WeirFoulds LLP

WeirFoulds Securities Law Review

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By Michael Dolphin,

Our coverage is succinct and targeted to serve the needs of issuers and their advisors. For more detailed information on our service offerings, please visit us online at weirfoulds.com.

Recent developments include:

- TSX releases guidance with respect to majority voting policies and advance notice policies
- Impact of the 2016 changes to the Canadian take-over bid regime
- OSC draws the line on private placements during proxy contests in the Eco Oro decision
- Securities Commission staff raise the bar for conflict transactions
- Exempt market dealers banned from prospectus offerings

TSX RELEASES GUIDANCE WITH RESPECT TO MAJORITY VOTING POLICIES AND ADVANCE NOTICE POLICIES

On March 9, 2017, the Toronto Stock Exchange ("**TSX**") published Staff Notice 2017-001 (the "**Notice**") providing guidance with respect to the following Sections of the TSX Company Manual (the "**Manual**"): (i) the majority voting requirement in Subsection 461.3 ("**Majority Voting Requirement**"), and (ii) the use of advance notice policies in the context of director election requirements in Subsections 461.1-461.4 ("**Director Election Requirements**").

Majority Voting Requirement

Majority voting was introduced to improve corporate governance standards in Canada by providing a meaningful way for security holders to hold individual directors accountable. TSX believes that the Majority Voting Requirement introduced on June 30, 2014 enhances transparency and improves the governance dialogue between issuers, security holders and other stakeholders. To comply with the Majority Voting Requirement, issuers are required to adopt a majority voting policy (a "Majority Voting Policy"), unless they otherwise satisfy the Majority Voting Requirement in a manner acceptable to TSX.

TSX conducted a review of 200 randomly selected Majority Voting Policies (the "Reviewed Policies") from TSX-listed issuers to assess compliance with the Majority Voting Requirement. Through its review TSX identified a number of deficiencies in the Reviewed Policies, as well as inconsistencies with the policy objectives of the Majority Voting Requirement

In response to these deficiencies, the Notice provided guidance and outlined the TSX's expectations as to how listed issuers should comply with the Majority Voting Requirement.

- Issuers are expected to ensure that their Majority Voting Policies have the effect of requiring a director to tender his or her resignation immediately if not elected by a majority of votes cast.

- To be compliant with the Majority Voting Requirement, Majority Voting Policies must state that the Board will accept the director's resignation within 90 days, absent *exceptional circumstances*.
- "*Exceptional circumstances*" are expected to meet a high threshold, such as the issuer would not be compliant with corporate or securities law requirements, applicable regulations or commercial agreements regarding the composition of the Board as a result of accepting the resignation; the director is a key member of an established, active Special Committee which has a defined term or mandate (such as a strategic review) and accepting the resignation of such director would jeopardize the achievement of the Special Committee's mandate; or majority voting was used for a purpose inconsistent with the policy objectives of the Majority Voting Requirement.
- TSX does not consider the following factors to be "*exceptional circumstances*", especially given their reoccurring nature and that such information is typically available to security holders when they make their voting decision: the director's length of service, qualifications, attendance at meetings, experience, or contributions to the issuer.
- TSX considers the phrase "*participate in any meeting*" to include attendance at the meeting. A director must not attend any part of a meeting of the Board or any sub-committee of the Board at which his or her resignation is discussed or a related resolution is voted upon. If they must attend such meeting in order to satisfy quorum requirements, then they must not speak or otherwise participate in the meeting.

Issuers should assess their Majority Voting Policies in light of the Notice. Majority Voting Policies that are not compliant with Subsection 461.3 should be amended as soon as practicable and sufficiently in advance of the next meeting of security holders at which directors are elected to allow nominees to comply.

Advance Notice Policies

For the purposes of the Notice, "Meeting" means any meeting of security holders of a TSX-listed issuer, whether annual or special, at which directors are elected.

The Director Election Requirements were adopted to strengthen the Canadian corporate governance regime and support the integrity and reputation of the Canadian capital markets. The avoidance of these policy objectives through by-law provisions or other means that have the effect of frustrating or circumventing the Director Election Requirements will be considered a failure to comply with such requirements.

TSX recognizes that nominating directors for election to the Board during or shortly before a Meeting may be viewed as unreasonable since it may not provide security holders with sufficient time to evaluate the new information and it may be unexpected by security holders, particularly those who have granted discretionary authority to a proxy. TSX also recognizes that issuers require adequate notice of nominees for election to the Board.

