GOVERNANCE INSIGHTS 2023

Diversity: Recent Trends and Developments

It has been approximately nine years since the Ontario Securities Commission (OSC) first implemented the "comply-or-explain" regime that requires companies listed on the Toronto Stock Exchange (TSX) either to disclose information about gender diversity (including the number of women on their boards and their policies on diversity) or to explain why they are not doing so. Since then, a number of other key developments have taken place in the corporate diversity context. Proxy advisers Institutional Shareholder Services Inc. (ISS) and Glass, Lewis & Co. (Glass Lewis) have updated their guidance and the federal government has amended the *Canada Business Corporations Act* (CBCA), all with a focus on promoting a range of diversity characteristics in addition to gender. Despite these developments, progress has been slow in Canada; the overall representation of women and other underrepresented groups on boards and in senior executive officer positions still does not reflect the demographics of the Canadian population or Canadian society's expectations for a more diverse corporate environment.

In this article, we refresh our discussions from the 2019 and 2020 editions of *Davies Governance Insights* regarding the legal framework on diversity in Canada and examine this framework's overall impact, including the effect of the 2020 CBCA amendments that came into force more than three years ago. We also consider notable diversity-related developments, which suggest that the existing regulatory and legal framework for diversity in both Canada and the United States is likely to undergo more significant change in the years to come and that stakeholders will continue to consider diversity when making investment and voting decisions.

Impact of Existing Diversity Framework in Canada

THE CURRENT LEGAL FRAMEWORK

In the 2019 and 2020 editions of *Davies Governance Insights*, we provided a detailed overview of the evolving legal framework relating to diversity in Canada. The current legal framework can be summarized as follows:

- As a result of amendments to the CBCA that came into effect on January 1, 2020, all CBCA public companies are required to disclose information about their policies, practices and metrics related to the diversity of their boards and senior management teams annually. In particular, CBCA public companies are now required to provide disclosure regarding four "designated groups" – women, members of visible minorities, Indigenous peoples (First Nations, Inuit and Métis) and persons with disabilities.

- All Canadian public companies are required to comply with Canadian securities laws – specifically, National Instrument 58-101 – *Disclosure of Corporate Governance Practices* (NI 58-101) – that delineate disclosure obligations to a company's approach to gender diversity, including data regarding the representation of women on boards and in executive positions, but do not extend to the representation of other underrepresented groups. Like the CBCA, NI 58-101 implements a comply-or-explain regime. It neither mandates diversity practices and disclosure beyond gender diversity nor requires companies to adopt gender diversity policies and practices, targets or quotas. However, as discussed below, the Canadian Securities Administrators (CSA) is currently seeking comments on two very different approaches to amending NI 58-101.

THE CBCA AMENDMENTS

The year 2021 marked the second year that CBCA public companies were required to comply with the new requirements resulting from the CBCA amendments. In March 2022, Corporations Canada released its 2021 Annual Report – *Diversity of Boards of Directors and Senior Management of Federal Distributing Corporations* (CBCA Report) – which reviewed 475 proxy circulars filed by CBCA public companies for meetings held in 2021. The CBCA Report compared the diversity data from 2021 with the baseline data from 2020. Notable findings from the CBCA Report include the following:

- Only 55% of CBCA public companies have at least one woman on their boards; however, women hold only 20% of all board seats.
- Only 23% of CBCA public companies have at least one member of a visible minority on their boards; only 2% have at least one Indigenous person on their boards; and only 2% have at least one person with disabilities on their boards. Members of visible minorities hold only 7% of all board seats, and persons with disabilities and Indigenous persons each hold only 0.4% of all board seats.
- Women hold 25% of all senior management positions; members of visible minorities hold 9% of all senior management positions; persons with disabilities hold 0.7% of all senior management positions and Indigenous persons hold 0.4% of all senior management positions.
- While 18% of CBCA public companies have set targets for the representation of women on their boards, only 4% have set targets for the representation of visible minorities on their boards and only 2% have set targets for the representation of persons with disabilities or Indigenous persons on their boards.

Although the CBCA Report shows that some progress has been made, it also illustrates that there continues to be a disparity between the representation of the four designated groups and the Canadian population. According to *Employment Equity in the Public Service of Canada for Fiscal Year 2019 to 2020*, 52.7% of the Canadian population available to work in 2019–2020 were women; 15.3% were members of visible minorities; 9% were persons with disabilities; and 4% were Indigenous persons. As noted above, these numbers are not reflected in the boards and senior management of CBCA public companies.

DIVERSITY AND TRENDS: GENDER AND BEYOND

We have continued to track developments in gender diversity disclosure since the OSC first implemented the comply-or-explain disclosure regime under NI 58-101 in 2015. Prior editions of *Davies Governance Insights* detail extensive data and analysis on issuers' progress toward meeting various diversity measures.

