

Headnote

Mutual Reliance Review System for Exemptive Relief Applications - issuer bids - relief granted from the valuation requirement in connection with an offer by the issuer for its out-of-the-money convertible debentures - issuer representing in order that convertibility feature is of no material value and debentures trade only on the issuer's underlying creditworthiness - offer otherwise to be made in compliance with issuer bid requirements - offer document to include summary of financial opinion on convertibility feature.

Applicable Ontario Rules Cited

Rule 61-501 - Insider Bids, Issuer Bids, Going Private Transactions and Related Party Transactions, ss. 3.3, 3.4(1) and 9.1.

**IN THE MATTER OF
THE SECURITIES LEGISLATION
OF BRITISH COLUMBIA, ALBERTA, SASKATCHEWAN, MANITOBA
ONTARIO, QUEBEC, NOVA SCOTIA AND NEWFOUNDLAND
AND**

**IN THE MATTER OF
THE MUTUAL RELIANCE REVIEW SYSTEM
FOR EXEMPTIVE RELIEF APPLICATIONS
AND**

**IN THE MATTER OF
THE DESCARTES SYSTEMS GROUP INC.**

MRRS DECISION DOCUMENT

WHEREAS the Canadian securities regulatory authority or regulator (the **ADecision Maker@**) in each of British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Quebec, Nova Scotia and Newfoundland (the **AJurisdictions@**) has received an application (the **AApplication@**) from The Descartes Systems Group Inc. (the **ACorporation@**) for a decision pursuant to the securities legislation of the Jurisdictions (the **ALegislation@**) that, in connection with the proposed purchase by the Corporation of a portion of its outstanding 5.5% Convertible Unsecured Subordinated Debentures due June 30, 2005 (the **ADebentures@**) pursuant to a formal issuer bid (the **AProposed Bid@**):

- (1) the Corporation be exempt from the requirements in the Legislation to obtain a valuation of the Debentures (the **AValuation Requirement@**); and
- (2) the Application and this MRRS Decision Document (the **ADecision@**) be held in confidence by the Decision Makers, subject to certain conditions.

AND WHEREAS pursuant to the Mutual Reliance Review System for Exemptive Relief Applications (the **ASystem@**), the Ontario Securities Commission is the principal regulator for the Application;

AND WHEREAS the Corporation has represented to the Decision Makers as follows:

1. The Corporation was amalgamated under the *Business Corporations Act* (Ontario) on January 26, 1999.
2. The Corporation is authorized to issue an unlimited number of Common

Shares (the ACommon Shares@). As of July 3, 2002, the Corporation had outstanding 52,241,265 Common Shares.

As of July 3, 2002, the Corporation had outstanding Debentures in the aggregate principal amount of U.S.\$72,000,000.

3. The Corporation is a reporting issuer or the equivalent in each of the Jurisdictions and its Common Shares are listed and posted for trading on the Toronto Stock Exchange (the ATSX@) under the trading symbol ADSG@ and on the Nasdaq National Market (ANasdaq@) under the trading symbol ADSGX@. The Debentures are listed and posted for trading on the TSX under the trading symbol ADSG.DB.U@.
4. The Debentures were issued pursuant to an indenture dated June 30, 2000 (the AIndenture@) between the Corporation and Montreal Trust Company of Canada (now Computershare Trust Company of Canada) and distributed pursuant to a short form prospectus dated June 26, 2000.
5. The Indenture provides that, unless an AEvent of Default@ (as defined in the Indenture) has occurred and is continuing under the Indenture, the Corporation may purchase for cancellation any or all of the Debentures by invitation for tenders. No Event of Default has occurred under the Indenture. There are no other restrictions upon the Corporation=s ability to purchase the Debentures.
6. The Debentures are convertible at the Debentureholder=s option into Common Shares at any time prior to the earlier of June 30, 2005 and the last business day immediately preceding the date specified for redemption by the Corporation. The conversion price for the Debentures is U.S.\$35.00 per Common Share, being a rate of approximately 28.57 Common Shares per U.S.\$1,000 principal amount of Debentures.
7. On December 21, 2001, the Corporation filed and the TSX accepted a Notice of Intention to Make a Normal Course Issuer Bid (the ANotice@) in respect of the Debentures.
8. Pursuant to the Notice, the Corporation may acquire through the facilities of the TSX up to a maximum of U.S.\$7,500,000 of its outstanding Debentures, representing approximately 10% of the public float of Debentures as at December 22, 2001. An aggregate principal amount of U.S.\$3,000,000 have been acquired pursuant to the Notice up to and including March 13, 2002, the last date on which Debentures were acquired pursuant to the Notice.
9. To the knowledge of management of the Corporation, no person or company

holds more than 10% of the aggregate principal amount of outstanding Debentures.

