



Canadian Investor Relations Institute
Institut canadien des relations avec les investisseurs

601, 67 Yonge St. Toronto ON M5E 1J8
Telephone: (416) 364-8200, Fax: (416) 364-2805, Website: CIRI.org

September 12, 2012

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

Mr. John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario
M5H 3S8
e-mail: jstevenson@osc.gov.on.ca

Me Anne-Marie Beaudoin, Corporate Secretary
Autorité des marchés financiers
800, Square Victoria, 22e étage
C.P. 246, Tour de la Bourse
Montréal, Québec H4Z 1G3
e-mail: consultation-en-cours@lautorite.qc.ca

Dear Mr. Stevenson and Me Beaudoin

Re: CSA Consultation Paper 25-401: Potential Regulation of Proxy Advisory Firms

The Canadian Investor Relations Institute (“CIRI”), a professional, not-for-profit association of executives responsible for communication between public corporations, investors and the financial community, is pleased to respond to Consultation Paper 25-401 (“the Paper”). CIRI is a strong advocate of good corporate governance practices as one element contributing to the integrity and efficiency of the capital markets and has previously expressed concerns regarding the influence and practices of proxy advisory (“PA”) firms. CIRI membership represents approximately 300 publicly listed issuers with a combined market capitalization of just under \$1.4 trillion. More information about CIRI is noted in Appendix 1.

General Statement of Concern

CIRI is aware that institutional investors are faced with an increasing volume of proxy-related disclosure information containing more complicated detail regarding governance-related issues including compensation plans, board structure, risk oversight, management performance and director qualifications. CIRI also recognizes that PA Firms play a beneficial role by providing services that can improve institutional investors' ability to exercise their stewardship responsibilities.

However, CIRI believes that the influence of PA Firms in the proxy voting process has increased significantly, that too many factual errors are being found in PA Firm research reports, that PA Firms have to-date demonstrated a lack of transparency and engagement; two key drivers of market integrity and efficiency. CIRI believes the current situation with regard to the role and practices of PA Firms is flawed and that some regulatory driven changes are appropriate to increase the integrity and transparency of the proxy voting process and to reduce the potential for ill-informed voting decisions. It is from this perspective that CIRI views the CSA Paper and provides not only a series of comments on selected questions as posed in the CSA Paper but also makes Key Recommendations for consideration regarding the regulation of proxy advisory firms.

Key Recommendations

CIRI believes that there should be some level of regulatory oversight of PA Firms in order to ensure transparency, which contributes to the integrity of the capital market. CIRI is proposing the following regulations:

- a) PA Firms should be required to disclose methodologies, sources of information, assumptions used to prepare their research reports and rationale for their voting recommendations;
- b) PA Firms should prominently identify in the research reports and voting recommendations provided to their institutional investor clients any specific potential conflicts of interest with regard to the issuer and analyst/reviewer ownership interests;
- c) PA Firms should be required to provide to all issuers draft research reports and voting recommendations for review for factual accuracy allowing 48 to 72 business hours for issuers to respond prior to the report being distributed to the PA Firm's clients;
- d) PA Firms should be required to include in the final report to investors any comments provided by issuers regarding the review process, the research report and the voting recommendations;
- e) PA Firms should establish an appeals process and identify an independent third-party or Ombudsman to adjudicate on behalf of those issuers who have concerns about a research report that cannot be resolved through direct dialogue with the PA Firm; and
- f) Institutional investors who use a PA Firm should comply or explain why they do not comply, with a requirement to disclose how they assess the advice received from the PA Firm and not automatically follow it.

Comments on Selected Questions from the Consultation Paper:

General

1. **Do you agree, or disagree, with each of the concerns identified in the Consultation Paper, namely: (i) potential conflicts of interest, (ii) perceived lack of transparency, (iii) potential inaccuracies and limited engagement with issuers, (iv) potentially inappropriate influence on corporate governance practices, and (v) the extent of reliance by institutional investors on the advice of such firms? Please explain and, if you disagree, please provide specific reasons for your position.**

(i) CIRI has consistently maintained that identifying and managing potential conflicts of interest is paramount for establishing and maintaining market integrity. It is clear that the influence of PA Firms on institutional

investor voting has increased significantly, principally as it affects reporting issuers whose shareholder base is largely comprised of institutional holders and who engage PA firms for consulting advice.

(ii) CIRI maintains that capital market integrity is enhanced through the consistent application of policies and procedures that are as transparent as possible. The increasing reliance by institutional investors on the research and voting recommendations of PA Firms is understandable, as indicated earlier, but is nonetheless problematic, primarily due to the lack of visibility by various market participants into the policies, methodologies, sources of information, assumptions and analytical models used by the PA Firms as well as the issue of factual inaccuracies in research reports.

(iii) The most pressing issue raised by issuers is the number of errors or factual inaccuracies in reports and recommendations from PA firms. A recent CIRI member survey revealed that a mere 13% of respondents reported no factual inaccuracies in PA Firm reports over the past five years. Fully one-quarter of respondents indicated that factual inaccuracies occurred ‘frequently’ with another 40% indicating that factual inaccuracies occurred “half the time” or “occasionally” over that time period.

(iv) As referenced throughout the CSA Paper, CIRI believes greater engagement through dialogue and discussion between PA Firms and issuers, especially before the PA Firm distributes its report to institutional investors, would significantly reduce factual errors, misapplications of the PA Firm’s policies, and incomplete or incorrect analyses. This would lead to better decision-making in the voting process and avoid the need for institutional investors to recast their vote(s) subsequent to revised reports being issued by the PA Firms, possibly with different voting recommendations.

(iv) CIRI agrees that the influence of PA Firms on corporate governance standards is growing as institutional investors increasingly seek their services. This trend is problematic, primarily due to the lack of visibility into the policies and decisions of the PA Firms. Indeed, by rating issuers against governance ‘best practices’ as defined by themselves, despite attempts to introduce various consultation processes, it remains clear that PA Firms are in essence shaping corporate governance rather than simply evaluating it. This activity could be construed as PA Firms creating business opportunities for themselves. As long as governance best practices remain relatively static, the ability of PA Firms to sell consulting services to issuers would reduce over time. However, in an environment where the best practices are always changing, the opportunity arises for PA Firms to provide even more consulting services that generate more revenue.