> The overall representation of women and other under represented groups on boards and in senior executive officer positions still does not reflect the demographics of the Canadian population or Canadian society's expectations for a more diverse corporate environment.

As Tables 1 and 2 illustrate, consistent progress has continued in the representation of women on boards, although the progress has been slow.

TABLE 1: Diversity Progress (2014–2022)

	2014	2016	2018	2020	2022
Board seats of TSX Composite and SmallCap Index issuers held by women	12.3%	17.7%	20.8%	25.8%	29.8%
Board seats of TSX 60 issuers held by women	20.1%	24.6%	27.5%	29.6%	35.3%
TSX Composite and SmallCap Index issuers with written diversity policies	8.6%	48.0%	61.3%	77.2%	78.1%
TSX Composite and SmallCap Index issuers with female board chairs	3.2%	4.4%	5.2%	6.8%	7.0%
TSX Composite and SmallCap Index issuers with targets	3.2%	16.1%	24.5%	41.1%	53.8%
TSX 60 Index issuers with targets	10.0%	35.0%	48.3%	55.2%	79.7%

TABLE 2: Issuers That Put Forward One, Two or No Female Directors

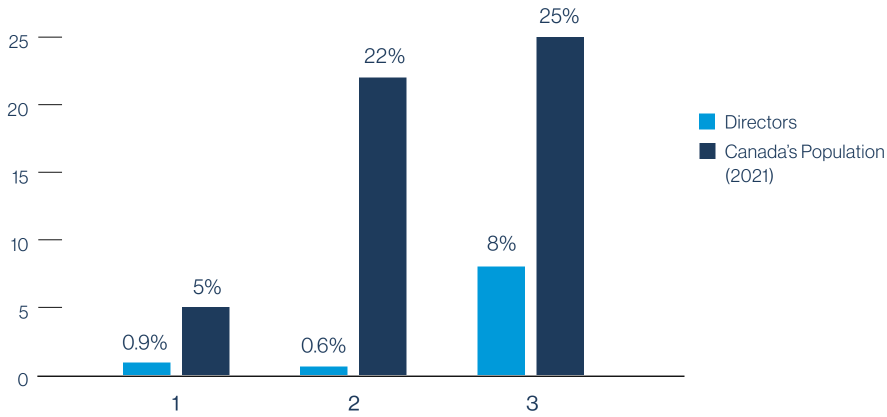
	2016	2018	2020	2022
TSX Composite and SmallCap Index issuers that put forward at least one woman for election to the board	76.6%	86.6%	94.1%	96.9%
TSX Composite and SmallCap Index issuers that put forward at least two women for election to the board	44.4%	50.8%	71.3%	78.8%
TSX Composite and SmallCap Index issuers that put no women forward for election to the board	23.4%	13.4%	5.9%	3.1%

We also analyzed the representation of visible minorities, Indigenous peoples and persons with disabilities on public company boards. The percentage of these groups has increased over the past two years, albeit modestly. In 2022, visible minorities held 8%, Indigenous peoples 0.6% and persons with disabilities

0.9% (2021: 6.8%, 0.5% and 0.5% respectively, and in 2020: 5.5.%, 0.5% and 0.4%, respectively) of board seats. However, as shown in Figure 1, the representation of these groups on boards remains significantly lower than their representation in Canada's population.

As of October 2022, 24% of board seats were held by women, up from 22% in the prior year. In addition, 87% of issuers now have at least one woman on their board, a 5% increase over last year.

FIGURE 1: Board Representation of Indigenous Peoples, Persons with Disabilities and Visible Minorities



Note: The data is based on the number of companies that disclosed the number of directors who identify as Indigenous peoples, persons with disabilities or visible minorities. In 2022, there were 268 such companies that disclosed the number of directors who are visible minorities; 269 companies that disclosed the number of directors who are Indigenous peoples and 250 companies that disclosed the number of directors who are persons with disabilities.

Current data on diversity was released in October 2022 when the CSA published *CSA Multilateral Staff Notice 58-314 – Review of Disclosure Regarding Women on Boards and in Executive Officer Positions (Year 8 Report)*, which reported on the results of the CSA's eighth annual staff review of women on boards and in executive officer positions.

The CSA reviewed 625 issuers with year-ends between December 31, 2021, and March 31, 2022, that filed their information circulars or annual information forms by July 31, 2022. The data collected by the CSA show that the total number of board seats occupied by women has increased each year. As of October 2022, 24% of board seats were held by women, up from 22% in the prior year. In addition, 87% of issuers had at least one woman on their boards, a 5% increase over the prior year.

