The following is an excerpt from:

*Directors' Duties in Canada, 3rd Edition*

Written by Barry J. Reiter & the Corporate Governance Group of Bennett Jones LLP

Published by CCH Canadian Limited, 2006
CHAPTER 1

CORPORATE GOVERNANCE: BASIC PRINCIPLES AND CURRENT ENVIRONMENT

There has never been a more exciting time to be a director of a corporation. There has never been a more challenging time to be a director of a corporation. Directors operate in a new and very changed environment. Expectations are high, and directors' actions (and inaction) are subject to observation and comment from a wide variety of interested constituencies.

This book attempts to provide guidance to directors, and to those who advise them, about the expectations that exist and the requirements and best practices that will help meet such expectations.

In general, the phrases "corporate governance" and "corporate accountability" refer to the broad functions of those who oversee a corporation's affairs and the means by which they are held to account for their stewardship.¹

"Corporate governance" refers to the overseeing and directing of a corporation, as distinguished from the day-to-day managing of one. It entails supervising and contributing to the executive functions of management.

Corporate governance obliges directors to:

- ensure the development and implementation of strategic direction for the corporation's survival and prosperity;
- select the CEO and, possibly, other principal executives, supervise the performance of these executives, and ensure adequate succession planning;
- evaluate risks and ensure that appropriate control mechanisms are in place;
- monitor the corporation's business results;
- ensure that the corporation has met appropriate standards of financial and ethical behaviour;
- be accountable to shareholders, employees, customers, suppliers, regulators, and the community in which the corporation functions;
- ensure that they have adequate information and support to enable them to discharge their responsibilities;

¹ See the Selected Bibliography, which contains a sample of some of the many articles, books, law firm publications, and regulatory and legislative materials produced in the past three years on the subject of corporate governance.
• monitor and ensure the satisfactory and appropriate reporting of business results; and

• discharge specific duties that are imposed on directors by legislators, regulators, stock exchanges, and observers of corporate affairs.

At its most basic level, the duty of a director is established under the governing legislation of the corporation and, in common law jurisdictions, in a very lengthy history of judicial decisions. The legislative regime of the Canada Business Corporations Act is typical. Under s. 102(1) of the CBCA, "[s]ubject to any unanimous shareholder agreement, the directors shall manage, or supervise the management of, the business and affairs of a corporation." The directors function by enacting by-laws (which ultimately must be confirmed by shareholders) or by passing resolutions that are signed by all directors or enacted by a majority of the directors at meetings.

At its most basic level, the duty of a director is established under the governing legislation of the corporation and, in common law jurisdictions, in a very lengthy history of judicial decisions. The legislative regime of the Canada Business Corporations Act is typical. Under s. 102(1) of the CBCA, "[s]ubject to any unanimous shareholder agreement, the directors shall manage, or supervise the management of, the business and affairs of a corporation." The directors function by enacting by-laws (which ultimately must be confirmed by shareholders) or by passing resolutions that are signed by all directors or enacted by a majority of the directors at meetings.

Each jurisdiction's business corporation legislation specifies the qualifications for directors. The legislation also specifies residency requirements for directors. Directors may, subject to specific exceptions, delegate many of their activities to executives, a managing director who is a resident Canadian, or a committee of directors.

Directors must disclose the nature and extent of any interest they may have in a material contract or material transaction, whether made or proposed, with the corporation if a director (1) is a party to the contract or transaction; (2) is a director, officer, or individual acting in a similar capacity of a party to the contract or transaction; or (3) has a material interest in a party to the contract or transaction. In general, a director who is required to disclose a conflict may not vote on any resolution to approve the contract or transaction.

Directors, in exercising their powers and discharging their duties, are required to (a) act honestly and in good faith with a view to the best interests of the corporation, and (b) exercise the care, diligence, and skill that a reasonably prudent person would exercise in comparable circumstances.

Layered on top of the statutory obligations are the results of centuries of judicial decisions about the responsibilities of directors. Courts have expanded greatly on the obligations

---

2 Canada Business Corporations Act, R.S.C. 1985, c. C-44, as amended ("CBCA").
3 For a more detailed discussion of director qualifications and residency requirements, see section II of Chapter 3, "Constituting the Board".
4 CBCA, s. 121 and ss. 115(1) and (3); see also the Ontario Business Corporations Act, R.S.O. 1990, c. B.16 ("OBCA"), s. 133 and ss. 127(1), (2), and (3). But where directors delegate to a committee, a majority of the members of the committee must be resident Canadians; see also Alberta Business Corporations Act, R.S.A. 2000, c. B-9 ("ABCA"), s. 121 and ss. 115(1), (2) and (3). Where the directors delegate to a committee, 25 percent of the members of the committee must be resident Canadians.
5 CBCA, s. 120(1).
6 CBCA, s. 120(5) creates an exception to this rule where the contract or transaction is (a) connected mainly to a director's remuneration as a director; (b) for indemnity or insurance under CBCA, s. 124; or (c) with an affiliate. ABCA, s. 120(6) and OBGA, s. 132(5) create an additional exception where the contract or transaction is by way of security for money lent to or obligations undertaken by the director for the benefit of the corporation or an affiliate. The British Columbia Business Corporations Act, S.B.C. 2002, c. 57 ("BCBCA") contains no such exceptions.
7 CBCA, s. 122(1).
to act honestly and in good faith with a view to the best interests of the corporation and to exercise the care, diligence, and skill that a reasonably prudent person would exercise in comparable circumstances. Directors are fiduciaries who are subject to obligations to meet stringent standards of ethical and altruistic behaviour. Directors must follow the high standard that is set for a trustee with respect to dealing honestly, in good faith, and without conflict of interest. A great many cases have elaborated on the implications of these principles.

The second element of a director’s duty to the corporation is the prescribed duty of care. This duty obliges directors to spend the time and pay the attention that is appropriate to someone who is charged with such responsibilities.  

These legislative and common law principles have been in place for some time and remain largely unchanged. What has changed, however, is the environment of corporate governance and the response of a plethora of interested constituencies as a consequence of that change. Corporate governance has received more attention as the power and significance of corporations have increased over the past one hundred years. Interest in corporate governance jumped sharply following a number of high profile, and in some cases, spectacular corporate failures. Reports asking such things as "Where were the directors?" were produced as long as a dozen years ago. But interest in corporate governance grew dramatically following the reporting of a number of colossal corporate failures whose names have now become synonymous with the view that there must have been massive dereliction of duty by the directors. In each of these cases, the state of health of the business appears to have been misrepresented to financial stakeholders, employees, and regulators. Although inept or criminal managers may have been the root cause, attention was also focused on the failure of the directors to identify and address the risks involved.

The response to this problem has been broad. In the United States, the most significant initiative has been the Sarbanes-Oxley legislation that imposes specific obligations on directors, prohibits certain behaviours, and requires regulators and stock exchanges to enact supplemental regulations. These matters have direct relevance to Canadian corporations that offer securities (or whose shares trade on stock exchanges) in the United States, and to Canadian professionals who advise companies that file materials with the Securities and Exchange Commission (the "SEC"). They have also served as a model against which the responses of comparable Canadian regulators might be contemplated and judged.

