Goodmans LLP Update

Corporate Securities Update

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Shareholder Activism Defensive Tactics Attract OSC's Attention

Shareholder activism continues to evolve in Canada. As the tactics of activists have become increasingly sophisticated, boards have responded by expanding and refining their defensive tactics. A recent example is the growing popularity of contractual restrictions on transferring shares to certain classes of shareholders, including specific activists. This new strategy has attracted the attention of the Ontario Securities Commission (OSC) and may prompt regulatory intervention.

Share Transfer Restrictions – A New Defense to Shareholder Activism

Canadian public companies may restrict the transfer of their shares if the authority to do so is contained in their articles of incorporation, and both Canadian and U.S. companies have used shareholder agreements to prevent shareholders from transferring their shares to "activist investors". Initially, these restrictions simply prohibited a shareholder from transferring shares to anyone engaged in an activist campaign involving that specific issuer. More recently, issuers have broadened the restriction to prohibit any transfer to specifically identified activist investors including, in some instances, any investor included on published lists of activists.

These provisions are designed to make it more difficult for well-known activist investors to accumulate a significant ownership interest in the issuer, thereby presumably making it less likely that the issuer will be targeted by those investors.

The OSC's Concerns

In response to these developments, the OSC has expressed concern about "extraordinary actions by issuers that may deter or hinder shareholder activism that is otherwise compliant with corporate and securities laws." These concerns are consistent with the OSC's views on so-called "voting pills" (shareholder rights plans that prohibit shareholders who collectively own more than a specified percentage of shares from acting in concert with respect to their voting rights).

It is unclear whether the OSC will take steps to prevent broad restrictions on the transfer of shares to activist investors or other proxy contest defensive tactics such as voting pills. While the OSC's traditional enforcement tool – the "cease trade" order – may have limited utility in this context, the commission retains broad public interest powers to fashion appropriate remedies. The OSC is mandated to protect investors and to foster fair and efficient capital markets. If the ongoing legal "arms race" between activists and boards continues to escalate, the OSC may feel obliged to intervene to restrain tactics that it believes unduly prejudice shareholder rights.

The Future of Shareholder Activism in Canada

Canada is typically viewed as a "shareholder friendly" jurisdiction. Activist investors may have been emboldened by recent victories, as well as by a regulatory framework that makes it easier for shareholders to influence corporate governance, such as by requisitioning a shareholder meeting with as little as 5% of a company's shares. The use of share transfer restrictions as a defensive tactic against activism that is increasing in scope and sophistication may have limited effect where activists remain free to accumulate enough shares from unrestricted sellers on the public market to initiate a contest. Nonetheless, the tactic is testing unsettled areas of securities regulation, where the reaction of the OSC and other regulators cannot be accurately predicted. Issuers or activists who wish to deploy untested tactics should carefully weigh the risk of regulatory intervention before proceeding.

For further information regarding shareholder activism and corporate governance in general, please contact any member our Corporate Securities Group.

[1] Scott Deveau and Miles Weiss, "OSC Troubled by Ban on Share Resales to Activist Investors", The Globe and Mail (17 November 2015). www.theglobeandmail.com/report-on-business/osc-troubled-by-ban-on-share-resales-to-activist-investors/article27303510/