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Concept Capital Management Ltd. v. Oremex Silver Inc. – Ontario Court sets new record date for shareholders' meeting to prevent manipulation of voting process and orders appointment of independent Chair

In the context of a proxy fight, Brown J. of the Superior Court of Justice (Ontario) in *Concept Capital Management Ltd. v. Oremex Silver Inc.*[1] ("***Concept Capital***") had to consider three principal issues:

- whether a duly called shareholders' meeting was properly postponed or cancelled by the board of directors of Oremex Silver Inc. ("**Oremex**");
- whether the record date for the rescheduled meeting should be changed in order to prevent shares purportedly issued under a private placement from being voted; and
- whether an independent Chair should be required for the rescheduled meeting.

The Court upheld the postponement of the shareholders' meeting on the basis that it could not conclude, on a balance of probabilities, that the postponement was motivated by an improper purpose or bad faith. However, the Court did conclude that the motivation behind the directors changing the terms of a private placement was to dilute the shares of the existing shareholders in order to enhance the directors' prospects of being re-elected. This constituted improper conduct by the directors. Therefore, the Court set a new record date for the rescheduled

[1] 2013 ONSC 7820.

meeting in order to protect the Oremex shareholders from the directors' improper conduct, and also agreed to the appointment of an independent Chair.

The reasoning of the Court, particularly as it relates to the basis on which shares can be issued that may impact the results of a contested election of directors, builds on earlier case law and may prove helpful in future contested elections of directors.

Background

Oremex is a TSX Venture Exchange ("**TSXV**") listed mining company. The applicants, Concept Capital Management Ltd. ("**CCM**") and Sprott Asset Management LP, were holders of 18.9% of the issued and outstanding common shares of Oremex.

On August 2, 2013, Oremex began negotiations with Global Resources Investment Ltd. ("**GRIL**") to enter into a private placement transaction (the "**GRIT Transaction**") with Global Resources Investment Trust Plc ("**GRIT**"), an investment trust to be constituted by GRIL. By September 23, Oremex and GRIL had generally agreed upon the documents to implement the GRIT Transaction.

On August 9, Oremex received a letter from the TSXV stating that the trading of its shares would be suspended pending satisfaction by Oremex of certain reinstatement requirements, including the requirement to hold an annual general meeting – which meeting was overdue. Oremex responded to the TSXV on September 18, undertaking to issue a notice of its 2013 annual general meeting by September 30, and to hold the meeting by November 30. The TSXV replied acknowledging the undertaking and noting that Oremex had a rolling stock option plan that required yearly shareholder approval and thus would need to be approved at the upcoming meeting.

On September 26, CCM requisitioned a meeting of shareholders. On the same day, GRIL submitted an application to the TSXV

seeking approval of the GRIT Transaction. The TSXV said that the GRIT Transaction was precedent-setting, and needed time to study it before approval could be granted. As a result, Oremex and GRIL expected at the time that the GRIT Transaction would close on November 8. On September 27, Oremex called a shareholders' meeting for November 26 (the "**November Meeting**"), with a record date of October 25.

The directors of Oremex were required to mail out the management information circular for the November Meeting by November 4. They did not do so. On November 7, Oremex cancelled the November Meeting and called a meeting for December 31 (the "**December Meeting**") with a record date of November 29. In spite of the cancellation, the applicants issued a press release on November 8 announcing that the November Meeting would proceed as scheduled, and on November 11 mailed an information circular to all shareholders.

On November 13, Oremex agreed to extend the closing date for the GRIT Transaction to no later than November 30, in order to allow more time to receive regulatory approvals, including approval for listing of GRIT's ordinary shares on the London Stock Exchange (the "**LSE**"), which was an essential step in the GRIT Transaction.

On November 26, the applicants conducted a shareholders' meeting. The incumbent directors did not attend the meeting and did not recognize the validity of the meeting. The shareholders represented at such meeting voted overwhelmingly to remove the three incumbent directors and elect three new directors.

