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Top public M&A and proxy contest developments in 2017

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While the number of Canadian M&A transactions this year has been slightly higher than in 2016, the total value of deals is somewhat lower. There was also a drop in the number of proxy contests. Nevertheless, there were a number of important legal developments. Set out below is our discussion of the most notable ones.

CSA Staff Notice on material conflict of interest transactions

In an important Staff Notice (Notice) published on July 27, 2017, staff of the securities regulatory authorities in each of Ontario, Québec, Alberta, Manitoba and New Brunswick (Staff) indicated that they intend to subject material conflict of interest transactions regulated by Multilateral Instrument 61-101 *Protection of Minority Security Holders in Special Transactions* (MI 61-101) to greater regulatory scrutiny. Material conflict of interest transactions are now being reviewed on a real-time basis to assess compliance with the requirements of MI 61-101 and to determine whether the transaction raises public interest concerns.

Staff have also provided guidance regarding their expectations of enhanced disclosure and the active role to be played by special committees of independent directors.

Moreover, where a fairness opinion is obtained for a material conflict of interest transaction, Staff are requiring disclosure of the structure of a financial advisor's compensation (but not the amount of the advisor's fee) as well as the financial analysis underlying the opinion.

Issuers and their advisors in material conflict of interest transactions need to be prepared for the possibility of real-time review of disclosure documents and the risk that supplemental disclosure may be required that could delay the transaction. To minimize this risk, boards of issuers in conflict transactions should ensure that special committees are formed early in the process, retain independent advisors, and include comprehensive disclosure in the transaction circular.

Staff's guidance on fairness opinions, like the Notice as a whole, only applies to material conflict of interest transactions. Nevertheless, it will be interesting to see whether the Notice will influence fairness opinion practice more generally, particularly given the interplay of the Notice with the *InterOil* decision, which is discussed in greater detail below.

For further information regarding the Notice, please refer to our Osler Update: Securities Commission staff raise the bar for conflict transactions.

Private placements in proxy contests

In April, the Ontario Securities Commission (OSC) overturned a decision by the Toronto Stock Exchange (TSX) conditionally approving a private placement of shares in the context of a proxy contest. The TSX had approved the issuance of almost 10% of the common shares of Eco Oro Minerals Corp. (Eco Oro) to existing shareholders supportive of the incumbent board of directors. The shares were issued just eight days prior to the record date for a shareholders meeting requisitioned to replace Eco Oro's board of directors. The OSC's decision effectively required Eco Oro to unwind the private placement unless it was approved by Eco Oro's shareholders. See our Osler Update: The Eco Oro decision – OSC invokes broad jurisdiction in effectively neutralizing a private placement.

While the OSC rendered its decision pursuant to a provision of Ontario securities law that provides for the review of TSX decisions, the OSC also indicated that, whether or not there is a TSX decision, a person may seek to invoke the OSC's public interest jurisdiction under Ontario securities laws based on the underlying policies in National Policy 62-202 – Take-Over Bids – Defensive Tactics (NP 62-202). The reference to NP 62-202 is instructive as there is a line of decisions addressing the use of private placements in the context of contested take-over bids, most recently the Dolly Varden decision described in our Osler Update entitled Contested private placements under the new take-over bid regime: the Dolly Varden decision. In that decision, the OSC and the British Columbia Securities Commission (BCSC) upheld a contested private placement by the target of an unsolicited take-over bid where they concluded that there was a legitimate need for the financing and the private placement was not implemented as a defensive tactic in response to the bid. The OSC and BCSC provided important guidance on the regulatory analysis and treatment of contested private placements in light of the traditional limitations on defensive tactics set forth in National Policy 62-202.

