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Soliciting dealers in proxyland

By Neill May

Soliciting dealer arrangements have been often used in Canadian proxy contests and have been controversial, but the market until very recently had no guidance as to when Canadian securities regulators might intervene where such arrangements are used. "Soliciting dealer" has the sound of something potentially problematic. After all, solicitation is a criminal offence. And dealing can certainly describe criminal activity. But you cannot always judge improper conduct by the label, as any first-year law student who was at least briefly confused by the meaning of cockfighting can attest.

This summer, the Alberta Securities Commission in *Re PointNorth Capital Inc.* was asked to exercise its public interest jurisdiction to terminate a "soliciting dealer arrangement" used in the Liquor Stores N.A. Ltd. proxy contest. The soliciting dealer arrangement in that case was implemented by Liquor Stores, a publicly traded issuer, in the context of a formal proxy fight initiated by PointNorth Capital Inc., a significant shareholder.

A soliciting dealer arrangement involves a company agreeing to pay a cash commission to brokers for soliciting the broker's clients to take actions supportive of the company (in the case of a proxy contest, to complete proxies *in favour* of the company's position). Use of these arrangements has generated much attention; its use by Agrium Corporation during the proxy contest initiated by JANA Partners LLC, for example, generated considerable comment from many market participants. The issue centred on the regulator's public interest jurisdiction because there is no law prohibiting the use of soliciting dealer arrangements.

The logic of such arrangements, and concerns about their use, is reflected in the parties' positions in *Re PointNorth*. Liquor Stores argued (and PointNorth agreed) that communication with shareholders was challenging because many of the company's retail shareholders were objecting beneficial owners (shareholders who, in accordance with applicable regulations, declined to provide their contact information to the company and could, therefore, be contacted only by their brokers). The company, therefore, contended that the soliciting dealer arrangement was required in order to engage registrants to, in the company's words, ensure that shareholder democracy functions. PointNorth counter-argued that the arrangement could not be justified on the basis of enhancing shareholder participation where payment was only being made to brokers whose clients were supportive of company management, and further that the one-sided compensation structure created a conflict that impacted the advice brokers provided to their clients and amounted to "vote buying." The company responded that, because its board had concluded that PointNorth's plan was contrary to the company's best interests, it would be a waste of corporate assets to compensate brokers for votes cast in favour of that path. Liquor Stores also noted that there was significant precedent for soliciting dealer arrangements in Canadian proxy contests so that it was not breaking new ground.

In *PointNorth,* the Alberta Securities Commission decided not to intervene on public interest grounds. In doing so, it:

- determined that because there is a detailed legislative framework governing proxy solicitation, a stringent test that should be applied to determine whether conduct that is not specifically prohibited should be found to be contrary to the public interest, one which requires an applicant to demonstrate that the impugned conduct is "clearly abusive" of investors or the integrity of the capital markets;
- concluded that there was no evidence of the harm or potential harm required to support a determination of abusive conduct and that in particular there was no indication that brokers (who, in PointNorth's submissions, would have been converted into "hopelessly conflicted" partisan solicitors rather than objective advisors focused on their clients' interests) had actually changed their advice because of the potential for commissions; and
- effectively rejected the notion that soliciting dealer arrangements are inherently abusive of investors or the capital markets.

The *PointNorth* decision is unlikely to be the final chapter on this subject. Reasons include the widespread use and controversial nature of these arrangements, the potential for a different result if a complainant can lead to evidence of harm and the fact that the ASC did not express a broad perspective on the practice. Additionally, the ASC did not consider potential corporate law issues (which would have to be adjudicated by a court), such as whether the use of a soliciting dealer arrangement in a proxy contest may be inconsistent with the fiduciary duties of the directors or oppressive (in the sense of unfairly violating shareholders' reasonable expectation about how the company would conduct the proxy contest), and the regulators may choose to address the issue on the policy side.

Hopefully, it has been established that labelling won't affect the legal outcome. Otherwise, in a normal day, I'd be concerned about my exposure for rush-hour delay (trafficking), clutching to visions of a lottery win (harbouring), trying to drum up business (soliciting) and even charging my phone (battery). Because of my good taste, I won't make any reference to concern about administering noxious substances. CL

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