CANADA BUSINESS CORPORATIONS ACT

DISCUSSION PAPER

SHAREHOLDER COMMUNICATIONS AND PROXY SOLICITATION RULES

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EXECUTIVE SUMMARY

SHAREHOLDER COMMUNICATIONS AND PROXY SOLICITATION

At the heart of shareholder democracy is the premise that shareholders are the owners of the corporation. Corporate statutes establish the rights of shareholders to control major decisions of the corporations in which they have an interest. It is essential, then, that for shareholders to exercise these rights, they must have access to corporate information in a timely manner, be able to make an informed decision on what that information means, and be prepared to vote, in person or by proxy. Shareholder communications can be examined from two perspectives: communications between a corporation and its shareholders, and communications among shareholders themselves.

Communications Between Corporations and Shareholders

Many of the problems that affect communications between corporations and shareholders arise out of the changes in how shares are registered. Until relatively recently, shareholders were generally individuals who had in their possession actual share certificates. Now, however, few shareholders of publicly traded corporations actually hold registered shares. Instead, most are held by nominees, typically brokers, financial institutions, and other intermediaries. According to the records of the issuer, the intermediary is the registered shareholder; the beneficial shareholders are generally not known to the corporation.

Concerns that beneficial (often minority) shareholders can effectively exercise their voting rights were addressed by National Policy Statement Number 41 (NP 41), instituted by the Canadian Securities Administrators (CSA) in 1987. NP 41 sets out obligations for issuers, intermediaries and clearing agencies concerning shareholder communications by establishing a regime for issuers to forward proxy materials to beneficial shareholders through the intermediaries. However, since NP 41 was implemented, many issuers have complained that the system does not meet their needs or legal obligations under corporate law with respect to communications with beneficial shareholders.

To address the need for more effective and timely communication between corporations and their owners, especially in light of concerns over NP 41, several possible amendments are considered.

For example, the CBCA could require registrants to furnish to issuers, upon request, a list of all beneficial shareholders. This list could be used by the issuer to communicate directly with non-registered shareholders. Reaction among stakeholders to the CSA's proposals to amend National Policy 41 is mixed. Some stakeholders maintain that non-objecting beneficial owner (NOBO) lists should be used for any shareholder communication requirements associated with corporate governance, not just the distribution of proxy related material. Others feel that the use of non-objecting shareholder lists for proxy mailings is impractical and would lead to greater inefficiencies, confusion and risk of error within the process. While the paper takes the position

that use of NOBO lists should be allowed for all corporate governance matters, the proposed amendment to the CBCA may need to be reviewed to take into account the final decision with respect to NP 41.

Other proposals include harmonizing the CBCA with NP 41 with respect to the definition of "registrant"; the record periods for determining which shareholders are entitled to receive notice of a meeting; and the period during which a notice of a meeting will be sent.

The absence of a fixed record date for voting, has the potential to cause problems for publicly-traded corporations by creating additional possibilities for over-voting. For example, when a new shareholder purchases shares after the record date for notice of meeting, the previous owner may have already received and voted the proxies. The discussion paper recommends allowing corporations to establish a fixed record date for voting shares.

Another issue that requires attention by regulators is loaned shares, which create the potential for over-voting. Currently in Canada there is no one comprehensive piece of legislation or regulatory provision dealing with securities lending. In contrast to the U.S. where there is an industry "standard" agreement, there is no one standard agreement that is used in Canada, but instead many individual and sometimes inconsistent agreements are seen. Standardization in the granting and delivery of voting rights could be attained by amending the CBCA to allow the regulations to require that share loan agreements should specify who had voting rights for the shares being loaned.

With respect to proxy solicitation by management, the CBCA, unlike provincial corporate statutes, makes no distinction between distributing and non-distributing corporations. Instead, it requires the management of all corporations with 15 or more shareholders entitled to vote at the meeting to formally solicit proxies in preparation for each annual or special meeting.

The discussion paper recommends that all distributing corporations shall, concurrently with giving notice of a meeting of shareholders, send a form of proxy in prescribed form to each shareholder who is entitled to receive notice of the meeting. However, only non-distributing corporations with 50 or more shareholders would be subject to similar proxy requirements.

Communications Among Shareholders

A major problem for shareholders arises out of possible interpretations of paragraph 147(c) of the CBCA which defines "communication to a shareholder under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy" as a solicitation.

As a result of this definition, almost any communication could be deemed to be a solicitation under section 147 of the CBCA. The shareholder could then be held liable, upon summary conviction, to a fine not exceeding $5000 or imprisonment for up to six months or both, for failing to send the requisite proxy documents to all shareholders.

The need for a new standard of shareholder democracy was recognized in the United States, which had a similar definition of solicitation. Accordingly, in 1992, the Security and Exchange Commission (SEC) amended its proxy rules for the purpose of "promoting free discussion, debate and learning among shareholders and interested persons." In the SEC's view, "the federal proxy rules [had] created unnecessary regulatory impediments to communication among shareholders and others and to the effective use of shareholder voting rights."

To address the need for wider flexibility in communications between shareholders, the paper examines the 1992 SEC changes and proposes incorporating those that are appropriate in the Canadian context. In particular, the paper recommends granting an exemption from the proxy circular delivery and disclosure requirements for oral and written communications between shareholders. This exemption would be granted so long as the person communicating is not seeking proxy authority and written communications are made public by another means (e.g. publication or deposit with the Director appointed under the CBCA).

Other recommendations to facilitate communications among shareholders include:

- changing the definition of "solicitation" to specify that a shareholder can publicly announce how it intends to vote without having to comply with the proxy rules;
- exempting solicitations conveyed by public broadcast or speech or publication from the proxy circular delivery requirements, provided a definitive proxy circular is on file with the Director;
- allowing corporations and other soliciting parties to commence a solicitation on the basis of a preliminary proxy circular publicly filed with the Director; and
- requiring corporations to provide shareholders with copies of any list of non-objecting beneficial owners where those name are in the corporation's possession, in addition to the list of registered shareholders, as currently required.

The recommendations contained in the discussion paper are not in any sense government or even departmental policy. Rather, they are ideas that have come about largely through preliminary discussions with stakeholders across the country. This paper, and the consultations that will follow, are intended to solicit new ideas on how shareholder communications can be improved. All suggestions are welcome.

CANADA BUSINESS CORPORATIONS ACT

SHAREHOLDER COMMUNICATIONS AND PROXY SOLICITATION RULES

GENERAL INTRODUCTION

[1] The Canada Business Corporations Act (CBCA) governs many of the largest corporations in Canada. Approximately 187,000 companies are incorporated under the CBCA, including some 800 distributing or publicly-traded corporations. Of Canada's top 500 corporations (based on the 1994 Financial Post 500), 238 are incorporated under the CBCA.

[2] The importance of CBCA corporations to the Canadian economy is evidenced by the fact that, in 1993, these 238 corporations had sales or operating revenues totalling over $320 billion. It is therefore crucial that the CBCA be kept effective and efficient so as not to impede Canadian business, our competitive position, and the economic well-being of hundreds of thousands of Canadians.

[3] Overall, the CBCA aims to provide a practical balance of interests among shareholders, management and other stakeholders of federal corporations. This balance ensures both adequate investor protection and management flexibility, within the overall context of the public interest. The rules on shareholder communication are among the key areas where the balance becomes particularly relevant.

[4] Issues surrounding shareholder communications can be examined from two perspectives -- communications between the corporation and its shareholders, and communications among shareholders themselves. Because each has its own unique problems and solutions, in the following pages they are treated separately.

[5] Issues to be addressed will include:

- Whether the CBCA should be amended to require intermediaries to provide share issuers with lists of beneficial shareholders.

- Whether to harmonize the CBCA with National Policy 41 by amending the definition of a "registrant".

- Whether to amend the CBCA concerning:

    a) the record date for determining shareholders entitled to receive notice of annual or special meetings;

b) the period during which notice of annual meetings shall be sent to shareholders;

c) the record date for purposes other than those regarding notice of or votes at annual or special meetings.

- Whether the CBCA should provide for a fixed record date for the voting of shares.

- Whether the CBCA should specify voting right entitlement for loaned shares.

- Whether the rules governing the mandatory solicitation of proxies should be harmonized with provincial securities and corporate laws, specifically,

  a) Whether the CBCA should be amended to require that the management of all distributing corporations should be covered by mandatory proxy solicitation rules.

  b) Whether the CBCA should be amended to exempt management of a non-distributing corporation with fewer than 50 shareholders (rather than the current 15) from having to send a form of proxy to each shareholder who is entitled to receive notice of a meeting of shareholders.

- Whether the CBCA proxy solicitation rules should be amended in a manner similar to those recently adopted by the Securities and Exchange Commission in the United States, particularly in the area of communications among shareholders.

PART I

COMMUNICATIONS BETWEEN CORPORATIONS AND SHAREHOLDERS

ISSUE 1: WHETHER THE CBCA SHOULD BE AMENDED TO REQUIRE INTERMEDIARIES TO PROVIDE SHARE ISSUERS WITH LISTS OF BENEFICIAL SHAREHOLDERS

BACKGROUND

[6] At the heart of shareholder democracy is the premise that shareholders are the owners of the corporation. Corporate statutes carefully establish the rights of shareholders to control major decisions of the corporations in which they have an interest. Examples include approval of fundamental changes (such as amalgamations and capital structure amendments) and appointment of directors. It is essential, then, that for shareholders to exercise these rights, they must have access to corporate information in a timely manner, be able to make an informed decision on what that information means, and be prepared to vote, in person or by proxy. The process by which this takes place is designed to ensure that management decisions are in the best interests of the shareholders and the corporation.

The Nominee System

[7] Under the CBCA, corporate information, such as notices of meetings, proxy-related materials, and audited financial statements, is required to be sent to shareholders by the corporation.[1] While this would appear fairly straightforward, problems have arisen due to the development of two kinds of shareholders - "beneficial" and "registered".

[8] Beneficial shareholders are those investors in whose name shares have been purchased and to whom dividends and capital gains accrue. However, these shareholders are not necessarily registered on the books of the distributing corporation for the purposes of voting at annual meetings. For a variety of reasons, a depository, broker or other intermediary may be identified as the registered holder. The reasons for and consequences of this situation are explained below.

[9] Until relatively recently, shareholders were generally individuals who had in their possession actual share certificates. These were registered with the appropriate issuer, the issuers knew who their beneficial shareholders were, and communications proceeded relatively smoothly.

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[1] CBCA, sec. 134. Note that the notice of meeting and proxy documents are to be sent to shareholders "entitled to vote at a meeting" (sec. 135). Thus, not all shareholders necessarily receive notice.

[10] Over the past few decades, however, shareholder ownership practices have evolved such that few shareholders of publicly traded corporations now actually hold registered shares. Rather, most are held by nominees, typically brokers, financial institutions, and other intermediaries.

[11] Under the nominee system, intermediaries hold securities in "nominee form", and maintain a list of the beneficial owners they represent. According to the records of the issuer, the broker, financial institution or other intermediary was the registered shareholder. Because of this development, the beneficial shareholders were generally not known to the corporations.

The Depository System

[12] This creation of a layer between the corporation and its beneficial shareholders was exacerbated with the expansion of the depository system. Until the development of securities depositories, transfers of securities were accomplished by endorsements of certificates by an intermediary. In the 1970s, securities depositories were developed to facilitate the trading and settlement of securities by eliminating the need for delivery of share certificates between intermediaries. Most securities are now held on deposit with clearing agencies for the intermediaries. Changes in share ownership are accomplished through book-entry transfers in the appropriate accounts, with the result that settlements are finalized more efficiently.

