

Canadian Coalition for  
**GOOD GOVERNANCE**

June 11, 2014

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

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Dear Sir/Madam:

**Re: Canadian Securities Administrators (“CSA”) Notice and Request for Comment  
Proposed National Policy 25-201 Guidance for Proxy Advisory Firms (the “Proposed  
Policy”)**

The Canadian Coalition for Good Governance (“CCGG”) thanks you for the opportunity to provide our comments on the CSA Proposed Policy released on April 24, 2014.

CCGG's members are Canadian institutional investors that together manage over \$2.5 trillion in assets on behalf of pension funds, mutual fund unit holders, and other institutional and individual investors. CCGG promotes good governance practices in Canadian public companies in order to best align the interests of boards and management with those of their shareholders. We also seek to improve Canada's regulatory framework to strengthen the efficiency and effectiveness of the Canadian capital markets. A list of our members is attached to this submission.<sup>1</sup>

## **GENERAL COMMENTS**

As we stated in our comment letter on the 2012 CSA Consultation Paper 25-401: *Potential Regulation of Proxy Advisory Firms* (the "Comment Letter"), we do not believe that the concerns expressed by some market participants regarding the role of proxy advisors justify a regulatory response.<sup>2</sup> The Proposed Policy does not challenge the important role that proxy advisors play in helping institutional investors carry out their fiduciary obligations to their clients in voting proxies, nor does it suggest that the role is fundamentally flawed. As we stated in the Comment Letter, if issuers and their advisors believe that institutional investors are inappropriately delegating their voting responsibilities to proxy advisors, then this issue should be taken up with the investor and not the proxy advisor – regulating proxy advisors is not the answer. A better approach, as we stated in the Comment Letter, would be to encourage proxy advisory firms to develop a voluntary code of best practices. The Proposed Policy recognizes that institutional shareholders and other clients are the "legitimate judges" of proxy advisory services and is intended to provide a framework for that judgment;<sup>3</sup> a voluntary code would provide the same framework. The European Securities and Markets Authority recommended this course of action after studying the issue and, as the Proposed Policy points out, a voluntary code of best practices was recently released by a group of proxy advisory with operations in the EU.<sup>4</sup> CCGG intends to study this document and make our representations on the voluntary code directly to proxy advisory firms, which we believe is the appropriate process.

Further, we believe that much of the guidance as to best practices contained in the Proposed Policy does not add substantive value because proxy advisors operating here already have similar policies and practices in place and disclose them publicly. As a basic principle, regulation should not be imposed if market forces are already eliciting the desired behaviour. Some of the guidance in the Proposed Policy is based on concerns that, as we explained in our Comment Letter, have little merit (e.g., a lack of transparency in developing proxy voting guidelines). It also is unclear how compliance with the Proposed Policy would be assessed and what resources the CSA intend to put to that effort.

However, given that the CSA have determined that a regulatory response is warranted, we are pleased that the Proposed Policy merely provides guidance as to suggested policies and practices to be followed by proxy advisors and is not intended to be prescriptive. As we set out below in our specific comments, though, we believe the Proposed Policy overreaches in some areas.

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<sup>1</sup> Please note that to avoid any appearance of a conflict of interest as a result of their ownership of Glass Lewis, our members Ontario Teachers' Pension Plan and Alberta Investment Management Corporation did not participate in the preparation or approval of this submission.

<sup>2</sup> [http://www.ccg.ca/site/ccgg/assets/pdf/submission\\_re\\_csa\\_consultation\\_paper\\_25-401signed-1.pdf](http://www.ccg.ca/site/ccgg/assets/pdf/submission_re_csa_consultation_paper_25-401signed-1.pdf)

<sup>3</sup> "The Proposed Policy will provide institutional investors or other proxy advisory firms' clients as the legitimate judges with a framework for evaluating the service provided to them by proxy advisory firms." Page 4341

<sup>4</sup> Best Practice Principles for Providers of Shareholder Voting Research & Analysis at <http://bppgrp.info/wp-content/uploads/2014/03/BPP-ShareholderVoting-Research-2014.pdf>

We also are pleased to see that the Proposed Policy appears to accept the view, supported by CCGG in its Comment Letter, that proxy advisory firms do not exert undue influence on the development of corporate governance practices but rather their guidelines reflect principles shared by their institutional shareholder clients that are developed in a symbiotic relationship rather than being forced on uninformed or unengaged institutional investors that are not carrying out their fiduciary obligations.

## ***SPECIFIC COMMENTS***

### **Purpose of the Policy**

We would like to point out that characterizing proxy voting as a “means for investors and issuers to engage in dialogue about matters concerning the issuer” does not accurately capture the nature of the proxy vote. For example, with Say on Pay advisory votes, shareholders are expressing a view as to the issuer’s approach to executive compensation and not telling the board what compensation policies to adopt or amounts to pay, so in this case shareholders can be said to be involved in a dialogue with issuers. In most other vote situations, however, the proxy vote is more than merely ‘engaging in dialogue’ with issuers and is generally a means of communicating shareholders’ instructions on a particular matter to management and directors. Perhaps this misunderstanding reflects the broader debate about whether it is the primacy of shareholders or directors that should prevail and underlies some of the sense of grievance shown by issuers towards proxy advisors who are, after all, advisors to the shareholders and not the issuer and are working in the interests of shareholders rather than management or the board.

