To the extent they established case law, it was in the relatively arcane areas of when to grant motions to stay and bankruptcy priorities. In the Northstar case, it appears the directors and officers settled because of the cost of ongoing remediation obligations. Legal commentary on the case indicates the directors and officers may well have had effective legal arguments in their defence.

Climate change is another developing area and is no longer just an ethical environmental issue. It has fast become a matter of corporate governance, with regulators both in Canada and abroad increasing oversight and pressure on greater corporate disclosure of climate change risks. At the same time, litigation against companies and their boards on climate change exposures has accelerated pace. Greater awareness of climate change and discussion of who should pay for the harm could lead to increased activity by third parties, shareholders and regulators, as well as claims in foreign jurisdictions that may be more supportive of this kind of activism and new laws that could facilitate climate litigation against Canadian companies and their directors and officers.

D&O insurance is principally intended to protect individual directors and officers from claims brought by third-party stakeholders (including shareholders from public companies) arising out of a breach of duty or error in allegedly failing to act in good faith with a view to the best interests of the company. These policies are not intended to be a substitute for the coverage provided under a general liability or an environmental liability policy. Historically, D&O policies contained pollution exclusions within the base policy wording. This exclusionary language was further supplemented by bodily injury and property damage exclusions. Over the past few years, many D&O Insurers have developed new wordings, some of which do not include specific pollution exclusions.

Directors and officers must be diligent in understanding the breadth of pollution coverage under a D&O policy even in the absence of a pollution exclusion. The reality is that many pollution scenarios would not be covered under the D&O policy by virtue of other provisions within the wording. The definition of loss may exclude fines and penalties. Furthermore, clean-up costs are typically excluded under the definition of loss.

A Side A Difference in Conditions (Side ADIC) policy provides dedicated and exclusive limits for claims made against directors and officers when the company cannot (i.e., financial insolvency) or will not indemnify the individual(s). These policies often provide broader definitions with less exclusionary language and can drop down and substitute for an underlying layer when the Side A DIC coverage is broader for non-indemnifiable actions. Specifically, the proprietary Marsh AlphaTM Side A DIC policy contains neither a pollution exclusion nor a bodily injury or property damage exclusion, and is silent with respect to clean-up costs. In theory, this may allow for coverage for pollution claims but as of yet the theory has not been tested.

The implications of climate change on the personal liabilities of company directors are increasingly apparent. Like pollution, coverage relating to climate change may implicate exclusions commonly found in D&O policies, such as the pollution exclusion, as well as, the exclusion for bodily injury and property damage. Carve-outs to the pollution exclusion which reinstate coverage for securities related claims may be obtained to provide coverage for securities claims emanating out of company disclosures relating to climate change. As well, like with pollution, a Side ADIC policy, although untested, may allow for coverage to individual directors and officers when the company cannot or will not provide indemnification to them in respect of matters relating to climate change.

4. CYBER THREAT

The enormity and magnitude of cyber threats have risen to a degree that the consequences of an attack can significantly impact a company's valuation. As a result, network security and data privacy are now boardroom governance concerns. Regulators have responded by increasing oversight and highlighting the need for public companies to make disclosures related to these risks. Boards need not only to devote more attention to this ever-increasing area of risk but also evaluate their corporate readiness for such attacks. Recent network attacks and data breaches have demonstrated that cybersecurity events can quickly accumulate significant costs, inflict reputational damage, and produce long-term financial and operational ramifications. A massive data breach is likely to invite litigation, generate regulatory investigations and/or fines (depending on the industry), and instigate significant media attention. A material denial-of-service attack can grind company operations to a halt and threaten a company's revenue. APTs (Advanced Persistent Threats) can cause physical damage by manipulating

processes carried out by control systems, and/or compromise an organization's IP, to name a few relevant issues. If the breach or incidents arising from cyber threats are material to a typical investor, financial regulators, as well as potential shareholder litigants may also have an interest.

The passage of the Digital Privacy Act (Bill S-4), which will require breach notification to individuals, and a report to the commissioner where it is reasonable to believe that the breach creates a "real risk of significant harm to the individual," will create new administrative burdens, costs, and risks for organizations. Perhaps even more impactful is the requirement to maintain a record of every breach involving personal information under an organization's control. These regulations coupled with developments pertaining to the European Union safe harbour and continued regulatory investigations by U.S. entities make for a complicated operating environment for Canadian businesses with operations spanning the noted geographies.

