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Me Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, Tour de la Bourse
Montréal, Québec
H4Z 1G3
Fax : 514-864-6381
e-mail: consultation-en-cours@lautorite.qc.ca

John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario
M5H 3S8
Fax: 416-593-2318
e-mail: jstevenson@osc.gov.on.ca

August 10, 2012

Re: CONSULTATION PAPER 25-401: POTENTIAL REGULATION OF PROXY ADVISORY FIRMS

Dear Sir/Madam,

ISS is a leading provider of corporate governance solutions to the global financial community, including corporate governance analysis and voting recommendations for institutional investors (also referred to as proxy advisory services). More than 1,700 global clients rely on ISS' expertise in providing background research and voting recommendations to help them make more informed voting decisions. In addition, ISS offers a full suite of

corporate governance solutions to assist institutional investors in meeting their compliance needs and fulfilling their corporate governance responsibilities.

ISS has over 26 years of experience in this field, and our teams of more than 600 researchers and other professionals are located in financial centers worldwide, including in the U.S., U.K., Canada, Europe, Japan, Australia, and Singapore.

We appreciate the opportunity to provide comments on the issues raised in the CSA's Consultation Paper and we welcome the opportunity to provide the CSA and all interested market participants with clarity as to our role as a proxy advisor, our business practices and our views on possible policy options.

We hope that you will find our comments and suggestions useful, and we are available if you would like to discuss anything in further detail.

Sincerely,

Debra L. Sisti,
Vice President,
Canadian Research, ISS
debra.sisti@issgovernance.com

Martha Carter,
Managing Director,
Global Research, ISS
martha.carter@issgovernance.com

ISS Response to CSA Consultation Paper 25-401

5.3 Specific Request for Comment

General

1. Do you agree, or disagree, with each of the concerns identified in the Consultation Paper, namely:
(i) potential conflicts of interest,
(ii) perceived lack of transparency,
(iii) potential inaccuracies and limited engagement with issuers,
(iv) potentially inappropriate influence on corporate governance practices, and
(v) the extent of reliance by institutional investors on the advice of such firms?
Please explain and, if you disagree, please provide specific reasons for your position.

(i) Potential Conflicts of Interest

We do not believe that proxy advisors are either more or less inherently subject to potential conflicts of interest than are corporations or financial institutions, generally. As with all organizations, such potential conflicts of interest need to be effectively managed and mitigated by appropriate measures. A further detailed discussion of the measures taken by ISS in this regard follows in our response to question #5.

(ii) Perceived Lack of Transparency

ISS has undertaken extensive efforts to make transparency a hallmark of our company. As described in more detail further below, beginning with our rigorous, inclusive and transparent policy development process – which includes an annual survey of both institutional investor clients and corporate issuers -- continuing with public dissemination of our voting guidelines and accompanying webcasts, also including background research papers on evolving corporate governance practices, through to our draft report review process that is extended to index constituents in major markets, ISS strives to inform all market participants about the policies and corporate governance expectations that drive voting recommendations. ISS relies only on publicly available information, including disclosure documents and press releases, in the conduct of its research activities. Any information contained in ISS research that is sourced from external service providers is identified and attributed accordingly. ISS produces its research reports and voting recommendations solely for the benefit of institutional investors who subscribe to these services, although any reporting issuer may obtain a copy of the final ISS report on their upcoming meeting upon request.

(iii) Potential Inaccuracies and Limited Engagement with Issuers

ISS is committed to providing complete and accurate analysis of all voting issues in its research reports, and our Canadian staff, alone, participates in hundreds of engagements each year. Research teams employ a rigorous review process in order to mitigate the potential for errors in our research reports and voting recommendations. ISS also has instituted a draft report review process for the most widely held index constituents, in order to provide these companies with the opportunity to verify for factual content. The ISS public website has also dedicated a section on "Engaging with ISS" which provides information regarding how companies may engage with ISS Research and which sets out operational parameters with respect to the types of engagement, expected outcomes from such efforts, as well as contact information. In the event that a factual error of a material nature has been made in an analysis, ISS will promptly rectify the error and amend any vote recommendation that may be impacted by the correction.

In certain markets, ISS includes third-party data in our research reports. In the Canadian market, ISS subscribes to company and peer financial data from Standard and Poors Compustat Expressfeed service which is pulled directly into the Financials page of North American ISS research reports. Reporting issuers may respond via the draft review process that the data contained in the Financials page of ISS Canadian research reports is incorrect and differs from the financials as reported by the company. ISS reminds companies that this information is not as reported by the company, but is standardized by S&P to facilitate peer comparisons as noted at the bottom of the page in each ISS report. This complaint is the single most frequently expressed "error" indicated by companies

during the draft review process. As noted elsewhere in this comment letter, the purpose of ISS research is not to provide investor relations material on a particular company.