Accordingly, four years after the passage of the Sarbanes-Oxley Act, the corporate governance responsibilities of directors are affected not just by basic corporate legislation and fiduciary duty law, but also by the following factors.

---

8 The matters addressed in this brief overview are dealt with in more detail in Chapter 2.
9 Report of the Toronto Stock Exchange Committee on Corporate Governance in Canada. Where Were the Directors? Guidelines for Improved Corporate Governance in Canada (the "Dey Report") (December 1994).
11 Ibid. at s. 307. The SEC has the authority to issue rules in the public interest that set standards of professional conduct for lawyers "appearing and practicing before the Commission". This phrase is defined broadly by the SEC and includes transacting any business with the SEC, representing an issuer in an administrative proceeding or in connection with an SEC investigation, providing advice in respect of United States securities law or the SEC's rules or regulations regarding any document that will be filed with or submitted to the SEC, and advising an issuer as to whether information or writings are required to be filed or submitted to the SEC.
I. Regulation

Regulators have focused on the qualifications of directors, the process and substance of what directors do, and the visibility of these matters to interested constituencies. Since many of the first corporate disasters involved a lack of financial integrity, the initial focus was on financial reports and audit committees.

The rules in place across most of Canada require that public companies have audit committees and that these committees be entirely made up of directors who are "independent" of management.\textsuperscript{12}

While the question of who is "independent" is, in general, left to the discretion of the directors, in the case of audit committees, very specific rules define independence. (For instance, the rules deny the status of independence to a director who has been a former employee within the past three years, to a member of a professional firm whose firm has any dealings with the corporation, or to a director who received any compensation whatsoever for services other than as a director.)\textsuperscript{13} Audit committee members must meet the qualification of "financial literacy", defined as "the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the issues that can reasonably be expected to be raised by the issuer's financial statements".\textsuperscript{14} Audit committees must operate under a mandate that is made public by the company\textsuperscript{15} and are required by the rule to deal with a number of specific matters, including the following: making recommendations to the board of directors regarding the selection and compensation of auditors; reviewing financial information before it is published; approving non-audit services to be performed by the auditors in respect of matters where these services are not prohibited; establishing procedures for the receipt, retention, and treatment of complaints received regarding accounting, internal accounting controls, or auditing matters; establishing procedures for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters (so-called "whistleblower procedures"); and approving the company's policies regarding the hiring of present and former members of the auditor.\textsuperscript{16} What all of this regulation represents is a statement that audit committee members cannot be trusted to develop and meet a satisfactory standard of care on their own, and therefore, their duties should be specified by regulators.

The current focus of regulatory direction is on compensation matters. Compensation issues have been identified in current materials and in speeches published by securities regulators in the United States and Canada. The first step actually occurred some time ago with the requirements for individualized disclosure of the compensation of the most highly paid executives and for transparency (in the form of a detailed report by the board committee charged with the management of executive compensation matters, which is, typically, the human resources or

\begin{itemize}
  \item \textsuperscript{12} Multilateral Instrument 52-110, Audit Committees, ss. 2.1(1) and 3.1(3) ("MI 52-110"). This Instrument has been adopted in all jurisdictions except British Columbia.
  \item \textsuperscript{13} Ibid. at ss. 1.4–1.5. See Chapter 6, "The Use of Committees", for further discussion on audit committees.
  \item \textsuperscript{14} Ibid. at s. 1.6.
  \item \textsuperscript{15} Ibid. at s. 5.1, which requires every issuer to include Form 52-110F1 in its Annual Information Form. Form 52-110F1 requires the inclusion of the text of the audit committee's mandate.
  \item \textsuperscript{16} Ibid. at s. 2.3.
\end{itemize}
compensation committee). Regulators on both sides of the border have been increasing the pressure on such committees to provide more detailed, comprehensive, accessible, and entirely accurate disclosure of executive compensation and of the principles and mechanics used to determine that compensation.

Regulators have strongly encouraged the existence of mandates specifying the responsibilities of the board (rather than those of management), of committees, and of those in certain positions (such as the chair, lead director, or CEO). Typically, where mandates exist, they must be made public. The most significant step has been the promulgation of National Policy 58-201, which is discussed in detail below. All of the Canadian Securities Administrators ("CSA") have agreed upon a set of duties, qualifications, processes, and substantive matters that they believe are appropriate for the operation of effective boards. Where the obligations are not mandatory (as they are, for instance, with respect to audit committees), the CSA have encouraged compliance with the guidelines and disclosure of the manner in which each particular concern is being addressed. In a far less than subtle way, public companies are strongly encouraged, by the transparency of their reporting, to be able to say that they have addressed a particular concern in a satisfactory manner.

Chapter 6, "The Use of Committees", discusses board committees in more detail and provides sample committee mandates.

II. Stock Exchanges

Under the Sarbanes-Oxley legislation in the United States, stock exchanges were assigned a major role in developing and implementing regulations. While this situation has not been the case in Canada, the Toronto Stock Exchange ("TSX") has had a lengthy history of interest in corporate governance, dating back at least to the Dey Report in 1994. Its recent interest was expressed through the promulgation of disclosure guidelines against which listed companies were required to report. These guidelines have now been surpassed by NP 58-201, although many companies continue, on at least a transitional basis, to also provide disclosure against the TSX guidelines.

III. Consequences

The legal environment provides for severe and direct consequences to directors who are derelict in their duties. Chapter 11 includes a catalogue of legislation and regulations that attach personal liability to directors. In general, the only escape from the various liabilities is on the basis of a "due diligence defence", meaning proof (with the burden being on the director) that the director took the appropriate steps to ensure that the particular requirement was complied with.

17 See, for example, the Ontario Securities Act, R.S.O. 1990, c. S.5, Form 40, Statement of Executive Compensation ("OSA"). This form was revoked by O. Reg. 56/04, s. 14(4), effective June 1, 2004. The disclosure of executive compensation is now required by National Instrument 51-102, Continuous Disclosure Obligations, Form 51-102F6 ("NI 51-102").

18 National Policy 58-201, Corporate Governance Guidelines, ss. 3.4-3.5 ("NP 58-201").


20 Supra note 10, s. 3.

21 The Dey Report, supra note 9.
Civil, criminal, or regulatory penalties against the director personally are used as indirect means of ensuring compliance by management, who typically have responsibility for the particular matter in the first instance.