Although some cyber events may be beyond the control of the company, nevertheless, directors and officers may be falling short in their duties to review the organization's risk practices, to include cyber/technology exposures in their business continuity planning and insurance coverages, and to disclose material cyber risks and incidents to stakeholders. Data from the National Association of Corporate Directors shows that many directors are challenged to understand the scope and evolving nature of cyber risks. Even those directors and officers who are aware of the importance of cyber and network risk issues often do not know specific company protocols in these areas. A knowledge gap exists between the awareness of a company's exposure and the practices implemented to defend against those threats. There may be a disconnect between security risk assessments and financial impact assessments. Further, security risk is complex, widespread, technical, and ever changing. As a result, it is difficult to quantify the probability of an event and its impact, as well as the impact of preventative measures in reducing risk.

With the above comments in mind, it comes as no surprise that we have seen significant privacy related class action litigation in both Canada and the United States. We are also now seeing increased activity as it pertains to derivative claims and securities class actions emanating from an underlying cyber event.

5. INITIAL PUBLIC OFFERINGS

Following the trend from the second half of 2015, the Initial Public Offering (IPO) market in 2016 was a very inactive year in terms of number of IPOs and total proceeds raised, both in Canada and in the U.S. This may be attributed to uncertainty in the market following the Brexit vote in June and the U.S. presidential election in November. The most notable Canadian IPO in 2016 was Aritzia Inc.'s $400 million offering in October. With the successful IPOs of Freshii Inc., Canada Goose Holdings Inc., and Snap Inc. (Snapchat) in the U.S in Q1 2017, there is hope and it is anticipated that 2017 will be a more active year for the IPO market.

Going public can be a significant step in a company's strategy to raise capital and enhance the company's profile. The adoption of legal and securities exchange requirements by directors and officers is essential to the transition to a public company. The company must prepare itself for the demands of investors, analysts, regulators, and the financial press by implementing sound practices prior to an IPO to ensure good corporate governance as a publicly traded entity. The unique risks and exposures to the executives and board of directors during the IPO process should be considered and the current D&O program analyzed to ensure it dovetails with the prospectus document and go forward securities exposure. Consideration should be given to Public Offering of Securities Insurance (POSI), which is transaction-specific insurance covering the liabilities relating to the IPO in conjunction with the traditional annual D&O insurance covering non-IPO liabilities. POSI is typically written for a six (6) year period with the payment of a single fixed premium and the policy is non-cancellable once the premium is paid. Terms are negotiable based on the transaction and may include coverage for the selling and/or controlling shareholder and coverage for the indemnification obligations to the financial underwriters pursuant to the underwriting agreement.

6. FOREIGN CORRUPT PRACTICES

The initial activism we saw in the wake of the strengthening of Canadian foreign corrupt practices laws has continued unabated since the amendments to the Corruption of Foreign Public Officials Act (CFPOA) came into force on June 19, 2013. Canadian companies with global operations are very much subject to the laws of Canada and other jurisdictions that prohibit bribery and the focus an enforcement of those provisions has not lessened. In 2013, Canada prosecuted and convicted the first individual under the CFPOA. The sentence of three years in prison was handed down to the agent responsible and it has had a chilling effect for all those who have dealings outside our borders. Additionally, there are numerous criminal proceedings pending in front of Canadian courts that are likely to lead to further examples of just how far the government is willing to go in the prosecution of perceived global corruption. The RCMP are no longer publicly giving an update as to the number of current investigations but, based upon publicly available information, it appears to be in excess of 40 active cases and

could very well be much higher than that. What we have also seen is increased sharing of information and resources between regulators across borders as the United States and Britain work closely with the Canadian regulators to track breaches of the respective legislation.

The costs of these types of incidents are causing potential for corporate bankruptcy. We see investigations eclipsing the $100 million mark per year. In some cases, the investigation costs exceed the ultimate costs to resolve the matter. The US Foreign Corrupt Practices Act (FCPA) has a significant impact on global companies. With legislation purporting to apply to entities with only a tangential connection to the U.S. and the increase in enforcement funding under the Dodd-Frank Act, Canadian companies are spending more and more time learning about the implications of FCPA and the CFPOA and related exposures. Canadian companies should also be aware of other international anti-bribery laws that parallel the FCPA in its prohibition against bribery including but not limited to the UK Bribery Act, which also imposes liability on organizations for failing to prevent bribery.

