

# Canadian Securities Administrators Proposed Corporate Governance Regime

March 4, 2009

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# Overview

- Request for Comment
- Background and Purpose
- Summary of Proposed Materials
- ASC Concerns with Proposed Corporate Governance Regime

# Request for Comment

The CSA has published for a 120-day comment period the following proposed materials:

- National Instrument 58-101 *Disclosure of Corporate Governance Practices*
- National Policy 58-201 *Corporate Governance Principles*
- National Instrument 52-110 *Audit Committees*
- Companion Policy 52-110CP *Audit Committees*

The proposed materials would replace the following instruments and policies currently in effect:

- National Instrument 58-101 *Disclosure of Corporate Governance Practices*
- National Policy 58-201 *Corporate Governance Guidelines*
- National Instrument 52-110 *Audit Committees*
- Companion Policy 52-110CP *Audit Committees*

Comment Period ends on April 19, 2009

# Background and Purpose

- April 2005: commitment to review current regime following implementation
- September 2007 - CSA Staff Notice 58-304: communicated plans to undertake broad review of current corporate governance regime and to publish proposed amendments (if any) in 2008
- Examined corporate governance regimes in other jurisdictions
- Considered realities of large number of small issuers and controlled issuers in Canadian market

# Summary of Proposed Materials

- The Proposed Corporate Governance Regime contemplates:
  - establishing nine broad corporate governance principles;
  - requiring issuers to disclose their governance practices that achieve objectives of principles; and
  - a new definition of “independence” that would eliminate current “bright-line” tests with a seemingly exhaustive list of factors to consider.
- Proposed Regime would require ALL reporting issuers (non-venture and venture) to report annually on their governance practices in relation to each high-level principle in *Proposed NP 58-201*.

# Summary of Proposed Materials

(cont'd)

- The nine corporate governance principles cover the following areas:
  1. Framework for oversight and accountability;
  2. Board structure;
  3. Attracting and retaining effective directors;
  4. Improving board's performance;
  5. Promoting integrity;
  6. Recognizing and managing conflicts of interest;
  7. Recognizing and managing risks;
  8. Compensating appropriately; and
  9. Engaging effectively with shareholders.

# Summary of Proposed Materials

(cont'd)

- Each principle in *Proposed NP 58-201* includes commentary that provides background and explains reason for principle, along with examples of practices that could achieve principle's objectives
- No single model of good corporate governance – issuer should formulate governance practices appropriate for individual issuer
- Disclosure requirements under *Proposed Form 58-101F1 Corporate Governance Statement* based on an “explain only” model (vs. current “comply or explain” model for non-venture issuers)

# Summary of Proposed Materials

(cont'd)

- Under *Proposed Form 58-101F1*, mandatory for issuers to disclose certain information in areas covered by each principle and any corporate governance practices used to achieve objectives of principles
- Each issuer required to provide disclosure annually in information circular (if no information circular prepared, then disclosure in AIF or annual MD&A)
- Disclosure requirements in *Proposed 58-101F1* apply to ALL reporting issuers (non-venture and venture)

# Summary of Proposed Materials

(cont'd)

## Proposed Definition of Independence:

- same definition of “independence” would apply for the purposes of the board generally AND audit committee membership
- additional requirements for audit committee membership removed
- “bright-line” tests no longer imposed, but seemingly exhaustive list of factors to consider in assessment of independence (section 3.1 of *Proposed NI 52-110*)
- proposed definition of “independence” similar to current broad, materiality-based definition

# Summary of Proposed Materials

(cont'd)

## The proposed definition is as follows:

*An independent director is a director of an issuer who:*

- (a) is not an employee or executive officer of the issuer; and*
- (b) does not have, or has not had, any business or other relationship with the issuer or its executive officers which could, in the view of the issuer's board having regard to all relevant circumstances, be reasonably perceived to interfere with the exercise of his or her independent judgment .*

# Summary of Proposed Materials

(cont'd)

- focus on any relationship with issuer or its executive officers (vs. current definition's "*direct or indirect material relationship*")
- employees and executive officers of issuer could never be considered independent
- board must perform objective test to determine a director's independence, i.e. proposed definition captures relationships that are reasonably perceived to interfere with exercise of independent judgment (in contrast to current definition which captures relationships that are reasonably expected to interfere with exercise of independent judgment)

# ASC Concerns with Proposed Corporate Governance Regime

## WHY IS THE ASC CONCERNED?

It is in the interests of all market participants that the application of the proposed regime (primarily those parts concerning independence) does not result in either:

**(a)** the board being denied the services of a valuable director;

or

**(b)** the issuer distorting the independence assessment in order to retain that director.

Neither outcome would be beneficial to issuers, boards or shareholders.

# ASC Concerns with Proposed Corporate Governance Regime

## INDEPENDENCE

“A director is independent if he or she

(a) is not an employee or executive officer of the issuer; and

(b) does not have, or has not had, any relationship with the issuer, or an executive officer of the issuer, which could, in the view of the issuer’s board of directors having regard to all relevant circumstances, be **reasonably perceived** to interfere with the exercise of his or her independent judgment.”