(v) CIRI believes that institutional investors are increasingly reliant upon PA Firms for voting recommendations given that corporate disclosure materials are more detailed and complex as issuers respond to stakeholders’ desire for increased transparency. CIRI is concerned that there may be an undue reliance on PA Firms’ research and recommendations, particularly among those smaller institutional investors (as pointed out in the Consultation Paper – page 5683) who may not have the necessary time, internal resources and expertise to conduct their own research and who may choose to rely more heavily on the research and recommendations of the PA Firms for voting guidance.

2. Are there other material concerns with proxy advisory firms that have not been identified? Please explain.

CIRI believes there is an unintended consequence that currently contributes to the lack of dialogue and discussion between an issuer and a PA Firm when that PA Firm is also in the for-profit consulting business. Simply put, we are concerned when told by some issuers that the proxy voting advisory arm of PA Firms are limiting their willingness to enter into dialogue with issuers (regarding research reports and voting recommendations) and instead are directing those same issuers to deal with the for-profit corporate consulting services arm of the business.

3. Are there specific gaps in the current practices of proxy advisory firms, which justify regulatory intervention? Is there a concern that future gaps could be created as a result of new entrants or changes in business or other practices?

There are two significant gaps in the current practices of PA Firms. The first is their documented lack of willingness to provide all issuers with a draft of the research report and to engage in dialogue with issuers prior to the report being sent to institutional investors. Closing this gap by engaging with issuers of all market cap sizes in this manner will go a long way toward identifying and rectifying factual errors while providing investors with higher quality information on which to base voting decisions.

The second gap is that issuers do not have the ability to have their comments included in the initial report issued by PA Firms to their clients. Closing this gap would ensure that the clients of PA Firms, especially the small and medium institutional investors, would have the appropriate level of information to make an informed voting decision.

4. Do you believe that the activities of Proxy Advisory Firms should be regulated in some respects and, if so, why and how?

CIRI believes that PA Firms should be subject to a degree of regulatory oversight given that their business model results in an obvious conflict of interest at a point in time when their influence over setting and evaluating corporate governance standards is steadily increasing. Furthermore, limited engagement with issuers coupled with a documented history of errors in reports leading to questionable voting recommendations, indicates that some degree of regulatory oversight regarding engagement is appropriate.

CIRI also believes regulation is needed to include issuer comments in the PA Firm's report in order to provide institutional investors (especially small and mid-sized institutions) with complete information upon which to base their voting decision.

CIRI has set out specific recommendations in the answers to the following questions and summarized above under Key Recommendations.

Potential Conflicts of Interest

- 5. To what extent do you consider proxy advisory firms to: (i) be subject to conflicts of interest in practice, (ii) already have in place appropriate conflict mitigation measures, and (iii) be sufficiently transparent regarding the potential conflicts of interests they may face? If you are of the view that current disclosure by proxy advisory firms regarding potential conflicts of interest is not sufficient, please provide specific examples of such insufficient conflicts of interest disclosure and suggestions as to how such disclosure could be improved.**

It seems wholly appropriate, given the increasing influence of PA Firms on the proxy voting process, that PA Firms should be required to establish, implement and regularly update effective policies and procedures to manage any real or perceived conflicts of interest in connection with their voting recommendations. It is also appropriate for PA Firms to publicly state that being in the for-profit corporate consulting business does not in any way restrict or limit their ability or willingness to enter into dialogue and discussion with issuers via their proxy advisory business and does not impact changes to governance best practices that they recommend on an annual basis.

Furthermore, and consistent with the extensive continuous disclosure requirements established for reporting issuers, PA Firms should be required to publicly disclose such conflict of interest policies and procedures and should also be required to prominently identify any specific potential conflicts in the research reports and voting recommendations provided to their institutional investor clients.

CIRI is not, at this time, recommending that PA firms separate their proxy voting services from advisory or consulting services into individual stand-alone businesses. There are numerous examples throughout the capital markets where similar forms of potential conflicts are effectively managed, such as between the investment banking and equity research arms of banks and brokerages.

- 6. If you are of the view that there are conflicts of interest within proxy advisory firms that have not been appropriately mitigated, which of these are the most serious in terms of the potential (negative) impact on development of their voting recommendations and why?**

While the CSA Paper discusses potential conflicts regarding PA Firm ownership structure and voting recommendations on shareholder proposals initiated by an investor client, CIRI is most concerned about a PA Firm providing voting recommendations on governance issues while concurrently providing governance related consulting services to the same issuer. The ability of PA Firms to run an unregulated consulting business that advises issuers on how to achieve an approval rating from the advisory side of their business is fraught with potential conflicts.

In addition, CIRI suggests that reports to investors include a declaration if either the analyst at the PA Firm or any other reviewer has an ownership interest in the stock of the issuer under review. Such a declaration would be consistent with the practice followed by equity research analysts.

- 7. Should we propose an amendment to NI 51-102 to require reporting issuers to disclose consulting services from proxy advisors in their proxy circular? Or would such disclosure undermine the existing controls and procedures (i.e., “ethical wall”) in place, which currently may prevent proxy advisory firm research staff who reviews an issuer’s disclosure from being made aware of the identity of their firm’s consulting clients?**

A key concern of virtually every issuer polled by CIRI is the conflict of interest between a PA Firm’s proxy advisory service and its for-profit consulting service. Any new regulation that may weaken existing controls

and procedures (i.e., “ethical wall”) only serves to heighten the potential for abuse inherent in that potential conflict. Other organizations, such as investment banking firms with equity research arms, have established significant controls to avoid breaches of such an ethical wall – to the extent that in some cases a banker and an analyst are not allowed to be in the same room with any issuer under research coverage. CIRI firmly believes that an amendment to NI 51-102 to require issuers to disclose consulting services from a PA Firm would serve only to weaken the already weak controls that PA Firms have put in place.