Canadian companies, especially in the mining, engineering and resource sectors, are large players on a global scale, owning, operating, and developing substantial foreign-based properties. Not all of these countries operate in a manner consistent with the North American regulatory regime. Specifically, the widespread culture of corruption of public officials in some jurisdictions is of serious concern. Therefore, a risk analysis based on jurisdiction is crucial for Canadian companies operating abroad.

The investigation and subsequent charges against Canadian companies continues and their ultimate resolution will reshape the Canadian experience. With more stringent legislative changes likely coming in the not too distant future, including the eventual abolishment of facilitation payments under Canadian law, the landscape in Canada is changing quickly. Companies now must have a proactive approach to their own governmental dealings both at home and abroad.

With increased enforcement of anti-bribery laws and the high federal and reputational costs of foreign corrupt practices investigations, companies and their directors and officers should assess and mitigate their risk. Companies should consider specific risk management and corporate governance practices and policies to help prevent future incidents. In addition to implementing appropriate preventative strategies, companies and their directors and officers may want to consider Marsh's proprietary insurance solution, FCPA Corporate Response, which provides insurance coverage for the costs of investigations of foreign corrupt practices for both the organization and the individuals.

7. REGULATORY ACTIVITY IN CANADA & NEW WHISTLEBLOWER PROGRAMS

According to the 2016 Enforcement Report by the Canadian Securities Administrators (CSA), the counsel of the 13 securities regulators in Canada, 2016 was another demanding year for the Canadian securities enforcement community. There were 56 proceedings commenced in 2016 against 72 individuals and 72 companies. In addition, CSA members concluded a total of 109 cases in 2016, involving 168 individuals and 94 companies. Total fines and administrative penalties for 2016 were approximately $62.1 million. The CSA report stated that as a result of closer collaboration with law enforcement agencies, there was an increase in the number criminal proceedings commenced and concluded in 2016, as well as several noteworthy prison sentences for 4 years, 3 years and 27 months respectively. The CSA Reported stated that the Ontario Securities Commission (OSC) has returned approximately $320 million to investors through its no-contest settlement program. Significantly, in 2016 the OSC and Autorité des marchés financiers (AMF) launched whistleblower programs to encourage individuals to come forward with tips relating to potential violations of securities laws. The whistleblower program offers compensation of up to $5 million to individuals who offer tips that lead to enforcement action. According to Maureen Jensen, Chair and CEO of the OSC, "[o]ur whistleblower program is a powerful addition to our enforcement arsenal and a game-changer for securities enforcement in Canada." In the United States the whistleblower program, which made it first award in 2012, approximately $149 million has been awarded to 41 whistleblowers, approximately $75 million of which was awarded in 2016. It will be interesting to see the impact of whistleblower programs in Canada.

Increased regulatory scrutiny puts greater demand on directors and officers of Canadian companies to fulfil their fiduciary obligations. It also means that directors and officers of Canadian companies may face an increased risk of being targeted in a regulatory investigation or proceeding. Some insurers have expanded the scope of their D&O policies to include coverage for pre-claim costs to individuals in respect of regulatory investigations, so that coverage may be triggered at an earlier stage under the policy for directors and officers when the regulators come knocking. A limited number of insurers have launched stand-alone policies that provide coverage for organizations in the event of an investigation by the SEC, DOJ, provincial securities commissions or other securities enforcement authority. The scope of coverage varies considerably and should be carefully reviewed.

8. OIL, GAS AND MINING

2016 continued to be a difficult year for Alberta's petroleum sector as it felt the negative impact of low crude oil prices and persistently weak natural gas prices. The effects were widespread on the industry as West Texas Intermediate (WTI) fell to $26 per barrel in February 2016 and an estimated 40,000 people have been laid off since the oil price collapsed in 2014. By April of 2016 there was a clear decline in borrowing bases and bankruptcies and debt restructuring were taking place throughout the sector. Companies entered into survival mode for the most part, managing their cash situation closely, while lenders tightened terms and conditions of financing, forcing many businesses to alter their business strategies to adjust.

