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Ms. Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090

Dear Ms. Murphy:

**Re: Release Nos. 34-62495; IA-3052; IC-29340; File No. S7-14-10, Concept Release on the U.S. Proxy System**

Davies Ward Phillips & Vineberg LLP ("Davies") welcomes the opportunity to provide the Securities and Exchange Commission (the "Commission") with comments, as requested, on its Concept Release on the U.S. Proxy System (the "Concept Release").

Davies is an integrated firm of more than 240 lawyers with offices in Toronto, Montreal and New York. We act for a wide range of leading industrial and commercial companies and financial institutions, both public and private, in Canada, the United States and abroad. Many are affected by the current rules and regulations of the Commission that address various aspects of the U.S. proxy system.

As you know, the Canadian and U.S. proxy voting systems are very similar. They are both based on the indirect holding system in which a depository is most often the registered shareholder, holding shares on behalf of intermediaries who in turn hold on behalf of their clients. A Canadian affiliate of Broadridge Financial Solutions, Inc. acts as proxy agents for virtually all Canadian intermediaries. Canada adopted the OBO/NOBO system in 1988 and while some distinctions from the U.S. system have developed, the two systems remain very similar. The similarities between the two systems should allow us to work together to find solutions to the current problems.

Davies has prepared a paper describing the Canadian proxy voting system and the problems that compromise the quality of the shareholder vote in Canada. We are releasing that paper as a discussion paper, which we will update periodically to reflect comments as we receive them from others who are interested in the proxy voting system in Canada. We hope you will find this paper useful. It deals with most of the issues raised in the Concept Paper. It is available at [www.shareholdervoting.com](http://www.shareholdervoting.com) or by emailing me at [chansell@dwpv.com](mailto:chansell@dwpv.com).

We have set out the context in which the paper was written, together with some excerpts from the paper to give you an overview of the issues we address and our conclusion.

### *Reasons for the Paper*

As a firm, we have extensive experience with shareholder meetings. Some of these meetings are routine, others involve proxy battles, the approval of important transactions or votes on governance matters such as shareholder rights plans or stock options plans. Together with our clients, we have encountered a variety of obstacles in making sure that votes are cast and counted at the meeting in question. We know others have had similar experiences. As a result, we have become concerned with the quality of the shareholder vote in Canada. In our view, a high quality vote is one that accurately reflects the informed view of investors who wished to vote at the meeting in question.

Because the results of shareholder meetings are important to our clients and to the capital markets generally, we decided as a firm to devote the time and resources necessary to understand the issues that might compromise the integrity of those results.<sup>1</sup> Our intention was to then engage in discussions with others who share our interest in the quality of the shareholder vote with a view to improving the system.

The first thing we discovered was that very few people understand how the proxy voting system works from end to end. Recognizing that without a common understanding of the system itself, the capital markets community would not be in a position to identify and resolve the problems that prevent that system from being effective, we took a step back. We decided to first work to bring together the information necessary to establish that common understanding.

Following 16 months of research and discussions, we have produced a paper that describes the history, mechanics and policy issues relevant to the proxy voting system in Canada. For aspects of the system in which we are not directly involved, we sought the assistance of organizations integral to the operation of the system. With very few exceptions, those organizations not only answered our questions, but provided us with further information that they felt would be relevant to this project. To the extent that interested parties have further information that would improve the discussion in this paper, we hope that they will share it with us so that everyone can benefit from the common base of knowledge.

We are releasing the paper initially as a discussion paper and have asked for comment from others with an interest in the proxy voting system. We have offered some suggestions for next steps on which we also invite comment. Based on the further comments we receive, we will post updated versions from time to time and will ultimately produce a final paper.

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<sup>1</sup> Researching and writing this paper was a project undertaken independently by Davies Ward Phillips & Vineberg LLP and not on behalf of any client or other party.

### *Elements of an Effective Proxy Voting System*

In our view, an effective proxy voting system must satisfy at least the following five criteria:

- investors must be in a position to make an informed decision about how to vote or how to direct that their votes be exercised and must therefore have adequate time to review the proxy materials;
- investors must be able to cast their votes or provide voting instructions in accordance with rules that are clearly explained, impartially applied and practical for investors to follow;
- if an investor casts a vote or provides voting instructions in accordance with the established rules, that vote must be given its full weight at the shareholder meeting in question;
- votes attached to the securities of an issuer should be cast by those investors who hold the economic interest associated with those securities; and
- there must be sufficient transparency in the voting system so that both issuers and investors are confident that the system works.

