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April 20, 2009

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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

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Dear Sirs and Mesdames:

Request for Comment: Proposed Repeal and Replacement of National Instrument 52-110 *Audit Committees* and Companion Policy 52-110 CP *Audit Committees*, National Instrument 58-101 *Disclosure of Corporate Governance Practices* and National Policy 58-201 *Corporate Governance Guidelines*

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We are pleased to respond to the above Request for Comment published on December 19, 2008. We believe that it is appropriate to reassess corporate governance disclosure obligations and guidance on corporate governance practices from time to time in light of accumulated experience and as practices evolve over time. Moreover, we have long held the view that the existing instruments fail to properly address the concerns of controlled companies arising from their ownership structure. However, we are surprised and troubled by the extent of the proposed changes, especially with respect to the standard for corporate governance disclosure and the meaning of “independent director” for purposes of the instruments. A complete overhaul of the current, well-understood regulatory approach to corporate governance in Canada is not necessary or desirable and will not be welcomed by the issuer community or investors. Further, the investment community’s ability to evaluate the proposal suffers from the proposal’s failure to articulate the problem which it is designed to resolve.

In the main body of this letter we outline our general concerns in more detail. We also attach a schedule in which we raise specific issues and provide specific technical comments which we hope will be considered to the extent the items referenced in the schedule are reflected in any revised version of the proposals.

Approach to Disclosure of Corporate Governance Practices

We do not support disclosure of corporate governance practices in the absence of a comparison to specified practices.

In 1994, the Dey Committee recommended that the Toronto Stock Exchange require each listed issuer to describe its corporate governance practices with reference to the guidelines proposed by the Dey Committee, including an explanation of the differences between the company’s system and the guidelines. The Dey Committee’s stated goal was to provide issuers with flexibility to develop their own systems of governance reflecting their own circumstances, but still provide a baseline against which governance practices could be evaluated. The Dey Committee’s approach to corporate governance disclosure has served Canada well over the last 15 years and is well-understood by both issuers and investors alike. Cogent reasons are needed before abandoning it.

We are concerned that the unstructured format and lack of guidance in the proposed requirements may lead either to the excessive disclosure of irrelevant material, or to a failure to address in the disclosure all pertinent elements of an issuer’s corporate governance practices. It seems unlikely that disclosure will be either consistent or comparable, either between issuers, or for the same issuer over various reporting periods. In order to generate useful information for investors, the disclosure requirements should carefully articulate what is expected of issuers.

The disclosure requirements also should recognize that corporate governance practices have evolved over time, with the result that there are many practices which are now so commonly accepted, and expected, that it is only informative to investors to disclose when they are not being followed. For example, the failure to have a board comprised of a majority of independent directors would be unusual and highlighting that difference would provide meaningful information to investors.

More importantly, aside from issues surrounding the quality and comparability of the disclosure, we are concerned about the substantive impact of these proposals on the quality of issuers' corporate governance. Disclosure with reference to best practices has proven to provide an effective incentive to improve corporate governance practices. We are concerned that the elimination of the "comply or explain" approach may slow the drive to enhance corporate governance practices over time.

We acknowledge the particular challenges faced by smaller issuers listed on the TSX Venture Exchange due to their more constrained resources. However, as a general principle we believe that all public companies, regardless of size, should have a benchmark to work from. Moreover, we believe that smaller issuers would find it less burdensome to comply with substantially the same current disclosure obligations as larger issuers than to comply with the proposed disclosure requirements set out in the Request for Comment.

Proposed Approach to Independence

General

We do not support the proposed revised test of director independence. We do not believe that the proposed reasonable perception test can or should be a substitute for the specific, fact-based analysis that must currently be undertaken, including a series of specified objective criteria that automatically preclude eligibility for status as an independent director. The reasonable perception test is unworkable because the views of reasonable people as to which relationships affect director independence vary greatly. For example, this test will not address the concerns of controlled companies because there are institutional shareholders and proxy voting services which view any representative of the controlling shareholder as being not independent. A reasonable perception test for the determination of whether or not a director is independent forces the board into the realm of supposition and conjecture, and may reduce accountability for the determination.

Furthermore, because the views of reasonable people regarding which relationships affect independence vary greatly, we recommend that there always remain, in addition to any facts-and-circumstances determination made by the Board, certain objective "bright line" tests for independence to provide a meaningful baseline for making independence determinations on a consistent basis between issuers.

