



Canadian Foundation *for*  
Advancement *of* Investor Rights  
Fondation canadienne *pour* l'avancement  
*des* droits *des* investisseurs

January 29, 2018

British Columbia Securities Commission  
Alberta Securities Commission  
Financial and Consumer Affairs Authority of Saskatchewan  
The Manitoba Securities Commission  
Ontario Securities Commission  
Autorité des marchés financiers  
Financial and Consumer Services Commission, New Brunswick  
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island  
Nova Scotia Securities Commission  
Superintendent of Securities, Newfoundland and Labrador  
Superintendent of Securities, Northwest Territories  
Superintendent of Securities, Yukon  
Superintendent of Securities, Nunavut

The Secretary  
Ontario Securities Commission  
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22<sup>nd</sup> Floor  
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Sent via e-mail to: [comments@osc.gov.on.ca](mailto:comments@osc.gov.on.ca)

**RE: Canadian Securities Administrators (“CSA”) Request for Comment on Consultation Paper 52-404  
*Approach to Director and Audit Committee Member Independence***

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FAIR Canada is pleased to offer comments in response to the CSA Request for Comment on Consultation Paper 52-404 *Approach to Director and Audit Committee Member Independence* (“Consultation Paper”).

FAIR Canada is a national, charitable organization dedicated to putting investors first. As a voice for Canadian investors, FAIR Canada is committed to advocating for stronger investor protections in securities regulation. Visit [www.faircanada.ca](http://www.faircanada.ca) for more information.

## **1. General Comments**

- 1.1. FAIR Canada supports the CSA’s current approach to determining director and audit committee member independence, which strikes an appropriate balance between prescriptive and principles based elements. Lessening or eliminating the bright-line tests that have been used for

over a decade to assess director and audit committee member independence would be a step backward and lead to less investor confidence in the capital markets.

### ***Rationale for Keeping the Current Approach to Determining Independence***

- 1.2. While assessing the merits of possibly moving to more of a principles based approach, it is important not to lose sight of the rationale behind the current provisions, which were established over a decade ago. After numerous financial reporting scandals in the United States, Canadian securities regulators found it necessary to address investor concerns regarding the capital markets. In particular, the motivating factors appeared to include the closely integrated nature of Canada's capital markets with the United States, and the move by U.S. exchanges to balance a principles based approach to director independence with bright-line tests. These conditions have not changed in the last decade, while the need to ensure that independence of directors and audit committee members is appropriately assessed, remains extremely important.
- 1.3. There are two primary reasons FAIR Canada believes the CSA's current approach is effective. First, it strikes the right balance between subjective guidelines and prescriptive bright-line tests. The bright-line tests serve the purpose of setting clear, minimum requirements that preclude a director from being considered independent or serving as an independent audit committee member. The bright-line tests ultimately ensure the presence of appropriate governance practices related to determining independence and that investors clearly understand the reasons a director may be classified as independent.
- 1.4. Second, the CSA's current approach provides predictability. With Canada's capital markets connected closely to the United States – along with many issuers being cross-listed in Canada and the United States – it makes sense that the regime governing board independence should mirror the independence regime in the United States, particularly considering the context behind these rules. Furthermore, the current approach is more predictable for investors as they do not have to consider starkly different approaches to independence, which could result if issuers had to make independence assessments on more of a principles (and subjective) basis, when deciding who to invest with.
- 1.5. Investors and issuers have both adapted to the current approach to independence, which have been in place for over a decade. It does not make sense to change the approach so that the rules are not only loosened but are entirely unfamiliar and unpredictable to investors.

### ***Potential Changes within the Current Approach***

#### *Augment and Enhance the Current Approach*

- 1.6. Any changes to the rules should be *within* the current approach and augment the current prescriptive and principles based rules in place. For example, it would be helpful to have additional guidance making it clear that the rules and guidelines are minimum requirements, and not an exhaustive list. While the bright-line test captures the most obvious ways to determine whether or not a director is independent, the guidance could highlight that other

relationships and interests not captured in the bright-line test may also prevent determinations of independence. The tendency should not be that issuers limit their assessments to the bright-line test, to the detriment of other situations that could hinder a director's independence. Such guidance could lead to a more fulsome analysis of whether a given director is independent in light of all the facts and circumstances.

#### *Improve Governance of Venture Issuers*

- 1.7. Another potential change for the current regime is to require that the majority of audit committee members and directors of venture issuers also be "independent" as defined by NI 52-110, or another suitable definition. This would increase the governance standard for venture issuers which would be appropriate given that retail investors are exposed to higher risk investments. Such standards would increase governance standards for venture issuers and thereby increase confidence in this area of our capital markets.

