Lock-Ups, Squeeze-Outs, and Canadian Takeover Bid Law: A Curious Interplay of Public and Private Interests

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Securities law permits takeover bidders to enter into prebid lock-up agreements with major target shareholders. Lock-up agreements may have a stifling effect on takeover auctions, but allowing them is thought to entice more bidders to make offers in the first place. Locked-up shares may then be counted in the minority approval vote needed to authorize a subsequent going-private transaction. In effect, these transactions override dissenting shareholders' property rights in the broader public interest of facilitating takeover bids.

Examining the decisions in BNY Capital Corp. v. Katotakis, the author considers the interplay between the current securities law practice and the effect of rights of first offer and first refusal in shareholder agreements, which can functionally resemble lock-up agreements. After canvassing the nature of such rights and the general regulatory framework governing takeover bids and going-private transactions, the author considers the Katotakis decisions by the Ontario Securities Commission and in the courts. These decisions provide rare insights into an area that has largely been unexplored by Canadian courts.

Some curious aspects of shareholders’ contractual rights and minority shareholders’ property interests in the takeover bid context are revealed. The case illustrates, but does not conclusively resolve, the issue of how the courts’ and the regulators’ divergent views of the relative importance of the public interest in encouraging takeover auctions and the private contractual and property interests of shareholders can affect the outcome of takeover litigation.

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Introduction

Under certain circumstances, small shareholders of Canadian public companies can be forced to sell their shares against their will. The law sometimes overrides a shareholder’s private interest to protect a greater public interest. It aims to indirectly benefit minority shareholders in general by encouraging takeover offers. Indeed, even the private interests of larger shareholders are susceptible to unexpected regulatory modifications made in the public interest.

This sort of interplay between shareholders’ property and contractual rights, and the broader public interest in the case of publicly traded corporations, has generated few Canadian court decisions. By way of contrast, in Delaware the same interplay has led to an impressive number of high-profile judicial pronouncements on lock-ups, freeze-out mergers, and going-private transactions generally. Nevertheless, one recent Canadian case, *BNY Capital Corp. v. Katotakis*, addressed these issues squarely. It exposed something curious and unique about Canadian takeover rules when they are applied to parties to a shareholders’ agreement containing mutual rights of first offer and first refusal. The case showed how an existing securities regulatory framework can interact in unusual ways with shareholders’ contractual commitments. It also highlighted the interplay that occurs in contested Canadian takeover bids between provincial securities regulators and the courts.

The *Katotakis* case has attracted considerable attention from securities lawyers and indeed, from securities regulators, for the trial judge’s very restrictive interpretation of the bid financing requirement mandated by section 96 of the Ontario

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1 See e.g. *Re Siliconix Inc. Shareholders Litigation*, [2001] WL 716787 (Del. Ch.) (WL); *Re Pure Resources Shareholders Litigation*, 808 A.2d 421 (Del. Ch.); *Glassman v. Unocal Exploration*, 777 A.2d 242 (Del. Sup. Ct. 2001); *Next Level Communications Inc. v. Motorola, Inc.*, 834 A.2d 828 (Del. Ch. 2003); *NCS v. Omnicare*, 818 A.2d 914 (Del. Sup. Ct. 2003) [*Omnicare*]. *Omnicare* has become of particular interest, in part because, as noted by Norman Veasey, Chief Justice of the Delaware Supreme Court at the time the decision was released, “it was a rare split (3-2) decision of the usually unanimous Supreme Court, [and was also controversial] because it was surprising that the majority of the Supreme Court reversed a well-reasoned decision of the Court of Chancery” (E. Norman Veasey, “What Happened in Delaware Corporate Law and Governance From 1992-2004?” (2005) 153 U. Pa. L. Rev. 1399 at 1458 [footnotes omitted]). In *Omnicare*, the majority held that a so-called “force the vote provision” permitted by Delaware’s *General Corporation Law*, Del. Code Ann. tit. 8 § 251 (2003) (this provision was amended in 2003; see now § 146 (2006)) constituted a preclusive and coercive takeover defence in a merger agreement when lock-up agreements signed by the major shareholders effectively guaranteed completion of the merger. It was therefore found invalid and unenforceable. Veasey C.J. (as he then was) and Steele J. vigorously dissented.

Securities Act. That aspect of the case will not be discussed here. This comment will instead focus upon its implications for rights of first offer and first refusal contained in parties’ shareholder agreements.

To appreciate precisely what Katotakis reveals about these matters, it is worthwhile to first review the concept of rights of first refusal and first offer in shareholder agreements, as well as some of the basic features of a common corporate transaction known as a “going-private transaction”.

I. Rights of First Offer and First Refusal

Two or more major shareholders of a public corporation may choose to enter into a shareholders’ agreement that consolidates their effective control over the corporation by governing the way in which they will vote their shares. These agreements may also include share sale restrictions, designed to protect signatories from finding themselves forced to deal with incompatible or inappropriate business partners in the future. Sale restrictions might include rights of first offer or first refusal or both. A right of first offer requires a shareholder who wishes to sell his or her shares to offer those shares to the other parties to the agreement before looking for potential buyers beyond the existing shareholder group. A right of first refusal requires a shareholder who has already received a good faith (i.e., bona fide and noncollusive) offer from a third party to give the other signatories the chance to match that offer before concluding any sale with the third-party offeror.

When triggered, such restrictions can effectively operate as “lock-up” agreements. A lock-up agreement in the share acquisition context refers to a contract between a prospective takeover bidder and shareholders of the target corporation, pursuant to which the bidder undertakes to launch a takeover bid at a price no lower than an amount specified in the contract. The shareholders in turn agree to tender their shares to the bidder’s bid. Once signed, lock-up agreements entered into by major shareholders of target corporations can stifle takeover auctions. In many cases,

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3 R.S.O. 1990, c. S-5, s. 96 [Securities Act]. Indeed, the trial decision prompted the Ontario Securities Commission to propose a rule ensuring more flexibility in the interpretation of section 96 than the court had appeared to think permissible. See infra note 48.

4 If an acquisition is proposed in a form other than a takeover bid—such as by way of amalgamation or arrangement—a lock-up (or support) agreement would include a covenant on the part of the target company shareholders to vote their shares in favour of the proposed transaction, either in person or by proxy, at the shareholders meeting that must ultimately be held to approve the matter. A support agreement of this latter sort was the subject of the British Columbia Court of Appeal’s controversial decisions in Pacifica Papers Inc. v. Johnstone (2001), 93 B.C.L.R. (3d) 20, 19 B.L.R. (3d) 62, 2001 BCCA 486 and Re Sepp’s Gourmet Foods Ltd. (2000), 211 D.L.R. (4th) 542, 98 B.C.L.R. (3d) 217, 2002 BCCA 108 [Sepp cited to D.L.R.].

