

# Shareholder Activism in the Canadian Mining and Energy Industries

**Fred R. Pletcher**  
**CIM 2016 Convention – MES Day**  
**May 4, 2016**



# Shareholder Activism



# Shareholder Activism – Broader Trends

**“Battered Canadian miners to face more shareholder activism”**

- ***Reuters Canada, March 7, 2016***

**“Shareholder activism is the ‘new normal’ ”**

- ***The Northern Miner, December 7, 2015***

# Shareholder Activism – Broader Trends

- **Activist funds managed US\$122 billion as of September 30, 2015**
  - vs US\$32 billion as at December 31, 2008
- **US activists were successful or partially successful in achieving their demands in 75% of cases in 2015**
  - vs 57% in 2008
- **Smaller ownership stakes supporting activist demands**
  - in 65% of campaigns directed against US\$25 billion market cap targets, the activist owned less than 1% of shares

# Shareholder Activism – Broader Trends

- **68% of US activists campaign holding periods are less than one year**
  - **Median holding period is six months**
- **Proxy fights are the option of last resort. US proxy contests proceeding to a vote in 2015 fell to 24%**
  - **vs 35% in 2014**
- **Average time to settlement with US activists in 2015 was 56 days**
  - **a 24% decrease since 2013**



# Shareholder Activism – Broader Trends

- **ISS recommended in favour of US activists 46% of the time in 2015**
- **Receiving support from passive institutional equity investors - 40% of market capitalization of the S&P is open to supporting activists**
- **One in seven companies in the S&P 500 index has been on the receiving end of an activist attack over the past five years**
- **DuPont (US\$55B market cap) and Dow/DuPont transaction illustrate that no target is too large**

# The Golden Age of Shareholder Activism



# Shareholder Activism – Broader Trends

- **US activist funds have underperformed the broader market over the past three years (HRF activist index posted a 7.7% three year return vs a 26.3% return for the S&P 500 index)**
  - **Improved performance in the last 12 months (HRF activist index posted a 1.06% 12 month return vs a -2.13% return for the S&P 500 index)**



# Shareholder Activism – Broader Trends

## 2015 FTI Consulting report

- 86% of activists surveyed expect to raise more capital in the next 12 months
- 70% of activists surveyed expect to increase partnerships with institutional investors and pension funds
- As competition increases in the US market, activists will look more closely at *Canadian* and European targets

