Canadian Coalition for
GOOD GOVERNANCE

THE VOICE OF THE SHAREHOLDER

July 12, 2013

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

C/O: Anne-Marie Beaudoin, Corporate Secretary
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The Secretary
Ontario Securities Commission
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Dear Sir/Madame:

Re: Proposed Amendments to Multilateral Instrument 62-104 *Takeover Bids and Issuer Bids*; National Policy 62-203 *Take-over Bids and Issuer Bids; and National instrument 62-103 Early Warning System and Related Take-over Bids and Insider Reporting Issues* (the "Proposal")

We have reviewed the Canadian Securities Administrators ("CSA") Notice and Request for Comment on the Proposal released on March 13, 2013 and we thank you for the opportunity to provide our comments, which are set out below.

CCGG's members are Canadian institutional investors that together manage approximately $2 trillion in assets on behalf of pension fund contributors, mutual fund unit holders and other institutional and individual investors. Representing the interests of shareholders, CCGG promotes good governance practices in Canadian public companies and the improvement of the regulatory environment to best align the interests of boards and management with those of their shareholders and to promote the efficiency and effectiveness of the Canadian capital markets. A list of our members is attached to this submission.

Overview

In our letter to the CSA of May 28, 2010, a copy of which is attached, we encouraged the CSA to look closely at the issues raised by a proposal being made at that time by a Canadian law firm to bring Canada's early warning system threshold down from 10% to 5% in line with the requirements of other significant capital market jurisdictions. In that letter, however, we stated that "we urge the CSA to closely examine [the proposal's] potential ramifications in light of the unique features of the Canadian marketplace". We also requested that if the CSA proposed to lower the threshold, "it should also consider whether eligible institutional investors who qualify for the alternative monthly reporting system should continue to report at the current 10% threshold".

Having examined the Proposal closely, our members are concerned that the CSA did not fully consider the unique features of the Canadian market and whether, in light of those features, the 10% threshold for passive[1] investors should be maintained. While CCGG agrees with some of the principles behind the Proposal, we are concerned that it ultimately would be detrimental to the clients/beneficiaries of passive institutional investors. As a result, we do not support the reduction of the Early Warning System threshold from 10% to 5% for passive institutional investors. We are not commenting on the application of the Proposal to non-passive investors.

The Proposal is also very complex, covering a wide array of matters. This complexity, combined with insufficient clarity and detail around methodology and application, make it impossible to comment definitively on its intended and unintended consequences. However, the issues that are of immediate concern to our members are set out below.

The Proposal fails to take into account the unique features of the Canadian market

It is inappropriate to reduce the threshold solely to make Canadian rules in this area consistent with global standards, in particular those of the U.S. Fundamental differences in market characteristics such as capitalization, liquidity, depth and institutional investor concentration can make a particular policy appropriate for one jurisdiction but inappropriate for another. While we appreciate the CSA's attempts to promote regulatory consistency across countries, we think that the CSA's mandate with respect to the efficiency and effectiveness of the Canadian capital markets should prevail. The features of the Canadian market that we believe make the Proposal inappropriate for passive investors are discussed below.

[1] In this response by 'passive investor' we mean investors who are not seeking to influence or acquire control, including (i) "Eligible Institutional Investors" (as that term is defined in NI 62-103) which are entitled to use the Alternative Monthly Reporting system and (ii) mutual funds which are subject to the control restriction in NI 81-102 section 2.2 (1) (b).

Market Size/Liquidity

Relative to the U.S. and many other markets, the Canadian market is much smaller and has a larger number of small companies. As a result, Canadian equities are generally less liquid than those in many other markets, particularly those in the U.S. For example, the Canadian public market consists of 3,495 public companies[2] with a total market capitalization of $2.1 trillion and an average market capitalization of $598 million. The 237 companies in the S&P/TSX Composite Index account for $1.75 trillion or approximately 84% of the total market capitalization in Canada. If one excludes companies that are cross listed in the U.S., the remaining 3,269 companies have a combined market capitalization of $790 million and an average market capitalization of $241 million. In the U.S., companies of that size would be considered micro cap[3].

Institutional Investor Concentration

Relative to the U.S., the Canadian market has a higher concentration of ownership by institutional investors rather than individual investors[4]. Although precise data measuring the aggregate equity holdings of institutional investors in Canada is not available, and comparing the concentration of this class of investors with those in the U.S. is difficult, available data indicates that the Canadian equity market, with large pension and mutual fund managers and a relatively small number of issuers with much smaller capitalizations, is significantly more concentrated than that of the U.S. This additional concentration results in a further reduction of liquidity for Canadian institutions, especially with respect to the ability to carry out large trades (see discussion below). It also increases the threat of predatory behaviour by high frequency traders and hedge funds since trading strategies are more easily discerned in a concentrated market (see discussion below).