The CSA review reveals similar progress for women in executive officer positions: 70% of issuers disclosed having at least one woman in an executive officer position, up from 67% in the prior year, with 5% of issuers having a female chief executive officer and 19% having a female chief financial officer.

Progress in increasing female representation on boards and in executive officer positions continues to vary across industries. The manufacturing industry led the way in terms of the percentage of issuers with one or more women on their board (98%), and the utilities industry was at the forefront in terms of the percentage of issuers with one or more women in executive officer positions (92%). In contrast, the mining industry had the lowest percentage of issuers with one or more women on their board (80%) and in executive officer positions (55%).

While some progress has been made on the diversity front in recent years, the composition of the corporate leadership of Canadian public companies has a long way to go before it reflects the overall diversity of Canada's population. Despite all the regulations, policies and guidance that have been adopted, real and meaningful progress continues to be slow and incremental. The research and findings to date make clear why many believe that the existing framework is lacking in achieving meaningful results. Given the slow pace of improvement, we expect the CSA to continue to investigate ways to incentivize issuers to improve their diversity-related practices.

Recent Notable Developments

In the 2020 edition of *Davies Governance Insights*, we indicated that we expected diversity to remain in the spotlight and that the focus would be on a broader range of diversity characteristics beyond gender. In that regard, a number of notable developments have underscored that investors, proxy advisers and securities regulators are increasingly focused on promoting greater diversity in corporate leadership. Many of these developments result from societal norms that place greater expectations and demands on enhanced diversity in all aspects of society. An August 2020 survey of 500 capital market professionals found that 92% of respondents supported targets for women and Black, Indigenous and People of Colour (BIPOC) on boards and in executive positions, as well as requirements for public companies to annually disclose data on such underrepresented groups. However, the current legal framework has not resulted in significant progress on key diversity metrics. Consensus appears to be growing among business leaders and regulators that further legal reform is required to affect real change.

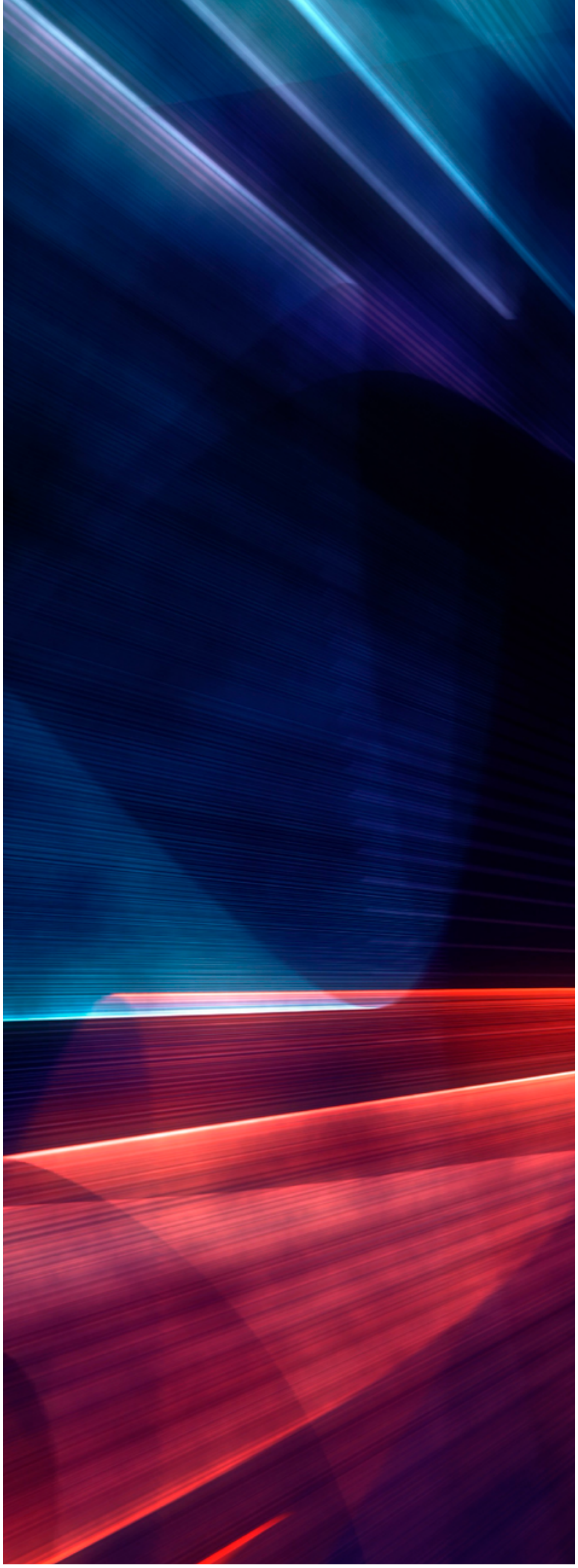
The following sections set out notable recent developments relating to diversity, signalling that further reform and regulatory action is likely forthcoming.

