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June 20, 2013

To:

- British Columbia Securities Commission
- Alberta Securities Commission
- Financial and Consumer Affairs Authority of Saskatchewan
- Manitoba Securities Commission
- Ontario Securities Commission
- Autorité des marchés financiers
- Superintendent of Securities, Prince Edward Island
- Nova Scotia Securities Commission
- New Brunswick Securities Commission
- Securities Commission of Newfoundland and Labrador
- Superintendent of Securities, Yukon Territory
- Superintendent of Securities, Northwest Territories
- Superintendent of Securities, Nunavut

c/o The Secretary  
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- and -

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**RE:  
CANADIAN SECURITIES ADMINISTRATORS REQUEST FOR COMMENTS REGARDING PROPOSED  
NATIONAL INSTRUMENT 62-105 SECURITY HOLDER RIGHTS PLANS DATED MARCH 14, 2013**

**AND**

**AUTORITÉ DES MARCHÉS FINANCIERS CONSULTATION PAPER  
AN ALTERNATIVE APPROACH TO SECURITIES REGULATORS' INTERVENTION IN DEFENSIVE TACTICS  
DATED MARCH 14, 2013**

This letter is submitted by me personally as a Canadian expert in international acquisition strategies and policies, in response to the invitation to comment on the Canadian Securities Administrators' ("CSA") proposed National Instrument 62-105 regarding security holder rights plans (the "CSA Proposal") and the Autorité des marchés financiers ("AMF") consultation paper regarding defensive tactics (the "AMF Proposal").

First, thank you for inviting comment on the CSA Proposal and AMF Proposal. Much has changed since the current policies were established and it is appropriate that they be updated.

As this is an individual's submission, allow me to qualify myself:

- **Industry perspective:** Over 25 years in strategy consulting, beginning with McKinsey & Company and later with SECOR Consulting, Canada's leading strategy boutique, where I was a Managing Partner and Chair of the Board. I now practice as an independent under the firm name Dundee Associates Limited.
- **International M&A research:** Client work and research have been focused on business and public policy issues related to industry restructuring and corporate development. In addition to serving many corporate clients on strategy and M&A issues, I worked in support of the Red Wilson Panel on Canadian Competitiveness in 2008 and have worked on M&A policy issues in several industry sectors. I have published several articles relating to the corporate governance and public policy issues associated with global industry restructuring, including "Losing (Ownership) Control" in the Harvard Business Review. Much of this work is included in the book "The Art of M&A Strategy", by Ken Smith and Alexandra Reed Lajoux, McGraw Hill, New York, 2012.
- **Corporate Governance:** Having retired from full-time consulting and my most recent position as a tenured professor in the College of Management and Economics at the University of Guelph, I am now a corporate director and an advisor to boards. I served previously as the Chair of the Ontario Chapter of the Institute of Corporate Directors. I am a founding partner and a member of the advisory board of the M&A Leadership Council (US) and have led numerous director education sessions on M&A issues.
- **Academic and professional designations:** B.Sc. in Mathematics from York University; M. Sc. and Ph.D. in Mathematics and an MBA from the University of Toronto; accredited director with an ICD.D from the Institute of Corporate Directors; Certified Management Consultant (C.M.C.).

It is from this background as an M&A professional who has made substantial investment in understanding the international policy issues that I offer comment.

## The Relevant Context is Global

The M&A market has become a global market in which Canadian companies have been losing ground under current policies. Note that:

- More than 50% of all transactions globally (by value) are now international<sup>1</sup>; going forward, international deals are expected to dominate the M&A market<sup>2</sup>.
- In the last decade Canada was among the largest net sellers of corporate assets, following only the US and the UK.<sup>3</sup> Relative to the size of our economy, Canada has been the largest net seller of corporate assets in the world.
- The biggest net buyers of Canadian corporate assets have been from Europe and the developing economies, ahead of the US.

Policy has been a contributing factor to Canada's poor performance in the market for corporate control. A combination of securities policies and takeover review policies and practices *relative to other jurisdictions* made Canada the most bidder-friendly jurisdiction of the major economies in the last decade. I emphasize that while the policies may or may not have been rational in a Canadian context, it is the differences in policies that have tilted the playing field in favour of foreign buyers.

As a result, many Canadian companies that might have pursued global growth strategies have been acquired. While a one-time premium was paid to shareholders in each case, these premiums pale in comparison to the value created by global growth.<sup>4</sup>

This distinction between one-time acquisition premiums and long-term value creation brings us to the issues at hand. On the one hand, directors' duties are to the corporation and, as such, directors are responsible to act in the long-term interests of the company and its shareholders. Current policies unduly limit the exercise of independent director judgment in one of the most important decisions in the life of a company – a change of control transaction, whether domestic or foreign.

On the other hand, in the context of a change of control transaction, shareholder interests are more short term. This is principally due to two factors: 1. The possibility of a transaction attracts many new shareholders only interested in the short-term; 2. Even long-standing shareholders are not privy to the long-term potential of the company that may be based on confidential strategic plans.