Perceived Lack of Transparency

8. Could disclosure of underlying methodologies and analysis provide beneficial information to the market or would the commercial costs of doing so be too significant?

In a recent survey of CIRI members 100% of survey respondents replied “YES” to a question that asked if it is an appropriate regulatory requirement that PA Firms be required to disclose their methodologies, sources of information used, assumptions and rationale for their voting recommendations.

In addition to the disclosure of general policies and guidelines at PA Firms, there are concerns that the application of the governance and/or voting guidelines of PA Firms may be too formulaic to properly assess the unique aspects of individual issuers. All-encompassing policies and rigid definitions designed for multiple jurisdictions can lead to a lack of appreciation of real and important differences among issuers (e.g. capitalization, sector, appropriate governance policies, corporate domicile, peer group comparisons, risk factors, etc.).

Simply put, if market participants cannot see how the PA firm reached its recommendations then how can the market participants judge the quality of the recommendations and, in the case of institutional investors, to what extent will they use the PA firms recommendations in determining their vote.

The combination of (i) disclosure of PA Firms methodologies, assumptions and analysis, (ii) enhanced dialogue and engagement with issuers prior to report distribution and (iii) inclusion of issuer comments in the report would result in a significant improvement in the quality of the shareholder vote, market integrity and efficiency.

Inaccuracies and Issuer Engagement

9. To what extent could there be an improvement in the dialogue with issuers during the vote recommendation process?

Based on member feedback, there seems to be little dialogue between PA Firms and issuers prior to the issuance of research reports and voting recommendations. The recent survey of CIRI members indicated that less than 25% of respondents always receive such draft reports from at least one PA firm either before or after the PA firm distributes the report to its clients and more than one-third either seldom or never receive draft reports.

The current lack of communication goes against the grain of investor relations practitioners, whose own activities are premised on open, transparent and fulsome dialogue between parties to foster understanding

and informed decision-making. CIRI believes that errors can be avoided through improved communication and this is not happening between PA Firms and issuers in the current unregulated environment. CIRI believes conceptually that the relationship between issuers and proxy advisory firms should operate in a manner similar to the relationships between issuers and sell-side equity research analysts where there is regular dialogue and discussion based on publicly disclosed information while the independence of the equity research analyst is maintained.

CIRI members expressed that errors in factual information are finding their way into PA research reports. While CIRI members appreciate that from time to time they may not agree with the opinions of PA analysts regarding a specific issue or situation they do not believe that an analysis or voting recommendation based on inaccurate facts enhances market integrity or efficiency. CIRI members have come forward with specific examples of such situations and several of these are exhibited in Appendix 2.

CIRI believes market integrity and efficiency would be enhanced if PA Firm reports and voting recommendations were provided to all issuers (not just large capitalization companies or those who subscribe to receive drafts) in advance of the research reports and voting recommendations being issued to their institutional investor clients.

10. During proxy season is it appropriate for a proxy advisory firm to engage with issuers in all circumstances or are there legitimate business and policy reasons why it should not be required to do so? Are there certain special types of situations where it is more important that issuers are able to engage with proxy advisory firms?

CIRI is an organization strongly rooted in the concepts of full and fair disclosure and open communication as a means to help foster efficient capital markets. As such, CIRI believes it is appropriate for a PA Firm to engage with issuers not only with regard to establishing annual governance policies, but to also include them in the research report review process to ensure accuracy.

CIRI further emphasizes that it is most appropriate for PA Firms to engage with issuers whenever the PA Firm is preparing to issue a negative vote recommendation on any proposed proxy motion. It should be required that a PA Firm ensures the facts and analysis relevant to the negative vote recommendation are accurate and there is no misunderstanding of the specific situation.

While PA Firms may need to establish base policies and guidelines for assessing proxy disclosures, it must be recognized that a one-size-fits-all approach detracts from market integrity. Given the nature of the Canadian capital market, it is not unusual for individual issuers to have unique situations and, in these cases to have mechanisms to engage directly with PA Firms to ensure that voting recommendations are based on clear and factually accurate information.

11. If a proxy advisory firm, as a matter of policy, believes that there are certain circumstances where it is not appropriate for it to give issuers an opportunity to review its reports, would it be sufficient to only require in these circumstances that the underlying rationale for such policy be disclosed? Please explain. Or, alternatively should proxy advisory firms be required to provide issuers with an opportunity to review

their reports in all circumstances?

CIRI recommends that in all circumstances draft PA Firm reports be sent to issuers with sufficient time to provide a real and meaningful opportunity for issuers to ensure factual accuracy or engage in a dialogue with advisory firms if contentious issues arise. We understand this practice is being followed by Governance Metrics International when it creates research reports on the risk profile of corporate issuers for its investor community clients and by the Canadian Coalition for Good Governance prior to the issuance of its reports on public companies to its members.

Results from a recent CIRI survey indicate that among the 45% of respondents that always or frequently received a report, one-third of these issuers did not receive a draft report before it was sent to investors and these reports were provided by only one PA firm. Furthermore, in only 40% of cases was the issuer asked to review and/or respond to the PA firm regarding the report.

As we understand the process, PA firms develop their recommendations based on publicly available information and, therefore, we cannot image a situation where it would not be appropriate for an issuer to review a report prior to distribution.

12. Should we prescribe the details of the processes that proxy advisory firms implement to engage with issuers? If so, what do you suggest the requirements should be?

CIRI believes primary consideration be given to a requirement, as indicated in Question 11 above, to provide draft reports to all issuers.

Issuers are only too well aware of the tight time lines associated with the entire proxy voting process (after all, the proxy process is driven by issuers) however, the need to improve market integrity cannot be ignored. CIRI believes that it is important to provide issuers with an appropriate period of time to review a draft report while not significantly impacting the processes of the PA Firms and their contractual obligations to their institutional investor clients. The recent survey of CIRI members indicated that among those issuers asked to review and respond to a draft PA Firm research report 52% were given less than 36 hours to do so. Furthermore 80% of the issuer respondents indicated a 48-hour to 72-hour timeframe is needed to adequately review a PA Firm report and to respond to the PA Firm with identified factual errors or inaccuracies or engage in a dialogue with PA Firms if contentious issues arise.

