

The Honourable / L'honorable  
**John P. Manley, P.C., O.C. / C.P., O.C.**  
President and Chief Executive Officer  
Président et chef de la direction

May 15, 2014

The Honourable James Moore, P.C., M.P.  
Minister of Industry  
Industry Canada  
C.D. Howe Building  
235 Queen Street  
11th Floor  
OTTAWA, Ontario  
K1A 0H5

Dear Minister,

I am pleased to enclose the submission of the Canadian Council of Chief Executives in response to the Industry Canada discussion paper on reform of the *Canada Business Corporations Act (CBCA)*.

As you know, the CCCE represents the chief executives of 150 of Canada's largest enterprises which are active in all sectors of the Canadian economy and highly engaged in international trade and investment. As such, we have a fundamental interest in ensuring that Canada upholds a reputation as a place where firms embrace high standards of corporate behaviour and responsiveness to shareholder concerns.

We believe that on the whole corporations in Canada have demonstrated a strong commitment to high standards of transparency and accountability. They have done so in an increasingly complex business environment, and in the face of growing and sometimes competing demands from an array of regulatory agencies, shareholders, institutional investors, hedge funds and market analysts.

The attached submission outlines the views of the Council on some of the key issues raised in the discussion paper. It reflects our view that the CBCA must remain as it was intended to be, an important piece of business framework legislation. While it can and should adapt, it is often the case that the provincial securities authorities are best placed to deal with the evolving state of corporate governance standards and changing marketplace needs.

We look forward to working with you on these important issues, and would be happy to discuss our recommendations in more detail if you would find it useful.

Sincerely,

A handwritten signature in blue ink, appearing to read "J. Moore". The signature is fluid and cursive, with the first name "James" and the last name "Moore" clearly distinguishable.

Enclosure

c.c. Mr. John Knuble  
Deputy Minister  
Industry Canada

Mr. Paul Halucha  
Director General  
Marketplace Framework Policy Branch  
Industry Canada

**SUBMISSION BY THE CANADIAN COUNCIL OF CHIEF EXECUTIVES**  
**RE CONSULTATION ON THE *CANADA BUSINESS CORPORATIONS ACT***

**Introduction**

As business leaders, we are firmly of the belief that good corporate governance must be a cornerstone of how Canadian companies operate. High standards of corporate behaviour and responsiveness to shareholder concerns and interests not only affect our ability to grow and prosper in Canada, they also are essential to the Canadian “brand” and the perception of Canadian companies in international markets.

We addressed issues of corporate governance in a major policy paper in 2002, *Governance, Values and Competitiveness: A Commitment to Leadership*, in the wake of Enron and other corporate failures. What we said at that time still holds true today – “Canada on the whole maintains a high standard of corporate governance” but that as CEOs we “should constantly strive to do better”.

Since that time, we believe that Canadian companies have indeed been improving their standards of transparency and accountability. And they have done so in an era of increasing scrutiny by shareholders, government and the public and under the spotlight of a widening array of players – analysts, hedge funds, institutional investors, proxy advisory firms and proclaimed governance experts – all of whom can place significant and sometimes competing demands on boards of directors.

***Before addressing the specific issues addressed in the consultation paper, we offer some comments on the broad framework of corporate governance in Canada.***

***A principles-based approach to corporate governance.*** The overall framework for corporate governance should be rooted in law, but not in a way that unduly restricts the need for boards to be flexible and able to respond to changing business circumstances. Canada has generally been blessed with a strong principles-based approach rather than one that relies on an excess of restrictive rules. Indeed, it has been one of our advantages in comparison to our neighbor to the south. When major reform of corporate legislation was undertaken early in the last decade, mostly in response to Enron and other corporate failures, the response in the United States was swift, legalistic and complex. In retrospect, Canada was wise to mirror some of the best practices from south of the border, while also avoiding some of the excesses of *Sarbanes-Oxley*. This more practical approach has stood the test of time and should continue to guide us. In particular, we note that securities authorities in Canada have shown that “comply or explain” policies are often best suited to the particular circumstances of the Canadian marketplace, in preference to more rigid rules or statutory standards.

As we noted in our 2002 paper, members of the CCCE head companies with a variety of corporate structures, including both widely held and majority controlled publicly traded companies, as well as privately held Canadian companies and wholly owned subsidiaries. The need to develop a “made-in-Canada” approach, based on sound principles, adherence to transparency and accountability standards and adapted to Canada’s particular market circumstances, remains equally relevant today. We remain of the view that there is no unique prescription that fits all different kinds of firms.

***The complex regulatory landscape in Canada.*** The Canadian corporate governance landscape includes not only the CBCA and other federal statutes, but also a number of provincial laws, rules and polices developed by the various securities regulators and stock exchanges, as well as significant jurisprudential standards that evolve over time.

