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
New Brunswick Securities Commission
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Nunavut

The Secretary
Ontario Securities Commission
20 Queen Street West
19th Floor, Box 55
Toronto, Ontario
M5H 3S8
Fax: 416-593-2318
e-mail: comments@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
Fax : 514-864-6381
e-mail: consultation-en-cours@lautorite.qc.ca

July 8, 2013

Re: Notice and Request for Comment – Proposed National Instrument 62-105 *Security Holder Rights Plans;* Proposed Companion Policy 62-105CP *Security Holder Rights Plans;* and Proposed Consequential Amendments

Dear Sir/Madam,

ISS is a leading provider of corporate governance solutions to the global financial community, including corporate governance analysis and voting recommendations for institutional investors (also referred to as proxy advisory services). More than 1,700 global clients rely on ISS' expertise in providing background research and voting recommendations to help them make more informed voting decisions.

ISS appreciates the opportunity to provide comments on the Proposed NI 62-105 Security Holder Rights Plans, Proposed Companion Policy 62-105CP, and Proposed Consequential Amendments. We hope that you will find our comments and suggestions useful.

Background

At the request of our institutional clients and over the course of several years, ISS has developed proxy voting guidelines for shareholder rights plans in Canada by means of a thorough and inclusive process that took into account the views of institutional investors, legal advisors, corporate issuers, bidders, and regulators. These continuously updated voting policies, subsequently utilized by many institutional investors, drove the evolution of the form of many Canadian rights plans, referred to as "new generation" rights plans by ISS, from the poison pill anti-takeover devices first imported from the U.S. market, to a form of shareholder friendly or benign shareholder "protection" rights plan that may be supported by institutional investors. This form of shareholder protection rights plan is structured to serve two purposes: (i) to provide extra time beyond the statutory 35-day minimum bid period to give the target board sufficient time to find or develop an alternative shareholder value enhancing transaction that would be more favourable to shareholders than the initial bid, and (ii) to ensure that all shareholders are treated fairly in the event of a bid for their shares. This was done by structuring a rights plan to permit only bids that comply with circular disclosure requirements, and providing that more than 50 percent of the shares held by independent shareholders must be tendered in order to "approve" a bid before any shares can be taken up and paid for, and by requiring announcement of the fact that the bid has received majority approval and ensuring that the bid remain open for an additional ten days in order to allow shareholders who have not yet tendered to do so if they determine it to be appropriate at that time. Furthermore, "new generation" plans remove a board's discretion to interpret the terms of the plan and administer it in a manner that may serve to entrench board and management or prevent a takeover bid from going forward to shareholders for consideration.

Not all Canadian companies with shareholder rights plans have adopted "new generation" plans. Reporting issuers that are widely held by institutions have tended to adopt "new generation" plans. However, of the roughly 150 shareholder rights plans a year ISS reviews, more than half are not structured as "new generation" plans. Thus, based solely on those plans reviewed by ISS, there are at least two to three hundred TSX and TSXV reporting issuers who have a form of "poison pill" in place that raises concerns particularly if, under its terms, it would either prevent shareholders from considering a bid or would allow a change of control without shareholder approval.

ISS is aware that some institutional shareholders will not support the adoption of an anti-takeover defense mechanism under any circumstances. Sometimes this view is the result of the perspective of other major global markets with respect to poison pills. We believe this perspective is relevant to this discussion because many of these institutional investors hold shares of Canadian companies. In the U.S., for example, where shareholder approval of pills is not required, aggressive activism has resulted in the termination of pills at most S&P 500 companies. As of May 31, 2013, only 55 S&P 500 companies have a rights plan currently in effect and of those, only 7 have been approved by shareholders. Shareholders in that market have filed numerous shareholder proposals requesting approval or termination of poison pills, and

have targeted directors with "vote no" campaigns at companies where pills have been adopted without shareholder approval or if they contained anti-takeover and entrenchment features such as “dead hand” provisions .

Certain large U.K. institutional investors will not support pills that are structured as anti-takeover devices. The Takeover Code which applies to public companies in the U.K. does not permit the taking of any action by a target board of directors that would preclude shareholders from determining for themselves the acceptability of a bid. The U.K. Code is in fact designed to ensure that shareholders are treated fairly and are not denied an opportunity to decide on the merits of a takeover and that shareholders of the same class are afforded equivalent treatment by an offeror.

It is therefore with great interest that ISS submits the following comments on the two regulatory proposals released on March 14th.

The CSA Proposal – Request for Comments

Is the Proposed Rule preferable to: (i) the status quo; (ii) amending the bid regime to mandate “permitted bid” conditions and disallow Rights Plans; or (iii) amending NP 62-202 to provide specific guidance on when securities regulatory authorities would intervene on public interest grounds to cease trade a Rights Plan?