On November 28, GRIL and Oremex signed off on the amended deal documents for the GRIT Transaction. However, GRIL informed Oremex that the LSE listing would not be complete until about December 31. Nonetheless, on November 29, Oremex closed the GRIT Transaction in escrow, whereby Oremex purportedly raised $1.725 million in financing through the sale of common shares and warrants. As consideration for the purchase

of the Oremex securities, GRIT issued to Oremex 1,053,756 subscription receipts (the "**Subscription Receipts**") exercisable to acquire 1,053,756 ordinary shares of GRIT at £1.00 per share (the "**GRIT Shares**"). The Oremex securities were issued from treasury and Oremex held those securities in escrow for GRIT pending completion of the listing of GRIT's ordinary shares on the LSE. Pursuant to the terms of the Subscription Receipts, once the listing of the GRIT ordinary shares occurred, the Subscription Receipts would automatically be exercised to acquire the GRIT Shares. Oremex would then sell the GRIT Shares through the LSE to realize the contemplated proceeds.

On December 5, Oremex filed its proxy materials and management information circular for the December Meeting.

Court's Decision

Issue 1: Validity of the November Meeting

Whether the November Meeting was called in response to CCM's requisition

Historically courts have held that it is more difficult for a board to postpone a meeting that was properly called by shareholders, as opposed to a meeting called by the board. The applicants therefore argued that the November Meeting was a requisitioned meeting. Oremex was first informed (orally) on September 27 that CCM had requisitioned a special meeting of shareholders, two days after Oremex's counsel had confirmed with the TSXV that Oremex would issue a notice for an annual shareholders' meeting by September 27. Oremex only received the requisition on September 30, after it had already called the November Meeting. Therefore, the Court held that Oremex did not call the November Meeting in response to the requisition.

Whether Oremex was required to call another meeting in response to the requisition

Oremex argued that by calling the November Meeting, it fell within s. 143(3)(a) of the *Canada Business Corporations Act*[2] (the "***CBCA***") and therefore was not required to call another meeting in response to the requisition. Section 143 provides:

(3) On receiving the requisition referred to in subsection (1), the directors shall call a meeting of shareholders to transact the business stated in the requisition, unless

> (a) a record date has been fixed under paragraph 134(1)(c) and notice of it has been given under subsection 134(3).

The applicants argued that, as of the date of the requisition, Oremex did not meet the requirements under s. 143(3)(a) as it had not given notice of fixing the record date. *CBCA* s. 134(3) requires that notice of the record date must be given by advertisement in a newspaper, and Oremex's advertisement in a newspaper was not published until October 7, 2013 – well after receipt of the requisition.

Brown J. reviewed his own reasons in *Wells v. Bioniche Life Sciences Inc.*,[3] in which he extracted the principles underlying

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[2] RSC 1985, c C-44.

[3] 2013 ONSC 4871 [*Bioniche*]. In *Bioniche*, the board of Bioniche called an annual general shareholders' meeting for November 5, 2013. Wells, a dissident shareholder, sent a requisition in May 2013 for a special meeting to remove the directors of Bioniche. The board rejected this requisition on the grounds that it was under no legal obligation, and that it was not in the best interests of the corporation, to proceed with a special meeting given that an annual general meeting was already scheduled for November 2013. In June 2013, Wells commenced an application to the Ontario Superior Court of Justice seeking an order requiring a special meeting to be called, or to declare that Wells was entitled to call a special meeting for August 27, 2013. Brown J. held that the November 5 meeting met the "reasonable timeliness" requirement, as it was only some two months after Wells' proposed August 27 meeting, and there was weak evidence to support an urgent need to hold the meeting.