Generally speaking, companies that participate in the draft review process recognize the need to limit comments to issues and facts that are important to and may impact review of an issue and resulting vote recommendation, due to the very tight voting deadlines within which all parties involved in the voting process must operate. In some cases, either the draft review process or release of a final report to clients may result in extensive dialogue and issuer criticism, including that ISS has made errors in conducting its analysis and arriving at a vote recommendation. In these circumstances, ISS engages as much as time permits and when the dialogue and potential actions an issuer may take stand to benefit ISS institutional clients, as well as benefitting issuers who may wish to amend and improve corporate governance practices or make additional disclosure required to enable investors and ISS to better understand a voting proposal or underlying rationale. The decision whether to update an already issued ISS research report is made at ISS' sole discretion, taking into account all relevant factors such as the nature and materiality of any update by the company, as well as timing with respect to vote cutoff. It should be noted that, in ISS' experience, global custodian vote cutoffs can be as early as 14 days prior to the meeting date. Even one very aggressive vote cutoff indicated by a custodian on behalf of an ISS institutional client requires that ISS maintain very tight delivery deadlines for its research and vote recommendations as well.

ISS does not provide issuers with a draft review of a research report for any meeting at which contentious issues require shareholder approval. These meetings would include M&A transactions, proxy contests, "vote no" campaigns and those for which shareholder proposals have been filed. In the case of a contested meeting, ISS will endeavor to speak with both sides in order to provide a balanced and complete analysis and informed vote recommendation, time permitting. Further public disclosures by a company, or dissident or proponent shareholders will be taken into consideration by ISS provided that such disclosure is made in sufficient time to reasonably permit further review and, if warranted, an update to the latest ISS report issued in respect of a specific meeting.

Certain types of engagement by ISS may take the form of directing an issuer to ISS voting guidelines which are available at www.issgovernance.com in the Policy Gateway section. ISS will discuss the policy implications and quite often the background leading up to development of the policy in order to provide a deeper understanding of the voting policies and rationale that underpin ISS analysis and vote recommendations. Conversations of this type may take place during proxy season as requested. However, in its discussions with issuers and via the "Engaging With ISS" FAQ also provided in the Policy Gateway section of the ISS website at <http://www.issgovernance.com/policy/EngagingWithISS>, ISS encourages issuers to contact ISS outside of proxy season for policy clarification discussions.

ISS has enhanced its commitment to accuracy and engagement with the launch of the ISS Feedback Review Board (FRB) which provides a mechanism for all stakeholders (corporate issuers, institutional investors and various other market constituents) to communicate with ISS. The FRB is an ISS committee that considers comments from market constituents regarding the accuracy of research, accuracy of data, policy application and general fairness of ISS policies, research and recommendations. ISS is committed to regularly review and consider the comments and concerns submitted to the FRB. ISS believes that with the introduction of the FRB, we have set a new standard for openness to all market participants.

ISS also participates regularly in industry events including speaking events and participation on various corporate governance panels. In addition, ISS holds regularly scheduled webcasts to: provide commentary on evolving corporate governance standards and practices; disseminate updated voting policies; and facilitate institutional investor access to market experts on topics such as M&A issues or executive compensation practices. ISS also releases research white papers on high profile issues meant to provide insight into market perspective on corporate governance issues.

Given the extensive efforts made by ISS to accommodate issuer engagement and feedback, to provide extensive communications in this regard on the ISS website, and to facilitate dialogue on a number of corporate governance

issues throughout each year, ISS believes that the perception of limited engagement is misinformed with respect to ISS.

(iv) Potentially Inappropriate Influence on Corporate Governance Practices

ISS policy and voting recommendations are based on widely accepted corporate governance standards, most of which have evolved over time by means of extensive market engagement and experience. Further, ISS voting policies are significantly informed by feedback from institutional investors, issuers and market experts. As such, we would view any changing market practice potentially influenced by ISS policy and vote recommendations to be the result of ISS broadly reflecting the views of the institutional investors we serve. Where an ISS client disagrees with our policy or vote recommendation, they can (and do) vote as they see fit. ISS provides recommendations that our clients are free to adopt or not, which is entirely appropriate.

ISS Canada, formerly Fairvest Securities Corporation, has provided corporate governance research and voting recommendations, and proxy voting services to Canadian institutional investors since 1985. In the formulation of ISS' first voting policies for the Canadian market, ISS worked closely with the Pension Investment Association of Canada (PIAC) to build a set of corporate governance standards as the foundation for voting decisions made by pension funds and other institutional investors in Canada. As corporate governance issues and regulation have evolved, ISS has continued to work closely with institutional investors and institutional investor organizations to evolve corporate governance standards and voting policies based on investor expectations for appropriate corporate governance of their portfolio companies. Additionally, ISS has retained external market experts to assist in policy development on behalf of institutional investors by providing expert opinion and background reference and documentation, in areas of complex corporate governance issues where regulatory and legal factors may weigh more heavily on the direction of voting policy development.

In recent years, ISS has expended considerable effort to conduct an annual policy update process that is both rigorous and inclusive, and which is discussed in further detail in our response to question #13.

(v) Extent of Reliance by Institutional Investors

As indicated in the previous sections, ISS' benchmark policies are based on generally accepted principles of good corporate governance taking into account national and international corporate governance best practice standards as well as investor and other stakeholder views. ISS is committed to the transparent and inclusive policy development process currently implemented, and extensive additional market outreach activities that we undertake to obtain the broadest possible market feedback in developing our institutional proxy voting policies.

As many investors can be expected to share a general approach to assessing corporate governance practices, it is perhaps not surprising that a correlation exists between ISS (and possibly other proxy advisors') recommendations and shareholder voting outcomes. However, this does not prove causality, nor are those correlations consistent. In our view, it is more logical to interpret broad correlation as indicating that ISS policies, analyses and recommendations are based on principles and approaches which are shared by many investors (whether or not they are ISS clients who receive ISS research and recommendations).