CAPITAL MARKETS MODERNIZATION TASKFORCE REPORT

In January 2021, the Capital Markets Modernization Taskforce (CMMT), which was established by the Ontario government to review and modernize Ontario's capital markets, released its final report. With respect to diversity, the CMMT's final recommendations are similar to those referenced in its initial July 2020 consultation report and summarized in the 2020 edition of *Davies Governance Insights*; however, the final report outlines more specific guidance and recommendations. One notable difference is that the July 2020 consultation report focused on extending the obligations of Canadian public companies beyond gender to include BIPOC. In the final report, the CMMT proposed further extending such obligations to persons with disabilities and LGBTQ+ persons.

In particular, the final report proposed the following amendments to Canadian securities laws:

- **Diversity targets, timelines and disclosure.** Canadian public companies should be required to set their own diversity targets for their boards and executive management teams (aggregated across both groups) and implementation timelines; in addition, they should annually provide data regarding the representation of those who self-identify as women, BIPOC, persons with disabilities or LGBTQ+ persons. Although the July 2020 consultation report did not provide precise recommendations on appropriate targets, the final report suggested that Canadian public companies set an aggregated target among their boards and executive management teams of 50% for women and 30% for BIPOC, persons with disabilities and LGBTQ+ persons. The CMMT further recommended that Canadian public companies should meet the target for women within five years of the amendment taking effect and the target for BIPOC, persons with disabilities and LGBTQ+ persons within seven years of the amendment taking effect. The CMMT also indicated that there should be a particular emphasis on representation of Black and Indigenous groups.
- **Written policy for director nominations.** Canadian public companies should be required to adopt a written policy regarding the director nomination process that expressly recognizes the identification of candidates who self-identify as women, BIPOC, persons with disabilities or LGBTQ+ persons during the nomination process.
- **Tenure limits.** Canadian public companies should be required to set a 12-year maximum tenure for directors, with exceptions for (i) 15-year maximum tenure for board chairs; (ii) non-independent directors of family-owned and controlled businesses, when such nominees represent a minority of the board; and (iii) no more than one other director who will be deemed not to be independent and



will still have a 15-year limit. Canadian public companies should be required to implement this recommendation within three years of the amendment taking effect.

The Ontario government is currently reviewing most of the recommendations of the final report, so it is still uncertain whether and to what extent securities laws in Ontario will be amended to reflect the above recommendations. Nonetheless, it is yet another example of regulators turning their minds to the need to address diversity issues through enhanced regulation.

UPDATED GUIDANCE FROM PROXY ADVISORY FIRMS AND GOVERNANCE EXPERTS

In recent years, both ISS and Glass Lewis have made significant changes to their respective policies and guidelines as they pertain to diversity and the Canadian Coalition for Good Governance (CCGG) has indicated that notable changes may be forthcoming.

ISS

Board Gender Diversity

ISS has continuously updated and enhanced its policy recommendations with respect to gender diversity on boards. Prior to February 2022, ISS generally recommended that shareholders withhold their vote if a company had not disclosed a formal written gender diversity policy and no women were on the board. As of February 2022, ISS updated its guidelines for S&P/TSX Composite Index companies, saying that it will generally recommend that shareholders withhold their vote for the chair of the nominating committee (or the chair of the committee designated with the responsibility of a nominating committee, or the chair of the board if no nominating committee has been identified or no chair of such committee has been identified) if women constitute less than 30% of the board and the company has not provided a formal, publicly disclosed written commitment to achieve a board composed of at least 30% of women at or prior to its next annual general meeting.

Table 3 shows the ISS guidelines that apply to shareholders' meetings held on or after February 1, 2023.

> Canadian public companies should be required to adopt a written policy regarding the director nomination process that expressly recognizes the identification of candidates who self-identify as women, BIPOC, persons with disabilities or LGBTQ+ persons during the nomination process.