Trading by Passive Institutional Investors

When required to disclose their holdings under the current rules, passive institutional investors in Canada are vulnerable to 'positioning ahead' (or 'front-running') by high frequency traders and hedge funds, which limits their ability to trade in the best interests of their clients/beneficiaries. By disclosing their holdings, large institutional investors may be forced to signal their trading strategies to the market, particularly when (as is often the case) it takes several days to complete a trade[5]. Other market participants, including those that apply predatory tactics, can use the disclosure information as a signal to take positions in the security in anticipation of the price movement common to the purchase or sale of large blocks of stocks in Canada. Liquidity available to the passive investor is therefore reduced, increasing the trading costs and negatively impacting the returns for their clients/beneficiaries.

For example, if one assumes that a month has 22 trading days, and that it takes, on average, seven days to complete a trade, at least one third of the time trades would occur in days surrounding month end disclosure events exposing them to predatory tactics and/or increased trading costs. Traders do have

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[2] http://www.tmx.com/en/mig/index.html. Excludes TSX listings that are exchange traded products.

[3] Common definitions used to classify market capitalizations for U.S. companies are: large cap (>$8 billion market cap), mid cap (between $1 and $8 billion market cap), small cap (<$1 billion in market cap) and micro cap (<$250 million market cap).

[4] *Who Controls Financial Markets in Canada? Individual vs. Institutional Investors*, Canadian Financial DYI website

[5] Depending on the market float of a holding, it is not unusual for a large institutional investor to take an average of between five and ten business days to complete a trade in a small-cap or mid-cap stock. The rule of thumb used by most traders is to trade less than 20% of an average daily trading volume of a security in order to avoid significant market impact. This is why trading in stocks with smaller market capitalization typically occurs over multiple days. If the trading occurs close to the month-end, the disclosure of holdings may have to be made before the trading in a particular issuer has been completed.

alternatives to avoid stretching executions over several days. They can accelerate the pace of the order execution, thus demanding a greater share of available liquidity, or they can arrange a block trade, both of which typically result in negative pricing consequences for the trader and reduced total return potential for their clients/beneficiaries.

Regardless of which approach a trader takes, once the reporting threshold is crossed and positions are disclosed the liquidity of a stock may be adversely affected, limiting further transactions and restricting the ability of institutional investors to act in the best interests of their clients/beneficiaries. Reducing the reporting threshold to 5% will magnify the impact of these liquidity issues and make it more difficult for institutional investors to act in the best interests of their clients/beneficiaries. When the unique market size, liquidity and institutional investor concentration of the Canadian market noted above are added to the mix, these problems are further exacerbated. Accordingly, we believe that passive investors, including Eligible Institutional Investors who qualify for the Alternative Monthly Reporting system, should continue to report at the current 10% threshold.

Even if the CSA decide to adopt a 5% threshold, we believe that the requirement to disclose a 2% decrease should not apply to passive investors on the same basis that it will be detrimental to their ability to act in the best interests of their clients/beneficiaries and such detriment trumps any arguments for greater transparency with respect to ownership decreases.

Negative Impact on Access to Capital

In order to avoid these trading impacts, some passive institutional investors may decide not to invest to a level that would trigger disclosure obligations, which could limit access to capital for the large number of mid to small cap[6] Canadian companies and create significant problems for the Canadian market as a whole. Many large institutional investors have minimum investment guidelines that would likely exceed the proposed 5% threshold, particularly since the reporting threshold for a Canadian company with an average market capitalization[7] would be triggered at an investment of $15.2 million or more. To avoid crossing the threshold, institutional investors may choose to deploy their capital in other markets where a similar (or larger) dollar size of investment would not trigger a reporting requirement. As a result, an unintended consequence of the Proposal may be to limit investment in mid and small cap Canadian companies, which arguably have the greatest need for capital from Canadian institutional investors. Accordingly, if the CSA proceed with the lower 5% threshold for passive investors notwithstanding our views to the contrary, then we believe the Proposal should exclude investments by passive investors in mid and small cap Canadian companies.