There are some signs of a modest rebound in 2017, although industry analysts are cautious at best. Drilling activity is expected to increase in 2017 but will still fall short of pre-recession levels in 2014, and the mind-set is towards shorter cycle projects, with several projects being deferred or even cancelled as a result of the downturn. On a more positive note, some analysts are suggesting IPOs could launch in 2017 as oil and gas companies look for fresh equity. We most certainly will continue to see further consolidation in the sector as the large, more financially sound companies look for opportunistic acquisitions.

The mining sector is facing similar challenges to companies in the oil and gas sector as commodity prices such as gold, silver, palladium, nickel and copper have been depressed for a prolonged period of time. In particular, a number of gold mining companies are struggling with high debt levels due to acquisitions made while the gold price was steadily increasing, hitting a high of nearly $1,900/oz. in 2011. Many of these acquisitions have since been written down as the price of gold declined. In addition to collapsing metal prices, companies continue to fight cost overruns in the construction of their mines, increasing their cash costs. As well, foreign governments have made investments outside of North America even more challenging for mining companies with operations internationally. Mining companies in Ontario have also been under increased scrutiny by the MMOEC as remediation orders have in certain instances been issued against directors and officers, as well as, their respective companies when a pollution event takes place and the company is concurrently experiencing financial distress.

Companies engaged in the commercial development of oil, gas and minerals will be particularly interested in the Extractive Sector Transparency Measures Act (ESTMA), that introduces new reporting and transparency obligations on the Canadian extractive sector. The Act is designed to contribute to global efforts against corruption in this sector and failure to comply with ESTMA could lead to penalties up to $250,000 per offense per day against companies and their directors and officers.

According to NERA Economic Consulting, the proportion of securities class actions brought against companies and their directors and officers in the minerals (both energy and mining) sectors has increased significantly. Publicly traded companies in oil, gas and mining continue to be targets from a securities class action litigation perspective. As a result, D&O underwriters are taking a harder look at these risks.

Well-positioned companies with strong balance sheets are taking advantage of reduced evaluations and favourable opportunities, while other companies will file for restructuring in Canada, or even bankruptcy. Both of these scenarios may attract personal liability for the companies' directors and officers. Some companies with extreme debt levels and severe cash flow challenges, unable to service their debt, may resort to recapitalization, exchanging debt into equity. As creditors have turned into majority shareholders, a change-in-control can take place which impacts coverage under the companies' D&O policies. In such situations, it is essential to provide continuous coverage beyond the recapitalization.

Companies with environmental risk exposures and regulatory exposures such as the new ESTMA will need to carefully consider how their insurance program may respond to personal liability in such an event or breach. Many directors and officers are looking for coverage under their directors and officers liability policies only to find that coverage is either non-existent or extremely limited.

9. MERGER AND ACQUISITION TRENDS AND TRANSACTIONAL RISK

If the tea leaves that we are reading and hearing about from the deal community are correct, then 2017 will continue the trend of a highly competitive and active year in the Canadian mergers and acquisitions (M&A) market. The competition looks to remain strong as private equity firms continue to battle with both pension funds and strategic buyers to find deals that will drive value both in the near term and in the long run. The participation of international interests continues to be high and will likely continue the ancillary effect of increased regulatory review.

Acquiring a new asset or business entails risk but private equity fund managers, corporate executives, risk managers and other stakeholders can mitigate some of the uncertainty with the right kind of contractual protections in the underlying purchase agreement or, increasingly, by utilizing transactional risk insurance. Traditionally, transactional risk insurance was used to protect against risks that arose during due

diligence but is now being used by both buyers and sellers strategically as a key component of M&A transactions. Transactional risk insurance is now a commonplace feature in the M&A landscape in Canada and globally. Private equity funds, corporate buyers and sellers, as well as individuals, can benefit from transactional risk coverages including representations and warranties insurance (R&W insurance), tax indemnity insurance and contingent liability insurance.

In the case of R&W insurance, it provides protection to the insured against financial loss, including defence costs, resulting from breaches of the representations and warranties made by the target company or the seller(s) in a purchase agreement. It is by far the most frequently used transactional risk coverage in Canada and is now a critical tool in facilitating M&A negotiations. For example, in competitive private company auctions R&W insurance allows buyers to distinguish their bids by requiring only minimal or no survival of the seller(s) representations and warranties. Sellers can then walk away post-closing without having to maintain long standing indemnity obligations, freeing up much needed capital for other ventures or putting capital back into the hands of investors faster. The rapid growth and acceptance of R&W insurance over the last few years has now made it more important than ever for deal professionals and risk managers to understand the product and how to use it strategically to get ahead.

