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Policy Prevails over Fine Print: Successful Ambush in British Columbia Clarifies the Use of Blank Proxies

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A recent decision of the British Columbia Supreme Court in *Russell v Synex International Inc.* (*Synex*) validated a dissident's floor nomination and the subsequent election of an entirely new board. Notably, the dissident cast his votes using the authority given to him by shareholders who appointed him as their proxyholder, using the management form of proxy. The Court concluded that when a shareholder uses a management form of proxy to appoint a proxyholder other than the named management appointees and does not provide voting instructions, the proxy provides full discretionary voting authority to the named proxyholder. Accordingly, the dissident in this case was able to elect an entirely new board by relying on the private proxy solicitation exemption and without issuing his own form of proxy.

Background

Synex International Inc. (Synex or the Company), a TSX-listed company incorporated in British Columbia, is involved in the development of hydroelectric projects. At its annual shareholder meeting on November 2, 2018, Synex proposed increasing the size of the board from six to seven and elect seven directors. The dissident was the Company's largest shareholder, holding approximately 33% of the outstanding shares as at the record date of the meeting. Together with the proxies that the dissident had gathered before the meeting, the dissident had authority to vote a clear majority (51.4%) of the votes attaching to all of the outstanding shares of the Company.

Notably, the Company did not have an advance notice policy, which would have required advance notice of the shareholder's director nominees; however, Synex management was aware of the dissident's intention to nominate directors because he announced that intention in an early warning report press release 10 days before the meeting. At the meeting, the dissident voted against the increase in the size of the board and nominated a new slate of six directors. However, the chair of the meeting, after seeking legal advice, disallowed the dissident's proxies, with the result that management's nominees were elected. After the meeting, the dissident applied to court seeking an order overruling the chair's decision to disallow the proxies and to declare that the dissident slate had been duly elected at the meeting.

The Proxies in Question

Each shareholder appointing the dissident as its proxyholder had used the Synex management form of proxy or voting instruction form (VIF) to do so and in each case had left the voting instructions blank. As is customary in a management form of proxy, the Synex form stated that in the absence of voting instructions provided by a shareholder, the shares would be voted in accordance with management's recommendation.

The dissident took the position that he was not bound by the default voting instructions and instead held "blank" proxies conferring full discretionary authority to vote the shares at the meeting as he saw fit. The central issue for the Court was to determine whether the default mechanism bound a non-management proxyholder appointed by the shareholder using the management form of proxy.

Decision of the Chair

The chair of the meeting disallowed the dissident's proxies on the basis that

- the proxy did not confer discretion to vote against the increase in the size of the board since that item of business had not been varied and therefore, in the absence of voting instructions, the proxy would be voted in accordance with management's recommendation; and
- applicable securities laws did not permit the use of proxies to elect any person as a director who is not named in an information circular.

The Court's Analysis

Legal Framework and Industry Standards Support Enfranchising Shareholders

In conducting its analysis, the Court had regard to applicable law, recognized industry practices and standards, including the Securities Transfer Association of Canada Proxy Protocol, and the proposition articulated in the 1989 Ontario case *Canadian Express Ltd. v Blair* [*Canadian Express*] that "disputed proxies must be construed in light of surrounding circumstances and where possible in a manner consistent with business common sense."

The Court undertook a detailed analysis of the proxy voting system as legislated under corporate and securities laws, including the mechanisms in National Instrument 54-101 (NI 54-101) to enfranchise beneficial owners of shares. The Court then concluded that the entire regulatory scheme is geared to facilitating the exercise of a shareholder's right to vote. The Court also found that prevailing industry standards and practices generally seek to give effect to a shareholder's voting intentions where possible. Relying on expert evidence, the Court concluded that, whether legally sound, the use of blank proxies and floor nominations have been common practice in Canada, although the use of advance notice bylaws has tempered the practice.

