REQUEST FOR COMMENT

NOTICE OF PROPOSED MULTILATERAL POLICY 58-201 EFFECTIVE CORPORATE GOVERNANCE

— AND —

PROPOSED MULTILATERAL INSTRUMENT 58-101 DISCLOSURE OF CORPORATE GOVERNANCE PRACTICES, FORM 58-101F1 AND FORM 58-101F2

This Notice accompanies proposed Multilateral Policy 58-201 *Effective Corporate Governance* (the Proposed Policy) and proposed Multilateral Instrument 58-101 *Disclosure of Corporate Governance Practices*, Form 58-101F1 and Form 58-101F2 (together, the Proposed Instrument). We are publishing the Proposed Policy and the Proposed Instrument for comment.

The purpose of the Proposed Policy is to confirm as best practice certain governance standards and guidelines that have evolved through legislative and regulatory reforms and the initiatives of other capital market participants. The purpose of the Proposed Instrument is to provide greater transparency for the marketplace regarding the nature and adequacy of issuers' corporate governance practices.

The Proposed Policy and Proposed Instrument are initiatives of certain members of the Canadian Securities Administrators. We expect the Proposed Policy to be adopted as a policy in each of Ontario, Saskatchewan, Alberta, Manitoba, Nova Scotia, Newfoundland and Labrador, New Brunswick, Prince Edward Island, the Yukon Territory, the Northwest Territories and Nunavut. We expect the Proposed Instrument to be adopted as a rule in Ontario, Alberta, Manitoba, Nova Scotia, and Newfoundland and Labrador, as a Commission regulation in Saskatchewan, as a policy in New Brunswick, Prince Edward Island and the Yukon Territory, and as a code in the Northwest Territories and Nunavut.

Background

The Proposed Policy and the Proposed Instrument represent one step in the evolution of corporate governance standards and practice. In 1994, a committee sponsored by the Toronto Stock Exchange (the TSX) published a report entitled *Where Were the Directors?* (the Dey Report). The Dey Report contained 14 recommendations to assist TSX-listed companies in their approach to corporate governance. In 1995, the TSX adopted the 14 recommendations as "best practice guidelines" and required every listed company to disclose annually their approach to corporate governance with reference to the guidelines, together with an explanation of any differences between the company's approach and the guidelines. The guidelines were not intended to be mandatory.

In 1999, the Institute of Corporate Directors and the TSX sponsored a report entitled *Five Years to the Dey*, which evaluated how Canadian companies were complying with the Dey Report's best practice guidelines. The report concluded that, although most

companies took the guidelines seriously, important areas remained where general practice fell short of the guidelines' intent.

Subsequently, the Canadian Institute of Chartered Accountants (the CICA), the TSX, and the TSX Venture Exchange (then the Canadian Venture Exchange) established the Joint Committee on Corporate Governance in July 2000 (the Saucier Committee). The mandate of the Saucier Committee was to review the state of corporate governance in Canada and recommend changes in this area. The Saucier Committee's final report, released in November 2001, recommended that the TSX amend its corporate governance guidelines in a number of ways to bring them into line with international developments. On April 26, 2002, the TSX proposed changes to its guidelines for effective corporate governance in response to the Saucier Committee's recommendations.

In July, 2002, the *Sarbanes-Oxley Act* (SOX) was enacted in the United States. SOX prescribed a broad range of measures designed to restore the public's faith in the U.S. capital markets in the wake of several U.S. financial reporting scandals. Recognizing the global implications of U.S reforms, particularly for Canadian capital markets, we initiated a review of the reforms that had been proposed or implemented in the U.S. and elsewhere for the purpose of considering whether we should adopt them in Canada. During the period of review, there have been a number of regulatory developments including, most recently, the approval of revised listing standards of the New York Stock Exchange (**NYSE**) and the Nasdaq Stock Market in November, 2003. At the same time, a number of Canadian institutional investors and other organizations have significantly influenced governance practices through proxy voting guidelines that focus on governance matters and by influencing the establishment of best practices.

