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July 12, 2013

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial Services Commission – Securities Division
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
New Brunswick Securities Commission
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Government of Yukon
Registrar of Securities, Department of Justice, Government of the Northwest Territories
Registrar of Securities, Legal Registries Division, Department of Justice, Government of Nunavut

c/o Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
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C.P. 246, 22e étage
Montréal, Quebec H4Z 1G3
E-mail: consultation-en-cours@lautorite.qc.ca

c/o The Secretary
Ontario Securities Commission
20 Queen Street West
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Toronto, Ontario M5H 3S8
E-mail: comments@osc.gov.on.ca

SENT VIA E-MAIL

Dear Sirs and Mesdames:

RE: CSA Consultation on Changes to the Early Warning System

Thank you for the opportunity to provide comments to the Canadian Securities Administrators (the “CSA”) in response to the CSA's Notice and Request for Comment on Proposed Instrument Multilateral Instrument 62-104 *Take-over 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 Bid and Insider Reporting Issues*. We hope that you find our comments thoughtful and relevant.

With more than $129.5 billion in assets, the Ontario Teachers' Pension Plan ("Teachers'") is the largest single-profession pension plan in Canada. An independent organization, it invests the pension fund's assets and administers the pensions of 300,000 active and retired teachers in Ontario.

General Comments

The Notice and Request for Comments suggests that the amendments are being proposed in large part to address concerns raised over "hidden ownership" and "empty voting". We are concerned that the analysis in The Notice and Request for Comments has been developed only in that context and does not give sufficient consideration to the capital market implications of the amendments. We believe that the Commissions need to undertake more work on the cost-benefit analysis of the amendments before they can responsibly be adopted. We note that a more thorough cost-benefit analysis is consistent with the acknowledgement by the Ontario Securities Commission ("OSC") in their 2013-2014 Statement of Priorities issued June 27, 2013:

> A key part of our plan is to improve our cost-benefit analysis of regulatory proposals and to improve the quality of this critical tool. As part of this analysis, we will be looking to industry to inform our process by providing input and assessment of expected impacts.[1]

In addition, the OSC identifies effective access to capital as among the most important areas where it intends to focus its resources: "The OSC recognizes that cost-effective access to capital is critical to companies of all sizes to grow and develop"[2]. As we outline below, we are concerned that the proposed amendments may limit access to capital for over 80% of Canadian companies (those identified as "small-cap" and "micro-cap"). Our concern is that the proposed amendments will alter the relative economics of investing by encouraging investment outside of Canada which could have profound negative impact on the Canadian issuers' ability to access capital.

In the CSA's laudable effort to respond quickly to concerns about "hidden ownership" and "empty voting", we found that many elements of the amendments have not sufficiently been articulated, including triggers for inclusion of derivative positions in calculating whether disclosure thresholds have been tripped. We are concerned that this approach can only lead to significant market inefficiencies, such as:

- investors struggling to determine whether disclosure is required and likely adopting differing disclosure practices as a result of differing interpretations of the language of the amendments,
- other market participants facing uncertainty in assessing that varied disclosure, and
- the Commissions and market participants potentially having to deal with these inconsistencies in the context of review and enforcement initiatives.

In this context, while the amendments to the existing system may warrant consideration, we find that a more extensive analysis of the alternatives and all of the relevant costs and benefits as well as a greater refinement of the amendments themselves is required before any changes can properly be considered and/or implemented.

[1] OSC Notice 11-768 Notice of Statement of Priorities for Financial Year to End March 31, 2014. June 27, 2013, page 6408.
[2] IBID, page 6411.

Reduction of Reporting Threshold from 10% to 5%

Ontario Teachers' is not supportive of reducing the Early Warning Reporting threshold from 10% to 5%. We are concerned that insufficient analysis has been undertaken of the structure and dynamics of the Canadian capital markets and the other markets that appear to be used by the CSA as the paradigm for the proposed changes to our early warning regime.

There is a general and long-standing theme in the development of the Canadian take-over bid regime – which is the context in which our early warning regime was developed – that recognizes the differences in the level of concentration of control in the US and Canadian markets. In the *1983 Report of the Securities Industry Committee on Take-Over Bids*, for example, it was noted in the contextual overview of take-over bid regulation in various markets that:

> *While Canadian public companies tend to be effectively or legally controlled, American public companies are in most cases widely held.*

This statement was accompanied by an analysis of the extent of control in the S&P 500 Index, which showed that 1.2% of the included companies were the subject of "legal control", 13.6% were the subject of "effective control", and 85.2% were "widely held". While market structure and dynamics undoubtedly have changed over the intervening decades, the nature of those changes and anticipated trends must be well understood before it can be appropriate to suggest that the differences the regulatory framework that has been developed in another market – like the United States – is necessarily appropriate in Canada.

