The Cover Note

Fall 2012 - Volume 5 Issue 3

EDITORIAL

Barry F. Lorenzetti

BFL has been offering insurance, risk management and employee benefit services to Canadian companies with activities on the international scene, as well as foreign companies with activities in Canada, for many years now. As an independent brokerage, with the strong desire to remain independent, we resorted to creating alliances with other brokers around the world in order to respond to evolving international client needs.

However, going forward, we will be able to further personalize and broaden the range and depth of services we provide these organizations.

Earlier this year, along with a group of foreign independent brokers, BFL founded Lockton Global LLP, a legal partnership of more than 30 leading privately owned insurance brokers around the world.

One of the great strengths of the Lockton Global partnership is that our broker partners deal with each other because we want to, not because we have to.

And what all the Partners want is to provide each client with the kind of service you are entitled to i.e. superior service, as part of an overall impeccable client experience. We are simply client-centric in our approach to delivering professional services. Our Partners have consistently committed to treat every client as their own when we were an informal alliance and so it will continue now that we are partners in the same venture.

Globalization has changed both our clients' businesses as well as ours. While clients speak with us locally and they trust us to guide them when dealing with international issues, they do realize that we, in turn, need to be able to rely on a solid global team with local knowledge and similar service standards, in order for seamless communications and relevant and effective service to be achieved. We deliver world-wide services through your local single point of contact.

To embark on this new initiative, which I regard as an extension of the BFL culture and business model, makes sense for both our clients and our team of professionals. If anything, it will only strengthen existing relationships and open the door to new ones as well.

As of this year, Lockton Global will be offering its founding members access to a series of tools which will further equip our professionals and as a consequence, enhance client experience even more. This includes international specialty practice groups as well as an online Account Management System.

This will be a memorable year for BFL. In our 25th anniversary year, we are embarking on an international adventure of great promise with trusted and respected Partners, all the while remaining totally independent and 100% employee owned!

Our feature article, written by our Vice-Presidents and Directors and Officers Practice Leaders, Lyne Benoît from our Montreal office and Eddie Fung from our Calgary office, deals with D&O liability and corporate exposures in Canada. Finally, our Employee Benefits Division article discusses Group Insurance Plans. ♦

Globalization has changed both our clients businesses as well as ours.

In this issue

INCREASING DIRECTORS AND OFFICERS AND CORPORATE EXPOSURES IN CANADA

Lyne Benoît, Vice-President, D&O Practice Leader (Eastern Region),
BFL CANADA Risk and Insurance inc., Montreal

Eddie Fung, Vice-President, D&O Practice Leader (Western Region),
BFL CANADA Insurance Services Inc., Calgary

Areas of trending, or the start of a trend, can be seen in Canadian exposures relating mainly to Bill 198, increasing regulatory investigations, Foreign Corruption, and to Bill C-45. We are providing below an overview of the situation.

Public D&O liability has always been the most prominent segment of the three primary classes of D&O insurance coverage due to the publicity of class actions required by disclosure regulations and media attention: Public Company D&O, Private Company D&O and Not for Profit D&O (NFP), but we cannot ignore the other two segments. Claims are also increasing on the private company and NFP segments; it may very well be evidence of the increasingly litigious nature of the Canadian environment. Although there is no regulatory body tracking litigation for private companies, there is no reason to believe it is not following the same trend. Securities allegations can also be made against private companies.

Private and NFP D&O is seeing favorable treatment from the D&O insurance community. Almost all insurers are actively pursuing growth in these segments in an attempt to diversify their heavy public portfolios. As such, the competition, coupled with coverage developments, are seeing drastically reduced premiums with increasing coverage grants on these two segments. Notably, some insurers are providing defence costs outside of policy limits (outside of Quebec) coupled with either deleted or softened 'hammer' clauses.

Canada's geographic landscape has been described as both beautiful and rugged and this metaphor can be used to describe the impact of Bill 198 to D&O Liability exposures. Prior to 2005 the high evidentiary burden imposed on Plaintiff's bar resulted in few shareholder actions, but Bill 198 changed all that enforcing continuous disclosure obligations defined under the Ontario Securities Act (OSC) and similar provisions in other provincial securities acts. Bill 198 was referred to as the Canadian Sarbanes-Oxley.