The recommended practices contained in the Policy have been derived from:

- the TSX corporate governance guidelines, after giving effect to proposed modifications;
- the listing standards of the NYSE; and
- other regulatory, legislative and market driven developments.

In order to avoid regulatory duplication and overlap, the TSX intends to revoke its corporate governance guidelines and related disclosure requirements on the date the Proposed Policy and Proposed Instrument become effective.

Summary and Discussion of the Proposed Policy and Proposed Instrument

The Proposed Policy

The Proposed Policy confirms as best practice certain governance standards and guidelines that have resulted from legislative and regulatory reforms and the initiatives of other capital market participants. The best practices it recommends include:

- maintaining a majority of independent directors on the board of directors (the board)

- holding separate, regularly scheduled meetings of the independent directors

- appointing a chair of the board who is an independent director, or where this is not appropriate, appointing a lead director who is an independent director

- adopting a written board mandate

- developing position descriptions for directors and the chief executive officer

- providing each new director with a comprehensive orientation, as well as providing all directors with continuing education opportunities

- adopting a written code of business conduct and ethics

- appointing a nominating committee composed entirely of independent directors

- adopting a process for determining what competencies and skills the board as a whole should have, and applying this result to the recruitment process for new directors

- appointing a compensation committee composed entirely of independent directors

- conducting regular assessments of board effectiveness, as well as the effectiveness and contribution of each board committee and each individual director

Although the Proposed Policy applies to all reporting issuers, the recommendations in the Proposed Policy are not intended to be prescriptive. Instead, we encourage issuers to adopt the suggested measures, but they should be implemented flexibly and sensibly to fit the situation of individual issuers.

In developing the Proposed Policy and Proposed Instrument, we recognized that corporate governance is in a constant state of evolution. Consequently, we intend to review both the Proposed Policy and the Proposed Instrument during the two years following the implementation of these initiatives, to ensure that their recommendations and disclosure requirements continue to be appropriate for issuers in the Canadian marketplace.

The Proposed Instrument

The Proposed Instrument applies to all reporting issuers, other than investment funds, issuers of asset-backed securities, designated foreign issuers, SEC foreign issuers, certain exchangeable security issuers and certain credit support issuers. The Proposed Instrument establishes both disclosure requirements and the requirement to file any written code of business conduct and ethics that the issuer has adopted.

The Proposed Instrument requires an issuer to disclose those corporate governance practices it has adopted. The specific disclosure items are set out in Form 58-101F1. However, because we appreciate that many smaller issuers will have less formal procedures in place to ensure effective corporate governance, the Proposed Instrument requires issuers that are "venture issuers" to disclose only those items identified in Form 58-101F2.

The Proposed Instrument requires every issuer that has a written code of business conduct and ethics (a Code) to file a copy of that Code on SEDAR no later than the date on which the issuer's audited annual financial statements must be filed, unless a copy of such Code has previously been filed. In addition, any amendment to such Code must be filed on SEDAR no later than 30 days after the final form of amendment has been approved by the board of directors.

Where the board grants a waiver of the Code in favour of an officer or director of the issuer or a subsidiary entity of the issuer, the issuer must promptly issue and file on SEDAR a news release that describes the details of the waiver. Where the waiver granted is an implicit waiver, the news release must be issued and filed promptly upon the board becoming aware of such waiver.