5 At the simplest level, a lock-up agreement will prevent an auction by precluding the possibility of any bidder obtaining a sufficient number of shares to acquire control of the target, other than the bidder with whom the major shareholders had entered into lock-up agreements. The very existence of a right of first refusal in a shareholder agreement among large shareholders of a public corporation
however, lock-up agreements actually facilitate takeover auctions, since many bidders would not launch takeover bids in the first place without reasonable assurance of the eventual success of their bids. A lock-up agreement provides this assurance.

II. Background to Rules Governing Canadian “Going-Private Transactions”

The majority shareholder of a Canadian public company may, under certain circumstances, eliminate (or “squeeze out”) the minority shareholders against their will. As this process transforms a public company into a private company, it has traditionally been referred to as a “going-private transaction”. It is still so called by many corporate statutes,6 by corporate practitioners, and by the policy statement applicable in Quebec to such transactions, Policy Q-27.7 For somewhat technical reasons, the Ontario Securities Commission (“OSC”) substituted the term “business combination” in place of the term “going private transaction” in recent amendments to the applicable OSC Rule.8 Terminology aside, these transactions permit the

similarly could preclude an outside bid for such a corporation, although an analysis of the possible effect of such an agreement requires consideration of differing types of auction. The auction literature broadly distinguishes between two types of auction: “common value” auctions (where the intrinsic value of the auctioned asset is the same for every bidder, and differing bids, therefore, only reflect varying levels of information and search, investigation, and bidding costs); and “independent value” auctions (where the value of the auctioned asset is actually worth more in the hands of one bidder than in the hands of another perhaps, in the case of business sales, because certain bidders can realize greater synergies than others). See e.g. Peter Cramton & Alan Schwartz, “Using Auction Theory to Inform Takeover Regulation” (1991) 7 J.L. Econ. & Org. 27. In a common value auction environment, a right of first refusal would be expected to prevent an auction because a rational outside bidder would not make a bid knowing that an informed insider had a right to match any such bid. Since the informed insider would typically have better information about the corporation’s value than the bidder (even ignoring the bidder’s search and investigation costs), an outside bidder would predict that its bid could only ever succeed if its offered price was in excess of the asset’s true value. Any bid at or below the true value (which the insider would be in a better position than the outside bidder to determine) would be matched by the insider. In the case of an independent value auction, however, a rational bidder might be prepared to bid even where an insider enjoyed a right of first refusal. The outside bidder, for example, might be able to realize synergies on the purchase that would be unavailable to the parties to the shareholder agreement, making it rational for that bidder to pay more for the shares than the insiders. Following Cramton & Schwartz, though, such a bid would only be made if the outside bidder’s private value for the asset exceeded the insider’s value by an amount at least equal to all of the outside bidder’s costs. Thus, even in an independent value environment, the existence of a right of first refusal will likely inhibit at least some bidders from participating.

6 See e.g. Canada Business Corporations Act, R.S.C. 1985, c. C-44, s. 193 [CBCA]; Canada Business Corporations Regulations, S.O.R./2001-512, s. 3(1); Business Corporations Act, R.S.O. 1990, c. B-16, s. 190(1) [OBCA].


successful bidder to transform the target company into a private company, freeing it from public companies’ reporting and other obligations.

There are two basic methods by which the interests of minority shareholders may be eliminated following a takeover bid. The first, formally known as a “compulsory acquisition” rather than a “going-private transaction”, is typically provided for by the incorporating statute of the subject company and can only be accomplished if the bidder has obtained at least ninety per cent of the outstanding shares of the target company.9 This sort of compulsory acquisition was not at issue in Katotakis.

Rather, the Katotakis case involved the second method of eliminating minority shareholders’ interests, available when a takeover bidder has acquired less than ninety per cent of a public company’s outstanding shares. This method can take several transactional forms, including share consolidations (or, as they are often called in the United States, “reverse stock splits”), arrangements, or reorganizations. Among the most common techniques in Canada is the “amalgamation squeeze”. In an amalgamation squeeze, the target corporation is amalgamated with a second corporation controlled by the majority shareholder. The terms of the amalgamation provide that the minority shareholders, upon completion of the amalgamation, will not receive participating securities in the amalgamated corporation but instead will be given either cash or, more typically, redeemable preferred shares that will be promptly redeemed for cash.10

Canadian corporate statutes typically require that an amalgamation be approved by a two-thirds vote of the shareholders of each of the amalgamating corporations

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9 See e.g. CBCA, supra note 6: A compulsory acquisition must be completed “within one hundred and twenty days after the date of a take-over bid [that] is accepted by the holders of not less than ninety per cent of the shares of any class of shares to which the take-over bid relates ... ” (ibid., s. 206). See also OBCA, supra note 6, s. 188. If the bidder, prior to the bid, owns any shares of the target corporation, this right to acquire will not be available unless ninety per cent of the remaining shares are tendered to the bid, meaning that the bidder would need to hold more than ninety per cent of the total. The compulsory acquisition provision appears to have its genesis in U.K. law, and an early version of the provision was introduced into the federal Companies Act (the predecessor to the CBCA) in 1934. See Esso Standard (Inter-America) v. J.W. Enterprises, [1963] S.C.R. 144 at 148, 37 D.L.R. (2d) 598 [Esso Standard cited to S.C.R.]. The English Companies Act has similar provisions today. See Paul L. Davies, Gower and Davies’ Principles of Modern Company Law, 7th ed. (London: Sweet & Maxwell, 2003) at 742ff. An early version of the ninety per cent compulsory acquisition rule, modelled on English legislation, was the subject of two Supreme Court of Canada cases: Rathie v. Montreal Trust, [1953] 2 S.C.R. 204, 4 D.L.R. 289; Esso Standard, ibid. In both cases, the Court took a rigid view of the provision and found that the bidder had not satisfied its requirements (including, in Esso Standard, a requirement not specifically included in the legislation) and so could not use the section to force out the minority shareholders.

10 The redeemable preferred share device is used principally for income tax reasons.
before it may be undertaken. Of course, if the shareholder undertaking the squeeze transaction already owns two-thirds of the target corporation’s shares, the outcome of such a vote is assured (subject to special minority approval requirements discussed below).

