

September 7, 2020

Mr. Walled Soliman  
Taskforce Chair  
Ontario Capital Markets Modernization Taskforce  
Submitted via email

Re: Ontario Capital Markets Modernization Taskforce initial consultation report

Dear Mr. Soliman,

The Principles for Responsible Investment (“PRI”) welcomes the opportunity to respond to the Ontario Capital Markets Modernization Taskforce initial consultation report.

## ABOUT THE PRI

The PRI is the world’s leading initiative on responsible investment.<sup>1</sup> It works to understand the investment implications of environmental, social, and governance (ESG) factors and support its international network of 3,000 investor signatories in incorporating these factors into their investment and ownership decisions. Launched in New York in 2006, the PRI’s signatories manage over \$100 trillion in AUM.<sup>2</sup> 171 Canadian investment managers, asset owners and service providers are PRI signatories.<sup>3</sup>

The Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice.<sup>4</sup> The Principles that signatories set out to achieve include incorporation of ESG issues into investment analysis and decision-making processes; engagement with companies around ESG factors; and seeking issuer disclosure on ESG factors. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system. They have attracted a global signatory base representing a majority of the world’s professionally managed investments.

Signatories to the PRI aim to integrate all financially material factors, including ESG factors, into their investment processes. This is a risk management strategy, as evidence shows factors such as climate change and human capital management have a material economic impact on asset prices, especially when taking into account the risks that long-term, universal investors like pension plans

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<sup>1</sup> Principles for Responsible Investment (the PRI), What are the Principles of Responsible Investment? available at: <https://www.unpri.org/pri/an-introduction-to-responsible-investment/what-are-the-principles-for-responsible-investment> .

<sup>2</sup> As of March 30, 2020.

<sup>3</sup> As of September 1, 2020.

<sup>4</sup> Principles for Responsible Investment (The PRI), About the PRI available at: <https://www.unpri.org/pri/aboutthe-pri>.

face. Therefore, the PRI will focus our comments on the recommendations that propose to improve the incorporation and disclosure of ESG factors.

## SUMMARY

The PRI commends the Taskforce in their efforts to improve capital markets regulations for Canadians.

The PRI supports the Taskforce's efforts to improve disclosure on material ESG information, executive compensation, corporate board diversity and increase transparency for investors around conflicts of interest that may arise from proxy advisory firms (PAFs) consulting services.

The PRI recommends the Taskforce remove the recommendations that would allow issuers to rebut PAF reports and create a process for the OSC to issue no-action letters.

## COMMENTS ON RECOMMENDATIONS

### Recommendation 19: Improve corporate board diversity

The PRI supports the recommendation to improve corporate board diversity and recommends expanding on the current OSC and Canada Business Corporations Act (CBCA) disclosure requirements, with a focus on increasing Black and Indigenous representation, and supports the proposal to extend this requirement to all issuers. The PRI recommends the Taskforce require:

- TSX-listed companies to establish and disclose policies to improve corporate board diversity, and review policies annually;<sup>5</sup>
- TSX-listed companies to set targets to achieve corporate board diversity and report on progress annually, with a comply or explain provision if their targets are below the thresholds suggested in the recommendations (40% for women and 20% for BIPOC);<sup>6</sup>
- The OSC to set policies and disclose progress on board and executive-level diversity using the metrics and targets required of issuers; and
- The OSC to set minimum quotas for TSX-listed companies for race and gender diversity.<sup>7</sup>

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<sup>5</sup> Sir John Parker and The Parker Review Committee, Ethnic Diversity Enriching Business Leadership: An update report from The Parker Review (February 5, 2020) available at: [https://assets.ey.com/content/dam/ey-sites/ey-com/en\\_uk/news/2020/02/ey-parker-review-2020-report-final.pdf](https://assets.ey.com/content/dam/ey-sites/ey-com/en_uk/news/2020/02/ey-parker-review-2020-report-final.pdf). One resource with criteria that could be referenced when developing corporate board diversity policies. For example, the Parker Review recommends policies that consider the whole cycle of recruitment, retention, development and promotion of diverse candidates within the organization for senior leadership and board candidates.

