Canadian Securities Administrators | Autorités canadiennes en valeurs mobilières

CSA Consultation Paper 52-404
Approach to Director and Audit Committee Member Independence

October 26, 2017

1. Introduction

The corporate governance regime in Canada was introduced over a decade ago and was largely based on the report sponsored by the Toronto Stock Exchange, *Where were the Directors?* (commonly referred to as the Dey Report) published in 1994. The regime encompasses guidelines related to the exercise of independent judgement, including the composition of the board of directors (the **board**) and the audit committee. Non-venture issuers must provide disclosure with reference to the guidelines within the framework of a "comply or explain" disclosure model, whereas venture issuers are subject to more basic disclosure requirements.[1]

The approach to determining whether a director or audit committee member is independent was introduced in 2004. This approach is largely subjective, but contains prescriptive elements (bright-line tests) that, when applicable, do not permit the board to determine whether a director could reasonably be expected to exercise independent judgement. It is predominantly derived from the concepts of independence adopted by the New York Stock Exchange (**NYSE**) and the Nasdaq Stock Market (**Nasdaq**) following several U.S. financial reporting scandals, as modified by the requirements set out in the *Sarbanes-Oxley Act of 2002*. This approach was taken following these financial reporting scandals in order to address concerns about investor confidence in our capital markets which are largely integrated with and affected by the U.S. markets and because companies inter-listed in the U.S. and Canada indicated a need for this alignment.

Some stakeholders have expressed concern about the appropriateness of our approach to determining independence. They believe that our approach has precluded individuals with the requisite expertise and sound judgement from being considered independent members of the board or being able to serve as audit committee members. In other instances, it has been argued that the application of our approach has limited the pool of individuals who could be considered independent to the detriment of certain issuers. Some of those stakeholders who have expressed these concerns point to the merits of approaches to independence adopted in other jurisdictions such as the U.K., Australia and

[1] The term "issuer" in this Consultation Paper refers to a reporting issuer.

Sweden. Other stakeholders, however, have pointed out that the market has adapted to our approach and are concerned with potential costs associated with making changes to the approach or transitioning to a new approach.

The purpose of this consultation paper (the **Consultation Paper**) is to facilitate a broad discussion on the appropriateness of our approach to determining director and audit committee member independence. The Canadian Securities Administrators (**CSA** or **we**) are publishing the Consultation Paper for a 90-day comment period to solicit views on whether or not any changes should be considered. In addition to any general comments you may have, we also invite comments on the specific questions set out at the end of the Consultation Paper.

The comment period will end on **January 25, 2018**.

The remainder of the Consultation Paper is structured as follows:

- Part 2 examines the key historical developments relating to our corporate governance regime;
- Part 3 sets out the approach to determining director and audit committee member independence in Canada;
- Part 4 provides a comparative overview of the approaches to determining director and audit committee member independence in Canada, Australia, Sweden, the U.K. and the U.S.;
- Part 5 discusses the benefits and limitations of the Canadian approach; and
- Annexes A through E provide additional information concerning the approaches to determining independence in Canada and in other jurisdictions.

2. Key historical developments relating to our corporate governance regime

The following table sets out the key developments relating to our corporate governance regime.

Date	Development
March 30, 2004	Participating CSA jurisdictions[2] adopted Multilateral Instrument 52-110 *Audit Committees* and Companion Policy 52-110CP *Audit Committees.* The purpose was to encourage issuers to establish and maintain strong, effective and independent audit committees. The rationale was that such audit committees enhance the quality of financial disclosure made by

[2] The securities regulatory authorities in every province and territory in Canada, other than British Columbia. The British Columbia Securities Commission adopted National Instrument 52-110 *Audit Committees* on March 17, 2008.

