



Pension Investment Association of Canada

Association canadienne des gestionnaires de fonds de retraite

June 15, 2004

Alberta Securities Commission
Saskatchewan Securities Commission
Manitoba Securities Commission
Ontario Securities Commission
Nova 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

c/o Mr. John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1900,, Box 55
Toronto, ON M5H 3S8

Via e-mail to: jstevenson@osc.gov.on.ca

Re: 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

Dear Sirs/Mesdames,

The Pension Investment Association of Canada (PIAC) is the representative organization for pension funds in Canada in matters relating to investment. The Association presently represents 135 Canadian pension funds that manage over \$595 billion in assets for the benefit of more than six million Canadian beneficiaries. PIAC's mission statement is "*to promote the financial security of pension fund beneficiaries through sound investment policy and practices*". This mission is the focus of all PIAC activities and is pursued by Members through its many programs and committee activities.

PIAC's Members are among the largest institutional investors in Canada. They have been interested in good corporate governance for many years. One of the main reasons for this interest is that their large holdings of securities cannot be disposed of without significant market impact when a company is not focused on creating shareholder value.

PIAC first published its *Corporate Governance Standards* in 1993 – prior to the publication of the Dey Report. These *Standards* were revised in 1997, and again in 2001, and are available on the PIAC website (<http://www.piacweb.org>). PIAC's *Standards* state:

*“Corporate management is accountable to the Board of Directors. The Board of Directors is responsible for maximizing long-term growth of shareholder value. The Board reports to the shareholders. The Board should reinforce these concepts in making its appointments and by appropriately defining the separate roles of Board members and management.”*¹

As you can see, PIAC is quite clear in its representation of the interests of shareholders, as opposed to securities issuers.

PIAC has made several submissions to regulatory authorities in response to the various reports of committees regarding corporate governance guidelines and standards, and we would like to submit our views regarding *Multilateral Policy 58-201 – Effective Corporate Governance* (“MP 58-201”) and *Multilateral Instrument 58-101 – Disclosure of Corporate Governance Practices, Form 58-101F1 and Form 58-101F2*.

The first thing that is apparent is that the proposed **MP 58-201 seems to set out best practice guidelines from the point of view of issuers** as no statement referring to the responsibility of the Board to shareholders has been included.

So, primarily, MP 58-201 seeks to outline standards for the organization and behaviour of the Board of Directors. Regarding the composition of the Board, and the independence of the Chair, MP 58-201 and PIAC agree. However, **no mention of the alignment of interests between Board members and shareholders is made, and there is no discussion of the fiduciary duty of Board members to shareholders**. PIAC feels that this represents a gap in the “effectiveness” of the corporate governance standards MP 58-201 is trying to espouse.

PIAC has identified a further gap in the fact that specific guidelines on “Takeover Protection” and “Shareholder Rights” are not addressed at all in MP 58-201 or in MI 58-101. In this regard, PIAC would suggest that good governance practices would require Boards to submit major corporate changes (such as take-over bids, going-private transactions, leveraged-buyouts, and the like) to a vote of shareholders not controlled by management. PIAC also feels that all shareholders should be treated equally, with the same rights per share, with the exception of stock purchased as a part of a senior class with separate, explicitly defined rights. Finally, good governance includes the disclosure of proxy voting results, which the Board should be required to ensure is full and complete. This should include, at a minimum the votes for, against and withheld.

PIAC believes that, while the section entitled “Compensation” in MP 58-201 clearly outlines the responsibilities of the Compensation Committee, it does not include the requirement of the Committee to inform shareholders of the principles and structure of the company’s executive compensation system for all forms of executive compensation, as well as SERPs.

However, MP 58-201 goes further than previous corporate governance guidelines in outlining the mandate for the Board. It suggests not only that the Board should adopt a written mandate, but what that mandate should encompass. MP 58-201 goes further to suggest that written position descriptions for the Chair of the Board, and the Chair of each committee be developed. MP 58-201 also addresses Board orientation and education, with consideration given to the skill set required on the Board and providing opportunities for Board members to maintain/enhance their skills on an on-going basis. **PIAC commends the securities regulatory authorities for their work on further specifying the responsibilities of Boards.**

¹ *PIAC Corporate Governance Standards*, section A, “Boards of Directors”

The proposed MP 58-201 suggests that all Boards must have a Nominating Committee and a Compensation Committee; and goes into some detail regarding the responsibilities of these committees. **PIAC agrees and supports this requirement.** In fact, one of the most encouraging aspects of MP 58-201 regarding compensation is the suggestion that the Compensation Committee have “a written charter that establishes the committee’s purpose, responsibilities, member qualifications, member appointment and removal, structure and operations (including any authority to delegate to individual members or subcommittees), and the manner of reporting to the board.”² However, PIAC would suggest including a statement of principle that the design of a compensation plan is more important than the size of the total remuneration; the Compensation Committee should develop a compensation system that induces management’s interests to coincide with those of shareholders in building long-term value. **This would provide the direction towards the interests of shareholders.**

Along a similar vein, the proposed guidelines state that the Nominating Committee should “consider what competencies and skills the board, as a whole, should possess... Assess what competencies and skills each existing director possesses... (T)he board should be considered as a group, with each individual making his or her own contribution.”³ **This is an enhancement over the previous standards and PIAC supports this enhancement.**