Meaning of Independence

Similar to the definition of "independence" in Multilateral Instrument 52-110 *Audit Committees*, the definition of "independence" used in both the Proposed Policy and the Proposed Instrument is based upon corresponding definitions in the United States. For the purpose of the Proposed Policy and the Proposed Instrument, a director is independent if the he or she has no direct or indirect material relationship with the issuer. A "material relationship" is a relationship which could, in the view of the issuer's board, reasonably interfere with the exercise of a director's independent judgement. However, an individual described in subsection 1.4(3) of Multilateral Instrument 52-110 *Audit Committees* (other than an individual described in clauses 1.4(3)(f)(i) or (g) of that instrument) is considered to have a material relationship with the issuer. The relationships included in clauses 1.4(3)(f)(i) and (g) were derived from SEC rules applicable to audit committee members only. Consequently, as in the United States, the test of whether or not a director is independent is less onerous than that used for the purposes of determining the independence of an audit committee member.

Specific Request for Comment

We invite comment on these materials generally. In addition, we have raised the follow questions for your specific consideration.

1. The Proposed Policy and Proposed Instrument describe best practices and require issuers to make disclosure in relation to those best practices.

   (a) Will these initiatives provide useful guidance to issuers?

   (b) Will these initiatives provide meaningful disclosure to investors?

(c) Would disclosure be more meaningful to investors if issuers were required to describe their practices by reference to certain categories of governance principles rather than by reference to the best practices described in the Policy?

(d) What will be the effect on market participants, including investors and issuers, of our publishing best practices in Canada?

2. The Proposed Instrument does not require an issuer to adopt a code of ethics, but issuers who do not have one must explain why they do not. If an issuer does adopt a code, the Proposed Instrument requires the issuer to file the code, as well as any amendments on SEDAR. It also requires an issuer to prepare and file a news release respecting any express or implied waiver of the code.

(a) Will the text of the code of ethics provide useful disclosure for investors?

(b) Will disclosure of waivers from the code provide useful disclosure for investors?

(c) Since there is no requirement to have a code of ethics, will the obligations respecting filing the code and any amendments and reporting waivers from the code have the effect of discouraging issuers from adopting a code of ethics?

3. The Proposed Instrument does not require issuers to have a compensation committee, nor does it require that committee to be entirely independent or to have a charter, but if an issuer does not have these structures, it must explain why not. An issuer is required to state whether it has a compensation committee, whether that committee is independent and whether it has a compensation committee charter. If there is a charter, the text of the charter must be disclosed. Additionally, the Proposed Instrument requires an issuer to disclose the process used to determine compensation, but that disclosure is only required if the issuer does not have a compensation committee.

(a) Would it be useful to investors for the issuer to disclose the process used to determine compensation, regardless of whether it has a compensation committee?

(b) Is disclosure of the text of the compensation committee's charter useful to investors?

4. The Proposed Instrument does not require issuers to have a nominating committee, nor does it require that committee to be entirely independent or to have a charter, but if an issuer does not have these structures, it must explain why not. An issuer is required to state whether it has a nominating committee, whether any such committee is independent and whether it has a nominating committee charter. If there is a charter, the text of the charter must be disclosed.

Additionally, the Proposed Instrument requires an issuer to disclose the process by which candidates are selected for board nomination, but that disclosure is only required if the issuer does not have a nominating committee.

(a) Would it be useful to investors for the issuer to disclose the process by which candidates are selected for board nomination, regardless of whether it has a nominating committee?

(b) Is disclosure of the text of the nominating committee's charter useful to investors?

5. The Proposed Instrument requires an issuer to disclose the process used to assess the performance of the board, committee chairs and CEO, but that disclosure is only required if the issuer does not have written position descriptions for those roles. Would it be useful for investors for the issuer to disclose the assessment process, regardless of whether it has written position descriptions?

Authority for the Instrument – Ontario

In Ontario, securities legislation provides the Ontario Securities Commission (the OSC) with rule-making or regulation-making authority regarding the subject matter of the Proposed Instrument.

Paragraph 143(1)22 of the *Securities Act* (Ontario) (the Act) authorizes the OSC to prescribe requirements in respect of the preparation and dissemination and other use, by reporting issuers, of documents providing for continuous disclosure that are in addition to the requirements under the Act, including requirements in respect of an annual information form.