This approach was given a significant boost with the enactment into law (on December 9, 2002) in Ontario of Bill 198, which added ss. 138.1–138.14 to the OSA.\(^\text{22}\) This legislation provides for director responsibility to those who buy or sell securities on the secondary market (for instance, through trading on a stock exchange) during a period when there is a "disclosure violation". A disclosure violation occurs when a company has failed to disclose material information when it should have or when it has disclosed erroneous information.\(^\text{23}\) Directors have a due diligence defence. Boards are currently working with their legal advisors to understand what due diligence means in the various contexts in which disclosure violation issues can arise. Bill 198 makes class actions far more likely by eliminating the need to prove reliance on inaccurate disclosure by a person who traded during the relevant period and by establishing the damages of each person who traded during that period on a formulaic basis (so that anyone buying or selling securities during that period will have damages that are assessed on a comparable basis). Legislation similar to Ontario's Bill 198 has been enacted in Alberta and British Columbia and will come into force on proclamation.\(^\text{24}\)

The regulatory initiatives described above (for instance, the specified skills required of audit committee members and the duties that they must undertake) have had an additional consequence. For centuries, the view adopted with respect to determining a director's duty of care was on an objective standard, a comparison to what was to be expected of a hypothetical director, without reference to the director's particular skills or background. A variety of more recent cases in litigation and in regulatory proceedings have suggested that the standard now includes a subjective element\(^\text{25}\) so that, for instance, an audit committee member might be held to a higher standard than another director with respect to a financial issue, a highly experienced financial expert on an audit committee might be held to a higher standard than another member of the audit committee, a lawyer serving on a board might be held to a higher standard than a non-lawyer with respect to corporate governance matters, and the like.\(^\text{26}\) There is also a widespread view that the bar has been raised for directors generally. While at some time in the past it might have been regarded as acceptable to review material briefly before a board meeting and then to politely attend a management presentation that constituted the meeting, all of those involved in the regulation of corporate governance have made it clear that diligent effort and a significant commitment of time are now required and expected.

\(^{22}\) See OSA, Part XXIII.1, Civil Liability for Secondary Market Disclosure, in force as of December 31, 2005.

\(^{23}\) See a more detailed discussion of this matter in Chapter 7.

\(^{24}\) In Alberta, Bill 25, the Securities Amendment Act, 2006, 2d Sess., 26\(^{\text{th}}\) Leg., Alberta, 2006, s. 52, creates civil liability for secondary market disclosure under Part 17.01 of the Alberta Securities Act. In British Columbia, Bill 38, the Securities Act, 5\(^{\text{th}}\) Sess., 37\(^{\text{th}}\) Leg., British Columbia, 2004, provides for a new Securities Act that includes civil liability for secondary market disclosure.


\(^{26}\) In YBM Magnex International Inc., Re (2003), 26 O.S.C.B. 5285, the Ontario Securities Commission considered the skill set and background of each individual director in determining culpability. See also OSA, s. 138.4(7)(b), which explains that in determining director liability, the court must consider all relevant circumstances, including the knowledge, experience, and function of a director.
These higher standards are backed by the transparency requirements described previously and by the existence of a significant number of constituencies paying attention to governance issues. Institutional investors have promulgated their own codes of good governance or have banded together as groups to do so. They observe corporate governance behaviours and rank companies against the standards they have set. Some of the organizations have voting guidelines that require them to withhold votes on matters that do not meet their guidelines. Some organizations are active in speaking to influencers of corporate governance behaviours with a view to encouraging compliance with guidelines; some go even further by introducing and supporting shareholder proposals that are introduced and required to be debated and voted upon at annual shareholder meetings. Corporations sometimes require the votes of these powerful influencers and will comply with their guidelines in aid of (for instance) passing a particular compensation regimen or obtaining approval for an additional allocation of stock options.

Beyond this, media interest in corporate governance is now intense. The Globe and Mail's Report on Business conducts an annual survey of corporate governance practices and ranks companies on a points system against its own questions and standards. While many take issue with the Globe's standards and weightings, there is no doubt that corporations and directors pay attention to the rankings and are pleased with, or concerned and embarrassed by, the performances of their companies. Transparency in corporate governance reporting has facilitated these sorts of surveys and rankings, since information in regards to compensation, director shareholdings, director meeting attendance records, the number of meetings held, the basis of compensation decisions, and other such matters are now public information and readily accessible. The views of the media, as expressed in surveys of this sort, and those of institutional shareholders, as expressed in guidelines and public statements, are significant factors influencing corporate governance behaviours.

So, what are the practical implications of saying that standards and expectations of directors are now at a higher level? This question focuses attention on a series of issues that arise about what directors should do and how they can do their jobs.

IV. Management and the Board

While management, through the CEO, executive team, and others, is responsible for managing the corporation, the board's role (except in a time of crisis) is limited to oversight and supervision. Difficulties arise when boards and management teams are unable to establish clarity about what fits into each of these essential elements of corporate life. Unless there is an agreement on what is and is not management business or board business, board time may be wasted on minor administrative trivia and important decisions may be made by management.
without the board's knowledge or approval. Matters of this sort are best resolved, in the first instance, through the existence of a board of directors' mandate and by delegating authority to management. Virtually every corporate governance initiative of the past few years has either required a mandate of this sort or strongly recommended one.\textsuperscript{31}

Boards should not adopt an "off the shelf" mandate. While it is certainly useful to consider what other companies have done, it is important for boards and management teams to work together to determine what is right for their corporation. The exercise of creating a mandate suited to a particular company is valuable in building the relationship between the board and the management and in enhancing the relationships between board members and among them.

The types of issues that should be addressed in a board mandate are:

- the corporation's strategic business goals and objectives and how they are to be achieved;
- the corporation's responsibility for ensuring the integrity of the CEO and other executive officers;
- the corporation's policy on communication;
- the corporation's means of receiving feedback from stakeholders;
- the corporation's policies and processes for the appointment, training, evaluation, and succession of management;
- the corporation's strategic and operational policies within which management will operate;
- the corporation's annual targets against which corporate and executive performance will be measured;
- the corporation's approach to appointing directors to the board committees;
- the corporation's executive compensation policies;
- the corporation's approach to identifying and monitoring the risks of the business in which the corporation is engaged; and
- the corporation's approach to corporate governance.

A sample board mandate is found in Appendix I at the end of this Chapter. A sample Delegation of Authority, in partial implementation of a board mandate, can be found in Appendix II at the end of this Chapter.

Board mandates should be reviewed regularly. The circumstances of the corporation, the governance environment, and the composition of the board and the executive team change so that minor refinements or even significant revisions in the relationship between the board and management may be appropriate. It is typical for board mandates to be reviewed at least once a year. The usual process is that the review is initiated by the corporate governance committee, working with the general counsel or secretary in consultation with the CEO and other appropriate board members, before being approved by the corporate governance committee for recommendation to and approval by the board.

V. Board, Committees, and Individual Directors

Once a mandate has indicated what the board believes its responsibilities encompass, the board must get on with doing the job. While much of what boards do occurs at meetings of the entire board, focused and detailed work is often undertaken by board committees. While audit committees are required, and some of their duties are specified with respect to public companies, boards usually create compensation committees (sometimes called human resources committees) and corporate governance committees. Depending on the size and nature of the responsibilities of the business and the board, other committees, such as environmental committees, risk committees, finance committees, executive committees, or other committees may be created to ensure that important matters are considered on an ongoing and timely basis. Such matters are considered by a group that is smaller than the entire board and is usually made up of board members who have a distinctive expertise and a particular interest in the committee's business.

It is important that boards and committees come to a clear understanding about which responsibilities are those of the committee (many matters could be assigned to more than one committee) and which are those of the entire board. In the past, the division of authority may have been decided by a loose agreement, but today, such a division is usually expressed and achieved through the adoption of committee mandates. Such mandates are required for audit committees and strongly recommended for other committees. The use of committees and matters related to their mandates are addressed in detail in Chapter 6.

