FL@SH BULLETIN

Securities

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Quebec's Anti-Take-Over Law: Coming Soon?

The issue made the headlines during the 2012 Quebec provincial elections. Each of the three major parties in the running claimed that they would make it harder for foreign companies to acquire Quebec-based ones. The Parti Québécois and the Coalition Avenir Québec also proposed creating multibillion-dollar funds within the Caisse de dépôt et placement du Québec, the province's pension-fund management arm, to buy up shares in Quebec-based companies "threatened" with foreign takeovers.

In November 2012, Quebec Finance Minister Nicolas Marceau said that the minority government formed by the Parti Québécois wanted to make it more difficult for Quebec companies to be sold following a hostile takeover bid from foreigners. Marceau indicated that his government wanted to give boards of directors the right to take into account the views not only of shareholders, but also employees, retirees, suppliers and affected communities after receiving a hostile bid.

Reporters and others have suggested that another component of the yet to come proposals would empower the board of directors of a Quebec company faced with a hostile bid to make such bid unavailable to the company's shareholders if the board of directors believes that the bid is inadequate.

On February 13, 2012, Marceau announced that he would shortly launch a consultation with the business community to gauge the community's reaction to the possibility of revising the current legal framework of take-over bids. One can expect that consultation to include a discussion or consideration of what new powers ought to be afforded to boards of directors of Quebec-based companies so that they could counter hostile bids by foreigners.

Takeovers, Generally

In Canada, takeovers, be they by foreigners or not, involve issues of both corporate and securities laws that bring to the forefront the determination of whom, between the shareholders and the directors of a Canadian corporation, gets to decide when and if a corporation should be sold.

The 2008 Supreme Court of Canada ruling in BCE expressly stated that the directors' statutory fiduciary duty under the *Canada Business Corporations Act* (which are substantially the same duties under the *Business Corporations Act* (Quebec)) are owed to the corporation, which can involve a consideration of the interests of more than just shareholders and requires a long-term view of the corporation. More broadly, this duty requires directors to act honestly and in good faith, to avoid self-dealing, and to consider the interests of shareholders and other stakeholder groups, as appropriate.

The Court in BCE affirmed the fact that directors of a corporation may take into account the impact of decisions on non-shareholding stakeholders and that there is no principles to the effect that one set of interests (*e.g.,* the interests of shareholders) should prevail over another set of interests. This is in contrast to what is generally understood to be duties of directors of United States companies, that is, to maximize shareholder value (often referred interchangeably to as "shareholder primacy theory", "shareholder value" or "shareholder wealth maximization").

Powers to Counter Hostile Bids

At this point in time, there is not much clarity as to what the Finance Minister's proposal could entail. Other than declarations and press reports, and the fact that the government intends to consult the business community before putting forward any plans, not much is known.

How could the government make it more difficult for Quebec companies to be sold following a hostile takeover bid from foreigners? By changing the corporate regulatory landscape, the securities regulatory landscape or, maybe, both? Given the Quebec-centric concern and Marceau's declarations, one could speculate that this could be accomplished by modifying Quebec's *Business Corporations Act* to extend the directors' fiduciary duties owed to the corporation to others stakeholders such as non-shareholder groups. Statutes that provide for those extended fiduciary duties are often referred to as "constituency statutes".

Constituency Statutes

Constituency statutes have been adopted by a majority of the states in the United States to address the concerns of groups other than shareholders that often have a meaningful economic stake in the welfare of corporations.

While the specific language of the constituency statutes varies, most statutes contain the following typical factors that a board of directors of a corporation ***may*** consider when discharging their duties:

- the interests and effects of any action upon non-shareholders, including employees, suppliers, customers, creditors, and communities;
- both long-term and short-term interests of the corporation;
- local and national economies;
- any other relevant community and societal considerations; and
- the continued independence of the corporation.

Most United States state constituency statutes are permissive, not mandatory, meaning that directors have the authority to consider other constituencies, but the discretion to focus solely on shareholder returns if they choose to do so (which is in line with the generally understood duty of American directors to maximize shareholder value in the context of change in control transactions).

Given the formulation of the Canadian directors' fiduciary duty in the BCE decision and the fact that boards may already be factoring in various stakeholders' interest when analyzing change of control transactions, the enactment of a constituency statute may, at best, have only a marginal effect on decision-making by directors. Indeed, it might simply very well be a codification of the principles set forth in the BCE decision.

It should be noted that a constituency statute alone does not address the conflicting perspectives of Canadian corporate and securities legislations (*i.e.*, corporate law's focus on the best interests of the corporation versus the shareholder-centric approach of National Policy 62-202 Take-Over Bids – Defensive Tactics (NP 62-202)). Canadian securities regulators have taken the position in NP 62-202 that the primary objective of take-over bid laws is to protect the bona fide interests of the target's shareholders. NP 62-202 provides that the decision on whether a bid succeeds should ultimately rest with the target company's shareholders rather than with its board of directors.

Impact of Constituency Statutes

In his paper, "*Moving Towards Stakeholderism? Constituency Statutes, Enlightened Shareholder Value and All That: Much Ado about Little*?" (available here) Andrew Keay examines so-called constituency statutes in the United States and their impact as well as the concept of enlightened shareholder value as it has been developed in the United Kingdom (under the *Companies Act* 2006).

Keay concludes that the pieces of legislations examined only appear to provide greater stakeholder focus and that they really add little in a drive towards stakeholderism. According to Keay, this is due to a number of reasons with a major one being that apart from shareholders, no other stakeholders appears to have the power to challenge actions by directors in the courts or in any other way.

Concerns with Constituency Statutes

Given their enormous potential for affecting the outcome of a take-over bid, non-shareholder constituency statutes offer surprisingly little guidance to directors faced with making corporate decisions or, for that matter, to courts faced with reviewing those decisions.

As a rule, non-shareholder constituency statutes are silent on many key issues. Constituency statues do not, for the most part, prescribe any constraint on the directors' discretion in deciding whether to consider non-shareholder interests and, should they decide to do so, which interests to consider and favour. They do not inform the directors on what weight ought to be assigned to shareholder and non-shareholder interests. They do not offer guidance as to what directors are to do when all interests considered cannot be reconciled nor do they offer any assistance as to what should directors do when the interests of various non-shareholder constituencies conflict amongst themselves.

Some commentators argue that constituency statutes should be enforceable by non-shareholder stakeholders and should create fiduciary duties on behalf of directors to the non-shareholder stakeholders. Arguably, this can only be the case where the constituency statute clearly directs the directors to consider non-shareholder constituents. Absent that clear legislative statement, it is questionable whether non-shareholder constituents would have standing to enforce these statutes. In the event that a fiduciary duty is owed to non-shareholder constituents, the statute should set out what standards of review will apply to actions of directors claimed to be motivated by concern for non-shareholder constituents.

Ironically, one of the most severe pitfalls of non-shareholder constituency statutes is the possibility that unprincipled directors could, in the name of some non-shareholder interests, cover their own self-interested behaviour (such as their own entrenchment in a change of control transaction). One can easily imagine that devious directors could justify self-interested, if not selfish, decisions in the interests of non-shareholder constituents.

That reason alone suggests that the Quebec government ought to be careful and fully consider all of the relevant factors before adopting a non-shareholder constituency statute. We look forward to participating in the public consultation when it is launched.

NEED ASSISTANCE?

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