Bill 198 has resulted in a surge in securities class actions filings in Canadian courts. In 2011, nine of the 15 new cases were the result of Bill 198. Since the advent of Bill 198, there have been 35 cases. Over the past four years (2008-2011) Canadian courts saw an average of 8 new cases in each of the past four years.

Surveillance and enforcement is a global trend with ever more regulation and even more regulatory bodies in certain cases. And the situation is not any different in Canada. The Canadian Securities Administrators (CSA), the umbrella organization of Canada's provincial and territorial securities regulators, released their 2011 Enforcement Report and the highlights of the concluded cases are:

- 66 involved illegal distributions (which represented the largest category of concluded cases);
- 124 involved a total of 237 individual and 128 companies that resulted in fines and administrative penalties of more than $52 million, nearly $50 million in restitution, compensation and disgorgement and jail sentences against eight individuals;
- 63 interim orders restricting trading and/or freezing the assets against 109 individuals and 108 companies;
- 47 of the 124 concluded cases were concluded by a contested hearing before a tribunal;
- And finally 31 appealed cases, an increasing number.

Canada's Corruption of Foreign Officials Act (1998) saw its most high profile case in 2011 with the conviction and imposition of a CAN$9.5M fine against Niko Resources Ltd. based in Calgary, Alberta, from bribery relating to its operations in Bangladesh. Immediately after the conviction, it was reported that Plaintiff's bar began to examine and investigate the disclosure and stock option practices of Niko. Currently, we are all looking at the Montreal-based SNC–Lavalin, an engineering and construction firm with international contracts, following the scandal surrounding questionable payments to secure contracts in North Africa. A Toronto law firm has filed a $1.5 billion lawsuit on behalf of investors, alleging the company's directors are liable for the firm's stock loosing 28% of its value because of the unfolding scandal.

Canada's other idiosyncratic statutory impact on D&O exposures is Bill C-45, commonly referred to as the "Westray Bill", named after the 1992 Westray coal mining disaster in Nova Scotia.

Bill C-45, which became law on March 31, 2004, added Section 217.1 to the *Criminal Code* to impose a duty on organizations and their representatives (whether a director, partner, manager, supervisor, employee, member, agent or contractor of the organization) who have authority to direct how others do work or perform a task to take reasonable steps to prevent bodily harm to persons performing the work or task, and to the public, arising from the work or task. Bill C-45 is expected to increase in activity with the necessary resulting judicial interpretation to follow; to date there have been four cases where charges have been laid. On June 15, 2012 following a guilty plea to a charge of criminal negligence causing death, Metron Construction Corporation of Ontario, was fined $200,000 and its president was also fined $90,000. The fine amounted to three times Metron's net earnings in its last profitable year. Canadian D&O insurance policy language can be amended to provide an element of coverage to respond to Bill C-45 claims.

Bill C-45 and the Corruption of Foreign Officials Act are both federal laws that apply to all provinces. Bill 198 provides regulation of securities issued in Ontario. In Quebec, the Autorité des marchés financiers regulates such activities, and the other provinces have their own. Canada's legal system is unique: Quebec is governed by civil law written into the Quebec Civil Code, and the rest of Canada is governed by common law. When it comes to D&O liability insurance, the main difference lays in the definition of "loss" which includes defence costs in Common Law jurisdictions.

Article 2503 of the Québec Civil Code dictates that "Costs and expenses resulting from actions against the insured, including those

BFL CANADA Risk and Insurance Inc.
45 Westwind Drive
Hammonds Plains, NS B3Z 1K6
Tel: 902-864-4982
Fax: 902-864-0200

2590 Laurier Blvd, Suite TBC 600
Quebec City, QC G1V 4M6
Tel: 418-658-6337
Fax: 418-654-2045

2001 McGill College, Suite 2200
Montreal, QC H3A 1G1
Tel: 514-843-3632
Fax: 514-843-3842

BFL CANADA Risk and Insurance Services Inc.
2685 Queensview Drive, Suite 101
Ottawa, ON K2B 8K2
Tel: 613-722-7798
Fax: 613-722-7829