While we understand that the current reporting threshold of 10% is dissimilar to that in other markets, particularly the United States, the benefit of "alignment" with thresholds in other markets must be assessed in the context of differences between the markets and the costs of such a change. We are concerned that the proposal does not take into account the very real and fundamental differences in market characteristics, such as capitalization, depth and institutional investor concentration that make policies appropriate for one jurisdiction unsuitable for the Canadian market.

The distinctiveness of the Canadian capital market lies in the preponderance of small companies. When compared to the US, the total market capitalization of Canadian public issuers is 10% of the US market[3]. The average US company is a little more than 8 times larger than a listed company in Canada. On a market capitalization basis, the average market capitalization of a Canadian issuer is $598 million compared to $4.9 billion in the US. When general market capitalization classifications are applied to public issuers in the Canadian and US markets, the average Canadian company would be considered Small-Cap[4] while an average US company is Mid-Cap. Generally, Mid-Cap companies have larger public floats and as a consequence have higher trading activity compared to Small-Caps. As a result the Canadian market is less liquid than that of the US.

It is worthwhile to note that the majority of the Canadian market by capitalization is already captured under the SEC's disclosure regime. Based on the most recent reporting from the Market Intelligence

[3] For the purpose of this discussion, the Canadian capital market is the total TSX and TSXV exchanges and the US capital market is the combination of the NYSE and NASDAQ. All US data is from Bloomberg. All Canadian data is from the April 30, 2013 TSX Market Intelligence Group (MiG) report.

[4] Market capitalization classifications used in this discussion are: Mega-Cap (+$200 billion), Large-Cap (between $10 billion and $200 billion), Mid-Cap (between $2 billion and $10 billion), Small-Cap (between $300 million and $2 billion), Micro-Cap (between $50 million and $300 million) and Nano-Cap (< $50 million).

Group at the TSX ("MiG")[5,6], 226 Canadian issuers, representing 63% of the total Canadian market capitalization are cross-listed on a US stock exchange and thus already captured under the SEC's 5% ownership reporting requirements. Furthermore, of Canada's major indices, 73% (44 out of 60) of companies in the S&P/TSX 60 and 37% (87 out of 237) of issuers in the broader S&P/TSX Composite Index are cross-listed on a US stock exchange.

The overall lower liquidity of the Canadian market becomes more acute when investors cross reporting thresholds. Generally, investors are hesitant to cross reporting thresholds because once they do they become susceptible to front-running, making additional trading activity challenging which in turn reduces liquidity and potentially impedes their ability to act in the best interests of their clients/beneficiaries as well as limits the access of issuers to capital. This can be particularly critical in the context of passive investment strategies.

When an investor is required to disclose to the market an intention to sell, other market participants can take advantage of this information which could result in a more heavily discounted stock price than would normally have been experienced had the intention to sell not been communicated to the market. At present, when confronted with selling once a reporting threshold has been crossed investors usually choose one of three options: 1) sell their shares into the market, at a discount to the market value, 2) execute a block sale (which also normally includes a discount) or 3) sell the shares slowly over an extended period of time. In executing the third option, investors are attempting to reduce the impact of selling at a discount which remains given that the intention to sell has been disclosed to the market. However, this ties up capital that could otherwise be deployed. No matter what action is taken, once a reporting threshold is crossed the stock's pricing dynamic changes making transactions in the stock more constrained in the hands of the investor and potentially impeding the ability of the investor to act in the best interests of their clients/beneficiaries as well as constraining the efficient operation of the capital markets in Canada. Reducing the reporting threshold to 5% will only amplify this impact of limited liquidity sooner.

As previously stated, the Canadian capital market is characterized by a large number of smaller companies with the total Canadian market being approximately 10% of the US market and the average US issuer is 8 times as large as its Canadian counterpart. Given that investors, particularly investors whose portfolios track an index and are otherwise passive, generally want to avoid crossing thresholds for a number of reasons – the difficulty in executing trades once a reporting threshold is crossed, a natural avoidance for regulatory burden and the competitive advantage gained when investment strategies remain confidential, it is reasonable to assume that investors will make investment decisions to maintain anonymity.

Investors choosing not to be subject to the disclosure requirements would be more likely to choose to deploy their capital in other markets where the same size of the investment (or even larger) would not trigger a reporting requirement because of the larger market capitalization available in that market. We believe that an unintended consequence of reducing the reporting threshold, which must be analysed and understood before amendments of the type that are being discussed are implemented, would be to deter investment in Small- and Micro-Cap Canadian companies, those occurring in the greatest percentage of the Canadian market and those with the greatest need of capital from Canadian institutional investors.

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[5] The May 2013 MiG Report is available from http://www.tmx.com/en/mig/index.html.
[6] All data presented is as of the end of April 2013.

The following table shows that 82% of issuers in the Canadian market that are not already cross-listed in the US fall in the Mid- to Small-Cap range[7]. The data clearly illustrates that investors have more investment choice in the US market for each market capitalization band.