A vast majority (87.5%) of CIRI survey respondents agreed that it would be appropriate that PA Firms be required to disclose in their final research report to institutional investors any comments that an issuer may choose to provide in response to the PA firm's analysis, factual information used and/or voting recommendations.

Providing investors with such information and potential clarifications would inevitably lead to better vote-related decision-making and thus contribute to improved market efficiency and integrity. CIRI believes this inclusion of issuer-provided comment is especially beneficial to those smaller institutional investors (as pointed out in the Consultation Paper – page 5683) who may not have the necessary internal resources to conduct their own research and may choose to rely more heavily on the research and recommendations of the proxy advisory firms for voting guidance.

Since the institutional investor clients of the PA Firm are also the shareholders of the issuer, it is reasonable to expect that there would be an automatic 'check and balance' to ensure that issuers will only provide thoughtful, accurate and germane statements/comments based on non-confidential publicly disclosed information that would be read by their own institutional shareholders.

Potentially Inappropriate Influence on Corporate Governance Practices

13. To what extent should there be a more fair and transparent dialogue between proxy advisors and market participants on the development of voting policies and guidelines? Is it sufficient for proxy advisors to address governance matters by soliciting comments from their clients?

The trend of PA Firms to set standards and guidelines that define good corporate governance is of concern to CIRI members since PA Firms are seen by many issuers as for-profit companies that, in many cases, have a poor understanding of issuer-specific issues.

The consultation paper states (page 5685): *'Anecdotal evidence suggests that some issuers may feel pressured to accept proxy advisory firms' corporate governance policies, regardless of whether the policies are appropriately taking into account key factors and the particular circumstances of the issuers'*. In a recent survey of CIRI members 100% of respondents indicated that it would be appropriate that PA Firms be required to disclose their methodologies, sources of information used, assumptions and rationale for their vote recommendations.

We believe there is now empirical evidence indicating the influence of PA Firms on corporate governance policies. The Rock Center for Corporate Governance (Working Paper Series No. 119, –*"The Economic Consequences of Proxy Advisory Say-On-Pay Voting Policies"*) states in its summary and concluding remarks:

'We examine the shareholder value implications of proxy advisory firm voting recommendations on say-on-pay. Using a large cross-section of firms, we find that proxy advisory firm recommendations have a substantive impact on say-on-pay voting outcomes. We also find that, anticipating this impact, a significant number of boards of directors change their compensation programs in the time period before the formal shareholder vote in a manner that better aligns compensation programs with the recommendation policies of proxy advisory firms. We interpret this result as evidence that boards of directors change executive compensation plans in order to avoid a negative say-on-pay recommendation by proxy advisory firms and thereby increase the likelihood that the firm will not fail the vote. The stock market reaction to these compensation program changes is statistically negative. Moreover, this effect is unique to the time prior to the initial say-on-pay vote (2011) and a similar stock market reaction is not observed during the 2006 – 2010 time period.'

CIRI suggests that disclosure requirements could be strengthened to require PA Firms to establish and make public a code-of- conduct, which would include at a minimum a requirement to disclose general policies, research methodologies, the effectiveness of their quality assurance controls and the appeal procedures for dissatisfied issuers.

In addition, CIRI proposes that PA Firms be required to establish a mandated appeals process that calls on an independent third party or Ombudsman to adjudicate on behalf of those issuers who have concerns about a research report that cannot be resolved through direct dialogue with the PA Firm.

While not necessarily a recommendation for regulatory action, it also seems appropriate that issuers be provided a real opportunity to provide input into the annual policy reviews conducted by PA Firms (generally following the proxy season and used as a basis for future policy guidelines). Issuers spend considerable time, effort and expertise in developing good corporate governance practices and are more than willing to contribute their resources toward the development of appropriate guidelines.

Proposed regulatory responses and framework(s)

14. Do you think a securities regulatory response is warranted in connection with each of the concerns identified above? Please explain why or why not.

CIRI has proposed a series of potential regulatory responses that it believes are warranted and these are listed at the beginning of this letter under Key Recommendations.

15. Do you agree with the suggested securities regulatory responses to each of the concerns raised? If not, what alternatives would you suggest?

Please see CIRI's answers to the questions above and our Key Recommendations, which outline CIRI's suggested regulatory responses.

16. Do you agree or disagree with the requirements and disclosure framework set out in section 5.2.1 to address the concerns identified? If not, please indicate why. Would you prefer instead one of the other suggested securities regulatory frameworks identified above? If so, please indicate why. Do you agree or disagree with our analysis of these frameworks? Do you have suggestions for an alternative regulatory framework?

As set out in several of the questions above, CIRI largely agrees with the requirements and framework set out in Section 5.2.1.

With regard to conflicts, a PA Firm should be required to have in place policies to deal with employee conflicts, including requiring analysts and reviewers to disclose (i) ownership of shares of an issuer they are reviewing, (ii) any ownership conflicts of the PA Firm itself, and particularly, (iii) conflicts arising from corporate consulting advisory service (to corporate issuers).

While the key conflict of interest from the issuer's perspective would be mitigated by the complete separation of proxy voting services from the corporate consulting services, CIRI is not currently advocating restricting PA Firms from operating in both businesses. Rather, regulators and PA Firms should consider

measures such as enhanced disclosure and strengthened “ethical wall” policies.

Most importantly, CIRI strongly supports and advocates (see Key Recommendations) the requirement outlined under 5.2.1 (2.e), which proposes that issuers be allowed to review and respond to draft reports from PA Firms prior to the issuance of the report to institutional investors. As mentioned earlier, in order to increase transparency CIRI further proposes that issuers be allowed, at their discretion, to provide comments on the report that would be included verbatim in the final report to investors.