181 University Avenue, Suite 1605
Toronto, ON M5H 3M7
Tel: 416-599-5530
Fax: 416-599-5458

BFL CANADA Insurance Services Inc.
175 Carlton Street, Suite 205
Winnipeg, MB R3C 3H9
Tel: 204-594-0260
Fax: 204-594-0259

877 Henderson Highway
Winnipeg, MB R2K 2L8
Tel: 204-661-2446
Fax: 204-663-0344

1167 Kensington Crescent NW, Suite 200
Calgary, AB T2N 1X7
Tel: 403-451-4132
Fax: 403-313-3365

5185 South Ridge Drive
Kelowna, BC V1W 4Z4
Tel: 250-863-8859
Fax: 778-477-0011

1177 West Hastings Street, Suite 200
Vancouver, BC V6E 2K3
Tel: 604-669-9600
Fax: 604-683-9316

1-866-688-9888

of the defence, and interest on the proceeds of the insurance are borne by the insurer over and above the proceeds of the insurance." This difference is a major advantage to Quebec insureds when you consider the length of time a case may be in front of the courts, and the total legal burden to defend such D&O claims. Everywhere else defence costs are not legislated to be excess of policy limits.

Notwithstanding the four main sources of litigation listed at the beginning of this article, there are also other emerging issues:

- In addition to and related to increasing Bill 198 actions, we are seeing the increase in parallel filings and cross-border cases in Canada, whether inter-provincially within Canada, or Canada-USA parallel filings; Filings against Chinese companies trading on Canadian stock exchanges (Sino-Forest), and effects on Canadian companies trading on a non-Canadian exchange (Canadian Solar; effects of Morrison v. Australia Bank) are the new trends being monitored throughout North America.
- M&A litigation: All the while, Canada is enjoying a strong dollar and stable economy; we are therefore seeing an increase in mergers and acquisitions. It has been the biggest single trend in the US in the past two years and as trends go, Canada usually catches up a little later so we can also expect an increase in this type of litigation.
- Cyber litigation is another area of concern for D&O or more specifically the failure to put in place processes and devoting the resources to protect the company.
- Canadian Revenue Agency (CRA) is enforcing compliance regulations for Canadian applicable insurances. Insurance applicable in Canada must be placed in Canada using authorized markets and Canadian-domiciled brokers, or be at risk of fines and penalties following an audit by CRA or provincial authorities. Fines and Penalties differ between provinces, but some of them are quite stiff.

Canada remains in the early growth in the class action bar, and the related success of class counsel and the attractiveness of the Canadian judicial environment for non-US investors and stocks seem to provide a favorable environment for an upward trend. Canadian law firms have been supported by well-known US securities class actions plaintiffs firms, and some of their attorneys have been called to the Ontario bar. It is expected that the trend in increasing securities class actions in Canada and other regulatory enforcement will continue.

When compared to our neighbours to the south, it is evident that litigation is not as prevalent in this country. It is often said that Canadians are less litigious by nature, but one could say that a major deterrent to bringing forward a case in front of a judge is Ontario's cost regime of "loser pays" for companies traded on TSX. As previously mentioned, the legal burden can be quite costly in Canada, so in addition to your own cost you need to consider the unfortunate conclusion of losing your case, and having to pay the other party's legal expenses.

We have presented above a very limited portrait of D&O Liabilities in Canada, but it should serve as a reminder, as new corporate governance rules are proposed and disclosure regimes are introduced, that more regulatory investigations will be triggered for failure to comply, and with that, new litigation, which, in turn, will bring new coverage demands upon insurers.

The exposure of D&O has been evolving constantly with the business, financial and regulatory environments and from all evidence, will continue to do so. One would be prudent to keep an eye on any development in order to anticipate, and properly manage new or enhanced risks for D&O in your organization. ♦

DOES YOUR GROUP INSURANCE MEET THE NEEDS?