[13] The key feature of both the nominee and, in particular, the depository systems is that, when shares are traded, no change is required in the corporate register of the registered shareholders. This allows for greater liquidity and facilitates trading.

[14] The depository system has been well received by the North American securities industry as a practical solution to the difficulties of share transfers. However, it has had the effect of adding a second layer (sometimes even a third) between the corporation and the beneficial owners of securities. This has increased the potential for alienation of the true owner from the governance of the corporation.

National Policy 41

[15] Increasing use of depository systems led issuers to expressions of concern that communications with shareholders have to go through layers of nominees. While the depository system solved the problem of facilitating share ownership transfers, there developed a general recognition that beneficial shareholders suffered from the increased difficulty and decreased effectiveness and timeliness of shareholder communications. Concerns over the continued assurance that beneficial (often minority) shareholders can effectively exercise their voting rights was addressed by National Policy Statement Number 41 (NP 41), instituted by the Canadian Securities Administrators in 1987.

[16] NP 41 sets out obligations for issuers, intermediaries and clearing agencies concerning shareholder communications by establishing a regime for issuers to forward proxy materials to beneficial shareholders through the offices of the intermediaries. These obligations ensure beneficial shareholders will obtain the necessary information and be able to exercise their right to vote either in person or by proxy at shareholders' meetings.

Concerns Over NP 41

[17] However, since NP 41 was implemented, many issuers have complained that the system does not meet their needs and legal obligations under corporate law with respect to communications with beneficial shareholders. Criticisms have been raised that NP 41 is unfair and costly because it requires issuers to pay others (intermediaries) to send information to beneficial shareholders without allowing the issuers to know who their shareholders really are.[2] It can therefore be difficult for corporations to plan for shareholder meetings, major changes, proxy battles and, in general, to know what shareholders want. As a solution, many issuers have suggested they, and shareholders, would be better served by a system that allows them to communicate directly with their beneficial shareholders.

CONSULTATIONS

[18] During public consultations undertaken by Industry Canada in February and March 1994, business people and their legal advisors were asked to suggest possible changes to the CBCA that would alleviate any problems.

[19] The issue of shareholder communications or proxy rules did not generate as animated a discussion as did issues such as directors' liability or directors' residency rules. Nevertheless, shareholder communications was identified as a priority area. In particular, concern was expressed over the lack of uniformity between the CBCA and NP 41.

[20] Specific problems associated with NP 41 were identified by stakeholders:

! There are "too many federal/ provincial differences, such as dates, signing of notices, etc. Nothing is the same. This increases costs; creates many difficulties. Firms have to run after shareholders."

! "Companies cannot quickly reach all their shareholders with direct mail. Many shareholders cannot prove their ownership [of shares] to the corporations....; the situation grows in direct proportion to the increase in depository registration."

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[2] Part X of National Policy 41 specifies that the issuer should bear the basic of cost of communicating with its shareholders, and sets a basic fee, payable to the intermediary by the issuer, of $1.00 per name of non-registered holder to whom the intermediary delivers proxy-related materials.

! "The current system doesn't work very well. By the time you get the information package, the annual meeting is upon you -- the next day in some circumstances. This is a disincentive to do anything with your shares."

! "The Asbestos case is an example. One shareholder wanted to start a class action, but the CDS would not give [that shareholder] a list of shareholders."

[21] On the other hand, one stakeholder felt that the CBCA should stay out of the business of regulating intermediaries, saying, "Corporate statutes should deal with registered shareholders. Intermediaries are not an issue for corporate statutes; that is an issue for securities legislation."

[22] Another stakeholder maintained that, if the CBCA were to become more involved in the shareholder communication issue, it should restrict itself to public corporations. As he put it, "It would be unfortunate if the CBCA were to apply rules to non-reporting issuers and force them into an NP-41 issue. This would add to costs."

[23] There was concurrence with this sentiment by other stakeholders, who felt that the issue of an intermediary is only there for a large public company.

[24] In response to concerns over the present system of shareholder communications, there could in the CBCA be:

RECOMMENDATION 1:

> **An amendment to section 153 requiring registrants to furnish to issuers, upon request, a list of all beneficial shareholders within a fixed time. This list could be used by the issuer to communicate directly with non-registered shareholders for any shareholder communication requirements of the Act associated with corporate governance, including the distribution of proxy related material.**

[25] A subsection could allow intermediaries to withhold the names and addresses of beneficial shareholders who have requested in writing that their names not be furnished to issuers. It could also be made subject to other legislation, such as the Quebec's privacy law,[3] which prohibits disclosure of information about a shareholder in the province of Quebec without the holder's express authority.

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[3] An Act respecting the protection of personal information in the private sector, R.S.Q., c. P-39.1.

Proposed CSA Amendments to National Policy 41

[26] The Canadian Securities Administrators are currently examining the possibility of amending National Policy 41 with a view to providing the express right for an issuer, subject to certain restrictions, to obtain from an intermediary a list of the names, addresses, holdings and preferred language of communications of the non-registered holders of the issuer's securities.[4] This non-objecting beneficial owner (NOBO) list allows the issuer to send security holder materials directly to non-registered shareholders. However, the present policy defines security holder materials only as proxy-related materials or audited annual financial statements or annual reports. General corporate governance materials are not covered by the new policy.

[27] Under the new proposals, a non-registered shareholder who does not expressly request anonymity is deemed to have given permission for his or her name to be forwarded to the issuers of any stocks he may hold.

[28] The CSA recognizes that intermediaries may feel constrained, in the absence of written instruction from their clients, from providing to a reporting issuer the above information of clients that have not responded to a request for permission to divulge such information. A requirement for confidentiality of client information may arise under statute (for example, the Quebec privacy act), common law, contract, trust agreement or otherwise. The ability of a reporting issuer to receive a list of the names and other information about the non-registered holders of its securities under the proposed revisions to NP 41 could therefore be subject to confidentiality requirements imposed upon the intermediary by law.

[29] The CSA supports the introduction of legislative provisions to expressly permit intermediaries to disclose to a reporting issuer the names, addresses, holdings and preferred language of communication of non-registered holders of the issuer's securities, except where the holder has given written instructions to the contrary.

[30] In addition, the proposed new draft of NP 41 proposes that a non-registered (beneficial) holder may elect to receive or not to receive security holder materials from reporting issuers. Where no instructions are sent by the beneficial shareholder to the intermediary, the new policy proposes that the beneficial shareholder be deemed to have elected not to receive security holder materials.

Concerns Over Amended National Policy 41

[31] Reaction among stakeholders to the CSA's proposals to amend National Policy 41 is mixed, although it is safe to say that virtually no one approves of the amended policy in its current form. On one side are issuing corporations, who maintain that NOBO lists should be used for any

[4] Ontario Securities Commission Bulletin, 17 (1994), p. 4828.

shareholder communication requirements associated with corporate governance, not just the distribution of proxy related material. They maintain that restricting the use of NOBO lists to proxy-related materials contradicts the original purpose of NP41 to improve communications to all shareholders.

[32] On the other hand, many intermediaries feel that the use of non-objecting shareholder lists for proxy mailings is impractical and would lead to greater inefficiencies, confusion and error risk within the process. They suggest that fragmentation and confusion could occur where issuers elect to request NOBO names only for intermediaries with large shareholdings, thereby leaving intermediaries with small holdings to mail the required materials themselves.

[33] Of more concern is the contention that the use of non-objecting shareholder names by issuers for proxy mailing purposes would move Canada away from harmonization with U.S. rules with additional resultant difficulties. Since Canadian jurisdiction cannot be extended to U.S. intermediaries and U.S. intermediaries cannot, under U.S. SEC rules,[5] provide NOBO lists for proxy purposes, there is a question as to whether U.S. intermediaries be dealt with differently than Canadian intermediaries by Canadian issuers.

[34] The proposed amendment to the CBCA seeks to bring the federal corporate statute into line with the new Draft National Policy 41 to the extent that issuers would be furnished with names of non-objecting beneficial shareholders. However, it goes further than the draft NP41 proposals in that it proposes to allow issuers to use the NOBO list for any shareholder communication requirements associated with corporate governance, including the distribution of proxy related material.

[35] At the present time, the Canadian Securities Administrators has directed its staff to work towards a resolution and reconciliation of outstanding issues. The proposed amendment to the CBCA may need to be reviewed to take into account the final decision with respect to National Policy 41.

ARGUMENTS IN FAVOUR OF CHANGE

[36] In combination with the proposed changes to National Policy 41, the proposed amendment would respond to at least two concerns expressed by issuers: the clarification of beneficial shareholder voting rights and proxy revocation.

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[5] Direct Communication rules governing the use of NOBO lists are not contained in U.S. corporate statues, such as the Model Business Corporation Act, but are found in Securities and Exchange Commission Regulations published in the Federal Register.

Beneficial Shareholder Voting Rights

[37] Beneficial holders of an issuer's shares are often confused about both their status and their rights as a shareholder. A shareholder who has purchased voting stock in a corporation rightly expects to be able to attend the meeting and cast a ballot. However, many beneficial holders are not aware that they are not registered on the books of the company. Issuers have claimed that, at virtually every shareholder meeting, individuals who have invested in a company arrive at the meeting expecting to be able to attend and to vote, only to find they cannot. Their perception is that they have been denied their rights.

[38] A corporation who is fully aware of who both its registered and beneficial holders are can clearly differentiate between them and supply the beneficial holder with the necessary voting authorizations.

Proxy Revocation

[39] Currently, because shareholder communications have to go through a number of layers, it is difficult, if not impossible, for beneficial shareholders to revoke or substitute specific proxies if the situation warrants. In a contentious meeting, revocations by beneficial shareholders must be denied until specific proxies can be identified. Should time constraints force a quick vote, beneficial shareholders appear to lose their rights once again.

[40] Under the proposed change, both registered and non-registered holdings will be maintained for meeting purposes within the same data base. Thus, revocations and substitutions could be handled for both registered and non-registered shareholders, right up to the time of a meeting or even up to the time of a specific vote during the meeting.

POSSIBLE OBJECTIONS

Confidentiality of Client Lists

[41] NP 41, as it currently exists, protects shareholders' privacy. Intermediaries are not required to inform issuers who holds the beneficial interests in the shares of specific companies. Rather, intermediaries may request from the issuer the number of packages of materials needed to be sent to the beneficial owners. Intermediaries must then forward these packages to their clients or arrange for a separate firm to do so.

[42] As noted, many intermediaries believe they are obliged to keep their client lists confidential. However, recent statements by some representatives of intermediaries indicate that if current legislation were amended so that intermediaries could not be held liable for breaching confidentiality in providing beneficial shareholder lists to issuers, there would be no problem with furnishing such lists upon request.

Creation of Dual Systems for Shareholder Communications

[43] Under the latest draft NP41, an issuer's request to an intermediary for a list of the issuer's beneficial shareholders would not create an obligation for the issuer to send proxy circulars or other material directly to those shareholders. If the issuer so wished, it could continue to employ the procedures set out in National Policy 41 to disseminate its material. This may raise concerns over the creation of dual and separate systems for issuers communicating with their shareholders.

[44] However, as already noted, Part X of the existing National Policy 41 already permits a reporting issuer the alternative of offering to deliver security holder materials itself or through its transfer agent if it can do so on a less costly basis. This part of NP41 invites an issuer to make arrangements with intermediaries to encourage them to use this option. In practice, the option has not been freely available to issuers.