		# of Listed Issuers			
		Canada[8] (TSX &TSXV)		US (NYSE & NASDAQ)	
		#	%	#	%
Mega Cap	> 200 billion	-	0%	14	<1%
Large Cap	10 billion to 200 billion	42	6%	375	10%
Mid Cap	2 billion to 10 billion	97	13%	863	23%
Small Cap	300 million to 2 billion	235	31%	1,438	39%
Micro Cap	50 million to 300 million	384	51%	1,038	27%

Our concern, should the disclosure threshold fall to 5%, is that investors, having considered an investment in a Canadian Micro- to Small-Cap company when the threshold was 10%, would reallocate their funds and invest in a Mid- or Large-Cap larger company on the US market (or other market) where there is more choice, more liquidity, less likelihood to cross reporting thresholds and thus a greater opportunity to meet the investment objectives of their clients/beneficiaries. The negative consequences for small Canadian issuers is that their access to capital would be constrained which in turn could inhibit their ability to grow and result in an overall strain on the Canadian capital market. As investors move their capital to markets outside Canada, the effects of supply and demand would raise share prices making those markets generally much more attractive for investors than Canada.

Disclosure Requirements

Teachers' supports transparency but also believes that disclosures must be useful and disclosure for the sake of disclosure runs the risk of providing little or no value or even being counterproductive by reducing overall clarity. We have reviewed the reporting requirements and find that while they would result in more disclosure, it would not necessarily be useful disclosure. For example, Item 5 of Annex C, *Proposed Amendments to National Instrument 62-103 The Early Warning System and Related Take-Over Bid and Insider Reporting Issues* presents a lengthy list of possible purposes of the transaction that need to be reported under the revised rule. We have reviewed the list and find it to be both overly prescriptive in the level of detail being required and very broad in terms of the number of plans or future intentions to be considered (for instance the "catch all" provision in Item 5(k)). In our view, such broad disclosure could be interpreted by the market in a number of different ways which leads us to be very concerned that the breadth and depth of disclosure being requested is not only burdensome for investors, but more importantly, would not result in the enhanced disclosure being sought and could very easily lead to disclosure that has little or no utility to the market.

In addition to our concern about the breadth of the disclosure not providing the desired clarity, we find that the prescriptiveness of the disclosure could be damaging to the Canadian market. In order to maximize returns for clients/beneficiaries, investors dedicate significant resources to seek a competitive advantage which could be uncovering an undervalued issuer based on an investment thesis. We are concerned that the prescriptive nature of the proposed disclosure would result in an investor being

[7] For the purpose of this example we have excluded Nano-Cap stocks – those issuers with a $50 million or less market capitalization. Had we included these companies, the percentage of small companies (i.e. Small-Cap and lower) would have risen to 87% for the Canadian market and 70% for the US market.
[8] Only those companies not cross-listed in the US (i.e. not subject to the 5% reporting threshold).

required to disclose their thesis to the market which could then be adopted by others thus removing any competitive advantage and potentially disadvantaging clients/beneficiaries. Investors are generally hesitant to disclose their investment thesis to protect their competitive advantage and would aim to stay below reporting thresholds to avoid harm. As a result, we believe the combination of lowering the investment threshold to 5% and the revised disclosure requirements will have the unintended consequence of incentivizing investors to invest less in the Canadian capital market and to allocate capital elsewhere.

Inclusion of Derivatives in Early Warning Calculation

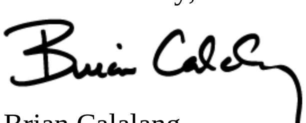
In our view, there is a lack of clarity around the inclusion of derivatives in the Early Warning Calculation. Upon our review of the proposed changes, a number of comments/questions have arisen, including the following.

1. Please provide a more detailed explanation of the definition of the concepts “substantially equivalent” and “substantially replicate” as discussed in the *Early Warning Reporting Trigger* section of the Proposed Instrument.
2. What is the rationale for using a 90% threshold?
3. Will the proposed regime allow netting of short equity equivalent derivatives against long cash positions? It is not inconceivable for one portfolio manager in one division to have differing views from another and netting would provide a closer approximation of our economic interest.
4. Would the CSA be able to provide an explanation of the definition of partial-exposure instruments, including examples? More specifically, how would the instrument address a total return swap (TRS) on the TSX 60, a TRS basket on 10 names and a volatility swap on the TSX 60?

Generally, we find that the current draft lacks sufficient clarity for us to provide meaningful comments and would result in widely divergent reporting practices if not refined by the Commissions. Once the above questions have been clarified, we would then be able to provide comments to the CSA.

Thank you again for this opportunity to comment on the proposed changes to the Early Warning System. Should you have any questions, please contact Brian Calalang, Senior Legal Counsel, Investments at brian_calalang@otpp.com or 416.730.6871, or Paul Schneider Manager, Corporate Governance at paul_schneider@otpp.com or 416.730.5307.

Yours sincerely,



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