KINGSDALE Advisors

June 11, 2018

To:

Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Financial and Consumer Services Commission (New Brunswick)
Manitoba Securities Commission
Nova Scotia Securities Commission
Nunavut Securities Office
Office of the Superintendent of Securities, Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Yukon Superintendent of Securities
Ontario Securities Commission
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

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Dear Sir/Madam:

Re: CSA Staff Notice 61-303 and Request for Comment Soliciting Dealer Arrangements

We thank you for the opportunity to provide you with comments on the use of soliciting dealer arrangements in Canada. We commend the CSA for exploring the issues related to soliciting dealer arrangements and the potential for guidance or rules to ensure the integrity of the tendering and voting process by securityholders. While the practice in the context of proxy fights in Canada has been controversial, it does not violate the law. We applaud you for considering how the practice's failure in the court of public opinion should influence the regulator's approach and weigh on the public's interest. In the past we have been critical of regulators who play the role of a police officer watching a street fight, only to intervene once a victor has been declared and the dust has settled. We hope to see that change.

Kingsdale Advisors is the proxy fight specialist in Canada having acted in more proxy contests than any other advisors combined. We have solidified our position as the most trusted advisor to management and boards because we reliably deliver the results our clients want, no matter how big the challenge. In obtaining that position, we have developed a unique understanding of the proxy voting system and pioneered new approaches to ensure our clients win.

HISTORY OF PROXY FIGHT INNOVATION: KINGSDALE HAS BEEN A KEY PLAYER IN ALL PROXY FIGHTS WHERE SOLICITING DEALER ARRANGEMENTS HAVE BEEN USED IN CANADA

Kingsdale holds the unique position of being involved in and having advised on every instance where soliciting dealer arrangements have been used in a proxy fight in Canadian history. The shareholding system is renowned for the barriers it throws up for issuers, bidders or shareholders to contact retail objecting beneficial owner (OBO) shareholders directly. With this, comes the drive to look for new and innovative ways to penetrate this system.

It is worth noting we also advised on more M&A deals in the last 15 years than any other shareholder advisory firm or proxy solicitor. We have seen the use of soliciting dealer arrangements migrate from usage in takeover bids conducted via a tendering process to transactions conducted by way of a shareholder vote. Within the latter category, we have seen soliciting deal arrangements further move from being used in board supported and recommended transactions to ones where a board has a conflicted or entrenched position. Even within the M&A context, arrangements have gone from compensating brokers for their time to reach out to shareholders, to compensating them to help achieve a particular result.

This is important because we understand the main differentiator between the use of solicitor dealer arrangements in transactions vs. proxy fights: In the former, a recommendation to tender to an offer or vote for a plan of arrangement is made by an unconflicted sub-committee of independent directors of the board, the basis for which is grounded on a relatively empirical and objectively verifiable set of facts, specifically the price the offeror is prepared to pay compared to the intrinsic value of the company and the availability of superior strategic alternatives, including the "go it alone" alternative.

In the latter, a vote appeal is made by a conflicted set of directors who are interested in self-preservation, have access to corporate funds, and base their views on highly subjective data points such as how they think they are doing in their roles and how well they could do going forward. Equally subjective in a proxy fight scenario are the merits of the dissident's nominees and their likely contribution to, or disruption of, the board. In both cases, caught in the middle you have brokers who have been placed in a position of trust by their clients, expecting them to act in the best interest of the client, not the broker. In most cases the broker is not qualified to assess the relative merits of the company vs. a dissident slate and accompanying business plan, but certainly has an incentive to recommend one over the other when a soliciting dealer arrangement is in place.

By our count, soliciting dealer arrangements have been used in excess of 40 times in the context of M&A and three times in proxy fights.

Four of those cases –three proxy fights and a recent hostile bid– are worth expanding on given our strategic advisory role in each.

- **2012 – Octavian Partners LP vs. EnerCare Inc.** Only 12 days prior to the annual meeting, EnerCare announced it intended to pay a fee of $0.05 for each share voted by shareholders against Octavian's board nominees provided that a minimum of 1,000 shares were voted subject to a minimum fee of $100 and maximum of $1,500 per account. Octavian immediately hit back accusing EnerCare of "an extraordinary abuse of power and waste of company resources that highlights the lengths to which the current directors will go to further entrench themselves." EnerCare was majority held by retail investors –more than 75% of the shares were held by retail investors-- thus proving a worthwhile strategy to combat the considerable initial dissident support. Shareholders defeated Octavian's proposal by a vote of 19.1mm against the proposal vs 15.7mm for the proposal. Octavian, the largest shareholder, held 7.23mm shares –more than the 7.21mm shares held by the next 20 largest shareholders in aggregate.