Dominique Richer, Group Insurance Broker,
BFL CANADA Consulting Services Inc., Montreal

We all know that being healthy is essential in order to accomplish our daily tasks, whether at work or at home. This shows just how necessary it is for an insurance benefit plan to include a broad range of health insurance coverages. In fact, employers as well as employees assess their benefit plan based on the level of health care reimbursements, such as medication, health care professional treatments (physiotherapy for example), dentist care or out-of-province travel insurance coverage.

But, what about the risks associated with partial or total disability? What would be the consequences on your employees' family life, not to mention the effects on the daily operations of your company? Why is it that some employers pay little attention to a protection considered essential by their own employees, i.e. income replacement benefit for disability, serious illness or accident? Your company has to fulfill its commitments towards its clients, suppliers, creditors, shareholders, etc., the same applies to your employees' families and their own creditors.

What kind of financial support would your employees receive in case of disability? Would the income compensation received be sufficient or would they have to take out loans or sell some of their investments? Providing appropriate disability coverage to your employees would allow them to continue a normal life, in spite of disability, whatever the length of time their recovery and absence from work lasts.

Nobody is immune to the risk of serious illness or accident.

It is part of your benefits advisor's role to make sure your company's program provides optimal conditions, or, if not, to show you how to improve it, as well as to explain the reasons why you should improve it. Your group insurance plan most probably provides for a whole range of coverages. However, are your employees properly covered in case of disability?

Let's consider a few parameters. First, the benefit amount can be taxable or non-taxable, depending on the definition of the paying agent:

- If the employee pays 100% of the disability insurance premium, the benefit will be non-taxable
- If the employer pays 1% or more of the disability insurance premium, the benefit will be taxable

Second, let's look at the benefit formula. It could differ according to the parameters set by the insurer. For example, 85% or 90% of the monthly net income could be used to calculate the maximum benefit.

Furthermore, the benefit formula could also be inequitable. Here is an example of how to calculate a premium for a monthly benefit in relation to the indemnification ceiling that will be paid by the insurer, as per the usual terms and conditions of contracts:

CALCULATION OF THE BENEFIT TO DETERMINE PREMIUM **66.7% of the total monthly salary of the maximum amount of benefit of $5,000**	**$5,000 x 66.7%**	**$3,335 (a)**
CALCULATION OF THE PAYABLE BENEFIT CEILING **Maximum amount of benefit from all sources (Net salary x 85%)**	**$3,000 x 85%**	**$2,550 (b)**
Difference between the two amounts		**$785 (a - b)**

We see above that there is a difference of $785 between the calculation of the amount of the benefit to determine premium and the maximum amount of benefit which will be payable to the employee by the Insurer. This fictitious employee is therefore unnecessarily paying premium on an amount of $785. By reviewing the calculation formula, your benefits advisor could correct this inefficiency and produce savings for your employees, preventing them from having to pay premium on the portion of a benefit they can never collect from the Insurer in case of disability.

In addition, an inequitable formula usually creates tax inefficiencies as well and those would also need to be addressed.

This type of situation does not only happen to others. That is why you need the advice and expertise of a qualified benefits advisor who will inform you about the various elements benefits plans, including the quality of benefits offered, their practicality for your employees, and their day to day importance for you the employer, as well as for employees. Besides, we all know that an efficient and comprehensive benefits plan is a powerful recruitment and retention tool. A matter that should not be neglected as Canadian society is about to experience a serious shortage of manpower with the upcoming mass retirement of baby boomers. ♦

BFL CANADA Consulting Services Inc.
2590 Laurier Blvd, Suite TBC 600
Quebec City, QC G1V 4M6
Tel: 418-658-6337
Fax: 418-654-2045

2001 McGill College, Suite 2200
Montreal, QC H3A 1G1
Tel: 514-937-4188
Fax: 514-937-5585

181 University Avenue, Suite 1605
Toronto, ON M5H 3M7
Tel: 416-599-5530
Fax: 416-599-5458

1177 West Hastings Street, Suite 200
Vancouver, BC V6E 2K3
Tel: 604-669-9600
Fax: 604-683-9316

1-866-688-9888

Send comments or suggestions to publications@BFLCANADA.ca