10. INTERNATIONAL OPERATIONS & LOCALLY ADMITTED POLICIES

The area of D&O liability continually changes and it is now clear that significant exposures for directors and officers are no longer limited to North American legal and regulatory actions. Compliance, accountability and transparency are on the lips of many global governments and regulators, which heighten the risk for foreign executives. Governments continue to introduce new laws and aggressive regulators are gaining stronger powers and better tools for enforcement. Legal activism continues to rise with a noticeable shift toward introduction of pro-plaintiff legislation in Europe and elsewhere.

Until recent years, Canadian corporations commonly purchased D&O insurance with insurers licensed in Canada. The policy territorial limits were worldwide, intending to respond to, defend, and settle claims against companies and their directors and officers which may be brought in any jurisdiction in the world. Consequently, companies often concluded that coverage was provided by these policies issued in Canada for the perceived minimal liability exposures of directors and officers serving in jurisdictions outside North America. What they may not have focused on until recently was where the policy would pay: on the ground where the claim was brought or here, where the D&O policy was placed.

Many foreign executives have now expressed concerns regarding the availability of indemnification protection from the parent company or its local subsidiary and the extent of protection offered by a single global tower of insurance issued in Canada. There are circumstances where corporate indemnification or insurance may be unavailable. For example, indemnification and/or advancement of defence by the either the local subsidiary or the corporate parent may prohibited by local law, or inadvisable. Or local law in many jurisdictions may prohibit insurers not licensed in a particular foreign jurisdiction from insuring local D&O risk.

Understanding and complying with foreign regulations and laws that can affect insurance procurement decisions is complex as:

- Rules are subject to legal interpretation which may be inconsistent. For example, not everyone concurs about which countries allow insurance not procured locally or where the company may be permitted to indemnify their executives.
- Many countries do not have any laws or statutes dealing with the issues of indemnity, advancement of defense or permissibility of locally unlicensed insurance, therefore indemnity and insurance certainty cannot be provided. In many jurisdictions the local laws are either unclear or untested. Because of the still relative scarcity of lawsuits in many jurisdictions, there is little or no case law available to lawyers to interpret opaque regulation. In any event, the value of case law is diminished in many jurisdictions as many countries do not have a common law legal system weighting past rulings.
- Compliant organizations are also concerned with the international tax implications where persons or organizations in a local country have the benefit of being covered by insurance placed in another country, which happens where there is a single global program of insurance; local placements also address applicable local premium taxes.

Multinational companies, which have been grappling with these issues for decades on their property and casualty programs, now need to understand the multitude of laws, regulations and nuances of each foreign jurisdiction in which it operates and how these laws change and can impact D&O insurance. To assure that a company's management liability program will perform fully in countries outside North America, companies should consider the purchase of local policies where they operate and have directors or officers or local equivalents. Where companies have minority owned joint ventures with significant assets and/or personnel seconded to these operations, they should consider

strategic alternatives to ensure adequate local D&O insurance. Coverage should be in compliance with local regulation from a carrier with developed resources in those jurisdictions. Coverage needs to be global in scope, but tailored to the local regulations of the respective foreign jurisdictions.

Whether or not D&O insurance from a Canadian insurer is prohibited in foreign jurisdictions, prudent insureds are erring on the side of caution and implementing coverage with carriers admitted in the relevant jurisdictions. Not only does this demonstrate to their local directors and officers effective and compliant coverage, but it also reduces the chance of associated regulatory problems and preserves the insureds' ability to rely on the regulatory capacity of the foreign jurisdiction to enforce carrier compliance. It is now increasingly important to work with a truly global multinational broker who can provide solid risk advice and those insurers who are best able to issue local admitted policies, respond to claims and demonstrate an ability to arrange payment in foreign jurisdictions.

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Marsh's FINPRO Practice is committed to keeping clients updated as to important developments relating to the legal and business trends that impact Canadian companies or companies with Canadian exposures. Marsh FINPRO brokers are specialists in directors and officers liability insurance and risk management. As such, we are well-positioned to assist our corporate clients and their directors and officers in identifying their exposures and obtaining the protection they need through a combination of effective risk management and the maintenance of appropriate insurance policies. We invite you to contact your local Marsh representative to discuss your needs.

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