17. Are you of the view that we should prescribe requirements in addition to or instead of those identified above for proxy advisory firms?

Investor Disclosure and Diligence- In addition to the potential regulation of PA Firms, and in the interests of capital market integrity, the quality of the overall proxy voting process also depends in part on the diligence of institutional investor firms that subscribe to the PA Firm reports and voting recommendations. While not specifically addressed in the CSA Paper, CIRI suggests that the institutional investor clients of PA Firms should be required to disclose whether or not and to what degree they rely on the recommendations of PA Firms with regard to shareholder voting issues, as they are in the UK under the Stewardship Code of the Financial Reporting Council (FRC), which states:

“Principle 1 of the Code states that institutional investors that make use of proxy voting and other advisory services should disclose how they are used. The FRC encourages those service providers in turn to disclose how they carry out the wishes of their clients by applying the principles of the Code that are relevant to their activities.”

We also believe that institutional investors should be required to adhere (or explain why it is in their best interest not to adhere) to a principle such as the Canadian Coalition for Good Governance Policy entitled “2012 Principles for Governance Monitoring, Voting and Shareholder Engagement”, particularly the section subtitled ‘Principle 2 -Exercising Voting Rights’, which states:

“Institutional investors generally should vote all the shares they own in a company where it is in the best interests of their beneficiaries or clients to do so. Institutional investors should use their best efforts to ensure that their voting decisions are made in light of the particular circumstances of each company and should avoid a ‘check the box’ approach. Accordingly, institutional investors should not automatically support management or directors and should cast their votes only after carefully considering all relevant information.

If an institutional investor uses outside service providers to assist in arriving at its voting decisions, the institutional investor should assess the advice it receives rather than automatically following it.”

In addition, institutional investors should be required to disclose or certify as to the internal controls they use to ensure the integrity and reliability of the services provided to them by a PA Firm.

Automatic Voting - The CSA Paper acknowledges that some institutional investors, generally smaller firms, may not have the time, expertise or staff to devote to reviewing and assessing a broad range of proxy related

material and will therefore be more likely to rely heavily on the research and recommendations of PA Firms. A certain significant percentage of such investors may engage in the practice of “automatic voting”, whereby the decisions of how to vote the institutions’ proxies is left entirely to the PA Firm, based on the voting guidelines established by the PA Firm and agreed to by the institutional investor. Given the problems and issues identified by CIRI members, it is felt that such automatic voting or delegating of voting responsibilities can and does negatively affect market integrity through potential inappropriate voting recommendations based on inaccurate information or analysis by PA Firm analysts.

CIRI, therefore, recommends, at a minimum, that in any case where the PA Firm under an automatic voting mandate from its investor client recommends a negative vote on a proxy issue, the PA Firm must essentially override its automatic voting mandate and seek from the institutional investor a specific and formal agreement to proceed with the negative vote or allow the institutional investor the right to vote or direct the PA Firm to vote as the investor, instructs on that particular matter.

Ombudsman – The role and responsibilities of PA Firms in the United States has recently been under scrutiny by the Securities and Exchange Commission (“SEC”). While broad issues and priorities are still under discussion in advance of the reputed issuance of an interpretive release (potentially providing guidance with regard to proxy advisory firms), the SEC has designated an official, Raymond Be, to receive complaints about PA Firms. CIRI believes this is a worthwhile initiative and encourages Canadian regulators to consider a similar mechanism whereby an independent third party (individual or office) is available to both issuers and PA Firms to hear complaints and possibly pursue dispute resolution.

OBO/NOBO System – CIRI takes the view that improved transparency is beneficial to the integrity of capital markets. However, although it is not mentioned in the Consultation Paper, the OBO/NOBO system, as it stands today, contributes to the opaque nature of the proxy voting system and adds to its complexity. The significant growth in the percentage of shareholders declaring OBO status, as indicated in Section 22.2 of the October 2010 paper, *The Quality of the Shareholder Vote in Canada* by Davies Ward Phillips and Vineberg LLP (the “Davies paper”), is not only expensive for issuers (thus impacting the value of the shareholders’ asset), it is also unique to only two capital markets worldwide - the USA and Canada – and so is anachronistic as capital markets become increasingly globalized. Any reforms or requirements placed upon PA firms must be considered only a partial remedy toward the improvement of the quality of the shareholder vote.

Additional questions for institutional investors (Q.18 – Q.23):

CIRI has no input regarding questions 18 – 22.

23. Do you view the policy development process and resulting proxy voting guidelines of proxy advisory firms as appropriate and reflective of your governance preferences and views? Would input from issuers further benefit or potentially hinder such process?

While this is a question for proxy advisory firms, CIRI believes that it is appropriate that the views and perspectives of issuers, as entities concerned and experienced with establishing and implementing good

governance practices, be sought and considered during the development of PA firm policies. However, CIRI does feel that PA firms need to move away from check-box assessments and “one-size-fits-all” solutions to governance and that preference should be given to procedures that allow each issuer firm to be looked at separately.

A recent article in the August 2012 edition of *CA Magazine*, entitled “Good Governance”, written by Marcel Cote, a founding partner at SECOR Consulting in Montreal, argues that the very foundation of good governance is first established by recognizing the basic principle that corporate directors are responsible for ensuring the company’s interests are aligned with shareholder interests. Cote goes on to outline five rules to complement this basic principle to ensure good governance: (i) a clear vision of the company’s purpose; (ii) a well-defined value-creation strategy; (iii) annual and mid-term performance objectives; (iv) a clear-cut succession plan for senior management; and (v) ambition, well defined. The article can be found in *CA Magazine* or on-line at <http://www.camagazine.com/archives/print-edition/2012/aug/columns/camagazine65888.aspx>.

24. Overall, what has been your experience with proxy advisory firms? Please be as specific as possible.

Those members of CIRI that have responded to this question and others posed in a recent survey indicate that reports from PA Firms contain too many factual errors or inaccuracies and in many cases these are published prior to correction. In the survey only less than 13% of respondents did not find some factual inaccuracy in reports over the past five years.

