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Introduction

A great deal of discussion and legislative and regulatory direction with respect to corporate governance are currently occupying public attention, in large part in reaction to the issues raised by the Enron, Worldcom and Tyco events in the U.S. In the post-Enron environment of responsible corporate governance, public companies and regulators are going to great lengths to regain the trust of the public in the capital markets. Changes, both voluntary and involuntary, are taking place and will continue to take place in all areas of corporate activity which are affected by governance issues.

This booklet, produced by Fasken Martineau, is part of a series intended to provide an overview of corporate governance issues as they affect public companies and their officers and directors. This booklet discusses Board and Director Evaluation, Orientation and Education. Other existing booklets discuss Corporate Disclosure and Investor Communications, Director Independence, Audit Committees, Executive Compensation, and Board Charters and Codes. The next booklet, which will be the last in the series, will cover Regulatory Penalties and Directors’ and Officers’ liability, including indemnification and insurance coverage matters, as relates to each of the areas discussed in the preceding booklets. Directors and officers may be able to secure at least partial protection against such liabilities but the processes of putting protective measures in place, and enforcing them when claims arise, raise complex issues requiring careful planning and execution.

By its very nature, a publication of this kind is not intended to provide a detailed analysis of all the issues, laws, regulations and policies affecting corporate governance. It is designed to provide a broad overview of the subject matter and to stimulate the reader to obtain further information as required in the reader’s particular circumstances. More comprehensive legal advice will be required to fully meet the specifics of each situation. What is presented in this booklet are suggestions for consideration by the reader.

For convenience of the reader, certain capitalized terms are defined in the Glossary at the end of each booklet.

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Board and Director Evaluation, Orientation and Education

Executive Summary

• Evaluation of a board and its committees is a good corporate governance practice:
  • Enables assessment of how the board is carrying out its responsibilities and mandate, its structure and organization as well as the processes by which it receives information.
  • Provides results which should be shared to enable improvement.
  • Prompts adjustments to corporate governance practices based on identified deficiencies.

• Evaluation of individual directors helps improve overall board and committee performance:
  • Enables assessments of an individual director’s contribution.
  • Conducted by peer and/or self-assessments.
  • Provides individual results which should not be shared with other directors except the Chair, the nominating committee and, depending on its mandate, the governance committee.

• Processes for evaluation:
  • Should be regularly conducted - at least annually.
  • May be conducted formally (in writing) or informally (through discussion).

• Director orientation and education:
  • Orientation initially for new directors and education on a continuing basis for all directors.
  • Critical to an understanding of roles and commitments.
  • Use of written materials (e.g. manuals) is important.
  • Review of these materials should occur at periodic meetings specifically designed for these purposes.
**Introduction**

Director performance is key to good corporate governance. Directors function at three levels - board, committee and individual. Effective performance at all levels is therefore important. Steps to support such effective performance would include regular evaluation of the board and each individual director, and the implementation of formal orientation or education programs for new directors and continuing education for all.

**Evaluation**

**Board of Directors Assessment**

The TSX Governance Guidelines provide that boards should implement a process for evaluating the effectiveness of the board as a whole. This task can be done by the nominating or governance committee or under the leadership of a single designated independent director working with or for the committee responsible for the evaluation process. Every TSX listed company must describe how it is complying with such guidelines or where there is a difference, describe the difference and the reason for it.

In Canada, the JCCG Report recommended that regular board and committee assessment is essential to improving corporate governance practices. The focus should be on how board or committee performance can be made more meaningful by setting and achieving goals that add value. The results of performance assessments should be reported to the full board.

Similar principles apply in the United States. The NYSE Rules require that a board and its committees be evaluated at least annually. Foreign private issuers listed on the NYSE who do not perform such evaluations are required to disclose significant differences between their processes and the NYSE Rules.

The board should use the results of the assessment process to enhance its governance system. Any deficiencies identified should be analyzed and appropriate measures taken to address them.

The assessment process should review how the board is carrying out its core functions in the following areas: (i) responsibilities and mandate, (ii) structure and organization, and (iii) processes and information.

- **Responsibilities and Mandate:** The TSX Company Manual indicates boards should explicitly assume responsibility for the stewardship of the company and adopt a formal mandate setting out the board’s stewardship responsibilities. In particular, the board should assume responsibility for:
  - adoption of a strategic planning process and an annual assessment of the opportunities and risks of the business;
  - identification of principal risks and implementation of systems to manage such risks;
• succession planning, training and monitoring of the CEO and senior management;
• communication policies addressing how the company interacts with various stakeholders;
• how the company complies with continuous and timely disclosure obligations; and
• integrity of internal control and management information systems.