At one time, the legality of this second method of going-private transaction was uncertain in Canada. Over time, the use of such transactions has become regulated and largely uncontroversial. The regulatory scheme, briefly, works this way (in the case of Ontario reporting issuers incorporated under the OBCA or the CBCA). The OSC, in Rule 61-501, mandates the procedures to be followed when a going-private transaction or “business combination” is undertaken. Where those procedures are followed, both CBCA and OBCA corporations are permitted to undertake going-private transactions without following any additional rules. Specifically, a CBCA

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11 See e.g. CBCA, supra note 6, s. 183(5); OBCA, supra note 6, s. 176(4); Business Corporations Act, S.B.C. 2002, c. 57, s. 271(6); Companies Act, R.S.N.S. 1989, c. 81, Sch. III, ss. 2(1)(c), 12(1). There is no requirement for a shareholder vote in the case of so-called short-form amalgamations. These amalgamations, by definition, do not involve corporations with minority shareholders.

12 Of course, approval for such a transaction might be achieved even where the majority shareholder holds fewer than two-thirds of the outstanding shares. It is highly probable that many shareholders will not be represented at the relevant meeting, either in person or by proxy. Corporate law rules typically require approval by way of a resolution passed by at least a two-thirds majority, not of all shares outstanding, but rather “of the votes cast by the shareholders who voted in respect of that resolution ...” (CBCA, supra note 6, s. 2(1) “special resolution” [emphasis added]).

13 See Christopher C. Nicholls, Corporate Finance and Canadian Law (Scarborough, Ont.: Carswell, 2000) at 367. Two early cases that raised questions about the going-private transaction were Burdon v. Zeller’s Ltd. (1981), 16 B.L.R. 59 (Qc. Sup. Ct.) and Alexander v. Westeel-Rosco Ltd. (1978), 22 O.R. (2d) 211, 93 D.L.R. (3d) 116, 4 B.L.R. 313 (H.C.J.). In Canadian Pacific Ltd. v. Alouette Telecommunications Inc. (1992), 6 B.L.R. (2d) 92, 42 C.P.R. (3d) 423 (Ont. Gen. Div.) [Alouette cited to B.L.R.], Ground J. held that shares tendered by the federal government pursuant to a lock-up agreement were properly included as shares tendered to a takeover bid, such that the compulsory acquisition provisions were available to the successful bidder. As Ground J. said: “I do not think that s. 206 of the CBCA should be interpreted so as to construct artificial barriers to the implementation of a successful take-over bid and compulsory acquisition and inhibit the operation of the capital markets” (ibid. at para. 34). See also Cathy Singer, “Going Private Transactions and Other Related Party Transactions” in Julia Milosh, ed., Critical Issues in Mergers and Acquisitions: Domestic and International Views: Papers Presented at the 6th Queen’s Annual Business Law Symposium 1999 (Kingston, Ont.: Faculty of Law, Queen’s University, 2000) 193 at 199.

14 In 1978, a panel of the OSC hearing an application for a cease-trade order in the context of a squeeze-out reorganization, noted that a number of highly publicized squeeze-out transactions had apparently been completed without incident. It acknowledged, however, that there was a need to improve OSC policies relating to such transactions (Re Cablecasting Ltd., [1978] O.S.C. Bull. 37 (OSC)). The process that began culminated in the drafting of Disclosure, Valuation, Review and Approval Requirements and Recommendations for Insider Bids, Issuer Bids, Going Private Transactions and Related Party Transactions, O.S.C. Policy Statement 9.1, 14 O.S.C. Bull. 3245 (5 July 1991), as am. by Revisions to Commission Policy Statement 9.1, 15 O.S.C. Bull. 2921 (26 June 1992) [OSC Policy 9.1], which, following the granting of rule-making power to the OSC, was reformulated and revised as Rule 61-501, supra note 8.

15 Ibid.
corporation is expressly authorized by the CBCA to undertake a going-private transaction when applicable provincial rules are followed,\(^{16}\) and an OBCA corporation that complies with Rule 61-501 is likewise exempt from the going-private rules that would otherwise apply under the OBCA itself.\(^ {17}\)

If a going-private transaction is carried out immediately following a takeover bid, it is referred to as a second-step going-private transaction (or, in the language of Rule 61-501, a second-step business combination).\(^ {18}\) One of the key requirements of Rule 61-501 is that a second-step going-private transaction may only be effected if it is approved, not only by the requisite two-thirds majority vote called for by corporate law, but also by a majority of the target company’s minority shareholders (sometimes called “the majority of the minority”). This majority excludes the takeover bidder who initiated the going-private transaction and those related to or acting jointly with the bidder.\(^ {19}\) Rule 61-501 includes an important qualification to this minority approval requirement. Shares that have been tendered to the original takeover bid may be included in the subsequent minority approval vote, even though, at the time of this postbid vote, those shares are actually owned by the majority shareholder (that is, the successful takeover bidder).\(^ {20}\) The rationale usually offered for this important provision is that any shareholders who willingly tendered their shares to the bid have, by so tendering, effectively indicated their approval of the transaction. Moreover, had an economically similar acquisition been structured as a one-step transaction (such as an amalgamation with the bidder or an arrangement) those shares could certainly have been voted in favour of the deal. The argument is thus that it would be nonsensical to effectively deny shareholders the right to support an economically similar two-step transaction.\(^ {21}\) Further, bidders willing to pay a price that most shareholders are happy to accept ought not be discouraged from launching such bids, fearing that they may not be able to extricate themselves from the burdens of

\(^{16}\) CBCA, supra note 6, s. 193.

\(^{17}\) OBCA, supra note 6, s. 190(6). The OSC may exempt interested persons from application of s. 190: Rule 61-501, supra note 8, s. 4.7.

\(^{18}\) This term is not specifically defined in Rule 61-501, ibid., but does appear, for example, as the heading of s. 8.2 of that rule.

\(^{19}\) Rule 61-501, ibid., s. 4.5. No minority approval is required if, among other things, interested parties (e.g., the major shareholder that is initiating the transaction) own ninety per cent or more of the outstanding securities of the class subject to the going-private transaction (ibid., s. 4.6(1)2). This exception is not identical to the ninety per cent threshold that applies in the case of postbid compulsory acquisitions under corporate law provisions, such as CBCA, supra note 6, s. 206, because it applies in all cases where interested parties seek to undertake a going-private transaction (not merely where such a transaction is pursued following a takeover bid) and it applies when interested parties hold ninety per cent of the outstanding securities of the affected class, rather than only to those cases where ninety per cent of the securities not owned by the bidder at the date of the bid are tendered to the bid.

\(^{20}\) Rule 61-501, ibid., s. 8.2.