The Proposal may impose a significant compliance burden on passive institutional investors

For many of our larger institutional investor members, it is not uncommon to acquire 5% of the outstanding shares of a public company. In addition to the significant trading and access to capital effects detailed above, the adoption of a 5% threshold will greatly increase the magnitude of their reporting obligations. A review by one of our larger Members showed that the proposed reduction in the reporting threshold would result in its reporting obligations increasing from a handful of issuers with the 10% threshold to several hundred with a 5% threshold, which would comprise a significant compliance burden. For passive institutional investors that either have no intention of acquiring control or are legally restricted from taking control positions, we do not believe that the Proposal offers benefits that outweigh the potential harm.

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[6] See footnote 3 for a classification of market capitalizations.
[7] Assuming it is not cross listed in the U.S.

We note that decreasing the reporting threshold to 5% will provide increased transparency only with respect to small and mid-size issuers. The majority of Canadian issuers by market capitalization are already subject to the SEC's 5% reporting threshold due to the fact that they are cross listed on a U.S. exchange. Of the TSX/S&P 60, 73% of companies (44 out of 60), representing 86% of the market capitalization of the index, are cross listed on a U.S. exchange. For the broader S&P/TSX index, 38% (89 out of 237) of index issuers or 67% of the index by market capitalization are cross listed. CCGG does not believe that the additional transparency with respect to small and mid-size issuers justifies the potential harm to the Canadian market resulting from the Proposal.

Again, if the CSA nonetheless decide to reduce the reporting threshold from 10% to 5%, we believe that the threshold should not be lowered for passive investors. Passive investors, including Eligible Institutional Investors who qualify for the Alternative Monthly Reporting system, should continue to report at the current 10% threshold.

Application to Mutual Funds

A majority of CCGG's members believe that if a 5% threshold is ultimately adopted and passive investors are not excluded, it should apply to all passive investors consistently, including public mutual funds. An argument can be made that as passive investors by virtue of National Instrument 81-102 section 2.2(1) (b), the lower 5% threshold should not apply to mutual funds. However, pension funds and most other institutional investors typically invest passively as well and should be subject to the same reporting threshold as mutual funds.

Equity Derivatives and Securities under Lending Arrangements

We welcome the CSA's attempt to update the early warning system to address empty voting and hidden ownership. As the Proposal points out, lack of transparency regarding the use of derivatives and securities lending arrangements is an important issue that should be addressed. In principle, CCGG agrees that it is appropriate to include derivatives and securities lending arrangements when calculating whether the threshold has been reached, in order to avoid underreporting of true ownership levels (i.e. hidden ownership) and empty voting. We point out that the problems of empty voting and hidden ownership exist regardless of whether the reporting threshold is 5% or 10% and thus should be addressed whether or not the threshold is reduced. We wonder whether amendments to the early warning system are the appropriate forum in which to address this broader issue.

In this area the Proposal is ambiguous and lacks detail crucial to assessing its merit. Many implementation issues are not addressed by the Proposal in its current form. For example, would investors holding index futures be required to include those holdings? It is arguable that to do so would lead to over-reporting. Will there be a de minimis exemption such as is found in the U.K. (which we would encourage the CSA to adopt) where holdings in a company that comprise less than a certain percentile of the index will not be included? Will institutions be expected to net out their positions when derivatives are involved?

Further, securities lending is an integral and common place activity that occurs on a large scale for many institutional investors in Canada. It generates significant revenue for clients/beneficiaries and provides liquidity for the market. The proposed requirement to disclose the general nature and all material terms for all securities lending transactions whenever a transaction results in going above or falling below the proposed threshold of 5%, or a proposed increase or decrease of 2%, may impose a significant administrative burden. Once again, we question whether the magnitude and complexity of the Proposal's reporting obligations for equity equivalent derivatives and securities lending arrangements have the potential to overwhelm the advantages to be gained from increased disclosure by passive institutional investors.

Moratorium on Further Acquisitions

The purpose of a moratorium following the acquisition of a specified percentage of shares (in the case of the Proposal, one business day following required disclosure) is to give the market time to absorb news of a takeover bid before the acquirer is permitted to make additional purchases. While this makes sense in the context of a bid for control, the logic of its application to those broader circumstances that reducing the threshold to 5% is intended to capture, such as the ability to call a shareholders meeting or providing issuers with greater visibility into their shareholder base, is not clear. In CCGG's view, while it may be understandable to apply a moratorium to active investors, it is not supportable in the case of passive investors.