Many TSX-listed issuers have chosen to adopt policies and by-laws prescribing timeframes and procedures to nominate directors for election to the Board ("**Advance Notice Policies**"). TSX randomly selected 25 Advance Notice Policies adopted by TSX-listed issuers for review and identified a number of concerns in connection with their use. In response to these deficiencies, the Notice provided guidance intending to clarify TSX's expectations with respect to the Director Election Requirement and the use of Advance Notice Policies.

TSX believes that the current guidelines published by Glass, Lewis & Co., LLC and Institutional Shareholder Services Inc. for Canada regarding notification periods prior to a Meeting to nominate directors (each, a "**Notice Period**") in Advance Notice Policies are generally satisfactory. TSX considers the following examples as consistent with the policy objectives of the Director Election Requirement:

- For an annual and general Meeting ("**AGM**") → a Notice Period ending at least 30 days before the Meeting date.

- If the AGM is to be held on a date that is less than 50 days after the first public announcement of the date of the AGM (the "**Notice Date**") → a Notice Period of at least 10 days following the Notice Date.
- In the case of a special Meeting called for the purpose of electing directors (whether or not also called for other purposes) → a Notice Period of at least 15 days following the Notice Date.
- Requirements and procedures imposed on a nominating security holder or a nominee director that are not more onerous than requirements for management and Board nominees.

Issuers should assess their Advance Notice Policies in light of this Staff Notice. Advance Notice Policies that are not compliant with the Director Election Requirements should be amended as soon as practicable and sufficiently in advance of the next meeting of security holders at which directors are elected.

For further information, please see TSX Staff Notice 2017-0001 (March 9, 2017).

IMPACT OF THE 2016 CHANGES TO THE CANADIAN TAKE-OVER BID REGIME As discussed in a previous WeirFoulds Securities Law Quarterly (March 31, 2016), the CSA published substantial changes to the take-over bid rules which came into force on May 9, 2016 under National Instrument 62-104 – Take-Over Bids and Issuer Bids ("**NI 62-104**").

Under this take-over bid regime, all non-exempt take-over bids are subject to the following requirements:

- A minimum tender requirement of more than 50% of the outstanding securities that are subject to the bid, excluding securities owned by the bidder itself or any person acting jointly or in concert with the bidder.
- A minimum deposit period of 105 days, which may be shortened in certain outlined circumstances to no less than 35 days.
- An extension period of a minimum of 10 days after the Minimum Tender Requirement is satisfied and all other conditions are met.

The main impact of the changes to the take-over bid regime was to extend the time required for unsolicited take-over bids to remain open. Under the old regime, a non-exempt take-over bid could remain open for as little as 35 days and was not subject to any minimum tender requirements or the extension requirement. In practice, this extension to the process has had an impact on the financing aspect of bid take-overs.

Under applicable Canadian securities laws, a bidder seeking to effect a take-over bid must make adequate arrangements before launching the bid to ensure that the required funds will be available to make full payment for the securities that are the subject of the bid. Essentially, a take-over bid cannot be subject to a financing condition. In light of the minimum deposit period being extended to 105 days from 35 days under the old regime, bidders and lenders now need to find a way to reconcile bidders needing a financing commitment for the elongated required period of time that will allow them to complete the take-over bid and lenders wanting to limit the commitment period in order to limit their exposure to changing rate environments. A longer commitment period, while now necessary, exposes lenders to fluctuations and instability. Practically speaking, this has caused significant increases to the costs of financing for unsupported/unsolicited take-over bids in the form of higher commitment fees and longer periods of ticking fees, which are payable to compensate lenders for their commitment from the date the commitment letter is signed to the earlier of the closing date and expiration of the commitment. Further, with a longer commitment period, it is also likely that lenders will insist on flexibility in the language of their commitment papers to allow them to change the amount, pricing, structure, yield, tenor, conditions and other terms of the financing if they deem it necessary.

In addition to the financing terms themselves, given the cost of preparing credit documentation and related security, a longer bid period also tends to result in delayed preparation of the credit documents as bidders may not want to incur the costs of negotiating these documents too far in advance of the end of the bid period. Despite the above, if at any time the unsolicited take-over bid turns friendly based on target board recommendation, the bid period may be accelerated to as little as 35 days, inclusive of any time passed,

adding significant pressure on those dealing with the financing to prepare the necessary documents quickly. Strong communication and regular updates between all parties involved are essential in minimizing this stress.