ISS recognizes that there are concerns (primarily among corporate issuers, but often also widely repeated by other commentators) about the perceived influence of proxy advisors in general, and ISS in particular, on voting at general meetings. We do not track the extent to which our clients follow (or not) ISS voting recommendations, but we believe that it is a misconception, albeit an often repeated one, that ISS' clients blindly follow ISS' recommendations.

Part of this misconception stems from a mistaken view that ISS reflects a single point of view on each proxy issue. It is our experience that investors are not of a single mind with respect to corporate governance issues. ISS implements a variety of proxy voting policies reflecting the differing views of our varied client base. In addition to

our benchmark policy guidelines (or “house” view), ISS offers research and vote recommendations under “specialty” guidelines such as our “Socially Responsible Investment” and “faith based” policies. More significantly, ISS manages and applies over 400 custom policies on behalf of institutions representing over 60% of the aggregate assets held by all of our clients. These customized voting policies reflect clients’ unique corporate governance philosophies. As a result, the vote recommendations issued under these policies often differ from those issued under our benchmark policies.

ISS provides research and voting recommendations that reflect the policies that clients have selected – whether benchmark or customized. The ultimate voting decision for each resolution at a company meeting remains the responsibility of the client, as we believe it should, in keeping with their fiduciary responsibilities.

It is important to recognize that ISS’ clients use our proxy research and voting recommendations in a variety of ways. ISS’ research and vote recommendations are just one of many resources that clients may use in arriving at their voting decisions. Many institutional investors have internal research teams that conduct their own proprietary research and use ISS research to supplement their own work. Some clients use ISS research as a screening tool to identify non-routine meetings or proposals. A number of ISS clients use the services of two or more proxy advisory firms. Many clients who subscribe to our benchmark policy recommendations, review and consider our research, but ultimately decide to vote differently from ISS’ recommendations – instead voting in line with their own investment and governance philosophy and company engagement activities in any particular situation.

It is unclear to what extent investors vote consistently with the recommendations of proxy advisory firms, particularly since investors use vote recommendations differently and such use is not easily monitored or quantified. Additionally, the same voting outcomes may be determined by any number of underlying reasons, and investors’ reasons may or may not be different to those highlighted by proxy advisors. Such complexity does not stop some commentators from asserting that a significant percentage of votes are “controlled by ISS”, however. These assertions have no factual basis, but have been repeated by other commentators referencing the initial statement as fact.

There is, however, empirical evidence to the contrary, albeit from the U.S. In a comment letter on an SEC Concept Release, University of Pennsylvania Law School Professor Jill Fisch addresses this issue through quantitative analysis. Professor Fisch cites a recent study that she conducted, along with academic colleagues from New York University. In their paper, *The Power of Proxy Advisors: Myth or Reality?*¹, the team analyzed the effect of proxy advisor recommendations on voting outcomes in US uncontested director elections and concluded that, while ISS is the most influential of the four major firms, media reports overstate the extent of its influence by failing to control for the underlying firm and director-specific factors that influence voting outcomes. Controlling for these factors, Professor Fisch and her colleagues estimate that an ISS recommendation shifts 6 to 10 percent of shareholder votes in the US. The paper suggests that a major component of this influence may stem from ISS’ role as information agent. This assessment is consistent with our experience of how our clients actually use our governance research and vote recommendations.

While we concur that there is limited information available about institutional investors’ reliance on the services provided by proxy advisory firms, the CSA Consultation Paper also asks whether institutional investors may have concerns about the activities of proxy advisors but are limited in their options due to the lack of competition in this industry or for other reasons. ISS is aware of several competitors in the Canadian market specifically. Glass Lewis, as the CSA has noted, also provides proxy advisory services to Canadian institutional investors. As well, there are a number of what might be regarded as niche service providers in the Canadian market, including the Shareholder Association for Research and Education (SHARE), Jantzi-Sustainalytics, and Groupe Investissement Responsable, all of whom provide research and voting capability. In addition, the Canadian Coalition for Good Governance

¹ See: http://papers.ssrn.com/sol3papers.cfm?abstract_id=1694535

provides proxy research papers and engagement services on behalf of its institutional members; and there are other service providers that compete in one or more areas of proxy research and voting services such as Broadridge and Hermes EOS. We do not therefore believe that any institutional investor in Canada is obligated or limited to subscribing to ISS services for any reason other than that they value the quality of the products and services provided by ISS.

General questions 2, 3 and 4 have been combined in the following response.

2. Are there other material concerns with proxy advisory firms that have not been identified?
3. Are there specific gaps in the current practices of proxy advisory firms which justify regulatory intervention: Is there a concern that future gaps could be created as a result of new entrants or changes in business or other practices?
4. Do you believe that the activities of proxy advisory firms should be regulated in some respects and, if so, why and how?

ISS has seen no evidence of a market failure arising from the proxy advisor industry or from the use of proxy advisors that might warrant regulatory intervention. On the contrary, we believe the use of proxy advisors positively assists institutional investors in carrying out their fiduciary obligations and stewardship responsibilities to vote in an informed and consistent manner across their portfolios. In fact, ISS aims to conduct independent research to identify potential concerns related to corporate governance and/or transactional proposals where we believe the risk to our clients warrants a vote against a proposal despite significant corporate issuer influence on vote outcomes through proxy solicitation and other avenues.

