



ONTARIO
SECURITIES
COMMISSION

December 18, 2009



OSC corporate sustainability
reporting initiative

Report to Minister of Finance



Report to Minister of Finance

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1. Introduction

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1. Introduction

1.1 OSC's mandate and project scope

Mandate

On April 9, 2009, the Ontario Legislature approved a broad resolution (the Resolution) introduced by MPP Laurel Broten calling upon the province of Ontario to review Ontario's existing corporate disclosure reporting requirements and compliance with those requirements, with a particular emphasis on additional financial and non-financial information needed to ensure that Ontario investors have access to all information material to them in making investment decisions. As part of the review, the resolution called upon the Ontario Securities Commission (OSC or we) to undertake a broad consultation to establish best practice corporate social responsibility and environmental, social and governance (ESG) reporting standards.

Following the approval of the non-binding resolution, the Ministry of Finance and the OSC discussed the appropriate focus and scope of the initiative. The OSC agreed to:

- review existing disclosure requirements under Ontario securities legislation for reporting issuers (other than investment funds) regarding corporate governance and environmental matters
- consult with investors, issuers, advisors and other stakeholders (together referred to as stakeholders) on these matters, and
- make recommendations to the Minister of Finance by January 1, 2010 regarding "next steps" to enhance disclosure of these matters, if determined necessary and appropriate.

Our recommendations must take into account the OSC's mandate of providing protection to investors from unfair, improper or fraudulent practices and fostering fair and efficient capital markets and confidence in capital markets. In addition, our recommendations should have regard to the following statutory principles:

- The integration of capital markets is supported and promoted by the sound and responsible harmonization and co-ordination of securities regulation regimes.
- Business and regulatory costs and other restrictions on the business and investment activities of market participants should be proportionate to the significance of the regulatory objectives sought to be realized.



In developing the OSC's mandate, a number of factors were considered, including the areas of concern expressed by investors and other stakeholders, various international developments and the relatively short timeline to complete the initiative. In light of those factors, the Ministry of Finance and the OSC agreed that the OSC should focus on the disclosure of corporate governance and environmental matters at this time. The Hennick Centre for Business and Law at York University (the Hennick Centre) is currently undertaking a review of the existing disclosure requirements under Ontario securities legislation for reporting issuers (other than investment funds) regarding corporate social performance. As part of that initiative, the Hennick Centre and Jantzi-Sustainalytics held a roundtable discussion with stakeholders on December 7, 2009. In early 2010, the Hennick Centre will make recommendations to the Minister of Finance regarding "next steps" to enhance corporate social performance disclosure.

The OSC and the Hennick Centre are working cooperatively on both of the OSC and the Hennick Centre initiatives.

Project scope

The OSC's consultation and review were guided by the following framework questions:

- What information on corporate governance and environmental matters would a reasonable investor need in order to make investment decisions?
- What are the challenges and benefits associated with providing information on corporate governance and environmental matters?
- Are existing disclosure requirements under Ontario securities legislation relating to corporate governance and environmental matters consistent with international requirements and standards?
- Is there additional information regarding corporate governance and environmental matters that is necessary to sustain the reputation of the Ontario capital markets?
- Are our existing continuous disclosure reviews of corporate governance and environmental matters adequate to support compliance with the applicable disclosure requirements?

1.2 Consultation process

OSC staff asked stakeholders for feedback on the adequacy of (i) the existing disclosure requirements regarding corporate governance and environmental matters and (ii) issuers' compliance with the requirements.



Roundtable discussion held on September 18, 2009

On September 18, 2009, the OSC held a roundtable discussion to which we invited representatives of investors, issuers and professional bodies (such as the Canadian Institute of Chartered Accountants), analysts, legal and accounting advisors and academics. The roundtable discussion was moderated by Edward Waitzer and Poonam Puri, Directors of the Hennick Centre. A consultation paper was distributed to the roundtable participants to seek their input on the initiative and an updated version of that paper is attached to this report as Schedule 1 (the Consultation Paper). A summary of the roundtable discussion is attached to this report as Schedule 2.

Consultations with advisory committees and other groups

Between May and November 2009, OSC staff consulted with the OSC's Continuous Disclosure Advisory Committee and Securities Advisory Committee, staff of the other Canadian Securities Administrators (CSA) and the Prospectors & Developers Association of Canada.

Individual consultations

Between April and December 2009, OSC staff also consulted with representatives of law firms, accounting firms, Ceres (a U.S.-based network of investors, environmental organizations and other public interest groups working with issuers and investors to address sustainability challenges such as global climate change), Canadian Business for Social Responsibility, Climate Change Lawyers Network, Corporate Knights and Shareholder Association for Research and Education (SHARE), as well as advisors to the Canadian Institute of Chartered Accountants.

The feedback OSC staff received from the consultation process has been incorporated into our recommendations to enhance disclosure of corporate governance and environmental matters set out in this report.

1.3 Review process

In addition to consulting with stakeholders, OSC staff reviewed the existing disclosure requirements regarding corporate governance and environmental matters and issuers' compliance with the requirements. This review involved an analysis of:

- CSA and OSC staff notices summarizing reviews of compliance with disclosure requirements regarding corporate governance and environmental matters under Ontario securities legislation
- written submissions relating to disclosure requirements on the CSA's corporate governance proposal published for comment on December 19, 2008



- disclosure requirements regarding corporate governance and environmental matters under securities legislation in Australia, Denmark, France, South Africa, the United Kingdom (U.K.) and the United States (U.S.)
- guidelines for disclosure of corporate governance and environmental matters under voluntary reporting frameworks, such as the Global Reporting Initiative Guidelines and the Carbon Disclosure Project (CDP)
- investor initiatives regarding climate change disclosure, such as the September 2007 petition to the U.S. Securities and Exchange Commission (SEC) (as amended)
- international developments in these areas, including initiatives undertaken by the SEC and the European Commission, and
- relevant academic research.





2. Recommendations to enhance disclosure

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2. Recommendations to enhance disclosure

2.1 Objective of recommendations

The proposed recommendations are designed to result in greater transparency for investors and the Canadian marketplace regarding (i) the nature and adequacy of issuers' corporate governance practices and (ii) the nature and extent of environmental risks and other environmental matters affecting issuers. This should assist investors when making decisions regarding investments and proxy voting. Investors have sought more information on these matters, and based on our consultations, would welcome regulatory action in this area.

The majority of stakeholders consulted as part of this initiative would like to see the OSC assume a greater role in advancing and promoting corporate governance and environmental disclosure. However, most of them believe that this can best be achieved through providing more guidance to issuers and conducting more continuous disclosure reviews, rather than by expanding existing disclosure requirements.

Both the majority of stakeholders and the OSC recognize the importance of a harmonized approach to disclosure of corporate governance and environmental matters across Canada. As a result, we have had, and will continue to have, discussions with the CSA regarding the recommendations set out in this report.

As a result, we recommend the following actions be taken to enhance disclosure of corporate governance and environmental matters.

2.2 Enhancing corporate governance disclosure

To enhance compliance with the existing corporate governance disclosure requirements set out in National Instrument 58-101 *Disclosure of Corporate Governance Practices*, we propose the following:

Recommendation #1 – Conduct a follow-up compliance review on corporate governance disclosure

OSC staff propose to conduct a follow-up compliance review of corporate governance disclosure. The review would build on the results of the CSA 2007 compliance review, outlined in CSA Staff Notice 58-303 *Corporate Governance Disclosure Compliance Review*.

While the scope and timeline for the review could be finalized at a later date, we recommend that the review involve assessing the corporate governance disclosure in information circulars (or annual information forms or annual management's discussion & analysis, if applicable) filed in spring 2010 by reporting issuers based in Ontario. Outcomes could include: (i) changes in corporate governance disclosure by the issuers in the review sample, either on a historical or prospective basis, and (ii) the



publication of a staff notice, summarizing results of the review and providing guidance on compliance with existing corporate governance disclosure requirements. We propose a completion date for this review by the end of 2010.

CSA staff would be invited to participate in the compliance review; however, the review could be done on an OSC-only basis if the other CSA jurisdictions choose not to participate.

Recommendation #2 – Continue educational outreach to issuers

OSC staff should continue to act as instructors with TSX staff at educational workshops on corporate governance disclosure offered by the TSX. The workshops are designed to provide issuers and their advisors with an overview of the corporate governance disclosure requirements and practical guidance on how to apply those requirements. The workshops historically have been offered on an annual basis.

2.3 Enhancing environmental disclosure

To enhance compliance with the existing environmental disclosure requirements set out in National Instrument 51-102 *Continuous Disclosure Obligations*, we propose the following:

Recommendation #1 – Provide additional guidance for issuers on existing environmental disclosure requirements

OSC staff propose to issue a notice providing guidance on compliance with existing environmental disclosure requirements, both in general terms and possibly on an industry-specific basis. The staff notice would seek to build on the guidance set out in OSC Staff Notice 51-716 *Environmental Reporting* and respond to the evolving nature of environmental matters.

In developing the staff notice, we recommend that an ad hoc advisory committee comprised of experts in this area be established to facilitate developing guidance that is both appropriate and useful for issuers.

While the timeline for the staff notice could be finalized at a later date, we recommend that it be published by fall 2010 so that reporting issuers have sufficient time to consider the guidance when preparing their 2010 annual continuous disclosure documents.

CSA staff would be invited to participate in the development of the staff notice; however, the staff notice could be an OSC-only notice if the other CSA jurisdictions choose not to participate.

Recommendation #2 – Improve training for OSC staff on environmental disclosure

OSC staff should hold training session(s) for Corporate Finance staff regarding disclosure of environmental matters. The objective would be to identify areas of concern and provide guidance on the types of



comments that may be raised during continuous disclosure reviews. These training sessions should be held after the staff guidance is issued.

2.4 Impact on reporting issuers

We are not proposing to impose any new disclosure requirements on issuers; however, issuers that are currently not fully complying with existing disclosure requirements may face greater compliance costs than in the past as they work towards improving their disclosure. During our consultations, we were advised that once reporting systems have been established, ongoing compliance costs are often minimal. The stakeholders consulted believe that the benefits to investors from receiving enhanced disclosure will likely exceed any increase in compliance costs for issuers as a result of our recommendations.

2.5 Commission notice

We published OSC Notice 51-717 *Corporate Governance and Environmental Disclosure* (the Notice) outlining our proposed plans to enhance disclosure of corporate governance and environmental matters on December 18, 2009. The Notice was intended to alert stakeholders to our response to the Resolution and the identified concerns regarding corporate governance and environmental disclosure. In particular, it provides issuers with an opportunity to review and enhance their corporate governance disclosure before being subject to a compliance review.





3. Feedback and analysis

- 3.1 Views expressed during the consultation process
- 3.2 Research and analysis

3. Feedback and analysis

3.1 Views expressed during the consultation process

Materiality of ESG disclosure

The stakeholders consulted as part of this initiative generally agree that information regarding environmental and corporate governance matters may constitute “material information” which is required to be disclosed in an issuer’s continuous disclosure documents filed under securities legislation.

The test for materiality in this context is a “reasonable investor” test. Information is likely material if a reasonable investor’s decision whether or not to buy, sell or hold securities in an issuer would likely be influenced or changed if the information in question was omitted or misstated. Stakeholders generally believe that the type of information that may affect a reasonable investor’s investment decision has shifted in recent years to include a greater scope of corporate governance and environmental matters. This shift is expected to continue as we move towards a carbon-constrained economy.

This view on the materiality of ESG disclosure is confirmed by the paper published by the CFA Institute in 2008, “*Environmental, Social and Governance Factors at Listed Companies: A Manual for Investors*”, which states that:

A growing number of investors (such as those committed to the [Principles for Responsible Investment] and other initiatives) have begun to focus on ESG factors to arrive at a more thorough understanding of the risks and opportunities that face the companies in which they invest. These investors share the view that a prudent investor ought to consider ESG issues in his or her analysis because these factors can have an impact on investment performance.

Concerns regarding deficient disclosure

During our consultations, stakeholders expressed concerns regarding the adequacy of corporate governance and environmental disclosure. In particular, they noted that:

- the information regarding corporate governance and environmental matters is found in multiple sources: management’s discussion & analysis, annual information forms, information circulars and voluntary reports
- the information is not necessarily complete or reliable, and is often not provided in a form that facilitates comparisons among issuers



- if the information is not included in securities regulatory filings, it is not necessarily provided on a timely basis, and
- in the case of environmental disclosure, the information is often not integrated with financial reporting, nor is it typically audited or verified by an external party.

Adequacy of existing disclosure requirements

During our consultations, we heard from stakeholders that our existing disclosure requirements regarding corporate governance and environmental matters are generally adequate.

With respect to corporate governance disclosure requirements, stakeholders generally do not support the implementation of the CSA's corporate governance proposal published for comment on December 19, 2008, which included significant changes to the disclosure requirements.¹ Instead, stakeholders favour retaining the existing "comply or explain" disclosure model for TSX-listed issuers and the general disclosure model for venture issuers. While they believe disclosure regarding areas such as risk management and shareholder engagement are important, they expressed the view that now is not an appropriate time to amend the existing requirements to address those areas. Stakeholders generally think that the existing disclosure requirements are adequate and securities regulators should focus on improving compliance with those requirements.

Stakeholders also generally agree that the existing disclosure requirements are broad enough to capture disclosure of material environmental matters.

Adequacy of compliance with existing disclosure requirements

The stakeholders consulted as part of this initiative generally believe that the poor compliance with existing disclosure requirements is primarily responsible for inadequate levels of disclosure. This view is supported by the results of compliance reviews conducted by OSC and CSA staff and third parties in respect of both corporate governance and environmental disclosure. Those results are discussed in section 3.2 under the heading *Concerns regarding deficient disclosure* below.

In addition, stakeholders agree that compliance with existing disclosure requirements could be enhanced. They recommend providing issuers with additional guidance on the nature and extent of disclosure required under

¹ On November 13, 2009, the CSA announced that they do not intend to implement the corporate governance amendments, as originally published for comment in December 2008. The CSA agreed that now is not an appropriate time to recommend significant changes to the CSA's corporate governance regime. The CSA is considering whether to recommend any limited changes to the corporate governance regime at this time. Any proposed changes would be published for public comment.



the existing environmental disclosure requirements, particularly in respect of climate change risk, and reinforcing compliance with corporate governance disclosure requirements through our continuous disclosure review program and educational programs.

3.2 Research and analysis

A summary of our research is set out in the Consultation Paper attached to this report as Schedule 1.

Concerns regarding deficient disclosure

Concerns regarding the adequacy of disclosure of corporate governance and environmental matters in continuous disclosure documents have been noted by OSC and CSA staff, third parties and investors.

a. Results from our continuous disclosure reviews

We conducted a review of corporate governance disclosure in 2007 and environmental disclosure in 2007-2008. Overall, we found several areas of deficient disclosure in both reviews.

- Corporate governance disclosure.** In 2007, CSA staff reviewed the corporate governance disclosure of 65 TSX-listed issuers and 35 venture issuers. The purpose of the review was to assess compliance with the disclosure requirements in National Instrument 58-101 *Disclosure of Corporate Governance Practices*, and in particular, to review the substance of the disclosure to assess whether the quality was sufficient to provide a clear and complete account of an issuer's corporate governance practices.