Far too many issuers never see the PA Reports; fully one-third of issuer respondents either never or seldom receive copies of PA Firm reports. Issuers indicate that draft reports are provided by only one of the two PA firms active in Canada and comments on draft reports were requested in only 40% of the cases where drafts were provided. Clearly there is a lack of engagement.

Additionally, Appendix 2 lists a number of specific examples of situations where issues or conflicts arose between issuers and PA Firms regarding the assessment of issuer proxy materials and the resulting voting recommendations by PA firms.

25. Do you believe that the concerns identified negatively affect voting outcomes at shareholders’ meetings? Please provide specific examples of situations where any of the concerns identified above resulted in what you consider to be an inappropriate vote outcome and describe the nature and extent of the harm caused to market integrity.

It is clear that without the actions and significant expense taken by issuers to correct errors and inaccuracies in the numerous examples included in Appendix 2 there would have been substantially more voting based on inaccurate data and/or analysis at shareholder meetings.

Given the current lack of transparency and engagement by PA firms with issuers, plus the uncertainties resulting from the NOBO/OBO status it is difficult to determine how many negatively affected voting outcomes occur. However, the simple extrapolation of the CIRI survey results and accompanying examples in

Appendix 2 indicates this is a real problem.

26. To what extent do you adopt the corporate governance standards proposed by proxy advisory firms in your choice of corporate governance policies, even if such standards are not appropriate for your organization? Please provide examples of the types of practices that have been changed due to a proxy advisory firm's guidelines and why such changes were not appropriate or did not improve your organization's overall corporate governance.

When this issue was presented in a CIRI survey to members, few responses were garnered, although nearly 8% of respondents did indicate that governance policies were adopted in response to PA Firm policy guidelines. While not extensive, it is clear that the policies of PA Firms do have some influence on processes and decisions at corporate issuers.

In one specific example, the company implemented a restriction on the grant of stock options to directors in response to PA Firm guidelines. The result of changing the compensation plan policy to adhere to the guidelines was that the company had to increase the cash component of its compensation package at a time when this particular issuer had limited cash balances.

Another issuer cited the example that they did a lot of work to ensure that the stock option renewal plan would fit within the guidelines presented by the PA Firm. Given the small size of the issuer, this was a difficult task and required significant effort. One benefit outcome of the overall change was that the issuer engaged in a specific outreach to its major institutional shareholders that was deemed positive.

We would draw your attention to the findings of the Rock Center for Corporate Governance research results referenced in our response to question 13.

27. In those instances where you have identified potential inaccuracies in a proxy advisory firm's recommendation, were these material inaccuracies that would have resulted in a change in the proxy advisory firm's vote recommendation? Please provide specific examples of how this situation resulted in an improper vote outcome (i.e., what was the risk to market integrity).

A number of the examples provided in Appendix 2 show where the PA Firm changed its recommendation when factual inaccuracies were corrected.

In addition, the CIRI survey shows that where the PA Firm sent a draft copy of its report to the issuer prior to distribution to its clients, 28% of the time a correction of factually inaccurate data was made by the PA Firm.

In those circumstances where an issuer received a copy of the PA Firm report (by whatever means) after it had been distributed and the report contained factual errors, 48% of the time a corrected report was issued by the PA Firm.

What is not known, and indeed is problematic, is whether all the PA clients that initially voted based on the initial PA recommendation changed their vote after the revised report was issued. Dialogue and engagement with the issuer prior to the issuance of the initial report would eliminate this problem.

We believe the actions by the PA Firms as outlined above would not have taken place if the errors were not material.

Additional questions for proxy advisory firms (Q.28 – Q.31):

CIRI has no input regarding questions 28 – 31.

Summary

CIRI strongly believes the current situation negatively impacts market integrity, efficiency and the quality of the shareholder vote and that a level of regulation of PA Firms is required.

Specifically CIRI recommends the following:

- a) PA Firms should be required to disclose methodologies, sources of information, assumptions used to prepare their research reports and rationale for their voting recommendations
- b) PA Firms should prominently identify in the research reports and voting recommendations provided to their institutional investor clients any specific potential conflicts of interest with regard to the issuer and analyst/reviewer ownership interests
- c) PA Firms should be required to provide to all issuers draft research reports and voting recommendations for review for factual accuracy allowing 48 to 72 business hours for issuers to respond prior to the report being distributed to the PA Firm's clients.
- d) PA Firms should be required to include in the final report to investors any comments provided by issuers regarding the review process, the research report and the voting recommendations.
- e) PA Firms should establish an appeals process and identify an independent third party or Ombudsman to adjudicate on behalf of those issuers who have concerns about a research report that cannot be resolved through direct dialogue with the PA Firm
- f) Institutional investors who use a PA Firm should comply or explain why they do not comply, with a requirement to disclose how they assess the advice received from the PA Firm and not automatically follow it.

CIRI supports the CSA's initiative to explore the potential regulation of Proxy Advisory Firms as discussed above in our comments and responses to questions posed by the CSA. However, we believe it is imperative to note that the issues raised and the recommendations proposed will not have significant impact for stakeholders until the broader issues regarding the quality of the proxy-voting process itself are addressed. The proxy-voting system as it exists currently in Canada is too complex and has the potential to generate significantly inaccurate voting

results. Addressing the impact of Proxy Advisory Firms may be seen as an improvement in governance but it may all be for naught as long as the accuracy of the vote itself remains suspect.

CIRI would like to thank the CSA for the opportunity to comment on this important topic and would be pleased to answer any questions or enter into dialogue on any of the above.

Yours truly,

A handwritten signature in purple ink, appearing to read 'Tom Enright', with a long horizontal flourish extending to the right.

Tom Enright
President and Chief Executive Officer
Canadian Investor Relations Institute

APPENDIX 1

The Canadian Investor Relations Institute

The Canadian Investor Relations Institute (“CIRI”) is a professional, not-for-profit association of executives responsible for communication between public corporations, investors and the financial community. CIRI contributes to the transparency and integrity of the Canadian capital market by advancing the practice of investor relations, the professional competency of its members and the stature of the profession.

