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British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial and Consumer Affairs Authority
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
New Brunswick Financial and Consumer Services 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

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Re : *Response to the request for comments*
CSA Consultation Paper 54-401
Review of the Proxy Voting Infrastructure

We preface this response by expressing our appreciation to the *Canadian Securities Administrators* (CSA) for their continuing efforts to address the serious concerns related to shareholder voting processes.

The *Canadian Society of Corporate Secretaries* (CSCS) is a national association representing corporate secretaries and governance professionals.

The movement to give shareholders a stronger voice in the way Canada's public companies are governed is a positive trend that benefits both investors and issuers. The question is not whether shareholders ought to have a voice, but rather whether that voice is being heard properly, and whether shareholder votes are being counted properly.

CSCS believes simply that shareholder votes must be counted with the same degree of care and integrity that applies to ownership and dividend rights. We also believe that all shareholders, registered and beneficial alike, deserve equal rights.

Unfortunately, the current system of shareholder voting falls far short of respecting these basic principles.



CSCS has devoted considerable time and resources to promote a fundamental reform of the rules for shareholder voting:

- In 2005 we conducted a series of forums in collaboration with the CSA in Montreal, Toronto, Calgary and Vancouver to discuss the functioning of National Instrument 54-101 on communications with beneficial shareholders.
- In 2007 we participated in a stakeholders' panel on shareholder voting at the annual conference of the *Canadian Investor Relations Institute*.
- We published a white paper in 2008 promoting changes to the corporation statutes to provide equal treatment for registered and beneficial shareholders.
- In 2010 we extensively reviewed and provided comments to assist in the preparation of the Davies paper on the *Quality of the Shareholder Vote in Canada*.
- We convened the 2011 *Shareholder Democracy Summit* and published an inaugural report with the Summit's findings.
- In 2012, following up on the Summit, we proposed to key stakeholders a *Facilitation Program* with a five year roadmap and milestones that would clear the path for reform.
- In the latest step in our campaign for reform we conducted a series of public forums along with the CSA. We held open meetings this October in Montreal, Toronto, Calgary and Vancouver in collaboration with the CSA.

Progress made to date, in spite of these efforts, has been painfully slow, and the modest progress that has occurred has been disappointing.

As the CSA acknowledge in the request for comments, the shareholder voting system has evolved over time into a highly complex intermediated system. The CSA request for comments focuses on the complexity inherent in the vertical dimension of the shareholder voting process. This is the dimension that allows votes and other shareholder rights to flow from the issuer at one end of the vertical process to the investor at the other end.

The degree of complexity in the vertical axis is matched by an equivalent degree of complexity in the horizontal axis.

On the horizontal axis we find at each layer of the vertical axis numbers of stakeholders who have similar roles. In certain cases collaboration among roles has resulted in some form of integration in the processes applied at that layer. For instance, transfer agents in Canada collaborate as members of the *Stock Transfer Association of Canada*. At the intermediary level there is similar industry collaboration in the *Investment Industry Association of Canada*. There are similar associations at most of the horizontal layers; for instance the *Canadian Coalition for Good Governance* for institutional investors; the *Canadian Securities Administrators* for securities regulators; and so on.

It is quite apparent that there are gaps in the collaboration that militate against meaningful progress. To mention one of those gaps, at the regulatory level, there does not appear to be sufficient engagement between the CSA and their regulatory counterparts on the corporate law side.

Also absent from the field is the *Bank of Canada*. To some degree the problems experienced in the shareholder voting process are a symptom of a settlement and clearing deficiency for which the *Bank of Canada* has traditionally played a central leadership role, yet there is no evidence that these issues are on the *Bank of Canada's* radar screen.

Any attempt to address the serious shortcomings of the current processes requires, as the request for comments points out, a "holistic" approach. CSCS emphatically agrees with that

assessment. The comprehensive approach that CSCS advocates is one that addresses not only the vertical dimension of complexity, but also its horizontal axis. CSCS believes that anything less will fail to lead to significant improvements in the process.