10. Over the 12 complete months prior to July 3, 2002, the Debentures traded on the TSX on 111 out of 250 trading days, with an average daily trading volume of U.S.\$68,396 on the days traded, and the price range over that period was U.S.\$580 to U.S.\$800 per U.S.\$1,000 principal amount of Debentures.
11. As at July 3, 2002, the closing price of the Debentures on the TSX was U.S.\$680 per \$1,000 aggregate principal amount outstanding.
12. The Debentures are convertible into Common Shares at a conversion price which is significantly in excess of the current market price of the Common Shares. The Debenture conversion price of U.S.\$35.00 per Common Share for each U.S.\$1,000 in aggregate principal amount of Debentures outstanding is equivalent to Cdn.\$53.61 per Common Share based on the foreign exchange rates as of July 3, 2002. On July 3, 2002, the closing price of the Common Shares on the TSX was Cdn.\$4.73, which was approximately 8.8% of the conversion price of the Debentures at such time, based on the foreign exchange rates then in effect. Over the 12 months preceding that date, the Common Shares traded on the TSX in a range between Cdn.\$4.10 and Cdn.\$27.40 per Common Share.
13. In a letter (the AOpinion Letter[@]) dated July 15, 2002, Griffiths McBurney & Partners (AGMP[@]) advised the Corporation that, in GMP's opinion:
 - (i) the convertibility feature of the Debentures is of no material value; and
 - (ii) the Debentures trade on the TSX like non-convertible, subordinated, unsecured debt based on the Corporation's underlying creditworthiness.
14. The Proposed Bid will proceed by way of an issuer bid circular which will include a summary and a copy of the Opinion Letter.
15. The Corporation intends to acquire up to an aggregate principal amount of U.S.\$51,428,571 of Debentures, representing approximately 71.4% of the outstanding Debentures. The Corporation anticipates using cash on hand and cash equivalents to fund the Debenture acquisitions.
16. The Proposed Bid will be an Aissuer bid[@] within the meaning of the Legislation in the Jurisdictions because the Debentures are convertible debt securities.

17. The Corporation has not yet announced its intention to proceed with the Proposed Bid, which remains subject to approval by the Board of Directors of the Corporation. Given the potential size of the Proposed Bid, release of the Decision prior to such an announcement could affect the market price of the Debentures.

AND WHEREAS pursuant to the System, this MRRS Decision Document evidences the Decision of each Decision Maker;

AND WHEREAS each of the Decision Makers is satisfied that the test contained in the Legislation that provides the Decision Maker with the jurisdiction to make the Decision has been met;

THE DECISION, of the Decision Makers in the Jurisdictions pursuant to the Legislation is that, in connection with the Proposed Bid, the Corporation is exempt from the Valuation Requirement, provided that the Corporation complies with the other applicable provisions of the Legislation relating to formal bids made by issuers.

THE FURTHER DECISION of the Decision Makers pursuant to the Legislation is that the Application and the Decision shall be held in confidence by the Decision Makers until the earlier of the date that the Circular is filed in connection with the Proposed Bid and August 14, 2002.

DATED July 30, 2002.

"John Hughes"

John Hughes - Manager, Continuous Disclosure



Securities Commission
valeurs mobilières
de l'Ontario

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Toronto ON M5H 3S8

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July 23, 2002

MEMORANDUM TO: John Hughes - Manager, Continuous Disclosure

FROM: Doug Welsh - Legal Counsel, Takeover/Issuer Bids

Descartes Systems Group Inc. (Descartes) - MRRS Exemption from Valuation Requirement - No. 641/02

Summary and Recommendation

Descartes is applying under MRRS for an exemption from the valuation requirement pursuant to section 9.1 of Rule 61-501 and the comparable provisions of the non-principal regulators. The exemption is requested in connection with a proposed issuer bid by Descartes for 79% of its convertible debentures (the Debentures).

I recommend that you grant the exemption in the form of the attached draft decision document (the Decision). The conversion price of the Debentures is significantly out of the money. Descartes has provided an opinion letter from Griffiths McBurney which states that the convertibility feature of the Debentures is of no material value and that the Debentures trade on the TSX like non-convertible debt based on Descartes underlying creditworthiness. Given the foregoing, it would not be prejudicial to the public interest for you to grant the Decision as non-convertible debt is generally more easily objectively valued than equity securities. This is why issuer bids for securities that are not participating securities and that are not convertible into participating securities are exempt from the valuation requirement under the exemption in paragraph 3.4(2) of Rule

61-501. Offers to acquire non-convertible debt securities are also exempt from the issuer bid requirements under the definition of issuer bid in subsection 89(1) of the *Securities Act* (Ontario).

Similar exemptions were previously granted under MRRS *In the Matter of Western Financial Group Inc.*, dated June 11, 2002, and *In the Matter of Revenue Properties Company Limited*, dated March 1, 2002 (copies of these decisions and accompanying staff memoranda are in the file).

The Proposed Issuer Bid

Descartes is contemplating the purchase of up to 79% of its outstanding Debentures for cash through a formal issuer bid. It has not yet publicly announced its intention to make the bid. Descartes started repurchasing Debentures over the TSX pursuant to a normal course issuer bid. Given that Descartes is now contemplating purchasing more than 10% of the outstanding Debentures, it must proceed by way of a formal bid. Descartes initially contemplated that the formal bid would proceed by way of modified dutch auction, but subsequently advised that it would be a fixed price bid.