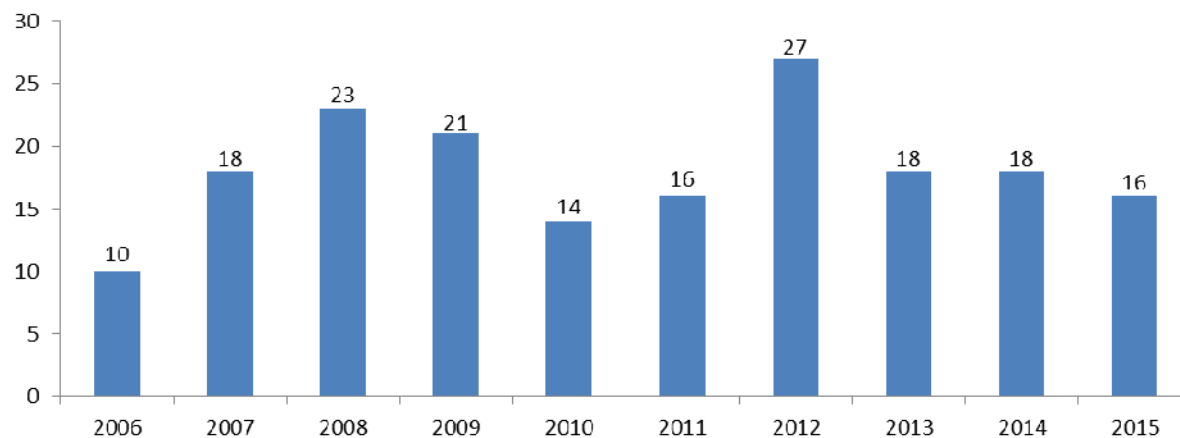


# Shareholder Activism Whither Canada?



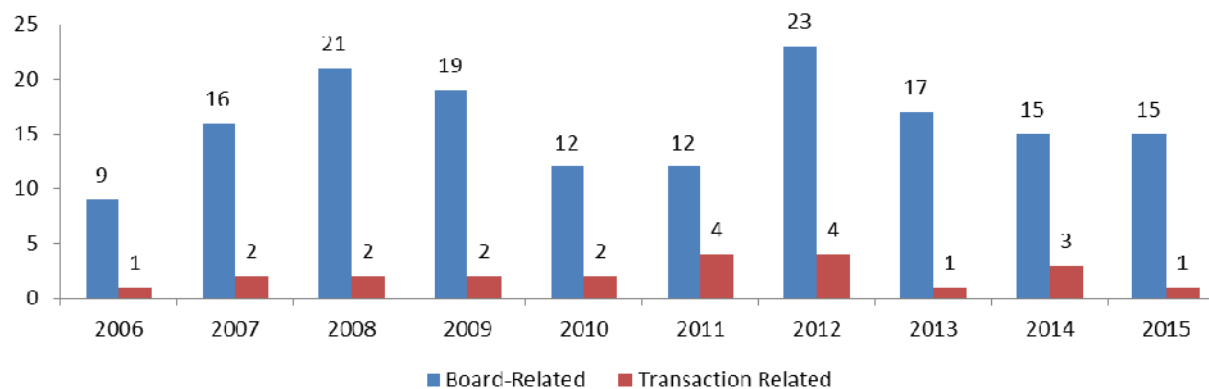
# Shareholder Activism Whither Canada?

Proxy Contests in Canada  
2006-2015  
(181 Contests)



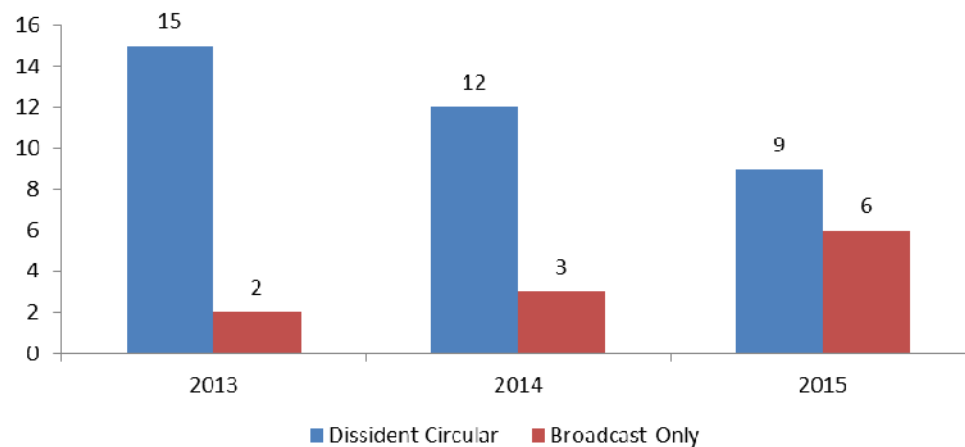
# Shareholder Activism Whither Canada?

**Board vs. Transactional  
Proxy Contests in Canada**  
2006-2015  
(181 Contests)



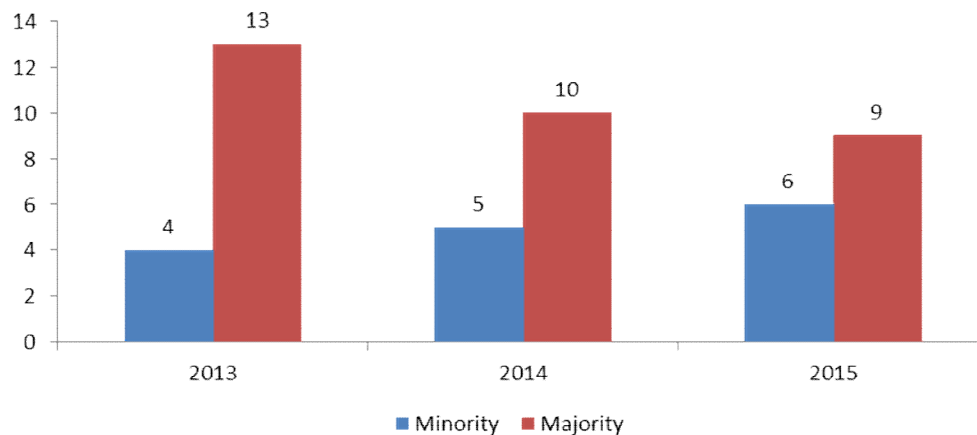
# Shareholder Activism Whither Canada?