Issues with design and operation of the proxy voting system in Canada create a reasonable apprehension that the system may not consistently meet these criteria. These issues, combined with public examples of the system failing in each of these areas, have compromised confidence in the effectiveness of the proxy voting system among many of its stakeholders.

### *Features of the Canadian Proxy Voting System*

The following is a summary of the features of the proxy voting system that are relevant to the discussion in this paper:

- ***Investors Hold Their Interest Indirectly*** – Most investors (both retail and institutional) hold their interest in shares indirectly, through one or more intermediaries. The issuer therefore has no direct relationship with most of its investors.
- ***Shares Held in Fungible Bulk*** – Each intermediary holds shares in "fungible bulk". "Fungible" means that each share is identical and so it does not matter to the investor whether it has invested in one share as opposed to another share. "Bulk" means that the intermediary has a position in the aggregate of all the shares in which it holds an interest for its clients.
- ***OBO Status*** – Investors have the right under Canadian securities law to elect *not* to allow their intermediaries to disclose their identity to the issuer. The investors who do so are referred to as "OBOs" (Objecting Beneficial Owners). Those who allow their

intermediaries to disclose their identity to the issuer are "NOBOs" (Non-Objecting Beneficial Owners).

- ***Unreconciled Records*** – The records submitted by intermediaries in connection with shareholder meetings are often not reconciled to eliminate positions relating to shares that have been loaned or should otherwise not be available to be voted.
- ***System is Operated by Third-Party Service Providers*** – The machinery of the proxy voting system is operated by third-party service providers. Transfer agents and proxy solicitors act on behalf of issuers, proxy agents act on behalf of intermediaries and proxy advisors act on behalf of investors.
- ***System is Complicated*** – The proxy voting system involves a number of different parties and at least as many different systems and data bases. It is susceptible to administrative and technological errors.
- ***System is Not Transparent*** – How communications flow between issuers and investors is not visible to any of them. The lack of transparency means that when an error occurs, it will often not be discovered – and therefore will not be rectified.
- ***Vote Confirmation Not Provided*** – The proxy voting system, as it currently operates in Canada, does not provide to an investor confirmation that the investor's voting instructions were translated into a vote that was counted at the shareholder meeting. Vote confirmation is possible in concept, but requires cooperation from everyone through whose hands the communications between the issuer and investors pass. Alternatively, one provider would need to control each of the steps of the communication process required to provide vote confirmation.
- ***Dominant Role of Broadridge*** – The proxy agent for almost all of the intermediaries in Canada is Broadridge. Accordingly, Broadridge is responsible for all of the mailings and tabulation of voting instructions for a very significant percentage of investors in every public company in Canada. Proxy agents are not regulated in Canada.
- ***Votes May Be Cast by Persons with No Economic Interest in the Issuer*** – Votes may be cast by persons who have no economic interest in the issuer. This may occur because the person sold its interest prior to the meeting, as a result of share lending or as a result of derivative instruments that allow a person to acquire a right to vote with no economic exposure to the share being voted.
- ***Power of Proxy Advisory Firms*** – Many institutional investors use the research services and proxy voting platforms offered by proxy advisory firms. As a result, proxy advisory firms have the ability to influence the way in which their clients (typically institutional investors) vote.
- ***Regulatory Engagement*** – The proxy voting system is regulated primarily under securities law. That regulation ends when investors give their voting instructions to their intermediaries. How the votes are tabulated and proxies are cast is completely

unregulated. Moreover, securities regulators do not monitor compliance with those aspects of the system that they do regulate.

### ***Key Issues That Need to Be Addressed***

The problems with the proxy voting system are so layered and complex that, in our view, a number of issues must be addressed before effective solutions can be proposed. The issues that we have identified as being the most immediate are set out below.