In response to the OSC decision in Eco Oro, in which there was some evidence that Eco Oro had not informed TSX staff of the proxy battle and impending shareholders meeting, the TSX issued a Staff Notice providing guidance with respect to the information required by issuers when completing TSX Form 11 – Notice of Private Placement. The TSX Staff Notice provides that, in connection with any notice of a private placement, the TSX expects issuers to provide the TSX with information regarding any relevant significant matters including, but not limited to, any upcoming shareholders meeting for which a record date has been or is shortly expected to be determined, any pending mergers, acquisitions, take-over bids, changes to capital structure or other significant transactions, and any details regarding potential dissident shareholders and/or anticipated proxy contests.

Fairness opinions after Interoil

In March, the Supreme Court of Yukon issued its reasons for approving Exxon Mobil's acquisition of InterOil [PDF], which closed on February 22, 2017. The original $2.3-billion arrangement had been blocked by the Yukon Court of Appeal on the basis that it was not fair and reasonable. This determination was made in large part due to the lack of disclosure of the financial analysis underlying the original fairness opinion in support of the transaction, leading to a concern that the shareholder vote approving the arrangement was not fully informed.

Responding to the criticism in the Court of Appeal decision, InterOil's revised proxy circular contained (i) a fixed fee long-form fairness opinion that contained detailed financial analysis about the value of InterOil and the consideration payable under the arrangement, and (ii) a report of an independent committee of directors in support of the arrangement.

In approving the amended arrangement, the Court noted that the interim order of the Court required the above-noted disclosure in the proxy circular and observed that, in the Court's view, these two requirements "provide a minimum standard for interim orders of any plan of arrangement. It is not acceptable to proceed on the basis of a Fairness Opinion which is in any way tied to the success of the arrangement."

Since the Yukon Court of Appeal's decision, there has been considerable debate in the legal and investment banking community as to whether Canadian practice relating to fairness opinions should change in response to the decision. So far, practice has been mixed. Market participants have not uniformly adopted the three practices suggested by the Court of Appeal and adopted by the parties in the revised InterOil arrangement: disclosure of the financial analysis underlying the fairness opinion, disclosure of the financial advisor's fees, and obtaining fixed fee opinions from financial advisors whose compensation is not conditional on the conclusion reached in the opinion or the outcome of the transaction.

As expected, several corporations completing arrangements under the laws of British Columbia have obtained a fairness opinion that includes at least some disclosure of the underlying financial analysis carried out by the provider of the opinion. The Yukon Court of Appeal is constituted with judges of the British Columbia Court of Appeal, so the decision of the Yukon Court of Appeal in *InterOil* would be expected to be followed by judges in British Columbia. There have also been arrangements in other jurisdictions in which *InterOil*-style fairness opinions have been obtained, although standard short-form opinions continue to be used in many transactions.

As noted above, Staff's guidance on fairness opinions in material conflict of interest transactions, coupled with the *InterOil* decision, may push issuers and their advisors to disclose more of the financial analysis underlying fairness opinions, as is the practice in the United States.

Until there is further judicial or regulatory consideration of this issue, market practice will likely continue to vary, depending on a number of factors, including the form of the transaction (arrangement or some other structure), the jurisdiction of the transaction, the robustness of the sale process, and the likelihood of legal challenge by a disgruntled shareholder.

Hostile take-over bids under the new bid regime

In May 2016, Canada's new take-over bid regime was adopted, which provides for a minimum 105-day bid period, a mandatory 50% minimum tender condition and a 10-day extension once the minimum tender condition has been satisfied. Following its adoption, there were questions as to whether the new regime – in particular the 105-day minimum bid period – might have a chilling effect on hostile bids.

Although it's too early to draw any definitive conclusions, to our knowledge, there have only been three hostile bids in 2017 to date: Nuri Telecom's bid for Apivio Systems; Pollard Banknote's bid for Innova Gaming; and Aurora Cannabis's bid for CanniMed Therapeutics. This is down from five hostile bids in 2016 and is well below the average over the past 10 years. Time will tell whether this is simply a slow year or the start of a broader trend.