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2016 Legal Year in Review

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Introduction

As 2016 comes to a close, it is time again to share with our clients and friends our observations about what we believe to be some of the most significant legal developments affecting Canadian business over the past year and their implications for 2017 and beyond.

Climate change regulation has moved to the forefront for governments facing mounting pressure to meet the commitments made at the UN Climate Change Conference in Paris in December 2015. The Ontario, Alberta, Quebec, and most recently, the Nova Scotia governments have adopted a range of different policy solutions – such as carbon taxes or cap-and-trade programs – for reducing greenhouse gas emissions. Meanwhile, the federal government began positioning Canada as a global leader on climate change by introducing a national carbon pricing floor in late 2016. Greenhouse gas emitters will clearly have to grapple with the challenges of conducting business on an economically viable basis while complying with these new regulatory requirements. At the same time, there is potential for significant innovation and opportunity for market participants in areas of green energy and energy conservation.

Prior to 2016, few people had heard the term "FinTech" or had any idea of what it meant. At one end of the FinTech spectrum are traditional software companies providing technologies specifically designed for financial institutions. At the other end are potentially "disruptive" technology-enabled financial services companies that make it easier for consumers to bypass traditional bricks-and-mortar financial institutions in engaging in financial transactions or acquiring financial services. Today, emerging FinTech companies are achieving unprecedented success in raising capital and the Canadian government is announcing plans to encourage innovation in financial services like never before. The FinTech opportunity also raises a challenge: how best to regulate this nascent industry and to balance the interests of new entrants and established players.

There were a number of significant developments in Canadian corporate and securities law in 2016. These encompassed regulatory amendments, such as the adoption of the new Canadian take-over bid regime and the revised early warning rules. As well, several significant decisions were released by courts and securities regulatory tribunals, including (most notably) the *InterOil* decision from the Yukon Court of Appeal. The Court's decision to block Exxon Mobil's proposed US$2.3 billion acquisition of InterOil Corporation, despite the fact that it was approved by over 80% of the votes cast by InterOil's shareholders, may have significant implications for the future conduct of public company acquisitions.

While 2016 was a year of political turmoil in the United States, the U.S. Securities and Exchange Commission (SEC) worked on ongoing initiatives, with developments that are more evolutionary than revolutionary. Of particular interest to Canadian companies and Canadian investors active in U.S. markets is a requirement for mining and oil and gas companies to disclose payments made to foreign governments relating to commercial development. Additionally, the SEC has proposed to shorten the standard securities trade settlement cycle by one business day to reduce risk during the period between trade and settlement. Finally, the SEC's proposed adoption of universal proxies could influence future similar developments in Canada.

The corporate governance landscape in Canada continued to evolve on a number of fronts. Diversity disclosure practices were under the microscope following the first full year of mandated disclosure under securities laws regarding the representation of women on boards and in executive officer positions. Initiatives in this area were also announced by the Ontario and federal governments. The Toronto Stock Exchange proposed corporate governance and security-based compensation website disclosure requirements. Proposals by the federal government to change the rules for director elections under the *Canada Business Corporations Act* (CBCA) are a potential cause for concern. Further shareholder engagement initiatives, including recommended amendments to the shareholder proposal provisions of the *Business Corporations Act* (Ontario) and proposed amendments to the CBCA to allow electronic delivery of proxies, are in process.

Contested regulatory enforcement cases in Canada were overshadowed by a number of record setting "no-contest" settlements that topped the unprecedented settlements seen in 2015. Although there were few cases of note on the regulatory front, a number of jurisdictions gave themselves new tools to employ in their battle against capital market abuses. For example, the OSC became the first regulator in Canada to introduce a "bounty-based" whistleblower policy. This policy has been hailed by the OSC as a "game changer" and an important means through which to obtain crucial evidence needed to pursue a number of complex securities violations, such as insider trading, market manipulation, and sophisticated fraud. On the other hand, companies will want to ensure that zealous whistleblowers do not foreclose their ability to enter into no-contest settlements with the OSC.

