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Board Representation Does Not Always Solve Issues With Activists

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The decision to provide an activist shareholder with board representation is not one to be taken lightly, and is no guarantee of quiet times ahead. Just ask Vancouver's BENEV Capital Inc., which is facing ongoing issues with Difference Capital Financial Inc. (DCF), after agreeing to add three DCF nominees to the company's board of directors.

The evolution of BENEV's business

BENEV emerged from the ashes of Bennett Environmental Inc., a soil remediation company that became the subject of fraud allegations by the Environmental Protection Agency in 2006. In the wake of the EPA investigation, Bennett replaced its board and executive management, and re-branded as BENEV. The company also sold its waste treatment operations, effectively becoming a shell company with cash, tax losses and no debt.

DCF holds a 28.4 percent stake in BENEV, most of which it acquired in March of this year. In May, DCF announced its intention to nominate an alternate slate to replace BENEV's incumbent board of directors. In order to avoid a dispute, BENEV agreed to increase its board to seven directors, and three DCF nominees were added to the BENEV board at the company's June 30 annual meeting of shareholders.

Following BENEV's annual meeting, the company announced it had entered into an agreement with Franworks Franchise Corp., a multi-brand restaurant chain based in Alberta, to acquire the trademarks related to Franworks' three brands - Original Joe's, State & Main and Elephant & Castle - for $103.0 million in cash and shares.

Franworks will license the trademarks from BENEV for a royalty on the gross sales of its restaurants, representing an annual payment of approximately $12 million. The model is similar to that utilized by A&W Revenue Royalties Income Fund and Pizza Pizza Royalty Corp., which license the A&W and Pizza Pizza trademarks in exchange for royalties on sales by certain Canadian restaurants.

Difference Capital objects to the Franworks transaction

On July 7, DCF issued a press release indicating its nominees had not participated in the decision to approve the Franworks transaction (which approval was presumably obtained prior to their election). DCF declared the deal a "dramatic shift in strategy" that had been implemented without consulting shareholders, and insisted that BENEV cease activity in such regard until shareholders have had an opportunity to speak and vote on the matter. DCF also referred to the timing and terms of the deal as "disconcerting".

The fact that DCF went public with its concerns, rather than have its nominees address them directly with the BENEV board, illustrates the fact that board representation does not necessarily eliminate ongoing disputes with activists.

Though the timing of the announcement was problematic, it seems unlikely that DCF will be able to do anything more than complain. Since 2012, BENEV has been signaling its intention to complete one or more "transformative transactions" which "may or may not be in the environmental space". In addition, the company has specifically stated that the Franworks transaction is subject to Toronto Stock Exchange and shareholder approval.

As part of its review, the TSX will presumably consider whether majority approval will suffice or a special resolution (potentially excluding interested shareholders, if any) will be required to effect the deal. In that regard, BENEV has indicated that shareholders holding in aggregate 33.8 percent of BENEV's shares have indicated they intend to support the transaction.
The company intends to convene a special meeting of shareholders to consider the Franworks transaction in August.