The results of the review are summarized in CSA Staff Notice 58-303 *Corporate Governance Disclosure Compliance Review*, published on June 29, 2007. Overall, deficiencies in each category of disclosure were identified.

As a result of the review, 27 TSX-listed issuers and nine venture issuers were required to address deficiencies in their next management information circular or annual information form. In addition, two venture issuers were required to refile their management information circulars because they failed to provide any corporate governance disclosure.

- Environmental disclosure.** In 2007, OSC staff reviewed the filings of 35 reporting issuers based in Ontario to assess compliance with the existing disclosure requirements regarding environmental matters. Staff focused on the adequacy of disclosure of matters such as financial liabilities related to the environment, asset retirement obligations, financial and operational effects of environmental protection requirements, environmental policies and environmental risks.



The results of the review are set out in OSC Staff Notice 51-716 *Environmental Reporting*, which was published on February 27, 2008. Staff found several areas of deficient disclosure. The information provided by issuers was often boilerplate and did not provide meaningful information to investors. The staff notice provided guidance for issuers to consider when preparing their continuous disclosure documents and was intended to be used by issuers as an educational tool to enhance their disclosure.

b. Results from reviews by third parties

The results from our continuous disclosure reviews are consistent with the findings of third parties:

- **Corporate governance disclosure.** The TSX has advised us that it conducts reviews of issuers' corporate governance disclosure annually. In the course of its reviews, when it identifies deficient disclosure, TSX staff engage with the issuers selected for review, with a view to improving their corporate governance disclosure. The results of those reviews are not made public.
- **Environmental disclosure.** On October 14, 2009, a coalition of Canadian investors and environmental groups (comprised of the British Columbia Investment Management Corporation, Ceres, Climate Action Network Canada and the Climate Change Lawyers Network) called on the OSC to pursue several actions aimed at increasing mandatory disclosure of climate change related risks in securities filings as part of the OSC's initiative on corporate sustainability reporting.

In their submission to the OSC, the signatories included a survey of disclosure in 2008 annual reports by 35 reporting issuers in Ontario in nine industry sectors with market capitalization of at least CDN \$1 billion. The survey found that the disclosure contained poor or limited descriptions of climate change risks, if the issue was discussed at all. The signatories recommended that the OSC work with the CSA to provide guidance to issuers on how to disclose climate change risks within the context of existing reporting obligations. The signatories also encouraged the OSC to improve corporate governance disclosure of how issuers are addressing their climate change risk at board and management levels.

c. Investor requests for information

Investors have been requesting information about environmental matters directly from issuers to supplement the information provided in securities regulatory filings.

- **Requests for information from issuers.** Investors have been requesting information about climate change directly from issuers. The CDP is the largest investor coalition in the world and includes more than 475 signatory investors with assets under management of US\$55 trillion. These investors reflect a wide range of institutions, including banks, fund managers, pension funds, socially responsible investors and



insurance companies. They sign an annual request for information which is sent to the chair of the board of each of the world's largest companies by market capitalization. The request for information covers four main areas: management's views on the risks and opportunities related to climate change, greenhouse gas emissions accounting, management's strategy to reduce emissions/minimize risk and capitalize on opportunity, and corporate governance with regard to climate change.

- **Shareholder proposals.** Investors are also making their desire for enhanced environmental disclosure known through shareholder resolutions. According to the Shareholder Resolution Database maintained by SHARE, in the 2009 annual general meeting year, 12 of the 101 shareholder proposals and resolutions filed with Canadian issuers related to environmental matters. They covered topics such as the monitoring of greenhouse gas emissions, participation in the CDP and reporting on the effect of, or exposure to risks relating to, climate change.

Adequacy of existing disclosure requirements

From our review, Canadian disclosure requirements are comparable to those in other jurisdictions. We reviewed the disclosure requirements in Australia, Denmark, France, South Africa, the U.K. and the U.S. We also reviewed guidelines for disclosure under voluntary reporting frameworks, investor initiatives and relevant academic research.

a. Corporate governance disclosure

The existing corporate governance disclosure requirements are set out in National Instrument 58-101 *Disclosure of Corporate Governance Practices*. From our review of the corporate governance disclosure requirements in other jurisdictions, existing Canadian requirements are comparable in many respects to those found in Australia, South Africa and the U.K. These three jurisdictions all apply some form of a “comply or explain” model similar to Canada, and their corporate governance disclosure regimes incorporate recommendations or principles on issues found in the Canadian framework, such as the independence of board directors and the mandate of the board. Some jurisdictions require certain disclosure relating to risk management and shareholder engagement that is not required under the existing Canadian framework. As noted above, the stakeholders consulted as part of this initiative do not believe that now is the appropriate time to amend the existing requirements to address those areas.

The OSC will nonetheless be considering as an on-going policy matter whether limited changes to the existing corporate governance regime are desirable.



b. Environmental disclosure

The existing environmental disclosure requirements are set out in Form 51-102F1 *Management's Discussion & Analysis* and Form 51-102F2 *Annual Information Form*. The requirements appear to be comparable in some respects to those in other jurisdictions. They are very similar to the requirements under U.S. securities legislation, and are arguably broad enough to capture the same disclosure required under the securities legislation of jurisdictions such as the U.K and Australia.





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As the regulatory body responsible for overseeing the capital markets in Ontario, the Ontario Securities Commission administers and enforces the provincial Securities Act, the provincial Commodity Futures Act and administers certain provisions of the provincial Business Corporations Act. The OSC is a self-funded Crown corporation accountable to the Ontario Legislature through the Minister of Finance.



Schedule 1 – Consultation paper

September 3, 2009
(as updated December 7, 2009)



OSC corporate sustainability reporting initiative

Consultation paper



Consultation paper

OSC staff prepared this paper for discussion purposes only in connection with the OSC's roundtable discussion on September 18, 2009 with respect to disclosure of corporate governance and environmental matters.

Note

The information provided in this paper is summary in nature and is not intended as legal or accounting advice. Readers interested in the environmental and corporate governance disclosure requirements in Canada and other jurisdictions should refer to the applicable legislative provisions and/or seek legal or accounting advice.

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Appendix B - Existing Canadian corporate governance disclosure requirements





1. Introduction

- 1.1 OSC initiative
- 1.2 Purpose of consultation paper
- 1.3 Background on initiative

1. Introduction

1.1 OSC initiative

This consultation paper was prepared by staff of the Ontario Securities Commission (OSC) in connection with the OSC initiative to review existing disclosure requirements for environmental and corporate governance matters under Ontario securities legislation.

1.2 Purpose of consultation paper

OSC staff prepared this paper for discussion purposes in connection with the OSC's roundtable discussion held on September 18, 2009. This paper was intended to provide background information for roundtable participants. It also sets out consultation questions on which we were seeking input from roundtable participants.

1.3 Background on initiative

Legislative resolution

On April 9, 2009, the Ontario legislature unanimously approved a broad resolution introduced by MPP Laurel Broten. The non-binding resolution calls on the OSC to conduct a consultation into best practices on corporate social responsibility (CSR) and environmental, social and governance (ESG) reporting standards. The resolution reads:

Be it resolved that, in the opinion of this House, the province of Ontario should undertake a review of Ontario's current corporate disclosure reporting requirements, standards and compliance therewith, with a particular emphasis on additional financial and non-financial information to ensure that Ontario investors have access to all information material to them in making investment decisions.

That, in undertaking such a review, the Ontario Securities Commission (OSC) should undertake a broad consultation with its own advisory bodies including the Continuous Disclosure Committee, concerned stakeholders, appropriate interest groups and individuals and other securities regulators, to establish best practice corporate social responsibility (CSR) and environmental, social and governance (ESG) reporting standards.

That the OSC seek to develop and adopt an enhanced standardized reporting framework for both quantitative and qualitative social and environmental information to ensure corporate disclosures are understandable, comparable and outcome-focused.



That the OSC shall report back to the Minister of Finance no later than January 1, 2010, with regard to its findings, together with recommendations for next steps to enhance disclosure.

OSC's mandate and project scope

a. Mandate

Following the approval of the non-binding resolution, the Ministry of Finance and OSC discussed the appropriate focus and scope of the initiative. The OSC agreed to:

- review existing disclosure requirements under Ontario securities legislation for reporting issuers (other than investment funds) regarding corporate governance and environmental matters, and
- consult with investors, issuers, advisors and other stakeholders on these matters, and
- make recommendations to the Minister of Finance by January 1, 2010 regarding “next steps” to enhance disclosure of these matters, if determined necessary and appropriate.

In developing the mandate, a number of factors were considered, including the areas of concern expressed by investors and other stakeholders, various international developments and the relatively short timeline to complete the initiative. In light of those factors, the OSC and the Ministry of Finance agreed that the OSC should focus on the disclosure of corporate governance and environmental matters at this time. The Hennick Centre for Business and Law at York University (the Hennick Centre) is currently undertaking a review of the disclosure requirements for social matters and will report directly to the Minister of Finance. As part of that initiative, the Hennick Centre and Jantzi-Sustainalytics hosted a roundtable on corporate social reporting on December 7, 2009, to which they invited representatives from government agencies (including the OSC), non-profit organizations and business. The OSC may consider reviewing the disclosure requirements for social matters as a separate initiative in the future.

b. Project scope

The OSC's review is guided by the following framework questions:

- What information on corporate governance and environmental matters would a reasonable investor need in order to make investment decisions?
- What are the challenges and benefits associated with providing information on corporate governance and environmental matters?



- Are existing disclosure requirements under Ontario securities legislation relating to corporate governance and environmental matters consistent with international requirements and standards?
- Is there additional information regarding corporate governance and environmental matters that is necessary to sustain the reputation of the Ontario capital markets?
- Are our existing continuous disclosure reviews of corporate governance and environmental matters adequate to support compliance with the applicable disclosure requirements?

Our recommendations must take into account the OSC's mandate of providing protection to investors from unfair, improper or fraudulent practices and fostering fair and efficient capital markets and confidence in capital markets. In addition, our recommendations should have regard to the following statutory principles:

- The integration of capital markets is supported and promoted by the sound and responsible harmonization and co-ordination of securities regulation regimes.
- Business and regulatory costs and other restrictions on the business and investment activities of market participants should be proportionate to the significance of the regulatory objectives sought to be realized.

Our review involves an analysis of:

- Canadian Securities Administrators (CSA) and OSC staff notices summarizing reviews of compliance with disclosure requirements regarding corporate governance and environmental matters under Ontario securities legislation
- written submissions relating to disclosure requirements on the CSA's corporate governance proposal published for comment on December 19, 2008
- disclosure requirements regarding corporate governance and environmental matters under securities legislation in Australia, Denmark, France, South Africa, the United Kingdom (U.K.) and the United States (U.S.)
- guidelines for disclosure of corporate governance and environmental matters under voluntary reporting frameworks, such as the Global Reporting Initiative Guidelines (GRI) and the Carbon Disclosure Project (CDP)



- investor initiatives regarding climate change disclosure, such as the September 2007 petition to the U.S. Securities and Exchange Commission (SEC) (as amended), and
- relevant academic research.

International developments

Initiatives are underway in the U.S. and Europe to review corporate disclosure of ESG matters.

a. U.S.

The Investor Network on Climate Risk sent a letter to the SEC in June 2009, requesting that the agency take a number of steps to improve corporate disclosure of material ESG risks in securities filings, with particular emphasis on climate change-related risk disclosure. In July 2009, SEC Commissioner Elisse Walter announced that the agency is taking a “serious look” at climate change disclosure and will be eliciting the views of experts in the area.

The SEC recently met with prominent advocates of climate change related-risk disclosure, including Wisconsin insurance regulator Sean Dilweg and Maryland Treasurer Nancy Kopp. The private meetings were coordinated by Ceres, a U.S.-based network of investors, environmental organizations and other public interest groups working with issuers and investors to address sustainability challenges such as global climate change. More meetings are planned for this year.

On July 27, 2009, the SEC’s Investor Advisory Committee discussed disclosure of ESG issues. The briefing paper for that meeting identified ESG disclosure as a key disclosure area for preliminary discussion. The paper set out the following questions for discussion:

- Do investors consider environmental compliance, climate change and sustainability issues important in making investment or voting decisions?
- Are current disclosure practices with respect to environmental compliance, climate change and sustainability issues sufficient for investors to make informed investment and voting decisions, or do investors need expanded disclosure in any of these areas?
- If additional disclosure in these areas would be useful to investors, should the SEC require additional disclosure on these matters by revising its forms and regulations? Alternatively, should the SEC highlight how its current forms and regulations may require disclosure in these areas?



Some members of the committee indicated that traditional reporting and accounting do not capture many important issues. Broadening disclosure to more meaningfully include ESG considerations would better reflect the real value of an issuer and the risks that it faces.

In a speech at the 48th Annual Corporate Counsel Institute on October 2, 2009, SEC Commissioner Elisse Walter indicated that the agency is taking a serious look at its disclosure system with respect to climate change disclosure. She stated that it is time for the SEC to consider issuing interpretive guidance regarding disclosure in this area. She noted that even without further guidance, this is one area where if she were drafting disclosure for a registrant today, she would “carefully consider whether that company’s particular facts and circumstances raise any disclosure obligations under the current rules...”.

The SEC's interest in this disclosure has been welcomed by the investor community, which has sought regulatory action in this area for several years.

b. Europe

The European Commission (EC) is planning to review corporate disclosure of ESG information. Between September 2009 and March 2010, the EC plans to hold a series of five workshops to:

- identify the most effective and efficient ways to promote a better and more widespread disclosure of ESG information
- facilitate better co-ordination and communication among existing initiatives in the field of ESG disclosure, and
- deepen the understanding of all stakeholders, including the EC, of the issues, recent developments and current good practice.

The EC’s Directorate-General for Enterprise and Industry is leading this initiative. The workshops will involve separate consultations with:

- public companies
- investors, financial analysts, accountants and rating agencies
- civil society and NGOs
- trade unions, and
- public authorities.



The conclusions of these workshops will be discussed during a conference to be organized by the Spanish Presidency in March 2010, and at a plenary meeting of the European Multistakeholder Forum on CSR in the second half of 2010 or early 2011.

In late 2009, the EC intends to contract a consultant to carry out a study of current CSR reporting practices, which will build on the outcomes of the workshops.

In April 2009, the European Social Investment Forum (Eurosif) issued a public policy position paper on sustainable and responsible investment for a roundtable discussion on sustainability disclosure hosted by the European Parliament. In the paper, Eurosif recommends mandating disclosure of ESG information by large, publicly traded companies and suggests using existing reporting initiatives (such as the GRI and CDP) and sector-specific key performance indicators to amend existing regulation. Eurosif further recommends that the European Commission coordinate collaboration among different stakeholders and initiatives to reach a common ground.





2. Background information on ESG disclosure

- 2.1 Role of ESG information in investment decision-making
- 2.2 Materiality of ESG information

2. Background information on ESG disclosure

2.1 Role of ESG information in investment decision-making

Incorporating ESG into investment process

Increasingly, investors appear to be taking ESG matters into account when making decisions regarding investments and proxy voting.