At a more basic level, individual directors must determine for themselves the nature of their role and responsibilities. Within the broad rubric of their role in overseeing and directing a corporation, directors must ascertain for themselves which matters, of a great many possibilities, they must pay careful attention to, they can defer to the careful work of others (such as a committee or a director who is an expert in a certain area), or they should provide personal leadership on.

Boards are collective and dynamic organizations. In general, directors must work well together, and they must be respectful of each other if their business is to get done. It is not the role of a board member to take an adversarial position at all times in order to challenge or assess the competence or good faith of other board members or management. On the other hand, a director should be expected, by both the board and by regulators and others involved in corporate

---

32 This is particularly the case because any mandate will be viewed as the "bar" that has been set by a board and committee, and it specifies the minimum requirements of the job.

33 MI 52-110, s. 2.3. Note also that NP 58-201 requires both the nominating and the compensation committees to create a written charter (see Part 3).
governance, to become more actively involved in, and to take a leadership role in, situations requiring that director's particular expertise, experience, or interests. During the recruitment process, directors should begin the task of understanding their role within a board by reading available information about the corporation and its current board, by speaking with the CEO and other corporate executives, and by learning about current directors and speaking with them. An individual director's roles and responsibilities vary with a particular board and with the circumstances and dynamics of that board over time. There is no substitute for experience when understanding what a director's responsibilities may be in any particular case. Directors can rely on their own advice or they should feel free to seek advice from fellow board members or from other advisors.

VI. Leadership

An examination of any board mandate reveals that the board has its own business that is distinct and separate from that of management. Corporate governance reformers of the past decade have recognized an inherent conflict in combining these roles, since the role of the chair is ultimately to lead the supervision of the CEO. Accordingly, the separation of these roles has been consistently recommended, and the implementation of these changes has occurred to a very large extent in Canada (but at a slower pace in the United States). The most relevant current reform initiative strongly supports the separation of these roles and requires that the leader of the board's business, the lead director, be in place if the roles of the chair and the CEO are otherwise combined. The CSA guidelines also recommend clarity in understanding the nature of the board leader's role, and therefore, the development of a position description for that leader. Examples of position descriptions for the chair of the board and for the lead director are found in Appendices III and IV, respectively, at the end of this Chapter.

There is much to be said beyond the words used in these position descriptions. Board leadership is an art in the field of interpersonal relations. The chair or lead director must be effective in being tactful, forceful, deferential, insistent, inclusive, and determined, as required by the circumstances, while remaining respectful of fellow directors and seeking to build and maintain a consensus and alignment between, and among, directors and management.

VII. Director Recruitment

Historically, directors were proposed by management, frequently from a small network of close business associates and friends of the CEO. Requirements for distinctive skill sets (for example, financial acumen, legal knowledge of corporate governance, human resources, and

34 Barry J. Reiter, "When Directors Should Get Worried", Corporate Governance Review (August/September 2004).
36 See Spencer Stuart. The 2005 Canadian Board Index (January 2006), available online at: www.spencerstuart.com. Spencer Stuart's analysis of the 100 largest publicly held Canadian companies revealed that the boards of 80 percent of these companies split the roles of chair and CEO. In the U.S., however, such a split is only made by 31 percent of comparable boards.
37 NP 58-201, Corporate Governance Guidelines, s. 3.2.
compensation) or simply for more independent directors have led searches further afield. This process has been accelerated by the recognition that the board's business is its own, and that an effective board must be comprised of compatible directors who will be respectful of, and work well with, each other and management, while bringing a suitable range of skills and experience to ensure that the various jobs required at the board and committee levels are performed well.

The process of building a board should be a continuous one, one in which the skill sets and contributions of existing directors are assessed on a regular basis against those of others and against the evolving needs of the corporation. While the invitation to become a director was once thought to be a great privilege, and prospective directors usually accepted, without hesitation, offers to join boards, most individuals now think carefully about such an offer and assess it against their personal interests, the considerable time required, the nature of the responsibility involved, and their view of what it will be like to work with the other directors and the current management team. Accordingly, the best boards are constantly in board-building mode, preparing lists of skill sets that might be useful to the board in the future, and considering and meeting on a preliminary basis with individuals who might possess those skill sets. Decisions are made carefully and incrementally, rather than being undertaken on a wholesale basis, only under the pressure of a massive change in board composition induced by a crisis or a fundamental disagreement. Boards now work hard at expanding the range of networks from which future directors might be drawn, and it is now common for boards to use professional executive recruitment services to aid the process.

VIII. Making Directors Effective

It is not easy to be a director. A good director must learn enough about the business to be able to offer his or her views in a supervisory capacity to those who are expert in managing the corporation on a day-to-day basis. Directors must also know enough about their board and its processes, as well as enough about governance generally, to be able to make an effective contribution as a board member and to comply with applicable policies and rules. The process of becoming an effective director begins before the director is recruited, with the director's due diligence in considering a board position. In a good board, this process continues with a director orientation program that is designed to move the director as far up the learning curve as quickly as possible. Such an orientation might include meetings with the CEO and with various members of operating management who can describe elements of the business, tours of the facilities, meetings with other directors, meetings with the general counsel and corporate secretary, one-on-one meetings with the chairman or lead director, and supplying the director with the appropriate materials presented in an organized form.

When supplying directors with materials, it is often helpful, both to a new recruit and to existing directors, to create and maintain an up-to-date "Directors' Binder" that is a comprehensive, current repository of relevant legal and constitutional material relating to the company. The table of contents of a typical board of Directors' Binder is reproduced in Appendix V at the end of this Chapter.

Directors require considerable ongoing support. While they should be interested in the company's affairs at all times, they should also be intensely focused on board or committee meetings and should not be engaged in the corporation's business on a day-to-day basis. As members of a collectivity, they are also not, generally, responsible for the leadership of the various tasks that must be undertaken. While board or committee chairs have a greater leadership role, they require professional support and ongoing attention. Such help is usually supplied through the management liaison to the board, usually the corporate secretary and/or the general counsel who have responsibility for implementing the board's legal obligations. In practice, significant reliance is placed on these individuals to organize the business of the board and its committees to establish an annual agenda that will permit matters to be addressed in a timely way and to recommend to appropriate members of the board initiatives that may be required by new legislation, best practices, or the evolving corporate governance environment. These individuals, who are employees of the corporation, have line responsibilities and report directly or indirectly to the CEO. They often find themselves in a difficult position because they are given competing responsibilities to management and the board, and often, to professional regulators, accountants or lawyers, and securities regulators, who may see them as gatekeepers responsible for the overall administration of securities regulation.

The board process needs to continually improve. Directors need to focus on how they can do their collective job better and on the nature of the contribution of particular directors. The existence of board and director evaluation processes is rated highly by governance observers, and it is recommended strongly by regulators. A well-run process can allow the board to identify which areas it wants to spend more of its time on (typically, strategy) and which areas it may be able to spend less time on. (For instance, it could reduce time spent on administrative matters through the use of well-constructed materials that are delivered on time, a consent agenda, or pre-framed resolutions.) The process may also identify constructive counselling that should be provided to particular directors or to directors in respect of whom succession is warranted. These are delicate matters, but the legal and interpersonal issues involved can be addressed by a careful and committed board.