TABLE 3: ISS Guidelines

Company	General Recommendation	Exemptions
S&P/TSX Composite Index	ISS will generally recommend that shareholders withhold their vote for the chair of the nominating committee (or the chair of the committee designated with the responsibility of a nominating committee, or the chair of the board if no nominating committee has been identified or no chair of such committee has been identified) *if women constitute less than 30% of the board of directors.*	Assuming a publicly disclosed written commitment has been made to achieve 30% representation of women on the board at or prior to the subsequent annual general meeting, an exception will be made for companies that: – joined the S&P/TSX Composite Index and have not previously been subject to a 30% representation of women on the board requirement as an S&P/TSX Composite Index constituent in the past; or – have fallen below 30% representation of women on the board owing to an extraordinary circumstance after achieving that level of representation at the preceding annual general meeting.
Non-S&P/TSX Composite Index *(TSX-listed companies that are not S&P/TSX Composite Index constituents)*	ISS will generally recommend that shareholders withhold their vote for the chair of the nominating committee (or the chair of the committee designated with the responsibility of a nominating committee, or the chair of the board if no nominating committee has been identified or no chair of such committee has been identified) *if no women are on the board of directors.*	This policy will not apply to: – newly publicly listed companies within the current or prior fiscal year; – companies that have transitioned from the TSX Venture Exchange (TSXV) within the current or prior fiscal year; or – companies with four or fewer directors. Assuming the company has a publicly disclosed written commitment to add at least one woman to the board at or prior to the subsequent annual general meeting, an exception will be made for companies that temporarily have no women on the board owing to an extraordinary circumstance after having at least one woman on the board at the preceding annual general meeting.

When providing its rationale for these changes, ISS indicated that widely held, TSX-listed company boards that have no policy commitment and no women on their boards are truly outliers and do not satisfy today's market expectations. ISS specifically referenced the fact that the Canadian 30% Club Investor Group committed to exercising ownership rights to encourage increased representation of women on S&P/TSX Composite Index company boards to a minimum 30% threshold in September 2017. ISS concluded that "it has become clear that a higher standard of representation by women is expected, with S&P/TSX Composite Index constituents playing a vital role in this process as market leaders."

Board Racial and/or Ethnic Diversity

As part of the 2023 policy updates, ISS provided its first set of formal recommendations in Canada with respect to racial and ethnic diversity on boards, which more closely aligns ISS's policy for S&P/TSX Composite Index companies with its policy for companies in the Russell 3000 and/or S&P 1500 indices in the United States.

For meetings on or after February 1, 2024, ISS will generally recommend that shareholders withhold their vote for the chair of the nominating committee (or the chair of the committee designated with the responsibility of a nominating committee, or the chair of the board if no nominating committee has been identified or no chair of such committee has been identified) of an S&P/TSX Composite Index company if the board has no apparent racially or ethnically diverse members. An exception will be made if there was racial and/or ethnic diversity on the board at the preceding annual general meeting and the board makes a firm public commitment to appoint at least one racial and/or ethnically diverse member at or prior to the next annual general meeting.

ISS defines racial and/or ethnic diversity to include Aboriginal peoples (being Indigenous, Inuit or Métis persons) and members of visible minorities (being persons other than Aboriginal peoples), who are non-Caucasian in race or non-white in colour. These definitions are the same as those used in Canada's *Employment Equity Act*.

In providing its rationale for these changes, ISS referred to the CBCA amendments that broadened disclosure requirements on board diversity as well as an increasing desire by many institutional investors for public company boards to become more diverse. In particular, ISS noted that many of its investor clients indicated that boards should better reflect their companies' customer base and the broader societies in which they operate by having directors from racial and ethnic minority groups. Investors also widely supported companies providing enhanced disclosure on their boards' racial/ethnic diversity.

GLASS LEWIS

Glass Lewis has also expanded its policy with respect to gender diversity on boards for TSX-listed companies in recent years. Prior to 2022, Glass Lewis would only recommend a vote against the chair of a nominating committee if the board had no female directors. In 2022, Glass Lewis updated its Canadian policy guidelines for TSX-listed companies to recommend voting against the chair of a nominating committee if the board had fewer than two female directors, or voting against the entire nominating committee if the board had no gender-diverse directors (Glass Lewis did, however, require only one female director for boards with six or fewer total directors).

In 2023, Glass Lewis further updated its policy guidelines for TSX-listed companies by transitioning away from a fixed numerical approach to a percentage-based approach.

In particular, for all shareholder meetings of such companies held after January 1, 2023, Glass Lewis will generally recommend voting against the chair of the nominating committee if the board is not at least 30% gender diverse, or voting against the entire nominating committee if the board has no gender-diverse directors. For boards of issuers on junior exchanges, including TSXV-listed companies, a minimum threshold of one gender-diverse director remains in effect. Glass Lewis defines gender-diverse directors as women and directors that identify as having a gender other than male or female.

It should be noted that Glass Lewis has outlined certain mitigating factors that may lead it to refrain from recommending that shareholders vote against directors. Such mitigating factors include the existence of a diversity policy with non-boilerplate language and clear targets or disclosure regarding the board's timeline for increasing gender diversity.

