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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
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Ontario Securities Commission
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Dear Sirs/Mesdames:

Re: Request for Comment – Proposed Amendments to Multilateral Instrument 62-104 *Take-over Bids and Issuer Bids* and National Instrument 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*

This letter is provided to you in response to the Notice and Request for Comment – Proposed Amendments to Multilateral Instrument 62-104 *Take-over Bids and Issuer Bids* and National Instrument 62-103 *Take-Over Bids and Issuer Bids* and National Instrument 62-103 *Early Warning System and Related Take-Over Bid and Insider Reporting Issues* (the "**Proposed Rule**") published at (2013) 36 OSCB 2675. Following our initial comments we will respond to a number of the specific questions set out in the Proposed Rule. We have only reproduced the questions to which we will be responding.

We are supportive of the CSA's proposal to reduce the early warning reporting threshold from 10% to 5% but only if the eligibility to be an EII and use the AMR is amended, as proposed, to eliminate anyone contemplating a proxy solicitation (subject to our further comments below). In addition we believe it is imperative that the EII eligibility is amended so as to expressly permit NI 81-102 mutual funds to be EIIs. We believe reducing the level to 5% aligns the Canadian requirements with those of many other countries which already have a 5% level.

1. Do you agree with our proposal to maintain the requirement for further reporting at 2% or should we require further reporting at 1%? Please explain why or why not.

We agree that further reporting should only be at the 2% level and not reduced to 1%. We believe that the added compliance costs of moving to a 1% level would outweigh the benefits of doing so.

2. A person cannot acquire further securities for a period beginning at the date of acquisition until one business day after the filing of the report. This trading moratorium is not applicable to acquisitions that result in the person acquiring beneficial ownership of, or control or direction over, 20% or more of the voting or equity securities on the basis that the take-over bid provisions are applicable at the 20% level.

The proposed decrease to the early warning reporting threshold would result in the moratorium applying at the 5% ownership threshold. We believe that the purpose of the moratorium is still valid at the 5% level because the market should be alerted of the acquisition before the acquiror is permitted to make additional purchases.

(a) Do you agree with our proposal to apply the moratorium provisions at the 5% level or do you believe that the moratorium should not be applicable between the 5% and 10% ownership levels? Please explain your views.

We support the moratorium at 5%, but are concerned about compliance costs for passive investors and suggest it remain at 10% for them. We support moratorium provisions applying to equity equivalent derivatives. We think the moratorium adequately addresses the balancing of the need for transparency before acquisitions are made. A requirement to issue the press release by the opening of business the following day is not practical, especially since the press release needs to include not only information about the acquirer's holdings, but also about the holdings of joint actors (see items 3 and 5 of Form 62-103). In any event, the existence of the moratorium makes it unnecessary to impose this deadline (or the

2 business day deadline to get the remainder of the info needed for the full report and get it signed by the acquirer as proposed under 5.2(1)(b) of MI 62-104). Adding these additional deadlines also results in a divergence between Ontario and other jurisdictions until such time, if any, as the Ontario Securities Act is amended to add such deadlines. The deadlines will necessitate further CSA enforcement expenditures and will generate additional disputes (between companies and bidders/activists) before the commissions and courts, and will provide an insignificant marginal benefit.

(b) The moratorium provisions apply to acquisitions of "equity equivalent derivatives". Do you agree with this approach? Please explain why or why not.

We agree that the moratorium provisions should apply to acquisitions of equity equivalent derivatives because the policy rationale for reporting is the same.

(c) Do you think that a moratorium is effective? Is the exception at the 20% threshold justified? Please explain why or why not.

We believe the exception at the 20% threshold is acceptable.

3. We currently recognize that accelerated reporting is necessary if securities are acquired during a take-over bid by requiring a news release at the 5% threshold to be filed before the opening of trading on the next business day.

With the Proposed Amendments to the early warning reporting threshold, we do not propose to further accelerate early warning reporting during a take-over bid.

(a) Do you agree? Please explain why or why not.

We agree that the early warning during a take-over bid does not need to be further accelerated.

4. The Proposed Amendments would apply to all acquirors including EIIs.

(a) Should the proposed early warning threshold of 5% apply to EIIs reporting under the AMR system provided in Part 4 of NI 62-103? Please explain why or why not.

