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**BY EMAIL**

British Columbia Securities Commission  
Alberta Securities Commission  
Saskatchewan Financial Services Commission  
Manitoba Securities Commission  
Ontario Securities Commission  
Autorité des marchés financiers  
New Brunswick Securities Commission  
Registrar of Securities, 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

**To the attention of:**

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Gentlemen and Mesdames

**CSA Notice and Request for Comment on Proposed Amendments to Multilateral Instrument 62-104 *Take-Over Bids and Issuer Bids* and National Instrument 62-103 *Early Warning System and Related Take-Over Bid and Insider Reporting Issues* and Proposed Changes to National Policy 62-203 *Take-Over Bids and Issuer Bids* (the “Draft Amendments to the Early Warning Requirements”)**


This letter is submitted in response to the CSA Notice and Request for Comment on the Draft Amendments to the Early Warning Requirements published on March 13, 2013.



We have participated in the preparation of Norton Rose Fulbright Canada's letter dated July 11, 2013, a copy of which is attached hereto, and confirm that we agree with the comments expressed therein.

Please do not hesitate to contact the undersigned should you have any questions.

Yours very truly,



**Simon Rivet**  
Vice-President, General Counsel  
and Corporate Secretary  
/db

C.C. Mr. Thierry Dorval, Norton Rose Fulbright Canada LLP  
Mr. Pierre H Lessard, Executive Chairman of the Board, Metro Inc.  
Mr. Eric La Flèche, President and Chief Executive Officer, Metro Inc.



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**CSA Notice and Request for Comment on Proposed Amendments to Multilateral Instrument 62-104 *Take-Over Bids and Issuer Bids* and National Instrument 62-103 *Early Warning System and Related Take-Over Bid and Insider Reporting Issues* and Proposed Changes to National Policy 62-203 *Take-Over Bids and Issuer Bids* (the “Draft Amendments to the Early Warning Requirements”)**

This letter is submitted in response to the CSA Notice and Request for Comment on the Draft Amendments to the Early Warning Requirements published on March 13, 2013. It reflects the views of a working group made up of issuers having a combined market capitalization of more than \$35 billion (the **Working Group**). We thank you for affording us an opportunity to comment on this important topic.

We begin by highlighting a number of developments in the Canadian securities markets which make it more necessary than ever for the CSA to go ahead with the proposed amendments. We then go on to address most of the specific questions raised by the CSA.

**1 GENERAL**

For the reasons discussed below, the Working Group generally agrees with the Draft Amendments to the Early Warning Requirements proposed by the CSA and is also of the view that such amendments, including the reduction of the early warning reporting threshold (the “**Early Warning Threshold**”) from 10% to 5% and enhanced scope of the disclosure obligations, will provide greater transparency about significant holdings of an issuer’s securities.

**(a) Early Warning Threshold in other jurisdictions**

Our system needs to be modernized. Canada's current Early Warning Threshold of 10% puts us in the company of jurisdictions such as Latvia and Pakistan. A 5% Early Warning Threshold would bring Canadian securities legislation in line with beneficial ownership disclosure requirements of other major capital market jurisdictions, such as the United States, Australia, Japan and Hong Kong. The United Kingdom and Germany have gone even further by imposing a 3% threshold, while Italy applies a 2% threshold.

**(b) Need for reporting issuers to be able to identify their shareholder base**

Most corporate regimes in Canada provide for shares to be issued in registered form and for the corporations themselves or their registrars and transfer agents to maintain records of shareholders and their share ownership, thus allowing issuers to know the identity of their registered shareholders and engage in a dialogue with them where required.

However, with the majority of securities owned by institutional and individual investors in Canada being held in street name (estimates based on anecdotal information range from 80% street name holding to 100% in the case of more recent book-based-only IPOs), reporting issuers have largely lost the ability to know who owns their shares. Issuers can piece together information on their shareholders under limited circumstances, such as where the shareholder is a non-objecting beneficial owner under National Instrument 54-101 – Communications with Beneficial Owners, or where a shareholder has crossed the current 10% Early Warning Threshold (press release and report under National Instrument 62-103 – Early Warning System).

Issuers may also use proxy solicitation firms, such as Kingsdale Shareholder Services, Georgeson Shareholder, Laurel Hill or others, which offer shareholder identity monitoring services. After they are retained by an issuer, these firms may perform haphazard interpolations of various available data points to try to identify the more significant beneficial owners of a given issuer and attempt to keep the information up to date between annual meetings.