Finally, we are surprised that the proposed test for director independence is substantially different from the definition applied under U.S. stock exchange listing requirements. At the time the CSA first proposed an instrument on audit committees, the CSA stated that in recognition of the fact that Canadian capital markets are largely integrated with and affected by U.S. markets it was appropriate to propose audit committee requirements in Canada which were similar to those

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in the United States. We believe that policy rationale still holds true. The proposed revised independence test not only fails to address the CSA's previously stated policy objective of harmonization with U.S. requirements, but does so without explaining any basis for why the previously articulated policy should be disregarded, or why the considerations underlying that policy no longer apply. Moreover, the reasonable perception test is more onerous in many respects than the tests for director independence under the U.S. stock exchange listing requirements, which, in light of the relatively smaller size of the Canadian market and of Canadian issuers on average, compared with the U.S. would be an odd and perhaps unintended result.

Controlled Companies

We believe director independence should be viewed in terms of independence from management and that nominees of controlled companies should not be disqualified from being considered to be independent. A controlling shareholder has a compelling interest in exercising strong oversight over management and reasonably ought to expect that its interests will be represented on the board of the companies in which it holds a controlling position. Concerns regarding potential conflicts of interest between the controlling shareholder and the issuer are already addressed by long-standing fiduciary principles and legislative requirements.

The proposed reasonable perception test for director independence does not address the CSA's stated goal of taking into account the concerns of controlling shareholders. Instead, it would be preferable to delete the words "and a parent of the issuer" from section 1.4(8) of the current version of NI 52-110 and modify section 1.3 or 1.5 of the same instrument to exclude controlling shareholders and their representatives from the definition of "affiliated entity". We also believe that there should be an explicit statement in the proposed revised instruments that a controlling or significant shareholder and its employees and executive officers are not disqualified from being independent.

<u>Proposed Corporate Governance Guidelines</u>

While we do have a number of specific comments on the proposed revised corporate governance guidelines, we do think that the proposed approach of identifying key corporate governance principles and providing additional commentary and specific examples of practices furthering the principles provides better guidance than the current version of the corporate governance guidelines. The tone of the current version of the corporate governance guidelines is prescriptive and fails to recognize the rich diversity of practices which enable issuers to achieve good governance.

Finally, as a general comment, in our view some of the statements made in the proposed revised corporate governance guidelines are inconsistent with the board's oversight responsibility and fiduciary duties under applicable corporate law. For example, the commentary in Principle 1 states that the board sets the vision and direction of the issuer and the strategy must meet the board's vision and direction. In fact, as a matter of corporate law, the responsibility of the board

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is to assess and approve the vision and direction of the issuer developed by management. Moreover, in several places the board is given responsibility for “ensuring” certain processes are in place or outcomes occur. In our view, the board’s oversight responsibility means that it should require management to implement practices in furtherance of the issuer’s objectives, but the board is not in the position of being able to guarantee outcomes.

We are pleased to have had an opportunity to provide you with our comments. If you have any questions or comments, please direct them to Andrew J. MacDougall (amacdougall@osler.com) at 416-862-4732.

Yours very truly,

Osler, Hoskin & Harcourt LLP

SCHEDULE

The following are our detailed comments on the proposed revised corporate governance instruments.

NATIONAL POLICY 58-201

Section 1.1

- We believe that the definition of "corporate governance" is inaccurate and the focus on direction and control is insufficiently robust. The rules, relationships, systems and processes which are referenced create a framework of authority within which issuers make decisions. They are not intended to dictate the way in which issuers are to operate and conduct their affairs. We would propose the following revised version:

  > "Corporate governance is the set of rules, relationships, systems and processes pursuant to which decisions of the issuer are made. It covers relationships between an issuer's executive officers, board of directors, shareholders and other stakeholders, and the mechanisms by which directors, executive officers and others are accountable for the issuer's decisions."

Principle 1

- Accountability of a board to the issuer "and its shareholders" is inconsistent with directors' fiduciary duties which are solely to the issuer.

- It is unclear what "empowering the CEO" to create a culture of integrity means or will require. Issuers are familiar with and understand the guideline in Section 3.4 of the current version of National Policy 58-201 relating to the board satisfying itself that the CEO and other executive officers create a culture of integrity throughout the organization. We suggest retaining the existing formulation of the board's responsibility.

- We disagree with the use of the term "ensure" or "ensuring" in this Principle and other Principles.

- With respect to the "strategic plan", in our experience issuers typically pursue multiple strategic initiatives and strategies for their business units and there is typically not a single document entitled a "strategic plan". Further, it is unclear why annual approval is appropriate.