ISSUE 2: WHETHER TO HARMONIZE THE CBCA WITH NATIONAL POLICY 41 BY AMENDING THE DEFINITION OF "REGISTRANT"

BACKGROUND

[45] Section 147 of the CBCA defines "registrant," whose duties correspond to those of an intermediary, as: "a securities broker or dealer required to be registered to trade or deal in securities under the laws of any jurisdiction".

[46] The definition of "intermediary" under National Policy 41 includes a much wider range of institutions, including:

(i) a registrant;
(ii) a financial institution (bank or trust company);
(iii) a participant;[6]
(iv) a trustee or administrator of a self-administered retirement savings plan, retirement income fund, education savings plan, or other similar self-administered savings or investment plan registered under the Income Tax Act (Canada); or
(v) a nominee of any of the foregoing;

that holds a security on behalf of another person or company who is not the registered holder of the security, but does not include a person or company that holds a security, or a trustee pursuant to a will, court order, inter vivos trust, or trust for a pension plan,

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[6] "Participant" in respect to a clearing agency means a securities dealer, trust company, bank or other person or company, including another clearing agency, on whose behalf the clearing agency or its nominee holds securities of an issuer. National Policy 41, Part II, "Definitions".

deferred profit sharing plan, retirement savings plan (other than as described in subparagraph (iv) of this definition) or other similar capital accumulation plan, with discretionary voting powers.

[47] In order to "capture" all intermediaries by the proposal to require intermediaries to furnish beneficial shareholder lists to issuers, the definition of "registrant" would have to be amended. We therefore recommend:

RECOMMENDATION 2:

An amendment to CBCA section 147 expanding the definition of "registrant" to also include

(a) a securities depository;
(b) a financial institution (bank or trust company);
(c) a participant;
(d) a trustee or administrator of a self-administered retirement savings plan, retirement income fund, education savings plan, or other similar self-administered savings or investment plan registered under the Income Tax Act (Canada);
(e) a nominee of any of the foregoing; or
(f) any person carrying out functions similar to identified above.

[48] This amendment would incorporate the definition of "intermediary" as defined in National Policy 41 into the CBCA definition of "registrant." It would also include securities depositories.

ISSUE 3: WHETHER TO AMEND THE CBCA CONCERNING:

a) THE RECORD DATE FOR DETERMINING SHAREHOLDERS ENTITLED TO RECEIVE NOTICE OF ANNUAL OR SPECIAL MEETINGS;
b) THE PERIOD DURING WHICH NOTICE OF ANNUAL MEETINGS SHALL BE SENT TO SHAREHOLDERS;
c) THE RECORD DATE FOR PURPOSES OTHER THAN THOSE REGARDING NOTICE OR VOTES AT ANNUAL OR SPECIAL MEETINGS.

Record Dates for Annual Meetings

[49] Under the CBCA,[7] the OBCA,[8] and other provincial corporate legislation, issuers may fix a date for determining which shareholders are entitled to receive notice of shareholder meetings. That date must fall within a period from 21 to 50 days prior to the meeting.

[50] Prior to the implementation of NP41, issuers complained that 21 calendar days was too short a time for proxy material to go through one or more layers of intermediaries and for proxies to be returned to the issuer. The speed of mail delivery was cited as a major impediment to timely shareholder communications. Even where material was delivered to registered security holders in accordance with the 21 day minimum period, some issuers stated that 30 to 50 percent of the proxies returned were received by the issuer after the meeting date.

[51] Accordingly, the Joint Regulatory Task Force on Shareholder Communication, out of which NP 41 was born, recommended in 1987 that issuers be required to set a record date for shareholder meetings to be 35 to 50 days before the date of the meeting. Subsequently, it was decided that 50 days still did not give sufficient time for issuers to complete notification in all instances. In the final version of NP 41, the maximum time for a record date prior to the meeting was extended to 60 days.

[52] NP 41 is grounded in the policy assumption that there is an intrinsic value in ensuring that shareholders receive corporate information in a timely manner and effectively exercise their voting rights. Among other things, NP 41 promotes effective shareholder communication by extending the allowable time periods for such communication. This ensures more, if not adequate, time for the receipt and assimilation of information by beneficial owners.

[53] However, federal companies cannot take advantage of the extension of the allowable time to communicate with shareholders. To be able to comply simultaneously with both the requirements of federal corporations law and National Policy 41, issuers incorporated under the CBCA have a window of between 35 days and 50 days to set a record date for determining which shareholders are eligible to attend a shareholders meeting.[9]

[54] This is a problem faced not only by federal corporations, but also those incorporated under provincial statutes. National Policy 41 is a set of rules that are accepted by all segments of the securities industry across Canada. As such, NP 41 has cut across corporate laws generally,

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[7] CBCA, sec. 134 (2).

[8] OBCA, sec. 95(2).

[9] This "window of opportunity" is that period where the periods for establishing a record date for a notice of a shareholders meeting under National Policy 41 (35 to 60 days) and the section 133 of the CBCA (21 to 50 days) overlap.

and has served to confuse many of the issues it set out to address. For that reason, some prominent corporate counsel have voiced concern over the CSA intruding into the corporate law area and have cited NP 41 as one of the examples.

[55] The revisions to the CBCA currently being discussed will allow the CBCA to set a possible standard for corporate statutes while bearing in mind the value of harmonized corporate and securities law provisions.

RECOMMENDATION 3:

> **An amendment to section 134(2) to allow for distributing corporations to determine shareholders entitled to receive notice of a meeting of shareholders, by fixing in advance a date as the record date for such determination of shareholders not to precede by more than sixty days or by less than thirty-five days the date on which the meeting is to be held.**

RECOMMENDATION 4:

> **An amendment to section 135(1) so that the notice of the time and place of a meeting of shareholders shall be sent to shareholders not less than 35 days nor more than 60 days prior to the meeting.**

RECOMMENDATION 5:

> **For non-distributing companies, it is recommended that the CBCA be amended to allow the directors, if the by-laws or articles of incorporation so provide, to set a shorter period for notice of both a meeting of shareholders, and the record date for determining which shareholders should receive notice of the meeting.**

[56] CBCA distributing companies are subject to National Policy 41, which sets out the parameters for fixing record dates for notice of meetings by distributing corporations.[10] The proposed amendments to the CBCA would harmonize the CBCA with National Policy 41, which is the current regulatory approach for distributing companies. In turn, they would permit easier understanding and compliance by persons subject to the CBCA and securities legislation and further cooperation among regulators. It may also serve to set a possible standard for adoption by provincial corporate law, which is also at odds with NP 41.

[57] On the other hand, it should be noted that the above recommendations specifically differentiate between distributing and non-distributing corporations.

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[10] This applies only to CBCA corporations that are reporting issuers in a Canadian province or territory. A CBCA company may be only a U.S. SEC registrant.

[58] In the areas of fixing a record date for shareholders' meetings as well as the sending of notice of such meetings to shareholders, the CBCA does not currently distinguish between distributing and non-distributing companies. However, it has been increasingly appreciated that, since 99% of CBCA corporations are non-distributing, some attention should be given to the possibility of the CBCA providing greater flexibility with respect to non-distributing corporations. The proposed amendments with respect to non-distributing corporations reflect this possibility.

Record Dates for Purposes Other than Annual Meetings

[59] The period for fixing record dates with respect to other matters should be consistent with section 134(2). Therefore we recommend that:

RECOMMENDATION 6:

> **Section 134(1), dealing with the fixing of a record date "for the purpose of determining shareholders (a) entitled to receive payment of a dividend, (b) entitled to participate in a liquidation distribution, or (c) for any other purpose except the right to receive notice of or to vote at a meeting", should be amended with respect to distributing companies to specify that the record date should not precede by more than sixty days the particular action to be taken.**

[60] Adoption of this amendment would harmonize the CBCA internally with respect to the fixing of record dates.

ISSUE 4: WHETHER THE CBCA SHOULD BE AMENDED TO PROVIDE FOR A FIXED RECORD DATE FOR THE VOTING OF SHARES

BACKGROUND

[61] Under corporate legislation in most Canadian jurisdictions, including the CBCA, the right of a security holder to vote at a meeting of security holders may not be restricted to those shareholders registered as of a fixed record date. With the exception of British Columbia,[11] corporate legislation in Canada does not permit the fixing of a record date for voting purposes.[12] Canadian legislative practice is in marked contrast to that of the United States. For a brief comparison, see appendix B.

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[11] BCCA, sec. 73(1).

[12] Section 134 of the CBCA permits the fixing of a record date for everything but voting.

[62] It has been argued that the absence of a fixed record date for voting promotes shareholder democracy. Shareholders have the right to attend and vote at the meeting if they establish ownership of the shares and demand the right to vote ten days, or less if the corporation's by-laws so provide, before the meeting.[13] The 1975 Briefing Book on the CBCA, detailing the amendments for Parliamentarians, explained that: "The provision is designed to prevent the disenfranchisement of shareholders."

[63] According to the Dickerson Report,

> After fixing a record date for a notice of meeting the directors must prepare a list of the shareholders to whom the notice is sent. Each such shareholder is deemed entitled to vote his shares as shown on the register, unless he transfers the shares and the transferee notifies the corporation accordingly. Thus the corporation has no duty to seek out the transferee, but the transferee has the right to have his name added to the shareholders list (voter's list) <u>at any time before the meeting</u>.[emphasis added][14]

[64] On the other hand, the prohibition on setting a fixed record date for voting has the potential to cause problems for publicly-traded corporations by creating a potential for over-voting.

[65] In contrast to 1975, when the CBCA was adopted, the majority of shares for most issuers are now held in the name of a registrant, usually the CDS, and owned beneficially through a chain of intermediaries. When a new shareholder purchases shares after the record date for notice of meeting, the previous owner may have already received and voted the proxies.

[66] With so many securities now held in non-registered form, the opportunity for over-voting is more likely to occur if both the non-registered holder, as of the record date, and the non-registered holder, post record date, vote. The corporation does not know which proxies, if any, should be cancelled. Should there be over-voting, the results of the vote may have to be cancelled or some other remedy implemented. In such a case, shareholder democracy would not be served.

RECOMMENDATION 7:

> **That the CBCA be amended to allow corporations to determine shareholders entitled to vote at a meeting of shareholders, by fixing in advance a date as the record date for such determination of shareholders not preceding by more than sixty days or by less than ten days the date on which the meeting is to be held.**

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[13] <u>CBCA</u>, sec. 138 (3)(ii)

[14] <u>Proposals for a New Business Corporations Law for Canada</u>, (the "Dickerson Report"), Volume I, page 52, no. 159.

TIMING OF RECORD DATE

[67] Establishing a period between ten and sixty days wherein a corporation can fix a record date for voting will have the virtue of maintaining internal consistency within the CBCA. The CBCA presently allows shareholders to demand to have their name included on a voter's list up to ten days before a meeting.[15] As well, the above proposed amendments to the CBCA regarding record dates for determining shareholders entitled to receive notice of a meeting of shareholders, entitled to receive payment of a dividend, entitled to participate in a liquidation distribution, etc., all provide for a maximum period of not more than sixty days from the appropriate event. There appears to be no utility for creating possible confusion by establishing a wide variety of periods for fixing record dates for various corporate events.[16]

Report of the Joint Regulatory Task Force on Shareholder Communication

[68] In its 1987 report to the Canadian Securities Administrators (out of which came National Policy 41), the Task Force noted that Canadian corporate law permits the establishment of a record date for notice of a meeting but not for the entitlement to vote. Accordingly, as has already been noted, a shareholder who acquires a security at any time up to the meeting date is entitled to vote that security, if the by-laws of that corporation so permit. The transferring shareholder becomes disentitled.

