Goodmans LLP Update

Corporate Securities Law

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Advance Notice Policies on the Rise

As shareholder activism increases in Canada, the mechanics of proxy disputes are becoming increasingly refined and more frequently tested. In the recent decision of *Northern Minerals Investment Corp. v. Mundoro Capital Inc.*, 2012 BCSC 1090, the Supreme Court of British Columbia considered two of the tools used by issuers in connection with proxy contests:

- the implementation of an "advance notice policy", and
- the postponement of a shareholder meeting.

In sustaining both initiatives by the Mundoro board, the court reaffirmed the authority of boards to pursue such initiatives – providing commentary on the principles that should inform courts' approaches to the use of such tools in proxy fights and the key factors that may influence the courts' views going forward – and suggesting an inclination to support advance notice by-laws and policies as a means of enhancing informed shareholder choice.

Advance notice by-laws and policies, generally speaking, require that advance notice be given to an issuer of shareholder proposals relating to the nomination of directors. Although such policies are relatively new in Canada, they may have particular relevance in Canada, where dissidents have had the ability to effectively "ambush" a meeting of shareholders and replace some or all of the board of directors, provided they have sufficient votes to do so, by making a motion to nominate replacement directors at a shareholder meeting (without advance notice to the issuer or to its shareholders generally).

In Mundoro, one of the company's shareholders, Northern Minerals, had asked the court to, among other things, set aside an advance notice policy that had been adopted by the Mundoro board after it had mailed the information circular for the meeting of Mundoro shareholders and prevent the board from postponing the annual meeting after Northern Minerals had challenged the policy. The court declined to do either, suggesting that the board's "reasonable" behaviour with respect to the policy and postponement was a key factor in reaching its decision. The implications of this decision for both shareholders and boards are discussed below.

Background

Briefly, the relevant facts are as follows:

- On April 20, 2012, Mundoro gave notice of its annual general meeting scheduled for June 26, 2012.
- On May 22, 2012, Mundoro issued its management information circular for the meeting, which indicated that the business to be considered at the meeting was to receive financial statements, elect directors and reappoint the auditors.
- On June 11, 2012, Mundoro issued a press release announcing that its board had approved an advance notice policy, which, among other things, imposed a deadline by which shareholders were required to submit nominations for directors to be appointed at annual or special meetings.
- On June 14, 2012, Northern Minerals brought an application against Mundoro seeking, among other things, a declaration that the policy was unenforceable.
- On the same day, Mundoro issued a press release postponing the annual general meeting for approximately one month and indicating that shareholders would be asked to approve the policy at the postponed meeting.

In its application to the court, Northern Minerals challenged both the authority of the Mundoro board to implement the advance notice policy and to postpone the date of the meeting of shareholders.

The Decision

Northern Minerals argued that, under the British Columbia corporate statute, directors have only those specific powers granted to them by the statute and the company's articles, and that, because neither the British Columbia statute nor the Mundoro articles explicitly permitted the Mundoro board to implement the policy or postpone the shareholder meeting, the board had no authority to do so. Mundoro argued, firstly, that the articles reserved to the directors all residual powers of the corporation and, secondly, the British Columbia statute should be interpreted in a manner that afforded the directors the same breadth of powers available to

directors under the Canadian and Ontario corporate statutes. The court concluded that, notwithstanding certain idiosyncrasies of the British Columbia corporate statute, the Mundoro board did have the authority to implement the policy and postpone the shareholder meeting in this context.

Of particular interest is the court's response to Northern Mineral's argument that the advance notice policy diminished shareholder democracy in that it would deprive shareholders of their statutory right to elect directors. The court concluded there was no infringement on the rights of Mundoro shareholders and cited the following factors as evidence of the good faith of the Mundoro directors and the reasonableness of the policy:

- the policy was not being implemented with the intention to influence or preclude a proxy contest,
- the board had unfettered discretion to waive any requirement in the policy (suggesting that, if a shareholder disagreed with the application of the policy by the board, the shareholder would have an opportunity to ask the court to review the board's exercise of that discretion), and
- the policy was to be put to shareholders for approval and confirmation at the upcoming annual general meeting (albeit after the election of directors at that meeting).

While the court made clear that its conclusion was not a general endorsement of advance notice policies, and that each case will be decided on its particular facts, the court seems to suggest that such policies could be considered to be consistent with, and supportive of, shareholder rights, rather than a simple tool of board entrenchment, in its comments that:

> In this case it has not been established that the Policy is one that infringes shareholder rights. Rather, the Policy in fact ensures an orderly nomination process and that the shareholders are informed in advance of an AGM what is in issue. In doing so the Policy prevents a group of shareholders from taking advantage of a poorly attended shareholders meeting to impose their slate of directors on what could be a majority of shareholders unaware of such a possibility arising. The submission of the petitioner equates the "rights" of a small group of dissident shareholders with all shareholders of the company. The interests of the two groups do not necessarily coincide.

Implications

Although advance notice policies and by-laws have not yet been widely adopted by Canadian public issuers, the *Mundoro* decision may open the door for more boards to consider using them in the future. The decision suggests that advance notice policies or by-laws will need to be carefully crafted with a view to striking a reasonable balance between the shareholders' rights to replace a board and the board's rights to ensure that a fair process – with a particular focus on an informed shareholder vote – for the removal and replacement of directors is in place. In addition, activist investors in Canada will need to take the existence and potential for implementation of an advance notice policy or by-law into account – whether in respect of timing, the process for selecting nominees, or the use of the court process to challenge a policy or by-law when contemplating a proxy contest.

Please contact any member of our Corporate Securities Group to discuss the implications of this decision.