

December 10, 2004

Mr. Gilles Gauthier  
Director  
Corporate and Insolvency Law Policy Directorate  
Industry Canada  
235 Queen Street, Room 561-F  
Ottawa, Ontario  
K1A 0H5

Dear Mr. Gauthier,

On behalf of the Canadian Coalition for Good Governance please find attached our submission to Industry Canada in response to *Towards an Improved Standard of Corporate Governance for Federally Incorporated Companies: Proposals for Amendments to the Canada business Corporations Act*.

We believe a combination of legislation, regulatory rules and guidelines are appropriate to the smooth functioning of capital markets and to the effective working of corporate boards. We think it might be appropriate in your preamble to state that the purpose of these amendments is not only to make the CBCA more attuned to the current state of capital markets but also to the current beliefs about best practices for boards to go beyond 'oversight' to the creation of shareholder value.

No company, whether operating in a foreign jurisdiction or not should be exempt from these provisions.

As our members normally own the larger capitalization stocks we do not have a strong opinion on the applicability of these rules to much smaller corporations.

As a matter of principle the Coalition believes that no corporation should have dual class share structures that allow one class of share different voting rights than other classes of shares. There are some 110 such companies currently listed on the TSX (see Appendix A for the 'fairness' frontier). Any corporate governance regime is suspect if all the structures, protections and processes can be negated by a voting interest well beyond the economic interest as, for example, is the case with Magna.

We would certainly favour the abolition of such dual share class structures and would certainly not wish any new ones to be created.

Yours truly,

Professor David R. Beatty O.B.E.  
Managing Director

## **Comments on Towards an Improved Standard of Corporate Governance for Federally Incorporated Companies: Proposals for Amendments to the Canadian Business Corporations Act**

The Canadian Coalition for Good Governance is a national not-for-profit organization comprised of over 50 members, including pensions funds, money managers and mutual funds, with over C\$550 billion in Assets under Management.

### **Governance in the Largest Canadian Public Companies is Improving**

The Coalition has published its own governance guidelines (these guidelines can be found at [www.ccg.ca](http://www.ccg.ca)). Since they were first published the Coalition staff have assessed over 50 of Canada's largest companies and met in person with the Chairs of these companies to discuss the details of our guidelines and their practices.

In addition, the Coalition purchases from the Rotman School of Management at the University of Toronto the results of the Rotman Board Shareholder Confidence Index. The BSCI is a rating system that measures adherence to the Coalition's governance guidelines.

You will see in the attached Appendix B a set of three PowerPoint slides that show the level of improvement. These 'quantitative' results are corroborated by the Coalition's 'qualitative' conclusions. Governance in the largest Canadian public companies is improving.

Yet, much remains to be done and for those companies under the CBCA your proposals are welcome.

In the remaining sections of this response we go into further detail in three sections:

1. Electing independent directors
2. Ensuring independence in board structure and systems
3. Enhancing the credibility of financial statements

World-class governance practices in Canadian public markets will make capital markets more efficient and effective – you will see that institutional investors do pay attention to national governance standards.



## 1. Electing independent directors

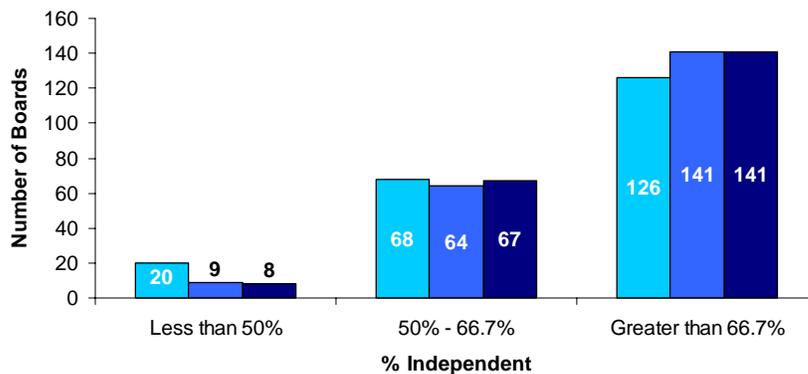
There are three sections that relate to the election of independent directors:

### 1. Establishing the meaning of independence

The Coalition believes that a **majority** of directors should be independent. There are a number of different standards some more exacting than others.

In the Rotman BSCI measurements there are now only 8 companies on the S&P/TSX Index that have less than a majority of independent board members

### Independence of Board Members



We agree with your Proposal 6 ...that the definition should be in the regulations and that the specific criteria you propose are apt. The Canadian Coalition for Good Governance supports the more stringent definitions you propose and the fact that these definitions should be applied to all CBCA issuers including closely held companies. However, the ultimate determining factor of 'independence' must be based upon the concept of a 'material' relationship however defined.

We also believe that an independent director of a parent who sits on a subsidiary board should, in most instances be deemed to be independent, with the exception of the audit committee of the subsidiary board which, in our view, must be composed of directors who are completely unrelated to any other company in a controlled group.

For companies controlled by a parent (public) company we believe that there must be a **Conduct Review** Committee composed entirely of directors who only sit on the board of that subsidiary company and no other in the group. This Conduct Review Committee will determine any and all areas of potential conflict from board and committee composition to payments to related parties.