The Proposed Policy also refers here to communications with not only clients and market participants but also “the media and the public”, which we believe is overreaching as is discussed in more detail below.

### **Conflicts of interest**

The Proposed Policy’s guidance with respect to addressing actual or potential conflicts of interests reflects best practices and we agree that proxy advisory firms should adopt the sort of policies and practices outlined. We believe as stated above, however, that proxy advisory firms operating in Canada already have such policies in place and so we do not expect that the Proposed Policy’s guidance will result in any substantive change.

We are pleased that the Proposed Policy does not suggest that issuers disclose their use of a proxy advisor in the proxy circular since such disclosure would compromise any ethical walls set up by the proxy advisors between institutional research services and consulting services sold to issuers. In the view of CCGG’s members, effective ‘firewalls’ are of the utmost importance in such circumstances and regulation should not lead to those walls being compromised. In support of this, we suggest that the guidelines make reference to the importance of proxy advisory firms ensuring that their compensation practices reflect a strict delineation between separate business units that could give rise to potential conflicts of interest (e.g. there should not be a common bonus pool for employees in institutional research services and employees in consulting services).

### **Transparency and accuracy of vote recommendations**

As stated in our Comment Letter, we believe that a concern with a lack of transparency on the part of proxy advisory firms is without merit and there should not be regulatory intervention in this area. Their corporate governance guidelines and their approach to governance issues are publicly available on their websites.

We question whether it is important for ‘market participants’ other than institutional shareholder clients and the issuers to whom the vote recommendations are related to understand how proxy advisory firms arrive at specific vote recommendations and assess the quality of the research and analysis behind such a recommendation. We suggest that while it may be important for market participants to have a general understanding of how proxy advisory firms arrive at vote recommendations, the level of detail described, such as analytical models and assumptions used and sources of information from third parties, is not necessary for anyone else other than clients and issuers.

We are pleased to see an exemption from the need to disclose such information in situations which would compromise the “proprietary or commercially sensitive nature of information”: such an exemption is essential in order to avoid undermining the proxy advisory firms’ business model. We anticipate, however, that reliance on this exemption by proxy advisory firms will be a source of friction between issuers and proxy advisory firms going forward.

### **Development of proxy voting guidelines**

As we stated in our Comment Letter, proxy advisors currently develop their proxy voting guidelines in a highly consultative and comprehensive manner, soliciting input from both institutional shareholders and issuers annually, so regulatory guidance in this area is not necessary. Perhaps the CSA should encourage issuers to take advantage of the channels currently offered by proxy advisory firms to contribute to shaping those guidelines.

We question whether proxy advisory firms need to regularly consult with and consider the preferences and views of the general public on governance issues and proxy voting guidelines. The proxy advisory firms are not regulators and their relationship with their clients is governed by private contractual arrangements. In order for their business model to work and for them to serve their clients effectively, we agree that they should request input from the issuers that are the focus of their vote recommendations, but we believe that guidance suggesting proxy advisors should solicit input from the general public is overreaching.

### **Communications with clients, market participants, the media and the public**

We question whether the guidance to communicate in reports to clients “any known or potential limitations or conditions in the research and analysis used to prepare the vote recommendations” is reasonable or even possible to fulfill in practical terms. Similarly, is it practical to suggest that proxy advisors’ reports provide “identification of the information that is factual and that information that comes from analytical models and assumptions”? The proxy advisors should be free to assume that the readers of their reports are sophisticated and have the requisite expertise to make these distinctions for themselves and the Proposed Policy should not set up unreasonable expectations.

Again, proxy advisory firms are not regulators and we question the guidance to put policies in place to manage communication with respect to the media and public in general and any questions, concerns or complaints that the proxy advisory firm may receive. Such policies are good business practice for any corporation and there is no reason to single out proxy advisory firms with such expectations.

### **Should the CSA encourage proxy advisory firms to have the person designated to assist with addressing conflict of interest also assist with addressing determination of vote recommendation, development of proxy voting guidelines and communication matters?**

We suggest that the specific policies and practices that proxy advisory firms use to identify and manage risk should be left to the firms themselves and they should not have to follow external guidance on persons

involved in any particular role or the scope of one person's responsibilities. There may be reasons based on the firm's business model where it may not make sense to have the person designated to assist with addressing conflict of interest to also be involved in determining vote recommendations, for example.