The Status Quo – The CSA state that the current regime under NP 62-20, has resulted in a market that is too bidder friendly.

However, investors have indicated, by tendering their shares to bids with an acceptable premium in the absence of a competing bid or absent the likelihood of a higher competing offer, that in most instances they wish to benefit from the offer on the table rather than take the chance that the target board and management can offer a better return within a reasonable period of time. The unrestricted ability of shareholders to accept the bid premium if it meets their return criteria is understood under current regulation and may not be impeded by a shareholder rights plan or other anti-takeover measure orchestrated by a target board. The unfettered ability of institutional shareholders to tender to such a bid and reinvest the proceeds is integral to the achievement of a competitive return on investment for plan beneficiaries and other beneficial owners for whom the investment is managed. In fact, as the CSA have pointed out, NP 62-202 was originally crafted after thorough and extensive due consideration and market outreach, to ensure that shareholders could make the final determination of whether to accept a takeover bid.

Furthermore, under current takeover bid regulation and oversight, boards have a fiduciary duty to make a recommendation to shareholders with respect to whether shareholders should accept a take-over bid and will avail themselves of expert financial and legal advice in doing so. Therefore, reporting issuers are not prevented from communicating to shareholders their reasons why a takeover bid should not be accepted, or from making a compelling argument for management’s strategy and plan for creating superior shareholder value as the preferred alternative to a hostile bid. In addition, shareholders increasingly have access to more current

and reasonably accurate market information with which to inform their investing decisions, including the attractiveness of a bid for their shares.

Perhaps the most compelling concern expressed with respect to the current regulatory practice of generally cease trading a shareholder rights plan upon request by an offeror, is that the shareholder protections offered by a "new generation" rights plan are then lost as soon as the rights plan is effectively terminated by the regulators. A bidder at that point may, for example, waive the majority approval condition which would then permit any shares tendered under the bid to be taken up. The bid may be repeatedly extended with the end result being the acquisition of effective control without majority shareholder approval. This concern could be dealt with without changing or interfering with the fundamental tenets of NP 62-202 that:

- Take-over bids play an important role in the economy by acting as a discipline on management and in reallocating economic resources to their best use;
- In considering a bid, the interests of target management may differ from those of target shareholders;
- The primary objective of bid legislation is to protect the *bona fide* interests of target shareholders and a secondary objective is to provide an open and even-handed environment for take-over bids;
- A specific set of rules for board conduct would not be appropriate but regulators will intervene in specific cases that may be abusive of shareholder rights;
- Unrestricted auctions produce the most desirable results in take-over bids and regulators will intervene if defensive tactics are adopted that will likely deprive shareholders of their ability to tender to a bid or a competing bid; and
- Prior shareholder approval will generally allay concerns with respect to a defensive tactic.

The Proposed CSA Amendments

We understand that under the CSA proposal, the Regulators will no longer cease trade an active shareholder rights plan except in extremely unusual circumstances which would be limited to cases where the board and management of a target company have not appropriately managed conflicts of interest or the integrity of the capital markets is at risk. As indicated in the CSA request for comments, at the time NP 62-202 was adopted, the Policy was structured to address the *"over-arching concern that, in the context of a hostile take-over bid, the interests of management of the target company may not coincide with those of shareholders and that management may implement defensive measures that deny shareholders the ability to respond to a bid*". In our experience in reviewing and making voting recommendations on many highly contentious take-over bids and other contentious shareholder meetings over the past 25 years, this concern is still as relevant today as it was in 1986. In fact, one might argue that this concern is further complicated by the control that insiders have over reserves of treasury shares earmarked for equity compensation, that would be exempt under current take-over bid rules.

Additional power in the form of a poison pill (that is, a rights plan that is not a "new generation" rights plan and thus may be used for anti-takeover purposes) in the hands of management absent the certainty that securities regulators, in determining whether to cease trade a pill, will

review management's actions and present their findings to the market in a regulatory decision, may be of great concern to shareholders. The loss of detail that is provided in these regulatory decisions, related to management actions in extremely contentious situations, that gives shareholders valuable information and insight into the quality of board and management and that provides regulatory and legal context for some unusual circumstances, may be viewed as unacceptable.

Principle concerns with the current approach referred to in the Request for Comment include that certain market participants, who are unhappy with the typical period of time in which a pill is generally cease traded, on the grounds that the timeframe is too short for a target board to negotiate with a hostile bidder, have suggested that regulators stop regulating take-over bid defensive tactics in any respect. They suggest that the courts should be the arbiters of pills as a matter of fiduciary duty law or pursuant to the "oppression" remedy under corporate legislation. Shareholders may view these alternative remedies as unacceptable, however, as this may significantly increase the cost of a take-over bid potentially discouraging some bids and deviating monies that might otherwise be received by shareholders as premium. As well, the result may be a cost to shareholders in cases where target company management have prevented them from accepting a take-over bid, if shareholders are forced to bring an oppression remedy case to the courts.