\(^{21}\) See e.g. Singer, supra note 13 at 218. Singer was General Counsel to the OSC from August 1996 to January 1999, during the drafting of Rule 61-501 (Singer, ibid. at 193).
operating a public company no matter how few shares remain in the hands of minority shareholders.22

Before formally launching a bid, it is common practice for prospective takeover bidders to negotiate with major shareholders of the target corporation. If those negotiations are successful, the bidders and these major target shareholders will typically sign lock-up agreements. There are two basic modes of lock-up agreement: the “hard” lock-up and the “soft” lock-up. A hard lock-up agreement contains a commitment on the part of the target shareholder to tender his or her shares to the takeover bid that is to be launched by the bidder, provided that the bid price is no lower than the price specified in the lock-up agreement. A soft lock-up agreement would typically contain a conditional commitment by the shareholder to tender to the bid and a covenant not to actively solicit competing offers (i.e., not to “shop” the bid), but would nevertheless have an “out”, allowing the shareholder to tender to a higher bid from a third party should one materialize.

At one time, the shares acquired by a bidder from shareholders who had previously entered into lock-up agreements could not be voted in subsequent going-private transactions.23 It was feared that allowing locked-up shares to be counted in the postbid “majority of the minority” approval vote would discourage takeover auctions.24 The regulators’ views on this issue have evolved. In a process of reform that began with the proposed reformulation of OSC Policy 9.1 as Rule 61-501,25 the

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22 As stated in Paul G. Findlay, ed., Securities Law and Practice, 3d ed., looseleaf (Toronto: Carswell, 2006) vol. 2:

The policy reason behind [the section permitting such shares to be voted] is that the parties should not be in a different position from if they had proposed the business combination without a formal bid first. Those securities that were tendered to the bid, but would have been part of the minority, if a formal bid had not been made, may be counted as having voted in favour of the business combination (ibid. at 20-202).

The link between permitting the shares of those who have accepted a bid to vote on the subsequent going-private transaction and the incentive to launch fair bids was drawn in a commentary co-written by James Baillie (a former Chairman of the OSC): “[W]here the majority shareholder is prepared to make a fairly priced offer for the minority, but only if there is assurance against a small rump minority holding being left outstanding, triggering all the regulatory issues attendant on a public corporation, then the minority shareholders should not be denied access to this offer” (James C. Baillie, Alfred Avanessey & Peter Johnson, “‘Acting Jointly or in Concert’ in Corporate Law: Re Sepp’s Gourmet Foods Ltd.” (2002) 37 Can. Bus. L.J. 281 at 282).

23 See OSC Policy 9.1, supra note 14, s. 32.2.


25 In the original proposed version of Rule 61-501, published for comment in 1996, votes attached to shares tendered by target shareholders who “effectively controlled” the target could not be counted as part of the “majority of the minority” in a postbid going-private transaction if those shares had been tendered to the bid “pursuant to an understanding entered into by the security holder prior to the distribution of the disclosure document” (i.e., a lock-up agreement): Notice of a Proposed Rule and Policy Under the Securities Act (Ontario)—Insider Bids, Issuer Bids, Going Private Transactions and Related Party Transactions, 19 O.S.C. Bull. 2981 at 3030 (31 May 1996), s. 8.4(1)2 [Proposed Rule
OSC has come to the view that shares acquired in a takeover bid from shareholders who had signed prebid lock-up agreements may (in the same way as any other shares tendered to the bid) properly be included in the subsequent minority approval vote if certain conditions are met. The locked-up shareholders must not have received different consideration for their shares, any collateral benefit, or any consideration for other securities they held in the target company that was greater than the entitlement of other security holders.26 In other words, it is important that such shareholders have not been treated differently from other shareholders; otherwise, their decision to tender to the bid might well have been influenced by special considerations that would not be relevant to the minority shareholders generally, and thus could not necessarily be viewed as an approval of the bid on its terms. The OSC recognized that lock-ups might stifle some takeover bid auctions. It was nevertheless persuaded that the use of lock-ups to entice potential bidders to make offers in the first place outweighed the possible disadvantages of the auction-inhibiting effect that lock-ups could have.27

In addition to easing restrictions on the counting of shares acquired by bidders pursuant to prebid lock-up agreements as part of the minority, the OSC further specifically indicated its view that an “ordinary lock-up agreement” would not “in and of itself” result in the parties to that agreement (namely, the bidder and the locked-up shareholders) “being seen to be acting jointly or in concert.”28 This conclusion would, among other things, have meant that the shares would be ineligible for inclusion in the postbid minority vote. The legal status of this view was buttressed when the OSC, in response to a controversial British Columbia Court of Appeal judgment,29 amended Rule 61-501 to specifically provide—in the rule itself and not 61-501]. Locked-up shares of noncontrolling shareholders (which would also have been excluded under Policy 9.1) could be voted. The OSC sought comment on this proposed treatment of lock-up agreements. When a revised version of Proposed Rule 61-501 was published for comment in 1999, the OSC acknowledged that:

there is a fundamental question of why a controlling shareholder receiving the same consideration as others should not be able to do what it wants with its shares regardless of the impact it will have on the ultimate outcome of the transaction. Since the shareholder can control the outcome by voting its shares at a shareholders’ meeting (for a going private transaction) or tendering its shares to a take-over bid, why should the shareholder be prevented from locking-up its shares or supporting an acquiror prior to the shareholders’ meeting or the expiry of the take-over bid, as the case may be?


26 Rule 61-501, supra note 8, s. 8.2.
28 Companion Policy 61-501 CP, 23 O.S.C. Bull. 2748 (14 April 2000), s. 2.3(2).
29 Sepp’s, supra note 4 at para. 30. Although the court was actually considering a support agreement, rather than a lock-up agreement, the principles underlying both types of agreement are effectively the same. The Court of Appeal’s judgment has been harshly criticized by practitioners. See e.g. Baillie, Avanessy & Johnson, supra note 22. A support agreement is functionally equivalent to a lock-up
simply in a policy statement—that merely entering into a lock-up agreement did not, without more, make a shareholder a joint actor with the majority shareholder. Accordingly, shares tendered to a bidder pursuant to a previously signed lock-up agreement normally ought to be eligible for inclusion as part of the minority for purposes of minority approval of the second-step going-private transaction.

To summarize, a prospective takeover bidder of a public corporation (who could, in some cases, already be a major shareholder of that corporation) may enter into a lock-up agreement with other shareholders of the corporation prior to launching the takeover bid. Once the bid is completed, if there are still some minority shares outstanding, the successful bidder may undertake a going-private transaction to force the remaining shareholders to sell their shares. Such a transaction (other than a ninety per cent compulsory acquisition permitted under most corporate law statutes) must be approved by a majority vote of the minority shareholders (that is, those shareholders other than the bidder). In this vote, however, any shares that were tendered to the bidder in the takeover bid—including shares tendered pursuant to lock-up agreements negotiated before the bid was commenced—normally may be counted as part of this minority.

