Canadian Public Company Mergers & Acquisitions

A practical guide to the issues surrounding acquisitions of public companies in Canada.

OSLER

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Acquisition Structures

While several different methods exist to acquire control of a Canadian public company, M&A transactions in Canada are most commonly effected by a "plan of arrangement" and less frequently by a "take-over bid." These transaction structures are outlined below.

PLAN OF ARRANGEMENT

Overview

A statutory arrangement, commonly referred to as a "plan of arrangement," is a voting transaction governed by the corporate laws of the target company's jurisdiction of incorporation. It is first negotiated with the target company's board of directors and remains subject to the approval of the target company's shareholders at a special meeting held to vote on the proposed transaction. Notably, an arrangement also requires court approval. Due to the ability to effect the acquisition of all of the outstanding securities of a target in a single step and its substantial structuring flexibility, the majority of board-supported transactions are structured as arrangements.

Court Supervision and Approval

Unlike any other transaction structure typically used to effect a change of corporate control, an arrangement is a court-supervised process.

The target company applies to court to begin the process of effecting the arrangement. An initial appearance will be made before the court for an interim order setting the procedural ground rules for the arrangement, which is almost always uncontested. The interim order will specify, among other things: (i) the manner in which a special meeting of the shareholders will be called and held (e.g., form of proxy solicitation materials and disclosure documents to be sent to security holders, record date for establishing security holders entitled to vote on the transaction, applicable notice periods, time and place of meeting); (ii) the persons entitled to vote at the meeting; (iii) whether any class of persons will be entitled to a separate class vote; and (iv) the requisite approval thresholds required to approve the arrangement.

Due to the ability to effect the acquisition of all of the outstanding securities of a target in a single step and its substantial structuring flexibility, the majority of board-supported transactions are structured as arrangements.

Once the meeting of the target company shareholders is held and the arrangement resolution has been approved by the requisite majorities of security holders, the target company seeks a final court order approving the arrangement. The final order will be granted if the court is satisfied that the arrangement is "fair and reasonable." While disaffected stakeholders can appear at the final order hearing to challenge the arrangement, the vast majority of arrangements are approved without opposition.

Shareholder Approval

Although the shareholder approval threshold for an arrangement is generally subject to the discretion of the court and addressed at the procedural hearing when the interim order is sought and obtained, an acquiror will typically propose that it seek the same approval threshold as would be required under the applicable corporate law statute governing the target company if the arrangement steps were effected outside the arrangement process. In most Canadian jurisdictions this threshold is 66⅔% of the votes cast at the meeting of the target company's shareholders. The approval of a majority of the minority shares voted at the meeting may also be required in circumstances where the business combination rules under securities law apply to the transaction (see "Minority Shareholder Protections" below). Depending on the jurisdiction of incorporation, option holders may be afforded the right to vote as part of the same class as common shareholders. Other convertible securities like warrants and convertible debentures are typically not given the right to vote in an arrangement, unless their rights under the applicable indentures or contracts are being altered as part of the arrangement in a manner that is not fair and reasonable.

TAKE-OVER BID

Overview

A take-over bid is a transaction by which the acquiror makes an offer directly to the target company's shareholders to acquire their shares. Although the board of directors of the target company has a duty to consider the offer and an obligation to make a recommendation to its shareholders as to the adequacy of the offer, the take-over bid is ultimately accepted (or rejected) by the shareholders. As the support of the target board of directors is not legally required, a take-over bid is the only practical means to effect an unsolicited or hostile acquisition. Take-over bids are also used infrequently for friendly transactions. A take-over bid is the substantive equivalent of a tender offer under U.S. securities laws.

Legislation and Governing Principles

Take-over bids are regulated under a uniform regime adopted by each province and territory.

A take-over bid must be made to all registered holders of the class of voting or equity securities being purchased (and sent to all registered holders of securities convertible into or exercisable for such voting or equity securities), but need not be made for all shares of that class, such that "partial bids" are permitted. The same price per security must be offered to each holder of the class of securities subject to the bid.

There are also minimum standards relating to the conduct of the bid, including disclosure requirements, the timing and delivery of take-over bid materials, and rules designed to ensure the equal treatment of all security holders.

A formal take-over bid is made pursuant to a disclosure document commonly referred to as a take-over bid circular. This document must contain prescribed information about the offer, the offeror and the target company. When the offered consideration consists (in whole or in part) of securities of the offeror, the circular must also include prospectus-level disclosure about the offeror. It is generally not necessary to pre-clear the contents of a take-over bid circular with the securities regulators in Canada and the take-over bid circular is not generally subject to their review once it is filed, absent a complaint being made.

Effective May 9, 2016, fundamental changes were made to the Canadian take-over bid regime. The new provisions will increase the amount of time afforded to a target issuer to respond to a hostile bid, effectively resulting in a 105-day "permitted bid" regime. The regime will have important implications for both tactical and strategic rights plans, and may also influence how transactions are structured in the future.

Under the new take-over bid regime, all non-exempt take-over bids (including partial bids) are subject to the following requirements:

- **50% Minimum Tender Requirement:** Take-over bids are subject to a mandatory, non-waivable minimum tender requirement of more than 50% of the outstanding securities of the class that are subject to the bid, excluding those beneficially owned, or over which control or direction is exercised, by the bidder and its joint actors (the Minimum Tender Requirement).
- **10-Day Extension Requirement:** Following the satisfaction of the Minimum Tender Requirement and the satisfaction or waiver of all other terms and conditions, take-over bids will be required to be extended for at least an additional 10-day period (the 10-Day Extension Requirement).
- **105-Day Bid Period:** Take-over bids will be required to remain open for a minimum of 105 days, subject to two exceptions discussed below – see "Timing and Delivery Requirements" (the 105-Day Requirement).

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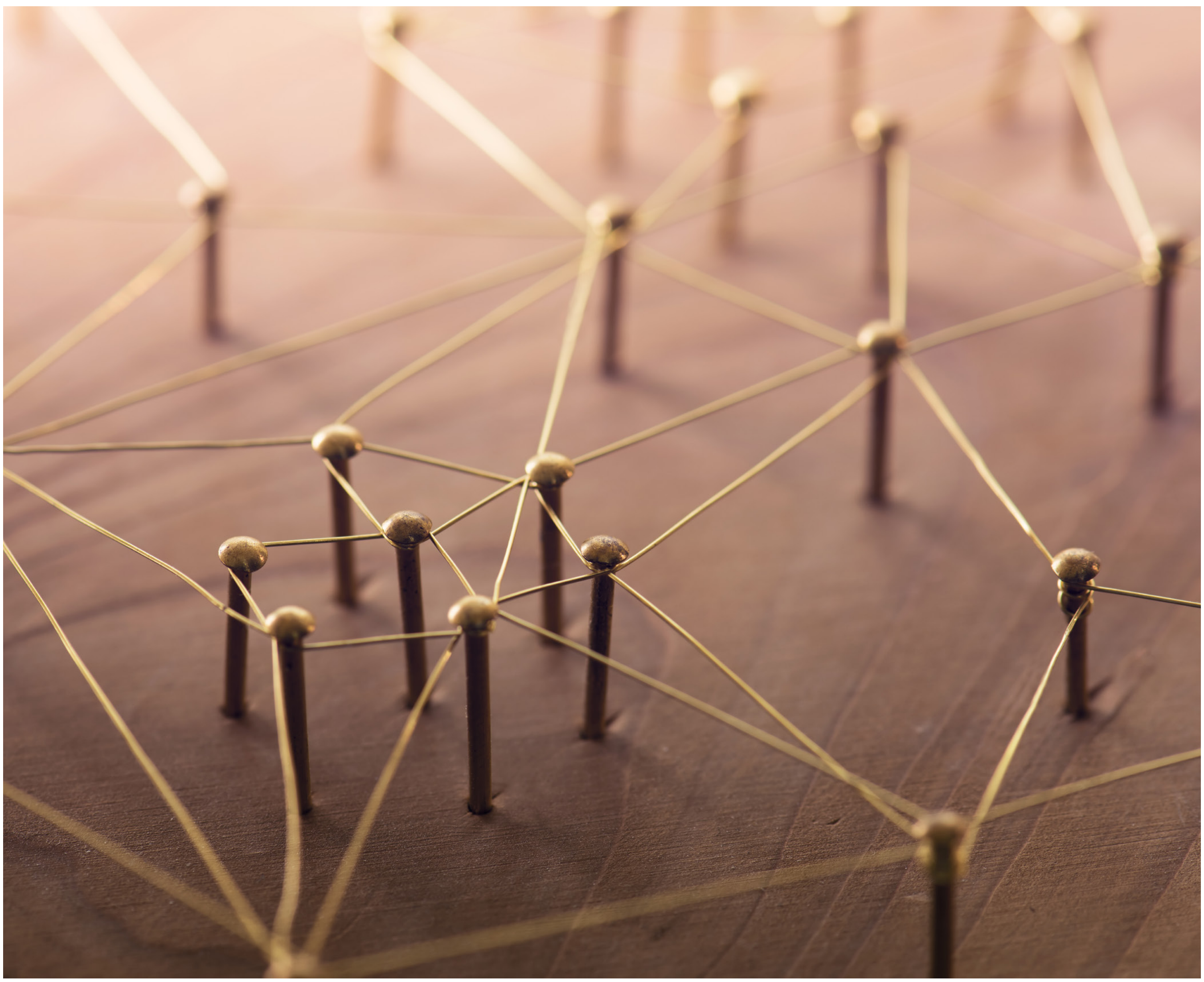
TAKE-OVER BID RULES