The CSA proposal also contains a requirement for shareholders to approve the adoption of any shareholder rights plan within 90 days of adoption, along with a further annual shareholder approval requirement for a rights plan to remain in effect. ISS, supported by institutional client feedback, views a frequent shareholder reconfirmation requirement to be essential to any acceptable shareholder rights plan adoption. Under the current regulatory approach whereby shareholders may not be denied the opportunity to consider a bid for their shares, "new generation" rights plans have been structured to require a three-year sunset or shareholder reconfirmation clause. However, in the absence of future regulatory intervention under the proposed amendments, a one year shareholder reconfirmation is considered to be too long a period during which a board of directors has complete authority to use a rights plan within the context of a take-over bid in any manner they deem appropriate potentially preventing one or more takeover bids from shareholder consideration. It must also be noted that of the roughly 150 rights plans reviewed by ISS each year, more than half are not structured as "new generation" shareholder friendly plans that serve to provide a longer minimum bid period and to enforce Permitted Bid and other provisions that ensure fair and equal treatment of all shareholders. Because the vast majority of rights plan adoptions in recent years are at mid to small-cap or venture issuers that are not widely institutionally held, these plans are generally approved by a large retail investor base that may not be well versed in these extremely technical legal documents. The potential for many of these plans to be used as anti-takeover defense mechanisms is therefore great. For this reason, we believe that there is an ongoing need for the regulators to protect the public interest more often than in the limited cases suggested under the CSA proposal.

A further concern for shareholders may be the ability of a board to adopt a second tactical rights plan before the 90-day approval period for the first rights plan is set to expire, which it appears would be allowed under the CSA proposal with the only condition being shareholder approval of the second tactical pill within 90 days from its adoption. This staggered pill adoption ability may

result in a protracted defense by the target company of closer to 180 days because there would be no certainty of regulatory intervention at all, and likely not within the 45-55 day period that has typically been the case under current regulatory practice. The extra time required for a shareholder vote to remove the second tactical pill would still allow it to remain in effect for too long a period. This may be of particular concern in cases where shareholders expecting to be able to remove the first pill within the first 90-day period have been denied the opportunity to do so in a timely manner.

The AMF Proposal

The AMF proposal goes beyond application to shareholder rights plans only and would apply to all takeover bids and defensive tactics. The AMF proposal presents an alternative to NP 62-202 which would update the policy framework for take-over bids by introducing two significant changes to the current take-over bid regime.

Given the limitations of shareholder rights plans to provide shareholder protections in a take-over bid scenario, particularly if they are not structured as "new generation" plans and in the event that they are cease traded, there may be merit in an approach that would regulate all take-over bids to provide those same protections.

However, the stated primary objective of the AMF proposal -- "*to restore the regulatory balance between bidders and target boards*" by updating the policy framework for take-over bids to reflect the current legal , economic and market practices related to hostile bids -- does not protect the interests of shareholders.

The AMF proposal as drafted completely reverses the single most important objective of NP 62-202, in our view, which is to protect the interests of shareholders and ensure regulatory intervention if defensive tactics are adopted that would deprive shareholders of their ability to tender to a take-over bid.

The AMF proposal to give deference to directors of target corporations in the exercise of their fiduciary duty, it is stated, is based on the premise that possible conflicts of interest and entrenchment issues facing target boards are appropriately identified and managed. While this may be true of many companies and especially those that are widely institutionally held, based on the corporate governance practices of roughly 2,800 Canadian public companies reviewed each year by ISS, there are many companies for which concerns are regularly raised regarding management conflicts of interest related to, for example, compensation arrangements, related party transactions, and response to a hostile bid. As well, until recent stock exchange rule changes forced the elimination of slate ballots and staggered director elections, these entrenchment practices were still supported and implemented by boards of directors. Dual class share structures with unequal voting rights that disenfranchise one class of shareholder are still prevalent in Canada, as are boards upon which not all directors are elected by all shareholders, perpetuating the longevity of certain directors whether or not they fairly and effectively represent all shareholders as is their duty. We therefore disagree with the statement that corporate governance standards have substantially improved so that the risk of board and management conflicts of interest has been reduced to the extent that regulatory oversight and intervention is no longer necessary, or that would justify depriving shareholders of the ability to

consider the merits of a take-over bid and make the final decision for themselves as to whether they should accept the bid. Absent a change to corporate law to require binding majority voting for director elections, shareholders have little recourse to change unresponsive or entrenched boards outside of the courts or collective activism, both of which may be considerable prohibitive barriers to action.