Date	Development
	issuers, and ultimately foster investor confidence in Canada's capital markets.
June 30, 2005	Multilateral Instrument 52-110 *Audit Committees* and Companion Policy 52-110CP *Audit Committees* were amended to clarify and update the definition of independence. The primary purpose of the amendments was to better align the definition of independence with the independent audit committee member requirements and independent director requirements applicable in the U.S.
June 30, 2005	The CSA adopted National Policy 58-201 *Corporate Governance Guidelines* (**NP 58-201**) and National Instrument 58-101 *Disclosure of Corporate Governance Practices* (**NI 58-101**) to confirm as best practices corporate governance guidelines and to provide greater transparency for the marketplace regarding the nature and adequacy of issuers' corporate governance practices. Following implementation, we committed to review both NP 58-201 and NI 58-101 periodically to ensure that the guidelines and disclosure requirements continue to be appropriate for issuers in Canada.
September 28, 2007	The CSA communicated its plans to undertake a broad review of NP 58-201 and NI 58-101 and to publish its findings together with any proposed amendments for comment in 2008.[3]
December 19, 2008	The CSA published for comment proposed changes to the corporate governance regime.[4] One of the proposals was to replace the current approach to independence in National Instrument 52-110 *Audit Committees* (**NI 52-110**) with a principles-based definition of independence and guidance in Companion Policy 52-110CP to National Instrument 52-110 *Audit Committees* (**52-110CP**) regarding the types of relationships that could affect independence.
November 13, 2009	Based on comments received from stakeholders, the CSA concluded that it was not an appropriate time to implement significant changes to the corporate governance regime.[5] Reconsideration at a later date was left open.

[3] CSA Staff Notice 58-304 *Review of National Instrument 58-101 Disclosure of Corporate Governance Practices and National Policy 58-201 Corporate Governance Guidelines*.
[4] Request for Comment – Proposed Repeal and Replacement of National Policy 58-201 *Corporate Governance Guidelines*, National Instrument 58-101 *Disclosure of Corporate Governance Practices*, and National Instrument 52-110 *Audit Committees* and Companion Policy 52-110CP *Audit Committees*.
[5] CSA Staff Notice 58-305 *Status Report on the Proposed Changes to the Corporate Governance Regime*.

3. Corporate governance and determining independence in Canada

The corporate governance regime in Canada includes voluntary guidelines that are set out in NP 58-201 and mandatory disclosure requirements that are set out in NI 58-101.

NP 58-201 includes voluntary guidelines that provide guidance on corporate governance practices. Although NP 58-201 applies to all issuers, the guidelines are not prescriptive. Issuers are encouraged to consider the guidelines when developing their own corporate governance practices. The practices encompassed by the guidelines relate to components of effective corporate governance, including those intended to foster independent decision making, such as the composition of the board, nominating committee and compensation committee. Issuers are, however, free to adopt those corporate governance practices that they determine to be appropriate for their particular circumstances.

NI 58-101 sets out mandatory disclosure requirements that provide transparency regarding issuers' corporate governance practices. As mentioned above, non-venture issuers are required to provide this disclosure with reference to the guidelines within the framework of a "comply or explain" disclosure model. Venture issuers are subject to more basic disclosure requirements that are framed more generally and are not "comply or explain" in nature.

NI 52-110 also forms part of our corporate governance regime, prescribing the approach to determining director and audit committee member independence, the composition of the audit committee and the responsibilities of the audit committee.

Independent directors or audit committee members must not have a direct or indirect material relationship with the issuer.[6] A material relationship is defined as a relationship which could, in the view of the board, be reasonably expected to interfere with the exercise of a member's independent judgement.[7]

NI 52-110 defines certain relationships as material relationships and thereby precludes some individuals from being considered independent. These relationships are set out as bright line tests in sections 1.4 and 1.5 of NI 52-110, and they apply regardless of any determination of independence made by the board. To be considered an independent director, an individual must not have a relationship captured by the bright line tests set out in section 1.4 of NI 52-110. To be considered an independent audit committee member, an individual must not have a relationship captured by the bright line tests that are set out in sections 1.4 and 1.5 of NI 52-110.

[6] Subsection 1.4(1) of NI 52-110.
[7] Subsection 1.4(2) of NI 52-110.

The audit committee of non-venture issuers must be comprised solely of independent audit committee members.[8] There are a number of conditional exemptions from this independence requirement set out in NI 52-110, including; (i) when an issuer recently obtained a receipt for a prospectus that constitutes its initial public offering; (ii) where the issuer is a controlled company;[9] (iii) when an audit committee member ceases to be independent for reasons outside that member's reasonable control; and (iv) if there is a vacancy on the audit committee due to the death, disability or resignation of an audit committee member.[10]

Venture issuers are exempt from the requirement that every audit committee member be independent, but are instead required to have a majority of audit committee members who are not executive officers, employees, or control persons of the issuer or an affiliate of the issuer.[11]

3.1 Relevance of the definition of independence

The definition of independence is a central component of our corporate governance regime. We believe that the exercise of independent judgment contributes to the effectiveness of boards and board committees.