- **2013 – JANA Partners LLC vs. Agrium Inc.** In the JANA/Agrium case both parties used boilerplate language in their proxy circulars to reserve the right to form a soliciting dealer group (a practice that has now grown common). The implementation by Agrium however was not press released and only came to light when an outraged shareholder was told by a confused broker that the shareholder would be paid for his vote. Kingsdale through its solicitation efforts worked to confirm with custodial back offices that a soliciting dealer arrangement was in place and obtained the greensheet. Agrium had agreed to pay brokers $0.25 for each share held by a Canadian voted in favour of the Agrium nominees, provided that the fee was no less than $100 (as long as they held a minimum of 30 shares) or no more than $1,500. Most importantly - no solicitation fees would be payable if the slate of Agrium nominees were not elected in full to the board. In the highly public discussion that ensued, Agrium attempted to make the case that they were simply trying to communicate with OBOs, while JANA argued that this was vote buying pure and simple. Much of the independent press, regardless of whether supportive of Agrium or JANA, found the vote buying to be inappropriate. All U.S. shareholders were surprised that soliciting dealer arrangements were and are even legal in Canada. Ultimately, Agrium saw all incumbent nominees elected, fending off JANA.

- **2017 – PointNorth Capital Inc. vs Liquor Stores N.A. Ltd.** Facing significant opposition, Liquor Stores set up a soliciting dealer group to pay brokers $0.05 for each share validly voted for each member of the Liquor Stores slate with a minimum of $100 and maximum of $1,500 to be paid per Canadian account. Fees would only be paid if each member of the Liquor Stores slate was elected to the board. Liquor Stores justified the action by indicating that this was done to try and reach the 49% of total shares held by retail OBOs who could only be contacted by their brokers. PointNorth quickly responded criticizing this as a vote buying and board entrenchment tactic given the conditions required for the payout. PointNorth also took the fight to the Alberta Security Commission (ASC) requesting that they terminate the arrangement as a matter of public interest. The ASC concluded however that there was insufficient evidence to demonstrate an abuse of the public interest as there were no clear examples of a broker offering advice that was contrary to their professional opinion and being passed along for financial benefit. The ASC was not the only influential group to weigh in on the matter; proxy advisor Glass Lewis was highly critical of the arrangement calling it "an inappropriate use of shareholder capital and a violation of basic corporate governance principles." Furthermore – multiple brokers advised they would not participate in the soliciting dealer group due to the contentious nature of the fight. In the end, the arrangement was ineffective in increasing support for Liquor Stores with six directors resigning days prior to the meeting, clearing the way for PointNorth to take control of the board.

- **2016 – Sprott Asset Management vs. Central GoldTrust (GTU) and Silver Bullion Trust (SBT).** Sprott launched a hostile tender for the silver and gold funds under the Central Fund of Canada. Both were almost exclusively comprised of long-term unknown retail OBOs. Many owned bullion funds for geo-political reasons and misunderstood the nature of their investment as one of owning actual bullion rather than actually owning units in a fund owning bullion.
    - The key economic case was that units of the trusts traded at a discount to NAV and that by tendering to Sprott that discount would be eliminated. In effect the typical tender offer premium was in fact the elimination of a discount. This message was not well understood by retail OBOs. After a drawn-out campaign that saw unitholders receive 14 mailings over 10 months, 49 press releases and with “unitholder fatigue” set in, Sprott announced a soliciting dealer arrangement that paid out to brokers whose clients tendered to the offer, and several U.S. brokerages participated for the first time.
    - Sprott paid a soliciting dealer fee of US$0.1358 per GTU unit and US$0.0448 per SBT unit deposited subject to a minimum fee of US$50.00 and a maximum fee of US$1,500.00 with respect to each beneficial unitholder of GTU or SBT and a minimum deposit of 300 GTU units or 1,000 SBT units.
    - On the final extension of the offer, Sprott included inclusion of a power of attorney to vote at a unitholders’ meeting. Ultimately Sprott secured over 50% tendered to GTU and used this to requisition and hold a unitholder meeting to replace the incumbent trustees, who then supported the subsequent plan of arrangement transaction which passed. Sprott negotiated with Central Fund that they would withdraw their offer on SBT if Central Fund did not contest the gold fund unitholders’ meeting.