IX. Director Compensation

Traditionally, directors were paid reasonably nominal compensation. Such compensation coincided with the apparent view that being a director was mostly an honourary position that required formal attendance at meetings four times a year and limited practical responsibility or

39 The costs of a public company, in particular, are substantial. Directors' compensation (see below) and support costs factor into the overall costs, and they have led to a rash of privatizations of smaller public companies, for which the costs do not justify the benefits of continuing to be public.

40 There is often a two-way benefit to involving directors on an informal, and more frequent basis. Directors have their reputations on the line for (typically) little compensation. They are therefore interested in the affairs of the company (why they serve), knowledgeable (by nature of their formal responsibilities), and (typically) expert in some specific aspect of the company's or board's operations (why they were recruited). They are, therefore, often excellent sounding boards for management and help to keep the directors up to date by testing their thoughts on them.


42 See Chapter 6, "The Use of Committees", for a fuller discussion of director evaluation processes.

liability. This view has changed dramatically over time with the fall-out from the corporate scandals discussed above.

As a consequence, compensation levels for directors have been rising. The issue now is to strike a correct balance on a number of points. First, directors must be compensated adequately for the time and effort they are expected to dedicate to their jobs and for the very significant liability risks that they assume. Directors do not expect to be paid at a rate similar to that charged for their services as executives, but most of them now expect meaningful compensation for meaningful input and exposure. However, directors and companies are aware of the need to keep remuneration in line so that directors retain their independence (in the sense of not becoming unduly dependent on their directors' compensation).

Secondly, boards and shareholders have attempted to compensate directors so that the interests of the directors are aligned with those of the shareholders. Such compensation was initially attempted through the granting to directors of stock options, which were believed to be a (cash) costless incentive for directors to improve shareholder value. Lately, some individuals have been questioning the wisdom of using stock options for this purpose. In general, stock options must now be expensed when granted as part of employment (including the employment of directors) remuneration. Of course, stock options also have an upside. Some observers believe that options create incentives for short-term, stock-enhancing behaviours, rather than a long-term view of what is ultimately in the best interests of shareholders. Accordingly, there has been some experimentation with a variety of long-term, director incentive arrangements, including the direct granting of shares and variations on that theme that either produce perceived better tax results or that tie the value of these incentives more to corporate performance, longer-term tenure, or the maintenance of stock positions by directors.  

Traditionally, directors' compensation consisted of an annual cash retainer, meeting fees, and some type of long-term incentive. In cases where this pattern is still maintained, all elements of the compensation package have increased significantly over the past few years. A number of studies track director compensation, and they can be used, along with executive compensation consultants, if required, to establish suitable compensation levels for particular boards. More recently, it is becoming an increasingly common practice to eliminate the meeting fee element of compensation. The theory behind this practice is that directors contribute at board and committee meetings but are also available to management between meetings and contribute in other important ways; therefore, they should be paid a single fee for their roles. Companies that adopt this compensation model tend to pay additional fees for committee service (although participation as a member of one committee may be considered to be part of the base retainer), and an additional retainer to the chairs of each of the standing committees. Payment for chairs tends to be graded, with a non-executive chair or lead director receiving the greatest amount, the chair of the audit committee receiving a substantial premium over committee members, and the chairs of corporate governance and human resources/compensation committees receiving lower amounts. Such a pay structure reflects the expected time commitment and responsibility involved.

Examples include deferred share units that produce tax benefits but require equity to be held through a director's entire tenure; restricted stock units that may "vest" on the basis of corporate performance, either in absolute terms or against a peer group; requirements to own stock in some multiple (typically three to five times) of the annual base director's retainer; and direct cash payments that are tied to corporate performance (as defined in various ways).
An express provision of the CBCA permits directors to vote on their own remuneration in their capacity as directors, despite the apparent conflict of interest.\textsuperscript{45} While the compensation of directors is usually a matter for the corporate governance or human resources/compensation committee in the first instance and ultimately, for the board, management tends to provide significant input into the process.

X. Self-Protection

Service on a board carries a significant risk. Directors' service carries risks of personal and collective criminal, regulatory, and civil liability, and a reputational risk (in the context of directors who, for whatever reason, are perceived to have failed in their duties). Chapter 18, in particular, deals at length with the various means by which directors can manage these risks. However, it bears noting here that part of a director's duty is to manage personal risk and the risk to the other directors, officers, and the corporation. While management, the general counsel or the corporate secretary, the corporate governance committee, the audit committee, or the human resources/compensation committee might take charge of certain elements of risk management, it is important that a director address his or her own mind to this issue.

A most significant matter for public companies is NP 58-201, which was approved by the CSA on April 15, 2005 and became effective on June 30, 2005. The policy, which is reproduced in Appendix VI at the end of this Chapter, reflects the considered view of securities regulators in the provinces of Alberta, British Columbia, and Ontario. In general, it is in keeping with the spirit and substance of corporate governance reform thinking over the past decade. This policy, combined with Form 58-101F1, which is reproduced as Appendix VII at the end of this Chapter, deals with corporate governance disclosure requirements, in effect, compliance with the best practices guidelines, or an explanation for how each matter recommended by the guideline is otherwise being addressed. These provisions, taken together, reflect the approach that has been taken generally in Canada to date, which is to rely on education and disclosure rather than on expressly required practices and procedures (other than those related to audit committees).

As will be apparent, the general obligations to manage or supervise the management of the business and affairs of the corporation, to act honestly and in good faith with a view to the best interests of the corporation, and to exercise the care, diligence, and skill that a reasonably prudent person would exercise in comparable circumstances, become complex when they are executed. The remainder of this book will attempt to address those complexities.

\textsuperscript{45} CBCA, s. 120(5)(a).
A P P E N D I X I

Board Mandate

The directors’ primary responsibility is to act in good faith and to exercise their business judgment in what they reasonably believe to be the best interests of the Corporation. In fulfilling its responsibilities, the Board is, among other matters, responsible for the following:

- Appointing the CEO and other corporate officers; On an ongoing basis, satisfying itself as to the integrity of the CEO and other executive officers and that the CEO and the other senior management create a culture of integrity throughout the Corporation;

- Monitoring and evaluating the performance of the CEO and the other senior management against the approved corporate goals and objectives;

- Succession planning (including the training of senior management);

- Adopting a strategic planning process;

- Approving an annual strategic plan which takes into account, among other things, the opportunities and risks of the business;

- Approving, on an annual basis, the corporate goals and objectives;

- Satisfying itself that the Corporation is pursuing a sound strategic direction in accordance with the approved corporate goals and objectives;

- Review with management, the Corporation's financial plans;

- Reviewing operating and financial performance results relative to established corporate goals and objectives;

- Ensuring that it understands the principal risks of the Corporation's business, and that appropriate systems to manage these risks are implemented;

- Ensuring that the materials and information provided by the Corporation to the Board and its committees are sufficient in their scope and content and in their timing to allow the Board and its committees to satisfy their duties and obligations;

---

46 Used by permission of Alliance Atlantis Communications Inc. and its general counsel, Andrea Wood, who was primarily responsible for management of the process by which it was developed.
- Reviewing and approving the Corporation's annual and interim financial statements and related management's discussion and analysis, annual information form, annual report and management proxy circular;

- Approving material acquisitions and divestitures;

- Overseeing the integrity of the Corporation's internal control and management information systems;

- Approving any securities issuances and repurchases by the Corporation;

- Declaring dividends;

- Approving the nomination of directors;

- Approving the charters of the Board committees and approving the appointment of directors to Board committees and the appointment of the Chairs of those committees;

- Adopting a communications policy for the Corporation (including ensuring the timeliness and integrity of communications to shareholders and establishing suitable mechanisms to receive shareholder views); and

- Developing the Corporation's approach to corporate governance, including developing a set of corporate governance principles and guidelines that are specifically applicable to the Corporation, or delegating these issues to a committee composed of a majority of independent directors and the balance being non-management directors.
Delegation of Authority

The purpose of this document is to articulate the delegation of decision making and operating authority within 724 Solutions Inc. between the Board of Directors and management.