Although efforts through the Canadian Securities Administrators (CSA) have demonstrated the merits of harmonization, the reality remains that Canada has 13 different provincial securities agencies. Accordingly, it is particularly important that the federal government approach the review of the CBCA with a view to ensuring that any proposed amendments to the Act do not conflict with regulations or policies adopted by one or more of the provincial securities authorities, nor impose duplicative obligations on Canadian companies.

Securities regulation and policies can more readily adapt to changing circumstances and needs, whereas a statutory instrument can be more inflexible and the amendment timeline more lengthy and uncertain. For these reasons, the CBCA should stay away from trying to overly regulate individual corporate behaviour.

***How should effective corporate governance be judged?*** While strong standards of corporate governance are important, and Canadian companies and regulators should be keeping abreast of best practices in this area, we need to ensure that excessive rule-making related to corporate governance does not hamper the ability of Canada's largest corporations to effectively pursue long-term growth for their enterprises. In particular, we should avoid creating a situation where companies feel pressure to recruit directors on the basis of their expertise in the more technical aspects of today's governance rules, which could very well come at the expense of securing directors who have the business acumen, sector experience and sound judgment to advise the company effectively on matters of short and long-term business strategy.

We also note the increasing trend towards external evaluation of the corporate governance performance of Canadian companies. The most recognized of these is the annual "Board Games" ranking, published by *The Globe and Mail*. The "Board Games" exercise purports to assess company performance on a broad range of criteria that "go far beyond minimum mandatory rules imposed by regulators". These include independence of directors, how many other boards they sit on, questions of stock ownership and compensation, voting policies, disclosure of information re directors' qualifications and attendance of directors at board meetings.

But good corporate governance is more than a question of ticking off boxes, as much as the Globe claims to use a "rigorous" set of criteria. A recent analysis of the "Board Games 2013" report by the law firm Norton Rose Fulbright LLP illustrated that having a high ranking on this kind of corporate governance score does not equate with superior financial performance. Indeed, they found quite the opposite trend in recent years. As the authors state, "Getting an 'A' in corporate governance isn't necessarily better than a 'B'. In fact, the data suggests that companies that focus too intently on corporate governance may be doing so at the expense of their shareholders."<sup>1</sup>

***Short term results vs. long-term value creation.*** As the sheer number of players in the corporate governance landscape has grown, so too has the pressure for improved transparency about corporate decision-making. It also has heightened the focus on short-term performance. To be clear, we recognize that much of the new shareholder activism is motivated by a legitimate desire to ensure shareholders have a means to voice their views on company management and strategy. However, we also see increasing activity by hedge funds and others aimed at short-term gain, with little apparent commitment to long-term value creation.

While many of the largest pension plans in Canada have shown clear attention to promoting long-term corporate success, the same cannot be said of some mutual funds and market analysts. And the financial media too often reinforce the focus on short-term

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<sup>1</sup> Orestes Pasparakis and Walied Soliman, "Good corporate governance is only good if it serves shareholders well", *National Post*, December 17, 2013.

performance. Management and boards feel continuing pressure to demonstrate quarter-by-quarter results, sometimes at the expense of duly considering strategies or investments aimed at longer-term growth.

Dominic Barton, Global Managing Director of McKinsey & Company, has written about the need to “fight the tyranny of short termism”. In a recent edition of the *Harvard Business Review*, Dominic Barton and Mark Wiseman of the Canada Pension Plan Investment Board note that too many large institutional investors “are not acting like owners”. In their view, many of these players use short-term investment strategies and pick external asset managers that reflect that orientation. A narrow view of a stock’s value “collectively leads to herd behaviour, excess volatility and bubbles”. It also leads to “boards and management making sub-optimal decisions for creating long-term value”.

In a recent survey undertaken by McKinsey of some 1,000 senior executives and directors across the globe, almost two-thirds of them indicated that the pressure to deliver short-term economic performance had increased over the past 5 years. And interestingly, a majority of CEOs whose companies had outperformed their competitors still reported an increase in short-term pressure.

A very recent and welcome development is the announcement of a new initiative spearheaded by McKinsey & Company and the Canada Pension Plan Investment Board (CPPIB). Entitled “Focusing Capital on the Long Term”, its members include the heads of major international asset funds and business experts. And its key mission is to develop “practical structures, metrics, and approaches for longer-term behaviours in the investment and business worlds”. The CCCE is fully supportive of this initiative and intends to work proactively with its proponents.

***With respect to the specific issues raised by Industry Canada in the CBCA discussion paper, we offer the following comments:***

### **Executive Compensation**

The Council supports Canada’s current voluntary approach to “say-on-pay”. We believe the board is in the best position to make decisions on the level and form of executive compensation, a responsibility that must be exercised consistent with the board’s fiduciary duty to act in the best interest of the company.