[69] If this were a frequent occurrence, scrutineering of shareholder votes would be extremely difficult. This would be especially so where the transferring shareholder, whose shares were registered in the name of a nominee, had already sent in a proxy or voting instructions.

[70] In order to make it easier for the issuer or scrutineer to determine the eligibility of the shareholder to vote, the Task Force recommended that corporate legislators require the establishment of a record date for entitlement to vote. It also recommended the imposition of an obligation upon the security holder to obtain the proxy or other voting entitlement from the transferring security holder.

[71] However, the Task Force felt that few unsophisticated security holders who acquire shares after the record date would be motivated to ensure their voting entitlement. As well, a fixed

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[15] Although, as also noted, a corporations by-laws can provide for a shorter period prior to the meeting. It is unlikely, however, that many corporations have by-laws that so provide.

[16] The Model Business Corporation Act (U.S.) does not set a minimum for date for the establishment of a fixed record date for determining shareholders entitled to notice of a shareholders' meeting, to demand a special meeting, to vote, or to take any other action. However, section 7.07 specifies that "a record date fixed under this section may not be more than 70 days before the meeting or the action requiring a determination of shareholders."

record date was not required for the implementation of National Policy 41. Because the matter is primarily one for corporate law, the issue was not pursued further.

[72] Presently, the Canadian Securities Administrators (CSA) supports efforts to address these problems through appropriate amendments to corporate legislation.

ISSUE 5: WHETHER THE CBCA SHOULD SPECIFY VOTING RIGHT ENTITLEMENT FOR LOANED SHARES

BACKGROUND

[73] Along with the lack of a fixed record date, the issue of loaned shares has arisen as factors in the creation of circumstances that may lead to over-voting. It has therefore been suggested that the CBCA be amended to provide rules for voting rights that would be attached to loaned securities.

[74] Securities lending is an arrangement where a person lends a security to another person who will, after a particular time, return to the lender a security identical to the loaned security. However, it need not necessarily be the very same physical security. The subsequent transfer would take place at a time which is either fixed or follows the expiry of a period after notice is given by either party. The security can be loaned for any period of time, although a short time period is usually specified, subject to renewal but always recallable by the lender on five or fewer days notice.

[75] The lending of securities generates potential problems in that it creates an illusion that there are more shares in a particular company's capital stock that are owned beneficially than are actually registered. The reality is that more than one proxy can be issued for the same shares when two or more shareholders feel that they have the right to vote them. This, in turn, can cause the number of proxies delivered by an intermediary to exceed the number of shares registered in the name of that intermediary. This may lead to adjustments to proxy tabulated votes that would affect a voting decision.

[76] The lending and borrowing of securities has become important to the financial marketplace for many reasons and serves several different functions. These include:

- to avoid delivery failures and defaults of settlement,
- to cover a short sale,
- to take advantage of Dividend Reinvestment Plans,
- to cover a "put" or a "call" or to obtain collateral to cover the put or the call,
- to maintain an arbitrage or hedging position, or
- to act as a source of revenue.

[77] Lending opportunities are created every day by the sheer volume and variety of securities transactions made in Canadian markets. There is a constant market for the temporary use of securities to be used for delivery on trade settlements to avoid delivery failures and to maintain short selling, arbitrage and hedging positions. What originally was used as a way to ease settlement and to cover failed transactions is now being put to increased use as a tool in sophisticated arbitrage and hedging deals. Because of the large volume of loaned securities in the marketplace on any given day,[17] the possibility of overvoting seems always to be present.

[78] Although securities lending transactions are characterized as loans of securities, the borrower is given the right to deal with the borrowed security freely. In particular, the borrower is permitted to deliver the security to a third party purchaser and to transfer ownership of the security to the third party. This right of transfer on the part of the borrower often creates confusion in assessing the true nature of the transaction.

[79] The right to exercise any voting rights in respect of the borrowed securities is reserved to the lender in most agreements. This means that if the lender wants to exercise his voting rights, the proxy must either be obtained from the borrower, or the borrower must attempt to obtain the voting rights for the lender.

RECOMMENDATION 8:

> **That the CBCA should require, either in the Act or in the Regulations, that share loan agreements should specify who has voting right entitlement when shares are loaned.**

Securities Lending Practices and Regulation in the United States

[80] Several years ago, overvoting in the United States was a much larger problem than it is now. At that time, the "proxy department" of brokerage firms was largely an extension of the mailroom, involved in little more than the mailing of meeting materials. In addition, brokerage firms would not take the time prior to a meeting to track loaned securities and therefore would distribute proxies that should not have been distributed - this is in fact one main cause of overvoting.

[81] In 1983, the Securities Industry Association issued a standard form agreement to be used in securities lending transactions between brokers, and between brokers and non-brokers (with banks having their own form of agreement). This standard agreement was used in the industry until early in 1994, at which time the Public Securities Association issued a standard securities

[17] A one-day "snapshot" of the Canadian securities lending marketplace taken by Nesbitt Burns in 1994 showed that $7.3 billion worth of equities was out on loan.

lending agreement which is now commonly used, both domestically and in transactions involving a Canadian lender or borrower.

[82] Securities lending transactions are recorded on the Depository Trust Company (the "DTC") books specifically as borrows and loans, whereas in Canada these transactions are recorded by depositories no differently than any other transaction. In this way, loans of securities can be tracked, and brokers are provided with two numbers - what portion of a share position is a loan, and what portion is not.

[83] The standard form agreement provides, as in Canadian agreements, that the borrower is obligated to return securities of the same issuer, class and quantity to the lender upon termination of the agreement, and that the borrower will collateralize the loan at what is usually more than 100% of the value of the loaned securities.

[84] However, where securities lending agreements in the U.S. differ from those in Canada is that, until the loan is terminated, the borrower is entitled to transfer ownership to others and to vote the securities.

[85] The right to vote the loaned securities is given to the borrower because of a New York Stock Exchange Rule which provides that one can vote only what is in one's "possession and control". Therefore, the lender loses the right to vote securities which are loaned because the lender is no longer in possession and control of the securities.

<u>The Canadian Situation</u>

[86] Currently in Canada there is no one comprehensive piece of legislation or regulatory provision dealing with securities lending. In contrast to the U.S. where there is an industry "standard" agreement, there is no one standard agreement that is used in Canada, but instead many individual and sometimes inconsistent agreements are seen.

[87] The agreement between the holder/lender of securities and the agent acting on behalf of the lender usually specifies that the agent will use its "best efforts" to get the proxy back from the borrower if the lender wants to vote the loaned securities. However, if the borrower has in turn transferred or lent the securities to a third party, there is little likelihood that the agent will be able to obtain the proxy. To ensure that it can indeed vote the securities, the lender must recall the loan and re-register the securities in its name. Currently, there is no mechanism to determine where the original proxy was delivered in those cases or to revoke or recall it in order to prevent a "double vote" of the shares.

[88] By amending the CBCA to allow the regulations to require that share loan agreements should specify who had voting rights for the shares being loaned, standardization of securities lending documentation may go a long way towards regulating the granting and delivery of voting

rights. As has previously been noted, most current agreements in Canada specify that voting rights remain with the lender, as opposed to the United States where voting rights are transferred to the borrower.

[89] In Quebec, however, article 2314 of the Civil Code of Quebec specifies that a simple loan is a contract by which the lender hands over to the borrower a certain quantity of money or other property that is consumed by its use. The borrower binds himself to return a like quantity of the same kind and quality of good to the lender after a certain time. Article 2327 states that the borrower becomes the owner of the property loaned. Therefore, the borrower can do anything he/she wants with the property, including selling and voting the shares.

[90] While, from a practical point of view, it does not appear to much matter which practice is adopted as a standard, so long as a standard is indeed adopted, there appears to be precedent set in the Civil Code of Quebec. Consideration would have to be made as to whether the rest of Canada wants to adopt a similar standard.

Dissenting View

[91] Guidelines for securities lending have already been published by the Office of the Superintendent of Financial Institutions (OSFI). These guidelines apply to financial institutions that make up the majority of agents acting for lenders or act as lenders themselves. A study commissioned by Industry Canada has recommended that the issue of entitlement to voting rights should not be legislated in a corporate statute, but could more properly be dealt with in the OSFI guidelines. In addition, the study proposes that National Policy 41 should also be amended to deal with securities lending issues, since it already addresses the issue of the voting of securities by non-registered shareholders.[18]

[92] Moreover, the same study suggests that many of the voting problems associated with securities lending could be resolved by amending corporate statutes to establish a fixed record date for the purpose of determining which shareholders are entitled to vote at a shareholders' meeting and the number of shares they may vote. In this way, holders who obtain securities either on loan or through a sale after the record date would not be entitled to vote the securities.

ISSUE 6: WHETHER THE RULES GOVERNING THE MANDATORY SOLICITATION OF PROXIES SHOULD BE HARMONIZED WITH PROVINCIAL SECURITIES AND CORPORATE LAWS

[93] This includes examining:

[18] The Draft Amended National Policy 41 does not address short sales or loaned securities. This has proven to be major problem to many stakeholders who have written to the Canadian Securities Administrators on the issue.

1) Whether the CBCA should be amended to require all distributing corporations (rather than just those with 15 or more shareholders), when giving notice of a meeting of shareholders, to solicit proxies from each shareholder who is entitled to receive notice of the meeting.

2) Whether the CBCA should be amended to exempt management of a non-distributing corporation with fewer than 50 shareholders from having to send a form of proxy and proxy circular to each shareholder who is entitled to receive notice of a meeting of shareholders.

BACKGROUND

[94] The primary objective of proxy rules is to provide shareholders with adequate information to enable them to exercise their voting rights in an informed manner and to monitor the affairs of the corporation. Disclosure requirements can enhance the corporation's accountability. They can also serve to raise corporate standards by discouraging questionable or unacceptable behaviour or by stimulating corporate reforms.[19]

[95] The CBCA and provincial corporate statutes call for the mandatory solicitation of proxies. However, under provincial securities and the corporate laws of most provinces, mandatory proxy solicitation rules apply only to reporting issuers.[20]

[96] Under sec. 149(1) of the CBCA, the management of a corporation is required to send a form of proxy to each shareholder who is entitled to receive notice of a meeting of shareholders. However, corporations with fewer than fifteen shareholders, two or more joint holders being counted as one shareholder, are exempted from this requirement.[21]

[97] The CBCA, then, requires the management of all corporations, distributing and non-distributing, with 15 or more shareholders entitled to vote at the meeting, to formally solicit proxies in preparation for each annual or special meeting.[22] In addition, such corporations are

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[19] Professor Raymonde Crête, Comparison of CBCA With Provincial Securities Laws, unpublished paper, page 39.

[20] The exceptions are the corporate laws of New Brunswick, Nova Scotia, Prince Edward Island and Quebec, which have no mandatory proxy solicitation laws for management.

[21] CBCA, section 149(2).