Matters Requiring the Approval of The Board of Directors and/or Duly Authorized Committees of The Board of Directors:

1. Governance:

(a) the setting of strategic corporate direction, the establishment of corporate performance objectives;

(b) the approval of operational policies regarding the conduct of the business, including, but not limited to: acquisitions, research and development, sales and marketing, finance and investment, risk management, human resources, codes of conduct for employees, customer relationships, relationships with significant shareholders, and management and reporting information;

(c) any decision that will result in a material deviation from Board approved strategic, business or operational plans or policies;

(d) the establishment of effective procedures for monitoring corporate performance;

(e) on the recommendation of the Governance Committee, the establishment of effective procedures for reviewing the performance of the Chief Executive Officer and senior management;

(f) on the recommendation of the Governance Committee, the development of effective Board governance processes and procedures, including the establishment of Board Committees;

(g) any matter that requires the review and approval of any Committee of the Board of Directors under the terms of the respective Committee mandates, as may be amended from time-to-time, and appended to this delegation;

(h) the enactment, amendment, restatement or repeal of any By-laws;

(i) the approval of policies governing related party transactions;

(j) the Corporation's investor and public relations policies;

47 Used by permission of 724 Solutions Inc. and Ian Giffen, Chairman of the Board of 724 Solutions Inc.
(k) except pursuant to explicit delegated authority by the Board in accordance with the *Ontario Business Corporations Act*, the making of, directly or indirectly, loans or advances to, or the giving of security for or the guaranteeing of the debts of, or otherwise the giving of financial assistance to, any Person;

(l) except pursuant to explicit delegated authority by the Board in accordance with the *Ontario Business Corporations Act*, mortgage, hypothecate, pledge or otherwise create a security interest in all or any currently owned or subsequently acquired property, real or personal, movable or immovable of the Corporation, including book debts, rights, powers, franchises and undertakings, to secure any present or future indebtedness, liability or obligation of the Corporation;

(m) any decisions required to be made by the Board of Directors under the terms of the applicable legislation and regulations governing the Corporation, including the declaration and payment of dividends;

(n) fundamental changes in the way in which the Corporation is governed, including, but not limited to, structural changes in the organization of the Corporation;

(o) matters which may involve personal legal liability of individual directors;

(p) on the recommendation of the Corporate Governance Committee, the appointment and compensation of directors; and

(q) any other matter that in the opinion of the Chief Executive Officer, or the Chair of the Governance Committee, on the advice of external counsel to the Corporation, should be determined by the Board of Directors.

2. Finance and Operations:

(a) the approval of any multi-year or annual business, capital or operating plans or budgets for the Corporation, or any amendment thereto;

(b) any material deviation from the approved business, capital or operating plans or budgets;

(c) the terms and conditions of any public or private distribution of securities of the Corporation (except pursuant to any Board-approved stock option, share purchase or dividend re-investment plans);

(d) the purchase or redemption or issuance of any shares in the capital of the Corporation;

(e) the purchase, sale, mortgage or lease by the Corporation of any material real property; except for those involving commercial leases for office space and other real property transactions of a minor nature;

(f) on the recommendation of the Audit Committee, any change in the accounting policies or practices of the Corporation;
(g) the Corporation's investment and treasury management policies; (on an interim basis, the following delegation regarding strategic investments shall prevail):

(i) for investments under U.S. $1 million, provided the investee company will yield a relationship to be expected to have measurable benefit to the Company's core business (i.e., perhaps assist in the speed of roll-out of licenses or installation), management would have an independent ability to pursue these transactions;

(ii) for investments in excess of U.S. $1 million to and including U.S. $5 million, approval of the Corporate Governance Committee is required; and

(iii) for investments in excess of U.S. $5 million, there shall first be a detailed review of the proposed investment by the Corporate Governance Committee, prior to the matter going to the Board for its approval. The Corporate Governance Committee may then decide whether such approval can be obtained by written resolution accompanied by written material, or whether the formality of a Board meeting will be required.

(h) on the recommendation of the Audit Committee, the approval of any annual or interim quarterly financial statements of the Corporation;

(i) any purchase, commitment, lease or expenditure which, if completed, would raise the total of capital expenditures of the Corporation in any fiscal year to more than the dollar amount authorized pursuant to an approved business plan for any fiscal year;

(j) the authorization, execution or entering into by the Corporation of any contract or transaction (or series of related contracts or transactions), the performance of which will require the expenditure or result in an actual or contingent liability of the Corporation for an amount exceeding $________; 

(k) the entry by the Corporation into any line of business outside of the ordinary business as specified in the Board defined corporate policies; except for circumstances relating to a Board approved acquisition;

(l) any material contracts out of the ordinary course of business;

(m) any matter that presents a real or perceived material risk to the financial position of the Corporation; and

(n) acquisitions or divestitures that are:

- of strategic significance to the Corporation; or

- represent a material deviation from the ordinary course of business; or

- have the potential for jeopardizing the Corporation's ability to meet its ongoing service commitments; or
• the performance of which will require the expenditure or result in actual or contingent liability of the Corporation for an amount exceeding $_______.

The Chief Executive Officer:

The Chief Executive Officer is delegated the authority to supervise the business and affairs of the Corporation, subject to the direction of the Board of Directors and the execution limitations established by the Board. This delegation shall include the authority to make all decisions on behalf of the Corporation that do not require shareholder approval, or have not been reserved by the Board of Directors to itself or to a Committee of the Board, under the terms of this Delegation of Authority.

All Board authority delegated to management is delegated through the Chief Executive Officer, so that all authority and accountability of management, unless otherwise stated in this Delegation of Authority, is considered to be the authority and accountability of the Chief Executive Officer. This shall not be interpreted as precluding interaction between the members of the Board and senior management, and relates solely to the accountability link between the Board and the Chief Executive Officer.

The Chief Executive Officer shall have the authority to sub-delegate operational decision making as he or she may determine as necessary and appropriate for the effective operation of the business. In this regard, the Chief Executive Officer shall put in place a delegation of operational authority policy within the organization.
APPENDIX III

The Chair Of The Board

Accountability:

The Chair of the Board is accountable to the Board of Directors for the fulfillment of the responsibilities of the office of Chair as outlined in the Corporation's by-laws and will lead the Board in establishing effective corporate governance processes and practices.

