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Be Careful What You Wish For (or, Be Careful What Contest Winner You Give Shares To)

It is not every day that a geologist wins an equity interest in a junior mining company through a contest. And it is not every day that the geologist then dissents to that company's amalgamation. But it does happen.
In *Bayliss v Plethora Exploration Corp*, the Ontario Superior Court addressed an Application brought by a contest winner for, inter alia, fair market value for his shares pursuant to section 185(1) of the *Business Corporations Act* ("OBCA").

Justice Cavanagh's decision in this case is a good reminder for corporations to comply with all contractual terms governing shareholding from the time of issuance, and how the failure to do so can have unexpected consequences.

Facts

Jack Bayliss, a geologist, won a geological competition. The prize was a 3% equity interest in a new junior mining company, Superior Nickel Inc. ("Superior"). Superior's controlling interest was owned by a private equity fund, Plethora Private Equity ("Plethora").

On June 18, 2021, Superior issued 900,000 common shares to Mr. Bayliss. At about the same time, Mr. Bayliss entered into an Anti-Dilution Agreement with Superior (the "ADA"). Among its material terms were provisions setting out that Mr. Bayliss' shares would be held by a trustee, in the trustees' name, and the trustee alone would exercise any voting rights.

In the fall of 2022, Plethora announced a proposed amalgamation of Superior with other companies it controlled. A few months later, Mr. Bayliss and Superior amended the ADA, making the forthcoming amalgamation a "Liquidity Event" under the ADA, which would trigger certain contractual rights.

On March 20, 2023, following notice of a shareholders meeting to vote on the amalgamation, Mr. Bayliss delivered a Notice of Dissent to Superior, in which he demanded fair value for his 900,000 shares. The amalgamation was approved on March 23, 2023.

Later that spring, Superior took the position that following the amalgamation, Mr. Bayliss was left with 423,471 shares, and

that the fair market value of those shares was $0. The company advised that it was willing to provide him with a sum of $1,000 “as a gesture of goodwill”.

The Decision

Mr. Bayliss brought an application for an order:

> (i) declaring that he owned 900,000 common shares of Superior as at March 22, 2023;
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> (ii) fixing the fair value of his shares as at this date and requiring Plethora to pay the fair value of these shares to him; and
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> (iii) declaring that Plethora acted oppressively toward him.

Justice Cavanagh allowed the first two heads of relief and dismissed the oppression claim.

i. Share Ownership and Dissent Rights

Justice Cavanagh first addressed whether Mr. Bayliss held the shares and was entitled to vote such that he had a statutory right of dissent under the OBCA.

Plethora argued that Mr. Bayliss was not a holder of shares of any class or series entitled to vote, such that he could not vote on the resolution, and that he did not have a statutory dissent right. It relied on ADA provisions regarding the shares being held by a trustee, who alone had the rights.

Notwithstanding the express contractual language of the ADA, Justice Cavanagh found that: (1) Superior did not issue the shares to a trustee; rather, Mr. Bayliss was the registered holder of the 900,000 common shares; and (2) Superior had only one class of shares.

Accordingly, Mr. Bayliss held the shares and had a statutory right of dissent.

Plethora further argued that the language of the ADA prevented Mr. Bayliss from being granted dissent rights because they would result in a windfall. It submitted, inter alia, that because the ADA specified that Mr. Bayliss (rather than the trustee) would only be a shareholder upon a Liquidity Event, at which time he would be limited to 3% of such shares, Mr. Bayliss would receive a windfall if he were able to obtain fair market value for the shares prior to the Liquidity Event.

Justice Cavanagh rejected Plethora’s argument because of the company’s own conduct. Its argument was premised on compliance with the ADA, but as set out above, Superior did not comply with that agreement:

The difficulty with this argument is that Mr. Bayliss’ statutory right to dissent arises because Superior did not, itself, act in compliance with the ADA. Superior did not issue the 900,000

shares to be held by the Trustee as the registered owner, as provided for by the ADA. If it had done so, Mr. Bayliss would not have had a right to dissent under s. 185(1) of the OBCA. Instead, Superior issued 900,000 shares to Mr. Bayliss to which, by statute, voting rights attached. It is not open to me to disregard s. 185(1) of the OBCA because Superior failed to issue the shares in question to be held by the Trustee, as it was permitted to do under the ADA and, instead, issued the shares to Mr. Bayliss to be held in his name.

ii. Fair Market Value

Having found that Mr. Bayliss was entitled to exercise his dissent rights, Justice Cavanagh assessed the fair market value of the shares.

Mr. Bayliss and Plethora submitted expert reports opining on the value of the shares. After reviewing and weighing the reports, and emphasizing that determination of fair value is a matter of judgment and is not the application of a fixed formula or calculation, Justice Cavanagh concluded that the fair market value per common share of Superior as at March 22, 2023 was $0.07.

iii. Oppression

Mr. Bayliss argued that the conduct of Plethora in response to his notice of dissent (i.e., to reduce his total number of shares and to offer $0/share) was oppressive. Mr. Bayliss argued that by its conduct, Plethora acted in an effort to unfairly expropriate the value of Mr. Bayliss' shares for its benefit, and that it visibly departed from standards of fair dealing.

Plethora argued that it had not acted oppressively by relying on the ADA and disagreeing with Mr. Bayliss on the value of his shares. It argued that it was entitled to take the position, which was informed by financial analysis and valuation principles, that Mr. Bayliss' shares had no standalone equity value.

Relying on the Supreme Court's decision in BCE Inc v 1976 Debentureholders, Justice Cavanagh reviewed Superior's evidence on the factors it considered in determining that the fair market value of the shares was $0. This evidence included, among other things, that Superior had a net working capital deficit of a minimum of $639,145 as of March 22, 2023, the significant cost of taking exploration steps that could potentially lead to a viable mine, and that attempts to attract interest from other major parties in Superior were unsuccessful.

Justice Cavanagh noted the difficulty in determining fair market value in these circumstances. He held that given the difficulty in valuing the shares of Superior with precision, the directors of Plethora must be afforded reasonable latitude in their

determination of Mr. Bayliss' shares. He concluded that Plethora did not act oppressively.

Takeaways

While the facts in this case are unique, the decision provides good reminders for corporations and for shareholders.

For corporations, where a company intends to limit shareholder rights through contract, the decision reaffirms the importance of complying with these contractual terms from the outset. A failure to do so may have unexpected consequences later on.

For shareholders, this decision reinforces the strong statutory protections under the OBCA, and the standard to which corporations will be held where these rights are limited by contract.

For both, the decision reaffirms the challenges and unpredictability in determining fair market value in many industries (and the cost of doing so through the litigation process). To that end, a shareholder's disagreement with the fair market value proffered by a corporation, or even hard bargaining or conservative forecasting by the corporation, will not on its own be enough to establish oppression.