When Does a Take-Over Bid Occur?

Determining whether a take-over bid exists is based on objective factors and, in particular, on the percentage of voting or equity securities beneficially owned or controlled by the offeror (and any joint actors) plus the number of additional securities subject to the take-over bid (as opposed to the more subjective factors used in the U.S., such as the method and timing of acquisition). The take-over bid threshold is 20% of any class of voting or equity securities. In determining whether the threshold level of ownership by the offeror will be crossed, the number of securities beneficially owned by the offeror includes securities that the offeror has a right or obligation to acquire within 60 days (e.g., through options, warrants or convertible securities) and securities held by affiliated entities and joint actors. In order to attract the jurisdiction of Canadian take-over bid rules, the offer must be made to a person who is either in Canada or is registered in the books of the target company with a Canadian address.

Equal Treatment of Shareholders

A cornerstone objective of the take-over bid regime is the equal treatment of all security holders of a target company. To this end, the take-over bid rules: (i) require that all holders of the same class of securities of the target company be offered identical consideration; (ii) prohibit side deals or "collateral benefits" that would have the effect of providing certain holders with consideration of greater value than other holders (subject to certain exceptions for employment compensation arrangements); and (iii) integrate securities purchases made in the 90-day period preceding the take-over bid by requiring the bidder to offer to purchase the same percentage of securities and offer the same amount and form of consideration (or the cash equivalent thereof) as was offered in any pre-bid purchases, other than normal course purchases on a published market.



Timing and Delivery Requirements

Take-over bids may be commenced by publishing an advertisement in at least one major daily newspaper in each province (including an advertisement in French in the Province of Québec in circumstances where the target company has shareholders in Québec) provided that the offeror files the bid circular with securities regulators and delivers it to the target company on or before the date of the advertisement and requests a shareholders' list from the target company. The take-over bid circular must be delivered to the target company's registered shareholders within two business days of receipt by the offeror of the shareholders' list.

The target company is, in turn, required to file with securities regulators and deliver to the target company's registered shareholders a directors' circular no later than 15 days after the date of the take-over bid. The directors' circular must: (i) contain a recommendation that shareholders accept or reject the take-over bid; (ii) adopt a neutral position to the effect that the board is unable to make or is not making a recommendation and the reasons why the directors have remained neutral; or (iii) advise shareholders that the directors are considering whether to make a recommendation, provided that the directors ultimately make a recommendation or adopt a neutral position at least seven days before the expiry of the bid.

Under the 105-Day Requirement, take-over bids will be required to remain open for a minimum of 105 days, subject to two exceptions. First, the target issuer's board of directors may issue a "deposit period news release" in respect of a proposed or commenced take-over bid providing for an initial bid period that is shorter than 105 days but not less than 35 days. If so, any other outstanding or subsequent take-over bids will also be entitled to the shorter minimum deposit period counted from the date that other take-over bid is made. Second, if an issuer issues a news release that it has entered into an "alternative transaction" – effectively a friendly change of control transaction that is not a take-over bid, such as an arrangement – then any other outstanding or subsequent take-over bids will be entitled to a minimum 35-day deposit period counted from the date that other take-over bid was or is made.

When all the terms and conditions of the take-over bid have been satisfied or waived at the expiry of the initial deposit period (which includes an extension of the deposit period prior to the mandatory 10-Day Extension Requirement), the offeror must immediately take up all deposited securities and then pay for them as soon as possible and in any event not later than three business days after the taking up of the securities.

Shares deposited to a bid may be withdrawn at any time before they have been taken up by the offeror. Moreover, deposited shares that have not been taken up may be withdrawn at any time up to 10 days after the date of any notice of change or any notice of variation in the offer unless the variation consists solely of the waiver of a condition in an all-cash bid, or solely of an increase in consideration and the bid is not extended for more than 10 days.

The take-over bid threshold is 20% of any class of voting or equity securities. In determining whether the threshold level of ownership by the offeror will be crossed, the number of securities beneficially owned by the offeror includes securities that the offeror has a right or obligation to acquire within 60 days (e.g., through options, warrants or convertible securities) and securities held by affiliated entities and joint actors.

Bid Conditions

A take-over bid may be subject to the satisfaction or waiver of conditions, including conditions relating to regulatory approvals, material adverse changes, market interruptions and other contingencies. However, a take-over bid may not be conditional upon financing. Where the consideration offered pursuant to a take-over bid is cash or has a cash component, the offeror must make adequate arrangements prior to launching the bid to ensure that required funds are available to make full payment for the target company's securities. Accordingly, it is customary for the offeror to obtain a binding commitment from a financing source prior to the launch of the take-over bid to the extent it does not have sufficient cash resources already available. The financing arrangements required to be put in place may themselves be subject to conditions if the offeror reasonably believes the possibility to be remote that, if the conditions of the take-over bid are satisfied or waived, the offeror will be unable to effect payment due to a condition to the financing not being satisfied. Accordingly, most offerors ensure that, at least substantively, the conditions of the take-over bid include any conditions to the financing. Alignment of the bid conditions and the drawdown conditions is designed to ensure that the offeror is not placed in the impossible position of being obligated to transact under its take-over bid (due to all conditions having been satisfied) but unable to draw down on financing commitments (due to certain conditions not having been satisfied).

Minimum Tender Condition

Under the new take-over bid regime, an offeror must comply with the Minimum Tender Requirement. The offeror may also set a higher tender threshold where the offeror's objective is to acquire all of the outstanding shares of the target company. In that event, there will also be a minimum tender condition, which is typically set at 66⅔% (75% in the case of some B.C. corporations) ownership by the offeror in order for the offeror to be certain that it will acquire sufficient shares to effect a second-stage, going private transaction.