**Dissident Circular vs. Broadcast-Only  
Board Proxy Contests  
2013-2015  
(47 Contests)**

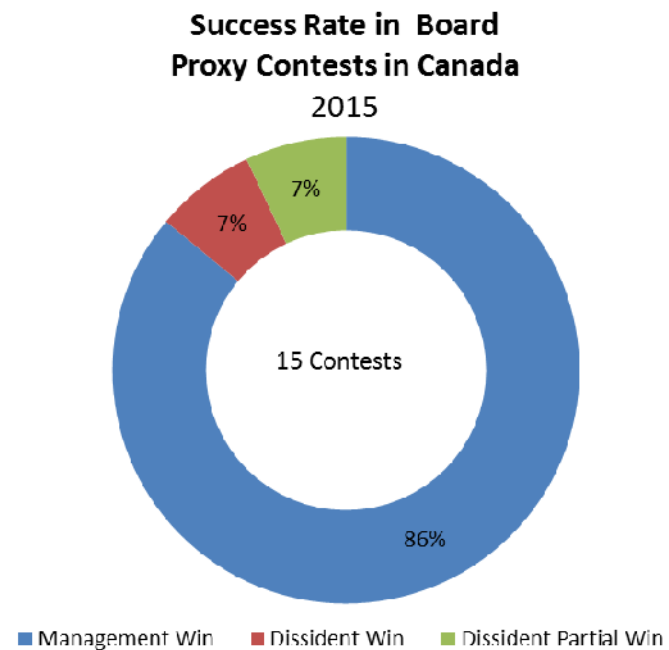


# Shareholder Activism Whither Canada?

Dissent Slate Types  
Board Proxy Contests  
2013-2015

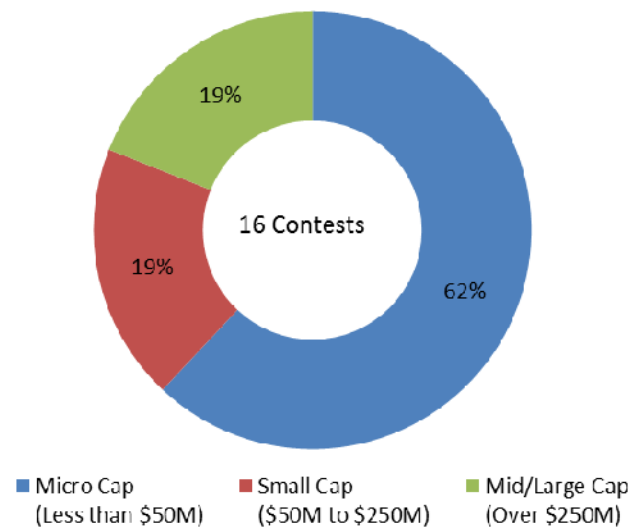


# Shareholder Activism Whither Canada?



# Shareholder Activism Whither Canada?

Proxy Contests in Canada by  
Issuer Market Capitalization  
2015





# Shareholder Activism Whither Canada?

## 2015 Board Proxy Fights with Dissident Circulars

TARGET NAME	TARGET INDUSTRY	TARGET MARKET CAP	OUTCOME OF CONTEST
Aberdeen International Inc.	Financial Services	Micro Cap	Management Win
Central Gold Trust	Financial Services	Mid/Large Cap	Management Win
Crown Point Energy Inc.	Energy	Micro Cap	Management Win
Dynacor Gold Mines Inc.	Mining	Small Cap	Management Win
Karnalyte Resources Inc.	Mining	Micro Cap	Dissident Win
Kobex Capital Corp.	Financial Services	Micro Cap	Management Win
Moag Copper Gold Resources Inc.	Mining	Micro Cap	Dissident Partial Win
Petromin Resources Ltd.	Energy	Micro Cap	Management Win
Terra Nova Energy Ltd.	Energy	Micro Cap	Management Win