Structure and Organization: This is key to effective functioning of the board and the following areas should be evaluated:

• constitution of the board;
• board independence;
• director succession;
• board size; and
• board committees.

Processes and Information: The processes by which a board or committee receives information are crucial to fulfilment of its responsibilities. For example, processes and the information itself must:

• enable assessment of the organization’s activities and management;
• be sufficiently detailed to facilitate informed decisions without being overly focussed on the minutia of an organization’s activities; and
• permit receipt in a timely manner so that the information can be used effectively.

Individual Director Assessment

The TSX Governance Guidelines and the JCCG Report recommend that evaluations of individual directors should occur regularly. This would enable directors to understand how they are performing against what is expected of them and, if required, to determine what changes should be made. Better individual performance will facilitate better relationships between board members, the Chair, management and shareholders. Such assessments will also highlight any performance deficiencies that may indicate the need for changes in board membership.

There appears to be a trend among organizations favouring annual, as opposed to bi-annual, assessments of individual directors. In the U.S., attention to date has focused on overall board, rather than individual, performance evaluation.

Methods of Assessment

Typical methods of assessment include using a form of written questionnaire or discussions between the board Chair/lead director/governance committee and the board or individual directors. For individual director assessments, peer and/or
self-assessment are the typical methods used. The former requires each director to evaluate the performance of the other directors, while the latter enables each director to evaluate his or her own performance and contribution.

The O’Callaghan Survey found that the favoured mode of evaluation was a written questionnaire followed by one-on-one interviews with the board Chair, lead director or governance committee Chair. According to the O’Callaghan Survey, “formal evaluations cover a wider range of content, cover issues more comprehensively and are more likely to result in a report and recommendations to the board. Director satisfaction with the evaluation process is much higher when it is a formal process.” The use of a written questionnaire ensures a standardized set of questions that can be answered candidly without a director experiencing the pressure typically inherent in situations of face-to-face interviews.

The process of compiling and interpreting the results of board assessment may be delegated to the Chair, the lead director or the governance committee. Alternatively, the board may choose to perform this function itself or may hire an outside consultant to perform that task. The O’Callaghan Survey indicated that approximately 78% of the survey participants used their governance or nominating committee to compile and interpret the assessment results. Regardless of the method chosen, the results of such assessments should be presented to the full board for consideration.

The O’Callaghan Survey found with respect to individual director assessments that self-assessment was used more frequently than peer evaluation. This may be attributable to peer evaluations being perceived as detracting from the collegiality and co-operation necessary for the effective functioning of boards as a whole.

The results of individual assessments should be compiled by the Chair, the lead director or the governance committee, or alternatively, by an outside consultant. Each director should also be encouraged to consider such results critically so that he or she can seek ways to improve his or her effectiveness and contribution. While results are best kept confidential and not shared with the board as a whole or other directors, it may be appropriate for the nominating or governance committee to receive a summary of the results to help improve the organization’s governance practices.

The following are some examples of the types of questions that might be included in the assessment questionnaires:

- Board as a whole-
  - Does the board have a written mandate?
  - Is the mandate reviewed regularly?
  - Is the board part of the company’s strategic plan process including review, input and approval?
  - Does the board review areas of business and legal risk to the company on a regular basis?
• Does the board receive adequate information to do its work?
• Is management responsive to board requests?
• Does the board participate in CEO and senior management evaluation?
• Does the board know who its stakeholders are?
• Does the board have adequate communications lines with its stakeholders?
• Does the board review/monitor the company’s timely disclosure policies and procedures?
• Does the board regularly meet without management present?
• Does the board have adequate contact with the external auditors and the company’s internal audit group?
• Does the board have input in setting criteria for new recruits to the board?
• Does the board have the right number and types of committees?
• Does the Chair allot sufficient time for meaningful discussion at meetings?
• Does the board regularly assess its performance?

• For each individual director-
  • Do you understand your role and legal responsibilities?
  • Do you know how to deal with a conflict of interest?
  • Do you objectively assess issues?
  • Do you have a collaborative work style with other directors and with management?
  • Do you attend meetings regularly?
  • Do you participate actively in meetings?
  • Do you prepare adequately for meetings?
  • Do you question conclusions reached by management on information provided to you?
  • Do you believe you have the requisite skills to be on the board?
Director Orientation and Education

The TSX Governance Guidelines recommend that every company provide an orientation and education program for new directors and provide continuing education for all directors. It is critical that new directors understand the role of the board, the role of the committees and the commitment of time and energy expected. Similarly, in the U.S., the NYSE Rules require addressing orientation and continuing education for individual directors.