[22] Section 2(1) of the CBCA defines "corporation" as "a body corporate incorporated or continued under this Act and not discontinued under this Act." The CBCA, therefore, makes no distinction between private and public corporations.

required to file with the Director appointed under the CBCA copies of a circular in prescribed form, a copy of the notice of meeting, the form of proxy and any other documents in connection with the meeting.[23]

[98] The CBCA therefore provides far more stringent obligations on private corporations than do provincial corporate statutes, which do not require private companies to send a form of proxy to their shareholders at all. On the other hand, because no corporation with fewer than 15 shareholders is required to send a form of proxy, the requirements for distributing corporations may be less stringent under the CBCA than is the case under provincial statutes.[24]

[99] The CBCA does permit the Director to make an order exempting the management of corporations or dissidents from the mandatory proxy solicitation requirements. However, it is still incumbent on the applicant to apply periodically to the Director for such an exemption.[25]

CONSULTATIONS

[100] During consultations, stakeholders overwhelmingly agreed that the CBCA requirement for mandatory proxy solicitation of private companies should be amended. As well, some suggested a clear distinction between public and private corporations. Specific comments were as follows:

- The simple solution to this dilemma is to make a clear distinction between private and public corporations and drop the solicitation requirement for private companies.

- Go with a distributing/non-distributing breakdown. Eliminate the mandatory proxy solicitation requirement for non-distributing corporations.

- The CBCA should exempt private companies. It makes no sense to have disclosure with respect to private companies.

- Perhaps the solicitation requirement should be for companies with more than 50 shareholders (including employees).

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[23] CBCA, sec. 150 (2).

[24] The Dickerson Report noted that every shareholder entitled to vote at a meeting of shareholders should be entitled to vote by proxy. However, only those shareholders in corporations with 15 or more shareholders who are registered in the corporation's records on the record date would be deemed to have been solicited. Given the rapid growth in the number of shares held in securities depositories, it is entirely possible that the shareholder register of a corporation could list only the names of a few depositories, completely disguising the fact that there are a substantial larger number of beneficial shareholders.

[25] CBCA, section 151(1). Applications must be made annually for annual shareholder meetings, and as required for special meetings.

- In the case of a family corporation that has been successful over a generation or two, the threshold of 15 is too low.

- The number of 15 people is not the issue. Rather, it is that information circulars are costly and complex. Raise the threshold to 50 shareholders, or simplify the requirements for information circulars.

- You sometimes need a lot of people to get a small amount of money. It is onerous for companies to comply. The threshold is too low.

- The old distinction was 50 shareholders, then you were a public corporation. Somewhere between 15 and 50 is optimum. The larger the number of shareholders, the larger the responsibility has to be.

Other views were also expressed:

- The impression created is that the number "15" applies regardless of whether these shareholders can vote. If the intention of the CBCA is that it catch only voting shareholders then the Act should say this.

- In a new company, you may have more than 15 shareholders, so the provision is appropriate.

- Perhaps there should be a provision concerning the "relatedness" of the shareholders.

RECOMMENDATION 9:

> **That section 149 be amended to state that "<u>all distributing</u> corporations shall, concurrently with giving notice of a meeting of shareholders, send a form of proxy in prescribed form to each shareholder who is entitled to receive notice of the meeting."**

RECOMMENDATION 10:

> **That sec. 149(2) be amended to read that, "<u>non-distributing</u> corporations with 50 or more shareholders, two or more joint holders being counted as one shareholder, shall, concurrently with giving notice of a meeting of shareholders, send a form of proxy in prescribed form to each shareholder who is entitled to receive notice of the meeting."**

[101] Implementation of these recommendations would increase the level of harmonization between the CBCA with provincial securities and corporate statutes with respect to differentiating between distributing and non-distributing corporations.

[102] The Dickerson Report, which led to the CBCA, did not preserve the traditional private-public corporation dichotomy. Instead, it defined "corporation" in different ways in different parts of the draft act where it seemed necessary or desirable to create a distinction. Corporations were therefore distinguished on functional rather than doctrinal grounds. In different parts of the CBCA, then, corporations are differentiated according to criteria which are relevant in the circumstances.

[103] Some commentators feel this presents significant advantages because of the simplicity and certainty of its application.[26] All corporations with 15 or more shareholders, whether they distribute securities or not, become subject to proxy regulation.

[104] On the other hand, the Kimber Report recommended that the solicitation of proxies by the management of all public companies be mandatory. The drafters of the report felt that it was crucial that investors in all publicly-traded companies receive, prior to an annual meeting, an information circular containing, among other things, sufficient information on the matters to be voted upon to enable them to cast their votes for or against the particular proposals.[27]

[105] Mandatory proxy solicitation for all reporting issuers was also recommended in the federal government's "Proposals for a Securities Market Law for Canada."[28]

ARGUMENTS IN FAVOUR

Distributing Corporations

[106] Mandatory proxy solicitation by management, accompanied by an information circular, is seen by some to have the effect of influencing corporate behaviour. As one commentator put it:

> Often referred to as the "sunlight effect" of disclosure, the simple fact of requiring management to disclose certain activities [to their shareholders] may discourage management from concluding questionable or illegal activities... A system of mandatory

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[26] For example, see Raymonde Crête, The Proxy System in Canadian Corporations: A Critical Analysis. Editions Wilson & Lafleur ! Martel ltée, Québec, 1986, page 32.

[27] Ontario, Report of the Attorney General's Committee on Securities Legislation in Ontario (The Kimber Report), page 54.

[28] Section 7.05, Proposals for a Securities Market Law for Canada, Volume 1, Consumer and Corporate Affairs Canada, Ottawa, 1979.

disclosure may also encourage corporations to implement what are generally recognized as advisable corporate governance mechanisms.[29]

[107] Requiring proxy solicitation by CBCA distributing corporations which have less than 15 shareholders would, however, place additional costs on such firm. On the other hand, this is the norm for companies incorporated in other Canadian jurisdictions. Provincial governments, such as Ontario, have chosen to come down on the side that all distributing corporations be subject to proxy rules.

[108] However, the Ontario Business Corporations Act allows the Ontario Securities Commission to deem corporations with less than 15 shareholders to have ceased to be offering its securities to the public if "to do so would not be prejudicial to the public interest."[30] This allows small, more closely-held corporations to avoid the cost of proxy solicitation.

[109] Since 1984, a total of 90 corporations in Ontario have been so deemed. At present, some 800 distributing companies are incorporated under the CBCA. Industry Canada has only begun to gather data on how many companies have fewer than 15 shareholders, but a computer search of recent filings indicates that 108 distributing corporations fall into this category.

[110] Because of the number of publicly-traded CBCA corporations with fewer than 15 shareholders, there may be resistance to extending mandatory proxy solicitation to the management of those companies. However, such objections may be alleviated by applying for an exemption order under the provisions of the CBCA, either pursuant to subsection 2(8), to deem that a corporation is no longer considered to a distributing corporation, or subsection 151(1), to be exempted in full or in part from the proxy solicitation requirements.

Non-distributing Corporations

[111] As was ascertained during the preliminary consultation process, there is little likelihood that a proxy solicitation exemption for the management of small, privately-held corporations would be vigorously opposed. There is a slight possibility that there may be an argument in favour of the status quo, in the interests of preserving the filing (hence, disclosure) requirements for private corporations with 15 or more shareholders.

[112] Even among those stakeholders who did not specifically state that mandatory proxy solicitation for private companies be eliminated, there was a strong consensus that the threshold be raised from the current 15 shareholders to 50.

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[29] Crête, The Proxy System in Canadian Corporations: A Critical Analysis, page 18.

[30] OBCA, sec. 1(6).

[113] Raising the threshold for mandatory proxy solicitation by management of non-distributing CBCA corporations to 50 shareholders would reduce the expense incurred by small, often family-held companies who are required to comply with the law as it is now constituted.

[114] At the same time, it would eliminate the paper burden and legal costs associated with the preparation and distribution of proxy forms by private corporations who now have between 15 and 50 shareholders. It would also reduce the paper burden on government due to the filing requirements of sec. 150. At present, even if an exemption is granted by the Director under section 151, companies are still required to seek new exemptions for further meetings.

[115] Mandatory solicitation requirements would be retained for larger privately-held corporations (those with 50 or more shareholders, including employee shareholders) in order that there be statutory protection for minority shareholders in private companies with a large number of shareholders. Management in such corporations would therefore be required to send proxy material to all shareholders and minority shareholders would be guaranteed the opportunity to participate in annual meetings or vote on resolutions by management or dissident shareholders.

[116] An exemption from the mandatory solicitation of proxies could be given to the management of private companies, even those with 50 or more shareholders, if an application is made under subsection 151(1), which allows companies to be exempted from proxy solicitation requirements.

POSSIBLE OPTION

[117] As previously noted, section 151(1) of the CBCA permits the Director to make an order exempting the management of corporations from the mandatory proxy solicitation requirements. However, there are still costs associated with the necessity for a corporation having to apply for such an exemption.

[118] To relieve corporations with small numbers of shareholders from the burden of undertaking proxy solicitations, or filing for an exemption, some form of blanket exemption may be appropriate. It may be possible to remove the distinction between distributing and non-distributing corporations when it comes to the applicability of the proxy provisions, as is currently the case, and simply raise the threshold number of shareholders to 50 in both cases. Less onerous rules, such as those above, could still apply to non-distributing corporations with respect to other provisions, if necessary.

PART II

COMMUNICATIONS AMONG SHAREHOLDERS (DISSIDENT PROXY SOLICITATION)

ISSUE 7: WHETHER THE CBCA DISSIDENT PROXY SOLICITATION RULES SHOULD BE AMENDED TO REFLECT THE CHANGES ADOPTED IN 1992 BY THE U.S. SECURITIES AND EXCHANGE COMMISSION

BACKGROUND

[119] Section 147 of the CBCA defines proxy solicitation as including:

(a) a request for a proxy whether or not accompanied by or included in a form of proxy,
(b) a request to execute or not to execute a form of proxy or to revoke a proxy,
(c) the sending of a form of proxy or other communication to a shareholder under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy, and
(d) the sending of a form of proxy to a shareholder under section 149...[31]

[120] A problem for dissident shareholders arises mostly with subsection (c). This section, echoed in provincial securities acts as well as corporation acts (with the exception of Quebec), has its origins in U.S. Securities Exchange Act amendments of 1956. These amendments were intended to restrict communications "by any person who has solicited or intends to solicit proxies" prior to the formal commencement of the solicitation, that is, the distribution of proxy circulars and a form of proxy to voting shareholders. Both oral and written communications are considered to be solicitations.

[121] The definition of a proxy solicitation that includes "the furnishing of a communication to security holders under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy" creates an inherent uncertainty for shareholders.

[122] As a result of this definition, almost any expression of views, including, for example, an informal discussion among shareholders or a personal letter from one associate to another criticizing the quality of a company's management, could be deemed to be a solicitation under sec. 147 of the CBCA. The shareholder could then be held liable, upon summary conviction, to a fine not exceeding $5000 or imprisonment for up to six months or both for failing to send the requisite

[31] Section 149 requires the management of a corporation to send a proxy form to each shareholder who is entitled to receive notice of a meeting.

proxy documents to all shareholders (sec. 150). More importantly, violators of this section could be compelled to prepare and send, at their own expense, the required proxy materials to all shareholders.

[123] Representations to the SEC on the proxy solicitation issue claimed that the scope of the definition of solicitation under the proxy rules had a chilling effect on discussion of management performance, out of fear that a communication could after the fact be found to have triggered disclosure and filing obligations under the proxy rules. The same situation holds for Canada.