Default Voting Instructions Apply Only to Management Appointees

Although the legislative framework and industry practice provide a clear preference for enfranchising shareholders, the Court noted that proxies are "fundamentally instruments of agency by which the proxyholder is appointed to represent the shareholder's interests." Accordingly, the proxyholder's specific authority at any particular meeting is only as broad as the language in the instrument conferring the authority. The Court examined in detail each of the three separate forms of proxy instrument that had been used to appoint the dissident.

Voting Information Forms

In accordance with NI 54-101, each shareholder holding shares through an intermediary received a VIF through which the beneficial owner could instruct the registered shareholder how to vote or, alternatively, appoint a third party to represent the beneficial shareholder at the meeting. In one of the forms of VIF, the Court concluded that the language was clear that a third-party appointee would not be bound to vote in accordance with the default instructions on the legal proxy where the VIF was otherwise left blank.

In the other form of VIF, the Court was required to resolve a conflict in the instructions. One instruction indicated that a third-party appointee would have full authority to act at the meeting, language that is specifically mandated by NI 54-101. A later instruction included the typical default voting language. To resolve the discrepancy, the Court concluded that the default voting language applied only when the beneficial shareholder chose not to appoint a third-party appointee; a third-party appointee should not be bound by the default provisions.

The Court noted that this conclusion was consistent with the legislative framework, industry practice, the holding in *Canadian Express* and, perhaps most notably, common sense:

> Conferring open authority on a named proxyholder who is not a management representative is more likely to give effect to the shareholder's intentions than presuming that this appointee is intended to vote in accordance with management's

> recommendations. If the shareholder were content with management's recommendations, why would he or she be refusing the invitation to appoint a management representative as proxyholder in the first place?

Form of Proxy

Applying similar reasoning to the conflicting instructions, the Court came to the same conclusion in reviewing the authority conferred by the management form of proxy, citing the following quote with approval from *Canadian Express*:

> [The proxies] were effectively converted to unsolicited shareholder proxies once the names of the proposed management proxyholders were deleted and the names of the shareholder designees were inserted. At that point, [the default voting instruction] on the back of the document ceased to apply as [that instruction] was a condition of the management proxy contract only.

Proxy Form Requirements Apply Only to the Party Sending the Proxy

The Court noted that the dissident had undertaken his solicitation on an exempt basis using the management forms of proxy and VIF. Since the dissident had not sent the forms to the shareholders solicited, applicable securities laws governing the content of proxies would not, on their face, apply to the dissident. Accordingly, the proxy form rules that confine the use of discretionary authority to limited circumstances applied only to Synex and not to the dissident.

No Implied Advance Notice Obligation

Synex also argued that, by law, a form of proxy must not confer authority to vote for a director who has not been named in an information circular. Synex argued that this restriction reflected a public policy concern that shareholders receive advance notice of director nominees in an information circular or through the public broadcast exemption. The Court did not find any public policy concern that should override the larger regulatory framework by "limiting the ability of shareholders to appoint proxyholders who are able to respond to unexpected developments shortly before or at a shareholders' meeting."

Key Takeaways

The logic applied by the Court appears consistent with long-standing industry practice and the reasoning in the *Canadian Express* case, which has stood for 30 years. As the Court noted, if there had been concern with the reasoning in *Canadian Express*, there was plenty of time for the legislature or industry practice to respond. However, it is also worth noting the context in which the *Synex* case was decided since the dissident held proxies in respect of an outright majority of the outstanding shares. In that regard, had the decision been to uphold the chair's decision, it is quite possible that the dissident could have, at additional cost, requisitioned a new meeting and elected the proposed slate. Nevertheless, the *Synex* decision provides a helpful overview of both the legislative framework and Canadian industry practice while also highlighting the overarching policy goal of enfranchising shareholders. At the same time, the decision highlights the fact that the proxy voting system does not preclude a dissident from planning an ambush at a shareholder meeting, strengthening the case for advance notice bylaws.

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