Director orientation is generally accomplished by providing new directors with a board manual and/or hosting an orientation session. Suggested topics for a new director orientation session include:

- Introduction of participants.
- Review of board organization and membership.
- Review of board operations, board and committee calendars and committee terms of reference.
- Review of constituting documents, by-laws and board policies.
- Overview of corporate governance policies.
- Review of duties of directors.
- Review of statutory and other legal liabilities of directors.
- Overview of business, including corporate structure and responsibilities of key management and functions.
- Review of key financial data.
- Review of Strategic Plan: mission, values, goals, strategies and planning.
- Review of key laws applicable to the company (e.g. Broadcasting Act if in broadcasting, etc.).
- Review of control procedures such as risk management, internal audit and whistle-blowing.

Ongoing director education is also very important. It will allow for periodic review of their duties as well as focus on any updates to the board manual. Such education should occur on an annual basis, and more frequently when appropriate. Annual board education should also take into account the results of the board evaluation process and aggregate individual director evaluations.
Conclusion

The O’Callaghan Survey concluded that assessments of the board and each individual director were necessary to improvement in corporate governance standards. It suggested that assessments would include many of the same principles applied to all employees, including setting objectives, evaluating performance, and allowing for corrections if deficiencies are uncovered. Moreover, directors cannot be expected to acquire the necessary knowledge about the company unless they are assisted in that process. Providing directors with the tools to inform themselves and be better educated, both as new directors, and on a continuing basis, is important to performing as directors. The corporate governance standards now being released by Canadian and U.S. regulatory authorities indicate that the regulators have reached the same conclusions.
Glossary

For ease of reference, the following is a glossary of certain terms that are referred to in this booklet.

Bill 198
An Act to implement Budget measures and other initiatives of the Government, S.O. 2002, c.22

CICA
The Canadian Institute of Chartered Accountants

Conference Board Commission Report

CSA
Canadian Securities Administrators

CSA Report
Report by the CSA on compliance by issuers with executive compensation disclosure requirements under Canadian securities regulatory disclosure rules (November 2002)

Exchange Act
U.S. Securities Exchange Act of 1934

JCCG
Joint Committee on Corporate Governance, which was a committee of representatives of the TSX, TSXV and CICA, chaired by Guylaine Saucier, that examined corporate governance issues

JCCG Report

MD&A
Management’s Discussion and Analysis as required to be included in a public company’s annual information form, annual report or other similar document, pursuant to securities legislation

MI 52-109
Multilateral Instrument 52-109 - Certifications of Disclosure in Issuers’ Annual and Interim Filings

MI 52-110
Multilateral Instrument 52-110 - Audit Committees

NASDAQ
The NASDAQ National Market

NASDAQ Rules
The rules concerning NASDAQ’s Marketplace Rules

NI 51-102
National Instrument 51-102 of the CSA regarding Continuous Disclosure Obligations

NI 52-108
National Instrument 52-108 of the CSA regarding Auditor Oversight

NP 51-201
National Policy 51-201 of the CSA regarding Disclosure Standards

NYSE
New York Stock Exchange
NYSE Rules
NYSE listing standards

O'Callaghan Survey

OSC
Ontario Securities Commission

OSC Rule 61-501
Rule 61-501 of the OSC regarding Insider Bids, Issuer Bids, Business Combinations and Related Party Transactions

Proposed MI 58-101
Proposed Multilateral Instrument 58-101 issued by the CSA regarding Disclosure of Corporate Governance Practices

Proposed Policy 58-201
Proposed Multilateral Policy 58-201 issued by the CSA - “Effective Corporate Governance”

Sarbanes-Oxley Act
U.S. Sarbanes-Oxley Act of 2002

SEC
U.S. Securities and Exchange Commission

SEC Certification Rules
Rules established pursuant to Section 302 of the Sarbanes-Oxley Act respecting certification of certain reports filed under the Exchange Act

SEC Rules
Rules adopted by the SEC pursuant to the Exchange Act

SEDAR
The System for Electronic Document Analysis and Retrieval, used by public companies in Canada in connection with filing of documents pursuant to Canadian securities laws

TSX
Toronto Stock Exchange

TSX Company Manual
The manual published by the TSX which contains the TSX Rules, TSX Governance Guidelines, TSX policy statements and other matters relating to listing on the TSX

TSX Disclosure Guidelines
TSX Policy Statement on Timely Disclosure and Related Guidelines contained in the TSX Company Manual

TSX Electronic Disclosure Guidelines
TSX Electronic Communication Disclosure Guidelines contained in the TSX Company Manual

TSX Governance Guidelines
TSX Governance Guidelines contained in the TSX Company Manual

TSX Rules
Rules contained in the TSX Company Manual

TSXV
TSX Venture Exchange
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