Lang Michener LLP
Lawyers – Patent & Trade Mark Agents

BCE Place, 181 Bay Street, Suite 2500
P.O. Box 747
Toronto ON M5J 2T7
Canada

Telephone: 416-360-8600
Facsimile: 416-365-1719

Reply to:
Philippe Tardif
Direct dial: 416-307-4085
Direct fax: 416-304-3761
ptardif@langmichener.ca

January 27, 2005

Alberta Securities Commission
Saskatchewan Financial Services Commission
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Nova Scotia Securities Commission
New Brunswick Securities Commission
Office of the Attorney General, Prince Edward Island
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Government of Yukon
Registrar of Securities, Department of Justice, Government of the Northwest Territories
Registrar of Securities, Legal Registries Division, Department of Justice,
Government of Nunavut
c/o John Stevenson, Secretary
Ontario Securities Commission
Suite 800
20 Queen Street West
Toronto, ON M5H 3S8

- and to -

Anne-Marie Beaudoin
Directrice du secrétariat
Autorité des marchés financiers
Tour de la Bourse
800, square Victoria
C.P. 246, 22^{e} étage
Montréal, Québec H4Z 1G3

Dear Sirs and Mesdames:

Re: Proposed Amendments to Multilateral Instrument 52-110 ("Proposed MI 52-110") – *Audit Committees* – Request for Comments

I am writing in response to the request for comment on Proposed MI 52-110 dated October 29, 2004. I have limited my comments to one aspect of the meaning of director independence in section 1.4 of Proposed MI 52-110 as incorporated into the definition of director independence in

subsection 1.2(1) of Proposed National Instrument 58-101 – *Disclosure of Corporate Governance Practices* ("Proposed NI 58-101"). In particular, I submit for the reasons noted below that the reference to "parent" in subsection 1.4(8) of Proposed MI 52-110 is not appropriate.

Background

1. The Corporate Governance Practices contained in draft National Policy 58-201-*Corporate Governance Guidelines* ("Proposed NP 58-201") provide in section 3.1 that "The board should have a majority of independent directors" and in section 3.2 that "the chair of the board should be an independent director." Section 2.1 of Proposed NP 58-201 states that "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*".

2. Proposed NI 58-101 provides in subsection 1.2(1) that "Except in British Columbia, a director is independent if he or she would be independent within the meaning of section 1.4 of Multilateral Instrument 52-110 *Audit Committees*".

3. The annual disclosure prescribed by section 2.1 of Proposed NI 58-101 (by reference to item 1(c) of Form 58-101F1) requires issuers to "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 judgment in carrying out its responsibilities". Proposed NI 58-101 (by reference to item 1(f) of Form 58-101 F1 also requires issuers to "Disclose whether or not the chair of the board is an independent director (…) 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."

4. Subsection 1.4(8) of Proposed MI 52-110 provides that "for the purposes of section 1.4, an issuer includes a subsidiary entity of the issuer and a parent of the issuer". The term "parent" is not defined in MI 52-110, the *Securities Act* (Ontario), the *Business Corporations* (Ontario) or the *Canada Business Corporations Act.* A plain meaning of the term "parent" may lead to the conclusion that a person or an entity which controls a majority of the voting rights of an issuer is considered to be a "parent".

5. Subsection 1.4(1) of Proposed MI 52-110 provides that "an audit committee member is independent if he or she has no direct or indirect material relationship with the issuer". Subsections 1.4(3) to (7) of Proposed MI 52-110 describe a number of individuals who are considered to have a "material relationship" with an issuer (to which I refer as "prescribed relationships").

6. As a result of the deeming provisions in subsection 1.4(8) of Proposed MI 52-110, an individual who has any one of the relationships referred to in subsection 1.4(3) to (7) of Proposed MI 52-110 with a parent, is deemed to have a material relationship with the

issuer and therefore not to be independent for the purposes of section 1.4 of Proposed MI 52-110, Proposed NP 58-201 and Proposed NI 58-101. Accordingly, individuals who have any prescribed relationship with a parent will be (i) precluded from being members of an audit committee of the issuers, and (ii) will be considered not to be independent for the purposes of Proposed NI 58-101 and Proposed NP 58-201. It is its second aspect of the inclusion of the deeming provisions in subsection 1.4(8) of Proposed MI 52-110 which is the focus of my letter.

7. Paragraph 1.5(1)(b) of Proposed MI 52-110 (which reflects the current requirements of paragraph 1.4(3)(g) of the provisions of Multilateral Instrument 52-110 ("MI 52-110") currently in force) provides that an individual who is an affiliated entity of the issuer or any of its subsidiary entities is considered to have a material relationship with the issuer. An affiliated entity is defined in MI 52-110 as follows:

"For the purposes of this Instrument, a person or company is considered to be an affiliated entity of another person or company if

(a) one of them controls or is controlled by the other or if both persons or companies are controlled by the same person or company, or

(b) the person or company is

(i) both a director and an employee of an affiliated entity, or

(ii) an executive officer, general partner or managing member of an affiliated entity."