ISS policies, analysis and recommendations are based on widely accepted principles of good corporate governance. Additionally, we are held to very high standards of accountability by our clients, who remain responsible for their final voting decisions. Our research process is highly transparent and the time devoted by ISS to proactive engagement with issuers, both in policy development and with respect to specific governance issues at individual companies, is extensive. Ultimately, the research process conducted by ISS is designed to deliver analysis and recommendations to our clients based on principles and policies that they endorse as investors, not to provide a platform for issuers' views except as we may consider them relevant to our analysis.

ISS provides voting recommendations, but the ultimate voting decision for each resolution at a company meeting remains the responsibility of the client, as we believe it should, in keeping with their fiduciary responsibilities. As already noted, for a significant portion of our client base, particularly our biggest clients who tend to have the broadest and largest holdings, we provide a custom analysis service which delivers voting recommendations based on the client's bespoke proxy voting policies developed by, or in conjunction with, each client rather than on ISS benchmark policies.

The provision of our proxy advisory and voting services is subject to the terms of a direct contractual relationship with our clients, with contractual obligations governing confidentiality, delivery times and service levels. Our first duty is to our clients – to ensure that they are given the information, insight and time to execute their votes in an informed and effective manner. Any proposed regulated practice which were to conflict with this duty, or otherwise seek to prioritize the interests of issuers over our clients would be incompatible with our contractual obligations and could restrict our clients' ability to receive and use independent research and information they consider relevant to their responsibilities as shareholders.

For the reasons stated here, ISS does not believe the activities of proxy advisory firms should be regulated. ISS believes that market forces, in particular institutional investors themselves, are efficient in dealing with material concerns under commercial relationships with service providers.

Potential Conflicts of Interest

5. To what extent do you consider proxy advisory firms to:
i) be subject to conflicts of interest in practice?
ii) already have in place appropriate conflict mitigation measures?
iii) be sufficiently transparent regarding conflicts of interests they may face?

5) i) We do not believe that proxy advisors are either more or less inherently subject to potential conflicts of interest than are companies or investors. Like all organizations, potential conflicts of interest need to be effectively managed and mitigated by appropriate measures.

Given their interrelated nature, we have responded to Questions 5 ii) and iii) in aggregate:

Because of the breadth of our client base and the work that we do, ISS understands and takes seriously the potential for real or perceived conflicts of interest which might impact the integrity of the research and services we provide to our clients and/or ISS' ability to fulfill its role in the dialogue between issuers and their shareholders. We therefore make a comprehensive due diligence package, including regarding conflicts of interest, available on our public website² as well as making all relevant information available to our clients.

In general we have identified three types of potential conflicts:

- The board of directors of our parent company, MSCI Inc., could seek to influence the formation of ISS policies;
- Institutional clients could seek to influence the advice given to other institutional clients (for example regarding advice on their parent company's general meeting or regarding shareholder resolutions filed by clients);
- Corporate clients could seek to influence the advice given to institutional clients.

Concerning the first potential conflict, MSCI has a policy³ on the mitigation of potential conflicts of interest related to the MSCI board of directors. As noted in our compliance package: "The MSCI Inc. Board of Directors has formally adopted resolutions stating: (i) that the formulation, development and application of ISS' proxy voting policies (including, without limitation, the establishment of voting standards), proxy analyses and vote recommendations is and shall remain the sole responsibility of ISS (and its management and employees) and within the control of ISS (and its management and employees and, where appropriate, the management and employees residing within MSCI Inc. or any of its subsidiaries) at all times and shall be performed in accordance with the standards set forth in the Code of Ethics; (ii) that the non-executive members of the Board of Directors shall have no role in formulating, developing or implementing ISS' proxy voting policies, proxy analyses and/or vote recommendations; (iii) that the non-executive members of the MSCI Board of Directors shall not be informed of the contents of any ISS proxy analyses or vote recommendations prior to their publication or dissemination."

Concerning the second potential conflict, we reiterate that at its core, ISS is a policy-based organization and ISS uses a series of published benchmark voting policies that provide a very practical check and balance to ensure the integrity and independence of ISS' research and vote recommendations. ISS research analysts follow these comprehensive policy guidelines when writing research reports and making vote recommendations to our clients. ISS also conducts regular Statement on Standards for Attestation Engagements no. 16 (SSAE 16) audits to ensure compliance with our internal control processes.

² Please see: <http://www.issgovernance.com/files/ISSDueDiligenceCompliancePackage20110413.pdf>; also see <http://www.issgovernance.com/practices>

³ Please see: http://www.issgovernance.com/files/MSCI_ISS2010.06BoardConflictsPolicy.pdf

The third potential conflict is between ISS' core business of analyzing the general meeting agendas of corporate issuers and making vote recommendations to institutional investors, and the work of an ISS subsidiary, ISS Corporate Services, Inc. (referred to as "ICS"), which sells Governance Risk Indicators (GRId) analytics and other factual market reference data; voting analytics, educational resources to help companies better understand and address corporate governance matters; our published research on industry peers or other companies of interest; and access to our compensation benchmarking tool (U.S. model). We believe that ICS' work with corporate issuers helps companies enhance their governance practices, which ultimately benefits all shareholders. At the same time, we understand the potential for conflict that arises when ICS provides corporate governance advice to an issuer and ISS subsequently makes vote recommendations on the proposals at that same issuer's general meeting of shareholders, and we therefore actively manage this potential conflict.