It was against this regulatory background that the intriguing facts in BNY Capital Corp. v. Katotakis arose.

III. Facts in BNY Capital Corp. v. Katotakis

The litigants were shareholders of Financial Models Company Inc. (“FMC”). FMC was a publicly traded corporation, but three shareholders collectively held more than eighty per cent of FMC’s outstanding shares: Katotakis held about 40.4 per cent; Waters, about 20 per cent; and BNY, about 22.4 per cent. These shareholders had agreement, but in the context of an acquisition structured as an amalgamation or an arrangement, rather than as a takeover bid. Instead of undertaking to tender their shares to an upcoming takeover bid, shareholders who enter a support agreement undertake to vote (or deliver proxies) in support of the proposed amalgamation or arrangement at the shareholders’ meeting called to approve such a transaction.

The issue of which shares acquired by a bidder should be excluded in determining whether or not the requirements for using the compulsory acquisition provisions have been satisfied has some history. The Supreme Court of Canada read into an early version of the compulsory acquisition provision a requirement that the 90% threshold may only include shares acquired from independent shareholders. See Esso Standard, supra note 9. Early English legislation (upon which the original Canadian provision was largely based) included an exclusion (absent from the first Canadian legislation) for “shares already held at the date of the offer by, or by a nominee for, the transferee company or its subsidiary” (Companies Act, 1948 (U.K.), 11 & 12 Geo. VI, c. 38, s. 209(1)). This language would not, on its face, deal with a distinct entity that was not a nominee but was acting jointly or in concert with the bidder. Nonetheless, the English Court of Appeal, in Re Bugle Press Ltd. (1960), [1961] Ch. 270, [1960] 3 W.L.R. 956, [1960] 3 All E.R. 791 (C.A.), likewise read such a requirement into the statute. It was upon this case that the Supreme Court largely relied in Esso Standard.

30 See 2003 Notice of Amendments, supra note 8 at 1823.
entered into a shareholder agreement with respect to those shares. The agreement contained mutual rights of first refusal and of first offer. The right of first offer required that any shareholder who wished to sell his or her shares must first offer to sell those shares to the other parties at a price chosen by the selling shareholder and specified in a selling notice.\textsuperscript{31} If the other parties elected not to purchase the shares from the selling shareholder, he or she was then free to sell the shares to a third party within a sixty-day period, provided the third party paid a price at least as high as the price contained in the selling shareholder’s original selling notice.\textsuperscript{32} The right of first refusal required that any shareholder who received, before delivering a selling notice, a bona fide third-party offer to purchase shares that he or she wished to accept was obliged to give the other shareholders the opportunity to match that offer.\textsuperscript{33}

A third party, Linedata Systems, became interested in acquiring the shares of FMC. In August 2004, Linedata began discussions with Katotakis (in his capacity as a representative of FMC). Katotakis indicated to the FMC board in October that he was not interested in pursuing these discussions. The board, however, formed a special committee to pursue further discussions with Linedata.

The major FMC shareholders other than Katotakis (holding, in the aggregate, about fifty-two per cent of the shares) were agreeable in principle to selling their shares to Linedata. In the normal course, Linedata might, at this point, have entered into lock-up agreements with these shareholders, obligating them to tender their shares to its takeover bid at an agreed-upon price. The right of first refusal in the FMC shareholder agreement appeared to mean, however, that any offer by Linedata to purchase FMC shares from an FMC shareholder who was a party to the shareholder agreement would compel that shareholder to give an opportunity to match the offer to the other parties (including Katotakis). The major non-Katotakis shareholders evidently agreed in principle that they would be prepared to lock-up their shares, and so draft lock-up agreements with Linedata were prepared (but not signed). The draft agreements were soft lock-ups. They would, if signed, obligate the shareholders to tender to a Linedata bid, but would permit them to withdraw their shares and tender to a competing bid if it constituted a “Superior Proposal”.

On 7 December, before Linedata had actually made an offer to purchase FMC shares, the major non-Katotakis shareholders delivered selling notices to Katotakis pursuant to the rights of first offer in the shareholder agreement. These selling notices were brief. They offered to sell the shares to Katotakis at a price of $12.20 per share, but went on to say that this offer was to be subject to “terms and conditions ... substantially in accordance with the terms and conditions set forth” in the draft lock-

\begin{footnotes}
\item[31] Shareholder Agreement, Stamos Katotakis, 1066821 Ontario Inc., William Waters, William R. Waters Limited, F.M.C. Investment Services Limited, and BNY Capital Corporation (13 January 1998), s. 3.3, from Ontario Court of Appeal File No. C43051; C43047; C43049 [Shareholder Agreement].
\item[32] Ibid., s. 3.3(d).
\item[33] Ibid., s. 3.3(e).
\end{footnotes}
up agreements and in the draft acquisition agreement between FMC and Linedata. It is reasonable to assume that the $12.20 price was based upon the price Linedata had indicated, at that point, that it would be prepared to pay for the FMC shares. It should be noted that the parties appear to have studiously avoided having Linedata formally offer to buy shares, or commit to launch a bid, before the selling notices were delivered.

Katotakis accepted each of these offers by written acceptance notice dated 29 December 2004. The acceptance specified that it was “subject to the terms and conditions set forth in the Selling Notice.” The purchase by Katotakis of the shares of the major non-Katotakis shareholders constituted a takeover bid within the meaning of the Ontario Securities Act. Katotakis was obligated, both under the terms of the shareholder agreement and as a matter of law,—since there did not appear to be an available formal bid exemption34—to launch a formal takeover bid for all of the shares of FMC (including both those shares referred to in the selling notices and all shares held by minority shareholders who were not parties to the shareholder agreement).

By the time Katotakis had delivered the acceptance notice, Linedata had launched its offer to purchase all of the outstanding shares of FMC in a cash and paper deal valued at $12.76 per share—materially more than the $12.20 price specified in the selling notices.35 Despite this higher bid, Katotakis maintained that he ought to be able to acquire all of the shares of the company—including from those public shareholders who were not parties to the shareholder agreement—at the lower price of $12.20.