The Issuer Bid Requirements

Descartes initially applied for relief from the proportionate take-up requirement in paragraph 95(7) of the *Securities Act* (Ontario) and the comparable provisions of the non-principal regulators to permit it to proceed with its bid by way of modified dutch-auction. Descartes withdrew its application under this head of relief by letter dated July 22, 2002 when it decided to proceed by way of a fixed price bid.

The Valuation Requirement

Since the proposed bid is for convertible debt securities, it is technically an issuer bid and subject to the valuation requirement of section 3.3 of Rule 61-501 and the comparable provisions of the non-principal regulators. Practically, however, the conversion price of the Debentures is so far out of the money that the Debentures trade like non-convertible debt. I recommend that you grant the Decision for this reason.

Issuer bids for non-convertible debt are exempt from the valuation requirement because debt is relatively more easily objectively valued based upon cash flows, prevailing interest rates, and the perceived creditworthiness of a given issuer. Given that Descartes has provided an opinion from Griffiths McBurney that the convertibility feature of the Debentures is of no material value and that the Debentures trade like non-convertible debt, it would not be prejudicial to the public interest for you to grant the Decision. This opinion will also be disclosed in and provided with the issuer bid circular.

The facts in this instance are different from the decisions in *Western Financial* and *Revenue Properties* because the proposed issuer bid will be a partial bid. This difference has no impact on my recommendation to grant the Decision.

The staff memorandum accompanying the decision in *Revenue Properties* indicated that the existence of a premium in the bid price may be a relevant factor to consider when there is a partial bid. There was no premium in either *Revenue Properties* or *Western Financial*, but those bids were not partial bids. B.C. staff requested information concerning the proposed bid price range when Descartes was still contemplating

proceeding by way of modified dutch auction. B.C. staff further commented that, in previous decisions, they usually considered whether it was appropriate to have comfort that the bid will be made at a premium to market and that one of the circumstances that the premium may be relevant is where the bid is a partial bid, and therefore debenture holders may be coerced into tendering for fear of an illiquid market following the bid.

The filing solicitor advised me that the bid will likely be made at market or slightly above market, but that Descartes would not know for sure until they announce the bid. At any rate, in my view, the existence of a premium in a partial issuer bid for convertible debt that trades like non-convertible debt is not a relevant factor to consider in recommending an exemption from the valuation requirement. As discussed above, the basis for the exemption is that generally non-convertible debt is relatively more easily objectively valued by investors. This is one of the reasons that issuer bids for non-convertible debt are exempt from the valuation requirement under Rule 61-501. I would also submit that concerns about coercion or illiquid markets in partial bids are much less compelling in bids for non-convertible debt relative to bids for equity securities.

Confidentiality

Descartes also requested that the Decision and the application be maintained confidential until the earlier of the date that the bid is announced and August 31, 2002. This period was changed to the earlier of the date that the bid is announced and August 14, 2002. A 2 week period is consistent with that granted in *Revenue Properties* and seemed reasonable in the circumstances. The filing solicitor did not object.

Consistent with National Policy 12-201, this request was set out as a separate head of relief. The Director in Ontario granted a similar request in *Revenue Properties*. I understand, however, from speaking with Paul Hayward, Ontario's staff representative on the MRRS Committee, and Cindy Rogers that Ontario staff's procedure on confidentiality requests continues to evolve given the uncertainty in our Act over exactly what materials must be publicly filed and what decision maker has statutory authority to grant these requests. Until we have finalized that procedure, however, I recommend that you grant the request for confidentiality in the Decision as was done in *Revenue Properties*.

Comments from Other Jurisdictions

1. CVMQ staff raised a number of comments to which the filing solicitor responded in writing directly. A number of these concerns were addressed when Descartes decided that it would not proceed by way of modified dutch auction for other reasons. I have not recreated the comments and responses here as I understand that CVMQ staff is satisfied with the responses provided by the filing solicitor and no further changes were required to the Decision.
2. As discussed above, B.C. staff requested information regarding the existence of a premium in the proposed bid price. Please see the discussion in the 4th and 5th paragraphs of The Valuation Requirement section above. Consistent with *Revenue Properties*, B.C. staff also inquired whether Descartes intended to proceed with the bid in the absence of obtaining relief from the valuation requirement. The filing solicitor advised that he did not know for sure. However, in further discussions

with B.C. staff, we concluded that it was unnecessary to include this as a representation in the Decision.

3. Manitoba staff commented as follows:

"While we can keep the application confidential at this time, once this matter is heard by our Commission the Order would be public unless the filer requests and is granted confidentiality relief. Such relief would have to be time limited and there should be representations in the Decision Document supporting such a request. I note the filer is asking for confidential treatment of any resulting order under the conditions noted in the application. Please confirm with the filer whether it still needs this relief. If so, they will have to revise the representation and operative sections of the Order as set out above".

The filer has requested that the Decision be maintained confidential for the reasons indicated in the Confidentiality section above. The filer confirmed that it still needs this relief as it is not yet in a position to announced the proposed bid. I further attempted to deal with Manitoba's concerns by adding representation #17 into the Decision and by limiting the period of confidentiality to a maximum of 2 weeks.