NP 58-201 provides guidance to issuers that the board should have a majority of independent directors.[12] NI 58-101 requires issuers to disclose the identities of directors who are independent and those who are not, along with the basis for those determinations.[13] Issuers, other than venture issuers, must also disclose whether or not a majority of directors are independent and if not, they must describe what the board does to facilitate the exercise of independent judgement in carrying out its responsibilities.[14]

The definition of independence is also relevant for purposes of board committee composition. There is no requirement that board committees, other than the audit committee, be comprised of independent members. NP 58-201 provides guidance that the nominating and compensation committees should be comprised entirely of independent

[8] Subsection 3.1(3) of NI 52-110.
[9] See section 1.3 of NI 52-110. For the purposes of NI 52-110, "control" means the direct or indirect power to direct or cause the direction of the management and policies of a person or company, whether through ownership of voting securities or otherwise.
[10] Sections 3.2 to 3.9 of NI 52-110.
[11] TSX Venture Exchange listed issuers are required to meet an almost identical requirement under that exchange's policies.
[12] Section 3.1 of NP 58-201.
[13] Items 1(a) and (b) of Form 58-101F1 and item 1 of Form 58-101F2.
[14] Item 1(c) of Form 58-101F1.

directors because these committees and their functions are fundamental elements of corporate governance that act as a check on management and non-independent directors.[15] NI 58-101 requires issuers, other than venture issuers, to disclose whether these committees are comprised entirely of independent members and if not, they must describe what the board does to ensure an objective decision-making process for these committees.[16]

As mentioned above, subject to certain exemptions, NI 52-110 requires audit committees of non-venture issuers to be comprised solely of independent audit committee members. The purpose of this requirement is to facilitate the independent exercise of the audit committee's responsibilities, including the review of the issuer's financial disclosure, oversight of its financial reporting processes and the work of the external auditors. NI 52-110 requires issuers to disclose whether or not each audit committee member is independent.[17]

3.2 Approach to determining independence

The approach to determining whether a director or audit committee member is independent is set out in NI 52-110. This approach includes:

- a definition of independence that is subjective;
- bright line tests that preclude a director or audit committee member from being considered independent; and
- additional bright line tests that relate specifically to the independence of an audit committee member.

Section 1.4 of NI 52-110 defines independence as the absence of any direct or indirect material relationship with the issuer. A material relationship is one which could, in the view of the issuer's board, be reasonably expected to interfere with the exercise of an individual's independent judgement. These types of relationships may include, for example, a commercial, charitable, industrial, banking, consulting, legal, accounting, or familial relationship, or any other relationship that the board considers to be material.[18] Notwithstanding any determination made by an issuer's board, an individual is deemed

[15] Sections 3.10 and 3.15 of NP 58-201.
[16] Items 6(b) and 7(b) of Form 58-101F1.
[17] Item 2 of Form 52-110F1 and item 2 of Form 52-110F2.
[18] Section 3.1 of 52-110 CP.

(bright line test) to have a material relationship with the issuer if the individual is, or has been within the last three years:[19]

- an employee or executive officer of the issuer;
- a partner or an employee of the issuer's internal or external auditor or a former partner or employee of the internal or external auditor who personally worked on the issuer's audit;
- an executive officer of another entity if a current executive officer of the issuer serves or served, at the same time, on the compensation committee of that other entity; or
- in receipt of more than $75,000 in direct compensation from the issuer during any 12-month period (except for acting as a director or committee member), excluding fixed amounts of compensation under a retirement or deferred compensation plan for prior service with the issuer if receipt is not in any way contingent on continued service.