For example, in 2005, the former UN Secretary General Kofi Annan founded the UN Principles for Responsible Investment (the PRI). The principles were developed in response to a growing view among investment professionals that ESG issues can affect the performance of investment portfolios and that investors fulfilling their fiduciary (or equivalent) duty therefore need to give appropriate consideration to these issues, but to date have lacked a framework for doing so. The principles were designed to provide this framework. The PRI reflect the core values of large investors whose investment horizon is generally long, and whose portfolios are often highly diversified. However, the PRI are open to all institutional investors, investment managers and professional service partners to support.

By becoming signatories to the PRI, institutional investors endorse the following statement:

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society.

In particular, signatories pledge to incorporate ESG issues into investment analysis and decision-making processes, and to seek appropriate disclosure on ESG issues by the entities in which they invest.

According to the 2009 PRI Annual Report, there are 538 signatories to the PRI, based in 36 countries and with total assets under management of US\$18 trillion. The signatories fall into three main categories: asset owners, investment managers and professional service partners. Eighty-five per cent of signatories have policies that make reference to responsible investment or ESG issues and 63% of asset owners now include responsible investment or ESG elements in contractual relationships with external managers.



The paper published by the CFA Institute in 2008, “*Environmental, Social and Governance Factors at Listed Companies: A Manual for Investors*”, states that:

A growing number of investors (such as those committed to the PRI and other initiatives) have begun to focus on ESG factors to arrive at a more thorough understanding of the risks and opportunities that face the companies in which they invest. These investors share the view that a prudent investor ought to consider ESG issues in his or her analysis because these factors can have an impact on investment performance.

The paper notes that a number of investment banks already have employed dedicated “ESG teams” to evaluate ESG issues and incorporate them into the larger equity analysis process, and consulting firms have recently enhanced their ESG competencies to meet the growing demand from their pension fund clients for consideration of ESG matters. The paper also states that clients with long-term horizons will often require that their investment managers take into account issues that have a long-term impact on valuations, including ESG factors.

Consistent with the PRI and the increased focus on ESG factors, investors have sought enhanced disclosure of ESG matters through petitions to regulators, questionnaires sent to issuers and shareholder proposals or resolutions. See section 3.2 *Investor needs* below for more information.

Fiduciary duty

Fiduciary duties are the key source of limits on the discretion of investment decision-makers in common law jurisdictions. Increased consideration of ESG matters by institutional investors is supported by the law of fiduciary duty.

For example, the Asset Management Working Group (AMWG) of the United Nations Environment Programme Finance Initiative (UNEP Finance Initiative) commissioned Freshfields Bruckhaus Deringer (Freshfields), a leading international law firm, to answer the following question: Is the integration of environmental, social and governance issues into investment policy (including asset allocation, portfolio construction and stock-picking or bond-picking) voluntarily permitted, legally required or hampered by law and regulation; primarily as regards public and private pension funds, secondarily as regards insurance company reserves and mutual funds?

Freshfields reviewed nine jurisdictions (Australia, Canada, France, Germany, Italy, Japan, Spain, U.K. and U.S.). In October 2005, it published the report, “*A legal framework for the integration of environmental, social and governance issues into institutional investment*” for the AMWG. In the report, Freshfields



concluded that integrating ESG considerations into an investment analysis so as to more reliably predict financial performance is clearly permissible and is arguably required in all jurisdictions.

In July 2009, UNEP Finance Initiative’s AMWG issued the report, “*Fiduciary responsibility – Legal and practical aspects of integrating social and governance issues into institutional investment*”. In the report, recognized fiduciary law expert Paul Watchman, Chief Executive of Quayle Watchman Consulting and principal author of the Freshfields report, articulates the evolving nature of fiduciary duties and ESG issues. Quayle Watchman Consulting clarifies that institutional investment consultants and asset managers have a professional duty of care to proactively raise ESG considerations with their clients and cautions that failure to do so may have serious consequences:

In tendering for investment mandates, it would be expected that the investment consultant or asset manager would raise ESG considerations as an issue to be taken into account and discussed with the client even if the pension fund had not specified ESG considerations as material to the tender. If the investment consultant or asset manager fails to do so, there is a very real risk that they will be sued for negligence on the ground that they failed to discharge their professional duty of care to the client by failing to raise and take into account ESG considerations.

As professional investment advisers, investment consultants and asset managers are under a contract for services rather than a contract of service. They are professional advisers to the client, not employees of the client; hence in exercising significant professional discretion ... investment consultants and asset managers must be proactive rather than reactive.

2.2 Materiality of ESG information

Definition of “material”

There are three primary definitions of “material”.

a. *Securities Act* (Ontario)

Under the *Securities Act* (Ontario), material fact and material change are defined with reference to a market impact test.

A “material fact”, when used in relation to securities issued or proposed to be issued, means a fact that would reasonably be expected to have a significant effect on the market price or value of the securities.



A “material change” is defined (for an issuer other than an investment fund) as:

- a change in the business, operations or capital of the issuer that would reasonably be expected to have a significant effect on the market price or value of any of the securities of the issuer, or
- a decision to implement such a change made by the board of directors of the issuer or other persons acting in a similar capacity, or by senior management of the issuer who believe that confirmation by the board of directors or other such persons acting in a similar capacity is probable.

b. Continuous disclosure documents

The test for “material” in continuous disclosure documents is based on a reasonable investor test. For example, in Form 51-102F1 *Management’s Discussion & Analysis* (MD&A Form) and Form 51-102F2 *Annual Information Form* (AIF Form), issuers are directed to focus on “material information”. They are not required to disclose information that is not material. The forms indicate that information is likely material if a reasonable investor’s decision whether or not to buy, sell or hold securities in an issuer would likely be influenced or changed if the information in question was omitted or misstated.

Some view the reasonable investor test as broader than the market impact test discussed above.

c. Voluntary reporting frameworks

“Materiality” is more broadly defined under voluntary corporate sustainability reporting frameworks. For example, under the GRI, “material information” covers topics and indicators that reflect the organization’s significant economic, environmental and social impacts, or that would substantively influence the assessments and decisions of stakeholders.

Examples of materiality of ESG information

There is evidence to support the contention that information relating to performance on ESG issues is material:

a. UNEP 2004 report

UNEP Finance Initiative’s AMWG commissioned 11 reports from nine major stock brokerage houses. The analysts were requested to identify specific environmental and social criteria likely to be material to an issuer’s competitiveness and reputation in seven industry sectors, and to the extent possible, to quantify their potential impact on stock price. The findings were published in the June 2004 report, “*The Materiality of Social, Environmental and Corporate Governance Issues to Equity Pricing*”. The report states that analysts agreed that ESG criteria impact both positively and negatively on long-term shareholder value. In some cases, these effects may be profound.

For example, Deutsche Bank AG's April 2004 report, "*Beyond the Numbers – Corporate Governance: Implication for Investors*" found investments in issuers with the highest quality of governance structures and behaviour have significantly outperformed those with the weakest governance. The following is a summary of the key findings:

- The report examined two portfolios of S&P 500 securities: (1) securities of companies with an above average corporate governance assessment and positive momentum regarding changes to their corporate governance standards and (2) securities of companies with a below average corporate governance assessment and negative momentum regarding changes to their corporate governance standards. The first portfolio made up of companies with above average corporate governance assessment outperformed the other portfolio over a two-year period in terms of share price, with a performance differential spread between the portfolios of 18.9%. Similar results were found with FTSE 350 companies.
- The report examined the FTSE 350 to determine the corporate governance impacts on profitability. It found a positive relationship between historic corporate governance assessment and return on equity (ROE) across the entire FTSE 350. In addition, companies with the top 20% of governance scores had an average 2002 ROE of 15.9%, while companies within the bottom 20% had an average 2002 ROE of 1.5%. Similar results were found using return on assets and earnings before interest, taxes, depreciation and amortization (EBITDA) margin measures.
- The report also compared volatility (using equity price 180-day volatility) to its corporate governance assessment of companies in the S&P 500 and FTSE 350. The report found that the higher the corporate governance score, the lower the volatility, with the trend line showing a negative slope.
- The report did not find a clear relationship for the aggregate S&P 500 or FTSE 300 companies between corporate governance and equity valuations. However, a few individual sectors showed some positive relationships.

Not all of the analyst reports cited, however, found a link between good corporate citizenship and share price. For example, Deutsche Securities' January 2004 report, "*No evidence to link share ratings with good corporate citizenship ... yet*" was unable to conclude that there is a link between shares' ratings and the level of compliance with good corporate citizenship. The report examined the apparel-retail sector in South Africa over a five-year period. Despite this finding, the report states that "[o]ver the longer term, we believe that share ratings, and hence share price performance will be strongly influenced by good corporate citizenship".



The AMWG report also notes that innovative techniques are being developed to perform financial analyses of ESG criteria in response to growing investor demand. Most of the analysts' reports and AMWG members agree that it would be easier to conduct a financial analysis of these criteria if governments, through their financial regulators, clarified and/or enforced existing financial disclosure regulations and standards, or developed new ones to specifically include disclosure of these criteria where they have been shown to be material.

b. UN Global Compact 2004 report

In December 2004, The UN Global Compact published the report, *"Who Cares Wins: Connecting Financial Markets to a Changing World"*. The report was endorsed by 23 financial institutions with more than US\$6 trillion under management. The report states:

The institutions endorsing this report are convinced that in a more globalised, interconnected and competitive world the way that environmental, social and corporate governance issues are managed is part of companies' overall management quality needed to compete successfully. Companies that perform better with regard to these issues can increase shareholder value by, for example, properly managing risks, anticipating regulatory action or accessing new markets, while at the same time contributing to the sustainable development of the societies in which they operate. Moreover, these issues can have a strong impact on reputation and brands, an increasingly important part of company value.

In reaching this conclusion, the report notes the following:

- In the January 2004 survey by the World Economic Forum's Corporate Citizenship Initiative, 70% of the chief executive officers and chief financial officers of the companies surveyed "expect to see increased interest in ESG issues by mainstream investors in the future".
- In a 2003 survey by Cap Gemini Ernst & Young, 81% of Global 500 executives rated environmental, health and safety issues among the top ten factors driving value in their businesses. Similarly, in a survey by CSR Europe, Deloitte and Euronext, 40% of interviewed fund managers and analysts, and over 50% of investor relations officers, confirmed that intangible aspects significantly contribute to value creation. Seventy-eight per cent of the fund managers, analysts and investor relations officers surveyed also believed that the management of environmental and social risk has a positive impact on an issuer's long-term market value. However, only 32% believed this to be the case for a shorter time horizon (3 to 12 months).



- In a February 2004 study by the Association of British Insurers, 90% of the pension trustees surveyed said their investment strategy took into account social, environmental and ethical (SEE) factors, and 87% of them indicated they exercise voting rights on SEE grounds.

The report invites regulators to shape legal frameworks to support integration of ESG issues in financial analysis. It states that “regulatory frameworks should require a minimum degree of disclosure and accountability on environmental, social and governance issues from companies, as this will support financial analysis. The formulation of specific standards should, on the other hand, rely on market-driven voluntary initiatives.”

c. UNEP 2006 report

In 2006, UNEP Finance Initiative’s AMWG launched its second materiality report, “*Show Me The Money: Linking Environmental, Social and Governance Issues to Company Value*”. The report provides strong independent support for the view that effective attention to ESG issues will enhance shareholder value. The AMWG requested 10 sell-side brokerage houses to write reports across various sectors and matters of relevance. The report identifies three key findings:

1. There is robust evidence that ESG issues affect shareholder value in both the short and long term. The report states that over the course of three years of research, analysts “presented significant evidence of the positive and negative impacts environmental, social and governance issues can have on share price across multiple sectors”.
2. The impact of ESG issues on share price can be valued and quantified. The report notes that of the analysts’ research provided for the project, nine reports had evidence of a link to materiality, of which six were quantified.
3. Key material ESG issues are becoming apparent, and their importance can vary between sectors. Several common themes were identified, including the importance of:
 - public policy and regulation in determining materiality
 - brand and reputation as emerging categories of risk (particularly to issuers whose primary exposure is directly to consumers)
 - global supply chains and the ability to manage outsourcing and supply chain risk
 - ageing workforces, pension obligations and healthcare costs, and
 - corporate governance.



The report concludes that investors and asset managers can manage risk better if they consider ESG issues and can potentially increase profits if they incorporate ESG issues into investment decisions.

d. UNEP 2007 report

In October 2007, UNEP Finance Initiative's AMWG and Mercer published a joint report, "*Demystifying Responsible Investment Performance*", which reviews key academic and broker research on ESG factors.

In summarizing its academic review, the report states:

Environmental factors: There are two studies of note that measure the impact of environmental factors on portfolio performance. Derwall et al. (2005) found that the benefits of considering environmental criteria in the investment process can be substantial and are statistically significant. Van de Velde et al. (2005) also found that companies with high sustainability ratings tend to have a positive impact on alpha, although sustainable portfolios were found to be highly sensitive to style biases. ...

Corporate governance factors: The academic evidence evaluating the impact of good corporate governance on a company and portfolio performance suggests that there is a positive relationship between the two, although it is not always straightforward to demonstrate this statistically or to isolate the effects from other 'factors'. The study by Gompers et al. (2003) concluded that good corporate governance was strongly correlated with stock returns during the 1990s. Opler & Sokobin (1995) also found that coordinated shareholder activism is effective in bolstering returns; with Smith (1996) reporting that when activism is successful in changing a company's governance structure, then it can result in a significant increase in shareholder wealth.

When discussing the results of these academic studies, the AMWG and Mercer joint report states:

- **The eco-efficiency premium puzzle, Derwall et al. (2005)**. Overall, the portfolio constructed of environmentally efficient stocks was found to produce superior returns to the portfolio of low-ranked environmental stocks. The authors conclude that environmentally responsible investment provides benefits. The return difference was found to be 3.05% p.a. under the Capital Asset Pricing Model (CAPM)¹ framework, although this difference was not statistically significant. The multi-factor model results showed a 5.06% p.a. difference in returns that was significant at the 10% level, but not the 5% level. After adjusting for industry tilt, size and style effects, the results were more robust and significant at the 5% level, with a 6.04% p.a. difference in alpha.