The existing rules and interaction of the systems currently in place, including the current 10% Early Warning Threshold, result in most reporting issuers having a very limited picture of their shareholder base, which is clearly at odds with the intent of the statutes governing most corporations incorporated in Canada, such as the *Canada Business Corporations Act*, as well as with the greater level of engagement with shareholders required of reporting issuers under evolving best corporate governance practices.

**(c) Need for reporting issuers to communicate with their shareholders in light of evolving best corporate governance practices**

**(i) Shareholder Engagement**

Best practices in corporate governance require issuers to be engaged with shareholders. Many issuers have adopted formal engagement policies and try in good faith to reach out to their shareholders and other stakeholders. However, such issuers are often faced with a very opaque system where they cannot even identify who their most important shareholders are.

Say-on-pay is an interesting example of the problems faced by issuers. As of the date of this letter, numerous senior Canadian reporting issuers, including major Canadian financial institutions, have moved ahead with Say-on-Pay votes at their annual general meetings. Say-on-Pay votes allow shareholders to express approval or disapproval of compensation practices. In order to avoid misunderstandings on complex compensation policies and principles and promote acceptance before the actual shareholders' meeting is held, issuers often need to be able to engage in a dialogue on compensation policies and principles with key shareholders. However, in the Working Group's experience, finding information about shareholders who hold between 5% and 10% of the share capital of Canadian issuers can be a major challenge.

If shareholders wish for more engagement from issuers, the ownership of issuers' shares in turn needs to be more transparent.

(ii) Proxy Fights

The current regulatory regime in Canada is favourable to dissenting shareholders wishing to mount or threatening to launch a proxy fight. The two key statutory components that make proxy fights possible in Canada are the ability of shareholders to requisition meetings and the ability of shareholders to communicate among themselves with respect to their voting intentions.

Under the *Canada Business Corporations Act*, holders, jointly or individually, of 5% or more of the issued and outstanding shares may requisition a special meeting of shareholders. Proxy solicitation rules in Canada allow the solicitation of proxies from not more than 15 shareholders.

Activist hedge funds that hold less than 10% of a corporation's shares and thus remain below the Early Warning Threshold may communicate with issuers to request short-term share value enhancing corporate actions (such as a special dividend, return of capital, share repurchase or division sale) and threaten a proxy fight to replace the issuer's board if the issuer's board does not cooperate.

The current street name beneficial ownership regime, combined with the current high Early Warning Threshold, makes it possible for activist hedge funds to deploy in Canada what are called "wolfpack strategies": activist hedge funds claim in their discussions with issuers widespread support for their proposals from a significant number of significant shareholders (not more than 15 of them, each holding less than 10% of the shares). The reporting issuer on the receiving end of an activist hedge fund wolfpack strategy to force a short-term share value enhancing corporate action may not have the tools necessary to debunk the alleged shareholder support.

A revised 5% Early Warning Threshold will provide reporting issuers with significantly more visibility into their shareholder base and a greater ability to engage directly in discussions with shareholders, either in response to threats from activist hedge funds or on significant governance issues.

## **2 SPECIFIC QUESTIONS**

1. *Do you agree with our proposal to maintain the requirement for further reporting at 2% or should we require further reporting at 1%? Please explain why or why not.*

Members of the Working Group were generally in favour of maintaining the 2% in order to avoid increasing the compliance burden even more. Also, signalling a decrease in a position could have a detrimental effect on prices and liquidity in the market as other market participants react to that information.

Obviously, there are also strong arguments in favour of establishing a 1% further reporting threshold. First, it would further enhance the market transparency and efficiency discussed above. Second, it would only be consistent to maintain a one-fifth ratio between the initial threshold and the further reporting threshold. Given that the further reporting threshold was 2% under a 10% initial reporting threshold, it is only logical that the further reporting ratio be lowered to 1% to match a 5% initial reporting threshold. The Canadian Investor Relations Institute (CIRI) advocates in favour of lowering the further reporting threshold to 1% for these reasons. It should also be noted that the United States, the United Kingdom and Australia apply a 1% further reporting threshold. Adopting such a standard would bring Canada even further in line with those major capital market jurisdictions.