In fact, we would go further and state that the decision by the Supreme Court of Canada in BCE Inc. *v.* 1976 Debentureholders[1] that has been seen to clarify directors' fiduciary duties by defining fiduciary duty as "*a broad contextual concept*"…."*not confined to short-term profit or share value*"….but that "*looks to the long term interest of the corporation*"…and may vary with the situation at hand, was given specifically within the context of a Plan of Arrangement which is fully within the purview of board direction and not a Take-over Bid which is instead made directly to shareholders for their shares. . The BCE Decision clarified that in determining what is in the best interests of the Corporation, directors may look to the interests of shareholders, employees, creditors, consumers, governments and the environment to inform their decisions. The Court further clarified that in making their decisions, there is no principle that one set of interests – for example the interests of shareholders -- should prevail over another set of interests. Insofar as the board of directors must meet their fiduciary obligation to make a recommendation to shareholders as to whether shareholders should accept a take-over bid, the board's decision may be informed by the broader contextual concept of fiduciary duty. In the event that a bidder wishes to have a favourable recommendation from the target board, the bidder may negotiate the terms of a bid with the board. However, as stated, a take-over bid by its very nature is made directly to shareholders for their shares and therefore shareholders must be entitled to make the final determination as to whether to tender their shares under the terms of the bid. For this reason, ISS' voting guidelines do not support the ability of a board to adopt any anti-takeover defense measure that would remove shareholders' ability to do so.

The AMF proposal suggests changing takeover bid regulation to incorporate two elements of a Permitted Bid clause found in "new generation" rights plans:

(i) a minimum share deposit approval requirement of more than 50% of the outstanding shares held by shareholders other than an Offeror;

(ii) in the event that the minimum deposit requirement is met, an announcement of that fact by the Offeror and a requirement that the bid remain open for an additional 10 days to permit other shareholders who have not yet tendered, to do so if they deem it appropriate.

While these changes would improve the fairness of the takeover bid process, ensure majority shareholder approval, and eliminate some of the coercive pressure to tender, they are not sufficient by themselves as they do not establish a reasonable minimum bid period. Nor do they prevent a "creeping acquisition" of control without payment of a premium or shareholder approval. Given that the stated reason for the adoption of all shareholder rights plans reviewed by ISS over many years is to provide extra time beyond the current statutory minimum bid period of 35 days, and to ensure the equal treatment of shareholders in the event of a bid, establishing a longer minimum bid period of 60 days seems necessary to any regulatory

[1] [2008] 3 S.C.R. 560

67 Yonge Street, Toronto, Ontario Canada M5E 1J8, T: +1 416 364.9000, F: +1 416 364.6710

amendments for take-over bids. Also, the concern related to creeping acquisitions of control may only be dealt with by implementation of a share acquisition threshold at which the acquiring person must make a takeover bid to all shareholders.

Conclusion

ISS has raised a number of concerns with respect to both proposals as drafted. We therefore view neither as sufficient improvement on the status quo and in fact believe both would be detrimental to the rights of shareholders, as both may potentially prevent a take-over bid from going forward to shareholders for consideration. We would encourage the CSA to revise their approach to cease trading pills to deal with the concern that, once a pill is terminated, a bidder can waive its requirements and/or extend the bid as needed until a significant amount of outstanding shares are tendered, thus potentially permitting the acquisition of effective control without majority shareholder approval. One approach might be to allow "new generation" rights plans to remain in effect, as they would not prevent a "permitted bid" and would serve only the two legitimate purposes of (1) providing extra time – 60 days rather than 35 days under current legislation – for the board to consider a bid or develop an alternative transaction that would be supported by shareholders, and (2) ensuring that all shareholders are treated fairly in the event of a bid for their shares. Developing policy in this direction would encourage companies to structure their rights plans as "new generation" plans in order to be viewed favourably by regulators as well as by shareholders. This would however, only deal with takeover bids that are subject to a shareholder rights plan.

We would encourage the CSA and AMF to rethink potential amendments to take-over bid legislation that would incorporate substantial shareholder protections into legislation that would be applicable to all bids. It may be suggested that The Takeover Code governing take-over bids in the U.K. presents an excellent example of a governing code that sets out a process and shareholder protections that would apply to all take-over bids. If this approach is taken, shareholder rights plans may become a thing of the past.

Under any regulatory proposal being contemplated in Canada, shareholders should not be prevented from considering the merits of a take-over bid for their shares and tendering if deemed appropriate. The final decision as to the acceptability of any take-over bid should be in the hands of shareholders.

Respectfully,

Debra L. Sisti,
Vice President,
Canadian Research,
ISS | An MSCI Brand,

67 Yonge Street, Suite 1400,
Toronto ON M5E 1J8
T: +1 416 687 6265
debra.sisti@issgovernance.com