Investor Relations Defined

Investor relations is the strategic management responsibility that integrates the disciplines of finance, communications and marketing to achieve an effective two-way flow of information between a public company and the investment community, in order to enable fair and efficient capital markets.

The practice of investor relations involves identifying as accurately and completely as possible current shareholders as well as potential investors and key stakeholders and providing them with publicly available information that facilitates knowledgeable investment decisions. The foundation of effective investor relations is built on the highest degree of transparency in order to enable reporting issuers to achieve prices in the marketplace that accurately and fully reflect the fundamental value of their securities.

CIRI is led by an elected Board of Directors of senior IR practitioners, supported by a staff of experienced professionals. The senior staff person, the President and CEO, serves as a continuing member of the Board. Committees reporting directly to the Board include, but are not limited to: Nominating; Audit; Membership; Issues; Editorial Board; Resource and Education; Certification.

CIRI chapters are located across Canada in Ontario, Quebec, Alberta and British Columbia. Membership as of August 15, 2012 consisted of 617 professionals serving as corporate investor relations officers in approximately 300 reporting issuer companies, consultants to issuers or service providers to the investor relations profession. Publicly listed issuers represented by CIRI members have a combined market capitalization of just under \$1.4 trillion. CIRI is a founding member of the Global Investor Relations Network (GIRN), which provides an international perspective on the issues and concerns of investors and shareholders in capital markets outside of North America. The President and CEO of CIRI also sits as a member of the Continuous Disclosure Advisory Committee (CDAC) of the Ontario Securities Commission. In addition, several members, including the President and CEO of CIRI, are members of the National Investor Relations Institute (“NIRI”), the corresponding professional organization in the United States.

APPENDIX 2

Examples of Issues between Proxy Advisory Firms and Corporate Issuers

2.1 Small Cap Issuer in the Resource Sector

This year, 2012, this Company, a small cap mining company, had two PA firms publish proxy-voting recommendations to shareholders.

PA Firm A declined to provide a draft or even final copy of their report unless the Company purchased the report, so the issuer was unable to confirm if the material published was accurate.

PA Firm B refused to provide a draft for review, stating the market capitalization was not high enough (draft reports are only available to Composite Index companies). Upon review of the published report, it contained factual inaccuracies including one of the fundamental determinants for them recommending shareholders vote AGAINST a motion. They incorrectly indicated that the Company did not have an independent lead director, while the previous page of the same report stated accurately that the Company did have an independent lead director. After advising them of this error they did correct it and reissued the correction, although with doubtful results as it was long after the initial recommendation.

2.2 Mid Cap Issuer in the Utilities Sector

Both PA firms issued reports in respect of the issuer's proxy circular for the 2012 and 2011 annual general meetings. Neither PA firm provided the opportunity to review the reports in advance of their public release. In both years, the issuer's proxy solicitation agent secured the reports on their behalf; neither PA firm made an effort to contact the issuer directly or to send the issuer their reports.

Both reports identify the lead or primary analyst by name with a telephone and email contact, but no information was provided regarding their professional credentials or background.

With respect to the 2012 proxy circular, the issuer identified two issues with PA Firm As report:

- 1. Factual inaccuracy** – A number of basic facts about the issuer company were incorrect, including the head office address and contact numbers, industry classification, number of employees, and income statement and balance sheet information. In addition, the company description was outdated and did not reflect recent changes within the business. The issuer provided several corrections to the report but only a few of those edits were implemented as the analyst was unable to “override” the balance of the data, which was provided to PA Firm A by a third-party provider (referenced Thomson Reuters and Fact Set).

Impact:

- Inaccurate information provided to investors, which potentially created confusion.
 - Raised questions about depth of research conducted and overall quality of work.
- 2. Voting recommendations made without proper context** – PA Firm A recommended that shareholders withhold their votes on the election of the Chair of the Audit Committee due to his roles on a total of five public company boards (and more than three public company audit committees). Notably, this particular director is retired from full-time employment and therefore has the capacity to focus exclusively on fulfilling the requirements of his directorships. In the days leading up to our AGM, the issuer became aware that one institutional investor who had automatically voted according to PA Firm As recommendation actually did not wish to withhold his vote from the Chair's election. While the issuer was ultimately able to assist the investor in changing his vote, it was only through a series of personal relationships that the matter came to the issuer's attention.

Impact:

- By not engaging in a discussion with the issuer, PA Firm A missed an opportunity to consider, evaluate and provide important context for their voting recommendations.
- In this case, the investor was an OBO. Had it not been for personal relationships it would have been impossible to conduct outreach to the investor and to share context/additional information to aid in making his voting decision.
- The process of assisting the investor to change his vote required significant time and resources from the issuer.
- Raises questions about the wisdom of investors automatically voting according to a proxy advisory firm's recommendation, particularly when advisory firms often have little or no one-on-one engagement with the issuers they are reporting on.

2.3 Mid Cap Issuer in the Industrial Sector

This issuer engaged the consultancy arm of a PA firm for a fee to have their proxy proposals evaluated for compliance with the PA firm's guidelines. However, when the proxy material was distributed, the research arm of the PA firm recommended voting against the issuer's proxy proposal on a compensation matter, citing that the wording of the proposal did not meet certain requirements under a new policy guideline that had been revised earlier in the year (such change was "missed" by the consultancy arm). Clearly the consultancy arm had provided inaccurate and out-of-date advice.

To make matters worse, the issuer was not provided a draft copy of the PA firm research report since the AGM was imminent. Instead, the PA firm suggested the issuer undertake to revise the wording in the proxy (to conform to their revised guidelines), do another full print run of the proxy documentation, conduct a repeat mailing to all shareholders and issue a news release explaining the change, all at the issuer's expense. The issuer instead undertook a significant effort to contact its shareholder base and explain the situation caused by the conflict-of-interest within the PA firm and was able to achieve a positive vote on the proxy proposal.