If an acquiror acquires more than 90% of the securities subject to the offer (which excludes shares held at the date of the take-over bid by the acquiror, its affiliates and associates), Canadian federal and provincial corporate legislation provide a procedure for the compulsory acquisition of the balance of the shares. No shareholder vote is required, although shareholders have the right to dissent and be paid the fair value of their shares.

When less than 90% but more than 66⅔% (or 75% in the case of some B.C. corporations) of the outstanding shares are acquired, the offeror can complete the acquisition of 100% of the target company by means of a subsequent going private transaction. This will require holding a special meeting of the shareholders of the target company to vote on the transaction. In this circumstance, the offeror can vote the shares that were acquired under the offer. Since the voting threshold under applicable corporate law for approval of a going private transaction (such as an arrangement or an amalgamation) is 66⅔% (or 75% in the case of some B.C. corporations) of the votes cast at the meeting of shareholders, the offeror can be assured that the transaction will be approved.

10-Day Extension Requirement

The 10-Day Extension Requirement is designed to eliminate coercion of shareholders to tender to the take-over bid, as they will be assured of an opportunity to tender after the take-over bid is already successful.

Partial Take-Over Bids

Partial take-over bids are permitted. However, bids for "any and all shares" tendered or bids for "up to 100%" of the outstanding shares are not permitted as a result of the Minimum Tender Requirement. Although partial bids for less than all of the outstanding shares of a target company are legally permissible, the Minimum Tender Requirement makes it especially difficult for them to succeed. This is because the Minimum Tender Requirement applies notwithstanding that a bid is being made for less than all of the shares. Accordingly, those shareholders that would be willing to sell to the partial bid may be prevented from doing so because other shareholders who hold more than 50% of the shares of the class choose not to tender to the bid.

Integration of Market Purchases

A take-over bid must be made for at least the same amount and form of consideration (or the cash equivalent) and for at least the same percentage as any purchases made by the offeror from any target company shareholder within the 90 days preceding the bid, unless those purchases were normal course purchases on a published market.

Once the take-over bid is announced, the offeror is generally prohibited from making any purchases other than through the take-over bid until the take-over bid expires. However, the offeror is permitted to purchase up to 5% of the class of securities subject to the bid (including securities convertible into that class) if, among other things: (i) the intention to make such purchases is disclosed in the take-over bid circular or in a news release issued at least one business day prior to making such purchases; (ii) the purchases are made in the normal course on a published market; and (iii) the offeror files a daily press release disclosing (among other things) the number of securities purchased and the price paid.

After the expiration of a take-over bid, the offeror is prohibited from making any further purchases for 20 business days except for normal course purchases on a published market.

Take-Over Protection for Inferior-Voting Rights

Many Canadian companies have made use of multiple-voting, non-voting and restricted-voting securities in their financing and capital structures. Under the Toronto Stock Exchange rules, listed companies with such a share structure are generally required to provide take-over "protection" (known as "coat-tail" provisions) to holders of subordinate voting, non-voting or restricted-voting shares. The coat-tail provisions are included in the share capital provisions of the subordinate voting, non-voting or restricted voting shares or are included in a trust agreement between the target company, the holders of the superior voting shares and a trustee for the benefit of the holders of the subordinate voting, non-voting or restricted voting shares. Coat-tail provisions generally permit holders of subordinate voting, non-voting or restricted voting shares to participate on an equivalent basis as a holder of superior voting shares in the event a formal take-over bid is made for those superior voting shares without also being made to holders of subordinate voting shares.

Exempt Take-Over Bids

There are a limited number of exemptions from the formal take-over bid requirements, which are set out below.

- **Private Agreements:** Private agreement purchases which result in the purchaser exceeding the take-over bid threshold are permitted in limited circumstances. The agreement must be made with not more than five sellers and the sellers may not receive more than 115% of the "market price" of the securities (generally the average closing price of the securities for the previous 20 trading days). Collateral agreements with selling security holders cannot be used to indirectly provide increased consideration.
- **Normal Course Purchases:** There is an exemption from the formal take-over bid requirements that permits the holder of more than 20% of a class of equity or voting shares (or a person acting jointly or in concert with such a person) to purchase up to an additional 5% of the outstanding shares of that class in a 12-month period (when aggregated with all other purchases in that period, other than purchases pursuant to a formal bid). There must be a published market in the shares and the offeror may not pay more than the "market price" of the securities (the last price paid for a standard trading unit of the securities by a person that was not acting jointly or in concert with the offeror) plus reasonable brokerage fees or commissions actually paid.
- **Foreign Take-Over Bid:** A take-over bid is exempt from the formal take-over if less than 10% of the outstanding shares of the class are held by Canadian residents and the published market on which the greatest volume of trading in shares of the class occurred in the 12 months prior to the bid was not in Canada. Shareholders in Canada must be entitled to participate in the bid on terms at least as favourable as the terms that apply to the general body of shareholders and any bid materials that are sent to shareholders must be filed with Canadian provincial securities regulators and sent to Canadian resident shareholders at the same time. If the bid materials are not in English, a brief summary of the terms of the bid in English and, if there are Québec resident shareholders, in French, must be filed and sent to shareholders in Canada. If no bid materials are sent to shareholders but the offeror publishes a notice or advertisement in the jurisdiction in which the target company is incorporated or organized, an advertisement in English and, if there are shareholders in Québec, in French, must be published in at least one major daily newspaper in each province of Canada in which there are shareholders.

- **Minimal Shareholdings in Canada:** The take-over bid rules include an exemption from the formal take-over bid requirements in a Canadian province if the number of beneficial holders resident in that jurisdiction is minimal. In order for this exemption to apply, there must be fewer than 50 beneficial holders in the jurisdiction holding less than 2% of the outstanding securities of that class. Shareholders in Canada must be entitled to participate in the bid on terms at least as favourable as the terms that apply to the general body of shareholders and any bid materials being sent to shareholders must be filed with Canadian provincial securities regulators and sent to Canadian resident shareholders at the same time.

Shareholder Rights Plans

Shareholder rights plans or "poison pills" have been a common defensive tactic employed by boards of directors of target companies to prevent anyone from acquiring 20% or more of the target's shares without board support. Under a shareholder rights plan, if an offeror acquires beneficial ownership of 20% of the target company's shares, the rights plan is potentially triggered and the offeror may be subject to dilution by virtue of the fact that all shareholders, other than the offeror, may become entitled to exercise rights to acquire additional shares at a discount to the current market price.

Prior to the adoption of the new take-over bid rules, rights plans were typically cease traded by securities regulators within 50 to 70 days of the commencement of an offer (although there have been notable variations in some recent decisions). While the new take-over bid rules do not specifically address how rights plans will be treated, the Canadian Securities Administrators have indicated that National Policy *62-202 Take-Over Bids Defensive Tactics* (the policy under which securities regulators review defensive tactics, including rights plans) continues to apply.

Our expectation is that rights plans will not be permitted to remain in effect to prevent acquisitions of shares made in compliance with the new formal bid requirements, absent unusual circumstances, and therefore securities regulators will be called upon less frequently to hold hearings as to when "the pill must go." This will result in greater certainty as to timing of bids than under the current regime. There may be exceptional circumstances in which regulators will be prepared to allow a rights plan to delay a bid beyond 105 days, such as where a clear majority of shareholders have approved the rights plan in the face of the bid, or where there have been late-breaking developments in an auction that justify providing the target issuer with additional time.

Since a target company will have 105 days to respond to a hostile bid (i.e., a period that is well in excess of the amount of time that securities regulators have in the past typically provided Canadian issuers before cease trading a rights plan), in many cases target companies may well conclude that they have sufficient time to respond to a hostile bid without needing to adopt a rights plan.