**Should the CSA encourage proxy advisory firms to engage with issuers during the process of preparing vote recommendations?**

The Proposed Policy recognizes that "it is for proxy advisory firms to determine whether or not to engage with issuers when they prepare vote recommendations and if so, in what manner". Accordingly, CCGG is of the view that the CSA should not encourage proxy advisory firms to engage with issuers during the process of preparing vote recommendations but instead leave that decision up to the proxy advisors themselves as best reflects their business model and their clients' preferences.

As we also said in our Comment Letter, proxy advisors should not be required to address issuer comments in their reports. Institutional investors engage proxy advisors to obtain the benefit of their research and analysis, not to provide a forum for issuers' responses. Issuers have the proxy circular to disseminate information about their governance practices and the reasoning behind those practices and they are also free to comment publicly on proxy advisory analysis, including posting comments or corrections on their website. They are also free to reach out to shareholders to discuss any disagreement they might have with the analysis prepared by the proxy advisor.

We agree that public disclosure of the proxy advisory firms' approach to any dialogue or contact with issuers is advisable.

**Should we encourage proxy advisory firms to consider obtaining confirmation that the client has reviewed and agreed with the proxy advisory firm's proxy voting guidelines leading to vote recommendations? If so, should we encourage proxy advisory firms to consider obtaining such confirmation annually and following any amendments to the proxy advisory firm's proxy voting guidelines?**

Again, we believe that decisions as to how best to ensure that clients' views are in alignment with a proxy advisor's proxy voting guidelines and whether the client continues to support those guidelines should lie with the proxy advisor working with its clients.

***SUMMARY***

The Proposed Policy provides best practices guidance that generally mirrors the policies and practices proxy advisors in Canada already follow as a result of market forces that help to ensure their clients' interests are met, though at times the guidance goes beyond what is practical. Without such policies and practices in place, proxy advisory firms could not survive and, accordingly, regulation appears unnecessary and a voluntary code of conduct the more appropriate route. On a cost/benefit analysis, regulation that does not provide positive benefits and that will presumably use scarce resources to assess compliance, is not desirable, even if the regulation takes the form of guidance rather than being of a prescriptive nature.

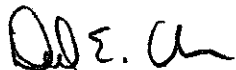
We believe that it is not the absence of such policies and practices that are the cause of the concerns expressed by issuers and their advisors about proxy advisory firms and their 'excessive' influence. Rather these concerns arise because of the nature of the proxy advisory firms' business model and the disagreements that inevitably occur at times between shareholders and management and/or directors on certain contentious issues. We suggest that the Proposed Policy will not prevent these concerns and disagreements from arising in the future and we believe issuers and their advisors may continue to be

frustrated with proxy firms and the level of influence issuers and their advisors perceive such firms to have. We encourage the CSA to not go beyond the Proposed Policy, however, and thus to resist any further suggestions to regulate proxy advisory firms.

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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 our Executive Director, Stephen Erlichman, at 416.847.0524 or [serlichman@ccgg.ca](mailto:serlichman@ccgg.ca) or our Director of Policy Development, Catherine McCall, at 416.868.3582 or [cmccall@ccgg.ca](mailto:cmccall@ccgg.ca).

Yours very truly,



Daniel E. Chornous, CFA  
Chair of the Board  
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 Pension Plan Investment Board (CPPIB)  
Canada Post Corporation Registered Pension Plan  
CIBC Asset Management  
Colleges of Applied Arts and Technology Pension Plan (CAAT)  
Connor, Clark & Lunn Investment Management  
Desjardins Global Asset Management  
Franklin Templeton Investments Corp.  
GCIC Ltd.  
Greystone Managed Investments Inc.  
Healthcare of Ontario Pension Plan (HOOPP)  
Industrial Alliance Investment Management Inc.  
Jarislowsky Fraser Limited  
Leith Wheeler Investment Counsel Ltd.  
Lincluden Investment Management  
Mackenzie Financial Corporation  
Manulife Asset Management Limited  
NAV Canada (Pension Plan)  
New Brunswick Investment Management Corporation (NBIMC)  
Northwest & Ethical Investments L.P. (NEI Investments)  
Ontario Municipal Employees Retirement Board (OMERS)  
Ontario Pension Board  
Ontario Teachers' Pension Plan (Teachers')  
OPSEU Pension Trust  
PCJ Investment Counsel Ltd.  
Public Sector Pension Investment Board (PSP Investments)  
RBC Global Asset Management Inc.  
Russell Investments Canada Limited  
Sionna Investment Managers Inc.  
Société de transport de Montréal - Régime de Retraite, Pension Funds  
Standard Life Investments Inc.  
State Street Global Advisors, Ltd. (SSgA)  
TD Asset Management Inc.  
Teachers' Retirement Allowance Fund  
The United Church of Canada (Pension Board)  
UBC Investment Management Trust Inc.  
UBS Global Asset Management (Canada) Co.  
University of Toronto Asset Management Corporation  
Workers' Compensation Board - Alberta  
York University Pension Fund