[124] Under the CBCA, when a person solicits proxies by or on behalf of the management of a corporation, a proxy circular must be sent to the auditor of the corporation, to each shareholder, to each director and to the Director appointed pursuant to the CBCA. Similarly, in the case of any other solicitation, a dissident's proxy circular stating the purposes of the solicitation must be sent to the same persons and, in addition, to the corporation.[32] The CBCA Director may grant a full or partial exemption from mandatory proxy solicitation requirements.[33]

[125] This restriction on shareholders communicating with each other has prompted some commentators and stakeholders to state that Canadian proxy solicitation rules do not necessarily serve the best interests of shareholders or, for that matter, of corporations. It has been argued that greater shareholder participation in corporate governance issues is necessary to provide an appropriate check on directorial abuses or mismanagement, especially since there is a growing belief in a direct correlation between good corporate governance and corporate performance.

[126] The major factor in this increased awareness of the importance of good corporate governance has been the phenomenal growth of institutional investors in both Canada and the United States.

Institutional Investors as an Emerging Power

[127] Over the past forty years, there has been a dramatic change in the structure of the Canadian investment community. Canadians have reduced their emphasis on self-directed investment in securities markets and instead have entrusted their dollars to mutual funds. In addition, pension plans, public and private, have experienced phenomenal growth. As a result of these trends, the aggregate market power of institutional investors has increased dramatically.

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[32] CBCA, sec. 150(1).

[33] CBCA sec. 151(1). This exemption is also found in some provincial and territorial corporate statutes: OBCA, sec. 113; ABCA, sec. 145; BCCA, sec. 179; MBCA, 145; NfldCA, sec. 249; SBCA, sec. 145; YBCA, sec. 153.

> In provincial securities law, persons other than management who solicit proxies from no more than 15 security holders need not comply with the requirement to send an information circular. This statutory exemption is not found in the CBCA.

[128] The five major institutional investors in Canada are public and private pensions, mutual fund companies, insurance companies, banks, and trust and loan companies. Combined, these types of institutional investors account for over 90% of total institutional investments within the Canadian investment community.[34] The remaining 10% is comprised of non-profit organizations such as foundations and endowments.

[129] The increase during the 1980s in the number of institutional investors and the size of their investments holdings has made it increasingly more complicated for them to "vote with their feet." For example, the total equity accumulated by institutional investors has recently been estimated to amount to $160 billion.[35] This, coupled with the limited number of publicly traded companies in Canada, makes it difficult for institutional investors to quickly move their investments from one company to another.[36]

[130] With such significant portfolios held in equity, institutional investors have a large stake in the effective management of the corporations in which they hold stocks, and in the long-term performance of these corporations. The reduced emphasis on maximizing short-term returns in favour of long-term gains has led to institutional investors' increased interest in the governance of corporations in which they have invested. Accordingly, there has been an increased trend by several institutional investors, particularly public pension funds, to become more actively involved in corporate governance issues through the issuance of proxy voting guidelines, court challenges, informal lobbying and, in some cases, even participation on boards of directors.

[131] A growing method of influencing corporate governance has been the use of voting to support or oppose the decisions made by a board of directors. The most common place to exercise voting power is at a corporation's annual meeting where shareholders elect the new board of directors and vote on strategic issues.

[132] Since most types of institutional investors are prohibited by law from acquiring more than a stated percentage of the voting rights of a corporation, the individual impact of one institution withdrawing its support may not be enough to have a significant impact on corporate

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[34] Statistics Canada, Cat. 74 - 001, 1993.

[35] Estimate given by Robert Bertram, Senior Vice-president, Investments for the Ontario Teachers Pension Plan Board to the Shareholder Rights & Communications Symposium, Toronto, October 5, 1994.

[36] All estimates of the increasing concentration of Canadian equity in institutional hands paint a similar picture. Robert Bertram of the Ontario Teachers' Pension Fund has written that "for the TSE as a whole, institutional ownership would represent about 61% of the float." This is echoed by Jean-Claude Delorme of La Caisse de dépôt, who has recently estimated that 57% of all liquid securities listed by the TSE is held by pension funds.

management.[37] However, the cumulative impact of several institutions voting in the same manner can be very powerful. In fact, similar voting by institutional investors can quickly influence corporate managers' decisions and force them to re-evaluate their business plan. On the other hand, if institutional, or any other investor, communicates its voting intentions to another investor, it runs the risk of violating the proxy solicitation rules.

1992 SEC Proxy Reforms

[133] The need for a new standard of shareholder democracy was recognized in the United States during the 1980s. As a result, the SEC devoted considerable resources and time in examining the proxy rules with a view to widening allowable communications among shareholders.

[134] In 1992, the SEC amended their proxy rules for the purpose of "promoting free discussion, debate and learning among shareholders and interested persons."[38] In its view, "the federal proxy rules [had] created unnecessary regulatory impediments to communication among shareholders and others and to the effective use of shareholder voting rights."[39] In particular, the SEC noted that,

> The Commission does not seem to have been aware, or to have intended, that the new definition might also sweep within all the regulatory requirements persons who did not "request" a shareholder to grant or to revoke or deny a proxy, but whose expressed opinions might be found to have been reasonably calculated to affect the views of other shareholders positively or negatively toward a particular company and its management or directors. Since any such persuasion, even if unintended, could affect the decision of shareholders even many months later to give or withhold a proxy, such communications at least literally could fall within the new definition.

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[37] For example, banks and other federally chartered institutions, such as insurance companies, are prohibited from owning more than 25% of the equity, or controlling more than 10% of the voting rights of a single issuer. Mutual funds (wherever chartered) are similarly prohibited and, in addition, may not "purchase securities for the purpose of exercising control or management over the issuer of such securities".

Provincial institutions, such as those chartered in Ontario, are constrained by guidelines with a similar translation. For example, the Ontario Pension Benefits Act limits an Ontario- regulated pension fund to ownership of no more than 30% of the voting shares of any one corporation; the aim being to impose passivity on the pension fund trustee.

[38] Federal Register, Part II, Securities and Exchange Commission, October 22, 1992, p. 48279. For a summary of the 1992 SEC proxy rule changes, see appendix C.

[39] ibid, p. 48277.

> The literal breadth of the new definition of solicitation was so great as potentially to turn almost every expression of opinion concerning a publicly-traded corporation into a regulated proxy solicitation. Thus, newspaper op-ed articles, public speeches or television commentary on a specific company could all later be alleged to have been proxy solicitations in connection with the election of directors, as could private conversations among more than 10 shareholders. This created a basis upon which claims that the proxy rules, including the mandatory disclosure, filing and dissemination provisions of those rules, could be brought to bear not only on persons seeking authority to vote another's shares, but also on those persons merely expressing a view or opinion on management performance or on initiatives presented by management and others for a shareholder vote.[40]

[135] The new rules instituted by the SEC were designed to reduce the cost of regulation to both the government and shareholders by removing unnecessary government interference in discussions among shareholders of corporate performance and other matters of direct interest to all shareholders. The amendments eliminated unnecessary regulatory obstacles to the exchange of views and opinions by shareholders and others concerning management performance and initiatives presented for a vote of shareholders. They also lowered the regulatory costs of conducting a regulated solicitation by management, shareholders and others by minimizing regulatory costs related to the dissemination of solicitation materials. The new rules also removed unnecessary limitations on shareholders' use of their voting rights, and improved disclosure to shareholders in the context of a solicitation as well as in the reporting of voting results.

CONSULTATIONS

[136] During preliminary consultations held in Spring 1994, a considerable number of comments were made that the CBCA, where practicable, should adopt some of the new SEC proxy solicitation rules. Some of the comments were as follows:

- Institutional investors have the resources to put an ad in the newspaper if they want their views known. Structure the mechanism so that there is a free exchange of information.

- Companies are controlled either by institutional investors or by management. It may be beneficial to allow communication between institutional investors; a group may get together to influence rather than change the management.

- Institutional investors are answerable to their stakeholders. Most communication would not be concerned with change of control. Communications regarding changes of control should become a public process.

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[40] Federal Register, Part II, Securities and Exchange Commission, October 22, 1992, pp. 48278-48279.

- The CBCA should go in the direction of the U.S. Securities and Exchange Commission by loosening the restrictions on the informal communications. Further importance should be given [to] ... institutional investors gaining more influence on corporate governance.

- Clarifications need to be made concerning communications between the corporation and the institutional investor. For example, a common practice of corporations is to guide corporate forecasts made by chartered financial analysts working for institutional investors. Institutional investors want to encourage reforms that permit them to practice increased corporate governance responsibilities.

- How do we deal with retooling the Act to further permit official meetings between large institutional investors?
  Institutional investors are becoming more demanding in their information requirements.

- Canada needs to adopt the U.S. model of shareholder communications. U.S. laws are more transparent. We need to be able to discuss issues back and forth.

- The CBCA should go further than the U.S. model. The U.S. model is highly structural. The existence of so few challenges by shareholders is a sign that the communications system does not work.

[137] To address the comments made by stakeholders, we recommend the following:

RECOMMENDATION 11:

> **An amendment to sec. 150 to create an exemption from the proxy circular delivery and disclosure requirements for communications with shareholders, where the person communicating is not seeking proxy authority and does not have a material interest in the matter subject to a vote or is otherwise ineligible for the exemption. Public notice of any written communication would be required from beneficial owners of more than $5 million or 10% of the corporation's securities through publication, broadcast or submission to the Director appointed pursuant to the CBCA of the written material.**

[138] This proposal arises out of the position that the current proxy rules unnecessarily curtail communications by shareholders on matters related to the company and its management, as well as with respect to matters presented by the corporation or a third party for shareholder action.

[139] The proposal to amend the CBCA would allow communications by persons (i) who do not seek the power to act as a proxy, or furnish or request, or act on behalf of a person who furnishes or requests, a consent or authorization for delivery to the corporation, and (ii) who are

disinterested in the subject matter of a vote,[41] from proxy requirements when communicating with other shareholders orally or in writing. Officers and directors of the company who are soliciting at their own expense will be entitled to rely upon the exemption.

[140] However, persons owning more than $5 million or 10% of the corporation's securities who make use of the exemption with respect to the dissemination of written communications would be required to submit that material within a fixed period of time to the Director for public disclosure.[42] Alternatively, this written material could be made public through a public notice, publication or broadcast (including a press release). No such requirement would be required for oral communications.

[141] The rationale behind exempting smaller shareholders from the requirement to file, or otherwise make public, written communications is the recognition of the unlikelihood of their having the resources to conduct "secret" solicitation campaigns in support of their proposals or against management proposals. Small, retail investors can therefore safely be spared the administrative and financial burden of disclosure of their written communications, provided they fall within the aforementioned description.

[142] However, because of the size of their holdings, larger shareholders, such as institutional investors, can quickly marshall the resources necessary to defeat a management proposition or to force through a proposal from the floor. There is therefore a definite discrepancy in power, which does not necessarily present a clear threat to management or minority shareholders, but does demand greater vigilance from the investment community and regulators.

RECOMMENDATION 12:

> **The definition of "solicitation" in CBCA section 147 would be amended to specify that a shareholder can publicly announce how it intends to vote and provide the reasons for that decision without having to comply with the proxy rules.**

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[41] Under SEC Rule 14a-2(b)(1), the exemption would not be granted to "any person who, because of a substantial interest in the subject matter of the solicitation, is likely to receive a benefit from a successful solicitation that will not be shared pro rata by all other holders of the same class of securities, other than by virtue of the person's employment with the registrant."