Our expectation is that rights plans will not be permitted to remain in effect to prevent acquisitions of shares made in compliance with the new formal bid requirements, absent unusual circumstances, and therefore securities regulators will be called upon less frequently to hold hearings as to when "the pill must go."

There will nevertheless still be a role for rights plans in protecting target issuers against "creeping bids," such as bids made through the normal course purchase and private agreement exemptions, and to prevent hard lock-up agreements. Issuers may also attempt to adopt tactical rights plans toward the end of the 105-day bid period if they conclude that additional time is needed to respond to a hostile bid (although as noted before, securities regulators are likely to quickly cease trade such rights plans, absent unusual circumstances). Issuers may also seek to adopt tactical "voting pills" in proxy contests (for example, a rights plan with a lower than 20% threshold), though it remains to be seen how securities regulators will respond to such rights plans.

U.S. Considerations

If the take-over bid includes shareholders of the Canadian target residing in the U.S., the U.S. tender offer rules will apply unless an exemption is available. If the target class of shares is registered under the U.S. Securities Exchange Act of 1934 (for example, because the shares are listed on the New York Stock Exchange or NASDAQ Stock Market) then the SEC's substantive disclosure, procedural and filing requirements under Regulation 14D and Regulation 14E may require full dual compliance with the Canadian and U.S. regimes. If the target class of shares is not registered with the SEC, the basic anti-fraud procedural protections under the Regulation 14E may still apply, although those requirements largely correspond to the Canadian take-over bid requirements.

If U.S. share ownership of the Canadian target is 10% or less, an exemption from almost all of the U.S. tender offer rules will usually be available under the SEC's Tier 1 exemption. If U.S. share ownership of the Canadian target is less than 40% and the bid complies with the Canadian rules, an exemption from the application of most of the U.S. tender offer rules, including all of Regulation 14D's substantive disclosure and procedural requirements, will usually be available under the U.S.-Canada Multijurisdictional Disclosure System, or MJDS. While use of the MJDS exemption requires filing the Canadian bid documents with the SEC, the SEC generally will not review and comment on them. If U.S. ownership of the Canadian target's shares is less than 40% but the other eligibility criteria for the MJDS exemption are not met, relief from the U.S. tender offer rules is also usually available under the SEC's Tier 2 exemption.

If share consideration is offered in a take-over bid for a Canadian target with shareholders residing in the U.S., the registration requirements of the U.S. Securities Act of 1933 will also apply unless an exemption is available. If both the bidder and the target are Canadian companies, MJDS may be available to quickly register the share consideration if, among other requirements, the bidder has been listed on a Canadian stock exchange for at least a one-year period and has a public float of at least US$75 million, and U.S. ownership of the target shares is less than 40%. To use the MJDS registration exemption, the bidder would file a registration statement with the SEC that primarily consists of the Canadian bid documents. Generally, MJDS registration statements are not reviewed and commented upon by the SEC. If U.S. ownership of the Canadian target's shares is 10% or less, a separate non-MJDS registration exemption under the SEC's Rule 802 may be available to the bidder. Use of the Rule 802 exemption would require the bidder to furnish the Canadian bid documents to the SEC, although the SEC would not review and comment on the Canadian bid documents.

An acquisition of a Canadian target with shareholders residing in the U.S. structured as a court-approved plan of arrangement will generally be the optimal approach from a U.S. securities law perspective. The solicitation of proxies to approve a plan of arrangement does not trigger the application of the U.S. tender offer rules and the SEC's proxy rules usually do not apply to Canadian companies. In addition, the exemption in Section 3(a)(10) under the U.S. Securities Act of 1933 is customarily relied upon to issue share consideration to U.S. holders of a Canadian target company under a court-approved plan of arrangement without the need to file a registration statement with the SEC.

Advantages and Disadvantages of Arrangement and Take-Over Bid Structures

An arrangement is usually the preferred transaction structure for friendly transactions due in part to the ability to effect the acquisition of all outstanding securities of a target company in a single step and in part to its substantial structuring flexibility. In particular, arrangements are not circumscribed by the take-over bid rules (e.g., there are no prohibitions against financing conditions, collateral benefits or paying differential consideration to shareholders) and, importantly, can facilitate tax planning objectives by enabling an acquiror (and a target) to set out the precise series of steps that must occur at and following the effective time of an arrangement.

In addition to the flexibility of an arrangement for implementing complex transactions, the directors of the target company may take comfort from the fact that an arrangement has been court approved and determined to be fair and reasonable, potentially insulating the transaction and directors of the target from criticism or post-closing liability.

The following chart highlights some of the key advantages and disadvantages of a take-over bid and an arrangement.

KEY ADVANTAGES AND DISADVANTAGES OF AN ARRANGEMENT

Advantages of an Arrangement	Disadvantages of an Arrangement
• Achieves acquisition of all outstanding target company securities in a single-step transaction. • Single step eliminates bridge financing risk. • Substantial flexibility in structuring, dealing with convertible securities (e.g., options, warrants) and achieving tax planning objectives. • Financing conditions, differential treatment of shareholders, collateral benefits and other prohibitions under take-over bid rules are permissible in an arrangement. • Lower approval threshold (generally, two-thirds of votes cast at the meeting, and absent related party issues and requirement for a minority shareholder vote, shares held by the acquisition proponent or merging party can be voted). • Where there are lengthy regulatory approvals, the “fiduciary out” ends at the date of the shareholders’ meeting, whereas in a take-over bid the “fiduciary out” effectively ends at the date all bid conditions have been satisfied or waived. • No SEC review of the proxy circular in certain circumstances where a take-over bid circular to acquire the same securities would be subject to SEC review. • Potential availability of registration exemption under U.S. securities laws in share exchange arrangement. • Both shareholder approval and court approval helps insulate the directors for any ongoing liability upon completion of the transaction.	• Cannot be used without target board approval. Target controls timing and agenda. • Court-supervised process and fairness hearing on arrangement creates incremental execution risk and may be used as a forum for objections and complaints by security holders. • Dissent and appraisal rights typically given to target company shareholders. However dissent rights would be available to non-tendering shareholders in a compulsory acquisition or subsequent acquisition transaction following a bid.

KEY ADVANTAGES AND DISADVANTAGES OF A TAKE-OVER BID

Advantages of a Take-Over Bid	Disadvantages of a Take-Over Bid
• In a hostile transaction, there is no need to negotiate any agreement with target's board of directors. • No dissent and appraisal rights given to target company shareholders, although dissent rights are available to non-tendering shareholders in a compulsory acquisition or subsequent acquisition transaction following a bid.	• The take-over bid may not result in the acquisition of all the outstanding shares and may need to be followed by a second-step going private transaction if less than 90% of the shares are tendered. • A second-stage going private transaction will require an additional six to eight weeks to obtain 100% ownership. • Mandated financing requirements that are not applicable in an arrangement are problematic for some purchasers. • Pre-bid integration provisions are applicable. • Prohibition on collateral benefits may make certain transactions more difficult to execute, such as private equity acquisitions with substantial management equity participation in the acquiror post-closing.

OTHER TRANSACTION STRUCTURES

Other forms of acquisition transaction structures include a statutory amalgamation and a capital reorganization involving mandatorily transferable securities. An amalgamation requires the approval of the target's board of directors and its shareholders while a capital reorganization may only require approval of the shareholders.

An "amalgamation" is a close substantive equivalent to a "merger" under the state corporation laws in the U.S.. However, there is no legal concept of a merger under Canadian corporate law (meaning one corporation merges into another, with the former disappearing and ceasing to have any legal identity, and the latter surviving and continuing in existence). Rather, under Canadian corporate law, the amalgamating corporations effectively combine to form a single corporation. The rights, assets and liabilities of each amalgamating corporation continue as the rights, assets and liabilities of the amalgamated corporation. Amalgamations are used infrequently in arm's length transactions. A capital reorganization can be used as an acquisition structure through an amendment to the share capital of the charter documents of a target company that results in a mandatory transfer of the target's shares to the acquiror in exchange for cash and/or shares of the acquiror.