# Shareholder Activism Whither Canada?

## 2015 Broadcast-Only Board Proxy Fights

TARGET NAME	TARGET INDUSTRY	TARGET MARKET CAP	OUTCOME OF CONTEST
Americas Petrogas Inc.	Energy	Micro Cap	Management Win
Clifton Star Resources Inc.	Mining	Micro Cap	Management Win
Fission Uranium Corp.	Mining	Mid/Large Cap	Management Win
Silver Bullion Trust	Financial Services	Small Cap	Management Win
STT Enviro Corp.	Diversified Industry	Micro Cap	Management Win
Temple Hotels Inc.	Diversified Industry	Small Cap	Management Win

## 2015 Transaction Proxy Fights

TARGET NAME	TARGET INDUSTRY	TARGET MARKET CAP	OUTCOME OF CONTEST
Pacific Rubiales Energy Corp.	Energy	Mid/Large Cap	Dissident Win

# Shareholder Activism Whither Canada?

**Who was winning board proxy contests in 2015?**

- **“King Lear is a tragedy” rule**
- **Former management/founders**
  - **Robin Phinney, founder of Karnalyte**
  - **Bradley Jones, founder and CFO of MOAG Copper Gold**



# “Who are those guys?”

## **Corporate Governance Organizations**

- **Canadian Coalition for Good Governance**

## **Proxy Advisory Firms**

- **ISS, Glass Lewis**

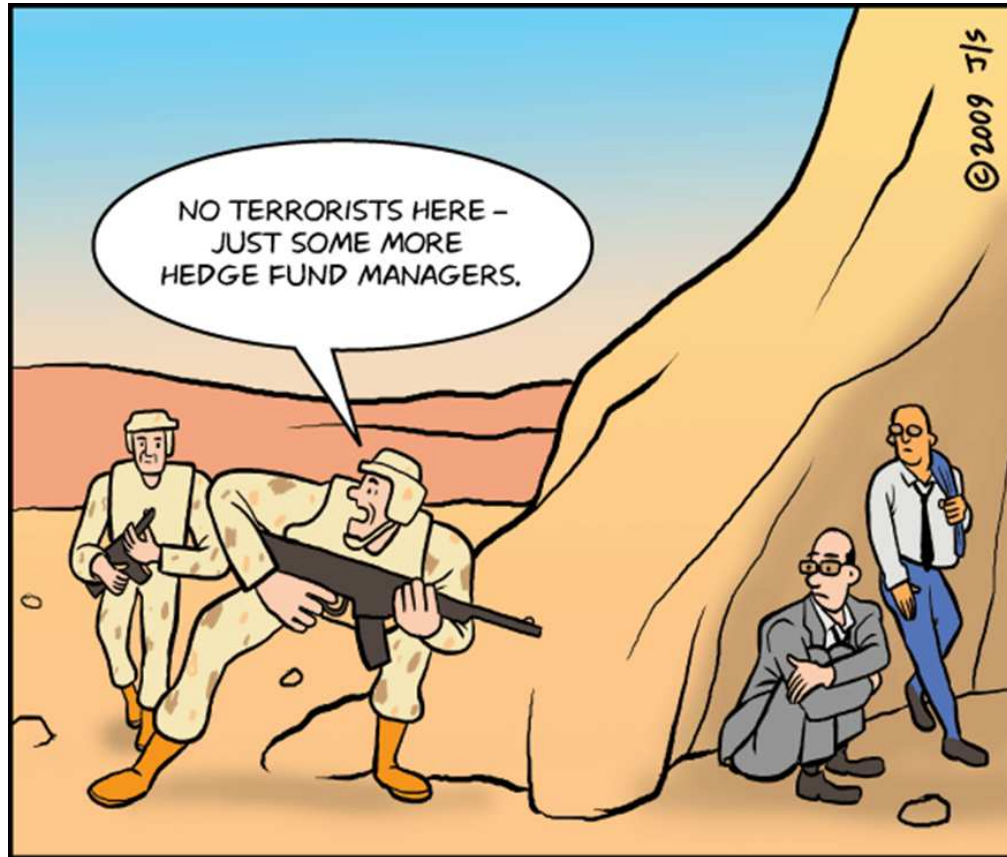
## **Institutional Investors**

- **Pension Funds, Mutual Funds**