He proposed to do so by first launching a formal takeover bid for all of the shares of the company at a price of $12.20. The parties to the shareholder agreement, who had delivered the selling notices (which Katotakis had accepted), would be obliged to sell their shares to him at this price. Since these shares, together with Katotakis’s own shares, totaled more than eighty per cent of all of FMC’s outstanding shares, Katotakis would be in a position after the bid was completed to undertake a going-private transaction to squeeze out (or, “squeeze in” if one prefers) the remaining minority shareholders. He proposed to do so. Katotakis had indicated his intention to pay the squeezed-out minority shareholders the same price per share—$12.20—

34 Although the offer to purchase shares from the other parties to the shareholder agreement was an offer to fewer than five people, such a purchase is only exempt from the formal takeover bid rules if the offer price does not represent more than a 15% premium above the market price for the purchased shares. The market price is determined by a 20-day trailing average. The bid was made for $12.20 per share on 29 December 2004. It disclosed that, as of 20 December 2004, the price of the shares had been $8.25, indicating that the bid price was significantly higher than 115% of the market price (see 1066821 Ontario Inc., “Offer to Purchase All of the Outstanding Common Shares and Class C Shares of Financial Models Company Inc.”, Takeover Bid Circular (29 December 2004) [Take-over Bid Circular], available through SEDAR Search for Public Company Documents, online: SEDAR <http://www.sedar.com/search/search_form_pc_en.htm> [SEDAR Search].

35 Linedata subsequently increased its offer to $14.65.
offered in his takeover bid, and it seemed to be assumed in the case that the going-private transaction could be successfully completed at this price. Minority shareholders voting against the transaction would typically enjoy appraisal rights that would entitle them to demand “fair value” for their shares. It is an open question whether, under these unusual circumstances, a court would be prepared to find that fair value was higher than $12.20. Given the risk, uncertainty, and expense of exercising appraisal rights, however, most dissenting shareholders may prefer to accept the offered price, provided it is not less than the price offered in the immediately preceding takeover bid.

As explained above, a second-step going-private transaction is often completed by way of an amalgamation squeeze. Since Katotakis would be certain of owning more than eighty per cent of FMC after his bid, the shareholder approval of the amalgamation required by corporate law would be assured. Recall that Rule 61-501 additionally requires minority shareholder approval, but expressly contemplates that shares tendered to a bid, including shares tendered pursuant to lock-up agreements, may normally be included as part of this minority vote. If the selling notices, as accepted by Katotakis, were considered equivalent to conventional lock-up agreements (rather than, for example, agreements that would make the selling shareholders and Katotakis joint actors) then the shares subject to those notices normally could be counted for purposes of the second-step minority approval requirement. Minority approval would therefore be assured, and the share interests of all of the remaining shareholders could be acquired by Katotakis at a price of $12.20, notwithstanding that another purchaser was ready and willing to pay a price more than two dollars higher for each share.

Recall that the underlying policy justification usually offered for permitting the shares acquired from tendering shareholders to be included in the postbid minority approval vote is that their free agreement to sell their shares indicates their approval of the terms of the transaction. The reason that shares acquired pursuant to lock-up agreements are usually treated in the same way is that, although they may inhibit auctions in specific cases, as a general matter lock-ups are often needed to entice bidders to make offers that they would otherwise not make.

The oddity in this case lies in two facts: none of the non-Katotakis shareholders actually wanted to tender their shares to the (lower) Katotakis bid, naturally

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36 See Take-over Bid Circular, supra note 34 at 27.
37 See e.g. OBCA, supra note 6, s. 185(4).
38 The fact that appraisal rights, owing to the expense and complexity of pursuing them, may offer illusory protection to minority shareholders is briefly explained by Philip Anisman in “Squeezing Out Minority Shareholders: A Comment” in Milosh, supra note 13, 229 at 236, n. 32.
39 The OSC has suggested that excluding such shares from voting could be regarded as a “significant imposition on the rights of substantial shareholders whose actions may be of benefit to the minority” and “a substantial shareholder can bring to the negotiations a sophisticated and informed party with negotiating power; looking for the best price ...” (Jan. 1999 Notice of Changes, supra note 25 at 502 [emphasis added]).
preferring to tender to the higher Linedata bid; and these lock-up agreements were not intended to bring an otherwise reluctant (higher) bidder to the table. On the contrary, the existence of the sale restrictions in the shareholder agreement that led to the delivery of the selling notices could only be expected to inhibit takeover auctions. Indeed, that was very much the point of them: to provide shareholders with a right to match (not to top) one—and only one—offer, rather than be drawn into a potentially lengthy and expensive auction. Did the existence of the right of first offer in the shareholder agreement make it impossible for the FMC shareholders to tender to the (higher) Linedata bid? Or could the reference they had strategically included in the selling notices to “terms and conditions substantially in accordance” with the draft Linedata lock-up agreement (agreements that had an “out” if the shareholders received a superior proposal) free the non-Katotakis shareholders to auction their shares to the highest bidder?

IV. The OSC Hearing

The Special Committee of FMC applied to the OSC for orders under subsections 104(1) and 127(1) of the Securities Act. The applicants’ allegation, simply put, was that Katotakis’s takeover bid did not comply with Ontario takeover bid rules and therefore should be halted, pursuant to section 104. Moreover, the Katotakis bid was said to be “abusive of the capital markets” and against the public interest, and therefore should be stopped by way of a cease-trade order under the OSC’s broad subsection 127(1) public-interest powers.

The OSC disagreed with the applicants. The commissioners on the panel found nothing abusive in Katotakis’s actions. They appeared to agree with the submission by counsel for Katotakis that each of the public shareholders of FMC should reasonably have anticipated that “one party to the Shareholder Agreement could eventually control 82% of the Shares,” and so would have “expected either to remain as a minority shareholder or be taken out in a Follow-on Transaction.” The panel moreover found that the Katotakis offer complied with Rule 61-501; there was thus “no basis for an order under section 104 of the Act.”

Nor was there any reason, in the panel’s view, to make an order under the broad public-interest jurisdiction of section 127, since it found “that no facts or evidence before us suggest any artificiality to the various transactions, nor any intention or engineering by Katotakis to defeat the reasonable expectations of the shareholders.”

It is intriguing that the OSC’s decision was premised on an assumption that the court would eventually reject. Specifically, the OSC concluded that there could not have been any defeat of minority shareholder expectations that there would be an

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40 Supra note 3.
41 Financial Models, supra note 2 at 2187.
42 Ibid. at 2189.
43 Ibid. at 2190.
auction of the FMC shares. Minority shareholders could not expect an auction because “FMC was never in ‘play’ for an auction. FMC could not be in play for an auction unless and until there were Selling Notices delivered under the Shareholder Agreement which were not accepted.”

It is implicit in this statement that the OSC did not contemplate that the selling notices delivered to Katotakis could incorporate an “out” allowing the shareholders delivering them to recant their offer to sell and accept a superior proposal from a third party (subject only to the obligation to, once again, give Katotakis the opportunity to match the superior proposal). Indeed, the OSC went on to state:

We agree with counsel for Katotakis and counsel for staff, that the Shareholder Agreement is, for these purposes, tantamount or functionally equivalent to a “hard” lock-up agreement which crystallized on December 29, 2004 when the Selling Notices were accepted.