In both an amalgamation and a capital reorganization, the acquiror will generally need approval of 66⅔% of the votes cast at the meeting of the target company's shareholders.

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Pre-Acquisition Considerations

EARLY WARNING AND INSIDER REPORTING

Canadian securities laws contain an "early warning" reporting system relating to the acquisition of securities of public companies. When a purchaser acquires sufficient voting or equity securities of any class of securities such that it and any joint actors beneficially own or have control or direction over 10% or more of such securities, the purchaser is required to issue and file a press release promptly and in any event no later than the opening of trading on the business day following the acquisition, and then file an early warning report promptly and in any event no later than two business days from the date of acquisition. Further press releases and reports are required upon the acquisition of each additional 2% or more of the outstanding securities of the same class, as well as upon dispositions resulting in a decrease in ownership of 2% or the purchaser's ownership falling below the 10% threshold.

The disclosure required in the press releases and reports must cover, among other things: (i) the number and percentage of securities acquired or sold; (ii) the purpose for acquiring or selling the securities; and (iii) any further intention to acquire or sell additional securities. There is also a cooling-off period that prohibits further purchases by the purchaser until the expiry of one business day after each report is filed. The cooling-off period ceases at the 20% ownership level, at which point the take-over bid rules are engaged. Schedule 13D reporting requirements under the U.S. Securities Exchange Act of 1934, which are triggered at the 5% ownership level, may also be required for target corporations that are U.S. registrants.

Eligible institutional investors, including financial institutions, pension funds and certain private equity and hedge funds, can avail themselves of the alternative monthly reporting system (AMRS), which is similar in concept to the Schedule 13G reporting regime in the U.S. A key difference between the conventional early warning system and the AMRS is that while the conventional system requires the prompt issuance of a press release and the filing of an early warning report within two business days of a reporting trigger, as well as a trading moratorium in the circumstances described above, the AMRS generally allows the reporting of ownership positions to be made on a monthly basis, with each filing due within 10 days of the end of the month, with no cooling-off period. An eligible institutional investor is disqualified from using the AMRS if it: (i) makes or intends to make a formal take-over bid or proposes or intends to propose a reorganization, amalgamation, merger, arrangement or similar business combination with respect to a reporting issuer that would result in the eligible institutional investor having effective control of the issuer; or (ii) solicits proxies from security holders in certain prescribed circumstances. The disqualification from using the AMRS for soliciting proxies does not apply where the eligible institutional investor "intends to solicit" proxies. Accordingly, activist investors may be able to use the AMRS as part of an accumulation strategy before commencement of a proxy contest.

In addition to reporting under the early warning requirements and AMRS, holders that have beneficial ownership of or control or direction over voting securities representing more than 10% of the outstanding voting rights attached to outstanding voting securities are required to file under the insider reporting regime. The initial filing must be made within 10 days of becoming a "reporting insider" and any subsequent trades must be reported within 5 days of the trade. The insider reporting regime can also extend to specified officers of the significant shareholder, including its CEO, CFO and COO. For shareholders reporting under the AMRS, there are exemptions from the insider reporting requirements that may be available so that the insider only needs to report on a monthly basis. In addition to reporting holdings of securities of the reporting issuer, the reporting insider must also report on related financial instruments, including contracts the value or market price of which are derived from, referenced to or based on the value or market price of a security of the reporting issuer.

ACQUIRING A TOEHOLD

Once an offeror has publicly announced its intention to make a take-over bid, the acquiror may not purchase shares of a target company outside the take-over bid until it has commenced its offer and then only up to 5% of the shares under prescribed circumstances. Accordingly, it is common for acquirors to consider whether to accumulate shares of a target company before commencing or announcing their intention to commence an offer in order to acquire a "toehold" position in the company. Prospective offerors typically acquire a toehold through open market purchases or private agreement transactions. The advantages and disadvantages of acquiring a toehold position must be carefully evaluated.

The following chart highlights some of the key advantages and disadvantages to acquiring a toehold position.

KEY ADVANTAGES AND DISADVANTAGES OF A TOEHOLD POSITION

Advantages of a Toehold Position	Disadvantages of a Toehold Position
• If large enough, may provide the offeror with some leverage when dealing with a target's management. • Affords the opportunity to acquire shares without paying a significant premium, thereby saving money that can be used to subsidize a higher price in a formal bid and, ultimately, lowering the average cost of the acquisition if the take-over bid is successful. • The initial purchase may either deter potential third party offerors or increase the possibility of recouping transaction expenses should a competing bid top the offeror's bid. • Initial purchases may permit the offeror to assert rights under corporate law available to shareholders, including the right to requisition a meeting of shareholders.	• Buying the target's shares may increase the offeror's cost and risk of loss if a transaction is not consummated. • Acquisitions may increase the likelihood of premature disclosure of the offeror's intentions. • Market movement could increase the price of the target's shares, thereby diminishing the apparent premium offered. • Acquisitions may have implications for pre-bid integration and insider bid requirements. • Acquisitions made prior to the bid may increase the difficulty of satisfying the Minimum Tender Requirement, since shares owned by the offeror and its joint actors are excluded from the calculation.

The amount of any accumulation of shares will generally be limited by the liquidity of the shares, the applicable take-over bid rules relating to pre-bid integration and early warning reporting obligations.

An acquiror needs to be mindful of engaging in discussions with other shareholders of the target when acquiring a toehold, since if it is found to be acting jointly or in concert with other parties, that may trigger early warning reporting obligations, a take-over bid, or a shareholder rights plan. It is a question of fact as to whether a person is acting jointly or in concert with the acquiror. However, if the acquiror has entered into any agreement, commitment or understanding with another shareholder to acquire or offer to acquire shares of the target, the acquiror is *deemed* to be acting jointly or in concert with that shareholder. A shareholder is not deemed to be acting jointly or in concert with the acquiror solely because the shareholder has entered into a lock-up agreement to tender its shares to a bid made by the acquiror, as discussed in greater detail below. Furthermore, a shareholder is *presumed* to be acting jointly or in concert with an acquiror if it has entered into any agreement, commitment or understanding with the acquiror as a result of which it intends to exercise voting rights jointly with the shareholder. If the acquiror plans to launch a proxy contest in connection with the proposed acquisition, a mere expression that the shareholder intends to vote its shares in support of the acquiror's proposal does not, without more, result in a joint actor relationship.

In addition, the timing of the acquisition of the toehold needs to be managed carefully if the purchaser is considering engaging with the target company. Once discussions with the target company have commenced, the acquiror may learn material undisclosed information about the target, which would prevent the acquiror from acquiring any more shares on the open market. In addition, a confidentiality agreement with the target company may include a standstill provision preventing the acquiror from buying any shares.