- **Corporate social responsibility and financial performance, Van de Velde et al. (2005).** The authors conclude that although the alpha results were not found to be statistically significant, the effect of the sustainable rating was found to have a positive impact on alpha over the sample period. ... On a style-unadjusted basis, the results showed the lowest scoring portfolio of stocks had the highest performance, although the results were insignificant. After adjusting for style, the results flipped and showed that the best performing portfolio is the 'good' portfolio with a monthly outperformance of 20bp, whereas the 'bad' and 'worst' portfolios underperformed by 34bp and 19bp, respectively. The alpha results were insignificant after adjustment.
- **Corporate governance and equity prices, Gompers et al. (2003).** This study examines the association between stock market performance and corporate governance policies. A Governance index (G-index) is created – the level of which gives a measure of the extent to which a company's corporate governance policies favour management or shareholders (a high G-index indicating weaker shareholder rights and lower governance quality). The authors conduct various tests on this G-index and conclude the following: corporate governance was strongly correlated with stock returns during the 1990s; however, the evidence is inconclusive as to the cause of this correlation.
- **Does coordinated institutional activism work? An analysis of the activities of the Council of Institutional Investors, Opler & Sokobin (1995).** The authors set out to examine whether coordinated and primarily 'quiet' governance activism generated value by examining the activities of the Council of Institutional Investors (CII). Specifically, they investigate whether firms that appear on the CII focus list experience improvements in performance in subsequent years. The study involves the construction of a benchmark portfolio that takes size, book-to-market ratio and industry performance into account. The authors find that firms on the CII focus list exhibited depressed performance in the three years prior to inclusion in the list, and significant improvements in performance in the following years. ... The stock market performance of firms on the CII focus list in the year following its listing showed at least 10% higher returns than the S&P 500. Over the full sample period, the CII portfolio exhibited a mean return of 21.2% in the year after listing compared to the market return of 9.5%. The mean one-year stock market performance was found to be two times greater than the long-term performance matched portfolio (5.3%), and five times greater than the book-to-market matched portfolio (2.2%).
- **Shareholder activism by institutional investors: Evidence from CalPERS, Smith (1996).** This study examines the benefits of shareholder activism through a case study of CalPERS' actions via the focus fund list. ... *"On net, activism appears to be beneficial to CalPERS on a net of costs basis, as the value increase of its holdings from activism is almost US\$ 19 million over the 1987-93 period (for the*



34 firms with sufficient data), while its estimated costs of activism over the same period were approximately US\$ 3.5 million (US\$ 500,000 per year)."

The AMWG and Mercer joint report also summarizes its review of broker studies. It highlights that, "in most cases, quantitative analysis resulted in an assumed positive influence of 'good citizenship' on the overall economic performance of a company". The report further states:

While brokers usually measure ex post that 'good' companies have an above average performance, it is still very difficult to find a clear link between share price volatility, the ability to generate cash flow, or sales growth on one hand; and good human resource management, use of efficient environmental management systems, or the ability to mitigate climate change risks on the other hand. This is not surprising – ESG factors have not yet been analysed long enough and in sufficient detail to allow greater comparability and to identify more distinct linkages with traditional financial criteria. Moreover, ESG factors have not yet been fully taken into account and priced in by many investors.

Consultation questions

1. Is information about environmental and corporate governance matters material?
2. How should materiality be defined in this context?
3. Should the threshold for including disclosure of environmental and corporate governance matters in regulatory filings be materiality?
4. Is the concept of materiality shifting as we move to a carbon-constrained economy?





3. Environmental disclosure

- 3.1 Scope of environmental matters
- 3.2 Survey of environmental disclosure requirements
- 3.3 Needs of investors and other users
- 3.4 Issuer's ability to provide information
- 3.5 Adequacy of disclosure and compliance
- 3.6 Need for regulatory action

3. Environmental disclosure

3.1 Scope of environmental matters

Environmental matters can include a broad range of issues, such as climate change, conservation, biodiversity, land degradation, nanomaterials, resource depletion, toxins and waste. As noted in the Canadian Institute of Chartered Accountants' (CICA) briefing, "*Climate Change Briefing – Questions for Directors to Ask*" published in July 2009, environmental and climate change risks that may impact an issuer's business and operations can be divided generally into four categories: physical, regulatory, reputation and litigation. Examples of each of these types of risks include:

Physical

- increased frequency of extreme weather events
- changes in air and ocean temperature, and sea levels
- availability of water
- contamination and remediation/clean-up costs
- disposal of hazardous waste
- resource depletion

Regulatory

- costs to comply with existing or pending government regulations such as:
 - greenhouse gas (GHG) emissions limits and trading systems
 - other instruments, such as carbon taxes, building codes, environmental permits and energy efficiency standards

Reputational

- reputational risks that may influence key stakeholders (e.g. customers, employees, suppliers, governments, communities) arising from an issuer's handling of climate change and environmental issues, and

Litigation

- pending nuisance, negligence, disclosure, regulatory compliance, or other legal actions against the issuer arising from its actions or inactions relating to the environment and climate change.



3.2 Survey of environmental disclosure requirements

Requirements under securities legislation

The existing Canadian requirements for environmental disclosure under securities legislation are set out in the MD&A Form and the AIF Form, and are reproduced in Appendix A. From our review of the environmental disclosure requirements in other jurisdictions, existing Canadian requirements are in some respects comparable to those in other jurisdictions (Australia, South Africa, the U.K. and the U.S.). In particular, Canadian and U.S. requirements are very similar. However, as discussed below, investors and investor groups in the U.S. have repeatedly petitioned the SEC to enhance, and issue guidance on, existing climate change disclosure requirements.

The environmental disclosure requirements in Australia and the U.K. take a principles-based approach to reporting and have more general requirements regarding environmental reporting rather than detailed, prescriptive requirements. Certain large issuers in those jurisdictions appear to be interpreting the requirements broadly and are providing greater detail in their environmental disclosure than some of their Canadian counterparts, often basing their disclosure on voluntary CSR reporting frameworks such as the GRI. This may be due to a number of factors, including the existence of a GHG emissions cap and trade regime in Europe and the greater acceptance of CSR reporting in the corporate culture.

The following is a high-level summary of the environmental disclosure requirements under securities legislation of various jurisdictions:

- **Canada.** As noted above, the disclosure requirements are set out in the MD&A Form and the AIF Form. Issuers should discuss in their management's discussion & analysis (MD&A), among other things:
 - material information that may not be fully reflected in the financial statements, such as contingent liabilities or contractual obligations, and
 - important trends and risks that have affected the financial statements, and trends and risks that are reasonably likely to affect them in the future.

An issuer's annual information form (AIF) is generally intended to:

- provide material information about the issuer and its business at a point in time in the context of its historical and possible future development, and
- describe the issuer, its operations and prospects, risks and other external factors that impact the issuer specifically.



In the AIF, an issuer must disclose risk factors relating to the issuer and its business, including, among others, environmental and health risks, regulatory constraints, and any other matter that would be most likely to influence an investor's decision to purchase securities of the issuer. In addition, the issuer must describe the financial and operational effects of environmental protection requirements on the capital expenditures, earnings and competitive position of the issuer in the current financial year and the expected effect in future years. If an issuer has implemented social or environmental policies that are fundamental to its operations, such as policies regarding the issuer's relationship with the environment or with the communities in which it does business, the issuer must describe the policies and the steps it has taken to implement them.

- **Australia.** The disclosure requirements are found in the *Corporations Act 2001*, the Australian Securities Exchange (ASX) Listing Rules and the ASX's Corporate Governance Principles and Recommendations. An issuer is required to prepare a directors' report for each financial year that:
 - gives details of any matter or circumstance that has arisen since the end of the year that has significantly affected, or may significantly affect the issuer's operations or results of operations in future financial years or the issuer's state of affairs in future financial years, and
 - refers to likely developments in the issuer's operations in future financial years and the expected results of those operations.

If an issuer's operations are subject to any particular and significant environmental regulation under a law of the Commonwealth or of a State or Territory, the issuer must provide details of the issuer's performance in relation to environmental regulation.

The term "significant" is not explicitly defined in the *Corporations Act 2001*. The Australian Securities and Investment Commission (ASIC) determined that "significant" does not necessarily mean "material". However, ASIC did not provide a definition of "significant".

An issuer must also either adopt policies for the oversight and management of material business risks, which may include environmental and sustainability risks, or explain why it has not done so in its corporate governance statement in its annual report. A summary of any policies on risk oversight and management of material business risks adopted by the issuer should be made publicly available, ideally by posting it to the issuer's website.

- **South Africa.** In February 2009, the King Committee on Governance released the draft *Code of Governance Principles for South Africa – 2009* and the draft *Report on Governance for South Africa –*



2009 (together referred to as the King III Code) for public comment. The final King III Code was published in September 2009 and will come into effect on March 1, 2010.

The King III Code states, among other things, that the board should ensure that an issuer acts as, and is seen to be, a responsible corporate citizen. The issuer as a good corporate citizen should protect, enhance and invest in the wellbeing of society and the natural ecology. Corporate citizenship and sustainability require business decision makers to adopt a holistic approach to economic, social and environmental issues in their core business strategy. As a result, the board is not only responsible for the issuer's financial bottom line, but for the issuer's performance in respect of its "triple bottom line".

The King III Code further states that effective communication with stakeholders is essential. Effective reporting means proactive and transparent communication and engagement with stakeholders on all material matters affecting the issuer, including economic, social and environmental issues.

Sustainability reporting should be focused on substance over form and should transparently disclose information that is material, relevant, accessible, understandable and comparable with past performance of the issuer. Successful issuers recognize that the principle of transparency in reporting sustainability (commonly but incorrectly referred to as "non-financial") information is a critical element of effective reporting. The key consideration is whether the information provided has allowed stakeholders to understand the key issues affecting the issuer and any positive or negative effects the issuer's operation has had on the economic, social and environmental wellbeing of the community.

Effective reporting should take place at least once a year. While the King III Code does not mandate specific content in a report, it refers to international and local guidance materials, including the GRI. It also recommends that sustainability reporting and disclosure should have independent assurance.

Under the Johannesburg Stock Exchange listing requirements, an issuer is required to disclose in its annual report:

- a narrative statement of how it has applied the principles set out in the King Code, providing explanations that enable its shareholders to evaluate how the principles have been applied, and
- a statement addressing the extent of the issuer's compliance with the King Code and the reasons for non-compliance with any of the principles in the King Code, specifying whether or not the issuer has complied throughout the accounting period with all the provisions of the King Code, and indicating for what part of the period any non-compliance occurred.



- **U.K.** The disclosure requirements are found in the business review of the director's report in the *Companies Act 2006*. Subject to exceptions for small companies, a directors' report must contain a business review, the purpose of which is to inform members of the issuer and help them assess how the directors have performed their statutory duty to promote the success of the issuer.

The business review must contain a fair review of the issuer's business and a description of the principal risks and uncertainties facing the issuer. In addition, in the case of a quoted issuer, the business review must, to the extent necessary for an understanding of the development, performance or position of the issuer's business, include:

- the main trends and factors likely to affect the future development, performance and position of the issuer's business
- information about environmental matters (including the impact of the issuer's business on the environment)
- information about any policies of the issuer in relation to those matters and the effectiveness of those policies, and
- analysis using financial key performance indicators, and where appropriate, analysis using other key performance indicators, including information relating to environmental matters.

"Key performance indicators" means factors by reference to which the development, performance or position of the issuer's business can be measured effectively.

- **U.S.** The disclosure requirements are found in Regulation S-K. An issuer's MD&A must describe:
 - any unusual or infrequent events or transactions or any significant economic changes that materially affected the amount of reported income from continuing operations and, in each case, the extent to which income was so affected
 - any other significant components of revenues or expenses that, in the issuer's judgment, should be described in order to understand the issuer's results of operations, and
 - any known trends or uncertainties that have had or that the issuer reasonably expects will have a material favourable or unfavourable impact on net sales or revenues or income from continuing operations.

An issuer is required to make appropriate disclosure about the material effects that compliance with federal, state and local provisions that have been enacted or adopted regulating the discharge of materials into the environment, or otherwise relate to the protection of the environment, may have on the capital expenditures, earnings and competitive position of the issuer and its subsidiaries. It must



also disclose information about any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the issuer or any of its subsidiaries is a party or of which any of their property is the subject. This may include material claims relating to the environment. In particular, this disclosure requirement extends to administrative or judicial proceedings arising under any federal, state and local provisions that have been enacted or adopted regulating the discharge of materials into the environment, or otherwise relate to the protection of the environment, where the proceeding is material to the issuer's business or financial condition, or certain other thresholds are met.

An issuer is also required to disclose any material estimated capital expenditures for environmental control facilities for the remainder of its current fiscal year and its succeeding fiscal year and for such further periods as the issuer may deem material.

The term "material" limits the information required to those matters to which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to buy or sell the securities registered.

Mandatory CSR reporting frameworks

Canadian disclosure requirements appear to be less stringent when compared to certain mandatory CSR reporting frameworks. For example, in Denmark, listed issuers in nine high-polluting sectors (including iron and steel, processing, oil and gas, chemicals, animal processing and power generation) must publish stand-alone environmental reports known as "Green Accounts" on an annual basis. The main disclosure elements of a Green Account are an issuer's consumption of energy, water and raw materials, as well as its polluting emissions and waste handling.

On December 16, 2008, the Danish Parliament adopted the proposed "*Act amending the Danish Financial Statements Act (Report on social responsibility for large businesses)*" (the Danish Act). Under the Danish Act, large Danish issuers must include information on their CSR policies and practices in their annual reports. Issuers covered by the statutory requirement must report on:

- their policies on CSR, including any standards, guidelines or principles
- how their CSR policies are being implemented, including any systems or procedures used, and
- their achievements resulting from CSR work during the financial year, and any related future implications for the business.



There is no obligation for issuers to have a CSR policy. Issuers that do not have a CSR policy must report this in the management review, but do not have to provide an explanation.

In France, listed issuers are required to report on environmental performance in their financial statements. A number of specific aspects must be included in the review of environmental impacts contained in the director's report, including an issuer's resource use, emissions, expenditure and management action on environmental protection measures.

Voluntary CSR reporting frameworks

Canadian disclosure requirements appear to be less detailed than the disclosure guidelines under voluntary CSR reporting frameworks. For example, under the GRI and CDP, issuers are asked to disclose major opportunities stemming from environmental/climate change matters, and how responsibility for environmental/climate change matters is managed within the organization.

The GRI requests disclosure of direct and indirect GHG emissions, as well as management's approach to specific environmental aspects, including water, biodiversity, waste and energy. The CDP questionnaire also incorporates disclosure of direct and indirect GHG emissions and energy consumption.

Consultation questions

5. Are existing Canadian environmental disclosure requirements adequate?
6. Should the existing Canadian environmental disclosure requirements be expanded to incorporate requirements in other jurisdictions or disclosure items in voluntary CSR frameworks (e.g. GHG emissions, governance of environmental matters, more detailed disclosure of climate change risks)?
7. Do issuers fully understand the scope of the existing Canadian environmental disclosure requirements?
8. Is additional guidance needed on how existing Canadian environmental disclosure requirements apply to climate change?

3.3 Needs of investors and other users

Requests for disclosure by investors

Investors appear to be demanding enhanced disclosure of environmental matters through a number of avenues.

- **Requests for guidance from SEC.** In the U.S., investors and investor groups have repeatedly called on the SEC to address climate change disclosure in issuers' mandatory public filings. In September 2007, a broad coalition of investors, environmental groups, state officials, pension fund managers and others petitioned the SEC to provide interpretative guidance on climate risk disclosure and examine the adequacy of registrants' climate risk disclosure. Since September 2007, investors and others have continued to press the SEC through petitions and letters.