Immediate family members having relationships similar to those described above are generally considered to have a material relationship with the issuer. For the purposes of these determinations, an issuer includes a subsidiary entity and a parent of the issuer.[20]

Section 1.5 of NI 52-110[21] sets out additional bright line tests applicable only to audit committee members deeming an individual to have a material relationship with the issuer if the individual:

- accepts, directly or indirectly, any consulting, advisory or compensatory fee from the issuer or any subsidiary entity of the issuer, other than as remuneration for board or board committee work; or
- is an affiliated entity of the issuer or any of its subsidiary entities. The definition of "affiliated entity" is broad and includes entities within a controlled group as well as an individual who is both a director and an employee of an affiliated entity, or is an executive officer, general partner or managing member of an affiliated entity.[22]

[19] Subsection 1.4(3) to subsection 1.4(7) of NI 52-110. This description of the relationships is general in nature and does not in all instances capture all the detail set out in NI 52-110. The detailed description of the relationships is included in Annex A.
[20] Subsection 1.4(8) of NI 52-110. For the purpose of section 1.4 of NI 52-110, an issuer does not include other entities under common control.
[21] This description of the relationships is general in nature and does not in all instances capture all the detail set out in NI 52-110. The detailed description of the relationships is included in Annex A.
[22] Section 1.3 of NI 52-110.

4. Approaches to determining director and audit committee member independence in other jurisdictions

In this part, we provide a comparative overview of the approaches to determining independence in Canada, Australia, Sweden, the U.K. and the U.S. Information included in this part is not intended to present a comprehensive review of the law in those jurisdictions. Please refer to Annexes A through E of this Consultation Paper for further information.

4.1 Definition of independence

The definitions of independence in Canada, Australia, Sweden, the U.K. and the U.S. are substantially similar, with a focus on an individual's independence as evidenced by the nature of their relationship with an issuer, including those relationships that could impair, or could be seen to impair, their independence.

Examples of interests, positions, associations and relationships that might raise doubts about the independence of an individual are provided by each of these jurisdictions. In some jurisdictions, examples are framed in a prescriptive manner as bright line tests, deeming an individual to not be independent. In other jurisdictions, examples are framed in a more principles-based manner, providing guidance to boards in making a determination as to whether an individual should be considered independent.

The table below highlights the approach to determining independence taken in Canada, Australia, Sweden, the U.K. and the U.S.

Jurisdiction	Definition of independence	Bright line tests vs guidance
Canada	The individual has no direct or indirect material relationship with the issuer, i.e., a relationship which could, in the view of the board, be reasonably expected to interfere with the exercise of independent judgement.	Definition of independence is supplemented with **bright line tests.**
Australia	The director is free of any interest or relationship that might influence, or reasonably be perceived to influence, in a material respect his or her capacity to exercise independent judgment and to act in the best interests of the company and its shareholders.	Definition of independence is supplemented with **guidance.**

Jurisdiction	Definition of independence	Bright line tests vs guidance
Sweden	There are no factors that may give cause to question the director's independence and integrity with regard to the company or its executive management.	Definition of independence is supplemented with **guidance.**
U.K.	The director is independent in character and judgement and there are no relationships or circumstances which are likely, or could appear, to affect the director's judgement.	Definition of independence is supplemented with **guidance.**
U.S.	NYSE: The board has affirmatively determined that the director has no material relationship with the listed company; Nasdaq: The director is not an officer or employee of the company, and, in the opinion of the board, the director has no relationship which would interfere with the exercise of independent judgment.	Definition of independence is supplemented with **bright line tests.**

4.2 Criteria relevant for determining independence

As noted above, corporate governance regimes in Canada, Australia, Sweden, the U.K. and the U.S. provide examples of interests, positions, associations and relationships that may raise doubts about the independence of an individual. These criteria are relevant when making independence determinations. The table below compares the criteria in general terms applicable in each jurisdiction and notes whether they are bright line tests or guidance.

Criteria in general terms[23]	Canada	Australia	Sweden	U.K.	U.S.
Employment	**BL**	**G**	**G**	**G**	**BL**
Direct compensation from the issuer greater than a specified threshold	**BL**		**G**	**G**	**BL**

[23] The intercorporate relationships among the issuer and other entities are relevant when applying the criteria. Immediate family members having relationships similar to those summarized in this table may also cause doubts about the independence of the individual.