### 2. Electing directors

There are many different practices of creating a board of directors:

a) In the United Kingdom, Australia and New Zealand shareholders VOTE AGAINST directors. If 50% +1 of the votes cast are AGAINST a director that director is not elected. It is curious that in Canada the only option is to WITHHOLD a vote of approval.

b) In Sweden the top five shareholders nominate members of the Nominating Committee who then recommend the candidates to the shareholders.

c) In Canada we have adopted the American system of WITHHOLDING votes from directors on the ballot. The adoption of this system in the United States occurred under the 1933 Securities

Act when the US Federal Government drew upon the 1929 British Securities Act for the “public offering” components but left the “governance components” out in deference to states rights.

The Coalition wants all companies to present each of their directors for election each year in a ‘ballot’ form as exemplified by TransCanada Pipeline’s ‘ballot’ (as found on p.2 of Appendix C) and it wants to re-establish the right to vote AGAINST a director and to have that vote binding if 50% +1 of the votes cast oppose the director.

In the last round of proxies there were only 18% of companies who presented shareholders with their directors in a ballot format. The rest had a peculiar mix of presentations most of which made it impossible or extremely onerous to indicate a WITHHOLD vote.

### 3. Disclosing matters relating to directors

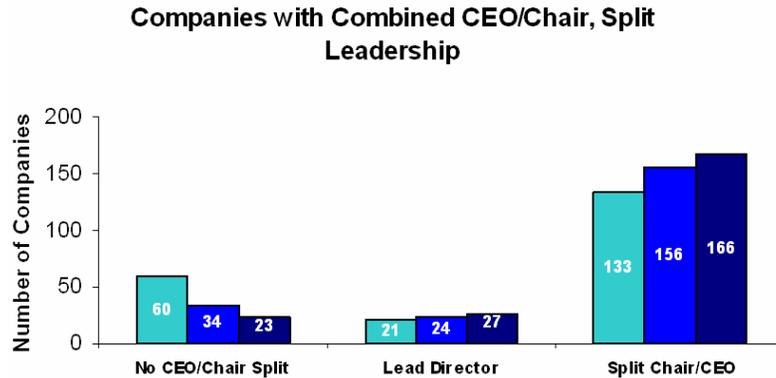
The Coalition has done a great deal of work on the disclosure of matters relating to directors in the Proxy Statement (see attached Appendix C). We believe a standardized form of disclosure similar to those required for executive compensation (see NI 51-102F6) would make it enormously easier for shareholders to understand who is representing their interests, how they are paid, what other boards they sit upon and how much interest they have in their duties as represented by compensation, attendance and shares owned.

## 2. Ensuring Independence in board structure and systems

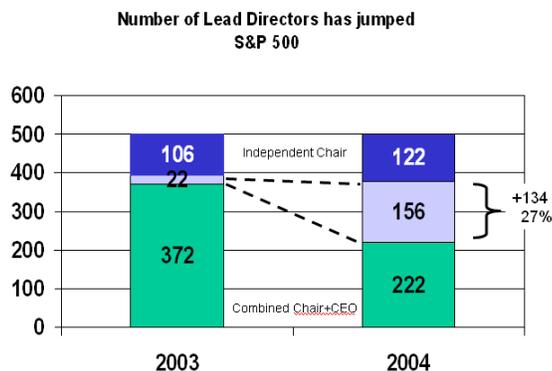
There are four sections that relate to ensuring independence in board structure and systems:

### 1. Separating the Chair and CEO positions

According to the Rotman BSCI the number of companies on the S&P/TSX Index with a split Chair/CEO has risen from 133 to 156 over the last three years. There are 27 further companies with a Lead Director and now only 23 companies with no split or lead director.



Canadian public companies more closely resemble their United Kingdom counterparts in the practice of splitting these roles. In the United States 90% of the companies on the S&P 500 Index retain a combined role but there is a growing use of the Lead Director function.



The Coalition believes that a Lead Director can play an important role in ensuring the independence of the board. We favour a complete split to an independent chair but are comfortable that a Lead Director is a reasonable half way house.

To assist in the building of a board acting in the shareholders' interests we strongly endorse 'in camera' meetings of the board at each and every meeting. We believe such meetings should cascade:

- First, all management save the CEO should depart leaving the board with its CEO
- Second, the CEO should be asked to leave, leaving the board alone
- Third, the controlling shareholder should be asked to leave while the lead director takes over.

In this way emerging issues can be aired and concerns uttered that may otherwise be suppressed in the board meeting proper due to time pressures or uncertainty.

## 2. Building a Completely Independent Audit Committee

The Coalition believes that a completely independent Audit Committee is necessary under all conditions of shareholder ownership – controlling or not. The provisions of MI 52-110 should be referenced and applied to all.

The Coalition also supports a number of practices you cite:

- The audit committee shall recommend to the board the auditors it proposes to put forward to the shareholders
- The audit committee shall have a mandate that includes the ability to hire independent counsel and advice
- The audit committee shall have members who are financially literate and whose credential form part of the annual disclosure to shareholders.
- The audit committee members, at each meeting, meet 'in camera' with the auditors and then alone
- Approval of consulting work **before** it is performed be required of the audit committee
- Certification by the CEO & CFO be mandated

## 3. Building a Largely Independent Compensation Committee

The Coalition believes that the Compensation Committee should have a majority of independent directors and that it's chair must be independent.

We concur with the Regulations proposed.

We also believe that all items of compensation for the 'named executives' must be disclosed. This includes not only salary, bonus and long term incentive programs but also all other perquisites and SERPs (Supplementary Executive Retirement Programs). SERPs have become the new 'stealth bomber' of executive compensation.

## 4. Building a Largely Independent Nominating Committee

The Coalition believes that the nominating Committee should have a majority of independent directors.

We concur with the Regulations proposed.

## **3. Enhancing the credibility of financial statements**

We concur with your proposed amendments.