IMPLICATIONS OF THE ECO ORO DECISION ON PRIVATE PLACEMENTS DURING PROXY CONTESTS

On June 16, 2017, the Ontario Securities Commission ("**OSC**") released reasons for their decision in In the *Matter of Eco Oro Minerals Corp.*. The reasons provide guidance with regards to private placements of voting securities in the context of proxy contests and expressed the OSC's views on the public interest in ensuring fairness in contested shareholder meetings.

Background and OSC Decision
In February 2017 Eco Oro Minerals Corp. ("**Eco Oro**") was involved in a proxy contest with dissident shareholders who sought to replace the incumbent board of directors at a requested shareholders' meeting then scheduled for April 2017. During this proxy contest, the board of Eco Oro approved a private placement of common shares (the "**New Shares**") to four recipients (the "**New Share Recipients**") who collectively held approximately 41% of the outstanding common shares at the time. It is important to note that the New Share Recipients had been solicited by Eco Oro management to deliver letters in support of the incumbent board and had agreed to do so. Further, the issuance of the New Shares resulted in the New Share Recipients increasing their ownership to approximately 46% of the outstanding common shares.

Before the record date for the requested shareholders' meeting, the TSX conditionally approved the private placement. The TSX did not require prior shareholder approval for the private placement, and the issuance of the New Shares was completed without advance public disclosure, shortly before the record date for the meeting. This conditional approval was based on the TSX's determination that the private placement did not "materially affect control of Eco Oro" as the issuance of the New Shares would not result in "a single shareholder, or a combination of shareholders acting together, holding more than 20% of the outstanding voting securities".

The dissident shareholders applied to the OSC for a review of the TSX decision that approved the private placement. During the OSC hearing, it was determined that the TSX was not informed about the pending proxy battle and the upcoming special meeting requested by the dissident shareholders. This omission was crucial as both sides of the issuer were not far apart coming into the proxy contest. An extra five percent support could have been enough to "tip the balance" and arguably "materially affect the control of Eco Oro". As the TSX rules require that shareholders approve any transactions that materially affect the control of the issuer, the OSC concluded that the Eco Oro shareholders should have voted before the private placement closed. The OSC rejected the argument that a regulatory requirement of a shareholder vote on a new share issuance can be ignored, absent illegal conduct of the recipients of the shares issued, simply because the new share issuance has closed and issued an order setting aside the TSX decision. As a result of the OSC order, the New Shares were cease-traded and shareholder approval was required for the issuance of the New Shares unless such issuance was reversed by Eco Oro. Further, the OSC ordered that until shareholder approval was obtained, Eco Oro could not consider the New Shares to be outstanding for voting purposes. In the event that shareholder approval was not obtained, Eco Oro was to take all necessary steps to reverse the issuance of the New Shares.

Implications

In light of the OSC's decision, issuers and their advisors should be wary of the following:

- TSX may review the facts and circumstances surrounding a private placement with more scrutiny and not just rely on the submissions of the issuer. Issuers and their advisors are advised to be diligent in disclosing all relevant facts to TSX and be prepared to respond to any follow up questions and requests.
- TSX may reduce the circumstances in which they permit a private placement to close without announcing the placement in advance, prescribing some sort of waiting period or/and obtaining shareholder approval.
- The bright-line test, being the creation of a 20% shareholder, previously used by TSX may no longer apply as seamlessly; TSX

is likely to consider other factors including the immediate impact on voting dynamics.

For more information, please see the OSC's [Reasons for Decision] (June 16, 2017).

SECURITIES COMMISSIONS INCREASE SCRUTINY FOR CONFLICT TRANSACTIONS

On July 27, 2017, the staff of the securities regulatory authorities in each of Ontario, Alberta, Manitoba and New Brunswick (collectively, the "**Staff**") published a Staff notice (the "**Staff Notice**") in which they advised market participants of their proposed approach to review and oversee transactions subject to Multilateral Instrument 61-101 Protection of Minority Security Holders in Special Transactions ("**MI 61-101**").

In this Staff Notice, "material conflict of interest transaction" referred to insider bids, issuer bids, business combinations and related party transactions, each as defined and within the scope of MI 61-101, that give rise to substantive concerns as to the protection of minority security holders. MI 61-101 establishes a securities regulatory framework that mitigates risks to minority security holders when a related party of the issuer, who may have superior access to information or significant influence, is involved in a material conflict of interest transaction.