Interestingly, and unlike ISS, Glass Lewis has not published any voting recommendations in Canada with respect to racial and ethnic diversity on boards.

CCGG

CCGG published its gender diversity policy in December 2018. In November 2020, Catherine McCall, executive director of CCGG, indicated that CCGG was developing a new policy for diversity beyond gender, but that the Black Lives Matter movement caused it to further revisit and refine that policy. CCGG has not provided any further updates regarding the publication of a new diversity policy.

DIVERSITY CONSIDERATIONS IN LIGHT OF THE CBCA'S NEW MAJORITY VOTING AMENDMENTS

Recent CBCA amendments, which came into force on August 31, 2022, mandate majority voting for all CBCA companies. TSX-listed companies are already required to have a majority voting policy that requires director nominees who do not receive more votes for their election than votes withheld to tender their resignation (which the board must accept absent exceptional circumstances within 90 days of the shareholders' meeting). The CBCA amendments, however, go a step further. Under these amendments, a nominee who does not receive majority support is deemed not to have been elected. Furthermore, the undersupported director cannot be appointed to the board before the next shareholders' meeting unless he or she is needed (i) to meet the corporation's obligation to have at least two directors who are not officers or employees of the corporation or its affiliates; or (ii) to maintain a certain percentage of the board members that are Canadian residents.

These majority voting amendments provide activist investors with another tool to make an instantaneous impact on boards that they view as needing a change, including owing to a lack of diversity. The amended majority voting rules allow activist investors to target specific directors for easier removal – for example, an activist investor may target a long-tenured director nominee on a board that it views as needing greater diversity. This development highlights the need for boards to maximize shareholder support for nominees by avoiding situations in which their board is seen as lacking in diversity and by implementing policies and practices that demonstrate to shareholders their commitment to increasing diversity.

PROPOSED CHANGES FROM CANADIAN SECURITIES REGULATORS

On April 13, 2023, the CSA released a notice proposing changes to corporate governance disclosure practices and guidelines (CSA Notice and Request for Comment – Proposed Amendments to Form 58-101F1 *Corporate Governance Disclosure* of National Instrument 58-101 *Disclosure of Corporate Governance Practices* and Proposed Changes to National Policy 58-201 *Corporate Governance Guidelines*).

The CSA is requesting comment on two approaches to proposed amendments to corporate governance disclosure rules and policy. These relate to the director nomination process, board renewal and diversity. While the two approaches are different they are both designed to promote diversity practices and disclosure beyond gender.

Approach A, supported by securities regulators in British Columbia, Alberta, Saskatchewan and the Northwest Territories, is less prescriptive and robust than Approach B.

Approach A would require companies to disclose their diversity policy as it relates to their boards and executive officers but would not mandate disclosure of any specific groups other than women. Companies would also be required to (a) describe their diversity objectives and how progress will be measured; (b) explain what mechanisms will be used to achieve their diversity objectives; and (c) disclose any data related to specific groups named in their diversity policy. Standardized tables or formats for disclosure would not be mandated.

According to the CSA, Approach A "is based on a view that securities regulators should not select categories of diversity, other than women, preferring to leave that to the issuer's determination as to what aspects of diversity are most beneficial to that issuer in advancing its business and strategy. In other words, a less prescriptive approach."

Approach B, supported by the OSC, is similar to the current CBCA approach. It would require companies to provide disclosure on the representation of women and four designated groups: Indigenous peoples, racialized persons, persons with disabilities and LGBTQ2SI+ persons, on boards and in executive officer positions. Companies would be required to report this data in a standardized tabular format to promote consistency and comparability. They would also be required to disclose any written strategy, written policies and measurable objectives relating to board diversity.

The securities regulators in Manitoba, Quebec, New Brunswick, Prince Edward Island, Nova Scotia, Newfoundland and Labrador, Yukon and Nunavut have not expressed a preference on approach at this time.

The proposed amendments were informed by consultations, research and reviews undertaken by the CSA and are open for public comment until July 12, 2023. The CSA are particularly interested in seeking feedback on how the two approaches address the needs of stakeholders.

Increasing Stakeholder Focus on Diversity Issues

INSTITUTIONAL INVESTORS AND KEY STAKEHOLDERS

In both Canada and the United States, diversity – and particularly racial and ethnic diversity – remains top of mind for an ever-increasing number of institutional investors and other key stakeholders, many of whom do not believe that companies have sufficiently advanced their diversity agendas. As a result, several have begun to take matters into their own hands, including by updating their engagement strategies and voting policies to address diversity disclosure issues and related board practices.