2. *A person cannot acquire further securities for a period beginning at the date of acquisition until one business day after the filing of the report. This trading moratorium is not applicable to acquisitions that result in the person acquiring beneficial ownership of, or control or direction over, 20% or more of the voting or equity securities on the basis that the take-over bid provisions are applicable at the 20% level.*

*The proposed decrease to the early warning reporting threshold would result in the moratorium applying at the 5% ownership threshold. We believe that the purpose of the moratorium is still valid at the 5% level because the market should be alerted of the acquisition before the acquiror is permitted to make additional purchases.*

- (a) Do you agree with our proposal to apply the moratorium provisions at the 5% level or do you believe that the moratorium should not be applicable between the 5% and 10% ownership levels? Please explain your views.*

The moratorium provisions should apply at the 5% level, as the moratorium should go hand in hand with the Early Warning Threshold.

- (b) The moratorium provisions apply to acquisitions of "equity equivalent derivatives". Do you agree with this approach? Please explain why or why not.*

The Working Group agrees with applying moratorium provisions to "equity equivalent derivatives" as the same economic logic applies to those instruments as to conventional equity holdings.

- (c) Do you think that a moratorium is effective? Is the exception at the 20% threshold justified? Please explain why or why not.*

The Working Group believes that a moratorium or cooling-off period is effective to make sure that the market has time to react and that new information about block ownership is impounded into share prices.

The exception at the 20% threshold is justified given that take-over bid provisions would be engaged at that stage.

3. *We currently recognize that accelerated reporting is necessary if securities are acquired during a take-over bid by requiring a news release at the 5% threshold to be filed before the opening of trading on the next business day.*

*With the Proposed Amendments to the early warning reporting threshold, we do not propose to further accelerate early warning reporting during a take-over bid.*

- (a) Do you agree? Please explain why or why not.*

The Working Group agrees with maintaining a 5% reporting threshold in the context of a take-over bid, as the purpose of ensuring greater transparency to identify influential block holders would already be fulfilled.

- (b) If you disagree, how should we accelerate reporting of transactions during a take-over bid? Should we decrease the threshold for reporting changes from 2% to 1%? Or do you think that requiring early warning reporting at the 3% level is a more appropriate manner to accelerate disclosure? Please explain your views.*

[Not applicable in light of the previous answer.]

4. *The Proposed Amendments would apply to all acquirors including EILs.*

*(a) Should the proposed early warning threshold of 5% apply to EILs reporting under the AMR system provided in Part 4 of NI 62-103? Please explain why or why not.*

The Working Group is of the view that the 5% threshold should apply equally to all acquirors, including EILs for the same transparency and efficiency reasons discussed previously.

*(b) Please describe any significant burden for these investors or potential benefits for our capital markets if we require EILs to report at the 5% level.*

The potential benefits are the same as those applying generally that were discussed previously.

The Working Group does not believe that imposing such reporting duty on EILs would impose an unreasonable burden on them, in light of the fact that they have reporting duties at a 5% level in other jurisdictions, such as the United Kingdom and Germany.

5. *Mutual funds that are reporting issuers are not EILs as defined in NI 62-103 and are therefore subject to the general early warning requirements in NI 62-104. Are there any significant benefits to our capital markets in requiring mutual funds to comply with early warning requirements at the proposed threshold of 5% or does the burden of reporting at 5% outweigh the potential benefits? Please explain why or why not.*

For the same efficiency and transparency reasons discussed previously, the Working Group believes that mutual funds should comply with the 5% Early Warning Threshold applied to other standard issuers.

6. *As explained above, we propose to amend the calculation of the threshold for filing early warning reports so that an investor would need to include within the early warning calculation certain equity derivative positions that are substantially equivalent in economic terms to conventional equity holdings. These provisions would only capture derivatives that substantially replicate the economic consequences of ownership and would not capture partial-exposure instruments (e.g., options and collars that provide the investor with only limited exposure to the reference securities). Do you agree with this approach? If not, how should we deal with partial-exposure instruments?*

The Working Group agrees with this approach. In order to ensure the efficiency of the Early Warning system and preserve market transparency and integrity, it is crucial that holders of substantially equivalent derivative instruments be subject to the 5% Early Warning Threshold. Such disclosure would curb hidden ownership, allow issuers to identify the persons that have actual voting rights at the general meeting and make it easier for issuers to engage with those holders. As exemplified by our recent Telus case in Canada, the “creative” use of derivatives can lead to surprising results. In another example abroad, in October 2010, LVMH surprised the market when it announced that it held a 17%-interest in Hermès. LVMH’s stake in Hermès increased to 22% since then. LVMH managed to acquire such interest through complex financial products held by LVMH international subsidiaries. The French Autorité des Marchés Financiers is currently investigating this case. The application of the proposed Early Warning system to derivatives is necessary to ensure that transactions are made in a transparent manner.