Criteria in general terms[23]	Canada	Australia	Sweden	U.K.	U.S.
Relationship with or compensation for (i) an internal or external auditor, (ii) consulting, advisory or other professional services, or (iii) any other material business or contractual relationships with the issuer	**BL**	**G**	**G**	**G**	**BL**
Employment by an entity if the issuer's executive officers serve on entity's compensation committee, cross-directorships or significant links with directors	**BL**		**G**	**G**	**BL**
Board term greater than certain number of years or for such a period that independence has been compromised		**G**		**G**	
Affiliate of the issuer or substantial security holder of the issuer or relationship with the substantial security holder	**BL**	**G**	**G**	**G**	**BL**

BL	Bright line tests	**G**	Guidance

5. The Canadian approach – benefits and limitations

We recognize that our current approach has both benefits and limitations.

Certainty, consistency and predictability have been noted as benefits of our approach to determining independence. Our approach has been in place for over a decade. Stakeholders understand our approach and issuers have incorporated it in how they structure and manage their boards and committees. Under NI 52-110 the board must determine whether or not an individual, given their relationship to the issuer, could reasonably be expected to exercise independent judgement. The bright line tests add a degree of certainty, consistency and predictability to this determination by listing specific relationships that preclude an individual from being considered independent. Certainty may be of assistance to boards in making independence determinations, while

consistency and predictability may better enable stakeholders to evaluate the independence of an issuer's board or its committees.

Inflexibility and overly-restrictive parameters have been noted as limitations of our approach to determining independence. Our approach does not leave much flexibility to the board to exercise its judgment in the event one of the bright-line tests has been met. If an individual has a relationship that is listed in the bright line tests, the individual is automatically disqualified from being considered independent regardless of any circumstances a board might consider as warranting a different determination. The bright line tests found in NI 52-110 have been criticized, including by certain controlled companies, as creating overly-restrictive parameters for determining independence that can result in a determination of independence which may not, in the particular circumstances, accord with the view of the board. Inflexibility and overly-restrictive parameters may unduly limit the pool of qualified candidates who could serve as independent directors or audit committee members.

Recognizing these benefits and limitations, this Consultation Paper is intended to facilitate a broad discussion on the appropriateness of our approach to determining director and audit committee member independence.

6. Consultation Questions

We welcome your comments on the issues outlined in this Consultation Paper. In addition, we are also interested in your views and comments on the following specific questions:

1. Our approach to determining director and audit committee member independence is described in section 3.2 of this Consultation Paper.
    a. Do you consider our approach appropriate for all issuers in the Canadian market? Please explain why or why not.
    b. In your view, what are the benefits or limitations of our approach to determining independence? Please explain.
    c. Do you believe that our approach strikes an appropriate balance in terms of:
        i. the restrictions it imposes on issuers' boards in exercising their discretion in making independence determinations, and
        ii. the certainty it provides boards in making those determinations and the consistency and predictability it provides other stakeholders in evaluating the independence of an issuer's directors or audit committee members?
    d. Do you have any other comments regarding our approach?

2. Should we consider making any changes to our approach to determining independence as prescribed in NI 52-110, such as changes to:
    a. the definition of independence;
    b. the bright line tests for directors and audit committee members; or
    c. the exemptions to the requirement that every audit committee member be independent?

    Are there other changes we should consider? Please explain.

3. What are the advantages and disadvantages of maintaining our approach to determining independence versus replacing it with an alternative approach? Please explain.

Please submit your comments in writing on or before January 25, 2018. Please send your comments by email in Microsoft Word format.

Please address your submission to all members of the CSA as follows:

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
The Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission of New Brunswick
Superintendent of Securities, Prince Edward Island
Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Nunavut

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

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We cannot keep submissions confidential because securities legislation in certain provinces requires publication of the written comments received during the comment period. All comments received will be posted on the websites of each of the Alberta Securities Commission at www.albertasecurities.com, the Autorité des marchés financiers at www.lautorite.qc.ca and the Ontario Securities Commission at www.osc.gov.on.ca. Therefore, you should not include personal information directly in comments to be published. It is important that you state on whose behalf you are making the submission.