We also question whether a one-day moratorium on further acquisitions makes sense at all even in cases of attempts to acquire control in an age where the dissemination and absorption of information is almost instantaneous. Accordingly, in response to the specific Proposal question, CCGG would not be in favour of reducing the moratorium trigger threshold to 5% from the current 10%.

Loss of Alternative Monthly Reporting Status for Proxy Solicitation

CCGG agrees with the proposed change that would result in investors that actively solicit or intend to solicit proxies on matters relating to the election of directors or mergers and similar transactions being unable to use the Alternative Monthly Reporting regime. In its current form, however, the Proposal is ambiguous given how broadly 'solicit' can be interpreted. We suggest that the Proposal use the definition of 'solicit' found in section 147 of the Canada Business Corporations Act so that it is clear, for example, that if an investor is being solicited for its proxy, then that investor will not lose its status as a passive investor entitled to use the Alternative Monthly Reporting regime.

We thank you again for the opportunity to provide you with our comments. If you have any questions regarding the above, please feel free to contact me at 416.847.0524 or serlichman@ccgg.ca or our Director of Policy Development, Catherine McCall at 416.868.3582 or cmccall@ccgg.ca.

Yours very truly,

S Erlichman

Stephen Erlichman
Executive Director
Canadian Coalition for Good Governance

CCGG MEMBERS

Alberta Investment Management Corporation (AIMCo)
Alberta Teachers' Retirement Fund Board
Aurion Capital Management Inc.
BlackRock Asset Management Canada Limited
BMO Harris Investment Management Inc.
BNY Mellon Asset Management Canada Ltd.
British Columbia Investment Management Corporation (bcIMC)
Burgundy Asset Management Ltd.
Canada Post Corporation Registered Pension Plan
CIBC Global Asset Management
Colleges of Applied Arts and Technology Pension Plan (CAAT)
Connor, Clark & Lunn Investment Management
CPP Investment Board
Franklin Templeton Investments Corp.
GCIC Ltd.
Greystone Managed Investments Inc.
Healthcare of Ontario Pension Plan (HOOPP)
Jarislowsky Fraser Limited
Leith Wheeler Investment Counsel Ltd.
Lincluden Investment Management
Mackenzie Financial Corporation
Manulife Asset Management
NAV Canada (Pension Plan)
New Brunswick Investment Management Corporation (NBIMC)
NEI Investments
Nova Scotia Pension Services Corporation
Ontario Municipal Employees Retirement Board (OMERS)
Ontario Pension Board
Ontario Teachers' Pension Plan (Teachers')
OPSEU Pension Trust
Public Sector Pension Investment Board (PSP Investments)
RBC Global Asset Management Inc.
Régimes de retraite de la Société de transport de Montréal
Russell Investments Canada Limited
Sionna Investment Managers Inc.
Standard Life Investments Inc.
State Street Global Advisors, Ltd.
TD Asset Management Inc.
Teachers' Retirement Allowance Fund
UBS Global Asset Management (Canada) Co.
United Church Pension Plan (Pension Board)
University of Toronto Asset Management Corporation
Workers' Compensation Board - Alberta
York University

Canadian Coalition for
GOOD GOVERNANCE

May 28, 2010
Mr. Jean St-Gelais
Chair
Canadian Securities Administrators
Tour de la Bourse
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Montreal, QC
H4Z 1J2

Dear Mr. St-Gelais:

Re: Proposal to Reduce Early Warning Threshold

We have received a copy of the letter that Ogilvy Renault sent to Mr. Louis Morisset of the AMF requesting a reduction of the early warning disclosure threshold set out in sub-sections 5.2(1) of Regulation 62-104 respecting Take-over Bids and Issuer Bids (Quebec) and in Ontario, sub-section 102.1(1) of the Securities Act (Ontario) (the "Early Warning Threshold").

We encourage the CSA to look closely at the issues raised by Ogilvy Renault and their proposal to bring Canada's Early Warning Threshold down from 10% to 5%, in line with the requirements of other significant capital market jurisdictions. Prior to making such a change, however, we urge the CSA to closely examine its potential ramifications in light of the unique features of the Canadian marketplace and to request input from the public in your usual manner.

If the CSA proposes to lower the threshold, it should also consider whether eligible institutional investors who qualify for the alternative monthly reporting system should continue to report at the current 10% threshold. In addition, we encourage the CSA to consider how the requirement to report subsequent purchases of 2% would be affected by any change to the Early Warning Threshold.

We look forward to considering the CSA's analysis of these issues when any proposal is released for public comment.

Yours very truly,

David Denison
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