the s. 143(3) exemptions. The underlying policy is that, where no need exists for the requisitioned meeting, the directors are not required to call it. If the directors have already called a meeting where the shareholders will have an opportunity to vote on the subject-matter of the requisition, then there would be no need to call another meeting. However, the meeting must be scheduled for a time reasonably soon after the receipt of the requisition. Applying the principles from *Bioniche*, and notwithstanding the clear language under s. 143(3)(a) requiring the giving of notice of a record date before a company may rely on this exemption, the Court held that the course of conduct by the directors was sufficient to justify proceeding with the November Meeting and not calling another meeting. In reaching this conclusion, the Court noted that the November Meeting would have taken place within 60 days of the receipt of the requisition and the newspaper advertisement was run within 7 days of receipt of the requisition.[4] In addition, the applicants had treated the calling of the November Meeting as a sufficient response to CCM's requisition.

Whether the directors were entitled to postpone/cancel the November Meeting

With the postponement of the November Meeting, the new date of December 31, 2013 would be some 90 days following the receipt of the requisition. The Court affirmed that a board of directors has the authority to postpone an already called shareholders' meeting, but the fundamental question is whether the directors have exercised corporate power unfairly or inequitably in doing so.[5] The Court also reviewed prior case law

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[4] In *Concept Capital*, *supra* note 1 at para 31, the Court said that the advertisement was run within 5 days of receipt of the requisition. However, a review of the facts shows that it was run 7 days after the requisition was received.

[5] See *Ewart v Higson-Smith*, 2009 CanLII 38517 (ON SC). In that case, the board of a corporation adjourned a shareholders' meeting for less than a month, in response to a dissident group of shareholders holding 27% of the issued shares delivering blank proxies on the day before the deadline for submitting proxies, and confirming that they intended to propose an alternative slate of directors. The dissident shareholders sought relief under the

relating to the ability of a board to postpone a meeting called by shareholders and noted that any exercise by directors of their residual powers under *CBCA* s. 102 to cancel a shareholders' meeting called upon a requisition would be subject to close scrutiny by the courts. Such judicial scrutiny allows directors to postpone a shareholders' meeting to conduct the corporation's business in the best interests of the corporation and the shareholders, but also protects shareholders' rights to call a special meeting by providing relief where the directors' action was taken for an improper purpose or in bad faith.[6]

Oremex attempted to justify the postponement on three bases: 1) Oremex was focussing its efforts on continuing to seek a reinstatement for trading on the TSXV; 2) there was no longer need for special business to be contemplated at the meeting, as the TSXV had approved a fixed stock option plan in lieu of the rolling stock option plan; and 3) according to an affidavit submitted on behalf of Oremex, the TSXV advised Oremex that it was required to put in place the fixed option plan prior to holding the shareholders' meeting.

The Court dismissed the first justification as providing little link between the seeking of reinstatement on the TSXV and the date of the meeting. It also noted the weakness of the second justification, in light of the fact that the fixed option plan was adopted on October 10, which was 47 days prior to the November Meeting. With respect to the third justification, the Court was unwilling to make a conclusive assessment due to a limited evidentiary record.

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oppression remedy. The Ontario Superior Court of Justice allowed the adjournment, holding that it was not unfair or inequitable, as the dissident shareholders capitalized on the element of surprise and the adjournment allowed other shareholders more time to make a reasoned judgment with respect to exercising their proxies.

[6] See *Canadian Jorex Ltd v 477749 Alberta Ltd* (1991), 4 BLR (2d) 174 (Alta CA) and *Oppenheimer & Co v United Grain Growers Ltd* (1997), 36 BLR (2d) 54 (Man QB).

The Court emphasized that, when the Oremex directors called the November Meeting on September 27, they expected that the GRIT Transaction would close two weeks after the record date for the November Meeting. When the directors postponed the November Meeting, there was still significant uncertainty as to the ability to achieve the closing date of the GRIT Transaction because of the required regulatory approvals. The Court held that the facts raised concerns about the directors' conduct; however, considering the thinness of the records, the uncertainty surrounding the closing date of the GRIT Transaction, and the directors' subsequent agreement to extend the closing date until a day after the record date of the December Meeting, the Court could not conclude on a balance of probabilities that the postponement of the November Meeting was motivated by an improper purpose or bad faith.