7. Questions

Please refer your questions to any of the following:

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Annex A – Canada

In Canada, the approach to determining director and audit committee member independence is prescribed in NI 52-110. The following are extracts from the relevant sections:

1.4 Meaning of Independence

(1) An audit committee member is independent if he or she has no direct or indirect material relationship with the issuer.

(2) For the purposes of subsection (1), a "material relationship" is a relationship which could, in the view of the issuer's board of directors, be reasonably expected to interfere with the exercise of a member's independent judgement.

(3) Despite subsection (2), the following individuals are considered to have a material relationship with an issuer:

(a) an individual who is, or has been within the last three years, an employee or executive officer of the issuer;

(b) an individual whose immediate family member is, or has been within the last three years, an executive officer of the issuer;

(c) an individual who:

(i) is a partner of a firm that is the issuer's internal or external auditor,

(ii) is an employee of that firm, or

(iii) was within the last three years a partner or employee of that firm and personally worked on the issuer's audit within that time;

(d) an individual whose spouse, minor child or stepchild, or child or stepchild who shares a home with the individual:

(i) is a partner of a firm that is the issuer's internal or external auditor,

(ii) is an employee of that firm and participates in its audit, assurance or tax compliance (but not tax planning) practice, or

(iii) was within the last three years a partner or employee of that firm and personally worked on the issuer's audit within that time;

(e) an individual who, or whose immediate family member, is or has been within the last three years, an executive officer of an entity if any of the issuer's current executive officers serves or served at that same time on the entity's compensation committee; and

(f) an individual who received, or whose immediate family member who is employed as an executive officer of the issuer received, more than $75,000 in direct compensation from the issuer during any 12 month period within the last three years.

(4) Despite subsection (3), an individual will not be considered to have a material relationship with the issuer solely because

(a) he or she had a relationship identified in subsection (3) if that relationship ended before March 30, 2004; or

(b) he or she had a relationship identified in subsection (3) by virtue of subsection (8) if that relationship ended before June 30, 2005.

(5) For the purposes of clauses (3)(c) and (3)(d), a partner does not include a fixed income partner whose interest in the firm that is the internal or external auditor is limited to the receipt of fixed amounts of compensation (including deferred compensation) for prior service with that firm if the compensation is not contingent in any way on continued service.

(6) For the purposes of clause (3)(f), direct compensation does not include:

(a) remuneration for acting as a member of the board of directors or of any board committee of the issuer, and

(b) the receipt of fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the issuer if the compensation is not contingent in any way on continued service.

(7) Despite subsection (3), an individual will not be considered to have a material relationship with the issuer solely because the individual or his or her immediate family member

(a) has previously acted as an interim chief executive officer of the issuer, or

(b) acts, or has previously acted, as a chair or vice-chair of the board of directors or of any board committee of the issuer on a part-time basis.

(8) For the purpose of section 1.4, an issuer includes a subsidiary entity of the issuer and a parent of the issuer.

1.5 Additional Independence Requirements

(1) Despite any determination made under section 1.4, an individual who

(a) accepts, directly or indirectly, any consulting, advisory or other compensatory fee from the issuer or any subsidiary entity of the issuer, other than as remuneration for acting in his or her capacity as a member of the board of directors or any board committee, or as a part-time chair or vice-chair of the board or any board committee; or

(b) is an affiliated entity of the issuer or any of its subsidiary entities,

is considered to have a material relationship with the issuer.

(2) For the purposes of subsection (1), the indirect acceptance by an individual of any consulting, advisory or other compensatory fee includes acceptance of a fee by

(a) an individual's spouse, minor child or stepchild, or a child or stepchild who shares the individual's home; or

(b) an entity in which such individual is a partner, member, an officer such as a managing director occupying a comparable position or executive officer, or occupies a similar position (except limited partners, non-managing members and those occupying similar positions who, in each case, have no active role in providing services to the entity) and which provides accounting, consulting, legal, investment banking or financial advisory services to the issuer or any subsidiary entity of the issuer.

(3) For the purposes of subsection (1), compensatory fees do not include the receipt of fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the issuer if the compensation is not contingent in any way on continued service.

Annex B – Australia

In Australia, the approach to determining independence is described in the ASX Corporate Governance Principles and Recommendations. The following are extracts from the relevant recommendation:

Recommendation 2.3

A director of a listed entity should only be characterised and described as an independent director if he or she is free of any interest, position, association or relationship that might influence, or reasonably be perceived to influence, in a material respect his or her capacity to bring an independent judgment to bear on issues before the board and to act in the best interests of the entity and its security holders generally.