We manage this through a combination of disclosure to our institutional clients, the consistent and transparent application of our voting policies, a robust compliance program and implementation of a strict "firewall" between ISS research and ICS. For further details on the management of this area, please see the relevant section below

Finally, the law firm of Sullivan & Cromwell LLP has assessed our conflict policies and procedures and found them to be appropriate and effective⁴.

ISS' Policy-Based Approach Provides Consistency of Application

As previously noted, at its core, ISS is a policy-based organization and ISS' use of a series of published benchmark voting policies provides a very practical and transparent check and balance that ensures the integrity and independence of ISS' research and vote recommendations. Our benchmark policies are subject to annual review and update, and we undertake a highly consultative process, including a policy survey, review and consultation with institutional investor clients, and a period of public consultation when all stakeholders including corporate issuers are invited to comment.

Our policy-based approach also provides for a transparent and consistent methodology to evaluate shareholder proposals. ISS does not provide any consultative or advisory service to our clients or other share-holders in the development of, or solicitation of support for, shareholder proposals.

ISS Compliance Program: Code of Ethics, Firewall and Training

While the policy framework is one aspect of our practical checks and balances, we have proactively developed and implemented a comprehensive compliance program that provides guidelines and specific policies and procedures that help us conduct our business with the highest degree of integrity and maintain sensitivity to the ethical aspects of our work.

As part of its compliance program, ISS has adopted a Code of Ethics that prescribes standards of conduct that the company's employees must follow in carrying out their responsibilities. At its core, the Code of Ethics obligates ISS and its employees to carry out their duties solely in the best interests of clients and free from any compromising influences and loyalties. The Code also contains restrictions on personal trading designed to prevent ISS employees from improperly trading on, or benefiting from, inside information and/or ISS' voting recommendations. The Code emphasizes the requirement that all research for clients be rendered independently of the personal interests of any of ISS' employees. ISS continuously monitors and tests employee trading activity to ensure adherence to these restrictions. Annual training and a yearly affirmation of the Code of Ethics by all employees are other elements of the compliance program.

The ISS firewall includes the physical and functional separation between ICS and the rest of the ISS organization, with a particular focus on the separation of ICS from the ISS proxy research function. For further details about

⁴ Available at: http://www.issgovernance.com/files/ISS_Corporate_Services_Conflict_Policy_Review_Project.pdf

how ISS comprehensively manages the potential conflicts with regard to the nature and scope of ICS' corporate business, please see "The Nature and Scope of ICS' Corporate Business" below. A key goal of the ISS firewall is to protect against the ISS proxy research team knowing the identity of ICS' clients. Enabling the research team to work without knowing the identity of ICS' clients is part of our approach to ensuring the objectivity and independence of ISS' research process and vote recommendations. ICS clients are also told explicitly that ISS will not give preferential treatment to, and is under no obligation to support any proxy proposal of an ICS client and that ISS' proxy research team prepares analyses and vote recommendations independently of, and with no involvement from, ICS.

ISS also maintains a robust training and compliance program, which includes quarterly tests of the ICS/ISS fire-wall, new hire orientation, annual training and certification, and review of certain marketing materials and disclosures. There is a whistleblower hotline available to both ICS and ISS staff for reporting potential issues of concern.

The Nature and Scope of ICS' Corporate Business

There are two areas for potential conflict that are commonly cited with respect to the ICS business at ISS. The first is the potential 'pay to play' conflict: the potential that a corporate issuer client purchasing advisory services from the ICS business may expect to receive a favorable vote recommendation and hence that there may be pressure on the ISS research analysts to provide that favorable recommendation. The second is the 'economic' conflict: the potential that the value of revenues accruing to the ICS business from a particular corporate issuer are of sufficient significance to the financial performance of ISS as a whole as to pressure the ISS research analysts to make favorable recommendations regarding the issuer's shareholder meeting in order to retain that revenue.

On the "pay to play" potential conflict, we would like to clarify that ICS does not provide services to corporate clients that can be classified as 'consulting services' of a nature that could give rise to expectations or conflicts impacting the integrity of our proxy voting recommendations. On the "economic" potential conflict, the ICS business does not in aggregate represent revenues that could realistically be characterized as presenting an 'economic conflict' relative to our core institutional proxy advisory and voting business.

Clients of our ICS business can purchase our Governance Risk Indicators (GRId) analytics and other factual market reference data; voting analytics; educational resources to help them better understand and address corporate governance matters (including membership in our Governance Exchange forum for all governance stakeholders); our published research on industry peers or other companies of interest; and access to our compensation benchmarking tool (U.S. model). In summary, these services provide access to data, market knowledge, and market benchmarks. They do not include any kind of consulting overlay.

As for the potential 'economic' conflict, the ICS business revenues represent less than 0.5% of the revenues from proxy research and voting services received by the ISS business from institutional investors located in Canada. Notwithstanding this, even in the U.S. we do not believe there is an economic incentive to risk favoring our ICS business at the expense of our institutional proxy business, which is much larger and critical to our brand.