The principles underlying MI 61-101 consist of the notion that all security holders be treated in a manner that is fair and that is perceived to be fair. MI 61-101 implements these principles through procedural protections for minority security holders that include formal valuations, enhanced disclosure, and approval by a majority of minority security holders. MI 61-101 also mandates the involvement of a special committee of independent directors in specific circumstances.

Reviews of Special Transactions

The objective of Staff's review program is to identify and resolve issues in "real time", before a transaction is approved by security holders or closed, so as to reduce the risk of harm to minority security holders. This real-time review begins upon the filing of a disclosure document, such as an information and bid circular or a press release and material change report filed in relation to transactions that are exempt from the minority approval requirements of MI 61-101. Throughout their review, Staff may contact issuers or their advisors with detailed questions and requests for supporting information.

Where Staff identify non-compliance or public interest concerns, they may seek corrective disclosure or other appropriate orders, and may even take enforcement action in certain circumstances, such as where they believe that materially misleading disclosure has been made. Although Staff recognize the time constraints associated with transactions, they may apply a temporary cease-trade or other appropriate order in respect of a proposed transaction if they believe it to be in the public interest to do so. In order to avoid the risk of such delay, boards of directors are advised to ensure that the issuer's disclosure complies with MI 61-101.

Special Committees

The Staff Notice also provides guidance regarding Staff's expectations of the active role to be played by special committees of independent directors in the context of material conflict of interest transactions. While the use of a special committee of independent directors is mandated by MI 61-101 only in the case of insider bids, Staff are of the view that a special committee is advisable for all material conflict of interest transactions. In particular, Staff believe that a special committee of independent directors should be formed and engaged early in the process as it may provide important protection for minority security holders in connection with all steps including negotiation, review, and recommendation of a material conflict of interest transaction.

Although special committee mandates will be tailored within the context of the specific transaction, Staff generally expect that a special committee mandate will include the ability to do the following:

- either negotiate or supervise the negotiation of a proposed transaction, rather than simply review and consider it,
- consider alternatives to the proposed transaction that may be available, including maintaining the status quo or seeking other transactions that would enhance value to minority security holders,
- make a recommendation regarding the proposed transaction, or, if it does not, provide detailed reasons why not, and
- hire its own independent legal and financial advisors, without any involvement of, or interference from, interested parties or their representatives.

It is important to note that where a board of directors or a special committee discloses its reasonable beliefs as to the desirability or fairness of a material conflict of interest transaction, such disclosure should address the interests of minority security holders and not be limited to whether the transaction is in the best interests of the issuer. Staff believe that the best interests of the issuer and its minority security holders will generally not be in conflict when considering these transactions; however, if in the view of the board of directors there is such a conflict, Staff expects that the disclosure document for the transaction will explain the conflict and how it was addressed by the board of directors in reaching its decision to propose the transaction for approval by minority security holders.

Enhanced Disclosure

Enhanced disclosure requirements constitute one of the fundamental minority security holder protections imposed by MI 61-101. They are intended to address the asymmetry of information that may exist when minority security holders are asked to consider and approve, or tender into, a material conflict of interest transaction. Staff reminds issuers that circulars provided to security holders must comply with MI 61-601 in addition to the requirements of any other applicable securities legislation such as National Instrument 62-104 Take-Over Bids and Issuer Bids and Form 51-102F5 Information Circular.

Staff believes that disclosure for a material conflict of interest transaction requires a thorough discussion of:

- the review and approval process,
- the reasoning and analysis of the board of directors and/or special committee,
- the views of the board of directors and/or special committee as to the desirability or fairness of the transaction,
- reasonably available alternatives to the transaction, including the status quo, and
- the pros and cons of the transaction.

Staff also identified problems with respect to disclosure of the background to and approval process for a transaction, including:

- inadequate disclosure of the context and background to a proposed transaction,
- failure to provide a meaningful discussion of the board of directors' or special committee's process and their rationale for supporting a proposed transaction,
- failure to provide disclosure of dissenting views of directors in respect of a transaction, and
- overly one-sided disclosure regarding a recommended transaction that did not identify potential concerns with the transaction or available alternatives to the transaction.

Staff believes that the enhanced disclosure requirements under MI 61-101 presuppose that an effective process has been undertaken so that the board of directors is able to appropriately inform security holders as to the desirability or fairness of the transaction proposed to them.