## **Individual Investors**

## **NGOs**

# Shareholder Activists



# “Who are those guys?”

## Hedge and Activist Funds

- **Elliott Associates, Pershing Square, JANA Partners, Trian Fund Management, Third Point**

# What do shareholder activists say they want (and sometimes even mean)?

## **Improve Corporate Governance**

- Board independence and effectiveness
- Voting mechanics and shareholder rights
- Executive and director compensation
- Capital structure and restructurings
- Takeover bid defenses

## **Corporate Social Responsibility**



# What do shareholder activists actually want?

## Advance Investment Strategy

- Increase (or decrease) share or bond price
- Cost cutting
- Increase/restructure leverage
- Monetize assets, divisions or the entire enterprise
- Cash distributions/dividends
- Promoting or blocking specific M&A transactions
- Replace board or management
- Greenmail



# What tactics do they employ?

**Publish Policies and Principles**

**Awards**

**Letter writing**

**Private discussions**

**Lobby regulators**

**Raising concerns in the media**

**Letters / white papers**

**Voting recommendations**

**Shareholder proposals**

**BLG**

Borden Ladner Gervais 25

# What tactics do they employ?

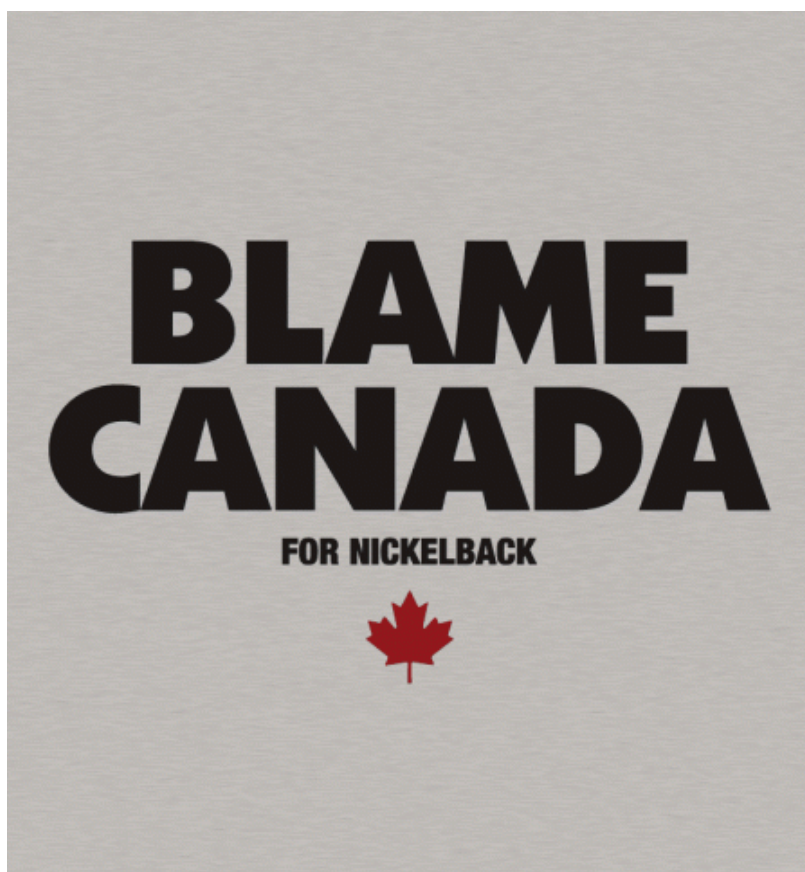
**Litigation and administrative actions**