Similarly, some members of U.S. Congress have also expressed the need for the SEC to address climate change risks in mandatory public filings. In December 2007, Senator Christopher Dodd, Chairman of the Committee on Banking, Housing and Urban Affairs, and Senator Jack Reed, Chairman of the Subcommittee on Securities Insurance and Investment, wrote a letter to the SEC requesting that the SEC issue interpretive guidance clarifying what existing regulations require with respect to climate change disclosure.

The SEC recently announced that it is reviewing climate change disclosure and is meeting with experts in the area to discuss the issue.

- **Requests for information from issuers.** Investors have been requesting information about climate change directly from issuers. The CDP is the largest investor coalition in the world and includes more than 475 signatory investors with assets under management of US\$55 trillion. The investors reflect a wide range of institutions, including banks, fund managers, pension funds, socially responsible investors and insurance companies. They sign an annual request for information, which is sent to the chair of the board of each of the world's largest companies by market capitalization. The request for information covers four main areas: management's views on the risks and opportunities related to climate change, GHG emissions accounting, management's strategy to reduce emissions/minimize risk and capitalize on opportunity, and corporate governance with regard to climate change.
- **Shareholder proposals.** Investors are also making their desire for enhanced environmental disclosure known through shareholder resolutions. According to the Shareholder Resolution Database maintained by the Shareholder Association for Research and Education, in the 2009 annual general



meeting year, 12 of the 101 shareholder proposals and resolutions filed with Canadian issuers related to environmental matters. They covered topics such as the monitoring of GHG emissions, participation in the CDP and reporting on the effect of, or exposure to risks relating to, climate change.

Requests for enhanced disclosure by regulators

Regulators have sought enhanced disclosure of environmental matters in public filings. For example, the New York Attorney General, Andrew Cuomo, is seeking to compel certain companies in the energy industry to disclose their climate change risks and carbon dioxide emissions. Relying on the New York State securities statute, Cuomo subpoenaed five publicly traded companies in September 2007, demanding additional information relevant to their analysis of climate change risks in connection with their business and the disclosure of those risks to investors.

In 2008, two of those companies, Xcel Energy Inc. and Dynegy Inc., signed settlement agreements with the New York Attorney General, under which each company agreed to provide more detailed climate change disclosure in their 2008 annual filings with the SEC. In November 2009, the New York Attorney General reached a similar agreement with The AES Corporation. The New York Attorney General's inquiries into the other two companies are reportedly ongoing.

In March 2009, the U.S. National Association of Insurance Commissioners (NAIC) announced the adoption of a mandatory requirement that insurance companies disclose to regulators the financial risks they face from climate change, as well as actions the companies are taking to respond to those risks. All insurance companies with annual premiums of \$500 million or more will be required to complete an Insurer Climate Risk Disclosure Survey every year, with an initial reporting deadline of May 1, 2010. They are required to report on:

- how they are altering their risk management and catastrophe risk modeling in light of the challenges posed by climate change
- the steps they are taking to engage and educate policymakers and policyholders on the risks of climate change, and
- whether and how they are changing their investment strategies.

Use of information by investors

Studies have shown that investors are factoring environmental matters, particularly climate change, into their investment decisions. In March 2009, the CDP published the results of a survey on investor use of CDP data. Eighty CDP signatory investors responded to the survey, including asset managers, pension funds, insurers and socially responsible investment funds. Seventy-seven per cent of respondents indicated that they factor climate change information into their investment decisions and asset allocations.



Of these, more than 80% indicated that climate change is a very or somewhat important factor. They mentioned using corporate climate change policies as an indicator in an assessment of an issuer's overall approach to risk management. The survey also found a general consensus among respondents that the materiality of climate change has been increasing over time and will continue to do so.

Consultation questions

9. What information do investors need about environmental matters to make investment or voting decisions?
10. How do investors incorporate this information into their decision-making?
11. Should this information be set out in regulatory filings or is it sufficient for investors to ask issuers for this information directly?

3.4 Issuers' ability to provide information

Challenges for information collection and dissemination

Issuers would need to familiarize themselves with any additional disclosure requirements and determine whether they have adequate information management and data collection systems in place to provide this information in a reliable and timely manner. We have been advised that environmental/sustainability reporting and financial reporting functions are often not integrated within issuers, and it may take years for an issuer to establish an effective environmental information management system. Boards of directors or committees of the board that approve financial statements and MD&A may require training or external assistance to review disclosure of these matters.

If issuers are able to generate this information, they may be hesitant to include it in public filings in light of civil liability for secondary market disclosures. Financial statements, MD&A and AIFs are "core documents" under the regime for civil liability for secondary market disclosure set out in the *Securities Act* (Ontario).

In addition, issuers may be reluctant to provide this information directly to investors through initiatives such as the CDP questionnaire. We understand that some issuers are concerned that doing so may constitute selective disclosure, which is prohibited under the *Securities Act* (Ontario).

Ability to estimate environmental liabilities

a. Estimations of liabilities by issuers

The study, *“Bridging the Credibility Gap – Eight Corporate Liability Accounting Loopholes that Regulators Must Close”*, released in June 2009 by the Investor Environmental Health Network (IEHN), found that as “a result of weak regulations, issuers do not assess, quantify or disclose potential and pending liabilities on a timely basis,” making it difficult for investors and analysts “to use existing disclosures for a realistic evaluation of many companies”. The study examines, among other things, the disclosure made by issuers bankrupted by asbestos liabilities. For example, the last quarterly report filed with the SEC by Johns-Manville Corporation prior to its 1982 bankruptcy implied a total cost of settling asbestos-related claims of approximately US\$350 million. On filing for bankruptcy, the issuer estimated that amount to be approximately US\$2 billion.

The study concludes that the “truth is that for companies facing substantial litigation or other pending liabilities, undisclosed and underestimated future losses can be so large as to swamp the remaining disclosed indicators of share-holder value”. In the view of the authors, the current regulatory framework favours reliability over relevance by “encouraging and allowing companies to estimate and disclose only information that is relatively certain”. They also note that issuers may be concerned about disclosing information beyond that is required by regulations if it may weaken their position in pending or future litigation.

b. Impact of IFRS

Following a period of public consultation, the Canadian Accounting Standards Board adopted a strategic plan to move financial reporting for Canadian publicly accountable enterprises to International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). For financial years beginning on or after January 1, 2011, Canadian generally accepted accounting principles (GAAP) for publicly accountable enterprises will be IFRS incorporated into the CICA Handbook.

The changeover to IFRS from existing Canadian GAAP may have a significant impact to financial reporting and other business activities of reporting issuers. IFRS contain some important differences from Canadian GAAP for recognition and measurement of provisions, including environmental provisions. Four of the key differences are summarized below.

- **When a provision exists.** A provision exists under Canadian GAAP if there is a legal obligation arising from past transactions or events, whereas a provision exists under IFRS if there is a legal or constructive obligation as a result of a past event. A constructive obligation arises when an entity creates a valid expectation to other parties that it will discharge certain responsibilities based on an



established pattern of past practice, published policies or indicated to other parties that it will accept certain responsibilities.

- **Recognition threshold.** The recognition threshold for provisions is lower under IFRS. To recognize a provision under Canadian GAAP, it must be “likely to occur” and “the chance of occurrence is high” but to recognize a provision under IFRS, the provision must be “probable” or “more likely than not to occur”. Although it is difficult to quantify the difference, “likely to occur” has been interpreted as a higher threshold than “probable” and could potentially lead to more provisions being recognized on the face of the financial statements, rather than simply being disclosed as a contingent liability in the notes to the financial statements.
- **Amount to be accrued.** When measuring provisions, Canadian GAAP allows issuers to accrue provisions at the low end of the range of estimates when no outcome is more likely than the others. Under IFRS, the mid-point of the range is used to measure the provision when no outcome is more likely than others. This could potentially lead to provisions being accrued at higher amounts under IFRS.
- **Note disclosure requirements.** In addition, IFRS disclosure requirements of provisions and contingent liabilities will be significant compared to current Canadian GAAP disclosure requirements. Under IFRS, issuers will be required to disclose a provision continuity schedule for each class of provision, disclosing the beginning and ending carrying amounts, additional provisions made in the period, amounts used in the period, unused amounts reversed during the period and changes resulting from the passage of time and any revisions to the discount rate. Issuers will also have to disclose a description of the nature of the obligation, the expected timing of any resulting outflows or economic benefits and an indication of the uncertainties about the amount or timing of those outflows and where necessary, they will have to disclose the major assumptions made concerning future events.

As a result of these four factors, under IFRS, issuers may potentially be required to accrue more environmental liabilities, at higher amounts, and provide more disclosure regarding these liabilities.

Corporate governance implications

National Policy 58-201 *Corporate Governance Guidelines* provides guidance on corporate governance practices, which have been formulated to achieve a balance between providing protection to investors and fostering fair and efficient capital markets and confidence in capital markets. Issuers are encouraged to consider the guidelines in developing their own corporate governance practices, which may include the management of environmental matters.



National Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings* requires certifying officers to certify, among other things, that the issuer's financial statements and the other financial information included in the issuer's MD&A and AIF, if applicable, fairly present, in all material respects, the issuer's financial condition. We are of the view that meaningful discussion of material environmental matters, where applicable, in an issuer's MD&A and AIF is important to achieve fair presentation of the issuer's financial condition in all material respects.

In addition, certifying officers must certify that they have designed:

- disclosure controls and procedures, which are generally defined as controls and other procedures of the issuer that are designed to provide reasonable assurance that information required to be disclosed by the issuer in its filings is recorded, processed, summarized and reported within the time periods specified, including controls and procedures designed to ensure that information required to be disclosed by the issuer in its filings is accumulated and communicated to the issuer's management to allow timely decisions regarding required disclosure, and
- internal control over financial reporting, which is generally defined as a process to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with the applicable accounting principles.

National Instrument 52-110 *Audit Committees* requires an audit committee to review an issuer's financial statements and MD&A before the issuer publicly discloses this information. The audit committee must also be satisfied that adequate procedures are in place for the review of the issuer's public disclosure of financial information extracted or derived from the issuer's financial statements, and must periodically assess the adequacy of these procedures. We are of the view that the audit committee's oversight of financial reporting related to material environmental matters, where applicable, in continuous disclosure documents is an important aspect of meeting these responsibilities.



Consultation questions

12. What are the challenges to issuers in providing information about environmental matters (including estimates of environmental liabilities)?
13. Do issuers have information management and data collection systems in place to provide this information?
14. Would the ability to provide this information vary by an issuer's size, stage of development and industry?
15. Are there liability concerns with providing this information (i.e. issues relating to selective disclosure and secondary market civil liability)?
16. How do boards and management determine whether material environmental matters are being disclosed?
17. Do issuers have the corporate governance procedures in place to enable:
 - a. boards to approve environmental information set out in financial statements and MD&A, and
 - b. certifying officers to certify environmental information set out in financial statements, MD&A and AIFs?

3.5 Adequacy of disclosure and compliance

Canada

In 2007, OSC staff reviewed the filings of 35 reporting issuers based in Ontario to assess compliance with the existing disclosure requirements regarding environmental matters. Staff focused on the adequacy of disclosure of matters such as financial liabilities related to the environment, asset retirement obligations, financial and operational effects of environmental protection requirements, environmental policies and environmental risks.

The results of our review are set out in OSC Staff Notice 51-716 *Environmental Reporting*, which was published on February 27, 2008. Staff found several areas of deficient disclosure. The information provided by issuers was often boilerplate and did not provide meaningful information to investors. The staff notice provided guidance for issuers to consider when preparing their continuous disclosure documents and was intended to be used by issuers as an educational tool to enhance their disclosure.

On October 14, 2009, a coalition of Canadian investors and environmental groups (British Columbia Investment Management Corporation, Ceres, Climate Action Network Canada and Climate Change Lawyers Network) called on the OSC to pursue several actions aimed at increasing mandatory disclosure of climate change related risks in securities filings as part of the OSC's initiative on corporate sustainability reporting.

In their submission to the OSC, the signatories include a survey of disclosure in 2008 annual reports by 35 reporting issuers in Ontario in nine industry sectors with market capitalization of at least CDN \$1 billion. The survey found that the disclosure contained poor or limited descriptions of climate change risks, if the issue is discussed at all. The signatories recommend that the OSC work with the CSA to provide guidance to issuers on how to disclose climate change risks within the context of present reporting obligations. The signatories also encouraged the OSC to improve corporate governance disclosure of how issuers are addressing their climate change risk at board and management levels.

U.S.

The report, "*Reclaiming Transparency in a Changing Climate: Trends in Climate Risk Disclosure by the S&P 500 from 1995 to the Present*" by the Center for Energy and Environmental Security, Ceres and the Environmental Defense Fund released in June 2009 found that useful climate risk disclosure in SEC filings is scarce. A review was conducted of more than 6,000 SEC filings of S&P 500 companies between 1995 and 2008. The review found that in 2008, 76.3% of the companies surveyed did not mention climate change in their reports and only 5.5% of annual reports filed by these companies laid out a strategy for managing climate risks. The report concludes that the failure to mention climate risk by the large majority of S&P 500 companies demonstrates the fundamental failure to implement securities law and underscores the need for action by the SEC to secure transparent and accountable climate risk disclosure, and to provide guidance to clarify proper climate disclosure practices.

Similarly, the June 2009 report, "*Climate Risk Disclosure in SEC Filings*" prepared by The Corporate Library for Ceres and the Environmental Defense Fund assesses climate risk disclosure in Forms 10-K and 20-F reports filed in 2008 by 100 global companies in five sectors: electric utilities, coal, oil and gas, transportation and insurance. The report assesses company filings in three main categories: emissions and climate change position, risk assessment and actions to address climate risk and opportunities. The report

found limited disclosure. Fifty-nine of the 100 companies made no mention of their GHG or public position on climate, 28 had no discussion of climate-related risks they face and 52 failed to disclose actions and strategies for addressing climate-related business challenges.

3.6 Need for regulatory action

Disclosure of environmental matters in Canada appears to be more limited than in other jurisdictions and investors appear to want enhanced disclosure of environmental matters in order to make investment decisions. We are considering whether regulatory action is warranted.

Consultation questions

18. What is the role of the securities regulator in this area?
19. Does disclosure of environmental matters in Canada need to be improved? If so, what is the best approach to improving disclosure of environmental matters:
 - a. making existing disclosure requirements more explicit,
 - b. providing more guidance to issuers on the types of disclosures they are required to provide through staff notices or educational seminars,
 - c. conducting more extensive reviews of disclosure of environmental matters, and/or
 - d. allowing the private sector to address the issue?



4. Corporate governance disclosure

- 4.1 Scope of corporate governance matters
- 4.2 Survey of corporate governance disclosure requirements
- 4.3 Disclosure model
- 4.4 Subject matter
- 4.5 Distinction between venture and TSX-listed issuers
- 4.6 Adequacy of disclosure and compliance
- 4.7 Need for regulatory action

4. Corporate governance disclosure

4.1 Scope of corporate governance matters

When referring to corporate governance, we generally mean board governance, which includes the set of rules, relationships, systems and processes that directs and controls the actions of issuers, and the mechanisms for holding issuers, its board of directors and management accountable.