GENERAL COMMENTS

In general, our view is there is nothing wrong with permitting soliciting dealer arrangements provided:

> a.) shareholders are properly informed of and understand the arrangement by those a shareholder has entrusted their money to, being both the issuer and the broker-dealer; and
>
> b.) the arrangement creates a level playing field in that solicitation is made evenly and fairly for any votes received and payment is not conditional on one side winning, thereby restoring the original basis behind broker payments – to compensate them for their time spent reaching out to securityholders.

The problem is that in each instance where soliciting dealer arrangements have been used in a proxy fight, neither has been true. Consideration should be given as to what constitutes adequately informing shareholders, including the time required to consider and digest the information. If you consider market practice for advance notice by-laws in Canada, 30 days may be appropriate.

Where one or both of these provisions are absent, the potential for abuse of shareholders, broker conflicts of interest, board entrenchment and exploitation of the integrity of the proxy voting process exists. Even in the thought experiment some have proposed, where a board would provide compensation for all votes received and not tied to outcome, brokers would still only see a greensheet from the incumbent –and therefore –conflicted board.

The bottom line: The only way to ensure the integrity of the shareholder voting system is to ban soliciting dealer arrangements within the context of proxy fights in their entirety. Shareholder outreach should be exclusively the purview of entities that are transparent in their task to contact and convince proxy voters and that lack a 'special relationship' with an investor that can be improperly exploited.

In the United States, broker-dealers have stringently avoided giving voting advice to their clients – even in the Agrium and Liquor Stores cases, U.S. broker-dealers chose not to participate. Two main reasons for this are a legal duty to act in the "best interests" of clients, a fiduciary standard, vs. to act "fairly, honestly and in good faith" in Canada, and a desire to avoid SEC filing requirements related to the proxy solicitation process.

SPECIFIC QUESTIONS

General

1. In what circumstances are soliciting dealer arrangements most typically used?

Transactions, and specifically plans of arrangement (POA), where the TargetCo needs $66^{2/3}$%, visibility is low (lots of retail OBOs), historical turnout is low and one or two negative shareholders could disproportionately impact the vote. Generally, issuers involved in POAs are equally concerned with participation and support given the two-step court process. It is much easier to get final court approval

if a majority of securityholders participated and supported the transaction. In a tender situation, similar attributes can be compounded by turnover in stock ownership as there is no record date.

2. What are the principal reasons for entering into soliciting dealer arrangements?

Expanding on the information provided in response to question 1, the appointment of the dealer manager is typically the financial advisor on file or the broker-dealer with the largest retail position. Often before a deal is announced the companies involved have had confidential discussions with larger securityholders in an effort to secure support or lock-up agreements. Failure to secure these or any perceived resistance to the deal is often a reason to drive participation higher to offset any perceived resistance. For this reason, it is common for soliciting dealer arrangements to be established some time after the deal is public and not from the outset.

3. Are soliciting dealer arrangement fees typically only paid in respect of votes "for" management's recommendations? Is that appropriate in all circumstances? Is there a reason to distinguish proxy contests in this regard?

In a POA there is only the management recommendation for the arrangement resolution. This applies to both mergers by way of POA and balance sheet or corporate restructurings by way of POA. In the latter, there is often more than one class voting but still a single management supported resolution.

The concept of paying for what management is recommending is also common in balance sheet restructuring where consent fees are now commonly paid only to those who voted for the arrangement (or indenture amendment) and not to all securityholders if the matter passes. In this case, the incentive goes directly to the securityholder and not the broker, eliminating the issue of conflict of interest.

There is a vast difference in proxy contests. In a transaction, a committee of independent directors, with advice from financial and legal advisors, comes to a recommendation for shareholders. Very often the independent opinions of the bankers (often more than one) in terms of valuation and strategic alternatives weighs heavily and the lawyers advise on fiduciary duty before a recommendation is made. It is possible for management to have a conflicted position due to change of control payments and/or new employment contracts, but the directors remain independent. In a proxy fight it is the directors' jobs on the line always (and often not the CEO). There is no possibility of being truly independent nor objective and use a dealer arrangement to shore up a result.