<sup>6</sup> Adams, Renée B. and Kirchmaier, Tom, Barriers to Boardrooms (June 22, 2015) ECGI - Finance Working Paper No. 347/2013, Asian Finance Association (AsFA) 2013 Conference, Available at SSRN: <https://ssrn.com/abstract=2192918>. This paper found diversity numbers were worse than reported because of double counting. The Taskforce could consider requiring companies to report on the number of directorships a board member is currently holding to avoid one person be counted as multiple diverse candidates across several boards in Canada.

<sup>7</sup> BNN Bloomberg Review, *Two in 100: 'Alarming' lack of female CEOs among top TSX companies* (August 26, 2020) available at: <https://www.bnnbloomberg.ca/two-in-100-alarming-lack-of-female-ceos-among-top-tsx-companies-1.1485106>. "As of last year, the total number of board seats occupied by women in Canada stood at 17 per cent, according to a report by the Canadian Securities Administrators. That compares to 11 per cent in 2015."

**Recommendation 20: Introduce a regulatory framework for proxy advisory firms (PAFs) to: (a) provide issuers with a right to “rebut” PAF reports, and (b) restrict PAFs from providing consulting services to issuers in respect of which PAFs also provide clients with voting recommendations**

**Recommendation 20(a):** The PRI is concerned with Recommendation 20(a) to provide issuers with a right to “rebut” PAF reports as issuer involvement and the new requirements for PAFs to facilitate this process are unnecessary and unworkable. The proposed changes could increase costs for PAFs and impact the independence of the advice provided to clients.

The PRI engages in policy topics in multiple markets, including the US. The US Securities and Exchange Commission (SEC) recently finalized rules that require proxy voting advice be provided to companies before or at the same time as it is provided to clients, and require proxy advisory firms to ensure their clients are aware if the company plans to respond and are provided companies’ responses to the proxy advisory firms’ voting recommendations.<sup>8</sup> Public companies and business organizations have argued that proxy advisory firm research and recommendations consistently contain factual errors, however, a 2016 Government Accountability Office (GAO) report found “[b]oth corporate issuers and institutional investors [the GAO] interviewed said that the data errors they found in the proxy reports were mostly minor.”<sup>9</sup> In the PRI’s view, the rules threaten the ability for investors to receive independent advice from proxy advisory firms.

Similar to the SEC’s rules, the proposed changes are based on general concerns from issuers and lacks data from market participants to determine if the issues raised regarding influence of and errors from PAFs reports need to be resolved with a new regulatory framework. The Taskforce’s proposal to require the PAF “to include the rebuttal in the report it provides to its clients” could similarly affect the ability of investors to receive third-party research, impose additional costs for investors and PAFs, and attempt to provide a solution for a problem the Canadian market does not have.<sup>10</sup>

**Recommendation 20(b):** The PRI supports Recommendation 20(b) that restricts PAFs from providing consulting services to issuers in respect of which PAFs also provide clients with voting recommendations.

PAFs should be restricted from providing consulting services to issuers if they also provide voting recommendations for those issuers. Investors rely on independent, third party research in order to make informed voting decisions. If PAFs are providing voting recommendations to clients on issuers as well as consulting services, it could reduce the confidence investors have in the independence of the research, undermining a key tool in the proxy process. Recommendation 20(b) would reduce conflicts of interest and increase transparency for investors.

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<sup>8</sup> Securities and Exchange Commission, *Final Rule: Exemptions from the Proxy Rules for Proxy Voting Advice* (July 22, 2020) available at: <https://www.sec.gov/rules/final/2020/34-89372.pdf>.

<sup>9</sup> Government Accountability Office (GAO), *Proxy Advisors Role in Voting and Corporate Governance Practices*, GAO-17-47 (Nov. 2016) (“The institutional investor said that the errors found in proxy reports generally were minor and that firms typically were able to update and correct their reports”).

<sup>10</sup> Consultation Report at 24.

### **Recommendation 23: Require TSX-listed issuers to have an annual advisory shareholders' vote on the board's approach to executive compensation**

The PRI strongly supports the recommendation to require an annual advisory shareholders' vote on the board's approach to executive compensation.