- ***Access to Information*** – There is not enough information available about the proxy voting system to allow an independent party to either prove that systemic problems exist or provide the confidence that they do not. Most of the information about the operation and effectiveness of the system resides with third-party service providers (transfer agents, proxy agents, proxy advisors and proxy solicitors) who have a great deal invested in the system and whose business interests would be affected by any change in the system. We hope this paper will contribute to a better understanding of the issues among issuers and investors. However, a more comprehensive audit of the system must be conducted by a task force of subject matter experts appointed by the government or by securities regulators.
- ***Movement Away from Paper-Based System*** – Some of the problems in the proxy voting system will be eliminated when issuers are no longer obligated to provide hard copies of their proxy materials to their investors. There will always be some investors who prefer paper versions of the materials, but there is a point at which the cost to the issuer and the mechanical complications outweigh the importance of providing the materials in the medium of choice to the investor. Canadian regulations need to do more to encourage the transition away from paper-based materials. Notice-and-access is a step in this direction, but the recent proposals by the Canadian Securities Administrators are only a first – and quite tentative – step towards a true paperless system.
- ***Revisiting the Commitment to the OBO Concept*** – One of the hallmarks of the Canadian (and U.S.) proxy voting system is that investors may elect to conceal their identity from the issuer (the OBO/NOBO system). The fact that issuers cannot communicate directly with many (today almost half) of their investors makes the communication process much more complicated.
- ***Problems Created by Intermediary Files That Are Not Reconciled for the Purpose of Proxy Voting*** – Intermediaries (brokers, banks, custodians) are required to create a list of their clients who are entitled to vote at a shareholder meeting, together with the number of shares held by those clients. However, those lists are often "unreconciled". They have not been adjusted to eliminate, for example, shares that have been loaned. The loaned shares will therefore still appear on the list prepared by the lender's intermediary for voting purposes, and will appear on the

list prepared by the borrower's intermediary for voting purposes. As a result, the vote attaching to a single share may be voted more than once.

- ***Issues Related to Broadridge's Place in the Market*** – Almost all of the intermediaries in Canada have outsourced their responsibilities in connection with communications between issuers and investors to Broadridge. Broadridge has played a leading role in improving and streamlining the proxy voting system in Canada. However, Broadridge is not subject to regulation in Canada and neither issuers or investors have a line of sight into how Broadridge has handled the voting instructions from investors in connection with any particular meeting.
- ***Deciding Whether Empty Voting Matters and How to Deal With It*** – There is no question that empty voting occurs, but there is no way to determine how extensive it is. If it has no real impact on the outcome of a shareholder vote, perhaps there is no reason to focus on it. If, however, it does have a material impact on the results of a shareholder vote, then the basis of shareholder decision making may come into question. More information needs to be collected about this issue. Consideration should be given to amending current disclosure requirements to make the necessary information available.
- ***Power of the Proxy Advisory Firms*** – Many institutional investors rely heavily on the recommendations of proxy advisory firms in deciding how to vote their proxies. Some issuers feel that the degree of de facto reliance gives proxy advisory firms the power essentially to dictate governance practices. Others are concerned that the proxy advisors do not understand issues specific to that issuer or even that they get some things wrong in their analysis. Finally, some are concerned with conflicts of interest where a proxy advisor both sells governance consulting services to issuers and provides voting recommendations to investors. A better understanding of the role and methods of proxy advisory firms is needed. In addition, issuers need a forum in which to articulate their concerns - a forum that would be capable of providing responses and solutions that alleviate the current concerns.
- ***Responsibilities of Investors*** – Do investors have any responsibilities to the issuers in which they invest or to the capital markets generally? Should they be expected to vote? If so, how do they reconcile securities lending with their proxy voting policies? These issues are receiving increased focus and in some cases affect other

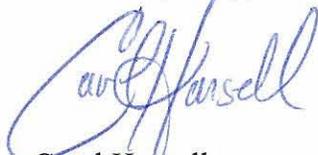
issues addressed in the paper. Institutional investors should engage actively in the issues facing the proxy voting system and the role that they play.

- ***Engagement of Securities Regulators*** – Securities regulators must acknowledge the importance of an effective and reliable proxy voting system. They should champion a comprehensive review of the system and be prepared to regulate aspects of the system in which they have not been involved.

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Davies appreciates the opportunity to comment on the Concept Release. We would be pleased to discuss any of the comments or suggestions in this letter or in our paper with the Commission staff in more detail. Please feel free to contact me at 416 863 5592 or Mark Connelly at 416 863 5526 or via e-mail at [chansell@dwpv.com](mailto:chansell@dwpv.com).

Yours very truly,



Carol Hansell