4. Are soliciting dealer arrangements important to the ability of issuers to contact retail OBOs?

That is their only real purpose. It is a different question if they are effective. It should be noted that while the arrangement is supposed to pay the broker for reaching out to the underlying OBO client and recommending a course of action, there is never any proof that any such outreach was undertaken. Rather, the back office of the broker simply claims all votes through their custodial position for payment. It is common that the sponsor (typically the issuer) of the arrangement has the right to inspect evidence, but the reality is there generally is no evidence kept that links the call to the vote. Dealer arrangements are particularly open to abuse by brokers with discretionary authority who do not require client instructions and can act entirely in their own interests. Discretionary accounts are common in the OBO space, particularly high net worth where voting entitlements are highest amongst retail shareholders.

Investment dealers and dealing representatives

8. How can investment dealers and dealing representatives participating in a soliciting dealer arrangement in respect of a proxy contest ensure compliance with the proxy solicitation rules?

One should first ask if they are qualified to provide advice on director elections as this is not a core competency of brokers. Neither the broker nor the back office make voting recommendations in a routine meeting nor on other governance matters. One must ask, what qualifies them to opine on director qualifications or the case for change in a contested situation?

Brokers have access to the voting control numbers for underlying clients. It would be illegal to vote a client position (without discretionary authority) without voting instructions, but almost impossible to prove if a broker either voted without instructions or overrode those instructions. For beneficially held positions there is no audit trail from individual accounts to the custodial position. It is worth asking if any compliance department could prevent a rogue broker from abusing the system.

In an investment situation, the brokers are supposed to familiarize themselves with the financial metrics and risk statements and compare them to the client's stated investment objectives and risk appetite before making any recommendation to clients. Brokers are not qualified to provide advice on contested elections and there is no 'suitability' benchmark to temper their fee based incentive.

9. Are investment dealers and/or dealing representatives involved in proxy contests where a proxy solicitation firm has been retained?

Yes . To expand on the commentary we have provided earlier on the three cases where they have been used, it is important to note the different roles broker-dealers have than a proxy solicitation firm. In addition to the fact that brokers are in a position of trust and do not necessarily disclose they are incented to secure and achieve a particular vote outcome, proxy solicitation firms openly disclose whose interests they are acting in.

10. Do you believe that an investment dealer or a dealing representative has a responsibility to encourage its client to respond to proxy solicitations (only value in POA, not generally), rights offerings (value), take-over bids (value) or other corporate transactions such as conversion of convertible securities (value)?

While we believe the responsibility exists in the case of POAs, rights offerings, take-over bids, and other corporate transactions, this is a matter for IIROC and must distinguish between encouraging *a* response vs. encouraging *a desired* response. None of these make money for brokers so they have zero interest and do not believe their fiduciary duty extends beyond investment recommendations. Rights offerings, take-over bids and conversions all have valuation issues for the holders but are voluntary events. The broker's only duty is to make clients aware. Proxy solicitations outside of transactions or restructurings are not considered value situations. The whole brokerage industry has been squeezed by online self-directed accounts (explicitly no advice given) and shrinking brokerage fees. There is more money to be made in selling packaged products than in providing any level of broker advice.

Issuers

11. Are there circumstances in which you think it would be contrary to the public interest or inconsistent with a board of directors' fiduciary duties for an issuer to

a. ***enter into a soliciting dealer arrangement?*** Where director elections or director compensation is being voted on and the broker fee is based on a desired outcome (i.e. no dissidents elected). This forces the broker into a risk position (not being paid for time) and also strains broker fiduciary duty.

b. ***retain a proxy solicitation firm?*** Never.

12. Can a board of directors comply with its fiduciary duties if it pays soliciting dealer fees for all votes, including votes that are contrary to the board's recommendation as to what is in the best interests of the corporation?