Fairness Opinions

The Staff Notice states that applicable securities legislation does not require a reporting issuer to obtain a fairness opinion as a condition of proceeding with a material conflict of interest transaction. It is the responsibility of the board of directors and any special

committee to determine whether a fairness opinion is necessary. Staff have also deferred to boards of directors and special committees as to the appropriateness of financial arrangements for the engagement of an adviser to provide a fairness opinion, including the payment of a success fee.

Where a fairness opinion is obtained for a material conflict of interest transaction, Staff believe that the disclosure document should:

- disclose the compensation arrangement, including whether the financial advisor is being paid a flat fee, a fee contingent on delivery of the final opinion, or a fee contingent on the successful completion of the transaction,
- explain how the board or special committee took into account the compensation arrangement with the financial advisor when considering the advice provided,
- disclose any other relationship or arrangement between the financial advisor and the issuer or an interested party that may be relevant to a perception of lack of independence in respect of the advice received or opinion provided,
- provide a clear summary of the methodology, information and analysis (including, as applicable, financial metrics, and not merely a narrative description) underlying the opinion sufficient to enable a reader to understand the basis for the opinion, without overwhelming security holders with too much information, and
- explain the relevance of the fairness opinion to the board of directors and special committee in coming to the determination to recommend the transaction.

Staff refers market participants to Rules 29.21 and 29.24 of the Investment Industry Regulatory Organization of Canada, as well as Standard No. 510 of The Canadian Institute of Chartered Business Valuators, which may apply to the party providing a fairness opinion, or, if not, set out a reasonable approach to meeting the appropriate standard for fairness opinions.

For further information, please see Multilateral CSA Staff Notice 61-302 (July 27, 2017).

EXEMPT MARKET DEALERS BANNED FROM PROSPECTUS OFFERINGS

On July 27, 2017 the Canadian Securities Administrators (the “CSA”) published a notice of amendments to National Instrument 31-103 – Registration Requirements, Exemptions and Ongoing Registrant (“**NI 31-103**“) and its companion policy (the “**Amendments**“). Pursuant to the Amendments, exempt market dealers (“**EMDs**“) may not participate in offerings of securities under prospectuses (a prospectus distribution) in any capacity, including as underwriters and selling group members, including securities underlying special warrants that are qualified by a prospectus.

The Amendments do not have any impact on the ability of an EMD to act as a dealer or underwriter in a distribution by any issuer, including a reporting issuer, if the distribution is being made under an exemption from the prospectus requirement (a prospectus-exempt distribution). Despite criticism about the negative impact of the Amendments, the CSA takes the view that the investment dealer category or the mutual fund dealer category, where applicable, are the appropriate dealer registration categories for prospectus distributions.

EMDs are not permitted to distribute “prospectus-qualified securities” to an exempt market purchaser in the sense that the specific securities that are being distributed to the exempt market purchaser are being distributed under a prospectus and are therefore “prospectus-qualified” securities. However, an EMD may distribute “prospectus-qualified securities” to an exempt market purchaser in the sense that the specific securities that are being distributed to the exempt market purchaser in reliance on a prospectus exemption are of the same class of securities as are being distributed to other investors through, for example, an investment dealer in a contemporaneous prospectus offering. For clarity, for prospectus deals, EMDs may participate in concurrent private placements in which their clients receive securities subject to a statutory hold period rather than freely tradeable securities under the prospectus.

The Amendments came into force on December 4, 2017. Canadian-registered EMDs should evaluate their current distribution

practices to ensure appropriate compliance with these new restrictions.

For further information, please see [Notice of Amendments to National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations](#) (July 27, 2017).

SECURITIES PRACTICE

WeirFoulds' extensive experience enables us to advise on the operation and regulation of markets, both in Canada and abroad. We represent issuers, securities dealers and advisors, underwriting syndicates, financial institutions, lenders, investors, and venture capitalists, as well as foreign issuers and investors in the Canadian and US financial markets. We provide legal services to public and private companies, and to governmental organizations throughout Canada, to assist in entering and resolving matters related to capital markets, restructuring, and mergers and acquisitions. In addition, with the assistance of our litigation lawyers, we provide expert litigation support for a wide range of matters involving securities regulation.

The information and comments herein are for the general information of the reader and are not intended as advice or opinion to be relied upon in relation to any particular circumstances. For particular application of the law to specific situations, the reader should seek professional advice.

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