- We are unclear what "providing directors with the terms and conditions" of their appointment means. Directors can only be removed by shareholder vote.

Principle 2

- Remove "will" from the Principle as directors should contribute to the board's effectiveness immediately upon appointment.

- In (b) please delete "with a view to its best interests" as that is subsumed in (a).

- Please replace the sub-heading "commitment" with "contribution" as it is ultimately the contribution of a director to the board which is important.

- Under "Board Interaction" it is unclear why "no individual or small group should dominate the board's decision-making". This is not necessarily inconsistent with the goal of facilitating effective decision-making.

- Under "Practices Related to the Composition of the Board" in (c) please define what an "appropriate number" of independent directors is – we are of the view that it should mean proportionate as recommended by the Dey Committee.

Principle 3

- We believe this Principle is subsumed in Principle No. 2 as both are about competency.

Principle 4

- While we agree that boards should strive to improve their performance we disagree that it can be done on a "continuous" basis, given that directors perform their functions on a periodic basis and do not devote their full time and attention to an issuer's affairs. The word "Continuously" should be removed from the main heading.

Principle 5

- Replace "issuer" with "investor" at the end of the second sentence in the commentary. Presumably investor confidence is enhanced by a board setting ethical standards acceptable to the investor rather than the issuer.

- Delete general practice (d) as a determination of whether a departure from the standards or code constitutes a "material change" involves a conclusion respecting a legal obligation to make disclosure rather than promotion of integrity.

Principle 6

- Principle 6 is not needed. While we agree that it is essential that boards of directors recognize and manage conflicts of interest, oversight and management of conflicts of interest is a long-standing fiduciary principle which has been enshrined in modern business corporations statutes and securities legislation.

- Commentary (a): Shareholders have different reasons for buying shares and therefore we don't believe this is an appropriate example of a conflict of interest.

- Commentary (b): It is unclear what "impartial" means in the context and it could be viewed as overlapping with independence requirements for directors. Perhaps substitute "disinterested".

Principle 7

- Paragraph 2 of the commentary is incorrect factually as there are a large number of financial institutions, for example, which treat risk management as a separate activity and therefore could not comply with this part of the commentary. Responsibility for risk "management" rests with management, not the board. Furthermore, even though ultimate responsibility for risk oversight may rest with the full board, the way the commentary is drafted implies that risk oversight cannot be assigned to a risk committee of the board.

Principle 8

- Issuers cannot "ensure" that the compensation policies align with the best interests of the issuer but can only design them with that intent.

- We disagree that compensation structures must necessarily include a balanced pursuit of short-term and long-term objectives. Depending on an issuer's particular circumstances at the time, it may be appropriate for the compensation structure to focus primarily or exclusively on short-term objectives. For example, issuers in financial difficulty may focus on incentives designed to meet short term objectives which must be met for the issuer to survive, even at the expense of pursuing longer-term objectives.

- The transparency of compensation disclosure deals with disclosure, not the substantive Principle, and is addressed by Form 51-102F6. Therefore it does not belong here.

- Under General Practices, (a)(iii) and (iv) do not provide any useful guidance and (a)(v) deals with disclosure, not the substantive Principle, so all should be deleted.

- Under "Practices related to compensation committee", practice (e) is not appropriate. Directors are directly involved in deciding their own compensation and executives need to have input into the process for deciding their own compensation.

Principle 9

- While we do not disagree with the principle of "engaging effectively with shareholders", the entire Principle is devoted to only the voting process. There are many other ways to ensure effective communication with, and input from shareholders including formal and informal meetings. This should be acknowledged, and examples of practices for "ongoing dialogue" that do not run afoul of the tipping rules should be provided.

- Principle 9 should be broadened to encompass the need for boards to engage effectively not only with shareholders, but also with other stakeholders, including creditors and local communities affected by the issuer's operations.

NATIONAL INSTRUMENT 58-101

Section 2.1

- Need to clarify its application to non-corporate issuers such as income trusts.
- Is it possible to meet this requirement by incorporation by reference into the proxy circular?
- What happens if a proxy circular is sent for an annual meeting but there is no requirement to elect the directors?

FORM 58-101 F1

General

- What happened to the obligation to file the code of conduct?

Principle 1

- **Section (d)** – What is meant by "qualifications"? Is it just those relating to the committee's mandate?
- **Section (e) –** Rather than "describe any" it would be more appropriate to say should "provide a general description of". However, since day to day management is delegated this disclosure could be voluminous and therefore we believe a better approach may be to describe the limits to management's approval authority instead.

