



Proposed Amendments to the Corporate Governance and Audit Committee Regimes

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On December 19, 2008, the Canadian Securities Administrators (the CSA) published proposed amendments to National Policy 58-201 - *Corporate Governance Principles* (NP 58-201), National Instrument 58-101 - *Disclosure of Corporate Governance Practices* (NI 58-101), National Instrument 52-110 - *Audit Committees* (NI 52-110) and Companion Policy 52-110CP (52-110CP) (collectively, the Proposed Materials).

National Policy 58-201

NP 58-201 currently sets out certain corporate governance guidelines that, although not mandatory, are coupled with the “comply or explain” disclosure regime of NI 58-101.

The proposed amendments to NP 58-201 establish nine core corporate governance principles that a board of directors should consider and in respect of which disclosure is required. Each principle is accompanied by commentary that provides relevant background and explanation, along with examples of practices that could achieve its objectives. However, these examples do not create obligatory practices or minimum requirements, and the principles do not establish minimum standards or “best practices”. The nine core corporate governance principles are as follows:

Principle 1 – Create a Framework for Oversight and Accountability

An issuer should establish the respective roles and responsibilities of the board and executive officers.

The responsibility of the board and executive officers should be clearly defined in order to, among other things, promote accountability to the issuer and its shareholders and an appropriate allocation of authority. Examples of recommended practices include adopting a written mandate or formal board charter and developing clear position descriptions for the chair of the board and chairs of board committees.

Principle 2 – Structure the Board to Add Value

The board should be comprised of directors that will contribute to its effectiveness.

Certain factors should be considered when determining the composition of a board, such as: (i) competencies; (ii) integrity; (iii) independent judgment; (iv) commitment; (v) board interaction; and (vi) board size.

Principle 3 – Attract and Retain Effective Directors

A board should have processes to examine its membership to ensure that directors, individually and collectively, have the necessary competencies and other attributes.

A board should have procedures for selecting and appointing directors to ensure members have the necessary competencies.

Principle 4 – Continuously Strive to Improve the Board’s Performance

A board should have processes to improve its performance and that of its committees, if any, and individual directors.

A board should provide its new directors with a comprehensive orientation and should provide continuing education opportunities for all directors.

Principle 5 – Promote Integrity

An issuer should actively promote ethical and responsible behaviour and decision-making.

The board has a responsibility to set the ethical standards applicable to the issuer’s directors, executive officers and employees. Examples of recommended practices include adopting a code of conduct.

Principle 6 – Recognize and Manage Conflicts of Interest

An issuer should establish a sound system of oversight and management of actual and potential conflicts of interest.

An issuer should have practices in place to identify, assess and resolve actual and potential conflicts of interest.

Principle 7 – Recognize and Manage Risk

An issuer should establish a sound framework of risk oversight and management.

Risk oversight and management should focus on identifying the most significant areas of uncertainty or exposure that could have an adverse impact on the achievement of the issuer's goals and objectives.

Principle 8 – Compensate Appropriately

An issuer should ensure that compensation policies align with the best interests of the issuer.

The board should be satisfied that appropriate compensation policies and practices are in place for executive officers and directors.

Principle 9 – Engage Effectively with Shareholders

The board should endeavour to stay informed of shareholders' views through the shareholder meeting process as well as through ongoing dialogue.

The board should promote a voting process that is understandable, transparent and robust, and that facilitates the board obtaining meaningful information on shareholder views in an effort to foster a productive relationship between shareholders and the board.

National Instrument 58-101

The CSA has proposed significant revisions to the disclosure requirements in Form 58-101F1. Under NI 58-101, an issuer would be required to disclose: (i) the practices it uses to achieve the objectives of each principle set out in NP 58-201; and (ii) certain factual information, such as the board's composition and information about any of its standing committees.

In addition, under NI 58-101, an issuer would no longer be required to file a copy of its code of business conduct and ethics or amendments to the code on SEDAR. However, an issuer would have to provide a summary of any standards of ethical and responsible behaviour and decision-making or code adopted by the issuer and describe how to obtain a copy of its code, if any.

National Instrument 52-110

Proposed Approach to Independence

The most significant change to NI 52-110 is the revision of the definition of independence that applies to audit committee members and other board members. Section 1.4 of NP 52-110 provides that "a director is independent if he or she (a) is not an employee or executive officer of the issuer, and (b) does not have, or has not had, any relationship with the issuer, or an executive officer of the issuer, which could, in the view of the issuer's board of directors having regard to all relevant circumstances, be reasonably perceived to interfere with the exercise of his or her independent judgment".

Under this definition, employees and executive officers of the issuer can never be considered independent. While a control person or significant shareholder is not disqualified from being independent, boards should consider the control person's or significant shareholder's involvement with the management of the issuer and, depending on the nature and degree of involvement, determine whether this relationship falls under the proposed definition of independence. In addition, the proposed definition is broader in that it will capture relationships that are reasonably "perceived" to interfere with the exercise of independent judgment (the current definition uses the language "reasonably expected"). The CSA propose to remove the "bright line" tests in NI 52-110, but will include a non-exhaustive list of relationships that could affect an individual's independence. Ultimately, determining independence will be left to the reasonable judgment of the board of directors. The new definition of independence would apply to all board members, including audit committee members.

Under NI 52-110, an issuer will be required to disclose certain information regarding director independence (such as names of directors considered to be either independent or not independent, and any relationships between the directors outside of common membership on the issuer's board).

Other significant changes to NI 52-110 include: (i) two new provisions that provide transitional relief from the requirement that all audit committee members must be independent, specifically: (A) when a "venture issuer" (i.e. a reporting issuer that, as at the applicable time, did not have any of its securities listed or quoted on any of the Toronto Stock Exchange, a U.S. marketplace, or a marketplace outside of Canada and the United States of America other than the Alternative Investment Market of the London Stock Exchange or the PLUS markets operated by Plus Markets Group plc) becomes a non-

venture issuer; and (B) in a reverse take-over when the acquirer is either a “venture issuer” or a non-reporting issuer; (ii) the removal of exemptions for controlled issuers (in light of the proposed definition of independence); (iii) the clarification of the scope of the exemption for U.S. listed issuers in section 6.1 of NI 52-110; (iv) the amendment to the temporary exemption from the requirement that all audit committee members be independent for limited and exceptional circumstances provided in section 3.8 of NI 52-110; and (v) the removal of the condition that the board of directors determine, in its reasonable judgment, that the audit committee member relying on this exemption is able to exercise the impartial judgment necessary to fulfill his or her responsibilities.

In addition, NI 52-110 explicitly provides that: (i) the issuer or any of its subsidiary entities must not obtain a non-audit service from its external auditor unless the service has been approved by the issuer’s audit committee; and (ii) the issuer must not publicly disclose information contained in or derived from its financial statements, MD&A or annual or interim earnings news releases, unless the document has been reviewed by its audit committee.

The CSA are inviting comments on the Proposed Materials until April 20, 2009.

This update is intended as a summary only and should not be regarded or relied upon as advice to any specific client or regarding any specific situation.

If you would like further information regarding the issues discussed in this update or if you wish to discuss any aspect of this commentary, please feel free to contact us.

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