For the purpose of this paper, we are not including shareholder communications and shareholder rights within the scope of corporate governance matters. Shareholder rights, including rights to advisory votes on executive compensation and matters such as majority voting, and shareholder communications will be dealt with as separate initiatives.

4.2 Overview of corporate governance regimes

International regimes

The following is a summary of the corporate governance regimes in Canada and certain other international jurisdictions:

- **Canada.** In April 2005, the CSA published in final form National Policy 58-201 *Corporate Governance Guidelines* (NP 58-201) and a related disclosure rule, National Instrument 58-101 *Disclosure of Corporate Governance Practices* (NI 58-101). These instruments came into force on June 30, 2005.

NP 58-201 applies to all issuers other than investment funds and provides non-prescriptive guidance on corporate governance practices. The corporate governance policy sets out 18 guidelines including, including guidelines for board composition and independence requirements, director responsibilities, the constitution and responsibilities of supervisory board committees for the nomination and remuneration of directors, and codes of business conduct and ethics.

NI 58-101 requires issuers to disclose their corporate governance practices and file their code of business conduct and ethics. TSX-listed issuers must disclose their corporate governance practices generally with reference to the guidelines in NP 58-201 or explain any departures or other practices used. Venture issuers, on the other hand, are only required to disclose their corporate governance practices in areas addressed by the guidelines. The existing Canadian disclosure requirements for corporate governance disclosure under securities legislation are reproduced in Appendix A. Based on our research, Canadian corporate governance disclosure requirements are comparable in many respects to those in other jurisdictions (Australia, South Africa and the U.K.).



On September 28, 2007, the CSA announced its review of the existing corporate governance regime, and on December 19, 2008, published for comment a proposal for a new corporate governance regime, including a new disclosure regime (the Proposal). The Proposal contemplated, among other things, replacing the existing “comply or explain” disclosure model with more general disclosure requirements and adding disclosure requirements in areas not addressed by the existing regime. The CSA received 57 written submissions on the Proposal, which are available on the OSC’s website.¹

- Australia.** In March 2003, the ASX Corporate Governance Council released ASX Corporate Governance Principles (the ASX Principles), identifying 10 core principles for effective corporate governance and 28 best practice guidelines. The ASX Principles are guidelines and are not intended to be prescriptive. Under the ASX listing rules, issuers are required to include a statement in their annual report disclosing the extent to which they have followed the best practice recommendations during the reporting period and give reasons for any alternative approaches. In other words, ‘if not, why not?’

The ASX Principles were updated in 2007 and came into effect January 1, 2008. The core principles for effective corporate governance include the composition and responsibilities of the board and management, the promotion of ethical and responsible decision making, safeguarding the integrity of financial reporting and timely disclosure, risk oversight and management, respecting the rights of shareholders, ensuring remuneration is reasonable, and recognizing legal and other obligations to all legitimate stakeholders.

- Denmark.** The Report on Corporate Governance in Denmark (the Report) prepared by the Copenhagen Stock Exchange Committee on Corporate Governance (the Committee) was adopted in December 2003 following the publication of the *The Nørby Committee’s Report on Corporate Governance in Denmark – Recommendations for Corporate Governance in Denmark* in December 2001.

¹ On November 13, 2009, the CSA publicly announced that they would not be proceeding with the Proposal. The CSA received numerous comments about the timing of the Proposal. A majority of commenters expressed the view that now is not an appropriate time to introduce significant changes to the corporate governance regime in Canada. Commenters pointed out that issuers are currently focused on business sustainability issues in a challenging economic climate, and on the transition to International Financial Reporting Standards. Based on the comments received, the CSA do not intend to implement the Proposal as originally published. The CSA concluded that now is not an appropriate time to recommend significant changes to the corporate governance regime. The CSA are reconsidering whether to recommend any changes to the corporate governance regime, and will publish any proposed changes for comment.

The Copenhagen Stock Exchange recommends that issuers address corporate governance as reflected in the recommendations in their annual reports. This may be a summary or contain an indication of the extent to which the issuer follows the recommendations and a statement or the reason for any use of other principles or for deviations.

The recommendations cover the role of the shareholders and their interaction with the management of the issuer, the role of the stakeholders and their importance to the issuer, the composition, tasks and responsibilities of the board, remuneration to the directors and the managers, and risk management.

- **South Africa.** Corporate governance in South Africa was institutionalized by the publication of the *King Report on Corporate Governance* in November 1994. As noted above, in February 2009, the King Committee on Governance released the draft King III Code for public comment. The final King III Code was published in September 2009 and will come into effect on March 1, 2010.

The principles and practices under the King III Code are based on an 'apply or explain' approach. If a board believes a practice not to be in the best interest of the issuer, it can adopt a practice different from that recommended in the code, but it must be able to explain the reason for its decision. It is recommended that all issuers disclose which principles and/or practices they have decided not to apply and explain why.

In contrast to earlier versions of the code, the King III Code applies to all issuers regardless of the manner and form of incorporation or establishment. The philosophy of the King III Code revolves around leadership, sustainability and corporate citizenship. The principles are drafted on the basis that, if they are adhered to, an issuer will have practiced good governance. The King III Code will cover board and director responsibilities, corporate citizenship, leadership, integrity and responsibility, audit committees, risk management, internal audit, integrated sustainability reporting and disclosure, compliance with laws, regulations, rules and standards, managing stakeholder relationships, and director responsibilities and duties in regard to mergers, acquisitions and amalgamations.

- **U.K.** The Financial Reporting Council (the FRC) is responsible for maintaining the Combined Code on Corporate Governance (the Combined Code) and promoting its application. The Combined Code contains broad principles and more specific provisions. Listed issuers are required to report on how they have applied the main principles of the Combined Code, and either to confirm that they have complied with the Combined Code's provisions or to provide an explanation if they have not complied. The Combined Code sets out standards of good practice in relation to issues such as board composition, development and independence, remuneration, accountability and audit, and relations with shareholders.



All issuers incorporated in the U.K. and listed on the Main Market of the London Stock Exchange are required under the listing rules to report on how they have applied the Combined Code in their annual report and accounts. Foreign issuers listed on the Main Market are required to disclose the significant ways in which their corporate governance practices differ from those set out in the Combined Code.

In March 2009, the FRC announced a review of the impact and effectiveness of the Combined Code and invited public comment. The FRC also published a progress report in July 2009 and expects to publish a final report later this year.

- **U.S.** The U.S. government responded to the crisis in confidence resulting from the large scale corporate collapses in 2001 by adopting the *Sarbanes-Oxley Act of 2002* (SOX), which focuses primarily on governance practices affecting financial reporting. SOX seeks to protect investors by improving the accuracy and reliability of corporate disclosure and reporting.

Other U.S. organizations also took a number of other initiatives. Among them, the New York Stock Exchange (NYSE) implemented prescriptive listing requirements that focused on corporate governance issues beyond financial reporting. Issuers listed on the exchange must comply with certain standards regarding corporate governance, including independence requirements for members of the board of directors, constitution and independence requirements for supervisory board committees, corporate governance policies and procedures, and codes of business conduct and ethics. Listed foreign private issuers must disclose any significant ways in which their corporate governance practices differ from those followed by domestic issuers under NYSE listing standards.

Voluntary CSR reporting frameworks

Under the GRI, disclosure requirements regarding corporate governance matters include, among others, disclosure of the composition, independence, and qualifications of board members, processes to deal with conflicts of interest, risk management processes, and performance regarding sustainability issues.

The CDP also seeks disclosure regarding corporate governance matters, such as overall responsibility for climate change, management of climate change issues including achieving GHG targets, communicating information about risks and opportunities presented by climate change, and whether the organization is engaged with policy makers in climate change issues.

4.3 Disclosure model

In Canada, TSX-listed issuers are subject to a “comply or explain” disclosure model, an approach that aims to provide sufficient flexibility to issuers while also providing investors with the information they need. In



recognition of their smaller size and more limited resources, venture issuers follow a more general, less stringent reporting regime. The corporate governance disclosure requirements in other jurisdictions generally operate under some form of a “comply or explain” disclosure regime.

The Proposal contemplated replacing the existing disclosure requirements based on a “comply or explain” disclosure model with more general disclosure requirements. The intention was to respond to concerns that the existing corporate governance guidelines are often perceived by market participants as obligatory practices or minimum requirements, given that they are coupled with a “comply or explain” disclosure model.

Approximately 30 of the commenters support the existing “comply or explain” disclosure model and question whether the proposed disclosure regime would result in better disclosure. They are concerned that moving away from a “comply or explain” disclosure model would affect comparability among issuers because there would not be a benchmark against which to evaluate issuers’ corporate governance practices.

In addition, some commenters believe that a “comply or explain” disclosure model encourages issuers to apply rigour to the development of their corporate governance practices. Without the model, some issuers may gravitate toward minimal corporate governance practices. Some commenters think that a regime based on “best practices” coupled with a “comply or explain” disclosure model is less costly for issuers.

In contrast, approximately 13 commenters support a disclosure model based on discretionary reporting as contemplated in a principles-based approach.

Consultation questions

20. What is the objective or purpose of corporate governance disclosure (i.e. to change corporate behaviour or enhance transparency)?
21. How do investors use information relating to corporate governance?
22. What are the relative merits of a principles-based approach for disclosure, compared to a “comply or explain” model? Which model would provide better disclosure for investors? Which model would issuers prefer?

4.4 Subject matter

From our review of the corporate governance disclosure requirements in other jurisdictions, existing Canadian requirements are comparable in many respects to those found in Australia, South Africa, and the U.K. These three jurisdictions all apply some form of a “comply or explain” model similar to Canada, and their corporate governance disclosure regimes incorporate recommendations or principles on issues found in the Canadian framework, such as the independence of board directors and the mandate of the board. However, some jurisdictions require certain disclosure relating to risk management and shareholder engagement that is not required under the Canadian framework.

In the U.K., issuers are required to describe the main features of the internal control and risk management systems in relation to the financial reporting process. Similarly, in Australia, it is recommended that issuers establish policies for the oversight and management of material business risks and disclose a summary of those policies. If they do not do so, they are required to provide an explanation. In South Africa, the King III Code states that the board of directors should report on the effectiveness of risk management, and sets out the components of that report.

Australia, the U.K. and South Africa have principles or recommendations relating to shareholder engagement. In the U.K., the board of directors should state in the annual report the steps it has taken to ensure that board members, and in particular the non-executive directors, develop an understanding of the views of major shareholders about their issuer, for example through direct face-to-face contact, analysts' or brokers' briefings and surveys of shareholder opinion. Furthermore, the board should use the annual general meeting to communicate with investors and to encourage their participation. For each resolution, proxy appointment forms should provide shareholders with the option to direct their proxy to vote either for or against the resolution or to withhold their vote.

The Proposal contemplated seeking disclosure regarding the following areas not addressed by the existing disclosure requirements:

- information regarding the fees paid to compensation consultants or advisors, if any have assisted the board of directors or the compensation committee
- a summary of any policies on risk oversight and management adopted by the issuer
- information on corporate governance practices used to identify, assess and resolve significant conflicts of interest, including information about ad hoc committees appointed to address such conflicts and consultants or advisors, if any have assisted the board of directors or a committee

- information on any practices or policies that are related to the shareholder voting process or that promote a voting process that is understandable, transparent and robust, and that facilitate the board of directors obtaining meaningful information on shareholder views, and
- a description of how directors of an issuer are elected, including if the issuer has adopted a majority or plurality voting standard.

While approximately 20 commenters on the Proposal suggested maintaining the existing corporate governance regime, several of those commenters suggested supplementing the existing regime by addressing the following areas: the recognition and management of conflicts of interest and risk, and effective engagement with shareholders. In their view, these areas provide additional useful information to investors.

Consultation questions

23. Are existing Canadian corporate governance disclosure requirements adequate?
24. Should disclosure include information in areas found in the reporting regimes of other jurisdictions, such as risk management and shareholder engagement?

4.5 Distinction between venture and TSX-listed issuers

As noted above, in recognition of their smaller size and more limited resources, venture issuers currently are subject to a more general, less stringent reporting regime.

The Proposal did not contemplate an alternate disclosure regime for venture issuers because the proposed disclosure requirements were not based on a “comply or explain” disclosure model. The CSA recognizes that venture issuers may be smaller issuers with less formal procedures in place to ensure effective corporate governance. As a result, in developing NI 58-101, the CSA decided that a “comply or explain” disclosure model was not appropriate for these issuers.

Approximately 13 commenters believe that venture issuers should be subject to the same disclosure requirements relating to their corporate governance practices as TSX-listed issuers. In contrast, approximately 10 commenters believe in proportionate regulation and do not agree that venture issuers should be subject to the same disclosure requirements as TSX-listed issuers. Approximately four commenters think that the existing disclosure approach is appropriate for venture issuers.

Consultation question

25. Should there continue to be different corporate governance disclosure standards for venture issuers?

4.6 Adequacy of disclosure and compliance

In 2007, CSA staff reviewed the corporate governance disclosure of 65 TSX-listed issuers and 35 venture issuers. The purpose of the review was to assess compliance with the disclosure requirements in NI 58-101, and in particular, to review the substance of the disclosure to assess whether the quality was sufficient to provide a clear and complete account of an issuer's corporate governance practices.

The results of the review are summarized in CSA Staff Notice 58-303 *Corporate Governance Disclosure Compliance Review*, published on June 29, 2007. Overall, significant deficiencies in each category of disclosure were identified.

Form 58-101F1 *Corporate Governance Disclosure* requires a TSX-listed issuer to disclose its corporate governance practices in eight categories. The table below sets out the average response rate for the required disclosure in each category.

Category of disclosure in Form 58-101F1	Response rate
Board independence	94%
Board mandate	77%
Position descriptions	70%
Orientation and continuing education	85%
Ethical business conduct	86%
Nomination of directors	82%
Compensation	80%
Assessments	85%

It is more difficult to discern the response rate for venture issuers given that Form 58-101F2 *Corporate Governance Disclosure (Venture Issuers)* generally requires disclosure if particular corporate governance practices are implemented, and does not require a "negative response".

The response rates do not necessarily reflect the quality of the disclosure. For example, several issuers disclosed summarized information that was insufficient for a reader to fully understand how the board exercises independent supervision over management and how the board delineates its roles and responsibilities. In some instances, it was not clear how the board satisfies itself that the board, its committees and individual directors are performing effectively. Finally, in describing the process by which the board identifies new candidates for board nomination, several issuers provided vague and uninformative disclosure. Some issuers merely disclosed that the board fills vacancies with required skill sets, without further elaboration.

As a result of the review, 27 TSX-listed issuers and nine venture issuers were required to address deficiencies in their next management information circular or AIF. In addition, two venture issuers were required to refile their management information circulars because they failed to provide any corporate governance disclosure.

Consultation question

26. What are the challenges to issuers in providing this information?

4.7 Need for regulatory action

Some believe that the existing Canadian corporate governance disclosure requirements are adequate, while others think that the requirements are inadequate and/or the extent and quality of disclosure of corporate governance matters in Canada could be improved. We are considering whether regulatory action is warranted.