A properly constituted board is responsible for making core decisions about the long-term success of the company. Part of this duty is to ensure the company can attract and retain high-calibre executives capable of steering that course. To do so, the board requires the freedom and flexibility to determine executive compensation in a manner that fully incorporates the long-term health and interests of the individual company. As such, the board should be left to determine whether say-on-pay is in their best interest.

Council members have a strong history of dialogue with shareholders. Since 2009, 63 per cent of TSX-listed CCCE members have voluntarily adopted say-on-pay.<sup>2</sup> Over the same period, 80 per cent of TSX 60 issuers put forward say-on-pay resolutions.<sup>3</sup> It can be reasonably expected that more public firms will follow suit in the years to come. In instances when a company chooses not to adopt say-on-pay, it is often because the firm’s voting structure would render say-on-pay unnecessary. Therefore, it is unclear what mandatory say-on-pay would accomplish.

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<sup>2</sup> Including TSX-listed subsidiaries of CCCE members.

<sup>3</sup> CCCE members make up 72 per cent of TSX60 issuers.

For these reasons, we see no need to amend the CBCA to deal with the issue of executive compensation, nor to impose obligations that would be duplicative of current disclosure requirements under provincial securities laws and/or TSX rules for listed companies.

### **Diversity of Corporate Boards and Management**

The Council is on record in support of the Ontario Securities Commission's proposal for a 'comply or explain' approach to the question of increasing gender diversity on boards and in senior management in Canadian companies. The results from the *2013 Catalyst Census of FP500 Women Board Directors* show that the largest companies in Canada are making progress on this front, although clearly more needs to be done. Amending the OSC's *Corporate Governance Disclosure Rule* to require companies to disclose their performance annually will help to increase transparency and accountability. It will also allow shareholders and investors to assess whether individual firms have taken appropriate action. As well, the process will provide baseline data, enabling progress to be better measured over time.

For the reasons noted above, we believe that this is another area where a 'comply or explain' approach is preferable to rigid rules enacted by statute, and we would recommend against amending the CBCA to deal with the issue. In fact, increasing diversity on Canadian boards requires a multi-faceted approach. It is equally important, if not more so, to ensure that over time we are significantly increasing the number of board and management-ready women. Women must be properly recognized and prepared to take on the responsibilities of board and senior management positions. Governments and enterprises should encourage mentorship and sponsorship opportunities. In addition, finding ways to encourage incorporation of gender diversity as part of the "way companies do business", from employee interactions to human resources development plans, from frontline work with customers to engaging senior management, will make gender considerations part of everyday business practices and over time, part of the company culture.

### **Shareholder Rights - Voting**

Some corporate governance advocates have suggested that corporations should establish term limits for directors as a means of ensuring board renewal. However, we believe that any amendment to the CBCA to impose mandatory term limits would be a retrograde step. While board renewal is important, for many companies a degree of continuity will be essential to ensure the ability of the board to maintain focus on overall strategic direction. Board renewal can be accomplished in several ways, and companies must have the flexibility to adopt the policy that is best for them. In its *2014 Corporate Governance Principles and Proxy Voting Guidelines*, the Ontario Teachers' Pension Plan has indicated that it is not persuaded that "tenure or age is an effective means to determine board rotation". Term limits could actually impede the ability of companies to ensure the appropriate degree of experience and continuity on their board that can be critical to safeguarding the long-term interests of the enterprise.

Other voting issues raised in the discussion paper include the shareholder vote on the election of directors individually (and not as part of a slate); public disclosure of the results of that vote; and a board policy for dealing with situations in which a majority of the votes cast were not in favour of the election of any individual director.

By June 30, 2012, almost all S&P/TSX Composite issuers (over 90%) had moved to individual director voting and 80% of TSX Composite issuers were reporting results of the vote on directors. Most issuers on the Small Cap Index had also adopted individual director voting (80%), although far fewer (40%) reported those results. Effective December 31, 2012, the TSX has made both practices mandatory for all TSX listed issuers.

Analysis also shows that in 2012 at least two-thirds of issuers on the TSX Composite (and 30% of issuers on the Small Cap Index) had adopted a board policy for dealing with situations in which a majority of the votes cast were not cast in favour of the election of any individual director. The new TSX rules have adopted a 'comply or explain' approach in this area – issuers must disclose whether they have such a policy and if not, why not. Issuers who have not adopted such a policy will be required to advise the TSX if any of its directors do not receive a majority of votes cast in favour of their election.

Given the policies that now apply to all TSX listed issuers, we see no need to adopt new rules on voting rights within the CBCA.

### **Over-voting and Empty-voting**

Proxy voting is a complicated process. Hedge fund activism, institutional shareholder ownership and shareholder engagement with issuers on governance and performance matters have led to a rise in proxy contests, placing a significant strain on the system.