Possibly but unlikely. Brokers would still only get the board's greensheet, not an alternative one from a dissident. On the positive side such an approach would preserve the underlying principles for formation of a dealer group: 1) that there is a significant retail OBO constituency and it is important they be informed; 2) that brokers are compensated for their time and in driving participation (and not support). It would remove a glaring conflict of interest. Boards that have used soliciting dealer groups to drive support (rather than participation) make the argument that their fiduciary duty extends to sustaining the status quo and that the current strategic path is in the best interests of shareholders. This argument is possibly over-reaching their fiduciary duty particularly when it also stifles the shareholder right and ability to hear both sides of the argument. Paying for all retail OBO votes reduces but does not eliminate the conflict. Banning soliciting dealer arrangements in contested situations is the only guaranteed way to eliminate conflicts.

13. Are there particular transactions which give rise to more or less concern with respect to the use of soliciting dealer arrangements, e.g.,

a. a take-over bid tender, Low concern unless the board is not majority independent and recommending rejection.

b. a securityholder vote in relation to a merger and acquisition transaction, Low concern unless management has material interests in the result not available to securityholders. If these exist they should be included in the greensheets.

c. a securityholder vote in relation to a merger and acquisition transaction, where the fee is contingent on the securityholder voting in favour of the transaction and/or the transaction being approved, Low concern unless management has material interests in the result not available to securityholders. If these exist they should be included in the greensheets. If proper process has been followed and the opinion is unconflicted there is no issue with paying for the supportive votes.

d. a securityholder vote in the context of a proxy contest, High concern.

or

e. a proxy contest, where the fee is contingent on the securityholder voting in favour of management's nominees and/or management's nominees being 1elected. Highest concern.

14. What type of communication and disclosure should an issuer make to securityholders respecting the existence of a soliciting dealer arrangement?

More than the boilerplate statement including "a soliciting dealer group may be formed". Information should be publicly released in a timely fashion including the terms of the soliciting dealer arrangement (including amount paid, desired result, etc.) and such information should be provided by brokers to clients in advance of providing them with solicitation information or a request for their vote.

CONCLUDING THOUGHTS

In our view, the responsibility of engaging shareholders is one that rests with issuers, not brokers, and does not simply start when a proxy contest requires it. Ongoing engagement with all levels of shareholders in and outside of a contested situation or transaction is a sign of good corporate governance and is illustrated in a regularly high turnout of votes at shareholder meetings.

It is important to note the views of influential proxy advisors Institutional Shareholder Services (ISS) and Glass Lewis. If the soliciting dealer fees are not conditional on favourable votes or outcome of the voting results, and are for the legitimate use of encouraging more vote participation from shareholders in uncontested meetings, proxy advisors consider such a practice generally acceptable. However, proxy advisors do not support solicitation dealer fees paid conditionally on favourable votes or outcome of the voting results, viewing such a practice as inconsistent with the basic tenets of shareholder democracy.

It is worth noting the timing of the announcement (or revelation) of the soliciting dealer arrangements in the examples cited. In the case of EnerCare, it was announced after the ISS recommendation fully in favour of management. In the cases of Agrium and Liquor Stores, ISS supported some of the dissident nominees. While we didn't know the exact date, the timing was likely after ISS' recommendation in both cases. Management will run into high risk if ISS is aware of the arrangement before issuing its recommendation.

Most, if not all, of the discussion regarding soliciting dealer arrangements has been focused on the issuers' use of the practice. Consideration should, however, be given to what would be appropriate in circumstances where an activist shareholder wishes to employ the tactic. Unlike a board who will be using the company's coffers to fund its campaign, the fact is an activist shareholder will be funding the campaign on their own. If an activist were to employ such a tactic, does this create an unfair advantage that new guidance or rules should allow a company to match? As noted, while not in the context of a proxy fight, this was done in the case of Sprott vs. Central GoldTrust and Silver Bullion Trust where there was clear evidence that inactive retail OBOs were preventing an economically sound offer from being contemplated and there was an inverse case of the dissident having potentially deeper pockets.

We thank you for the opportunity to provide you with our comments. Should you wish to discuss any of these points further or seek additional background on the practical application and implication of changes related to the use of soliciting dealer arrangements please feel free to contact Amy Freedman, CEO at 416-867-4557 or afreedman@kingsdaleadvisors.com.

Sincerely,

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Executive Chairman and Founder
Kingsdale Advisors

Amy Freedman
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Kingsdale Advisors