It has become clear that the investment community is looking to companies to provide more than simply demographic data. They want to know about the broader diversity policies and processes that companies have adopted. For investors, disclosure of this information signals that diversity discussions are at least happening at the board level. This is particularly relevant for companies that have been slower to implement diversity changes throughout their organizations, including with respect to the composition of their boards, executive teams and their overall employee base.

The following are notable recent examples that highlight the growing interest of institutional investors and key stakeholders in advancing diversity and promoting business-related diversity initiatives.

BlackRock

Beginning in 2022, BlackRock updated its proxy voting guidelines to encourage public companies to have at least one director who identified as a member of an underrepresented group (which includes individuals who identify as Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, or Native Hawaiian or Pacific Islander; individuals who identify as LGBTQ+; individuals who identify as underrepresented on the basis of national, Indigenous, religious or cultural identity; individuals with disabilities; and veterans). This is in addition to BlackRock's expectation that boards aspire to at least 30% diversity of membership, including at least two female directors.

In its 2022 Voting Spotlight, BlackRock disclosed that it did not support 1,664 directors at 936 companies globally owing to board diversity concerns. It also stated that in the United States, insufficient board diversity was BlackRock's top reason for not supporting a director.

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State Street Global Advisors

In an August 27, 2020 letter addressed to the chairs of corporate boards, State Street stated that "the lack of racial and ethnic diversity and inclusion poses risks to companies that senior managements and boards should understand and manage" and that "it is critical for boards and investors to have more robust information and data regarding the racial and ethnic workforce diversity of companies in their portfolios and to understand the steps they are taking to achieve relevant goals."

In January 2022, State Street published formal guidance on diversity disclosures and practices, which included the following:

- State Street will vote against the chair of the nominating committee of any company in the S&P 500 or FTSE 100 that does not disclose the racial and ethnic composition of its board or does not have at least one director from an underrepresented racial or ethnic community.

- State Street expects company boards in all markets and indices to have at least one female director.

- State Street expects companies in major indices in the United States, Canada, United Kingdom, Europe and

Australia (Russell 3000, TSX, FTSE 350, STOXX 600 and ASX 300) to have boards comprising at least 30% female directors; however, a company may waive the policy if it engages with State Street and provides a specific, timebound plan for reaching 30% representation of female directors.

While State Street has primarily focused on increasing diversity at the board level, it has indicated that it intends to shift its focus to the workforce and executive levels in the coming years. To this end, State Street advised companies to begin focusing on recruiting, promoting and retaining diverse individuals throughout their organizations.

Vanguard

Vanguard recently updated its diversity guidelines in its proxy voting policy for Canadian portfolio companies. Vanguard will now generally vote against the nominating and/or governance committee chair (or other directors, if applicable) if a company's board is making insufficient progress in its diversity composition or in adequately preparing its board diversity disclosure. To determine progress on enhanced board diversity and disclosure, Vanguard will consider applicable market regulations and expectations.

Furthermore, Vanguard's proxy voting policy now includes a fairly robust set of guidelines relating to diversity, including the following:

– Boards should have a range of perspectives that are informed by a variety of backgrounds, skills and experiences, and they should represent diversity of personal characteristics, including at least diversity of gender.

– Companies should make progress in ensuring the representation on their boards of other forms of diversity beyond just gender, including specifically underrepresented racial or ethnic groups and Indigenous persons.

– Boards should take action to ensure that their board compositions are appropriately representative, relative to their markets and to the needs of their long-term strategies. Since many boards still have an opportunity to increase diversity in many areas, Vanguard believes that such boards should demonstrate how they intend to continue to make progress.

– Vanguard may vote against the nominating and/or governance committee chair (or other directors, if applicable) if a board is less than 30% gender diverse.

A recent paper by The European Corporate Governance Institute – *The Big Three and Board Gender Diversity: The Effectiveness of Shareholder Voice* – indicated that BlackRock, State Street and Vanguard could be responsible for up to two-thirds of the 50% spike in women on U.S. company boards in recent years. The research also found that the 2017 campaigns launched by these institutional investors to increase gender diversity on corporate boards contributed to U.S. companies appointing at least two-and-a-half times as many female directors in 2019 compared with 2016. These findings highlight, among other things, the impact that investors, and especially institutional investors, can have on companies and their ability to influence change.

Nasdaq

On August 6, 2021, the United States Securities and Exchange Commission (SEC) approved the Nasdaq's proposal to amend its listing standards to encourage greater board diversity and to require board diversity disclosures for Nasdaq companies. The new rules require all companies listed on the Nasdaq exchange to publicly disclose consistent and transparent diversity statistics regarding their boards. Subject to certain exceptions, most Nasdaq companies are also required to have, or to explain why they do not have, at least two diverse directors, including one female director and one other director who identifies as either LGBTQ+ or an underrepresented minority (which the Nasdaq defines as an individual who self-identifies in one or more of the following groups:

Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander or two or more races or ethnicities). The new requirements are to be phased in by Nasdaq companies between 2023 and 2026, with the specific timing depending on the particular requirement and the company's listing tier.