[42] The $5 million limit is similar to that specified under SEC Communications Among Shareholder rule 14a-2(b), which requires that public notice of written soliciting activity will be required by beneficial shareholders of more than $5 million of the registrant's securities through publication, broadcast or submission to the Commission of the written soliciting materials.

The alternative threshold of 10% of shares provides internal harmony within the CBCA, since the threshold level with respect to insider reporting and takeover bids is also 10%.

[143] The simple announcement by a shareholder or group of shareholders of how they intend to vote, whether or not coupled with the shareholders' reasons for their voting decisions, should not be subject to the proxy rules.

[144] Excluded from the definition of solicitation would be announcements that are published, broadcast or disseminated other than by a means specified.

[145] This exemption would be available to all shareholders entitled to vote, including officers and directors of the corporation, so long as they do not engage in an otherwise regulated solicitation.

RECOMMENDATION 13:

> **An amendment to exempt solicitations conveyed by public broadcast, speech and publication from the proxy circular delivery requirements, provided a definitive proxy circular is on file with the CBCA Director.**

[146] A person broadcasting or publishing solicitation material is required to deliver a proxy circular to all shareholders, since the publication or broadcast can be viewed as soliciting material furnished to all shareholders.

[147] The proposed amendment to the CBCA is intended to mirror the recent American rule revision in this area. It is intended to remove the regulatory obstacle to published or broadcast solicitations. This would be accomplished by adding a section to the CBCA allowing solicitations made solely by means of a speech in a public forum, or an opinion, circular or advertisement broadcast through radio or television media, or appearing in a newspaper, magazine or other publication disseminated on a regular basis. However, a definitive proxy circular would have to have been delivered to the CBCA Director prior to the solicitation.

[148] In any event, delivery of a form of proxy to a shareholder still must be accompanied by delivery of a proxy circular. Thus, the modification would not affect proxy circular delivery requirements where a form of proxy is provided in conjunction with a speech, publication or broadcast, or where a communication is made other than by a means specified.

RECOMMENDATION 14:

> **Amendments to allow corporations and other soliciting parties to commence a solicitation on the basis of a preliminary proxy circular publicly filed with the Director, so long as no form of proxy is provided to the solicited shareholders until the dissemination of a definitive proxy circular.**

[149] CBCA section 150 provides that a solicitation may not be made unless each person solicited concurrently is furnished with a written proxy circular. The proposal would permit the solicitation process in, for example, election contests to begin prior to the delivery of a proxy circular. Such preliminary solicitations could take place only if a form of proxy is not provided, certain background information concerning the participants is disclosed, and a formal proxy circular is sent to all shareholders eligible to vote as soon as practicable.

[150] The communications made pursuant to these provisions would be to provide background information on the soliciting party and other participants, including their interests in the subject matter of the solicitation.

[151] In non-election contest matters, the proposal would allow a solicitation to begin prior to delivery of a formal proxy circular to solicited persons. This could only take place if such a solicitation is made in opposition to a prior solicitation or other publicized activity and which, if successful, could reasonably have the effect of defeating the first solicitation.

[152] All written solicitation material disseminated in such solicitations would have to be filed or mailed for filing with the Director appointed pursuant to the CBCA on the same day they are first published, sent or given to shareholders.

RECOMMENDATION 15:

> **An amendment to CBCA section 21, requiring corporations to provide shareholders, upon written request and satisfaction of certain conditions, copies of its list of shareholder names, addresses, and position listings, as well as any list of non-objecting or consenting beneficial owners where in possession of the corporation.**

[153] Section 21 of the CBCA already requires a publicly-traded corporation to furnish anyone, including shareholders and creditors, a list of shareholders within ten days of receipt of the request. The request must be accompanied by payment of a reasonable fee and an affidavit attesting to the prescribed use of the list.

[154] If a record date for determining shareholders entitled to receive notice of a meeting has been fixed, a corporation is required to prepare a list of such shareholders. A shareholder is entitled to examine the list of shareholders (a) during usual business hours at the registered office of the corporation or at the place where its central securities register is maintained; and (b) at the meeting of shareholders for which the list was prepared.[43]

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[43] CBCA, sec. 138 (4).

[155] However, this shareholder list includes only registered shareholders. Today, few shareholders actually hold registered shares.

[156] The proposed amendment would require that a corporation send to a shareholder who has furnished proof of beneficial ownership, within a reasonable amount of time, the names of all non-objecting beneficial shareholders (or any portion requested) upon request in addition to a list of registered shareholders.[44] This would allow a dissenting shareholder to solicit proxies at his own expense, independent of management. However, the shareholder would be required to reimburse the corporation for any reasonable expenses incurred in providing the list.

[157] If the corporation has not itself obtained from intermediaries a list of its beneficial shareholders, it would be required to inform the requesting shareholder of that fact. Furthermore, the corporation would undertake to furnish to the beneficial shareholder such a list upon it being available to the corporation. However, a request by a shareholder for a list of non-objecting beneficial shareholders would not in itself obligate the corporation to obtain such a list from intermediaries.

[158] The list provided to requesting shareholders would necessarily be reasonably current and include the names, addresses, and security positions of registered holders, including banks, brokers and similar intermediaries, registered as owning securities in the same class or classes as holders solicited by management, or a more limited sub-group as designated by the shareholder. The information also must include a reasonably current list of non-objecting beneficial owners, if the corporation has obtained such a list (or updated list) for its own use prior to the meeting or other shareholder action.

[159] Shareholders receiving a list would be required to provide the corporation with an affidavit identifying the proposal that would be the subject of the shareholder's solicitation or communication and attesting that the shareholder would not:

(a) use the list for any purpose other than to communicate with or solicit security holders regarding the same meeting or action by consent or authorization for which the registrant is soliciting proxies; or

(b) disclose the list to any person other than a beneficial owner for whom the list request was made, or an employee or agent to the extent necessary to affect the communication or solicitation.

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[44] This amendment presupposes that lists of beneficial shareholders would be made available to corporations under changes to CBCA sec. 153 (discussed above) as well as an amended National Policy 41 that would allow NOBO lists for proxy purposes.

Draft Amended National Policy Statement 41

[160] Section 2.4 of the proposed amended National Policy 41 allows a dissenting shareholder to use the procedures set out in the policy to send proxy-related materials to non-registered shareholders of securities of the issuer. Dissenting shareholders who use the procedures established by NP41 are obligated to pay the fees and costs set out in the policy and are governed by rules regarding authorized use of the names provided by intermediaries. For example, offering for sale or purchase a list of names of beneficial shareholders is strictly prohibited.

[161] As has been previously noted, acceptable use of the NOBO list is controversial; some stakeholders making the case that it should not be used for proxy purposes, with others arguing that its use should be permissible for all corporate governance communications. The proposed amendment to the CBCA makes the assumption that use of the NOBO lists would be used for all corporate communications, including the sending of proxy materials. This, however, is subject to review depending on the final decision of the CSA with respect to the amended National Policy 41.

Compatibility of Proposed Amendments with Securities Legislation

[162] The above proposals concerning dissident shareholder communication, as has been previously noted, are based in large measure upon the changes to shareholder communication rules adopted by the Securities and Exchange Commission effective October 22, 1992. It may be that amending the CBCA along similar lines could put it into conflict with provincial securities laws, which govern proxy solicitation of distributing corporations.

[163] However, if it can be seen that the new American proxy rules do indeed foster greater shareholder democracy and an improved corporate governance climate, then the present review of the CBCA may provide an opportunity for the federal statute to break new ground in corporate law.[45] The CBCA has, in the past, served as a model for provincial corporate statutes as well as federal incorporating statutes such as the Bank Act. It may well be that the ideas that generated new proxy solicitation requirements in the United States are ideas whose time has come in Canada.

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[45] The Ontario Securities Act does allow reporting issuers to comply with the requirements of their home jurisdictions. Section 88(1) states that "where a reporting issuer is complying with the requirements of the laws of the jurisdiction under which it is incorporated, organized or continued and the requirements are substantially similar to the requirements of this Part, the requirements of this Part do not apply". Whether the CBCA's proxy solicitation rules under the proposed amendments would be considered "substantially similar" remains to be seen.

POSSIBLE ALTERNATIVES

[164] Although several stakeholders have raised the issue of adopting, to the extent possible, the recent revisions to the U.S. Securities and Exchange Act with respect to dissident proxy solicitation, such a wholesale copying of American legislation may not be appropriate in the Canadian context. Rather, simpler, and more direct, approaches may be preferable.

[165] Under provincial securities acts, persons other than management who solicit proxies from no more than 15 security holders need not comply with the requirement to send an information circular.[46] To alleviate at least some of the concerns regarding shareholder democracy and communications among shareholders, all that may be necessary, therefore, is to harmonize the CBCA with existing provincial securities legislation. Persons undertaking a wider solicitation would, however, be required to send an information circular to all shareholders entitled to vote on the proposition.

[166] Another possibility is to allow dissidents the option of soliciting shareholders of only one class or series, if a class vote is provided. For example, in situations where certain fundamental change to the articles of a corporation is proposed,[47] the CBCA provides for each class or series to vote separately on the proposal. If it is defeated by any single class or series, the proposal fails.

[167] Therefore, for a shareholder to defeat a fundamental change proposal, it could be necessary for him or her to solicit (and obtain) proxies from holders of only one class or series of voting shares. Allowing this limited or targeted solicitation under the CBCA would reduce the cost of undertaking a solicitation of all shareholders as is currently required. Dissident shareholders would then be more likely to contest fundamental changes with which they and the shareholders of the same class or series disagree.

[168] Another way the costs of dissident proxy solicitation could be reduced is by lessening the amount of information currently required to be provided in a dissident proxy circular.[48] Reduction of the amount of information required could be accomplished by changes to the Regulations, rather than amendments to the Act. However, for the purposes of this discussion paper, all possibilities should be explored. The Director appointed under the CBCA is currently reviewing key parts of the Regulations, including Part IV - "Proxy and Proxy Solicitation," with a view, among other things, to eliminating unnecessary requirements and to ensuring greater consistency with similar securities law provisions.

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[46] ASA, s. 128(2)a); BCSA, s. 101(3)a); MSA, s. 102(2)a), 103; NfldSA, s. 87(2)a); NSSA, s. 92(2)a); OSA, s. 86(2)a); QSA, s. 83, 263; SSA, s. 95(2)a).

[47] CBCA, sec. 176.

[48] CBCR, sec. 38 details the requirements of information to be included in a dissident's proxy circular.

CONCLUSION

[169] The purpose of this discussion paper, along with eight others dealing with CBCA reform,[49] is two-fold:

1) to address problems with the existing legislation that have been brought to the attention of Industry Canada, and
2) to provide, where possible, new approaches to advance the field of corporate law in Canada.

[170] The options outlined above are not in any sense the final word on the subject. They are ideas that have come about largely through discussions with stakeholders across the country. As such, they are not government or even departmental policy.

[171] There may be strong objections to the options contained in this discussion paper. There may be alternatives that we have not yet been made aware of. There may even be entirely different ways of looking at the issue of shareholder communications. This paper, and the consultations that will follow, are intended to solicit from those who use the CBCA and others new ideas on how shareholder communications can be improved.

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[49] The other eight discussion papers deal with:

- Financial Assistance to Directors and Officers;
- Directors' Liability;
- Takeover Bids;
- Insider Trading;
- the Residency Requirements for Directors;
- Going Private Transactions;
- Close Corporations (Unanimous Shareholder Agreements); and
- Technical Amendments.