The Council fully supports efforts to improve the accuracy, transparency and integrity of the proxy voting infrastructure in Canada, including enhancements to disclosure obligations. Hidden ownership strategies, over-voting (where voting rights may be exercised both by an intermediary and the beneficial owner) and empty-voting (where a holder of the voting right has reduced his economic interest through a hedge or derivative) are significant disadvantages to issuers and undermine early warning regimes and other disclosure requirements that are based on beneficial ownership and control.

There are more immediate steps which provincial regulators can and should take to work with market participants and adopt rules aimed at stemming such practices. We also would be open to legislative change through the CBCA, with the overall goal to make clear that shareholder proposals and requisitions should only be able to be utilized by shareholders who reveal their identity and who have held an actual beneficial interest in the company for a meaningful period of time.

### **Separation of the Role of Chair and CEO**

A decade ago, when corporate governance issues were on the front burner, part of the debate around director independence focused on the question of whether a single individual should hold both the position of Chair of the Board of Directors and Chief Executive Officer. Since that time, the trend has been clear and most publicly traded companies in Canada have adopted the practice of having a non-executive Chair or an independent lead director to ensure the Board undertakes appropriate supervision of management.

In the case of privately-owned companies and those with a controlling shareholder, the rationale for separating the roles is less clear. Accordingly, we would not support an amendment to the CBCA that would make this a requirement for all federally incorporated companies. We maintain the position that we stated in our 2002 governance paper – where the Chair and CEO positions are occupied by the same person, independent directors should elect and disclose the name of a lead director who will be responsible for ensuring that the board is in a position to act independently of management when necessary.

### **Corporate Governance and Combating Bribery and Corruption**

We believe that with the passage of the *Corruption of Foreign Public Officials Act* (CFPOA) in 1998, Canada took appropriate steps to implement its commitments under the *OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions*. Since this legislation is purpose-built, we see little additional value in trying to shoehorn additional requirements into the CBCA, which at best would be duplicative and

could very well lead to conflicting or inconsistent standards and obligations for Canadian companies doing business internationally.

The CFPOA was amended in June, 2013, in part to address criticism that the Act's reach was essentially limited to wrongdoing occurring in Canada. Offences committed outside Canada, by Canadian citizens or firms headquartered in Canada, are now subject to the Act. It is worth noting that this change, together with tougher sentences for offenders and increased resources for enforcement, have given Canada a favourable ranking in the eyes of Transparency International.

As a result of *Dodd-Frank* and rules adopted by the Securities and Exchange Commission (SEC), US companies engaged in commercial development of oil, natural gas and minerals are required to disclose payments made to domestic and foreign governments. A similar directive has been adopted in the European Union.

In Canada, the growth of the "publish what you pay movement" motivated the Canadian mining industry to work proactively with some critics and establish the "Resource Revenue Transparency Working Group". Their report was published earlier this year and recommends improved revenue transparency.

At one time, the federal government had indicated that it would bring in legislation sometime in 2014, requiring Canadian extractive companies to publicly report payments over \$100,000 to all levels of government, both domestic and foreign. In early March, then Natural Resources Minister Joe Oliver indicated that the federal government's "preference is to work with the provinces and territories to implement mandatory reporting standards through the securities regulators". He also indicated the government's intention to bring in federal legislation by April 1, 2015 if the provinces do not implement adequate standards.

In light of considerable progress already being made by the extractive industry on this question, as well as ongoing discussions between the federal and provincial governments, it would be premature to contemplate amendments to the CBCA at this time to deal with the issue. Rather, a coordinated federal-provincial approach, and likely implemented through provincial securities authorities, would appear to be the wiser course.

### **Shareholder Proposals**

The consultation paper makes reference to complaints from some quarters that shareholder proposals can be difficult to utilize. Such proposals can be an important means for shareholders to raise legitimate issues for consideration at the annual meeting. Nonetheless, we believe these provisions should largely be reserved for shareholders with a demonstrated longer-term interest in the wellbeing of the company. Accordingly, we would urge caution in further expanding these rights, in order to avoid the possibility of unscrupulous hedge funds or activists interested only in short-term gain putting forward proposals that do not serve the interests of shareholders in general.

### **Shareholder Approval of Significantly Dilutive Acquisitions**

In the course of a major corporate acquisition, the acquirer may choose to issue new shares in lieu of cash payments, which can result in the dilution of the existing shareholder's interest in the corporation. Companies listed on the TSX are required to obtain shareholder approval in cases where the means of acquisition would result in a dilution of the existing shareholders' interests in excess of 25 percent. Accordingly, we do not believe that the CBCA should be amended to deal with this situation. Additional rules in this area would at best be duplicative, and at worst could lead to considerable uncertainty and delay to the acquisition, and potentially handcuff the board in being able to make the acquisition on a timely basis. It should be remembered that the board has a statutory fiduciary duty to look after the interests of all shareholders.