

## Corporate Securities Law

January 29, 2016

### Ontario Court of Appeal Clarifies Scope of “Promoter” Definition

The Ontario Court of Appeal decision in *Goldsmith v. National Bank of Canada*,<sup>1</sup> provides important guidance on the meaning of the term “promoter,” a significant characterization, as under Canadian securities laws a “promoter” can be liable for a public company’s misrepresentations in prospectuses and continuous disclosure documents. In *Goldsmith*, the Court established a framework for determining whether a person is a promoter, concluding that a “promoter” is someone who:

- “plays a vital role in the organization of or reorganization of an issuer’s business;”
- “played a driving role in founding an issuer, and consequently wields influence comparable to that of an officer or director;” or
- is “an active participant” or a “driving force” behind a reorganization or is at the very heart of the issuer and organization.”

Conversely, mere involvement in an issuer’s organization or reorganization is not sufficient for “promoter” status, “even if that involvement involves important services and support.”

Although the Court stated that each claim must be analysed on a case-by-case basis, lenders and advisors who are involved in the organization and reorganization of an issuer’s business can be comforted that unless they are acting beyond the normal scope of those roles and are playing a driving or vital role, as outlined, they should not be potentially exposed to statutory liabilities applicable to promoters.

#### Background

In *Goldsmith*, the plaintiff alleged misrepresentations in public documents released by Poseidon Concepts Corp. (“Poseidon”) in connection with a reorganization that separated Poseidon’s business segments (a tank rental business and an oil and gas exploration and production business) into two separate, publicly-traded corporations.

After Poseidon filed for protection from creditors, a series of class actions were commenced against Poseidon’s former directors and officers, its underwriters for a prospectus offering, its financial advisor, National Bank Financial Inc. (NBF), and Poseidon’s main commercial lender, National Bank of Canada (NBC). The *Goldsmith* decision deals with the plaintiff’s motion for leave to commence an action against NBC for secondary market misrepresentations.

Under the *Securities Act* (Ontario) (the “Act”) promoters are liable for secondary market disclosure where they knowingly influenced the release of a document or the making of a public statement containing a misrepresentation. The plaintiff claimed that NBC was a “promoter” of Poseidon because (i) it provided loans that were necessary for the reorganization, and (ii) was liable for the conduct of its wholly-owned subsidiary, NBF.

#### A Promoter Takes Initiative to Found, Organize or Reorganize A Business

The Act defines a “promoter” as:

...a person or company who, acting alone or in conjunction with one or more other persons, companies or a combination thereof, directly or indirectly, takes the initiative in founding, organizing or substantially reorganizing the business of an issuer.

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<sup>1</sup> 2016 ONCA 22 (“*Goldsmith*”)

# Goodmans<sup>LLP</sup> Update

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The Court considered the plain meaning of “promoter,” the context in which “promoter” appears in the Act and the purpose of the Act.

First, it rejected a broad interpretation proposed by the plaintiff. It held that “taking the initiative” cannot mean simply “influencing or participating with decision-makers.” The kind of “passive involvement” the plaintiff focussed on was “simply incompatible” with the words “taking the initiative.”

Second, the plaintiff’s interpretation of “promoter” was inconsistent with the legislative context in which the term “promoter” is used. For example, the Act defines “influential persons” by referring to promoters and other persons “who exercise meaningful control over a reporting issuer’s business,” such as directors or officers.

Finally, the plaintiff’s interpretation of “promoter” was “completely unconnected from the goals of protecting investors and deterring corporate misconduct” and “undermines the goal of fostering fair and efficient capital markets,” as it would impose potential liability on the ordinary, everyday activities of many capital market participants.

In that context, the Court held that NBC could not become a promoter “by providing a credit facility, even if it was essential for Poseidon’s liquidity during the reorganization.” Nor could it be a promoter because it “acquiesced” to the decision to spin off certain assets,

as this acquiescence was merely a “passive agreement... something conceived and implemented by others.”

The Court also rejected the plaintiff’s contention that NBC could be liable for NBF’s conduct as Poseidon’s financial advisor. Although NBF was directly sued in a separate action not before the Court in this decision, the Court reviewed the evidence the plaintiff relied on to characterise NBF as a promoter, finding it did not demonstrate that “NBF took a central or controlling role in the reorganization.”

While it may be possible that a plaintiff could in a different case present evidence to convince a court to grant leave for a misrepresentation claim against a lender or advisor as a promoter, the decision in *Goldsmith* confirms the evidence would have to demonstrate conduct and involvement with an issuer’s decision-making well beyond the customary services that these types of institutions provide when involved with the organisation and reorganisation of an issuer’s business.

Please contact any member of our Corporate Securities Group if you wish to discuss this case.