SHAREHOLDER ACTIVISM/SPACS

Diversity on its own is not currently a key driver of shareholder activism, but poor performance and disclosure of diversity within a company can be emblematic of, and a contributor to, overall lacklustre company performance and poor corporate governance. This can expose companies to shareholder activism, with poor diversity being used by dissident shareholders to build support for their director candidates and their campaign for change within a company. While climate change has often been viewed as a top priority for shareholders, we expect to see a larger number of social mandates revolving around diversity in the years to come.

In recent years, we have also witnessed the rise of special purpose acquisition companies (SPACs) as popular investment vehicles, especially in the United States. SPACs have typically performed poorly on most diversity metrics for a multitude of reasons, including that SPAC transactions are mostly negotiated in private and SPACs are usually exempt from diversity regulations because of their board size. However, as attention on SPACs and public scrutiny on all forms of diversity increase, regulation and expectations of SPACs will likely shift. In January 2021, Empowerment & Inclusion Capital I Corp (EICC), the first purpose-driven SPAC that focused on acquiring a diverse-led business or a business focused on promoting an inclusive economy and society closed its IPO and raised US$276 million. It will be interesting to see whether EICC is a signal of similarly laudable diversity initiatives in the SPAC space in the future.

"By pushing its listed companies to address racial and gender equity in corporate boards, Nasdaq is heeding the call of the moment. Incremental change and window-dressing isn't going to cut it anymore as consumers, stakeholders and the government increasingly hold corporate America's feet to the fire. Nasdaq's efforts to prod and push its listed companies is a welcomed and necessary first step. With increased representation of people of color, women and LGBTQ people on corporate boards, corporations will have to take actionable steps to ensure underrepresented communities have a seat at the table." Anthony Romero, executive director, American Civil Liberties Union

Our Take:
Prepare for Change

In the 2020 edition of *Davies Governance Insights*, we highlighted how boards and senior management should be thinking about their overall corporate governance frameworks and placing a greater emphasis on all forms of diversity in light of recent world events relating to diversity, systemic racism and discrimination. The calls for more diversity and representation in all aspects of society, including business, have only grown louder and now seem to be at the forefront of the minds of market participants and regulators. With further regulatory changes likely forthcoming in both Canada and the United States, it is imperative that companies review and enhance their diversity initiatives and policies, and demonstrate their willingness to take concrete actions to address company diversity so that they are best prepared to navigate the changing legal, social and business landscape.

Database and Methodology

The quantitative analysis in this publication, except when otherwise noted, is based on data provided by ISS Corporate Solutions, Inc., and drawn from the management information circulars of 424 issuers on the Toronto Stock Exchange (TSX) issued between August 1, 2021 and July 31, 2022, which are included in one (or both) of the S&P/TSX Composite Index and the S&P/TSX SmallCap Index as at May 31, 2022. Descriptions of the relevant indices discussed in this report are set out below.

Composite Index: The S&P/TSX Composite Index (referred to as the Composite Index) comprises 239 issuers. It is the "headline index" and the principal broad market measure for the Canadian equity markets. It includes common stock and income trust units. Six of the 239 Composite Index issuers did not issue proxy circulars for the relevant period discussed; accordingly, our analysis is based on 233 Composite Index issuers.

Two components of the Composite Index are referred to in this report:

- **TSX 60:** The S&P/TSX 60 Index (referred to as the TSX 60) is a subset of the Composite Index and represents Canada's 60 largest issuers by market capitalization. (Our analysis includes only 59 of the issuers on the TSX 60 because, as noted above, one issuer on the TSX 60 did not issue a proxy circular during the period covered.)
- **Completion Index:** The S&P/TSX Completion Index (referred to as the Completion Index) is the Composite Index excluding the TSX 60 issuers. It comprises 179 issuers. (Our analysis includes only 174 of the issuers on the Completion Index because, as noted above, five issuers on the Completion Index did not issue proxy circulars during the period covered.)

SmallCap Index: The S&P/TSX SmallCap Index (referred to as the SmallCap Index) includes 230 issuers, 35 of which also meet the market capitalization eligibility criteria and are part of the Composite Index. (Our analysis includes only 225 of the issuers on the SmallCap Index because five issuers did not issue a circular for the period covered.)

The number and specific constituents of the two indices covered in our study universe change periodically. These factors may, in some cases, affect comparisons of data points year over year.

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