**Wolf packing**

**Proxy contests**



# Structural vulnerabilities to shareholder activists in Canada?



## Structural vulnerabilities to shareholder activists in Canada?

- **Early warning requirement at a 10% shareholding threshold**
- **Less extensive early warning disclosure requirements and enforcement mechanisms**
- **Ability to solicit up to 15 shareholders or to publicly broadcast without a proxy circular**
- **Ability to requisition a meeting at a 5% shareholding threshold**
- **Ability to submit proposals for meetings at a 1% shareholding threshold**

# Structural vulnerabilities to shareholder activists in Canada?

- **TSX majority voting requirements makes issuers susceptible to “withhold the vote” campaigns**
- **TSX does not permit staggered boards**
- **Inefficient proxy voting system**
- **Regulatory bias towards activism**
- **Recent amendments to take-over bid legislation**

# Targets for shareholder activism



"Bummer of a birthmark, Hal!"

# Targets for shareholder activism

- **Share price underperformance**
- **Poor or infrequent communication with largest shareholders**
- **Poor communication of corporate strategy**
- **Lazy balance sheet**
- **Lack of corporate clarity / not a “pure play” / valuable non-core assets**
- **Corporate governance issues (independence, Chair, overboarding, tenure, diversity)**

# Targets for shareholder activism

- **Change-of-control target**
- **High operating or G&A costs**
- **Poorly received M&A transaction**
- **Disgruntled founders or former management**
- **Executive compensation not linked to performance**
- **Slim insider stock holdings**
- **Related party transactions**



# Targets for shareholder activism

- **Regulatory investigations or proceedings / material litigation**
- **Corporate social responsibility issues**
- **Unqualified directors**
- **Historic proxy advisory recommendations against board members**
- **Low historic voting support for directors, say-on-pay or meeting turnout**
- **Presence of other activist investors**

# Targets for shareholder activism

- **Opportunity for arbitrage among classes of securities**
- **Lack of structural defenses**

# Case study: Taseko Mines Limited

**Taseko**



# Case study: Taseko Mines Limited

- Targeted by a newly incorporated Chicago-based activist fund, Raging River Capital LP (“RRC”), which acquired a 5% equity stake in Taseko
- Two weeks after its first share acquisition, RRC requisitioned a shareholder meeting to remove three Taseko directors and replace them with four RRC nominees
- Less than an hour of engagement before RRC went public with the requisition. No white paper
- Two of the RRC nominees had no management or board experience with a publicly traded operating mining company

# Case study: Taseko Mines Limited

- RRC's initial Schedule 13D filing only disclosed share ownership by RRC and no bankruptcies involving any of its directors
- RRC announced that it had the support of a 3.9% institutional shareholder of Taseko
- RRC claimed its activism was intended to address:
  - Taseko share price underperformance
  - Three targeted directors' shareholdings were disproportionately low (4.0%) compared to their combined board positions (three of nine)

# Case study: Taseko Mines Limited

- **RRC claimed its activism was intended to address:**
  - **Alleged conflicts of interest between the three targeted directors and a management services company, Hunter Dickenson Inc. (“HDI”), in which they held interests, which provides geological, engineering, legal and other administrative services to Taseko**
  - **Taseko’s acquisition of a mining company with a permitting stage copper ISL asset in Arizona (“Curis”), in which HDI affiliated directors held an 8% interest, for \$45 million in equity and \$31 million in debt. RRC claimed Curis had no value.**

# Case study: Taseko Mines Limited

- **RRC claimed its activism was intended to address:**
  - **Strategic need to focus on core assets, sell non-core assets, cut costs, maximize cash flow from the Gibraltar mine by changing stripping ratios, and addressing the Company's balance sheet through bond repurchases**
- **Taseko responded by adopting corporate governance changes**
  - **Say-on-pay and say-on-HDI-services vote**
  - **Seek shareholder approval of any acquisition or disposition in which HDI or HDI-related parties have an interest**
  - **Appoint two new independent directors**