Consultation questions

27. What is the role of the securities regulator in this area?
28. Does disclosure of corporate governance matters in Canada need to be improved? If so, what is the best approach to improving disclosure of corporate governance matters:
- a. expand the existing disclosure requirements (and the related guidance on corporate governance practices),
 - b. providing more guidance to issuers on the types of disclosures they are required to provide through staff notices or educational seminars,
 - c. conducting more extensive reviews of disclosure of corporate governance matters, and/or
 - d. allowing the private sector to address the issue?



5. Questions or comments

5. Questions or comments

If you have any questions or comments, please contact any of:

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Appendix A – Existing Canadian environmental disclosure requirements

Appendix A - Existing Canadian environmental disclosure requirements

Form 51-102F1 Management's Discussion & Analysis

Trends and uncertainties

(Part 1(a))

MD&A is a narrative explanation, through the eyes of management, of how your company performed during the period covered by the financial statements, and of your company's financial condition and future prospects.

MD&A should, among other things, discuss: (i) material information that may not be fully reflected in the financial statements, such as contingent liabilities or other contractual obligations; and (ii) important trends and risks that have affected the financial statements, and trends and risks that are reasonably likely to affect them in the future. ...

(Item 1.4(g))

Discuss your analysis of your company's operations for the most recently completed financial year, including ...

- (g) commitments, events, risks or uncertainties that you reasonably believe will materially affect your company's future performance including net sales, total revenue and income or loss before discontinued operations and extraordinary items; ...

Results of operations and significant projects that have not yet generated operating revenue

(Item 1.4(d))

Discuss your analysis of your company's operations for the most recently completed financial year, including ...

- (d) for issuers that have significant projects that have not yet generated operating revenue, describe each project, including your company's plan for the project and the status of the project relative to that plan, expenditures made and how these relate to anticipated timing and costs to take the project to the next stage of the project plan;

Your discussion under paragraph 1.4(d) should include

- (i) *whether or not you plan to expend additional funds on the project; and*
- (ii) *any factors that have affected the value of the project(s) such as change in commodity prices, land use or political or environmental issues.*



Liabilities and accounting estimates

(Item 1.12)

If your company is not a venture issuer, provide an analysis of your company's critical accounting estimates.

Your analysis should

- (a) identify and describe each critical accounting estimate used by your company, including:
 - (i) a description of the accounting estimate;
 - (ii) the methodology used in determining the critical accounting estimate;
 - (iii) the assumptions underlying the accounting estimate that relate to matters highly uncertain at the time the estimate was made;
 - (iv) any known trends, commitments, events or uncertainties that you reasonably believe will materially affect the methodology or assumptions described; and
 - (v) if applicable, why the accounting estimate is reasonably likely to change from period to period and have a material impact on the financial presentation;
- (b) explain the significance of the accounting estimate to your company's financial condition, changes in financial condition and results of operations and identify the financial statement line items affected by the accounting estimate;
- (c) [repealed]
- (d) discuss changes made to critical accounting estimates during the past two financial years, including the reasons for the change and the quantitative effect on your company's overall financial performance and financial statement line items; and
- (e) identify the segments of your company's business that the accounting estimate affects and discuss the accounting estimate on a segment basis, if your company operates in more than one segment.

Instructions

(i) *An accounting estimate is a critical accounting estimate only if*

(A) it requires your company to make assumptions about matters that are highly uncertain at the time the accounting estimate is made; and

(B) different estimates that your company could have used in the current period, or changes in the accounting estimate that are reasonably likely to occur from period to period, would have a material impact on your company's financial condition, changes in financial condition or results of operations.

(ii) As part of your description of each critical accounting estimate, in addition to qualitative disclosure, you should provide quantitative disclosure when quantitative information is reasonably available and would provide material information for investors. Similarly, in your discussion of assumptions underlying an accounting estimate that relates to matters highly uncertain at the time the estimate was made, you should provide quantitative disclosure when it is reasonably available and it would provide material information for investors. For example, quantitative information may include a sensitivity analysis or disclosure of the upper and lower ends of the range of estimates from which the recorded estimate was selected.

Asset retirement obligations

(Item 1.2)

Provide an analysis of your company's financial condition, results of operations and cash flows. Discuss known trends, demands, commitments, events or uncertainties that are reasonably likely to have an effect on your company's business. ...

(Item 1.6)

Provide an analysis of your company's liquidity, including ...

Instructions

(iv) In discussing your company's balance sheet conditions or income or cash flow items you should present a summary, in tabular form, of contractual obligations including payments due for each of the next five years and thereafter. The summary and table do not have to be provided if your company is a venture issuer. An example of a table that can be adapted to your company's particular circumstances follows:



<i>Payments Due by Period</i>					
<i>Contractual Obligations</i>	<i>Total</i>	<i>Less than 1 year</i>	<i>1-3 years</i>	<i>4-5 years</i>	<i>After 5 years</i>
<i>Long Term Debt</i>					
<i>Capital Lease Obligations</i>					
<i>Operating Leases</i>					
<i>Purchase Obligations¹</i>					
<i>Other Long Term Obligations²</i>					
<i>Total Contractual Obligations</i>					

Notes:

- ¹ “Purchase Obligation” means an agreement to purchase goods or services that is enforceable and legally binding on your company that specifies all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction.
- ² “Other Long Term Obligations” means other long-term liabilities reflected on your company’s balance sheet.

The tabular presentation may be accompanied by footnotes to describe provisions that create, increase or accelerate obligations, or other details to the extent necessary for an understanding of the timing and amount of your company’s specified contractual obligations.

Form 51-102F2 Annual Information Form

Trends and uncertainties

(Part 1(a))

An AIF is a disclosure document intended to provide material information about your company and its business at a point in time in the context of its historical and possible future development. Your AIF describes your company, its operations and prospects, risks and other external factors that impact your company specifically.

Risk factors

(Item 5.2)

Disclose risk factors relating to your company and its business, such as cash flow and liquidity problems, if any, experience of management, the general risks inherent in the business carried on by your company, environmental and health risks, reliance on key personnel, regulatory constraints, economic or political conditions and financial history and any other matter that would be most likely to influence an investor's decision to purchase securities of your company. If there is a risk that securityholders of your company may become liable to make an additional contribution beyond the price of the security, disclose that risk.

Environmental protection requirements (including discharge into environment)

(Item 5.1(1)(k))

Describe the business of your company and its operating segments that are reporting segments as those terms are used in the Handbook. For each reportable segment include: ... the financial and operational effects of environmental protection requirements on the capital expenditures, earnings and competitive position of your company in the current financial year and the expected effect in future years.

Environmental policies

(Item 5.1(4))

If your company has implemented social or environmental policies that are fundamental to your operations, such as policies regarding your company's relationship with the environment or with the communities in which it does business, or human rights policies, describe them and the steps your company has taken to implement them.





Appendix B – Existing Canadian corporate governance disclosure requirements

Appendix B - Existing Canadian corporate governance disclosure requirements

Form 58-101F1 Corporate Governance Disclosure

1. Board of Directors

- (a) Disclose the identity of directors who are independent.
- (b) Disclose the identity of directors who are not independent, and describe the basis for that determination.
- (c) Disclose whether or not a majority of directors are independent. If a majority of directors are not independent, describe what the board of directors (the *board*) does to facilitate its exercise of independent judgement in carrying out its responsibilities.
- (d) If a director is presently a director of any other issuer that is a reporting issuer (or the equivalent) in a jurisdiction or a foreign jurisdiction, identify both the director and the other issuer.
- (e) Disclose whether or not the independent directors hold regularly scheduled meetings at which non-independent directors and members of management are not in attendance. If the independent directors hold such meetings, disclose the number of meetings held since the beginning of the issuer's most recently completed financial year. If the independent directors do not hold such meetings, describe what the board does to facilitate open and candid discussion among its independent directors.
- (f) Disclose whether or not the chair of the board is an independent director. If the board has a chair or lead director who is an independent director, disclose the identity of the independent chair or lead director, and describe his or her role and responsibilities. If the board has neither a chair that is independent nor a lead director that is independent, describe what the board does to provide leadership for its independent directors.
- (g) Disclose the attendance record of each director for all board meetings held since the beginning of the issuer's most recently completed financial year.



2. Board Mandate

Disclose the text of the board's written mandate. If the board does not have a written mandate, describe how the board delineates its role and responsibilities.

3. Position Descriptions

- (a) Disclose whether or not the board has developed written position descriptions for the chair and the chair of each board committee. If the board has not developed written position descriptions for the chair and/or the chair of each board committee, briefly describe how the board delineates the role and responsibilities of each such position.

- (b) Disclose whether or not the board and CEO have developed a written position description for the CEO. If the board and CEO have not developed such a position description, briefly describe how the board delineates the role and responsibilities of the CEO.

4. Orientation and Continuing Education

- (a) Briefly describe what measures the board takes to orient new directors regarding
 - (i) the role of the board, its committees and its directors, and
 - (ii) the nature and operation of the issuer's business.

- (b) Briefly describe what measures, if any, the board takes to provide continuing education for its directors. If the board does not provide continuing education, describe how the board ensures that its directors maintain the skill and knowledge necessary to meet their obligations as directors.

5. Ethical Business Conduct

- (a) Disclose whether or not the board has adopted a written code for the directors, officers and employees. If the board has adopted a written code:
 - (i) disclose how a person or company may obtain a copy of the code;
 - (ii) describe how the board monitors compliance with its code, or if the board does not monitor compliance, explain whether and how the board satisfies itself regarding compliance with its code; and



- (iii) provide a cross-reference to any material change report filed since the beginning of the issuer's most recently completed financial year that pertains to any conduct of a director or executive officer that constitutes a departure from the code.
- (b) Describe any steps the board takes to ensure directors exercise independent judgement in considering transactions and agreements in respect of which a director or executive officer has a material interest.
- (c) Describe any other steps the board takes to encourage and promote a culture of ethical business conduct.

6. Nomination of Directors

- (a) Describe the process by which the board identifies new candidates for board nomination.
- (b) Disclose whether or not the board has a nominating committee composed entirely of independent directors. If the board does not have a nominating committee composed entirely of independent directors, describe what steps the board takes to encourage an objective nomination process.
- (c) If the board has a nominating committee, describe the responsibilities, powers and operation of the nominating committee.

7. Compensation

- (a) Describe the process by which the board determines the compensation for the issuer's directors and officers.
- (b) Disclose whether or not the board has a compensation committee composed entirely of independent directors. If the board does not have a compensation committee composed entirely of independent directors, describe what steps the board takes to ensure an objective process for determining such compensation.
- (c) If the board has a compensation committee, describe the responsibilities, powers and operation of the compensation committee.
- (d) If a compensation consultant or advisor has, at any time since the beginning of the issuer's most recently completed financial year, been retained to assist in determining



compensation for any of the issuer's directors and officers, disclose the identity of the consultant or advisor and briefly summarize the mandate for which they have been retained. If the consultant or advisor has been retained to perform any other work for the issuer, state that fact and briefly describe the nature of the work.

8. Other Board Committees

If the board has standing committees other than the audit, compensation and nominating committees, identify the committees and describe their function.

9. Assessments

Disclose whether or not the board, its committees and individual directors are regularly assessed with respect to their effectiveness and contribution. If assessments are regularly conducted, describe the process used for the assessments. If assessments are not regularly conducted, describe how the board satisfies itself that the board, its committees, and its individual directors are performing effectively.

INSTRUCTION:

(1) *This Form applies to both corporate and non-corporate entities. Reference to a particular corporate characteristic, such as a board, includes any equivalent characteristic of a non-corporate entity.*

Income trust issuers must provide disclosure in a manner which recognizes that certain functions of a corporate issuer, its board and its management may be performed by any or all of the trustees, the board or management of a subsidiary of the trust, or the board management or employees of a management company. In the case of an income trust, references to "the issuer" refer to both the trust and any underlying entities, including the operating entity.

(2) *If the disclosure required by Item 1 is included in a management information circular distributed to security holders of the issuer for the purpose of electing directors to the issuer's board of directors, provide disclosure regarding the existing directors and any proposed directors.*

(3) *Disclosure regarding board committees made under Item 8 of this Form may include the existence and summary content of any committee charter.*



Form 58-101F2 Corporate Governance Disclosure (Venture Issuers)

1. Board of Directors

Disclose how the board of directors (the board) facilitates its exercise of independent supervision over management, including

- (i) the identity of directors that are independent, and
- (ii) the identity of directors who are not independent, and the basis for that determination.

2. Directorships

If a director is presently a director of any other issuer that is a reporting issuer (or the equivalent) in a jurisdiction or a foreign jurisdiction, identify both the director and the other issuer.

3. Orientation and Continuing Education

Describe what steps, if any, the board takes to orient new board members, and describe any measures the board takes to provide continuing education for directors.

4. Ethical Business Conduct

Describe what steps, if any, the board takes to encourage and promote a culture of ethical business conduct.

5. Nomination of Directors

Disclose what steps, if any, are taken to identify new candidates for board nomination, including:

- (i) who identifies new candidates, and
- (ii) the process of identifying new candidates.

6. Compensation

Disclose what steps, if any, are taken to determine compensation for the directors and CEO, including:

- (i) who determines compensation, and
- (ii) the process of determining compensation.



7. Other Board Committees

If the board has standing committees other than the audit, compensation and nominating committees, identify the committees and describe their function.

8. Assessments

Disclose what steps, if any, that the board takes to satisfy itself that the board, its committees, and its individual directors are performing effectively.

INSTRUCTION:

- (1) *This form applies to both corporate and non-corporate entities. Reference to a particular corporate characteristic, such as a board, includes any equivalent characteristic of a non-corporate entity.*

Income trust issuers must provide disclosure in a manner which recognizes that certain functions of a corporate issuer, its board and its management may be performed by any or all of the trustees, the board or management of a subsidiary of the trust, or the board, management or employees of a management company. In the case of an income trust, references to “the issuer” refer to both the trust and any underlying entities, including the operating entity.

- (2) *If the disclosure required by Items 1 and 2 is included in a management information circular distributed to security holders of the issuer for the purpose of electing directors to the issuer’s board of directors, provide disclosure regarding the existing directors and any proposed directors.*
- (3) *Disclosure regarding board committees made under Item 7 of this Form may include the existence and summary content of any committee charter.*





ONTARIO
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OSC corporate sustainability reporting
initiative
Consultation paper



As the regulatory body responsible for overseeing the capital markets in Ontario, the Ontario Securities Commission administers and enforces the provincial Securities Act, the provincial Commodity Futures Act and administers certain provisions of the provincial Business Corporations Act. The OSC is a self-funded Crown corporation accountable to the Ontario Legislature through the Minister of Finance.



Schedule 2 – Summary of roundtable discussion held on September 18, 2009

Schedule 2 – Summary of roundtable discussion held on September 18, 2009

Moderators

The roundtable discussion was moderated by Edward Waitzer and Poonam Puri, Directors of the Hennick Centre for Business and Law at York University, which assisted the OSC with this consultation.