Disclosure to Clients Regarding Potential Conflicts

ISS provides its institutional investor clients with extensive information to ensure that they are fully informed of potential conflicts and the steps that ISS has taken to address them. In addition, many of ISS' clients conduct their own due diligence regarding the way ISS implements the procedures governing conflicts, and perform audits and visits to satisfy themselves that ISS' rules governing conflicts are robust and effectively adhered to.

ISS is transparent about its ICS business and the entire business is described in detail on our public website. Additionally, ISS' standard institutional client contract contains disclosures regarding ICS and its work with corporate issuers, and each proxy research report issued by ISS contains a legend indicating that the subject of the analysis or report may be a client of ICS, and reminds ISS' institutional clients of how they can enquire about any issuer's use of ICS products and services.

We believe that these disclosures are an effective and transparent way of disclosing to our institutional investor clients without compromising the effectiveness of the ISS firewall. The process ensures reliable disclosure to clients whilst also providing that the identity of an ICS client is not available to research analysts as they undertake research and vote recommendations.

6. If you are of the view that there are conflicts of interest within proxy advisory firms that have not been appropriately mitigated, which of these are the most serious in terms of the potential (negative) impact on development of their voting recommendations and why?

We believe that ISS' potential conflicts of interest are appropriately mitigated and we are not aware of any instance where a conflict of interest has had any impact on development of voting recommendations being given by ISS.

The three main areas of potential conflict of interest for ISS and the mitigation that ISS has in place for them are detailed in our response to question #5 above.

7. Should we propose an amendment to NI 51-102 to require reporting issuers to disclose consulting services from proxy advisors in their proxy circular? Or would such disclosure undermine the existing controls and procedures (i.e., "ethical wall") in place which currently may prevent proxy advisory research firm staff who review an issuer's disclosure from being made aware of the identity of their firm's consulting clients?

An amendment requiring issuers to disclose consulting services from proxy advisors in their proxy circulars would circumvent the firewalls in place to insure the integrity of voting recommendations and would undermine a proxy advisor's ability to sufficiently mitigate potential conflicts. Both disclosure and the firewall are essential in preserving the integrity of the research provided and allowing clients to use that research most effectively.

ISS believes that research recipients should be aware of both the potential conflict with the ICS business as well as the measures in place to properly mitigate them. While this requires disclosure of ICS clients to ISS' research clients, it also requires that research analysts remain isolated from such information. To this end, ISS requires that ISS client requests for ICS client lists be directed to the compliance department, which responds to the requests directly. This eliminates the need for contact between ISS and ICS regarding corporate client names and addresses the need for disclosure to ISS clients. These measures, in addition to those described in responses 5 and 6, achieve the goals of ensuring the independence of ISS research and being as transparent as possible with clients so that they can make a fully informed analysis of ISS' recommendations.

This is in contrast with what question #7's proposal would achieve, which is simply detailed disclosure to the market in general. While there may be instances in the financial regulatory scheme where market disclosure is desirable, here, market disclosure as proposed does not add any benefit to ISS research recipients. Instead, it would undermine the integrity of the research by allowing research analysts to become aware of whether the subjects of their analysis are ICS clients. ISS firmly believes that broad market disclosure of the identity of ICS clients would prevent the mitigation of the potential conflicts previously identified. ISS does believe, however, that it is necessary to inform ISS clients in every research report that the possibility of a conflict exists. Such a notice is provided by ISS on all of its proxy research, along with instructions on how to obtain a list of ICS clients. In this way, each client of ISS research can determine if the company that is the subject of the research is also a corporate client of ICS and can evaluate for itself the integrity and independence of the ISS research.

Additionally, it should be noted that it is only the clients of ISS proxy research who have any reason to know the potential conflicts with ICS. Investors who are not clients of ISS research derive no benefit from knowing that an issuer is an ICS client. A rule requiring broad public disclosure would be unnecessarily over inclusive while undermining the safeguards described above by revealing the identity of ICS clients to ISS research analysts.

Perceived lack of transparency

8. Could disclosure of underlying methodologies and analysis provide beneficial information to the market or would the commercial cost of doing so be too significant?

As the CSA has pointed out in the Consultation Paper, the services provided by ISS to its institutional clients are based on a commercial relationship. ISS has developed proprietary methodologies and models to facilitate quantitative analysis of certain governance issues, including but not limited to, for example compensation related issues. Complex voting issues, in particular, sometimes require subjective qualitative analyst review. ISS clients may value the analytical insight and experience of our research staff as much as the quantitative aspects of our research. In any case, both are competencies that are developed by ISS at considerable cost and effort to enhance the value of our products and services to our clients. We would therefore view it as inappropriate and competitively harmful if ISS were required to divulge its proprietary methodologies publicly, as the CSA has suggested for consideration. ISS clients, who consist of institutional investors capable of making sophisticated investment decisions, are also capable of evaluating the quality and effectiveness of the analytical methods employed by ISS.

Issuer Engagement

Questions 9, 10, 11 and 12 have been combined in the following response.

9. To what extent could there be an improvement in the dialogue with issuers during the vote recommendation process?

10. During proxy season, is it appropriate for a proxy advisory firm to engage with issuers in all circumstances or are there legitimate business and policy reasons why it should not be required to do so? Are there certain special types of situations where it is more important that issuers are able to engage with proxy advisory firms?