#### *Urgent Need to Improve Governance of Group Scholarship Plan Trusts*

- 1.8. FAIR Canada urges the CSA to improve the governance structure of group scholarship trusts and apply its current approach to independence to the governance of Group Scholarship Plans. FAIR Canada strongly recommends there be a requirement that the majority of the board of a group scholarship trust should not have a financial interest in the distributor and meet the test of independence.
- 1.9. The federal government released a report almost a decade ago - in August, 2008 - entitled "Registered Education Savings Plan Industry Practices: Report prepared for Human Resources and Social Development Canada by Infometrica Limited, Final Report" ("Federal Report")<sup>1</sup>, which highlighted its concern with the governance structures of group scholarship trusts and noted that at two of the five trusts the majority of the board had a financial interest in the distributor (either a senior employee of the distributor or a shareholder of the distributor, or both). A 2014 Ontario Securities Commission enforcement proceeding highlighted the poor corporate governance practices and the extent of related party transactions amongst the related entities.<sup>2</sup> In addition, four out of five group scholarship plan dealers were the subject of public interest orders requiring the use of an independent monitor as a result of serious compliance issues.
- 1.10. FAIR Canada notes that those who invest in group scholarship plans are amongst the most vulnerable financial consumers, have low or modest income, low financial literacy, and who sometimes do not have the literacy skills to read the official disclosure documents and instead rely on the multi-language marketing materials produced by these firms.

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<sup>1</sup> Available online: <[http://publications.gc.ca/collections/collection\\_2009/rhdcc-hrsdc/HS4-55-2008E.pdf](http://publications.gc.ca/collections/collection_2009/rhdcc-hrsdc/HS4-55-2008E.pdf)>.

<sup>2</sup> See Settlement Agreement between OSC Staff and Issam El-Bouji, Global Resp Corporation, Global Growth Assets Inc., Global Educational Trust Foundation and Margaret Singh, online: <[http://www.osc.gov.on.ca/documents/en/Proceedings-SOA/soa\\_20140414\\_el-bouji.pdf](http://www.osc.gov.on.ca/documents/en/Proceedings-SOA/soa_20140414_el-bouji.pdf)> and Order in the Matter of Issam El-Bouji, Global Resp Corporation, Global Growth Assets Inc., Global Educational Trust Foundation and Margaret Singh, online: <[http://www.osc.gov.on.ca/documents/en/Proceedings-RAD/rad\\_20140416\\_el-bouji.pdf](http://www.osc.gov.on.ca/documents/en/Proceedings-RAD/rad_20140416_el-bouji.pdf)>.

- 1.11. FAIR Canada urges the CSA to require adequate standards of corporate governance of group scholarship plans including that a majority of the board of directors of the scholarship plan trust or foundation be independent directors.

## 2. Responses to Specific Questions

### Question 1:

- a. *Do you consider our approach appropriate for all issuers in the Canadian market? Please explain why or why not?*

FAIR Canada considers the CSA's approach appropriate; however, we would like to see the CSA's current approach extended to venture issuers. Our reasons for believing that the CSA's approach is appropriate, and for this approach to be extended to venture issuers is outlined above. We would also like to see it extended to group scholarship trusts or foundations.

- b. *In your view, what are the benefits or limitations of our approach to determining independence? Please explain.*

As we mentioned above, the benefits of the CSA's current approach consist of setting clear, minimum requirements that preclude a director from being considered independent or serving as an independent audit committee member. The approach also provides predictability for investors and issuers.

Limitations to the approach includes the absence of more guidance making it clear that the rules and guidelines are minimum requirements, and not an exhaustive list.

- c. *Do you believe that our approach strikes an appropriate balance in terms of:*
- i. *the restrictions it imposes on issuers' boards in exercising their discretion in making independence determinations, and*
  - ii. *the certainty it provides boards in making those determinations and the consistency and predictability it provides other stakeholders in evaluating the independence of an issuer's directors or audit committee members?*

We believe that the CSA achieves an appropriate balance with respect to these issues, particularly in light of the predictability it provides investors to assess director or audit committee member independence.

### Question 2:

*Should we consider making any changes to our approach to determining independence as prescribed in NI 52-110, such as changes to:*

a. *the definition of independence;*

FAIR Canada favours more emphasis on the *principles* behind director and audit committee member independence, rather than simply what does and does not constitute independence. As we stated earlier, it should be clear that the bright-line tests for independence are just minimum requirements. The definition of independence should be worded in a way that more clearly emphasizes the broader conceptions of independence.

b. *the bright-line tests for directors and audit committee members; or*

FAIR Canada does not believe that any changes need to be made to the bright-line tests for directors and audit committee members.

c. *the exemptions to the requirement that every audit committee member be independence?*

FAIR Canada does not recommend any changes to the requirement that every audit committee member be independent.

*Question 3:*

*What are the advantages and disadvantages of maintaining our approach to determining independence versus replacing it with an alternative approach?*

Please see our comments above, which outline the advantages of maintaining the current approach to determining independence.

We thank you for the opportunity to provide our comments and views in this submission. We welcome its public posting and would be pleased to discuss this letter with you at your convenience. Feel free to contact Frank Allen at [647-256-6693](tel:647-256-6693)/[frank.allen@faircanada.ca](mailto:frank.allen@faircanada.ca), Marian Passmore at [647-256-6691](tel:647-256-6691)/[marian.passmore@faircanada.ca](mailto:marian.passmore@faircanada.ca) or Samreen Beg at [647-256-6692](tel:647-256-6692)/[samreen.beg@faircanada.ca](mailto:samreen.beg@faircanada.ca).

Sincerely,



Canadian Foundation for Advancement of Investor Rights