Since it was held that the postponement of the November Meeting was valid, it followed that the shareholders' meeting that took place was not a valid meeting of shareholders. Therefore, Brown J. declined to confirm the results of such meeting.

Issue 2: The alternative relief with respect to the December Meeting

Analysis of the November 29 GRIT Transaction escrow closing

In order to determine whether the GRIT Transaction was structured in a way so as to facilitate improper or bad faith conduct by the directors, the Court first undertook an analysis of the transactional documents. In the subscription agreement entered into in connection with the GRIT Transaction, "Admission" was a defined term meaning the admission of the GRIT ordinary shares onto the LSE for listing. Pursuant to the provisions of the subscription agreement, the issuance of the Oremex shares and warrants was conditional upon "Admission."

As "Admission" had not yet occurred, Oremex was under no obligation to subscribe for the GRIT Shares or to issue Oremex securities. Yet 1,053,756 Subscription Receipts were issued to

Oremex that entitled Oremex to automatically receive one GRIT Share for each Subscription Receipt upon the listing of the GRIT ordinary shares on the LSE. If listing did not occur within 60 days following closing, Oremex would be entitled to withdraw its consideration and return its shares into treasury. This occurred in spite of the fact that the subscription agreement made no reference to Subscription Receipts.

The Court questioned why Oremex issued its securities to GRIT in exchange for the Subscription Receipts on November 29, exactly the same date as the record date for the December Meeting, when the subscription agreement contained no obligation for it to do so. Oremex did not present any clear justification as to why GRIT and Oremex did not simply further extend the closing date until GRIT could secure LSE listing approval. Furthermore, the Court emphasized that 30 other junior mining or exploration companies had recently entered into private placement transactions with GRIT, yet no other such transaction involved subscription receipts, the issuance of shares prior to listing, or the holding of shares in escrow pending approval for listing.

Whether the escrow closing demonstrated improper or bad faith conduct by the directors

Considering the evidence, the Court concluded that the directors pursued the escrow closing of the GRIT Transaction in order to dilute the shares owned by the existing shareholders in time for the record date for the December Meeting so as to enhance their prospects of being re-elected. It reached this conclusion for four reasons:

1. The issuance of the Oremex shares was on the exact same day as the record date for the December Meeting. This was a critical issue; the merits of the financing and whether it was in the best interests of Oremex as a means of raising funds was not considered to be important to this analysis.

2. The subscription agreement did not contemplate the use of Subscription Receipts; in fact, it provided that Oremex would

not be required to subscribe for GRIT Shares until the listing of the GRIT ordinary shares on the LSE had occurred.

3. The use of the Subscription Receipts in the GRIT Transaction stands out as a singular, unexplained anomaly compared to all other transactions that GRIT had entered into.

4. S. 25(3) of the *CBCA* provides that a share shall not be issued until the consideration for the share is fully paid. Brown J. held that, since the listing of the GRIT ordinary shares on the LSE may or may not occur, the issuance of Oremex shares may or may not end up being supported by the consideration of the GRIT Shares. This raised doubts as to whether the November 29 issuance of Oremex shares met the consideration requirements under s. 25(3).

The Court affirmed prior jurisprudence that held that a record date is important to the fair conduct of a shareholders' meeting because it provides certainty to shareholders regarding how many individuals will be voting, allowing shareholders to make strategic voting decisions and preventing late manipulation of the voting process by diluting the shares.[7] While fixing a record date does not necessarily prevent directors from issuing further stock before the date of the shareholders' meeting,[8] each case must be assessed on its specific facts.

Citing *Teck Corp. Ltd. v. Millar*,[9] *Carter Oil & Gas Ltd. v. Inland Natural Gas Co*.[10] and *Bernard v. Valentini*,[11] Brown J. held that

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[7] See *Fox-Davies Capital Ltd v CEP International Petroleum Ltd*, 2007 YKSC 21.