"FRIENDLY" ACQUISITON

A key consideration in structuring a public M&A transaction is whether the target board's cooperation is necessary or desirable. Proceeding with the support of a target's board (whether by way of bid, arrangement or otherwise) affords an acquiror several advantages:

- a significant potential shortening of the 105 days otherwise required for a hostile take-over bid, as the target board can agree to reduce the minimum deposit period to as little as 35 days in the case of a bid, and shareholder approval for an arrangement can typically be obtained 45–60 days after the arrangement agreement is announced;
- access to the arrangement procedure, which requires board approval;
- access to confidential information (typically in exchange for the acquiror agreeing to be bound by a confidentiality and standstill agreement) and the corresponding ability to conduct more extensive due diligence investigations beyond the public disclosure record;
- the negotiation of deal protections (such as break fees, expense reimbursement, "no-shop" provisions and the right to match a topping bid) designed to secure the successful outcome of the proposed acquisition;
- the achievement of tax efficiencies and benefits through a mutually structured transaction;
- cooperation on securing regulatory approvals, particularly where the target is in a concentrated or regulated business or where foreign investment or national security review considerations are at play;
- the ability to retain management and key employees, who may be more inclined to leave in the face of a hostile take-over;
- the avoidance of defensive measures being adopted by the board of a target company and the subsequent exploration of value-maximizing alternatives, which can make unsolicited take-over bids more complex and costly;
- structuring the form of transaction to minimize the risk of interlopers and obtaining a timing advantage; and
- a favourable recommendation may assist in satisfying the Minimum Tender Requirement (if the transaction is structured as a take-over bid).

"HOSTILE" TAKE-OVER

There may be circumstances in which it makes sense for an acquiror to decide to proceed by way of a "hostile" or "unsolicited" transaction where, for example:

- friendly overtures have failed to result in an acquisition transaction;
- the acquiror has set its price and does not anticipate any interlopers with the result that it would prefer not to negotiate with the target board, which may seek a price increase in exchange for a favourable recommendation;
- the acquiror has obtained "lock-ups" from significant shareholders;
- the acquiror's objectives may not be to acquire control of the target company but rather to instigate change or exert influence over the board; and
- there is such a wide valuation gap between the views of the acquiror and the target board that the acquiror is left with no choice but to extend an offer directly to the target's shareholders.

As the support of the target company's board of directors is not required for a take-over bid, this is the only practical structure available to effect an unsolicited or hostile acquisition.

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LOCK-UP AGREEMENTS

Acquirors may choose to enter into a lock-up agreement with the principal shareholder(s) of the target in order to increase the probability of a successful transaction. Under the lock-up, shareholders will agree to tender their shares to the take-over bid or, in the case of a voting transaction, vote in favour of the transaction. The agreement may be "hard," in which case the tendered shares may be acquired by the acquiror or the shareholder must vote in favour of the transaction irrespective of whether a topping bid emerges that is ultimately supported by the board of the target, or "soft," in which case the shareholder has the right to terminate the lock-up and tender its shares to or vote in favour of a higher offer. The prohibition on acquiring beneficial ownership of shares outside of the take-over bid from the date of announcement of the intention to make the take-over bid does not prohibit lock-up agreements, and the entering into of a lock-up agreement does not, without more, trigger the early warning reporting obligations or result in a joint actor relationship between the acquiror and the locked-up shareholder. However, certain shareholder rights plans may be triggered where shareholders enter into hard lock-up agreements.

BUY-SIDE SHAREHOLDER APPROVAL

In a share-for-share transaction in which capital stock of the acquiror is proposed to be issued to target shareholders, it is essential to consider whether buy-side shareholder approval is required. Under the Toronto Stock Exchange rules, listed issuers are required to obtain buy-side shareholder approval for public company acquisitions that would result in the issuance of more than 25% of the outstanding shares of the acquiror on a non-diluted basis. In calculating the number of shares issued in payment of the purchase price for an acquisition, any shares issued or issuable upon a concurrent private placement of securities upon which the acquisition is contingent or otherwise linked must also be included.

3

Minority Shareholder Protections

Acquisition transactions involving related parties such as significant or controlling shareholders, board members or senior management raise conflict of interest concerns and may implicate additional corporate and securities law requirements.

Two Canadian securities regulators (Ontario and Québec) have established specific rules applicable to:

- insider bids;
- issuer bids (self-tender transactions);
- certain types of related party transactions; and
- certain types of business combinations.

These rules are set out in Multilateral Instrument 61-101 – *Protection of Minority Security Holders in Special Transactions* (MI 61-101) and are designed to afford certain protections to shareholders where conflicts of interest are present in transactions involving related parties. For example, a take-over bid may engage the "insider bid" rules in addition to the usual take-over bid rules in circumstances where an "insider" (e.g., a holder of more than 10% of the outstanding shares of the target) proposes to make a take-over bid. An arrangement may also engage the "business combination" rules in circumstances where a shareholder is compelled to sell its shares as a consequence of the transaction and where the transaction involves a related party that is either acquiring the company (either alone or with joint actors) or a related party is not treated identically to the general body of shareholders (e.g., because it is receiving a collateral benefit).

MI 61-101 regulates these transactions by giving minority shareholders the following procedural protections:

- a formal valuation by an independent valuator supervised by an independent committee of directors of the target company;
- "majority of the minority" shareholder approval; and
- enhanced disclosure, including disclosure of prior valuations prepared for, and offers received by, the target in the past two years.

MI 61-101 provides exemptions from the formal valuation and minority approval requirements in circumstances where, in general terms, there are no conflict of interest concerns between the related party and the target company and where there is no informational advantage about the target in the possession of the insider. These are highly technical rules that need to be carefully considered in the context of an M&A transaction.

4

Directors' Duties

The corporate statutes in Canada impose two principal duties on directors: the fiduciary duty and the duty of care. Directors cannot contract out of these responsibilities and may be held personally liable for any breach of these duties.

FIDUCIARY DUTY

Directors are fiduciaries of the corporation they serve. This long-standing principle is codified in the corporate statutes by the requirement that directors act "honestly and in good faith with a view to the best interests of the corporation" in exercising their powers and discharging their duties.

The Supreme Court of Canada set out the scope of the fiduciary duty in its decision in *BCE Inc.* The key principles from the decision are as follows:

- the fiduciary duty is owed to the corporation, not to any particular stakeholder;
- the fiduciary duty of the directors is a broad, contextual concept. It is not confined to short-term profit or share value. Where the corporation is an ongoing concern, it looks to the long-term interests of the corporation. The content of this duty varies with the situation at hand;
- in considering what is in the best interests of the corporation, directors may look to the interests of, among others, shareholders, employees, creditors, consumers, governments and the environment to inform their decisions;
- the duty of the directors to act in the best interests of the corporation comprehends a duty to treat individual stakeholders affected by corporate actions fairly and equitably based on those stakeholders' objectively determined reasonable expectations; and
- where stakeholders' interests conflict, there is no principle that one set of interests should prevail over another set of interests. In particular, unlike the Revlon duties under Delaware law, there is no principle that shareholder interests in maximizing shareholder value prevail over other stakeholder interests in a change of control transaction. Everything depends on the particular situation faced by the directors and whether, having regard to that situation, they exercised their business judgment in a responsible way and resolved any conflicting interests fairly and equitably based on an objective determination of such stakeholders' reasonable expectations.

Although *BCE* did not specifically endorse a duty to maximize shareholder value, shareholders obviously have a great deal at stake in a change of control transaction, and have a reasonable expectation that directors will give considerable weight to shareholders' interests when considering how to respond to an acquisition proposal. Accordingly, determining whether an acquisition proposal delivers the best value reasonably available to shareholders should remain a central focus of directors' deliberations. This is all the more important since shareholder approval is required to complete a transaction, and most Canadian corporate statutes provide shareholders with the ability to bring a claim against a corporation and its directors alleging oppressive conduct if shareholder interests have been unfairly disregarded.

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DUTY OF CARE

In discharging their duties, directors must also "exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances." This standard of care can be achieved by any director who devotes reasonable time and attention to the affairs of the corporation and exercises informed business judgment. The standard of care is measured against the objective standard of what a reasonably prudent person would do in comparable circumstances. Failure to meet the standard often stems from passivity and a failure to inquire.