2.4 Mid Cap Issuer in the Resource Sector

This issuer subscribed to a service whereby draft reports from the PA firm were to be provided to the issuer. In year one of the service, no such report was provided. In year two the report was provided only following probing by the issuer.

2.5 Large Cap Issuer in the Consumer Products Sector

This large cap issuer had to repeatedly ask to obtain a copy of the PA firm research report and then was given no more than 24-48 hours to respond. In fact, there was a range of material factual errors including a purported conflict of interest for a director based on three-year out of date information.

Additional errors have also been experienced with the other PA firm active in Canada and review time has been as short as one day.

2.6 Large Cap Issuer in the Technology Sector

This issuer had requested a draft report from the PA firm but did not get it. The issuer's proxy solicitation agent advised there was a negative vote recommendation regarding the issuer's option pricing policy. Upon further request the PA firm sent the report but to the issuer's CEO rather than the contact specified (corporate secretary). The PA analyst, who made repeated references to his own "extensive experience", disagreed with the specific wording in the issuer's information circular regarding the option pricing plan,

despite the fact the intent of the plan was in line with the PA firm's governance guidelines. Despite substantial discussion and exchange of e-mails, the PA firm declined to change its initial position.

This issuer has also repeatedly experienced other factual errors regarding director attendance at board meetings and the company's compensation plan. PA reports have arrived with only 5-6 hours allowed for review and response. This issuer also notes that the "ombudsman" responsible for dispute resolution was, in fact, the president of the PA firm.

2.7 Large Cap Issuer in the Resource Sector

This issuer was involved in a contentious M&A battle (making a bid for one company while being subject to a hostile bid from another) and the PA firm issued a recommendation on which was the better option based on financial metrics. The reporting analyst at the PA firm was not identified (to determine qualifications) and there was little or no financial analysis provided regarding the transaction or the recommendation. The recommendation appeared to be based primarily on business factors and had nothing to do with governance, the supposed strength of PA firms. There was a total lack of transparency and rationale.

2.8 Mid Cap Issuer in the Resource Sector

This issuer received a completed (not a draft) report that included a recommendation to vote against the chair of the issuer's audit committee and against the engagement of the auditing firm, such recommendations based on an assessment that non-audit fees (fees not payable to the auditor) for the year were too high. The issuer explained to the PA analyst that the fees for the relevant period were higher than usual due to conversion to IFRS and the engagement of an additional independent auditor as well. The PA firm, in this case did revise its report and recommendation.

2.9 Small Cap Issuer in the Resource Sector

In a report issued with regard to a proposed merger transaction, the PA firm recommended voting against the make-up of the proposed Corporate Governance Committee, which was deemed not sufficiently independent by the PA firm. This situation was a specific time-limited situation created solely due to a pending merger and plans. The PA firm did not revise its negative recommendation and the issuer and its agents were forced to pursue an outreach effort to explain the situation to shareholders. The merger transaction was successfully completed despite the negative recommendation of the PA firm.

2.10 Large Cap Issuer in the Industrials Sector

This issuer has found that reports from PA firms have not factually represented the company's compensation programs, particularly with regard to stock options and other share related performance compensation plans. The issuer has found that PA firm analysts tend to recommend negative ratings based on a very strict and inflexible approach to the wording used in proxy disclosure information.

This issuer was also surprised to learn (from a shareholder, not the PA firm) that there were two reports sent to investors from the PA firm, each with different voting recommendations. It turns out that the "base" report recommended "for" votes across the board, but that a second analysis, performed by a separate analysis team within the same PA Firm, provided another set of voting recommendations, including "against" recommendations for the Nominating Committee based on "custom" governance criteria. This process was not explained beforehand and did result in the shareholder admitting

confusion.

2.11 Large Cap Issuer in the Resource Sector

The large cap issuer did not receive a draft report but determined that the report distributed by the PA firm to institutional investors had recommended against a motion that is standard in virtually all forms of proxy; namely the phrase "...to transact such other business as may properly come before the Meeting or any adjournment." The PA firm, when advised of the error, did change the recommendation and issued the correction, prior to the Meeting. However, the issuer believes that the time and effort required to address and rectify such mistakes can be minimized by establishing opportunities for improved engagement between the parties, including the requirement to provide issuers with a draft report.

2.12 Large Cap Issuer in the Energy Sector

The issuer, in advance of the proxy vote regarding the conversion of the company from an income trust to a corporation, engaged the consulting arm of the PA firm to review and comment on certain aspects of the issuer's planned compensation plan subsequent to the conversion to ensure the issuer was on-side with current guidelines for such policies. While appropriate, advice had been provided previously by the PA consulting group, in this case it was unable to provide an accurate assessment back to the issuer. It was not clear whether the PA consulting arm was unsure of how current PA firm guidelines would be applied by the proxy voting staff or whether there was sufficient expertise available regarding this question in the face of such conversions, despite that fact that numerous other issuers were proceeding similarly in Canada at this time.

2.13 Small Cap Issuer in the Energy Sector

This issuer found errors in reports from two PA Firms with regard to a proposed takeover transaction as follows:

(i) The first PA Firm's analysis included the phrase "to the best of our knowledge" while claiming in the report that the details of the third-party fairness opinion were not disclosed by the issuer. The fact of the matter is that the fairness opinion letter in its entirety was fully and publicly disclosed in an appendix in the proxy circular.

(ii) The five-page report of the second PA Firm assessing the merits of the same proposed takeover transaction contained questionable opinions (which will not be discussed here) but, importantly, had the following factual inaccuracies:

(a) In discussing prior legal actions involving the issuer, the PA Firm's report named the wrong party to the action, despite the correct party being identified in a news release at the time and quarterly MD&A's since.

(b) The PA Firm's report said that the bidder in previously unsuccessful takeover proposal was "affiliated" with the bidder in the current transaction. This was wrong.

(c) The PA Firm incorrectly reported that a financing transaction was done while a previous takeover offer was pending, while in fact the financing occurred after that offer was terminated and this was clear in the issuer's public disclosure record.