[8] See *Shield Development Co v Snyder*, [1976] 3 WWR 44 (BCSC).

[9] (1972), 33 DLR (3d) 288 [*Teck*]. Teck Corp. Ltd. bought sufficient shares of Afton Mines Ltd. to enable it to take over control of Afton. Afton's directors, knowing that they would soon be replaced, entered into an agreement with Canadian Exploration Ltd. whereby Afton issued sufficient shares to Canadian Exploration to wipe out Teck's majority position. The British Columbia Supreme Court held that the directors were not actuated by an improper purpose, as they acted in the honest belief that the Canadian Exploration agreement was in the best interests of the shareholders, and that a takeover by Teck was not. The Court held that directors are not to be restrained from issuing shares merely because the object of

the directors, in trying to "jump the gun" by issuing shares to GRIT at a time when they were not obligated to do so, engaged in improper conduct by attempting to dilute the shares and manipulate the voting process. Although Brown J.'s judgment did not review the principles from these cases setting out what constitutes improper conduct by a director, his conclusion appears consistent with the jurisprudence. These cases held that a proper purpose for the issuance of shares by a director is where he or she honestly, reasonably and in good faith believes that the issuance is in the company's and the shareholders' best interests. On the other hand, an issuance of shares purely for the purpose of manipulating or maintaining control of the corporation would be improper. In *Teck*, it was also held that an issuance of shares was valid because the primary purpose motivating the directors to issue the shares was to serve the best interests of the company, even though they may have had a subsidiary purpose of retaining control of the company.[12] This has been applied in subsequent cases such as *Icahn Partners LP v. Lions Gate*

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such issuance is to frustrate the efforts of an outsider to gain control, provided that their primary purpose was not improper vis-a-vis the shareholders, and that they honestly, reasonably, and in good faith believe that such action is in the company's best interests.

[10] [1982] BCJ No 1423 (BCSC). The British Columbia Supreme Court granted an injunction preventing the directors of Trans Mountain Pipe Line Co. and Carter Oil & Gas Ltd., a shareholder of Trans Mountain, from accepting or offering shares pursuant to options held by Carter to purchase shares of Trans Mountain, on the ground of oppression due to improper exercise of the directors' powers. The exercise of the options would dilute the shares of Trans Mountain and cause Inland Natural Gas Co, which was pursuing a takeover bid of Trans Mountain, to have to acquire significantly more shares to gain control. The Court applied the principle in *Teck v Millar* and held that the underlying purpose of the issuance of shares pursuant to the options was not proper, as it would deprive the shareholders of Trans Mountain from the choice of whether or not to accept Inland's offer.

[11] (1978), 18 OR (2d) 656 (HCJ). A shareholder of a corporation, who was also the sole director and officer, allotted shares to himself for nominal consideration two days before a shareholders' meeting in order to allow himself to defeat a motion to increase the number of directors. The Ontario Supreme Court granted an injunction restraining the director from exercising any right flowing from the new shares, holding that a director's issuance of shares must be for the benefit of the company and must not be for the purpose of manipulating or maintaining control of the company.

[12] *Teck, supra* note 9 at para 165.

Entertainment Corp., where the British Columbia Supreme Court held that the issuance of convertible notes (which were priced to be, and were, converted into shares) to an entity affiliated with an insider in advance of a contested election was acceptable in light of the fact that the board's primary purpose was to deleverage the company, which was a previously articulated goal and in the company's best interests.[13]

Pursuant to *CBCA* s. 144(1)(c), which allows a court to make an order that a meeting "be called, held and conducted in the manner that the court directs," the Court ordered that the record date for the December Meeting be changed to November 27, two days before the escrow closing, in order to protect the shareholders from the directors' improper conduct. The Court also noted that, since Oremex shares had not traded for many months, the only shareholder affected by this order would be GRIL.