Role/Responsibilities:

The role and responsibilities of the Chair of the Board will include:

- To assume principal responsibility for the operation and functioning of the Board of Directors

- To provide overall leadership to the Board without limiting the principle of collective responsibility and the ability of the Board to function as a unit

- Fulfilling his or her Board leadership responsibilities in a manner that will ensure that the Board is able to function independently of management. This should include ensuring that the appropriate procedures are in place for the Board to meet regularly without management present, and to allow for Directors to engage outside advisors at the expense of the Company in appropriate circumstances, subject to the approval of the Governance Committee

- Consulting with the Board and the Corporate Secretary to set board agendas that are based on the responsibilities of the Board and reflect current priorities

- Chairing Board meetings effectively, including ensuring that appropriate briefing materials are delivered in a timely fashion, encouraging full participation and discussion by individual Directors, stimulating debate, facilitating consensus, and ensuring that clarity regarding decisions is reached and duly recorded

- Ensuring compliance with the governance policies of the Board regarding conduct of board meetings, managing and reporting information and other policies related to the conduct of the Board's business

- Taking a leadership role in ensuring effective communication and relationships between the Corporation, shareholders, stakeholders and the general public

48 Used by permission of 724 Solutions Inc. and Ian Giffen, Chairman of the Board of 724 Solutions Inc.
APPENDIX IV

Lead Director

There will be a Lead Director as long as the Chairman is a member of management.

1. Provide Leadership to Enhance Board Effectiveness

   - The Lead Director shall be elected by the entire Board and shall be fully independent of management.
   - The Lead Director shall be entitled to request materials and receive notice of and attend all meetings of Committees.
   - The Lead Director shall have primary responsibility for:
     - Ensuring that the responsibilities of the Board are well understood by both the Board and management and the boundaries between the Board and management are clearly understood and respected;
     - Providing leadership to ensure the Board works in an independent, cohesive fashion;
     - Ensuring the Board has the requisite resources to support its work effectively;
     - Ensuring a process is in place to regularly assess the effectiveness of the Board, its committees and individual directors; and
     - Ensuring that a process is in place to monitor legislation and best practices which relate to the responsibilities of the Board.

2. The Lead Director Shall be Responsible for:

   - Consulting with the Chairman to set the agenda for Board meetings;
   - Ensuring Board leadership in times of crisis;
   - Where functions are delegated to Board committees, ensuring the functions are carried out as represented and results are reported to the Board;

---

49 Used by permission of Alliance Atlantis Communications Inc. and its general counsel, Andrea Wood.
• Chairing regular meetings of independent Board members without management present; and acting as liaison between the independent directors and the Chairman on sensitive issues; and

• Chairing Board meetings when the Chairman is not in attendance.

3. Acting as Liaison Between Board and Management

• The Lead Director shall work to ensure that the relationship between the Board and management is conducted in a professional and constructive manner. The Lead Director will work with the Chairman to ensure the conduct of Board meetings provides adequate time for serious discussion of appropriate issues and that appropriate information is made available to Board members on a timely basis.

This description will be revised from time to time.
APPENDIX V

Directors' Binder

I. Corporate Information

(1) 2005 Annual Information Form
(2) 2005 Annual Report and MD & A
(3) 2005 Management Information Circular
(4) Articles & By-Laws
(5) Corporate Chart
(6) Executive Management Chart

II. Board Policies

(8) Charter of Expectations
(9) Disclosure Policy and Disclosure Committee Terms of Reference
(10) Confidentiality and Insider Trading Policy
(11) Insider Trading Report and Memo Regarding New Procedures
(12) Insider Reports filed on your behalf (to be inserted as filed)
(13) Whistleblower Policy
(14) Code of Conduct

---

50 Used by permission of Alliance Atlantis Communications Inc. and its general counsel, Andrea Wood.
III. Corporate Policies

(15) Corporate Commitment Policy

(16) Payment Approval Policy

(17) Privacy Code

(18) Other Policies (to be inserted as approved)

- Workplace Harassment Policy

IV. Board and Committee Information

(19) Directors' Contact List

(20) Directors' Bios

(21) Senior Management Contact List

(22) Board/Committee 2006 Meeting Schedule

(23) Board of Directors

I. List of Directors

II. Board Mandate

III. Lead Director Mandate

IV. 2006 Minutes

(24) Executive Committee

I. Chair and Member List

II. Terms of Reference

III. Chair Description

IV. 2006 Agenda Outline

(25) Audit Committee

I. Chair and Member List

II. Terms of Reference
III. Chair Description

IV. 2006 Agenda Outline

V. 2006 Minutes

(26) Human Resources and Compensation Committee

I. Chair and Member List

II. Terms of Reference

III. Chair Description

IV. 2006 Agenda Outline

V. 2006 Minutes

(27) Corporate Governance and Nominating Committee

I. Chair and Member List

II. Terms of Reference

III. Chair Description

IV. 2006 Agenda Outline

V. 2006 Minutes

NOTE: (28) and (29) do not appear related to IV Board and Committee Information

(28) Directors' and Officers' Insurance

I. Policy

II. Extension

(29) Directors Indemnification Agreement

V. Compensation Information

(30) Directors' Share Ownership Memo

(31) Share Compensation Plan

(32) Deferred Share Units

I. DSU Plan
II. Notice of Redemption

III. Election Form

IV. Your 2006 Election Form

(33) Restricted Share Unit Plan

(34) PSAP

(35) 2006 Compensation Statements (to be inserted as received)

VI. Other

(36) Analyst Contact List
National Policy 58-201 Corporate Governance Guidelines

Part 1—Purpose and Application

1.1 Purpose of this Policy—This Policy 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;
- be sensitive to the realities of the greater numbers of small companies and controlled companies in the Canadian corporate landscape;
- take into account the impact of corporate governance developments in the U.S. and around the world; and
- recognize that corporate governance is evolving.

The guidelines in this Policy are not intended to be prescriptive. We encourage issuers to consider the guidelines in developing their own corporate governance practices.

We do, however, understand that some parties have concerns about how this Policy and National Instrument 58-101 Disclosure of Corporate Governance Practices affect controlled companies. Accordingly, we intend, over the next year, to carefully consider these concerns in the context of a study to examine the governance of controlled companies. We will consult market participants in conducting the study. After completing the study, we will consider whether to change how this Policy and National Instrument 58-101 treat controlled companies.

1.2 Application—This Policy applies to all reporting issuers, other than investment funds. Consequently, it applies to both corporate and non-corporate entities. Reference to a particular corporate characteristic, such as a board of directors (the board), includes any equivalent characteristic of a non-corporate entity. For example, in the case of a limited partnership, we recommend that a majority of the directors of the general partner should be independent of the limited partnership (including the general partner).

Income trust issuers should, in applying these guidelines, recognize 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. For this purpose, references to "the issuer" refer to both the trust and any underlying entities, including the operating entity.
Part 2—Meaning of Independence

2.1 Meaning of Independence—For the purposes of this Policy, a director is independent if he or she would be independent for the purposes of National Instrument 58-101 Disclosure of Corporate Governance Practices.