Principle 2

- **Section (a) –** Replace "commitment" with "contribution".
- **Section (b) –** Should be limited to "key" competencies and attributes.
- **Section (c) –** This requirement should link to 2(b) so that the disclosure is of only those competencies and attributes which the board determines are necessary for the board (and therefore its directors) to fulfill its functions.
- **Section (d) –** It is not practical to require disclosure of all relationships the board may have considered. There needs to be a standard for determining which relationships are material and warrant disclosure.

Principle 3

- **Section (b) –** We do not see the value to investors of this disclosure and recommend it not be included. In any event, any disclosure regarding consultants or advisors who have assisted the nominating committee should specify which areas of advice would result in such disclosure. For example, is it just recruiting firms or does the disclosure include firms which provide advice on director compensation? Does it include legal advice on nomination practices? Does it include firms retained to do background checks on directors?

Principle 4

- **Section (a)(iii) –** We do not believe it is practical to disclose outcomes of an assessment process but if there is to be such an obligation then there must be more guidance as to what is meant by disclosure of "outcomes".

Principle 5

- **Section (a) –** This disclosure is likely to be generic and not meaningful. Furthermore, for this Principle to be meaningful there should be a corresponding obligation to make the code available.

Principle 6

- **Section (b) –** There are occasions when boards establish an ad hoc committee to consider a variety of matters where there is a potential conflict of interest in circumstances where identification of the existence of the committee and its mandate would be premature or harmful including: (a) consideration of whether there may be a potential transaction with a significant shareholder, and (b) investigation into allegations of wrongdoing by senior executives. At the very least there should be a materiality threshold for determining when disclosure is required.

- **Section (c) –** What is the value to investors of this disclosure? In addition, it could be premature to make such disclosure. The extent of the disclosure appears to be sweeping, especially in the absence of a transaction to be considered by shareholders – does it really intend to capture all investment banking, auditing and legal firms involved?

- **Section 7 –** This obligation is vague and will either result in voluminous disclosure or generic disclosure which does not provide meaningful information.

Principle 7

- A requirement under the proposed disclosure instrument to provide disclosure of "a summary of any policies on risk oversight and management adopted by the issuer" is too vague to provide guidance needed to assist issuers in providing meaningful disclosure respecting their practices for the oversight of risk management.

Principle 8

- **Section (a) –** This should be deleted as it is already addressed by the CD&A requirements in Form 51-102F6.

Principle 9

- **Section (a) –** The obligation is vague and unlikely to result in meaningful disclosure. Also the voting process is not as valuable a mechanism for engaging with shareholders as formal and informal communications are.

- **Section (b) –** Form 51-102F5 already addresses the requirement to disclose how directors are elected.

NATIONAL INSTRUMENT 52-110

Section 1.4(a)

- The standard also should exclude employees of affiliates who are not executive officers.

- Need to provide for the exceptions currently included in s.1.4(7) of NI 52-110 for (a) interim CEOs and (b) chairs and vice-chairs of the board.

Section 1.4(b)

- There should be an explicit statement in the proposed revised instrument or companion policy that a controlling or significant shareholder and its employees and executive officers are not disqualified from being independent. A statement to this effect is included in the Request for Comment (under "Proposed approach to independence (found in the Proposed Audit Committee Materials) - Definition of independence"), but has not been included in the proposed instruments themselves.

Section 2.3(5)

- The requirement for the audit committee to review all financial information "derived from" financial statements before disclosure is not practical. It should be sufficient for there to be a process for identifying when financial information must be reviewed by the audit committee and when an extract from financial statements can be disclosed without prior review by the audit committee.

Section 2.3(6)

- The requirement to assess procedures is the subject of management certification under NI 52-109 and does not need to be included here.

Section 2.4CP

- No explanation is given as to why this has been added. If the concept is to be retained then there will be a need to define what is meant by "an appropriate number", especially in the context of a three-person audit committee. Furthermore, guidance is needed on the meaning of "unrelated" and, in particular, guidance on whether a director who is an independent director of the controlling shareholder is considered to be unrelated to the controlling shareholder.

Section 3.1CP

- Guidance is required on the duration of any look-back tests.

- What is meant by "close association"?

- What is meant by "family ties"?

- From whose perspective is the significance of contractual or other business relationships to be assessed?

- What is meant by "significant professional adviser or consultant" and "significantly associated with the service provided"?

- For purposes of assessing independence, directors should consider compensation paid by the issuer, but also compensation paid by subsidiaries of the issuer.