ECO ORO: OSC Trumps TSX and Shows Willingness to Unwind Transactions

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On June 16, 2017, the OSC released the reasons for its earlier order (the "**Order**") which reversed a tactical private placement in the context of a proxy contest involving Eco Oro Minerals Corp. ("**Eco Oro**").[2] The Order was initially issued in April of 2017. The OSC's reasons unpacked the regulator's determination to overturn a decision of the TSX and cease trade certain recently issued Eco Oro shares (the "**New Shares**").

The Order set aside the TSX's conditional approval of Eco Oro's issuance of New Shares in connection with the conversion, at Eco Oro's exclusive right, of unsecured convertible notes held by certain Eco Oro investors. For more details on the Order, see last month's *Securities Law Bulletin*.

The Proxy Contest and the Conversion

Certain shareholders of Eco Oro (the "**Dissidents**") requisitioned a shareholder meeting for the purpose of reconstituting the board of Eco Oro. Subsequent to the meeting requisition, Eco Oro applied to the TSX requesting expedited approval of the issuance of the New Shares. Proximate to such date, Eco Oro also obtained letters of support regarding its current board from certain shareholders who would ultimately be issued the New Shares.

The TSX then conditionally approved the issuance of the New Shares. Pursuant to the TSX's company manual, the TSX will generally require shareholder approval as a condition to accepting private placements where such a transaction, among other things, "materially affects control" of the issuer. However, in the TSX's cover letter to Eco Oro's counsel, the TSX stated, "We confirm your advice that the transaction will not materially affect control of [Eco Oro]" and thus, no shareholder approval was required.

Eight days prior to the record date for such meeting, Eco Oro then completed the conversion of certain debentures.

The Reasons for the Order

The OSC has jurisdiction to review the decisions of a recognized exchange, such as the TSX, upon the application of a person who is directly affected by a decision of such recognized exchange. It was found that the Dissidents had standing to seek a review of the TSX's decisions as the issuance of the New Shares could affect their ability to reconstitute the board of Eco Oro.

However, the OSC is typically reluctant to interfere with a decision of the TSX, given its expertise in considering applications under its company manual. The OSC will therefore only interfere if, among other things, it believes the TSX may have overlooked material evidence or it believes the TSX's perception of the public interest conflicts with that of the OSC.

In this case, the OSC found that it had ample reasons to interfere, including that the TSX's conditional approval of issuance of the New Shares did not consider: (i) the proxy contest that

was underway, (ii) the imminent record date for the requisitioned meeting, and (iii) that support letters were solicited by management and provided by certain New Share recipients.

Further, the OSC found that the TSX employed a narrow definition of "materially affect control", limiting its analysis to whether a new 20% shareholder or voting trust was created. However, in the view of the OSC, "the public interest requires an evaluation of whether an issuance of shares by a listed issuer is for the purpose of entrenching management in the face of a proxy contest, thwarting the justified expectations of shareholders trusting in a system that appropriately promotes shareholder democracy and board accountability."

The OSC then found that the issuance of the New Shares would allow shareholders supportive of Eco Oro's management to increase their aggregate voting control from roughly 41% to 46%, which "could reasonably tip the balance in favour of management" and that "[e]ven if the transactions are supported by the objective of an improved balance sheet, there was no compelling business objective for the transaction to close prior to the [requisitioned meeting's record date] that would negate the tactical motive to tip the vote in favour of management."

Therefore, the OSC substituted its own decision pursuant to the Order for that of the TSX, finding that the issuance of the New Shares did in fact materially affect control of Eco Oro and that shareholder approval of the issuance was required per the TSX's company manual. Given that the shares were already issued and so as to prevent the frustration of its requirement for shareholder approval, the OSC then relied on its public interest power to cease trade the New Shares and to prevent Eco Oro from considering the votes attached to the New Shares unless their issuance is ratified by Eco Oro shareholders.

...and the Saga Continues

It is unlikely that the OSC's Order is the last chapter in this ongoing dispute. Eco Oro has already lodged an appeal to the Divisional Court in Ontario with respect to the Order. Further, in June of 2017, the Dissidents announced that they would petition the BCSC to compel Eco Oro to hold a special shareholders' meeting immediately, so that shareholders have the opportunity to replace Eco Oro's directors *before* the shareholders meeting required to ratify the New Shares' issuance.

Application of the Order Going Forward

Going forward, when seeking TSX approval of share issuances, a listed issuer should be mindful of the contextual approach the OSC took in interpreting "materially affect control". There is no bright line test with respect to new 20% shareholders. Further, as we would think is already obvious, issuers should be sure to include fulsome information in their regulatory submissions as incomplete contextual information may provide the OSC with the justification for intervening in seemingly settled transactions.

Moreover, the OSC made clear that the same public interest considerations that arise under a takeover bid are at play in a proxy contest, as these are effectively alternative means for effecting a change of control. Therefore, even if shareholder approval is not required for a particular transaction, or there is no specific TSX issue at hand to be contested, the OSC left the door open to separately challenge an issuance completed during a proxy contest pursuant to the OSC's public interest jurisdiction. As with the OSC's decisions regarding private placements in the face of a bid, as recently exemplified by *Re Hecla Mining*, which was reviewed in our December 2016 *Securities Law Bulletin*, fairness to shareholders and integrity of the markets will be paramount in such public interest challenges.

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[2] *Re Eco Oro Minerals Corp.*, 2017 ONSEC 23.

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