However, other than referring to another Multilateral Instrument (MI 52-110) on Audit Committees, no mention of an Audit Committee is made, and no direction is given as to the Audit Committee’s responsibilities. **Presumably, MI 52-110 covers those responsibilities, although it would be useful for MP 58-201 to at least paraphrase MI 52-110 and explicitly direct readers to that Instrument.**

There is a suggestion that a Corporate Governance Committee might be appointed to “develop the issuer’s approach to corporate governance, including developing a set of corporate governance principles and guidelines that are specifically applicable to the issuer.”⁴ **No suggestion of reporting to shareholders on the company’s governance standards and practices and its evaluation of their effectiveness is made, and PIAC would welcome this requirement.** MP 58-201 does outline the need for a code of conduct and the board’s responsibility for monitoring compliance with the company’s code of business conduct and ethics policy. **Again, PIAC supports this requirement.**

PIAC noted in its submission commenting on the recommendations of the Saucier Committee that emphasis was placed on guiding behaviour of issuers rather than outlining practices in the interest of shareholders. The same comment can be made regarding MP 58-201. While the Multilateral Policy goes further in detailing the responsibilities of Boards and some Committees, **it does not address other issues important to shareholders and potential investors, such as the alignment of interests between Board members and shareholders, specific issues regarding shareholder rights, the nature of executive compensation, and limitations on takeover protection measures.**

While MP 58-201 goes further in detailing how a Board should be organized, what it should do, and some of the ways it should do it, **the policy falls short on fully describing all the aspects of “effective” corporate governance.**

For example, it is not clear whether MP 58-201 applies to the governance of income trusts. PIAC believes that income trusts, which are becoming a larger and larger part of the securities marketplace, deserve particular attention when it comes to corporate governance because they are

² Part 2, “Effective Corporate Governance”, subsection 2.2 (16) of Multilateral Policy 58-201

³ Ibid, subsection 2.2 (12) of Multilateral Policy 58-201

⁴ Ibid, subsection 2.2 (4) (g) of Multilateral Policy 58-201

not corporations, which are subject to basic, common governance principles as found in the *Canada Business Corporations Act (CBCA)* or equivalent provincial legislation. As income trusts can be extremely complicated structures governed by a combination of dozens of unique, complex documents the governance aspect of each income trust must be evaluated individually. Also, since the income trust unitholder owns securities which may be several layers removed from the corporation conducting the actual business of the trust, it is not enough for MP 58-201 to apply only to the issuer level. Most corporate governance concerns are unlikely to surface at this level.

PIAC urges the securities regulators to facilitate investors' understanding of the complete picture of corporate governance practices at income trusts by considering at a minimum, that the final recommendations put forth by MP 58-201 apply to the underlying business corporation in income trust structures, whether wholly-owned or not. This includes separately filed forms 58-101F, preferably for each entity in the trust structure. At the level where the trust makes distributions to unitholders, 58-101F should include a section to clarify general trust-related governance aspects:

- (1) Describe the recourse mechanism for investors if distributions are decreased.
- (2) Describe how the corporate governance structure compensates for any conflict of interests (e.g. management fees, sponsor).
- (3) For each entity in the Trust structure: Describe how unitholders have access to shareholder protection mechanisms similar to those provided under the CBCA, or equivalent provincial legislation. If unitholders do not have similar access, explain why explain this is appropriate.

As well, **language in MP 58-201 should be changed to reflect the nuances of income trusts (e.g., add Directors and Trustees, rather than just Directors).** PIAC has additional specific recommendations regarding income trusts that we would be pleased to share with the securities regulators.

Concerning disclosure, Multilateral Instrument 58-101 and Form 58-101F1 and 58-101F2, **PIAC feels that the major source for disclosure should be the Management Information Circular (MIC), not the Annual Information Form (AIF). The former is mailed to all shareholders, while the latter is not.** Therefore, disclosure in the MIC would ensure that all shareholders receive the information.

Finally, PIAC urges regulators to conform disclosure in MP 58-201 to other rules that have potential corporate governance implications. We state above that alignment of the interests of all shareholders is a fundamentally important concept. We understand that the practice of equity monetization of ownership can disrupt that alignment without other shareholders being aware, absent disclosure requirements. We believe that, if an insider is subject to the reporting requirements of MI 55-103 and has entered into an equity monetization transaction, form MP 58-201F should disclose:

1. Complete details of how the economic interest was altered, including total shares held by the insider and how many of those shares were subject to such derivative transactions, and
2. How such insider voted for each item in shareholder meetings held in the most recent twelve months.

Such insiders need to disclose how they voted on issues with economic implications to the issuer such as overly generous or dilutive compensation plans or certain mergers and acquisition

transactions. The potential exists that insiders may terminate the monetization transaction when the price of the security has decreased significantly.

Addressing the issues surrounding income trusts, adding guidelines regarding the alignment of interests between Board members and shareholders, setting out specific issues regarding shareholder rights, the nature of executive compensation, and limitations on takeover protection measures would go a long way to making MP 58-201 truly address "effective" corporate governance.

Respectfully submitted on behalf of the Members of the Pension Investment Association of Canada,

A handwritten signature in black ink, appearing to read "J. Richard Abbott". The signature is written in a cursive, flowing style.

J. Richard Abbott
Chair