# ASC Concerns with Proposed Corporate Governance Regime

- Proposed definition of “independent” director essentially turns on reasonable person’s perception as to whether or not that director can exercise independent judgment
- In other words, the board’s subjective assessment is not the determining factor

QUESTION: Is the reasonable person litmus test appropriate?

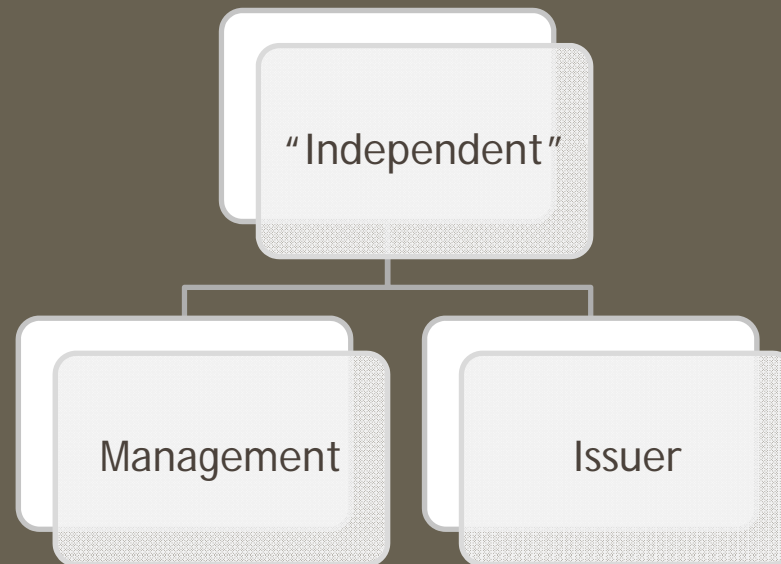
# ASC Concerns with Proposed Corporate Governance Regime

- In the alternative, would it be appropriate to:
  - (i) require that the board, relying on its collective knowledge and expertise, make a determination that the director is capable of exercising independent judgment; and
  - (ii) require that such a determination be reasonable?

# ASC Concerns with Proposed Corporate Governance Regime

## INDEPENDENCE & CONTROL PERSONS

- Under the proposed regime:

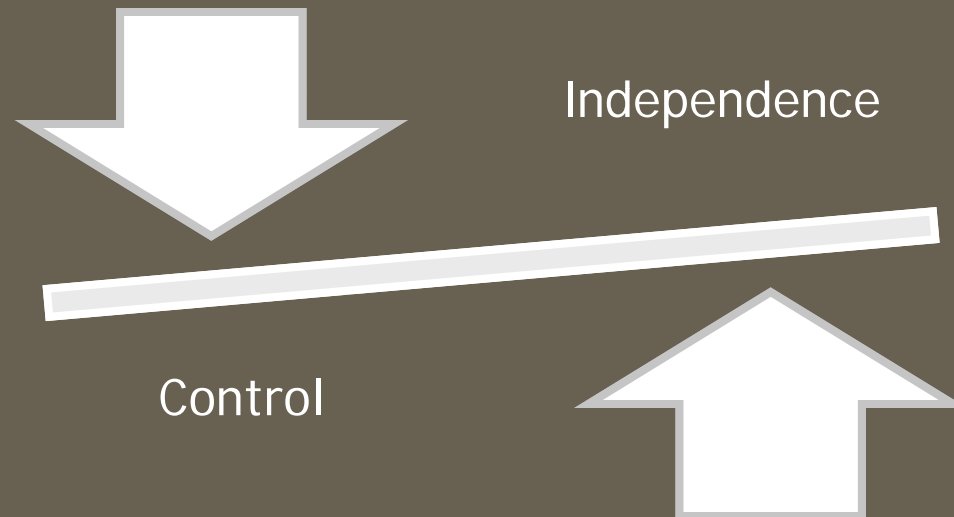


# ASC Concerns with Proposed Corporate Governance Regime

- In addition, the proposed regime includes a specific reference to addressing conflicts of interest (Principle 6 of NP 58-201)
- Principle 6 is specifically formulated to recognize that the concerns of self-dealing by control persons can be addressed through an issuer's conflict of interest policies and related practices

# ASC Concerns with Proposed Corporate Governance Regime

- Proposed regime forges an ideological link:



QUESTION: Is this ideological position appropriate?

# ASC Concerns with Proposed Corporate Governance Regime

## INDEPENDENT... WHY?

- Proposed regime requires that each issuer explain why each independent director has been labeled as such

QUESTION: Is it appropriate to require such an explanation?

# ASC Concerns with Proposed Corporate Governance Regime

## NOT INDEPENDENT... WHY?

- Directors who are not identified as independent would be required to be identified as being “not independent”
- In addition, issuers would be required to explain why such directors are “not independent”

QUESTION: Is such a label appropriate? Is such an explanation appropriate?

# ASC Concerns with Proposed Corporate Governance Regime

- The term “not independent” has a strong negative connotation:





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