11. If a proxy advisory firm, as a matter of policy, believes that there are certain circumstances where it is not appropriate for it to give issuers an opportunity to review its reports, would it be sufficient to only require in these circumstances that the underlying rationale for such policy be disclosed? Please explain. Or, alternatively should proxy advisory firms be required to provide issuers with an opportunity to review their reports in all circumstances?

12. Should we prescribe the details of the processes that proxy advisory firms implement to engage with issuers? If so, what do you suggest the requirements should be?

ISS is committed to dialogue with issuers to gain the greatest possible insight for our clients. We make our approach to such dialogue public. As mentioned in section 1(iii) of this comment letter, our global engagement policy and more information on our engagement practices can be found at <http://www.issgovernance.com/policy/EngagingWithISS>.

ISS participates in engagement activities throughout the year in addition to the communications that may occur during the meeting research process with the aim of delivering to our clients a final research report that contains relevant and accurate information for a particular meeting. Our engagement goal is constructive and informative dialogue between ISS and issuer companies. ISS will discuss current voting policies applied in the Canadian market, providing background rationale and examples. We will provide insight into the general concerns expressed by institutional investors related to certain corporate governance practices, explain the diverse nature of our client base and take the opportunity to remind issuers that our client base is global and therefore votes on proposed agenda items for any particular meeting may reflect the voting policies of institutional investors in other global markets where stricter corporate governance expectations may have become the standard.

Also as mentioned earlier in this letter, ISS participates in industry panels and other speaking engagements, often sponsored by issuer advisors or industry organizations. Our belief is that these opportunities promote constructive dialogue that provides insights into evolving corporate governance practices of reporting issuers and evolving corporate governance expectations of institutional investors. ISS is aware that the Canadian market comprises a large number of small companies, some of which may grow faster than their corporate governance resources and therefore there is a role for ISS to play in communicating even minimum acceptable corporate governance standards on behalf of our clients.

During the draft review process implemented for S&P/TSX Composite issuers, we generally aim to provide these Canadian companies with a 24-48 hour review period prior to publication of our research report in order to give them the opportunity for fact checking and the correction of any material factual errors. We make good faith efforts to provide this review window; however, in circumstances when voting deadlines, client cutoff dates and high meeting volumes in the peak of proxy season mean that a 24 hour window for issuer review would result in late delivery of a report to our clients, our obligations to our clients take precedence. The delivery of reports and vote recommendations to our clients is extremely time-critical, and our respect for this has the highest priority. We have, however, tried whenever possible to accommodate issuer concern with these quick turnaround times by giving advance notice in the Canadian market when the analyst is finishing a report and can provide an indication of timing for draft review in advance so that an issuer can be prepared to deal with the short timeframe. Again, we make good faith efforts to do so, time and circumstances permitting.

As indicated in our response to question 1 (iii), ISS will not permit a draft review of any controversial or contentious agenda item covered by its reports; however upon request an issuer may receive the final report once it has been released to our clients. Aside from concerns expressed by certain institutional clients that they believe the potential for issuer influence and pressure should be prevented and issuer communication with ISS analysts strictly limited during the completion of meeting research and vote recommendations, in order to ensure that institutional clients receive independent-minded voting recommendations, ISS believes the contentious nature of certain types of meetings and agenda items present the potential for non-productive communications that may negatively impact our ability to deliver voting recommendations in a timely manner. This concern may be compounded by the complications of the proxy voting system which seem to increase in contentious voting situations.

ISS believes that regulation prescribing increased activity or specific timing with respect to issuer engagement and/or draft reviews would require additional resources to manage at a significant cost that would ultimately have to be borne by our institutional clients, as corporate issuers do not pay for ISS research services or the resources that they access during these processes.

Potentially inappropriate influence on corporate governance practices

13. To what extent should there be a more fair and transparent dialogue between proxy advisors and market participants on the development of voting policies and guidelines? Is it sufficient for proxy advisors to address governance matters by soliciting comments from their clients?

ISS undertakes extensive market outreach in developing and finalizing voting policies. This effort ramps up post proxy season. In addition to many informal discussions with a variety of market constituents, ISS actively engages with institutional clients, the academic community and industry experts worldwide to gather input on corporate governance issues and on ISS' proxy voting policies and methodologies.

Led by the ISS Policy Board, the firm deploys a bottom-up approach to policy formulation that incorporates ISS' own expertise combined with feedback from a diverse range of market participants through multiple channels beginning with an annual global policy survey. By means of roundtables, panel discussions and conference calls or webcasts bringing in expertise of the broader governance community including regulators, ISS facilitates the

exchange of information and views on issues of high interest and concern that influence policy development as well. These discussion forums may also follow changes in regulatory rules or disclosure requirements that may drive policy updates. The largest part of this market outreach effort takes the form of discussions with our institutional clients to obtain their views, criticisms, and other feedback on corporate governance generally, and on ISS policy development specifically. The feedback related to corporate governance generally is to a large extent informed by their experience in recent proxy seasons and is an opportunity for institutions to raise concerns with respect to current issuer practices, proposed regulatory changes, and ISS services.