Examples of interests, positions, associations and relationships that might cause doubts about the independence of a director include if the director:

- is, or has been, employed in an executive capacity by the entity or any of its child entities and there has not been a period of at least three years between ceasing such employment and serving on the board;

- is, or has within the last three years been, a partner, director or senior employee of a provider of material professional services to the entity or any of its child entities;

- is, or has been within the last three years, in a material business relationship (e.g. as a supplier or customer) with the entity or any of its child entities, or an officer of, or otherwise associated with, someone with such a relationship;

- is a substantial security holder of the entity or an officer of, or otherwise associated with, a substantial security holder of the entity;

- has a material contractual relationship with the entity or its child entities other than as a director;

- has close family ties with any person who falls within any of the categories described above; or

- has been a director of the entity for such a period that his or her independence may have been compromised.

In each case, the materiality of the interest, position, association or relationship needs to be assessed to determine whether it might interfere, or might reasonably be seen to interfere, with the director's capacity to bring an independent judgement to bear on issues before the board and to act in the best interests of the entity and its security holders generally.

Annex C – Sweden

In Sweden, the approach to determining independence is described in the Swedish Corporation Governance Code. The following are extracts from the relevant rules:

Rule 4.4

A director's independence is to be determined by a general assessment of all factors that may give cause to question the individual's independence and integrity with regard to the company or its executive management. Factors that should be considered include:

- whether the individual is the chief executive officer or has been the chief executive officer of the company or a closely related company within the last five years,

- whether the individual is employed or has been employed by the company or a closely related company within the last three years,

- whether the individual receives a not insignificant remuneration for advice or other services beyond the remit of the board position from the company, a closely related company or a person in the executive management of the company,

- whether the individual has or has within the last year had a significant business relationship or other significant financial dealings with the company or a closely related company as a client, supplier or partner, either individually or as a member of the executive management, a member of the board or a major shareholder in a company with such a business relationship with the company,

- whether the individual is or has within the last three years been a partner at, or has as an employee participated in an audit of the company conducted by, the company's or a closely related company's current or then auditor,

- whether the individual is a member of the executive management of another company if a member of the board of that company is a member of the executive management of the company, or

- whether the individual has a close family relationship with a person in the executive management or with another person named in the points above if that person's direct or indirect business with the company is of such magnitude or significance as to justify the opinion that the board member is not to be regarded as independent.

Rule 4.5

In order to determine a board member's independence and integrity, the extent of the member's direct and indirect relationships with major shareholders is to be taken into consideration. A member of the board who is employed by or is a board member of a company which is a major shareholder is not to be regarded as independent.

Rule 4.6

Nominees to positions on the board are to provide the nomination committee with sufficient information to enable an assessment of the candidate's independence as defined in 4.4 and 4.5.

Annex D – United Kingdom

In the U.K., the approach to determining independence is described in the UK Corporate Governance Code. The following are extracts from the relevant provision:

B.1.1

The board should determine whether the director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement. The board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination, including if the director:

- has been an employee of the company or group within the last five years;

- has, or has had within the last three years, a material business relationship with the company either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company;

- has received or receives additional remuneration from the company apart from a director's fee, participates in the company's share option or a performance related pay scheme, or is a member of the company's pension scheme;

- has close family ties with any of the company's advisers, directors or senior employees; holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;

- represents a significant shareholder; or

- has served on the board for more than nine years from the date of their first election.

Annex E – United States

In the U.S., issuers listed on a national securities exchange[24] must comply with the audit committee requirements contained in SEC rules as well as the director independence and audit committee requirements of the applicable national securities exchange.