8. Accordingly, as a result of the definitions in MI 52-110 currently in force, an officer of an affiliated entity is only deemed to have a prescribed relationship for the purpose of determining eligibility for membership on an audit committee.

9. The following provisions of section 303A of the New York Stock Exchange Rules (and accompanying commentary) are relevant:

"1. Listed companies must have a majority of independent directors.

2. In order to tighten the definition of "independent director" for purposes of these standards:

(a) No director qualifies as "independent" unless the board of directors affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company).

Commentary: It is not possible to anticipate, or explicitly to provide for, all circumstances that might signal potential conflicts of interest, or that might bear on the materiality of a director's relationship to a listed company (references to "company" would include any parent or subsidiary in a consolidated group with the company)(...) However, as the concern is independence from management, the Exchange does not view ownership of even a significant amount of stock, by itself, as a ban to an independence finding."

10. The following sections of Rules 4350(c) and 4200(a)(15) of the NASDAQ (and accompanying commentary) are also relevant:

> 4350(c)(1) "A majority of the board of directors must be comprised of independent directors as defined in Rule 4200…"
>
> 4200(a)(15) "Independent director" means a person other than an officer or employee of the company or its subsidiaries or any other individual having a relationship, which, in the opinion of the company's board of directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. The following persons shall not be considered independent:
>
> > (A) a director who is, or at any time during the past three years was, employed by the company or by any parent or subsidiary of the company.
>
> Commentary: (…) The rule's reference to a "parent or subsidiary" is intended to cover entities the issuer controls and consolidates with the issuer's financial statements as filed with the U.S. Securities and Exchange Commission (but not if the issuer reflects such entity solely as an investment in its financial statements).

11. Controlled companies (defined companies of which more than 50% of the voting power is held by an individual, a group or another company) are stated to be exempt from the NYSE (section 303A) and NASDAQ (Rule 4350(c)) provisions requiring the board be comprised of a majority of independent directors.

12. The rules of the Toronto Stock Exchange (section 474 of the TSX Company Manual) provide as follows with respect to the definition of an unrelated director**:** "An unrelated director is a director who is independent of management and is free from any interest and any business or other relationship which could, or could reasonably be perceived to, materially interfere with the director's ability to act with a view to the best interests of the corporation, other than interests and relationships arising from shareholding."

13. Section 3.1 of proposed amendments to Companion Policy 52-110 CP states:

> "Although shareholding alone may not interfere with the exercise of a director's independent judgment, we believe that other relationships between an issuer and a

shareholder may constitute material relationships with the issuer, and should be considered by the board when determining a director's independence. However, only those relationships which could, in the view of the issuer's board of directors, be reasonably expected to interfere with the exercise of a member's independent judgment should be considered material relationships within the meaning of section 1.4."

14. Neither Proposed NP 58-201 or Proposed NI 58-101 provide an exception from the board independence (or independent chair) provisions for controlled companies.

Submissions

I submit that the reference to "parent" in subsection 1.4(8) of Proposed MI 52-110 is not appropriate for the reasons noted below:

(i) Although the guideline of Proposed Policy 58-101 with respect to the majority of a board being independent are not mandatory, a departure from such guideline imposes an burden on an issuer whose controlling shareholder believes it is entitled to proportionate representation on the board of directors. In order to comply with the provisions of the Proposed Policy 58-201 that a majority of directors of an issuer be independent, a controlling shareholder loses its right to representation in the board of directors proportionate to its voting interests.

(ii) Absent a prescribed relationship, executive officers of a controlling shareholder should not be considered to have a material relationship which results in such individuals not being independent for the purposes of board membership or the purposes of acting as chair. The interests of a controlling shareholder are generally aligned with those of other shareholders.

(iii) A controlling shareholder (or its representative) would be discouraged from being appointed chair notwithstanding that it has no relationship to the issuer other than its shareholdings.

(iv) The inclusion of the reference to "parent" in section 1.4 of MI 52-110 is inconsistent with the reference in Proposed Policy 58-201, the TSX Rules and the NYSE commentary to its rules that shareholdings alone may not constitute a material relationship which results in the interests of a controlling shareholder not being aligned with those of shareholders.

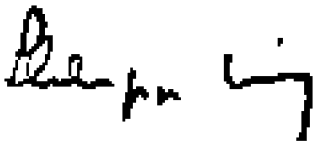
(v) Such an approach is inconsistent with the approach of the NYSE and NASDAQ to exclude "controlled companies" from the requirement to have a majority of independent directors.

I would urge the Canadian Securities Administrators to reconsider the deeming provisions relating to a "parent." One alternative would be to provide an exemption for controlled

companies similar to that available under the NYSE and NASDAQ rules. Should the Canadian Securities Administrators determine that the current draft accurately reflects the intent of MI 52-110, I submit that a separate comment period be initiated in respect of the above where comments would be sought as to whether representatives of a controlling shareholders should be considered not independent for the purposes of membership on the board and appointment as chair (absent any other prescribed relationship).

The above is respectfully submitted in my personal capacity and represent my views and not necessarily those of this firm.

Yours truly,



Philippe Tardif
PT/fl
Encl.