With respect to ISS policy development specifically, ISS clients are asked to weigh in on a number of corporate governance issues or practices where either they or ISS analysts have noted the need for potential clarification or change, and where potential policy updates are being considered by ISS or encouraged by ISS clients. Through this process, ISS policy development is directly informed by our clients over the course of several months post proxy season before policy updates are finalized. ISS views this direct input by its institutional investor clients into voting policy development as entirely appropriate and in keeping with institutional investor responsibilities.

The ISS Policy Board uses this input to develop its draft policy updates on emerging governance issues each year. Before finalizing these updates, ISS publishes draft updates for an open review and comment period. All comments received during the comment period are posted publicly on ISS' Policy Gateway at <http://www.issgovernance.com/policy> in order to provide the highest level of transparency into the market's feedback. ISS reviews all market feedback received and if deemed appropriate may make further revisions to policy updates to ensure that they are appropriate, clear, balanced, well-reasoned, and compliant with any regulatory or legal requirements.

Proposed regulatory responses and framework(s)

- 14. Do you think a securities regulatory response is warranted in connection with each of the concerns identified above? Please explain why or why not.**
- 15. Do you agree with the suggested securities regulatory responses to each of the concerns raised? If not, what alternatives would you suggest?**
- 16. Do you agree or disagree with the requirements and disclosure framework set out in section 5.2.1 to address the concerns identified? If not, please indicate why. Do you agree or disagree with our analysis of these frameworks? Do you have suggestions for an alternative regulatory framework?**
- 17. Are you of the view that we should prescribe requirements in addition to or instead of those identified above for proxy advisory firms?**

Please refer to our response to questions 28, 29, 30 and 31 below.

Additional questions for proxy advisory firms

- 28. What are your views with respect to the concerns identified and with any of the possible regulatory approaches to these concerns?**
- 29. In connection with possible regulatory approaches, do you have concerns about disclosure of confidential or proprietary information? Please explain.**
- 30. What impact could the preferred securities regulatory framework (requirements and disclosure) have on your operations? Please provide details and, where appropriate, propose an alternate approach.**
- 31. In addition to your responses to the questions posed, we also welcome any additional information and data you can provide to inform our continued review and analysis of the issues identified in the Consultation Paper.**

ISS does not believe that a securities regulatory response is warranted in the absence of evidence of a market failure arising from the proxy advisory industry or from the use of proxy advisors. On the contrary, we believe that the use of proxy advisors positively assists institutional investors in carrying out their fiduciary obligations and stewardship responsibilities to vote in an informed manner across their portfolios.

ISS policies, analysis and recommendations are based on generally accepted principles of good corporate governance. Additionally, we are held to very high standards of accountability by our clients, who remain responsible for their voting decisions.

Our policy development and research process is highly transparent and the time devoted by ISS to proactive engagement with issuers and to accommodate engagement by issuers, both in policy development and with respect to specific governance issues at individual companies, is extensive. However we do not believe that this should be mandated – ultimately the research process is to deliver analysis and recommendations to our institutional clients based on principles and policies that they endorse as investors, not to provide a platform for issuers' views except as we consider them relevant to our analysis. As well, ISS believes that regulation prescribing increased activity or specific timing with respect to issuer engagement and/or draft reviews would require significant additional resources to manage at a cost that would ultimately have to be borne by our institutional clients.

ISS provides voting recommendations, but the ultimate voting decision for each resolution at a company meeting remains the responsibility of the client, as we believe it should, in keeping with their fiduciary responsibilities. For a significant portion of our client base, particularly our biggest clients who tend to have the broadest and largest holdings, we provide a custom analysis service through which the voting recommendations for those clients are based on bespoke proxy voting policies developed by, or in conjunction with, each client rather than on ISS benchmark policies. There is no 'one size fits all' approach.

ISS maintains rigorous compliance processes to ensure the firm has clear separation between groups that may appear to have conflicts – by physical separation of employees, independent staffing to prevent the sharing of data or information, technical barriers to restrict access to and exchange of certain data and information, training of employees, and periodic auditing of our policies and procedures. ISS is committed to providing our clients with the highest level of transparency into our business operations and quality control processes and thus each year we undergo an independent audit with an external third party audit firm. We make our audit report available to all clients for review and we invite clients to perform their own on-site audits, which many have undertaken in the course of their due diligence.

The provision of our proxy advisory and voting services is subject to the terms of a direct contractual relationship with our clients, with contractual obligations governing confidentiality, delivery times and service levels. Our first duty is to our clients – to ensure that they are given the information, insight and time to execute their votes in an informed and effective manner. Any proposed regulated practice which were to conflict with this duty, or otherwise seek to prioritize the interests of issuers over our clients would be incompatible with our contractual obligations and could restrict our clients' ability to receive and use independent research and information they consider relevant to their responsibilities as shareholders.

ISS has developed proprietary methodologies and models to facilitate quantitative analysis of certain governance issues, at considerable cost and effort to enhance the value of our products and services to our clients. We would therefore view it as inappropriate and competitively harmful if ISS were required to divulge our proprietary methodologies publicly, as the CSA has suggested for consideration. Institutional investors are best positioned to evaluate the quantitative or qualitative methods and analysis that they receive as paying subscribers to ISS services, as well as the overall quality of the products and services delivered by ISS. Therefore, ISS believes that market forces rather than regulation are the most appropriate and effective oversight mechanism for the proxy advisory industry.