In 2016, plaintiffs continued to try to circumvent the protections – such as the requirement to obtain leave to commence a proceeding and the cap on damages – that are offered to defendants under the *Securities Act* (Ontario) in relation to secondary market claims. Other creative plaintiffs sought unsuccessfully to characterize primary market claims against underwriters as secondary market claims in order to increase potential liability. Market participants should continue to be confident that Ontario Courts are prepared to uphold the hard-won protections under the secondary market provisions of the *Securities Act*, and to recognize the difference between primary and secondary market claims. At the same time, market participants should be prepared to fend off similar creative approaches in future.

Aboriginal issues and the duty to consult continue to be among the primary risks to resource development in Canada. While the basic legal principles that govern Aboriginal consultation in Canada are well established, consultation requirements for both project proponents and the Crown can be elusive in practice and execution. This was highlighted in the recent Federal Court of Appeal decision in *Gitxaala Nation v. Canada*, which overturned the federal government's approval of Enbridge's Northern Gateway Project – a multi-billion dollar pipeline system proposed to run from Edmonton, Alberta, to Kitimat, British Columbia. Just prior to the time of writing, the federal government announced that the Northern Gateway Project has been rejected. Even though *Gitxaala* represents a loss for the Northern Gateway Project and its proponent, it provides helpful clarity in relation to the duty to consult that may allow future projects to avoid a similar outcome.

In response to mounting public concern over tax avoidance and evasion, the federal government in Budget 2016 announced the dedication of an additional $444.4 million to the Canada Revenue Agency (CRA) over the next five years to combat these issues. In light of public scrutiny, it is not surprising that 2016 has seen the CRA increase the number and scope of its audits, take aggressive positions under the general anti-avoidance rule and the transfer pricing rules, and impose penalties at unprecedented levels. We expect this environment of heightened audit and assessment activity to persist in the near term. Businesses should closely examine tax risk management practices, monitor key legal developments and adjust tax planning accordingly, as well as ensure that appropriate processes are in place to prepare for increased audit scrutiny.

Private equity continues to attract significant amounts of capital. According to Preqin's "2016 Preqin Global Private Equity & Venture Capital Report", the global amount of "dry powder" has now topped US$1.3 trillion, the highest since the data provider's records began in 2000. One noteworthy trend is the elevated appetite for direct investments by limited partners in private equity and venture capital deals. In 2015, limited partners were involved in 168 completed deals, a 23% rise from 2012. This appetite for direct investing can be troubling for the general partners of private equity funds who have historically relied – and continue to rely – on investments in their funds from institutional investors such as sovereign-wealth funds and pension plans. Given that the appetite and capacity for direct investing seems unlikely to diminish in the near future, co-investment rights on reasonable terms provide a solution for general partners seeking to ensure the continued availability of flexible and committed capital.

The oil and gas industry continues to suffer through a downturn, leading to a number of restructurings. Corporations in financial difficulty are increasingly turning to the arrangement provisions of the CBCA or equivalent provincial corporate statutes to restructure corporate bonds and similar debt obligations at a lower cost and on an accelerated timetable relative to more traditional insolvency proceedings. CBCA arrangements have proven to be an effective and flexible alternative for restructuring or recapitalizing certain debt obligations and making other fundamental changes to a corporation's capital structure without a formal admission of insolvency. A successful CBCA arrangement proceeding has fewer repercussions for a corporation's business and its reputation than a traditional insolvency filing.

Last year we noted the wave of special purpose acquisition corporation (SPAC) offerings. The deadlines for completing qualifying acquisitions – namely, an acquisition by the SPAC of a business using the escrowed proceeds of the initial equity offering – is fast approaching, and four proposed transactions have been announced. Whether these qualifying acquisitions can be completed will likely determine the viability of this acquisition structure going forward.

As we monitor these and other legal developments in 2017, we would be happy to discuss them with you.

Articles

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