Paragraph 143(1)39 of the Act authorizes the OSC to make rules requiring or respecting the media, format, preparation, form, content, execution, certification, dissemination and other use, filing and review of all documents required under or governed by the Act, the regulations or the rules and all documents determined by the regulations or the rules to be ancillary to the documents.

Paragraph 143(1)44 of the Act authorizes the OSC to vary the Act to permit or require the use of an electronic or computer-based system for the filing, delivery or deposit of (a) documents or information required under or governed by the Act, the regulations or rules, and (b) documents determined by the regulations or rules to be ancillary to documents required under or governed by the Act, the regulations or rules.

Related Instruments

The Proposed Instrument is related to National Instrument 51-102 *Continuous Disclosure Obligations*, National Instrument 71-102 *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers* and Multilateral Instrument 52-110 *Audit Committees*.

Anticipated Costs and Benefits of Proposed Instrument

The Proposed Instrument will provide greater transparency for the marketplace regarding the nature and adequacy of issuers' corporate governance practices. It is anticipated that the benefits of such transparency, including enhanced investor confidence in Canadian capital markets, will exceed the relatively nominal cost for issuers to provide the disclosure required by the Proposed Instrument. We note that issuers currently incur equivalent costs to comply with the TSX's corporate governance disclosure requirements.

Alternatives Considered

In developing the Proposed Policy and Proposed Instrument, we considered seeking legislative authority to require reporting issuers to adopt certain corporate governance practices. However, we appreciate that corporate governance is in a constant state of evolution, and that some "best practices" may not be appropriate for all issuers. Consequently, we determined to confirm as best practices certain corporate governance standards and guidelines and to require issuers to disclose those corporate governance practices they currently utilize.

Reliance on Unpublished Studies, Etc.

In developing the Proposed Policy and Proposed Instrument, we did not rely upon any significant unpublished study, report or other written materials.

Comments

Interested parties are invited to make written submissions on the Proposed Policy and Proposed Instrument. Submissions received by April 15, 2004 will be considered. **Due to timing concerns, comments received after the deadline will not be considered.**

Submissions should be addressed to the following securities regulatory authorities:

Alberta Securities Commission
Saskatchewan Securities Commission
Manitoba Securities Commission
Ontario Securities Commission
Nova Scotia Securities Commission
Securities Administration Branch, New Brunswick
Office of the Attorney General, Prince Edward Island
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Government of Yukon
Registrar of Securities, Department of Justice, Government of the Northwest Territories
Registrar of Securities, Legal Registries Division, Department of Justice, Government of Nunavut

Please deliver your comments to the addresses below. Your comments will be distributed to the other participating CSA members.

John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario M5H 3S8
Fax: (416) 593-2318
E-mail: jstevenson@osc.gov.on.ca

A diskette containing the submissions (in Windows format, preferably Word) should also be submitted.

Comment letters submitted in response to requests for comments are placed on the public file and form part of the public record, unless confidentiality is requested. Comment letters will be circulated among the securities regulatory authorities, whether or not confidentiality is requested. Although comment letters requesting confidentiality will not be placed in the public file, freedom of information legislation may require securities regulatory authorities to make comment letters available. Persons submitting comment letters should therefore be aware that the press and members of the public may be able to obtain access to any comment letters.

Questions may be referred to the following people:

Kari Horn
Alberta Securities Commission
Telephone: (403) 297-4698
E-mail: kari.horn@seccom.ab.ca

Rick Whiler
Ontario Securities Commission
Telephone: (416) 593-8127
E-mail: rwhiler@osc.gov.on.ca

Michael Brown
Ontario Securities Commission
Telephone: (416) 593-8266
E-mail: mbrown@osc.gov.on.ca

Text of Proposed Policy and Proposed Instrument

The text of the Proposed Policy and the Proposed Instrument follow.

Dated: January 16, 2004