# Case study: Taseko Mines Limited

- Taseko initiated litigation in the US to require RRC to amend its Schedule 13D and over the course of three amendments exposed that RRC failed to disclose that:
  - RRC held a significantly greater amount of Taseko bonds than shares
  - the RRC nominees were parties to “golden leash” arrangements, where they would be compensated based on the performance of RRC and its principal’s bondholdings – which Taseko alleged was a serious conflict of interest with shareholders
  - The institutional investor supporting RRC also held a greater amount of Taseko bonds than shares



# Case study: Taseko Mines Limited

- **RRC failed to disclose that:**
  - **the RRC nominees had been involved in past bankruptcies, one of which involved a nominee who was acting as both a creditor and shareholder of a bankrupt company. The bankruptcy trustee stated in a court approved settlement that the directors may have “violated their fiduciary duties” and lenders may have “improperly benefited from the actions of the directors” (including deepening the company’s insolvency). The nominee neither admitted nor denied the trustees allegations.**

# Case study: Taseko Mines Limited

- RRC failed to disclose that:
  - RRC had several undisclosed principals, one of whom was a member of an Asian auto-parts conglomerate which had previously been in negotiations to acquire a 19.9% interest in the Curis property for US\$75 million.
- Taseko also rebutted many of RRC's principal arguments:
  - RRC's allegations of share price underperformance ignored the decline in copper prices and Taseko, in fact, had outperformed its peer group

# Case study: Taseko Mines Limited

- **Taseko also rebutted many of RRC's principal arguments:**
  - **the four RRC nominees' personal shareholdings (0.5%) were significantly lower than those of the Taseko directors they sought to replace (4.0%)**
  - **service payments to HDI were immaterial (amounting to ~0.3% of Taseko's annual expenditures), fully disclosed in Taseko's financial statements and cost effective (being either at cost or below third party replacement costs)**
  - **The Curis acquisition followed 18 months of due diligence, was overseen by a special committee, supported by an independent fairness opinion, and the HDI-related directors abstained from voting on the acquisition**

# Case study: Taseko Mines Limited

- **Taseko also rebutted many of RRC’s principal arguments:**
  - **RRC’s strategic plan would sacrifice long term shareholder value and upside to higher copper prices for short term cash flow to finance bond repurchases – which represent a clear conflict of interest as RRC’s principal interest in Taseko is as a bondholder.**
- **RRC threatened a defamation action for disclosure of the bankruptcy, but never proceeded on its threat**
- **RRC alleged that Taseko was about to undertake a dilutive financing and offered to underwrite the deal. No basis in fact for the allegations**
- **RRC made allegations of insider trading and “questionable trades” against a number of directors and officers of Taseko.**

## Case study: Taseko Mines Limited

- All trading allegations were investigated by Taseko's independent Nominating and Governance Committee and Taseko's external counsel. The specific insider trading allegations were also investigated by an independent law firm, Stikeman Elliott. No evidence was found of any violation of securities laws or regulations. Taseko invited securities regulators to review the trading with Taseko and its counsel.
- RRC initiated an oppression action against Taseko for the Curis transaction, and sought an interim order to prevent Taseko's directors and officers from voting any Taseko shares received on the Curis transaction. The BC Supreme court declined to grant the order.

# Case study: Taseko Mines Limited

- **Proxy advisory firms ISS and Glass Lewis both recommended that shareholders vote against all of RRC's proposals**

“[W]e believe the Company successfully deflects many of the more specious concerns levied by RRC, an entity which, based on publicly available information, appears to be both hastily formed and opportunistic, with a greater financial interest in Taseko's bonds than in the Company's equity. Perhaps more disconcerting still, RRC was decidedly lax in disclosing this prospectively conflicted financial interest -- as well as the similarly conflicted and affiliated financial interests of the bulk of its own nominees -- until pressured by Taseko's own public disclosures.”