CSCS advocates a comprehensive approach to reform with the following salient features:

- Fundamental reform of both corporate and securities law rules relating to shareholder voting:
 - Securities and corporate regulators both fully engaged and committed to the reform process.
 - Registered and beneficial shareholders to enjoy the same voting and participation rights.
- Elimination of the OBO NOBO distinction:
 - Restoring the issuer's right to know the identity of its shareholders.
 - New rules for nominee holders that respect the investor's right to maintain privacy in relation to holdings and voting, while also respecting the issuer's right to know its shareholder.
- Complete dematerialization of the voting process:
 - Entirely digital end-to-end processes.
 - Normalized data flows for shareholder security positions as of the record date including voting and participation entitlement;
- Auditable data trails coupled with effective processes and controls to ensure respect for the integrity of the voting process.
- A specific roadmap for reform with defined milestones and a reasonable horizon for completion.

CSCS acknowledges that the challenge presented by the approach we advocate is substantial. It is important for stakeholders to bear in mind however that the ultimate objective is a very modest one: to ensure that shareholder votes count with the same degree of integrity that applies to other shareholder rights like dividends for instance.

Canada is not the only country experiencing challenges when it comes to shareholder voting. We could seize the opportunity to be the first country to tackle the issue in a straightforward and intelligent way to deliver effective reform, as well as industry-leading processes.

Regulators, who coexist in horizontal silos similar to other stakeholders, have a key role, perhaps the key role to play. It is unfortunate that the regulators have yet to come together on this issue.

The CSA, the provincial and federal regulators who determine corporate law and policy, and the *Bank of Canada* have a responsibility to lead the way by entering into a meaningful collaboration to address shareholder voting processes.

Effective shareholder voting is one of the cornerstones of effective governance and healthy capital markets. The CSA's primary responsibility is to protect Canadian investors and to regulate the functioning of Canada's capital markets. That mandate led the CSA in its pioneering efforts to address shareholder voting processes. It is clear however that the CSA cannot succeed in resolving the current problems without engaging with other regulators in a concerted way.

The request for comments asks two key questions:

Is accurate vote reconciliation occurring within the proxy voting infrastructure?

The answer to this question at the present time cannot be anything other than “no”. There are some processes currently in place that seek to reconcile shareholders, issuers, and votes, but none could be called “end-to-end.”

What type of end-to-end vote confirmation system should be added to the proxy voting infrastructure?

For “end-to-end” to have any real meaning, the system has to reconcile voting from the shareholder to the issuer, and it has to happen for all shareholders. At the present time that is not occurring.

Information technology has been the key enabler that allowed the capital markets to grow in scope, pace and volume of transactions in the recent past. It has done so by forsaking paper-borne processes in favour of machine-borne processes. Given the timing constraints of shareholder meetings, given the large number of shareholders, given the sheer volume of information and transactions that must flow to enable shareholders to vote effectively, there is no longer any room for paper-borne processes.

It is time to adopt end-to-end digital processes for shareholder voting, that is to say, to dematerialize the entire voting process. With digitization, there will be a sound basis for end-to-end vote reconciliation, for the audit of processes and transactions, for quality assurance, and for greater timeliness.

Some aspects of the current dysfunction, in particular the impact of share lending on the quality of the shareholder vote, will be very difficult to deal with effectively unless the process is dematerialized.

There is evidence at the present time that certain institutional shareholders are now reluctant, or have completely ceased, to lend their portfolios because share lending interferes unduly with the ability to exercise voting rights. What will be the impact on the capital markets if more and more institutional shareholders follow suit?

Information technology is a powerful enabler and can support robust processes that accomplish objectives that paper-borne systems are incapable of achieving. For instance, if all data flows for voting information were normalized:

- voting information could flow at electronic speeds rather than post office speeds;
- shareholder entitlements could be effectively tracked and reconciled without privacy concerns;
- it might become possible to allow portfolios to be lent ex-vote;
- it is also possible that an IT-borne voting infrastructure would allow concerns related to ‘empty-voting’ to be addressed effectively;
- for the first time, shareholder voting dashboards could become a reality for all shareholders, not just for the privileged few who have access to a transfer agent’s voting platform or Broadridge’s *Proxy Edge* system.

The foregoing only begins to scratch the surface of possibilities could emerge as the fruit of dematerialization and fundamental reform in the voting process.

Next Steps

The request for comments seeks guidance on next steps.