Appointment of Independent Chair

The Court also granted an order that the Chair of the December Meeting be independent of both the management of Oremex and of the applicants. Brown J. held that a proxy fight may not lead in the ordinary course to the appointment of an independent Chair, but a finding that the directors have attempted to manipulate the voting process should. Although the judgment does not provide any authority to support this conclusion, it is consistent with jurisprudence on this issue, which has held that the appointment of an independent Chair is justified where the alleged conduct of a Chair raises doubts as to whether he or she would conduct the

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[13] 2010 BCSC 1547, aff'd 2011 BCCA 228 [*Icahn*]. The board of Lions Gate Entertainment Corp. entered into a series of transactions that had the effect of converting more than $100 million of debt into equity and issued 16,236,305 common shares to an investment fund affiliated with one of Lions Gate's directors. The Lions Gate board said its primary purpose was to deleverage Lions Gate, and a secondary purpose was to dilute the holdings of a group of affiliated limited partnerships engaging in a takeover bid for Lions Gate and intending to replace the Lions Gate board through a proxy vote. The action commenced by the plaintiff was for relief under the oppression remedy.

meeting appropriately and without a view to his or her personal interests in a dispute.[14]

No Postponement of December Meeting

Finally, the Court granted an order that the December Meeting shall not be cancelled, rescheduled or adjourned.

Observations

Over the past few years, there has been a significant increase in litigation in the context of proxy fights or contested director elections. The jurisprudence has reflected a judicial approach of providing directors with significant latitude in making decisions in the context of proxy fights. However, courts will generally prevent boards from taking steps that are undertaken for the primary purpose and with the effect of manipulating the voting process for their benefit. Nevertheless, clear evidence of actions undertaken for an improper purpose or in bad faith will be required in order for a court to intervene.

In considering circumstances where securities have been issued to "friendly" parties in the context of a contested transaction, it is clear that courts will engage in a detailed analysis of the facts in order to determine the primary purpose of the securities issuance or whether it constitutes oppressive conduct. In such a fact-based analysis, it may be difficult to discern practical guiding principles. However, it would appear that if a share issuance is undertaken in a commercially reasonable manner to meet clear business goals, such action should be upheld if it was

[14] See *Allied Cellular Systems Ltd et al v Bullock et al*, 49 BLR 306. The British Columbia Supreme Court ordered that an independent chairperson be appointed to conduct a shareholders' meeting where the plaintiff director alleged that the defendant shareholders were pursuing an illegal takeover bid, and the defendants in turn alleged that two directors and an executive, including the plaintiff, exercised options to acquire additional shares in order to influence the vote at a shareholder meeting and control the company. The Court held that the plaintiff director's alleged conduct raised doubts as to whether the meeting would be appropriately conducted with him as chairman, justifying the appointment of an independent chair who is not interested in the outcome of the dispute.

commenced, or the reasons therefore were known and publicly articulated, prior to the contested transaction – provided that changes in a company's course of conduct that have the effect of improving an incumbent's chances of being re-elected could still prove to be fatal.

From a purely academic perspective, it is interesting to observe the continued resurgence of the "primary purpose test", notwithstanding the subjective nature of such an assessment particularly where the onus remains on the plaintiff to prove such a fact-based test. It would appear that courts have equated a board having an improper primary purpose to a breach of fiduciary duty.[15] In *Concept Capital*, the Court did not see the need to examine the merits of the financing nor whether the financing was in the best interests of Oremex. Presumably, the Court believed that, the board of Oremex having failed the threshold issue of not acting in good faith, there was no need to analyze the matter further. Finally, it is important to note that it would appear that, in *Concept Capital*, the applicants did not make an oppression remedy claim. As bad faith is not necessary to be proved to have a successful claim under the oppression remedy, it may well be that in the appropriate circumstances plaintiffs could be successful even if directors satisfy the primary purpose test.

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[15] See *Icahn Partners LP v Lions Gate Entertainment Corp*, 2011 BCCA 228, aff'g *Icahn*, *supra* note 13.

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a cautionary note

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