Glass Lewis & Co., LLC



# Responding to shareholder activism: the price of freedom is eternal vigilance



**BLG**

Borden Ladner Gervais 47

**Responding to shareholder activism:  
the price of freedom is eternal vigilance**



# Responding to shareholder activism: the price of freedom is eternal vigilance

**Under Canadian law, boards must act in the best interest of the corporation and take a long-term view.**

**Leading institutional investors are developing a new paradigm of corporate governance that prioritizes sustainable value over short term thinking, integrates long-term corporate strategy with substantive corporate governance and requires transparency as to director involvement**

- **Letter of Larry Fink of Blackrock to the CEO's of the S&P 500**

**Issuers can help to inoculate themselves against shareholder activism by clearly and pro-actively communicating their adherence to these strategic and governance principles**

- **Trust cannot be built after an activist surfaces**

# Responding to shareholder activism: the price of freedom is eternal vigilance

## What to communicate?

- **Lead with strategy**
- **Confirm board involvement in the strategy**
- **Make the case for long-term investments for growth**
- **Describe capital allocation priorities**
- **Explain why the right mix of directors is in the boardroom**
- **Address sustainability and CSR**
- **Link executive compensation design and corporate strategy**
- **Describe how board practices and culture support independent oversight**

# Responding to shareholder activism: the price of freedom is eternal vigilance

## How to communicate it?

- **Periodic “letters” to investors**
- **Investor days**
- **Quarterly communications**
- **Management information circulars, annual reports, other securities filings and website**
- **Ongoing investor engagement**
  - **Director level interaction**

# Responding to shareholder activism: the price of freedom is eternal vigilance

- **Bring activist inquiries to the attention of the board (likely the governance committee)**
- **Ensure the board rigorously complies with its fiduciary duties and has the benefit of the business judgment rule**
- **Know who will be in your response team**
- **Retain independent proxy solicitors, financial advisors, counsel, accountants, PR firms, investigators if necessary**
- **Recognize potential for litigation. Adopt procedures to ensure solicitor-client privilege**

# Responding to shareholder activism: the price of freedom is eternal vigilance

**Police shareholder activists to ensure they are complying with securities and corporate laws**

- **TELUS litigation against Mason Capital**
- **Silvercorp litigation against short sellers**
- **Genesis Land Development litigation challenging “joint actor” status**
- **Chair of St. Elias Mines’ decision to reject dissident proxies where dissidents failed to correct material misstatements notwithstanding notice**

**Resist overly technical responses to dismiss shareholder activist inquiries**

- ***HudBay Minerals* decision**

**Never close the door on a negotiated settlement with shareholder activists**

# Responding to shareholder activism: the price of freedom is eternal vigilance

## Know your shareholder base

- **closely monitor trading patterns and significant trading volumes**
- **monitor advance warning reports**
- **monitor investor/activist conferences**
- **monitor attendance on quarterly earnings calls**
- **be aware of relationships between significant shareholders (“wolf pack” activists)**
- **Actively consider ISS’ and your shareholders’ voting policies when structuring transactions or governance and compensation practices**
- **Actively monitor ISS and Glass Lewis reports**

# Responding to shareholder activism: the price of freedom is eternal vigilance

Consider the adoption of an advance notice bylaw or policy to ward off “stealth” proxy campaigns

- common in US
- ISS and Glass Lewis recommend in favor of 70-30 day windows
- policies upheld by BC Supreme Court in the *Mundoro Capital* decision
- bylaws upheld by Ontario Superior Court in *Maudore Minerals* decision
- 70% instituted in constating documents, 30% by policy
- 91% average shareholder approval level

# Existential issues of shareholder activism



# Existential issues of shareholder activism

## Does shareholder activism create value

- L. Bebchuk, A. Brav, and W. Jiang, *The Long-Term Effects of Hedge Fund Activism*, 115 Colum. L. Rev. 1085 (2015)
- John C. Coffee and Darius Palia, *The Wolf at the Door: The Impact of Hedge Fund Activism on Corporate Governance*, 1 Annals of Corporate Governance 1 (2016)
- S&P U.S. Activist Interest Index
  - one year annual return -24.99%
  - three year annual return of 0.65%
  - five year annual return of 6.26%
  - ten year annual return of 12.45%

# Existential issues of shareholder activism

- Will increased activism adversely governance
- Value of experience vs independence & diversity
- Increased responsibility vs quality candidates
- A significant percentage of directors of TSX issuers will need to be replaced in the coming years

**Thank you**

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