In *BCE*, the Supreme Court of Canada confirmed the existence of a Canadian "business judgment rule" under which courts will defer to directors' business decisions so long as they are within a range of reasonable alternatives. Courts defer to decisions of directors taken in good faith in the absence of conflicts of interest, provided the directors undertook reasonable investigation and consideration of the alternatives and acted fairly. Courts will not subject directors' business judgment to microscopic examination and will not substitute their view for that of the directors, even if subsequent developments show that the directors did not make the best decision.

FORMATION OF A SPECIAL COMMITTEE

In discharging the duty of care, a threshold consideration is whether a board should constitute a special committee of independent directors to review and consider a take-over bid or credible acquisition proposal.

Where there is a true conflict transaction that engages the procedural protections contained in MI 61-101 (e.g., because the potential acquiring party is a related party of the target company), then a special committee of independent directors with independent legal and financial advisors should be, and may be required to be, established to review an acquisition proposal, supervise and direct any negotiations and make recommendations to the board.

In other circumstances where the conflict is not as acute, such as where there is a perception that management may be influenced by considerations relating to their continued employment, the board will need to consider how best to address the conflict. In some cases, the conflict may be addressed by excluding management and any potentially conflicted director from those portions of the Board's deliberations as considered appropriate in the particular circumstances.

In other cases, the Board may choose to establish a special committee. Canadian courts have looked favourably upon the establishment of special committees as a means of addressing potential conflicts.

A special committee may also be desirable as a matter of convenience, depending on the relative expertise of the directors and their differing time commitments and availability.

OPPRESSION REMEDY

Under the oppression remedy, courts are granted broad remedial powers if a court is satisfied, among other things, that the powers of the directors have been exercised in a manner "that is oppressive or unfairly prejudicial or that unfairly disregards the interests of any security holder." Although it is not necessary for an oppression remedy complainant to establish that directors have breached their fiduciary duty in order to succeed in an oppression claim, demonstration of compliance with the board of directors' fiduciary duty is of valuable assistance towards protecting the board of directors against such claims.

The objective of the remedy is to protect the reasonable expectations of shareholders and other stakeholders, giving the court (as described in *BCE*) "broad, equitable jurisdiction to enforce not just what is legal but what is fair." In determining whether a particular decision of a board was oppressive, the court must necessarily assess the impact of the business decision made by the board.

If a court finds oppression, it may make any order it considers appropriate to remedy an oppressive or unfair situation.

Where a company has debt or equity securities outstanding that are not subject to the offer to acquire, particular care needs to be taken to ensure that the interests of holders of such securities have been fully considered.

DIRECTORS' ACTIONS IN RESPONSE TO AN ACQUISITION PROPOSAL

In light of the foregoing principles, in formulating a response to an acquisition proposal, the directors must be able to demonstrate that they exercised their judgment on an informed basis, after reasonable investigation and analysis of the situation and with a reasonable basis for believing that their actions are in the best interests of the corporation. There is no absolute duty to negotiate with a potential acquiror or to conduct a process designed to achieve a sale of the corporation simply because the corporation has received an acquisition proposal.

Assuming the board concludes that it is in the best interests of the corporation to explore a potential sale of the corporation, there is no single blueprint that the board must follow. The board has broad latitude under the business judgment rule in designing a sale process, provided that the board acts on an informed basis. Typically this will involve receiving the advice of the corporation's financial and legal advisors.

Accordingly, the board could choose to engage with a potential acquiror on an exclusive basis, without conducting any form of pre-signing market check of other potential buyers or running an auction. Alternatively, the board may decide that a pre-signing market check is advisable in the circumstances. The board could also consider running an auction, although it is under no legal obligation to do so. The board's judgment will be informed by, among other things, the terms of any acquisition proposal, whether the potential acquiror demands exclusivity as a condition of continuing negotiations, the universe of other potentially interested buyers, the impact of the process on the corporation's business and what process is reasonably calculated to lead to the best outcome for shareholders and the corporation's other stakeholders.

Where the corporation is the subject of a hostile take-over bid, the same principles apply. There is no obligation for the corporation to put the company up for sale. However, given the reality that shareholders will ultimately have the ability to tender to the bid, directors will need to consider a variety of alternatives to maximize shareholder value, including staying independent, a potential sale to another party, or a higher bid from the hostile bidder.

DEAL PROTECTIONS AND DEFENSIVE TACTICS

In Canada it is customary to include deal protection measures in the arrangement agreement or support agreement (in the case of a take-over bid) and for boards to adopt certain defensive tactics in response to hostile bids. These deal protections and defensive tactics may be reviewed by one or more of the courts, the securities regulators or by the applicable stock exchange (in the case of issuance of shares or rights to acquire shares). Challenges to the exercise by the target board of its fiduciary duty and duty of care will typically be made in court, as the board owes its duties to the corporation under applicable corporate law. Notwithstanding that the court is the appropriate forum to determine whether the directors have complied with their duties, the securities regulators retain a broad discretionary power to review the actions of the target board as part of their mandate to protect the capital markets. The securities regulators have issued guidance under National Policy *62-202-Take-over Bids-Defensive Tactics*, in which capital market participants are advised that the regulators are prepared to examine target company tactics in specific cases to determine whether they are abusive of shareholder rights.

Common deal protections in supported transactions include non-solicitation ("no shop") provisions, in which the target company agrees not to solicit or negotiate other offers, as well as a commitment to recommend the supported transaction and pay a break fee if the agreement is terminated in certain circumstances. The non-solicitation provisions generally permit the board in the exercise of its fiduciary duties to engage with a rival bidder that makes an unsolicited acquisition proposal that is likely to result in a superior proposal. The "fiduciary out" of the board of directors also typically permits the board to change its recommendation and enter into an agreement to support a superior proposal. What constitutes a superior proposal is a matter of negotiation, but it is almost invariably defined to include a requirement that the acquisition proposal is more favourable from a financial point of view to the target shareholders than the existing transaction. A break fee is permissible under Canadian law, provided that it represents a reasonable commercial balance between its negative effect as an auction inhibitor and its potential positive effect as an auction stimulator (including if the fee was necessary in order to induce a bid). Break fees typically range from 1 to 4% of deal equity value.

In defending against hostile bids, target boards have also employed a number of defensive tactics. The most common is the use of rights plans or poison pills, which were previously discussed. Additional defensive tactics include issuances of treasury securities to dilute the bidder or potential bidder (often by placing the securities in friendly hands), the sale of assets, recapitalizations, and asset lock-ups.

5

Competition Law and Foreign Investment Review

COMPETITION ACT

Canada's *Competition Act* (CA) provides a procedure for the review of transactions that involve the acquisition of a business in Canada.

Pre-Merger Notification

Subject to certain exceptions, the CA requires pre-merger notification of transactions which meet the following two thresholds:

- all parties and their affiliates have assets in Canada the aggregate gross book value of which exceeds $400 million, or have aggregate gross revenues from sales in, from or into Canada that exceed $400 million; and
- the aggregate book value of the assets in Canada being acquired, or the gross revenues from sales in or from Canada generated from those assets, exceeds $87 million (2016 threshold, revised annually and indexed to the growth of Canadian GDP).

If the transaction is an acquisition of shares, an additional threshold requires that the voting interest of the purchaser post-transaction exceed 20% for a public company (or 50% if the 20% threshold is already exceeded). Accordingly, an acquiror is required to file a pre-merger notification with the Competition Bureau if it would acquire more than 20% of the voting shares of a publicly traded company and the financial thresholds noted above would be crossed.

Where a notification is required, the parties must provide certain information to the Competition Bureau, including transaction details, affiliate information, product descriptions, customer and supplier lists, and certain pre-existing documents that assess the competitive impact of the transaction. The transaction cannot close until the expiry of a 30 day statutory waiting period. If, prior to expiry of the waiting period, the Commissioner of Competition issues a supplementary information request (SIR), the waiting period is extended for an additional period ending 30 days following full compliance with the SIR. A transaction may be completed following expiry of the applicable waiting period, unless the Commissioner has sought and obtained an injunction preventing closing.