An annual review and vote on a board's approach to executive compensation is an important engagement tool for investors. According to the Shareholder Association for Research and Education (SHARE), more than 71% of TSX-listed companies had adopted a 'Say on Pay' resolution.<sup>11</sup> As stated in our comment on the Ontario Securities Commission (OSC) 2017-2018 Draft Statement of Priorities, "[i]t is critical to investors that executive compensation is adequately aligned to a company's business plan and strategic objectives. The structure of executive compensation packages can also help embed long-term and sustainability approaches in management practice."<sup>12</sup>

In addition, the PRI recommends the Taskforce and the OSC review the UK's The Companies Regulations 2019, which requires an annual advisory vote by shareholders on directors' remuneration, and that the Directors' remuneration policy be "subject to a binding vote by shareholder at least every three years", as one example of a recurring review and vote on executive compensation by shareholders.<sup>13</sup>

### **Recommendation 24. Empower the OSC to provide its views to an issuer with respect to the exclusion by an issuer of shareholder proposals in the issuer's proxy materials (no-action letter)**

The PRI recommends withdrawing the Taskforce recommendation to allow the OSC to provide its views to an issuer with respect to the exclusion by an issuer of shareholder proposals in the issuer's proxy materials (no-action letter).

The recommendation references the US SEC's no-action letter process and asks commenters if the OSC should create a similar process. In the US, the no-action letter process is used frequently by issuers requesting the SEC state whether it agrees issuers have a legal basis for excluding a shareholder proposal from their proxy ballot. In November 2019, the SEC's Division of Corporate Finance stated for the "2019-2020 shareholder proposal season, the staff may not respond by letter to every no-action request submitted" and instead states views in a No-Action chart available on the SEC's website.<sup>14</sup> The number of proposals that received no-action relief remained at 15% for 2019.<sup>15</sup>

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<sup>11</sup> SHARE, *Canadian markets are moving on Say on Pay, and governments may be catching up* (April 11, 2019) available at: <https://share.ca/say-on-pay-imperial-linamar-april-2019/>.

<sup>12</sup> PRI, *Input on the Ontario Securities Commission (OSC) 2017-2018 Draft Statement of Priorities* (May 23, 2017) available at: <https://d8g8t13e9vf2o.cloudfront.net/Uploads/w/h/o/PRI-OSC-Statement-of-Priorities-Consultation-2017.pdf>.

<sup>13</sup> United Kingdom Department of Business, Energy & Industrial Strategy, *The Companies (Directors' Remuneration Policy and Directors' Remuneration Report) Regulations 2019* (June 14 2019) available at: <https://www.gov.uk/government/publications/companies-directors-remuneration-policy-and-directors-remuneration-report-regulations-2019>. The UK has had a binding vote on remuneration since 2013, with the revision of the Companies Act 2006.

<sup>14</sup> Securities and Exchange Commission, *Shareholder Proposal No-Action Responses Issued Under Exchange Act Rule 14a-8* (2019) available at: <https://www.sec.gov/corpfin/shareholder-proposals-no-action>.

<sup>15</sup> Orowitz and Rosati, Georgeson, Harvard Law School Forum on Corporate Governance, *An Early Look at the 2020 Proxy Season* (June 10, 2020) available at: <https://corpgov.law.harvard.edu/2020/06/10/an-early-look-at-the-2020-proxy-season/>.

The recommendation proposes a solution to a problem that does not exist in Canada, and as a result, it could be time-consuming and costly for all parties. US shareholders submitted 657 proposals in 2020.<sup>16</sup> Canada's 2020 proxy season included only 77 shareholder proposals. According to SHARE, there have been almost no cases of Canadian issuers refusing to accept shareholder proposals in the last twenty years, as it is an accepted part of the shareholder engagement process for Canadian issuers to include shareholder proposals without challenge.<sup>17</sup> The PRI recommends the Taskforce remove this Recommendation.

### **Recommendation 25: Require enhanced disclosure of material environmental, social and governance (ESG) information, including forward-looking information, for TSX issuers**

The PRI strongly supports disclosure of material ESG information by issuers.

The fiduciary duties of investors require incorporation of material ESG factors. The PRI encourages transparency and disclosure on how ESG is incorporated in a firm's mainstream and ESG products/mandates, as there will often be substantial differences that are important to disclose. This allows investors to mitigate risks and capitalize on opportunities, which increases the long-term value of their investments. Empirical evidence demonstrates that the practice of incorporating ESG factors into investment decisions is a source of investment value, while the failure to effectively manage ESG issues can destroy investment value.<sup>18</sup>

The PRI recommends the Taskforce mandate the use of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD).<sup>19</sup>

Investors are increasingly adopting the TCFD recommendations as they provide a global framework for translating climate risks and opportunities into financial metrics and disclosing that information to investors and the public.<sup>20</sup> Climate disclosures are every bit as suitable for disclosure as forward-looking economic projections, and they are critical to provide investors a complete understanding and plug material omissions in those economic projections.