This analysis raises a number of issues. First, even if the shareholder agreement were equivalent to a lock-up agreement, is it clear on these facts that the shares acquired pursuant to this sort of lock-up agreement should necessarily be counted in calculating the “majority of the minority”? At one time, the OSC had proposed that shares obtained pursuant to a lock-up from shareholders who “effectively controlled” the corporation could not be counted as part of the “majority of the minority”; a view that was ultimately abandoned as a hard and fast rule, but which may still, on unusual facts such as those raised by this case, be pertinent. Further, it would seem that the OSC did not anticipate that the subsequent court ruling would, in effect, make the accepted selling notices functionally equivalent to soft lock-ups, rather than hard lock-ups. To the extent that the selling notices were merely soft lock-up agreements, surely FMC could indeed be “in play” for an auction, thus undermining, at least in part, the basis of the OSC’s decision.

But even if the OSC had, in fact, characterized the selling notices as soft lock-ups (as the court subsequently, in effect, did) would the panel have reached a different conclusion? After all, during the process of formulating Rule 61-501, the OSC explicitly stated that it did “not propose to distinguish between hard and soft lock-up agreements.” It might be argued, accordingly, that nothing material turns on the fact that the court’s understanding of the accepted selling notices differed from that of the OSC. The complication here is that the panel not only characterized the selling notices as equivalent to hard lock-up agreements, but assumed that all minority shareholders who had purchased shares in FMC in the market must be taken to have understood that their future rights would always be subject to the existence of such hard lock-up agreements, such that they could never have expected to benefit from an unrestrained auction for their company’s shares. It is this latter assumption—implicit

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44 Ibid.  
45 Ibid. at 2191.  
47 Dec. 1999 Notice of Changes, supra note 24 at 7840.
but critical to the panel’s reasoning—that is largely undone if there were a lawful way for parties to the shareholder agreement to facilitate an auction for the company’s shares despite the existence of the rights of first offer and first refusal. Of course, the subsequent judgments of the Ontario Superior Court of Justice and the Court of Appeal suggested just such a possibility.

V. The Court Hearing

The OSC Hearing was held 28 January 2005, and the decision was rendered that day (although the panel’s reasons were not issued until 27 February 2005). In the meantime, an application had been made to the Superior Court of Justice to determine two additional legal issues: whether Katotakis had complied with section 96 of the Securities Act\(^\text{48}\) (an issue that will not be dealt with here); and whether the selling shareholders could, in fact, include a superior proposal condition in their selling notices. Implicit in the second issue was the question of whether the form of selling notices they had already delivered to Katotakis effectively included such a condition.

Both the trial judge and the Court of Appeal accepted the argument that the superior-proposal provisions of the draft Linedata lock-up agreements could be, and indeed were, effectively incorporated into the selling notices that had been delivered to and accepted by Katotakis. The effect of this ruling was that the right of first offer contained in the FMC shareholder agreement could not function as an effective takeover defence.\(^\text{49}\) The non-Katotakis shareholders were not in the end bound to sell


\(^{49}\) The hypothetical possibility of a right of first refusal being used as a takeover defence was raised by Burton Kellock in a critique of *GATX v. Hawker Siddeley Canada* (1996), 27 B.L.R. (2d) 251, 62 A.C.W.S. (3d) 700 (Ont. Gen. Div.) [*GATX cited to B.L.R.\]*, a case in which Mr. Kellock had appeared on behalf of the unsuccessful party. See Burton H. Kellock, “The Relationship Between Rights, Such as Rights of First Refusal and Tag Along/DrAg Along Rights and the Oppression Remedy” in *Canadian Bar Association of Ontario Conference on Shareholder Rights, Oppression and Good Faith: In Tandem or a Tangle* (N.p.: Canadian Bar Association—Ontario, 1997) Tab 7 at 40. The facts in *GATX* were quite different because the right of first refusal in that case was contained in a shareholder agreement relating, not to the shares of the publicly traded company (Hawker Siddeley), but rather a private company (CGTX) of which Hawker Siddeley was a large shareholder. Nevertheless, since the shares in CGTX represented substantially all the assets of Hawker Siddeley, by insisting that the right of first refusal could not be subverted by a two-step transaction that was technically permitted by the words of the shareholders’ agreement, the court’s decision raised the
their shares to Katotakis for the $12.20 per share price they had specified in their selling notices. They were, instead, free to entertain superior proposals from other bidders, subject only to the requirement that before accepting any such superior proposal they must first give to Katotakis the opportunity to match it.

There are a myriad of interesting implications arising from this decision. In a forthcoming paper, for example, I will discuss the case in terms of auction theory.50 In the remainder of this short comment, however, I will offer only a few modest observations.

It must be noted that the outcome in Katotakis arose from an interpretation of the right of first offer, not the right of first refusal, as the selling notices were delivered before Linedata had made a formal offer for FMC’s shares.51 By delivering selling notices in this case, which were said to be subject to the terms and conditions of the draft lock-up agreements, each selling shareholder was effectively saying to Katotakis: “I am offering to sell my shares to you for $12.20 each. But if I receive a higher offer from someone else before our deal closes, then I am instead offering to sell to you for that higher price, whatever it might be.”

It may be argued that if Katotakis had been unwilling to accept a selling notice on such conditions, he was certainly free to reject it. Such a response would have been impractical, however. If he had rejected the selling notices, under the terms of the shareholder agreement, the offering shareholders would have been free to sell their shares at a price no lower than that contained in the respective notices to anyone they chose within a sixty-day period. In other words, rejecting the selling notice would have meant that Katotakis would have forfeited even the right to match an eventual competing offer. Yet, if including such a superior proposal condition in this sort of selling notice is permissible (as the court held it to be), there are at least two practical difficulties.

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51 This important distinction was specifically referred to in a letter written by one of the selling shareholders (William R. Waters Limited) to Mr. Katotakis. The letter stated, in part:

You have misconstrued section 3.3 [of the shareholder agreement] which is designed, as its title Right of First Offer and First Refusal suggests, to provide rights to the shareholders in two different sets of circumstances: the first being those in which no bona fide offer has been received from a Third Party ... ; and, second, if a Shareholder has received a bona fide offer ... from a Third Party ... [c]learly the circumstances as at the date of the Selling Notice were the first of these two sets of circumstances, as no offer had been made as at the date of the Selling Notice ... [a]ccordingly, section 3.3(e) of the Shareholder Agreement [i.e., the right of first refusal] is inapplicable to both the Selling Notice and the rights of the parties to the Shareholder Agreement flowing from the Selling Notice” (Compendium of the Respondents, 1427937 Ontario Inc. and William R. Waters Limited, from Ontario Court of Appeal File No. C43051, Tab 6).
First, how precisely is the nonselling shareholder (i.e., a person in Katotakis’s position) expected to quantify the financial obligation to which he or she becomes subject by choosing to accept an offer when the selling price is, evidently, something of a moving target?