CSCS strongly advocates the following next steps:

1. **The regulators should collaborate.** CSA, the corporate regulators, and the *Bank of Canada* need to come together to address the concerns with the shareholder voting system.

At its heart shareholder voting is a corporate law concern. For many issuers the ratio of beneficial shareholders to registered shareholders is in excess of 90%. Yet corporate law largely ignores beneficial shareholders. It is more than high time that beneficial shareholders get equal rights. The corporation regulators need to take ownership of that issue and work closely with the CSA to ensure that all shareholders are treated equally.

Finally, the *Bank of Canada* has a key role to play. The problems with shareholder voting are a symptom of a partial settlement and clearing failure. The current depository system came about to address settlement and clearing problems for securities transactions that resulted from the pace and volume of transactions that had outstripped the shareholder registration paradigm that prevails under corporate law. The old share registry and paper certificate system was dying under its own weight and impeding the efficient flow of capital. The book-based depository system that evolved solved the capital markets problem for two of the three key shareholder entitlements: i) the right to buy and sell, and ii) the right to dividends. Voting, the third key entitlement was neglected. In the result, the gates and processes that must be aligned to allow votes to be properly exercised and counted in many cases are in disarray. In fairness to all concerned, it is only recently that shareholder voting has emerged as a key governance tool for modern public companies. The problems are well-documented, and the time to act is now.

2. **Reliable information must be gathered.** The request for comments asks a series of excellent questions for which answers are urgently needed. The questions probe for information on the processes at work amongst the agents whose roles lie between the shareholder and the issuer: transfer agents, intermediaries and Broadridge.

If dematerialization is to occur (and it must occur for the system to improve), the information flows and processes at play among all those agents must be mapped. That is the only path that can lead to creating the normalized data structures that will allow high integrity data to flow in real time from end to end in the voting system. The CSA already have the regulatory tools and authority that will allow that information to come to light. Doing that process mapping is a vital first step. It will be painstaking work and it will be time consuming if it is to be done properly. Without that information gathering phase, it will be very difficult and perhaps impossible to make any real progress.

3. **A roadmap for reform should be proposed.** If the problems with shareholder voting are to be addressed effectively and in a timely manner, the regulators need to set the pace and there has to be a reasonable timetable for reform. As part of its proposed Facilitation Program, CSCS proposed five years as a reasonable timeframe for reform. A roadmap for reform should have three distinct phases:

- Information gathering;
- Determining the reforms needed to be implemented;
- Implementation.

Without a disciplined process and milestones to judge progress, it will be very difficult or impossible to make any significant improvements.

4. **Sectorial approaches to the problem should be set aside in favour of overall reform.** *Notice and Access* is a case in point. *Notice and Access* has largely failed to deliver the hoped-for benefits of reducing paper burdens, streamlining the meeting information process, and reducing costs. The reason is that *Notice and Access* simply does not go far enough, and there was a lack of collaboration among concerned regulators. At the core of *Notice and Access* remain paper-borne processes. The result is another layer of regulation, longer lead times and additional fees that, at least for issuers, have failed to deliver much in the way of savings, and made setting key dates for the meeting process even more difficult to do. Additional sectorial approaches to the problem should not be contemplated in the absence of a compelling need.
5. **Funding for a dematerialized voting system should be studied.** At the present time issuers bear substantial proxy solicitation costs, as do other stakeholders. A well-functioning, end-to-end, dematerialized voting system should yield cost savings for all stakeholders, but it will not eliminate all of the current expense. A new information technology-based voting system will need to be funded by stakeholders in a fair way so that everyone benefits. Planning will be required to make that happen.

We at CSCS will continue to do our best to advance the cause of reform and to work with all stakeholders to achieve that objective. We encourage all stakeholders to come forward to share their concerns, to discuss avenues for reform, and to collaborate to address these concerns.

On a final note, the request for comments at footnote 58 notes that unresolved over-reporting situations occurred in at least 17% of meetings. At the CSCS annual governance conference in Halifax this past August, Computershare provided updated statistics that showed 17.02% for 2011, 22.70% for 2012 and 25.71% for 2013.

These metrics are truly a cause for concern and they reveal a troubling and worrisome trend. All the more reason to marshal vigorous efforts to address these important issues.

Yours truly,



David Masse
Chairman of the Board