Objective of roundtable discussion

The objective of the roundtable discussion was to obtain feedback from participants on the adequacy of corporate governance and environmental disclosure by reporting issuers in Canada and the need to enhance disclosure of those matters, either through amendments to the disclosure requirements under securities legislation or through enhanced compliance with the existing requirements.

Summary of key points of roundtable discussion

ESG disclosure

Usefulness of ESG information

Based on external studies, surveys and consultations with institutional investors, participants generally agreed that environmental, social and governance (ESG) information is useful for investors, particularly those with a longer investment horizon. They acknowledged that there were many examples of investors taking ESG matters into consideration when making investment and proxy decisions. It was noted that a March 2009 report by the Canadian Financial Executives Research Foundation (CFERF) examined ESG disclosure from the perspective of stakeholders and supports the notion that investors are interested in ESG reporting.

Materiality of ESG disclosure

a. Definition of materiality

Currently, materiality is determined by a “reasonable investor” test. Information is likely material if a reasonable investor’s decision whether or not to buy, sell or hold securities in an issuer would likely be influenced or changed if the information in question was omitted or misstated.

One participant noted that there are two elements to the definition of materiality: (1) who is the information material to: current investors, prospective investors, the capital markets or a broader stakeholder group, which includes customers and suppliers, and (2) what time horizon should be considered.



Many participants agreed that the current definition is appropriate in the ESG context. However, one participant suggested that a lower materiality threshold could be adopted to broaden ESG disclosure. Investors would then be able to decide for themselves what information is material. Another participant similarly supported broader disclosure so that analysts could make the materiality determinations. A further participant believed that materiality should be determined, not just in reference to “reasonable investors”, but a broader stakeholder group. The participant noted that studies show that “best in class” issuers are responsive to all stakeholders, not simply investors.

One participant stated that, when considering the definition of materiality, it is important to balance the needs of investors with the desire to have efficient capital markets.

Certain participants recommended that the OSC provide guidance on the meaning of materiality in the ESG context to assist issuers in making materiality assessments.

b. Materiality of ESG disclosure

Participants generally agreed that ESG information may constitute material information, which is required to be disclosed in continuous disclosure documents filed under securities legislation.

Participants acknowledged that materiality of ESG information will vary among industries. For example, environmental issues are typically more relevant and material to the mining industry than the financial services industry. As a result, some participants do not believe that issuers in low risk industries should be required to provide the same level of disclosure as those in higher risk industries. Requiring issuers in low risk industries to do so would not provide meaningful information to investors and would result in higher compliance costs.

c. Materiality determinations

One participant thought issuers should be required to disclose the process used to determine materiality.

Some participants believed that it was important to consider the time perspective when assessing materiality. They felt that issuers should be reminded that they need to focus on the long-term, and not just on the short-term. An issue that may not be material in the short-term can be material in the long-term, and as a result, is relevant for investors with a longer investment horizon. In addition, an issue that is perceived to be a long-term issue can quickly become a short-term issue as the timeframe may be unknown. For example, some would argue that climate change has shifted from a long-term issue to a short-term one because the regulatory framework has changed more quickly than expected.



Similarly, some participants argued that materiality should be determined over a longer time horizon since environmental impact or damage is often incremental.

However, a participant expressed reservations about adopting a long-term view, noting that it may not result in useful disclosure. There must be a crystallization event or point. Otherwise, almost anything could be material and require disclosure. For example, there may be a risk of a meteorite striking the earth in the future. The participant questioned whether this event should be disclosed, given that there is no short-term risk.

Issues with disclosure of ESG information

Certain participants believed that both institutional and retail investors do not currently have access to a sufficient level of ESG information. They are seeking additional disclosure through mechanisms such as shareholder proposals and questionnaires.

In addition, while some ESG information is available, participants noted that there are often issues associated with it. The information is found in multiple sources, including both regulatory filings and voluntary reports. There is no coherent or consistent standard or framework for ESG reporting. The absence of a consistent standard for disclosure renders comparisons among issuers difficult. A participant also noted that it can be difficult for investors to find ESG information to use in making voting decisions. This issue could be resolved through the creation of universal standards and requirements. Requiring all issuers to adhere to consistent standards and requirements would also create a level playing field.

ESG disclosure requirements generally

Participants noted that ESG disclosure requirements can either be prescriptive or principles-based. Some participants acknowledged that prescriptive requirements would facilitate compliance. However, other participants expressed reservations about adopting a prescriptive approach as requirements may not be relevant to all issuers in all industries. Prescriptive requirements may also lead to issuers adopting a “check the box” approach to preparing disclosure.

Participants expressed concerns regarding the potential regulatory burden on issuers, especially smaller issuers. They argued that the OSC should use guidance and educational tools to assist issuers with their ESG disclosure, rather than impose prescriptive requirements.

One participant also noted that imposing prescriptive requirements may not address the issue of inadequate ESG disclosure given the current non-compliance with the existing requirements by some issuers.



A more detailed discussion of the disclosure requirements regarding environmental and corporate governance matters is set out below.

Environmental disclosure

Disclosure of environmental matters in regulatory filings

Participants noted that investors want to see disclosure of environmental matters in securities regulatory filings; however, they recognized that there is a tension between the relevance and reliability of environmental disclosure. Reliability of information is a concern given the complexity of environmental issues, the changing nature of the debate on these issues and the frequent use of models and assumptions by issuers. While environmental information may be relevant to an issuer and its investors, the information may not be reliable. One participant advocated the disclosure of relevant information even if there are questions regarding its reliability, provided that there is accompanying cautionary language or caveats.

A participant expressed concerns about mandating extensive environmental disclosure in securities regulatory filings. The participant did not support requiring issuers to comply with requirements that special interest groups may deem material, but are not considered necessary for investor protection by others. The participant questioned whether all investors are concerned with environmental matters, noting that investing involves a certain amount of risk. Certain investors may be willing to invest in issuers that have greater environmental risk, but which offer greater returns.

Nature and extent of environmental disclosure

a. Environmental disclosure as subset of sustainability disclosure

One participant suggested that the focus on environmental matters is too narrow and recommended disclosure on sustainability generally, rather than only environmental matters, be required. A participant indicated that this could be accomplished by allowing an issuer to refer to a sustainability report in its securities regulatory filings.

b. Key performance indicators

Several participants agreed that a sectoral or industry-specific approach to reporting would be useful. A participant noted that for each industry sector, there are a limited number of key performance indicators (KPIs) that would be material to an investment decision and should be disclosed. Another participant noted there are successful examples of implementing the use of metrics or KPIs as part of environmental disclosure. However, recognizing that different industries impact and interact with the environment in varying ways, several participants advocated allowing industries to select the most relevant metrics and information for them. It was



also suggested that the OSC develop a set of KPIs applicable to all issuers and then give issuers discretion in creating and reporting on additional KPIs that they believe are relevant to them.

There were different views on the feasibility of developing KPIs. Most participants believed that KPIs should be developed; however, a participant did not believe that KPIs are readily available for all industries. Even if KPIs could be easily developed, the participant questioned whether it was the OSC's role to dictate specific KPIs for an issuer.

c. Quantification of environmental disclosure

Some participants advocated quantification of environmental matters so that progress on these matters by issuers can be compared, charted and monitored over time. However, other participants noted that many environmental matters do not easily lend themselves to quantification. For example, it may be difficult to quantify an issuer's impact on biodiversity.

Costs and benefits associated with environmental disclosure

The participants acknowledged the importance of considering the costs and benefits associated with environmental disclosure. The majority of participants believed that the benefits associated with environmental disclosure outweigh the costs. These benefits include: enhancing investor protection, generating goodwill with society, reducing the cost of capital and insurance premiums, increasing access to markets, boosting employee morale and increasing the ease of entering new markets. One participant noted that damaging relationships with a broad range of stakeholders may have a negative impact on shareholder value, and as a result, disclosure of material matters relevant to these stakeholders is also important to investors.

One participant also suggested that the benefits of environmental disclosure should not be measured by examining the impact of environmental matters on share price performance, as it is currently difficult to link ESG matters to share price performance. The participant noted that earnings per share, a well-used financial measure, similarly is not a good indicator of share price.

Participants recognized that there are costs of compliance with disclosure requirements; however, once a disclosure and reporting system has been established, the ongoing costs should be minimal. In addition, the implementation of any disclosure system will enable issuers to satisfy other regulatory agencies and bodies that are seeking the same information.



Regulatory action

Participants generally thought the OSC should take regulatory action to enhance disclosure of environmental matters. Action by the OSC was considered necessary given that some issuers are resistant to providing this type of disclosure.

Many participants recommended that the OSC issue more guidance to issuers regarding the existing environmental disclosure requirements instead of developing new requirements. In their view, the OSC should not impose additional requirements simply because some issuers were not fully complying with existing requirements. In addition, they cautioned against requiring more disclosure than is needed by investors. The guidance should seek to standardize the presentation of environmental disclosure. Participants noted that a framework for disclosure is needed to result in consistent and complete disclosure.

While the general consensus of participants was that amendments to the existing disclosure requirements were not required, a few participants noted that developing prescriptive requirements for environmental disclosure might benefit small or venture issuers. Prescriptive requirements provide greater certainty to issuers regarding the nature and extent of the requirements, which in turn reduces compliance costs.

In addition, a few participants noted that enhancements to the existing disclosure requirements would be helpful. For example, one participant suggested requiring environmental disclosure to be included in one document, rather than dispersed in various regulatory and voluntary filings. In particular, the participant noted that many of the requirements are found in Form 51-102F2 *Annual Information Form*; however, the annual information form is not delivered to investors. As a result, the participant suggested moving these requirements, particularly the requirement to disclose risks, to Form 51-102F1 *Management's Discussion & Analysis*, so that the disclosure would be more accessible to investors.

Another participant suggested minor enhancements to the existing requirements. For example, Form 51-102F2 *Annual Information Form* requires disclosure of environmental policies that are fundamental to an issuer's operations, but there is no requirement to disclose whether these policies are effective.

In contrast, a few participants believed that the OSC should allow the marketplace to address concerns regarding environmental disclosure. They felt that larger issuers should take the lead in developing environmental disclosure standards, rather than having the OSC impose those standards on issuers.



Corporate governance disclosure

Objectives of corporate governance disclosure

Participants noted that the objectives of corporate governance disclosure include communicating with shareholders, changing corporate behaviour and enhancing transparency. A participant stated that corporate governance disclosure is a means to educate and inform investors about good corporate governance, which may motivate issuers to adopt better practices over the long-term.

One participant noted that issuers and their management generally want to be ranked well in private sector corporate governance rankings and surveys. These rankings and surveys often prompt issuers to improve their disclosure. A participant noted that, by having to disclose information regarding their corporate governance policies and practices, issuers are forced to review their performance and may improve their practices as a result.

Disclosure model

The majority of participants expressed their support for a “comply or explain” disclosure model over a principles-based disclosure model. One participant noted that smaller issuers prefer the “comply or explain” model mainly because it is the model that is currently in place and switching to a new regime would be costly.

TSX-listed issuers and venture issuers

Many participants felt that the distinction between the disclosure requirements applicable to TSX-listed issuers and those applicable to venture issuers is appropriate and should be maintained. One participant felt that the Canadian market is distinct from other markets given the large number of small issuers. That participant believed that venture issuers should not be subject to onerous disclosure requirements given their more limited resources. However, participants generally felt that venture issuers should not be exempt from all corporate governance disclosure requirements.

One participant argued that venture issuers should be subject to the same disclosure requirements as TSX-listed issuers, even if the degree or extent of disclosure is less than provided by TSX-listed issuers. The participant stated that it is important for venture issuers to adopt sound corporate governance practices as they may grow into larger issuers over time and investors should be informed of the controls and systems that are in place. In response, one participant reiterated that extensive corporate governance disclosure requirements would be onerous for venture issuers. The participant noted that issuers are concerned with the costs of compliance, which is a deterrent to raising money in the capital markets.

Several participants thought that the OSC should more rigorously enforce the disclosure requirements



applicable to venture issuers, particularly given that they are subject to less stringent requirements. However, one participant felt that enforcement of those disclosure requirements is not necessarily fundamental to good corporate governance. From an investor's perspective, good corporate governance is achieved when issuers have a structure in place that is reliable, transparent and aspires to recognized good practices.

Quality of disclosure

Several participants noted that some issuers do not communicate effectively with shareholders and stressed the need for plain and comprehensible language when describing corporate governance practices in their securities regulatory filings. The disclosure is often written in an obtuse and vague manner, and relevant information is difficult to locate. Another problem is that corporate governance disclosure can be difficult to compare among issuers. One participant stated that corporate governance disclosure should only include information that is material to investors.

One participant noted that certain issuers cannot afford lawyers and consultants to help them comply with disclosure requirements, which may lead to non-compliance. Non-compliance can also be due to the fact that issuers are not reading the disclosure requirements and are merely relying on precedents or staff who do not have the necessary expertise to draft the disclosure. Participants believed that issuers are not deliberately violating the requirements; rather they do not completely understand them. One participant argued that having consistent requirements that do not constantly change would help issuers understand and comply with the requirements.

Regulatory action

Most participants agreed that guidance and education from the OSC would be the best way to improve compliance with the corporate governance disclosure requirements. Instead of issuing more detailed requirements, which would be burdensome for smaller issuers, stricter enforcement of existing requirements would be one way to achieve the objectives of corporate governance disclosure.

It was suggested that the guidance to issuers should include examples of good disclosure by issuers. One participant noted that this could help issuers to learn from their own or others' mistakes and develop best practices.

Social disclosure

Several participants disagreed with the OSC's decision to not include a review of disclosure requirements regarding social matters in its mandate. They noted that disclosure of social matters may constitute material information for investors, and is an area of disclosure that has not received sufficient attention. Excluding social



matters sends a message to investors, issuers and other stakeholders that social matters are less relevant than corporate governance and environmental matters, which is not necessarily the case.

In addition, participants believe that environmental and social matters are inextricably linked, and as a result, it is not appropriate to review disclosure of environmental matters without taking social matters into account.

Role of the securities regulator

Consistent with the earlier discussion, the majority of participants would like to see the OSC take a greater role in advancing and promoting ESG disclosure. Participants noted that issuers and investors recognize that ESG matters are important and failure to meet environmental and social objectives and obligations may negatively impact financial performance.

Most participants agreed that the basic role of the securities regulator is to set disclosure standards and ensure that issuers disseminate information to investors and other stakeholders so that Canadian markets remain fair and efficient. It was suggested that the OSC should work with investors, issuers and other stakeholders in developing those disclosure standards and/or a related certification system. Instead of new requirements, most participants believed that the OSC should provide additional guidance on corporate governance and environmental disclosure requirements. In doing so, the OSC should monitor actions taken by other securities regulators, such as the U.S. Securities and Exchange Commission.

One participant noted that securities law and environment law should be integrated. While the OSC has an important role to play, there is a shift away from the regulatory model where the regulators or government play a central role to a model where multiple parties are involved. Both entities and activities must be regulated. Securities regulators regulate the former while environmental laws regulate the latter. The participant also suggested that the OSC should consider imposing a fiduciary duty on directors with respect to ESG matters; however, several other participants cautioned against doing so as this would not fall within the OSC's mandate.