APPENDICES

APPENDIX A

SUMMARY OF POSSIBLE AMENDMENTS

1) An amendment to section 153 requiring registrants to furnish to issuers, upon request, a list of all beneficial shareholders within a fixed time. This list could be used by the issuer to communicate directly with non-registered shareholders for any shareholder communication requirements of the Act associated with corporate governance, including the distribution of proxy related material. *(page 6)*

2) An amendment to CBCA section 147 expanding the definition of "registrant" to also include
   (a) a securities depository;
   (b) a financial institution (bank or trust company);
   (c) a participant;
   (d) a trustee or administrator of a self-administered retirement savings plan, retirement income fund, education savings plan, or other similar self-administered savings or investment plan registered under the Income Tax Act (Canada);
   (e) a nominee of any of the foregoing; or
   (f) any person carrying out functions similar to identified above. *(page 11)*

3) An amendment to section 134(2) to allow for distributing corporations to determine shareholders entitled to receive notice of a meeting of shareholders, by fixing in advance a date as the record date for such determination of shareholders not to precede by more than sixty days or by less than thirty-five days the date on which the meeting is to be held. *(page 13)*

4) An amendment to section 135(1) so that the notice of the time and place of a meeting of shareholders shall be sent to shareholders not less than 35 days nor more than 60 days prior to the meeting. *(page 13)*

5) For non-distributing companies, an amendment to allow the directors, if the by-laws or articles of incorporation so provide, to set a shorter period for notice of both a meeting of shareholders, and the record date for determining which shareholders should receive notice of the meeting. *(page 14)*

6) Section 134(1), dealing with the fixing of a record date "for the purpose of determining shareholders (a) entitled to receive payment of a dividend, (b) entitled to participate in a liquidation distribution, or (c) for any other purpose except the right to receive notice of or to vote at a meeting", should be amended with respect to distributing companies to specify that the record date should not precede by more than sixty days the particular action to be taken. *(page 14)*

7) An amendment to allow corporations to determine shareholders entitled to vote at a meeting of shareholders, by fixing in advance a date as the record date for such

determination of shareholders not preceding by more than sixty days or by less than ten days the date on which the meeting is to be held. *(page 16)*

8) A requirement, either in the Act or in the Regulations, that share loan agreements should specify who has voting right entitlement when shares are loaned. *(page 19)*

9) An amendment to section 149 so that all distributing corporations shall, concurrently with giving notice of a meeting of shareholders, send a form of proxy in prescribed form to each shareholder who is entitled to receive notice of the meeting. *(page 24)*

10) An amendment to section 149(2) so that non-distributing corporations with 50 or more shareholders, two or more joint holders being counted as one shareholder, shall, concurrently with giving notice of a meeting of shareholders, send a form of proxy in prescribed form to each shareholder who is entitled to receive notice of the meeting. *(page 24)*

11) An amendment to sec. 150 to create an exemption from the proxy circular delivery and disclosure requirements for communications with shareholders, where the person communicating is not seeking proxy authority and does not have a material interest in the matter subject to a vote or is otherwise ineligible for the exemption. Public notice of any written communication would be required from beneficial owners of more than $5 million or 10% of the corporation's securities through publication, broadcast or submission to the Director appointed pursuant to the CBCA of the written material. *(page 35)*

12) An amendment to the definition of "solicitation" in CBCA section 147 to specify that a shareholder can publicly announce how it intends to vote and provide the reasons for that decision without having to comply with the proxy rules. *(page 36)*

13) An amendment to exempt solicitations conveyed by public broadcast, speech and publication from the proxy circular delivery requirements, provided a definitive proxy circular is on file with the CBCA Director. *(page 36)*

14) Amendments to allow corporations and other soliciting parties to commence a solicitation on the basis of a preliminary proxy circular publicly filed with the Director, so long as no form of proxy is provided to the solicited shareholders until the dissemination of a definitive proxy circular. *(page 37)*

15) An amendment to CBCA section 21, requiring corporations to provide shareholders, upon written request and satisfaction of certain conditions, copies of its list of shareholder names, addresses, and position listings, as well as any list of non-objecting or consenting beneficial owners where in possession of the corporation. *(page 38)*

APPENDIX B

LEGISLATION REGARDING A FIXED RECORD DATE FOR VOTING

Provincial corporate laws

No provincial statute, except British Columbia, allows a fixed record date for voting by shareholders. Only the British Columbia Company Act expressly permits the corporation to establish a fixed record date for share voting. It stipulates that:

72.(1) Every company having more than 100 members shall,

(a) unless the register of members is in a form constituting in itself an index, keep an index of the names of the members of the company as a part of its register of members; and

(b) within 14 days after the date on which an alteration is made in the register of members, make any necessary alteration in the index.

73.(1) For the purpose of determining members, or members of a class of members, entitled to notice of, or to vote at, a general meeting or class meeting or entitled to receive payment of a dividend or for any other proper purpose, the directors may fix in advance a date as the record date.

(2) Where a record date is fixed, it shall be not more than 49 days before the date on which the particular action requiring the determination of the members is to be taken.

In British Columbia, it seems that only the shareholders registered at the record date can vote. There is no possibility, as in s. 138 of the CBCA, to add the name of a person who has subsequently purchased shares.

A search of British Columbia case law has not revealed a body of jurisprudence that would indicate that shareholders are prejudiced by this provision.

U.S. corporate laws

All American laws studied provide a record date for the purpose of determining shareholders entitled to vote at a meeting.

The New York Business Corporation Law establishes that a list of shareholders as of the record date shall be produced at any meeting of shareholders. If the right to vote is challenged, the list of shareholders shall be produced as evidence of the right of the persons challenged to

vote. Only the persons who appear from the list to be shareholders entitled to vote may vote at the meeting.

The Illinois and Delaware statutes make the list of shareholders a prima facie evidence as to who are the shareholders entitled to vote at a meeting.

There is no statutory procedure in New York, Delaware and Illinois laws which permits one to include the name of a shareholder in the voting list after the record date.

The text of these American laws is similar to sections 72 and 73 of the British Columbia Company Act, except for the length of the record date for notice or vote.

APPENDIX C

EXCERPT FROM FEDERAL REGISTER

Regulation of Communications Among Shareholders
Vol. 57, No. 205
Part II
57 FR 48276
Thursday October 22, 1992

AGENCY: SECURITIES AND EXCHANGE COMMISSION
DOC TYPE: Rules and Regulations
CFR: 17 CFR Parts 240 and 249
NUMBER: Release Nos. 34-31326170; IC-19031170;
File No. S7-15-92170;
RIN: 3235- AE12

ACTION: Final Rules

SUMMARY: The Securities and Exchange Commission ("Commission") today announces the adoption of amendments to its proxy rules promulgated under section 14(a) of the Securities Exchange Act of 1934 ("Exchange Act"). By removing unnecessary government interference in discussions among shareholders of corporate performance and other matters of direct interest to all shareholders, these rules should reduce the cost of regulation to both the government and to shareholders. The amendments eliminate unnecessary regulatory obstacles to the exchange of views and opinions by shareholders and others concerning management performance and initiatives presented for a vote of shareholders. The amendments also lower the regulatory costs of conducting a regulated solicitation by management, shareholders and others by minimizing regulatory costs related to the dissemination of soliciting materials. The rules also remove unnecessary limitations on shareholders' use of their voting rights, and improve disclosure to shareholders in the context of a solicitation as well as in the reporting of voting results.

EFFECTIVE DATE: These rules are effective October 22, 1992.

Transition Provision: The new rules are effective October 22, 1992, and any registrant or person engaging in a proxy solicitation may rely on the new rules at any time thereafter. However, to facilitate a smooth transition to use of the new rules, the following transition provisions will be allowed by the Commission. Soliciting parties and registrants are required to comply with the new rules for: (1) Any new proxy or information statement, form of proxy, and any periodic report under the Exchange Act filed on or after November 23, 1992; and (2) any request for a mailing or shareholder list received from a shareholder on or after that date.

SUPPLEMENTARY INFORMATION: The Commission is today adopting several amendments to its proxy rules and related disclosure requirements. These changes include:

(1) Rule 14a-2(b)[50] has been amended to create an exemption from the proxy statement delivery and disclosure requirements for communications with shareholders, where the person soliciting is not seeking proxy authority and does not have a substantial interest in the matter subject to a vote or is otherwise ineligible for the exemption. Public notice of written soliciting activity will be required by beneficial owners of more than $5 million of the registrant's securities through publication, broadcast or submission to the Commission of the written soliciting materials;

(2) The definition of "solicitation" in Rule 14a-1[51] has been amended to specify that a shareholder can publicly announce how it intends to vote and provide the reasons for that decision without having to comply with the proxy rules;

(3) Rule 14a-3[52] has been amended to add a new paragraph (f), exempting solicitations conveyed by public broadcast or speech or publication from the proxy statement delivery requirements, provided a definitive proxy statement is on file with the Commission;

(4) Rules 14a-3(a) and 14a-4[53] have been amended to allow registrants and other soliciting parties to commence a solicitation on the basis of a preliminary proxy statement publicly filed with the Commission, so long as no form of proxy is provided to the solicited shareholders until the dissemination of a definitive proxy statement;

(5) Rule 14a-6[54] has been amended to allow solicitation materials other than the proxy statement and form of proxy to be filed with the Commission in definitive form at the time of dissemination. In addition, preliminary proxy statements are now available for public inspection when filed except in connection with business combinations other than roll-ups and going-private transactions;

(6) Rule 14a-7[55] has been amended to require registrants, in the case of transactions subject to the Commission roll-up or going-private rules, to provide shareholders, upon written request and

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[50] 17 CFR 240.14a-2(b)

[51] 17 CFR 240.14a-1(l)

[52] 17 CFR 240.14a-3

[53] 17 CFR 240.14a-4

[54] 17 CFR 240.14a-6

[55] 17 CFR 240.14a-7

satisfaction of certain conditions, copies of its list of shareholder names, addresses, and position listings, as well as any list of non-objecting or consenting beneficial owners where in possession of the registrant. In all other cases, registrants are required to make an election either to provide a list to, or mail materials for, the requesting shareholders;

(7) Rules 14a-4(a) and (b)(1)[56] have been amended to require that the form of proxy set forth each matter to be voted upon separately in order to allow shareholders to vote individually on each matter;

(8) Rule 14a-4(d)[57] has been amended to allow shareholders who seek minority representation on the board of directors to seek proxy authority to vote for one or more of management's nominees, so long as the names of non-consenting nominees do not appear on the dissident's form of proxy or in the dissident's proxy statement;

(9) Rule 14a-11(c)[58] which mandated the filing of Schedule 14B[59] by all participants other than the registrant in an election contest, has been rescinded; and

(10) Items 4(c) of Forms 10-K,[60] 10-Q,[61] 10-KSB[62] and 10-QSB[63] and Item 21 of Schedule 14A[64] have been revised to require improved disclosure of voting results and of the vote needed for approval of matters presented to shareholders.

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[56] 17 CFR 240.14a-4(a) and (b)(1)

[57] 17 CFR 240.14a-4(d)

[58] 17 CFR 240.14a- 11(c)

[59] 17 CFR 240.14a-102

[60] 17 CFR 249.310

[61] 17 CFR 249.308a

[62] 17 CFR 240.310b

[63] 17 CFR 240.308b

[64] 17 CFR 240.14a-101