Part 3—Corporate Governance Guidelines

Composition of the Board

3.1 The board should have a majority of independent directors.

3.2 The chair of the board should be an independent director. Where this is not appropriate, an independent director should be appointed to act as "lead director". However, either an independent chair or an independent lead director should act as the effective leader of the board and ensure that the board's agenda will enable it to successfully carry out its duties.

Meetings of Independent Directors

3.3 The independent directors should hold regularly scheduled meetings at which non-independent directors and members of management are not in attendance.

Board Mandate

3.4 The board should adopt a written mandate in which it explicitly acknowledges responsibility for the stewardship of the issuer, including responsibility for:

- to the extent feasible, satisfying itself as to the integrity of the chief executive officer (the CEO) and other executive officers and that the CEO and other executive officers create a culture of integrity throughout the organization;
- adopting a strategic planning process and approving, on at least an annual basis, a strategic plan which takes into account, among other things, the opportunities and risks of the business;
- the identification of the principal risks of the issuer's business, and ensuring the implementation of appropriate systems to manage these risks;
- succession planning (including appointing, training and monitoring senior management);
- adopting a communication policy for the issuer;
- the issuer's internal control and management information systems; and
(g) developing the issuer's approach to corporate governance, including developing a set of corporate governance principles and guidelines that are specifically applicable to the issuer.  

The written mandate of the board should also set out:

(i) measures for receiving feedback from stakeholders (e.g., the board may wish to establish a process to permit stakeholders to directly contact the independent directors), and

(ii) expectations and responsibilities of directors, including basic duties and responsibilities with respect to attendance at board meetings and advance review of meeting materials.

In developing an effective communication policy for the issuer, issuers should refer to the guidance set out in National Policy 51-201 Disclosure Standards.

For purposes of this Policy, "executive officer" has the same meaning as in National Instrument 51-102 Continuous Disclosure Obligations.

Position Descriptions

3.5 The board should develop clear position descriptions for the chair of the board and the chair of each board committee. In addition, the board, together with the CEO, should develop a clear position description for the CEO, which includes delineating management's responsibilities. The board should also develop or approve the corporate goals and objectives that the CEO is responsible for meeting.

Orientation and Continuing Education

3.6 The board should ensure that all new directors receive a comprehensive orientation. All new directors should fully understand the role of the board and its committees, as well as the contribution individual directors are expected to make (including, in particular, the commitment of time and resources that the issuer expects from its directors). All new directors should also understand the nature and operation of the issuer's business.

3.7 The board should provide continuing education opportunities for all directors, so that individuals may maintain or enhance their skills and abilities as directors, as well as to ensure their knowledge and understanding of the issuer's business remains current.

---

51 Issuers may consider appointing a corporate governance committee to consider these issues. A corporate governance committee should have a majority of independent directors, with the remaining members being "non-management" directors.
Code of Business Conduct and Ethics

3.8 The board should adopt a written code of business conduct and ethics (a code). The code should be applicable to directors, officers and employees of the issuer. The code should constitute written standards that are reasonably designed to promote integrity and to deter wrongdoing. In particular, it should address the following issues:

(a) conflicts of interest, including transactions and agreements in respect of which a director or executive officer has a material interest;

(b) protection and proper use of corporate assets and opportunities;

(c) confidentiality of corporate information;

(d) fair dealing with the issuer's security holders, customers, suppliers, competitors and employees;

(e) compliance with laws, rules and regulations; and

(f) reporting of any illegal or unethical behaviour.

3.9 The board should be responsible for monitoring compliance with the code. Any waivers from the code that are granted for the benefit of the issuer's directors or executive officers should be granted by the board (or a board committee) only.

Although issuers must exercise their own judgement in making materiality determinations, the Canadian securities regulatory authorities consider that conduct by a director or executive officer which constitutes a material departure from the code will likely constitute a "material change" within the meaning of National Instrument 51-102 Continuous Disclosure Obligations. National Instrument 51-102 requires every material change report to include a full description of the material change. Where a material departure from the code constitutes a material change to the issuer, we expect that the material change report will disclose, among other things:

- the date of the departure(s),
- the party(ies) involved in the departure(s),
- the reason why the board has or has not sanctioned the departure(s), and
- any measures the board has taken to address or remedy the departure(s).

Nomination of Directors

3.10 The board should appoint a nominating committee composed entirely of independent directors.

3.11 The nominating committee should have a written charter that clearly establishes the committee's purpose, responsibilities, member qualifications, member appointment and removal, structure and operations (including any authority to delegate to individual members and
subcommittees), and manner of reporting to the board. In addition, the nominating committee should be given authority to engage and compensate any outside advisor that it determines to be necessary to permit it to carry out its duties. If an issuer is legally required by contract or otherwise to provide third parties with the right to nominate directors, the selection and nomination of those directors need not involve the approval of an independent nominating committee.

3.12 Prior to nominating or appointing individuals as directors, the board should adopt a process involving the following steps:

(A) Consider what competencies and skills the board, as a whole, should possess. In doing so, the board should recognize that the particular competencies and skills required for one issuer may not be the same as those required for another.

(B) Assess what competencies and skills each existing director possesses. It is unlikely that any one director will have all the competencies and skills required by the board. Instead, the board should be considered as a group, with each individual making his or her own contribution. Attention should also be paid to the personality and other qualities of each director, as these may ultimately determine the boardroom dynamic.

The board should also consider the appropriate size of the board, with a view to facilitating effective decision-making.

In carrying out each of these functions, the board should consider the advice and input of the nominating committee.

3.13 The nominating committee should be responsible for identifying individuals qualified to become new board members and recommending to the board the new director nominees for the next annual meeting of shareholders.

3.14 In making its recommendations, the nominating committee should consider:

(a) the competencies and skills that the board considers to be necessary for the board, as a whole, to possess;

(b) the competencies and skills that the board considers each existing director to possess; and

(c) the competencies and skills each new nominee will bring to the boardroom.

The nominating committee should also consider whether or not each new nominee can devote sufficient time and resources to his or her duties as a board member.

Compensation

3.15 The board should appoint a compensation committee composed entirely of independent directors.
3.16 The compensation committee should have a written charter that establishes the committee's purpose, responsibilities, member qualifications, member appointment and removal, structure and operations (including any authority to delegate to individual members or subcommittees), and the manner of reporting to the board. In addition, the compensation committee should be given authority to engage and compensate any outside advisor that it determines to be necessary to permit it to carry out its duties.

3.17 The compensation committee should be responsible for:

(a) reviewing and approving corporate goals and objectives relevant to CEO compensation, evaluating the CEO's performance in light of those corporate goals and objectives, and determining (or making recommendations to the board with respect to) the CEO's compensation level based on this evaluation;

(b) making recommendations to the board with respect to non-CEO officer and director compensation, incentive-compensation plans and equity-based plans; and

(c) reviewing executive compensation disclosure before the issuer publicly discloses this information.

Regular Board Assessments

3.18 The board, its committees and each individual director should be regularly assessed regarding his, her or its effectiveness and contribution. An assessment should consider

(a) in the case of the board or a board committee, its mandate or charter, and

(b) in the case of an individual director, the applicable position description(s), as well as the competencies and skills each individual director is expected to bring to the board.
APPENDIX VII


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.