In the case of a hostile transaction, the waiting period commences once the offeror has submitted its portion of the notification. After the Commissioner advises the target company of the offeror's notification, the target company then has 10 days to file its portion of the notification.

Where there is no or minimal competitive overlap, the parties may request that the Commissioner issue an advance ruling certificate (ARC), or in the alternative, a no action letter, which usually can be obtained within 14–21 days of filing. Where an ARC is issued, the Commissioner cannot challenge the transaction and the transaction is exempt from the pre-merger notification requirement. Where a no-action letter is issued, the Commissioner states that he does not intend to challenge the transaction (but retains the right to do so), and the transaction is exempt from the pre-merger notification requirement through the issuance of a waiver.

If an ARC is not issued, but the Commissioner has issued a no action letter or the waiting period has expired, then the Commission still may challenge a transaction up until one year after closing. The Commissioner also has the right to review and challenge transactions until one year after closing regardless of whether they are notifiable.

Standard of Review

The substantive test is whether the transaction is likely to prevent or lessen competition substantially in a market in Canada. When conducting this analysis, the Competition Bureau will consider a number of factors including the appropriate product and geographic markets, market share and concentration, effectiveness of remaining competition in the market and prospects for entry of new competitors, barriers to entry, whether the target company is a failing firm, the role of regulation or innovation in the relevant market, and the countervailing power of purchasers. Transactions that result in a combined post-merger market share of greater than 35% generally receive a more detailed review by the Competition Bureau, but market share and concentration are not determinative. There are many examples of mergers that were permitted to proceed where the parties' combined market share exceeded 35%. Where a transaction is likely to lessen or prevent competition substantially, the Commissioner may seek from the Competition Tribunal an order such as an injunction or a divestiture.

The CA process will likely only impact the timing and closing of a transaction where the business activities of the purchaser, its affiliates or entities in which it has a significant interest compete with those of the target company in Canada, or the purchaser has some significant "vertical" relationship (such as that of being a major supplier or customer) with the target.

INVESTMENT CANADA ACT

In general, the *Investment Canada Act* (ICA) applies when a non-Canadian investor proposes to acquire control of a Canadian business (as defined in the ICA) directly or indirectly.

Acquisition of Control

Generally, an acquisition of control occurs where the investor acquires one-third or more of the voting shares of a corporation (subject to a rebuttable presumption that the corporation will not be controlled in fact by the investor). The acquisition of less than one-third of the voting shares of a corporation is deemed not to constitute an acquisition of control. The acquisition of a majority of the voting shares of a corporation is irrebuttable and deemed to constitute an acquisition of control. Where the Canadian business is engaged in a cultural business, or the investor is a state-owned enterprise (SOE), the applicable Minister has the discretion to make a determination that an acquisition of control has occurred regardless of these rules and presumptions.

Application for Review and Notification

Direct investments in Canada exceeding certain monetary thresholds are reviewable in advance of closing by the Minister of Innovation, Science and Economic Development (or the Minister of Canadian Heritage where the Canadian business is engaged in a cultural business), while all other acquisitions of control are subject to notification. There are six different thresholds for review of direct acquisitions by a non-Canadian to acquire control of a Canadian business:

- **Direct acquisition of a publicly traded entity:** $600 million or more in enterprise value, based on the target's market capitalization, plus total liabilities (less operating liabilities), minus cash and cash equivalents.
- **Direct acquisition of a privately held entity:** $600 million or more in enterprise value, based on the total acquisition value, plus total liabilities (less operating liabilities), minus cash and cash equivalents. Where acquiring less than 100%, total acquisition value will include amounts in addition to those payable by the non-Canadian acquiring control.
- **Acquisition of substantially all of the assets of a Canadian business:** $600 million or more in enterprise value, based on the total consideration payable, plus the liabilities that are assumed by the investor (other than operating liabilities), minus the cash and cash equivalents that are transferred to the investor.
- **Direct acquisition of a cultural business:** book value of assets of a Canadian business is $5 million or more.
- **Direct acquisition by a non-WTO investor of a non-WTO controlled target:** book value of assets of a Canadian business is $5 million or more.
- **Direct acquisition by a SOE:** book value of assets of a Canadian business is $375 million or more (2016 threshold, revised annually).

The $600 million enterprise value threshold will rise to $800 million in April 2017 and then to $1 billion two years later in April 2019, after which time, the threshold level will be adjusted annually based on a GDP-derived indexing formula. Direct acquisitions of Canadian businesses below the thresholds, and indirect WTO investments, including by SOEs, are subject to notification only, but may still be reviewed on national security grounds. An indirect investment (an acquisition of a foreign company with a Canadian subsidiary) is not

reviewable unless it is an indirect non-WTO investment or the Canadian business is a cultural business, in which case the threshold is $50 million in book value of assets or more (or $5 million in certain cases). In such cases, the review occurs post-closing.

Where an acquisition is subject to pre-closing review, the parties cannot close the transaction until approval is granted by the reviewing Minister. The application for review includes transaction details, information on the investor and the Canadian business, and the investor's plans for the Canadian business. The investor is usually required to submit written binding undertakings that will generally remain in force for three to five years, in order to confirm its commitment to perform key components of its plans.

The reviewing Minister has up to 45 days to determine whether the investment should be approved (which may be unilaterally extended by the Minister for an additional 30 days). The review period may be extended for a further period as agreed upon by the Minister and the investor.

Where only a notification is required, it must be filed within 30 days of closing and requires limited information relative to a pre-closing review.

Standard of Review

The standard of review is whether the investment is likely to be of "net benefit to Canada." The reviewing Minister will consider the following statutory factors: effect of the investment on economic activity in Canada; participation of Canadians in the Canadian business; effect of the investment on productivity, technological development and products in Canada; effect of the investment on competition in Canada; compatibility of the investment with national industrial, economic and cultural policies; and contribution of the investment to Canada's ability to compete globally. Where the investor is a SOE the reviewing Minister will also consider the nature and extent of control by a foreign government, the SOE's corporate governance, operating and reporting practices, and whether the acquired Canadian business will retain the ability to operate on a commercial basis.

ADDITIONAL CONSIDERATIONS

National Security Review

The ICA provides for the review of any investment where it could be "injurious to national security" (and this is regardless of whether the investment exceeds the identified monetary thresholds or whether an acquisition of control occurs). "National security" is not defined in the ICA or the regulations. Accordingly, the federal government has wide latitude to review and veto a transaction, or seek commitments, on "national security" grounds.

There is no process in Canada for submitting a transaction to voluntary national security review (unlike in the U.S. in connection with Committee on Foreign Investment in the United States [CFIUS] approval). However, for an investment involving an acquisition of control (regardless of whether a pre-closing review is required), an investor may obtain comfort on whether a national security review will be conducted by submitting a notification at any time prior to, or within 30 days after implementing an investment or by submitting an application for review (where required) at any time prior to implementing an investment. An indication that a national security review process may be commenced must be sent by the reviewing Minister within 45 days of submitting a notification or application. There is no prescribed clearance process for investments that do not involve an acquisition of control. If no such indication is received, the investor can be certain that a national security review will not be undertaken.

A full national security review could take up to 200 days. If the reviewing Minister is of the opinion that the investment may be "injurious to national security," he/she can refer the investment to the Governor in Council (Cabinet). Cabinet may take any measures it considers advisable to protect national security, including directing the investor not to implement the investment (or divest if the investment has been implemented) or permitting the investment subject to certain conditions.

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