So, ironically, by providing the shareholders with greater influence relative to directors, the potential long-term shareholder value creation is blunted. This is evidenced by the relative ease with which Canadian companies can be put into play under today's policies, the resulting disadvantaged position of Canadian companies versus foreign competitors, and the ongoing net sell-off of Canadian corporate assets.

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<sup>1</sup> Bloomberg M&A Outlook, available at [www.bloomberg.com](http://www.bloomberg.com)

<sup>2</sup> *ibid*

<sup>3</sup> "Losing (Ownership) Control", Ken Smith, Harvard Business Review, June 2009

<sup>4</sup> "The Art of M&A Strategy", by Ken Smith and Alexandra Reed Lajoux, McGraw Hill, New York, 2012

It is from this context of the global M&A market, Canada's disadvantaged position, and the undermining of the directors' duties to the corporation in change of control transactions that I wish to comment on the proposed policy changes.

### **AMF Proposal**

The AMF Proposal takes a fresh look at defensive tools available to Canadian companies, respecting the duties of directors to the corporation and putting the onus on the courts to rule on the discharge of directors' duties:

- Decisions regarding defensive tactics would reside with directors who are obliged under Canadian corporate law to act in the best interests of the corporation, including long-term shareholder value creation.
- Courts would determine the propriety of defensive tactics as part of their jurisdiction over the discharge of directors' fiduciary duties.
- Securities regulators would intervene only where a board's actions or decisions are clearly abusive of shareholder rights or negatively impact the efficiency of capital markets.

Increasingly, Canadian boards are engaging with shareholders to learn their perspectives and share information. Shareholders have the opportunity to sell their shares, vote for changes on the makeup of the board or to challenge in the courts.

The AMF approach would put decisions regarding change of control transactions with directors who have a legal responsibility to act in the best (long term) interests of the corporation. As a result, a hostile bid, whether domestic or foreign, would no longer automatically put the company in play.

In particular, the AMF Proposal would close some of the gap between Canada's available defensive tactics and those of other relevant jurisdictions. However, it would by no means be protectionist – Canada would remain more open than the US, most of Europe, Japan, Australia and the developing economies.<sup>5</sup>

### **The CSA Proposal**

The CSA proposal is a directional improvement but is limited in scope and potential impact.

By providing a comprehensive regulatory framework for rights plans and more discretion over the use of rights plans as proposed by CSA, there would be less need and less frequent need for regulator intervention. Moreover, the CSA Proposal has the CSA exiting the business of regulating individual shareholder rights plans, which would be a positive development.

However, the CSA proposal is too limited in scope to impact Canada's position:

- Extending rights plans to 90 days leaves companies vulnerable to short-term holders voting for the termination of the plan, pushing the company into auction. This remains contrary to the board's legal fiduciary duty, underscored by the Supreme Court of Canada decision in the BCE case.

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<sup>5</sup> See *The Art of M&A Strategy*, pp 194 to 203 for a summary of international defensive tactics

- Annual shareholder approval of rights plans would define rights plans as short-term measures, contrary to the board's responsibility for the long-term interests of the corporation.
- Other defensive tactics commonly employed in other jurisdictions are not addressed.

### Summary and Conclusion

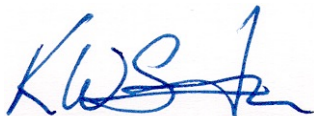
The market for corporate control has become a global market. Canada's regulations and policies regarding takeovers are outdated and not aligned with international policies and practices, and as a result Canadian companies are disadvantaged.

A comprehensive rewrite of policies is, therefore, required to address the new global context for M&A. The AMF proposal considers the duties of directors and seeks to position boards to consider the long-term interests of the corporation and its shareholders in change of control transactions. The CSA proposal is a relatively minor improvement on one defensive tactic, but it would leave Canadian companies subject to auction in the event of any opportunistic bid.

In particular, the AMF proposal would keep Canada an open market for foreign investment while making more normative defensive tactics available. However, the CSA proposal would not materially alter the disadvantaged position of Canadian companies in the global market for corporate control.

Thank you for considering my perspective on these issues. Do not hesitate to contact me if you have any questions regarding my comments or references, or if I can help in any way.

Yours truly,



Ken Smith, Ph.D., MBA, ICD.D

### References:

1. ***Positioning Canadian Firms for the Global Market for Corporate Control***, SECOR Consulting's submission to Canada's Competition Policy Review Panel, February 2008. (SECOR was acquired by KPMG in 2012; the report remains available on line (search by title) or from the author).
2. ***Compete to Win***, Final Report of Canada's Competition Policy Review Panel, June 2008; see especially pp 76-78 titled ***Strengthening the Role of Directors in Mergers and Acquisitions***.
3. ***Losing (Ownership) Control***, Ken Smith, Harvard Business Review, June 2009.
4. ***The Art of M&A Strategy***, Ken Smith & Alexandra Reed Lajoux, McGraw Hill, New York, 2012; See Chapter 9 ***Global Industry Restructuring*** for review of international policies and practices.