We believe that the 5% threshold should also apply to EIIs, subject to two comments. First, we strongly believe that the definition of EII should be amended to delete the exclusion of NI 81-102 mutual funds from paragraph (c) of the

definition. The ability of such funds to qualify as EIIs may currently be of limited significance as pursuant to NI 81-102 they are not allowed to acquire ownership stakes of 10% or more in any one issuer and it may have been believed that as a result they would never be caught by the early warning requirements (notwithstanding that this could be complicated by ownership of convertible securities). However, under a 5% reporting threshold, being clearly entitled to qualify as Ells will become extremely significant. We believe they should expressly be included in the definition of an EII; indeed, reporting by such funds under the early warning system would only clog up otherwise important reporting by those who are not EIIs. Secondly, while we believe there is no reason not to have the 5% level apply to EIIs we would certainly defer to EIIs (and NI 81-102 mutual funds) who may have a better sense, given the size of the Canadian markets and the number of small and mid cap issuers in that market, as to whether lowering the reporting levels for them might cause undue compliance burdens given then number of issuers in whom they might easily attain a 5% holding, or given competitive concerns.

5. Mutual funds that are reporting issuers are not EIIs as defined in NI 62-103 and are therefore subject to the general early warning requirements in MI 62-104. Are there any significant benefits to our capital markets in requiring mutual funds to comply with early warning requirements at the proposed threshold of 5% or does the burden of reporting at 5% outweigh the potential benefits? Please explain why or why not.

Please see our discussion above—we strongly support expressly including NI 81-102 mutual funds in the definition of EII.

6. As explained above, we propose to amend the calculation of the threshold for filing early warning reports so that an investor would need to include within the early warning calculation certain equity derivative positions that are substantially equivalent in economic terms to conventional equity holdings. These provisions would only capture derivatives that *substantially replicate* the economic consequences of ownership and would not capture partial-exposure instruments (e.g., options and collars that provide the investor with only limited exposure to the reference securities). Do you agree with this approach? If not, how should we deal with partial-exposure instruments?

We agree that equity derivative positions as described in the Proposed Rule should be included in the calculation of the threshold for filing early warning reports due to hidden ownership concerns and because it provides meaningful information to the market regarding persons who have made a significant economic investment in the issuer. However, we believe that it is also important

to include certain partial-exposure instruments in the definition of equity derivative positions. It is common for activist hedge funds to acquire a position in an issuer by buying options since they anticipate that their actions (or the fact of their interest in the issuer) will cause the stock price to rise. Therefore call options, or at least call options held by non-passive investors, should also be included. In addition, as detailed in our answer to question 7, we have concerns regarding the current definition of equity equivalent derivatives.

7. We propose changes to NP 62-203 in relation to the definition of equity equivalent derivative to explain when we would consider a derivative to substantially replicate the economic consequences of ownership of the reference securities. Do you agree with the approach we propose?

We support fully the concept of including partial exposure instruments in the calculation of the threshold for filing early warning reports. However, we feel that the current definition of equity equivalent derivatives is too uncertain and imprecise to be able to comment meaningfully on at this time, and would encourage the CSA to work closely with market participants to improve this definition. As one example, it is not clear if positions can be netted in calculating exposure; we would note that in the derivatives marketplace netting is the norm. In addition, the current guidance is too limiting. What about a derivative on a publicly traded parent company which holds a controlling position in a publicly traded subsidiary? Also, it is unclear how this definition will apply to some of the existing specialized publicly traded fund vehicles, including those that (i) invest in certain classes of shares of a bank or (ii) invest in a distinct group of companies. Further, the guidance in NP 62-203 is inconsistent (please see below).

8. Do you agree with the proposed disqualification from the AMR system for an EII who solicits or intends to solicit proxies from security holders on matters relating to the election of directors of the reporting issuer or to a reorganization or similar corporate action involving the securities of the reporting issuer? Are these the appropriate circumstances to disqualify an EII? Please explain, or if you disagree, please suggest alternative circumstances.

We fully support the proposed disqualification from the AMR for an EII who solicits or intends to solicit proxies from security holders on matters relating to the election of directors or to a reorganization of similar corporate action involving the securities of the reporting issuer. However, we feel that the definition of "solicits" is too vague. Does the CSA mean the definition of "solicit" in NI 51-102 and the exceptions from it? Nevertheless, we agree with

the suggestion that it needs to refer to solicitations concerning elections of directors as well as for corporate transactions but believe that the types of corporate transactions identified may be too narrow and should include any transaction under which securities are to be changed, exchanged, issued or distributed (consistent with item 14.2 of Form 51-102 F5).