Under the NYSE listing requirements, an individual is only independent if the board affirmatively determines that the individual has no material relationship with the listed company, either directly or as a partner, shareholder or officer of an organization that has a relationship with the company. Under the Nasdaq listing requirements, an individual is considered independent only if the individual is not an executive officer or employee of the company and the board affirmatively determines that the individual does not have any relationship which would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. The NYSE and Nasdaq have adopted additional independence requirements for compensation committee members.[25]

Both the NYSE and Nasdaq have bright line independence criteria, i.e. disqualifying relationships and transactions. The following are extracts from the relevant NYSE and Nasdaq listing requirements:

NYSE[26]	**Nasdaq**[27]
The director is, or has been within the last three years, an employee of the listed company, or an immediate family member is, or has been within the last three years, an executive officer, of the listed company.	A director who is, or at any time during the past three years was, employed by the Company. A director who is a Family Member of an individual who is, or at any time during the past three years was, employed by the Company as an Executive Officer.
The director has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than $120,000 in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not	A director who accepted or who has a Family Member who accepted any compensation from the Company in excess of $120,000 during any period of twelve consecutive months within the three years preceding the determination of independence, other than the following: (i) compensation for board or board

[24] 17 CFR. 240.10A-3(b)(1).
[25] NYSE Listed Company Manual Section 303A.02(a)(ii) and Nasdaq Listing Rule 5605.(d)(2).
[26] NYSE Listed Company Manual Section 303A.02(b).
[27] Nasdaq Listing Rule 5605.(a)(2).

NYSE[26]	**Nasdaq**[27]
contingent in any way on continued service).	committee service; (ii) compensation paid to a Family Member who is an employee (other than an Executive Officer) of the Company; or (iii) benefits under a tax-qualified retirement plan, or non-discretionary compensation.
(A) The director is a current partner or employee of a firm that is the listed company's internal or external auditor; (B) the director has an immediate family member who is a current partner of such a firm; (C) the director has an immediate family member who is a current employee of such a firm and personally works on the listed company's audit; or (D) the director or an immediate family member was within the last three years a partner or employee of such a firm and personally worked on the listed company's audit within that time.	A director who is, or has a Family Member who is, a current partner of the Company's outside auditor, or was a partner or employee of the Company's outside auditor who worked on the Company's audit at any time during any of the past three years.
The director or an immediate family member is, or has been with the last three years, employed as an executive officer of another company where any of the listed company's present executive officers at the same time serves or served on that company's compensation committee.	A director of the Company who is, or has a Family Member who is, employed as an Executive Officer of another entity where at any time during the past three years any of the Executive Officers of the Company serve on the compensation committee of such other entity.
The director is a current employee, or an immediate family member is a current executive officer, of a company that has made payments to, or received payments from, the listed company for property or services in an amount which, in any of the last three fiscal years, exceeds the greater of $1 million, or 2% of such other company's consolidated gross revenues.	A director who is, or has a Family Member who is, a partner in, or a controlling Shareholder or an Executive Officer of, any organization to which the Company made, or from which the Company received, payments for property or services in the current or any of the past three fiscal years that exceed 5% of the recipient's consolidated gross revenues for that year, or $200,000, whichever is more, other than the following:

NYSE[26]	Nasdaq[27]
	(i) payments arising solely from investments in the Company's securities; or (ii) payments under non-discretionary charitable contribution matching programs.

For purposes of applying the NYSE and Nasdaq bright line independence criteria, a parent or subsidiary company of a listed company is considered as if it were the listed company.

In addition, audit committee members of NYSE and Nasdaq listed companies[28] must satisfy the requirements for independence set out in the SEC rules.[29] As directed by the *Sarbanes-Oxley Act of 2002*, the SEC adopted rules to direct the national securities exchanges to prohibit the listing of any security of an issuer that is not in compliance with the audit committee requirements mandated by the *Sarbanes-Oxley Act of 2002*, including the requirements relating to the independence of audit committee members.[30] The following is an extract from the relevant SEC rules:

In order to be considered to be independent for purposes of this paragraph, a member of an audit committee of an issuer may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee

(i) accept any consulting, advisory or other compensatory fee from the issuer; or
(ii) be an affiliated person of the issuer or any subsidiary thereof.

[28] NYSE Listed Company Manual Section 303A.07 and Nasdaq Listing Rule 5605(c)(2)(A).
[29] Section10A-3(b)(1) of the Securities Exchange Act of 1934.
[30] Section 10A(m)(1) of the Securities Exchange Act of 1934, as added by Section 301 of the Sarbanes-Oxley Act of 2002.