The Working Group also agrees that partial-exposure instruments should not be captured, as such instruments do not necessarily replicate the economic consequences of ownership and would lead to over-reporting. Moreover, these instruments are often held by institutional investors as part of an investment strategy that is not always useful to have reported publicly.

7. *We propose changes to NP 62-203 in relation to the definition of equity equivalent derivative to explain when we would consider a derivative to substantially replicate the economic consequences of ownership of the reference securities. Do you agree with the approach we propose?*

The Working Group agrees with this approach.

8. *Do you agree with the proposed disqualification from the AMR system for an EII who solicits or intends to solicit proxies from security holders on matters relating to the election of directors of the reporting issuer or to a reorganization or similar corporate action involving the securities of the reporting issuer? Are these the appropriate circumstances to disqualify an EII? Please explain, or if you disagree, please suggest alternative circumstances.*

The Working Group agrees with the proposed disqualification from the AMR system for EII's involved in proxy solicitation. If they actively engage with an issuer's security holders for the purposes of influencing the vote at a shareholders meeting, they should be subject to the same scrutiny as other equity holders.

That being said, the Working Group believes that what is meant by "solicit" should be further specified. For example, it is unclear whether it applies to EII's soliciting proxies both alone or in concert with other persons. Reference to the definition of "solicit" found at section 147 of the *Canada Business Corporations Act* could be useful.

9. *We propose to exempt from early warning requirements acquirors that are lenders in securities lending arrangements and that meet certain conditions. Do you agree with this proposal? Please explain why or why not.*

The Working Group agrees with this proposal and believes that the conditions required to meet the exemption are sensible. It is indeed not useful to alert the market to a change in position of a lender who has the option of recalling his shares at will. Other market participants could react negatively to such information, thereby provoking an unwarranted reduction in price and liquidity in that market for no valid reason.

10. *Do you agree with the proposed definition of "specified securities lending arrangement"? If not, what changes would you suggest?*

The Working Group agrees with the proposed definition, for the reasons mentioned under the previous question.

11. *We are not proposing at this time an exemption for persons that borrow securities under securities lending arrangements as we believe securities borrowing may give rise to empty voting situations for which disclosure should be prescribed under our early warning disclosure regime. Do you agree with this view? If not, why not?*

The Working Group agrees with this view as it is also concerned with empty voting situations and values greater transparency in that regard. The Working Group considers that it is important for issuers to have information about the identity and position of a borrower of securities who has voting rights without a corresponding economic interest in the securities, as borrowers often use such votes to further personal interests that are unrelated to the maximization of the value of an issuer.

12. *Do the proposed changes to the early warning framework adequately address transparency concerns over securities lending transactions? If not, what other amendments should be made to address these concerns?*

The Working Group believes that the proposed changes adequately address transparency concerns over securities lending transactions. The Working Group's main concern with regard to securities lending transactions is knowing the identity and position of securities borrowers, who hold voting rights without any corresponding



economic interest. Securities borrowers often have an agenda different from that of ordinary shareholders, and it is important for issuers to know these persons in order to be able to engage with them.

*13. Do you agree with our proposal to apply the Proposed Amendments to all reporting issuers including venture issuers? Please explain why or why not. Do you think that only some and not all of the Proposed Amendments should apply to venture issuers? If so, which ones and why?*

For purposes of greater market transparency and efficiency, the Working Group is of the view that in principle, the Proposed Amendments should apply to all reporting issuers.

However, the Working Group understands that a 5% Early Warning Threshold may have adverse effects on small and mid-cap issuers that benefit from funding from institutional investors. In order to avoid disclosing their position, these investors may prefer to invest in an amount under the 5% threshold, thus restricting the sources of funding of smaller issuers. It should also be noted that these investors change their positions regularly for reasons often unrelated to an issuer's performance. Reporting of an investor's intention to sell its position in a small or mid-cap issuer may send an unwarranted negative signal to the market with regard to that issuer. Hence, the Working Group would not be opposed to certain exemptions being applied with regard to small or mid-cap issuers.

### **3 CONCLUSION**

In light of the internationally recognized Early Warning Threshold of 5%, the growing need for Canadian reporting issuers to be able to identify their shareholder base more clearly in order to further governance initiatives with an open dialogue, and in the absence of compelling reasons for maintaining a 10% Early Warning Threshold in Canada, the Working Group strongly advocates the implementation of the Draft Amendments to the Early Warning Requirements.

Thank you for allowing us to comment on this subject.

Yours truly,

(s) Norton Rose Fulbright Canada LLP