Second (and perhaps more fancifully), why would it not be equally valid for a selling shareholder to deliver a selling notice subject to even broader conditions? Would it be acceptable, for example, for a selling notice to provide, “I am offering to sell to you for $X, but if I receive an offer of at least $X from someone else (a “Competing Offer”), then I am offering to sell to you only at some price higher (even, perhaps, “materially higher”) than that Competing Offer”? Note that including such a condition in a selling notice delivered pursuant to the right of first offer would wholly defeat the right of first refusal. Even if a third-party offer were subsequently received by a selling shareholder, there would be nothing to require the selling shareholder to provide the nonselling shareholder the right to match this offer before agreeing to sell to the third party.

To understand why, recall that the rights of first refusal in the FMC shareholder agreement were triggered only when a third-party offer was received prior to the delivery of a selling notice.\(^\text{52}\) True, the nonselling shareholder (like Katotakis) would retain the “right” to participate in an auction that he or she could win if (but only if) his or her bid were higher than (not merely equal to) any other bid. But such a right is not really a right at all. The selling shareholders would always be more than happy to allow the highest bidder to acquire their shares for the highest price.

By accepting such a selling notice, the recipient’s rights of first offer and first refusal would effectively be eliminated (at least for the ensuing sixty-day period) in favour of the nugatory right to participate in an auction.\(^\text{53}\) If the notice were rejected, however, the shareholders who had delivered the notice could freely sell the shares, defeating in a sense the recipient’s contracted-for rights of first offer and first refusal. Nor does it seem probable that Katotakis, or any of the other parties to the shareholder agreement, would have anticipated at the time the rights of first offer and first refusal were originally negotiated that the protection such provisions are normally thought to provide could prove to be so illusory. For that matter, such an interpretation does not appear to accord with the OSC’s understanding of such

\(^{52}\text{Shareholder Agreement, supra note 31, s. 3.3(e).}\)

\(^{53}\text{It is noteworthy that the court in GATX condemned the elaborate arrangements of the defendant, who was seeking to circumvent a right of first refusal in a shareholder agreement. The court explained that, if this complex plan were upheld, “the Right of First Refusal would cease, in effect, to be a right of first refusal. It would become instead a right to participate in a bidding war ... ” (supra note 49 at para. 79). Mr. Katotakis’s counsel prominently referred to GATX, but the Court of Appeal regarded it as readily distinguishable from the Katotakis matter, saying curtly (without supporting analysis) that GATX “involved a scheme to deprive a party of rights of first refusal and is distinguishable” (Katotakis, supra note 2 at para. 16).}\)
provisions either, at least based upon its comment, quoted earlier, that the company was not in “play.”54

One appreciates that the concerns raised by such a hypothetical case may be dismissed; the example, it may be said, simply pushes the reasoning in the Katotakis case too far. Surely it could not have been the intention of the court to permit selling shareholders to effectively propose an amendment to the shareholder agreement that would constrain or arguably eliminate a valuable right, then force the nonselling shareholder to accept this unilateral amendment by making it a term or condition of the selling notice. While the courts might well be prepared (as in Katotakis) to blunt the effectiveness of the right of first refusal, it would be surprising if they would sanction a scheme that would render such a right wholly ineffective. Alternatively, it is possible that the Katotakis case is sui generis since it is unusual for rights of first offer to be drafted (as they were in this case) to permit the inclusion of additional conditions in the selling notices.55 The larger point remains: it is not entirely clear why, strictly speaking, the principles upon which the Katotakis case was decided would forbid this more aggressive selling strategy.

And what of the OSC’s decision to permit Katotakis to complete a second-step going-private transaction at $12.20 per share? That decision, of course, became academic once the court made it possible for the non-Katotakis shareholders to entertain higher offers. The OSC’s decision thus appeared to be sound, given the assumptions upon which it was based. When the court subsequently undermined one of those key assumptions, the OSC’s decision became largely irrelevant. Yet it is interesting that the OSC’s approach appeared considerably more formalistic (i.e., legalistic) than that of the court, and accordingly, in this instance, less protective of the interests of minority shareholders of a public corporation than the court’s ruling. It suggests a somewhat peculiar reversal of roles; the OSC has historically positioned itself as a defender of the interests of minority shareholders of corporations that are the targets of takeover bids. Could this result be explained, at least in part, by the fact that the OSC has accepted that the purpose of the going-private rules is to “regulate conflict of interest situations” and, accordingly, has chosen to “de-emphasize the ‘expropriation’ theory of going private transactions”?56

Conclusion

The thorny issues of interpretation of the FMC shareholder agreement eventually became moot. Neither Katotakis nor Linedata ultimately acquired the shares of FMC.

54 *Financial Models*, *supra* note 2 at 2190.
55 I am grateful to James Baillie for this observation.
56 Dec. 1999 Notice of Changes, *supra* note 24. For a discussion of the “conflict of interest” versus “expropriation” basis for the regulation of going-private transactions, see Singer, *supra* note 13. Phillip Anisman has been a strong advocate for emphasizing the “expropriation” aspect of these transactions (Anisman, *supra* note 38).
Once the auction-inhibiting effect of the shareholder agreement had been broken, a subsequent bidder for FMC’s shares emerged, offering $17.70 per share.57 The major shareholders—including Katotakis—entered into lock-up agreements with this new bidder, SS & C. The bid was successful; SS & C acquired about 99.9 per cent of the outstanding shares58 and promptly initiated a compulsory acquisition under section 188 of the OBCA to acquire all of FMC’s remaining shares.59 FMC then applied to the securities regulators of Ontario, Quebec, Saskatchewan, Newfoundland and Labrador, and Nova Scotia, for an order deeming FMC to cease to be a reporting issuer. That order was granted on 27 May 2005.60

The statutory and regulatory scheme governing more straightforward takeover bids and postbid transactions ran its course, and concerns over the nuances of shareholders’ proprietary and private contractual rights fell by the wayside, at least for the time being. But the surprising sort of interplay between privately negotiated shareholder rights and the regulation of takeover bids that this case revealed may well arise again. The courts or the securities regulators, and not the serendipitous emergence of a generous topping bid, will finally need to determine the extent of the interests of minority shareholders.

60 28 O.S.C. Bull. 4887 (3 June 2005).