

Canadian Securities Administrators requests comments on activist short selling

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On December 3, 2020, the Canadian Securities Administrators (CSA) published consultation paper 25-403 – *Activist Short Selling*, to facilitate a discussion of concerns relating to activist short selling and the potential impact on capital markets in Canada. The term "activist short selling" refers to when an individual or entity takes a short position in a security and then publically shares information that is likely to have a negative impact on the price of such security in an effort to realize a profit.

In 2019, the CSA formed a committee that analysed activist short selling campaigns targeting Canadian issuers and reviewed relevant academic literature. The empirical analysis was limited to activist short selling campaigns identified by a third-party data provider, Activist Insight (AI), which focused on tracking activist short sellers on both the long and short side. It is noted that AI's database only tracks campaigns by prominent activist short sellers.

The CSA noted that while activist short selling is not new, it has become more prevalent in recent years and that with this increase, there has been an associated rise in concerns and complaints from stakeholders. The consultation paper sets out the initial results of its research, summarizes stakeholder concerns, and poses questions to stakeholders and invites feedback on, *inter alia*, whether the rules and regulations pertaining to activist short selling in Canada should be revisited.

While activist short sellers are subject to general securities law rules and requirements, they are not currently subject to specific regulatory requirements in most CSA jurisdictions. In its discussion of the regulation of activist short selling in Canada, the CSA noted that "activist short selling campaigns can be understood as occurring on a spectrum and their utility to the market ultimately depends on whether the information being disseminated is material and neither false nor misleading." While much of stakeholder concern is focused on the overall impact of activist short selling on the markets, the CSA also notes that there is stakeholder concern surrounding potential regulatory intervention inhibiting beneficial short selling activities, as well as detracting from the price discovery process.

Notable findings from the consultation paper include:

- Generally, activist short sellers gravitate towards the securities of issuers and sectors where an overvaluation is perceived.
- Campaigns targeting Canadian issuers tended to focus on larger issuers compared to the broader Canadian market, with the median market capitalization being \$867 million and the average market capitalization being \$4.5 billion. This finding is consistent with U.S. academic studies.
- Between 2010 and September 2020, 73 Canadian issuers have been the target of 116 activist short selling campaigns. According to AI, 16 of the identified campaigns remain active.
- Annually there have been no more than five Canadian targets per every 1,000 Canadian listed issuers. U.S. issuers are targeted more often, with there being 21 targets per 1,000 U.S. issuers annually.
- In terms of price impact, approximately 75% of targets experienced a negative price impact on the day of the first announcement by the campaign and up to a month following such

announcement. However, the extent of the short-term price impact varied across targets and over time.

- Across the 116 identified Canadian campaigns, 40% involved allegations of fraud at the issuer, with the most common type of fraud allegation being a stock promotion scheme.
- Across the 73 identified Canadian targets, approximately 73% of targets pursued certain responses during the campaign, such as replacing an executive or halting trading of the issuers stock.

The CSA invites feedback from stakeholders on the issues identified in the consultation paper, including the following:

- What is the perception of activist short sellers and what are some examples of conduct in activist short selling campaigns that stakeholders view as problematic?
- Whether issuers are reluctant to approach securities regulators when they believe that they are being unfairly targeted by an activist short seller and why such issuers are reluctant?
- Whether there is specific evidence suggesting that Canadian markets are more vulnerable to activist short selling and how such vulnerabilities may differ from other jurisdictions?
- Whether the existing regulatory framework in Canada is adequate to address the risks associated with problematic activist short selling and whether the existing enforcement mechanisms adequately deter problematic activist short selling?
- Whether there are other regulatory or remedial provisions that could be considered to improve the deterrence of problematic activist short selling?

Feedback on the consultation paper must be submitted in writing by March 3, 2021. The consultation paper is available [here](#).

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