We note that in the United States the test is "not with the purpose nor with the effect of changing or influencing the control of the issuer nor in connection with or as a participant in any transaction having such purpose or effect"; we encourage the CSA to consider such a two prong test tied to purpose and to effect.

9. We propose to exempt from early warning requirements acquirors that are lenders in securities lending arrangements and that meet certain conditions. Do you agree with this proposal? Please explain why or why not.

We agree.

13. Do you agree with our proposal to apply the Proposed Amendments to all reporting issuers including venture issuers? Please explain why or why not. Do you think that only some and not all of the Proposed Amendments should apply to venture issuers? If so, which ones and why?

Yes. As a practical matter the transparency concerns are more significant for venture issues given their smaller market cap.

15. If the proposed new requirement does lead to an over-reporting of these derivatives, is this rectified by the requirement in the early warning report for acquirors to explain the purpose of their acquisition and thereby clarify that they do not intend to acquire the referenced securities upon termination of the swap?

We are concerned about the amount and type of information that will be required to be reported in respect of an equity equivalent derivative. We believe it seeks information that is confidentially bilaterally negotiated and likely will not be of any assistance to the marketplace

<u>Comments Concerning MI 62-104</u>

- In the definition of "equity equivalent derivative", for clarity, "of the security" needs to be replaced with "of the voting or equity security" since it is otherwise not clear whether it means the voting or equity security of the issuer or the derivative.

- Definition of "specified securities lending arrangement" – in (a), delete "a copy of which is retained by each party to the agreement" since the existence of the written agreement is what is relevant, not who has copies of it (which might include the law firm rather than the party). In (d) it needs to be made clear that the record date is "for voting", since the record date for voting can be separate from the record date for mailing for the meeting

- Definition of "securities lending arrangement" – We are concerned with the reference to returning the security or "an identical" security. In TELUS' case, anyone who borrowed non-voting shares under a securities lending arrangement ended up delivering voting shares. We would instead suggest the language regarding the return of the security also encompass any security substituted for it under a transaction under which the original security was changed, exchanged, or replaced.

- 5.2(2) - If the time limits for issuing a press release under 5.2(1)(a) and filing a report under 5.2(1)(b) are retained, do those time limits apply to the disclosure under 5.2(2)? If so, that just compounds the difficulty of complying – and timing is less relevant as a practical matter when reporting 2% decreases.

- 5.2(3) – We believe this provision should be deleted as it could result in substantial compliance costs, with little benefit, to the extent that the investor has acquired very close to 5% and is constantly falling above or below that threshold. The 2% rule provides a reasonable band for immaterial changes.

Comments Concerning NP 62-203

We believe the Proposed Rule is inconsistent in the approach to partial-exposure derivatives. It says equity equivalent derivatives "generally" include only cash-settled TRS or substantially similar derivatives. Then it expressly states in absolute terms that they do **not** include partial-exposure derivatives. Then in the next paragraph it says that they might include partial –exposure derivatives if "abusive".

Regarding securities lending arrangements, the borrower never has "full" ownership rights – it only has substantially all of the benefits of ownership. Title remains with the titleholder (i.e. a depositary or broker), for example.

Comments Concerning Form 62-103F1

- Item 3.2 – We do not understand "including control that is deemed to exist under the law". Is this supposed to require identification of situations of "effective control" as defined in 62-103 or something more? What law is "the law"?

- Item 3.6 – It would be helpful to clarify whether you need to provide a separate breakdown for each of (a), (b), (c) and (d), or can just give the aggregate number and percentage.

- Item 3.8 – Should limit disclosure of securities lending arrangements to those involving the acquiror.

- Instruction (iii) to item 3.10 – It would be better to say the counterparty identity need not be provided unless the counterparty is one of the joint actors.

- Item 5 – It is not clear that this covers plans or intentions to cause the issuer to effect an issuer bid, stock split or stock dividend or a spin-out of a division (unless it is a "material change") – all of which have been pursued by activists in the past and should be covered.

- Item 6 – We are concerned it will not be possible to name all such persons – either because they are unknown, or because disclosure is prohibited due to confidentiality obligations or privacy requirements at law.

We would be happy to discuss our comments with you; please direct any inquiries to Andrew MacDougall (416) 862-4732 (amacdougall@osler.com) or Robert Lando (212) 991-2504 (rlando@osler.com).

Yours very truly,

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