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<sup>16</sup> Sullivan & Cromwell LLP, *2020 Proxy Season Review: Part 1 Rule 14a-8 Shareholder Proposals* (July 15, 2020) available at: [sullcrom.com/files/upload/SC-Publication-2020-Proxy-Season-Review-Part-1-Rule-14a-8.pdf](http://sullcrom.com/files/upload/SC-Publication-2020-Proxy-Season-Review-Part-1-Rule-14a-8.pdf). "A total of 657 shareholder proposals have been submitted to date in 2020, relative to 678 at this time last year, 722 for 2019 as a whole and 788 for 2018."

<sup>17</sup> SHARE, *Shareholder Proposal Data* (July 28, 2020).

<sup>18</sup> Khan, M., Serafeim, G. and Yoon, A. (2016), 'Corporate Sustainability: First Evidence on Materiality', *The Accounting Review*, Vol. 91, Issue 6, pp. 1697–1724, available at: <http://www.aaajournals.org/doi/abs/10.2308/accr-51383>.

<sup>19</sup> This year, PRI signatories were required to report against the TCFD Framework with voluntary option to publicly disclose. All 2097 signatories reported on the climate indicators (strategy and governance and risks and opportunities). 20% signatories chose to disclose their responses to at least one of the indicators. 20% of Canadian signatories chose to publish at least one of their responses. We have noticed that mandatory reporting likely contributed to an increase in practices such as Board oversight on climate. (538 signatories reported Board oversight on climate in 2020, that had not done so in 2019). In 2021, all TCFD disclosures are mandatory, except for the metrics and targets, which will be mandatory in 2022. See PRI, TCFD-based reporting to become mandatory for all PRI signatories in 2020 (February 18, 2019) available at: <https://www.unpri.org/news-and-press/tcf-based-reporting-to-become-mandatory-for-pri-signatories-in-2020/4116.article>.

<sup>20</sup> TCFD, *TCFD Supporters* (as of February 2020, "support for the TCFD has grown to over 1,027 organizations, representing a market capitalization of over \$12 trillion.") available at: <https://www.fsb-tcf.org/tcf-supporters/>. Support does not indicate that these organizations are reporting against the TCFD in a uniform manner. See also The PRI, *PRI FAQ on mandatory climate reporting for PRI signatories*, available at: <https://www.unpri.org/reporting-for-signatories/faq-on-mandatory-climate-reporting-for-pri-signatories/5356.article>. The PRI required signatories to report against the TCFD Framework this year.

The PRI advocates for ESG reporting data that is comparable, accessible and consistent.<sup>21</sup> The PRI believes the most decision-useful information for investors stems from a combination of quantitative and qualitative disclosures of ESG information.

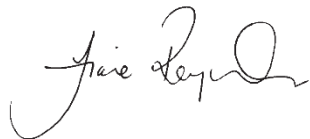
## Conclusion

In addition to the recommendations above, the PRI recommends the OSC create a review process to update capital markets regulations. The global financial markets have and continue to change, and the OSC should ensure the securities regulatory framework is reviewed regularly in order to promote Canadian businesses and protect Canadian investors.

Thank you for the opportunity to share our views. For further conversation and follow up, please contact:

- Lindsey Walton, Head of Canada Signatory Relations, [lindsey.walton@unpri.org](mailto:lindsey.walton@unpri.org)
- Kelly Krauter, Canada Signatory Relations, [kelly.krauter@unpri.org](mailto:kelly.krauter@unpri.org)
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Yours sincerely,



Fiona Reynolds  
Chief Executive Officer  
Principles for Responsible Investment

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<sup>21</sup> PRI, *PRI Reporting Framework Main Definitions 2018* (November 2017) available at: <https://www.unpri.org/download?ac=1453>. There is no definitive list for ESG issues, however, the PRI Reporting Framework includes main definitions of ESG issues to help guide signatories in identifying factors that may be financially material in their investments.