A Q&A Guide to M&A in Canada

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Market and regulation

1. Please give a brief overview of the public M&A market in your jurisdiction. (Has it been active? What were the big deals over the past year?)

The market for corporate control has been very active in Canada in recent years, although consistent with global trends, 2002 saw both the number and the value of transactions decline for the second consecutive year. Over 65 takeover bids were commenced in Canada in 2002, almost three-quarters of which were friendly. Canadian merger activity during 2002 was highest in the natural resource and financial services sectors.

The number of international transactions involving Canadian companies remains high. Historically, Canada-US cross-border deals have dominated this category. A number of the largest acquisitions involving Canadian companies during the past two years were Canada-US transactions in the resource sectors, including the US$8 billion acquisition by Duke Energy Corporation of Westcoast Energy Inc. the US$6.3 billion takeover of Gulf Canada Resources Limited by Conoco Inc., and the US$4.4 billion three-way merger between Newmont Mining Corporation, Franco-Nevada Mining Corporation Limited and Normandy Mining Limited. However, in recent years there has been an increasing number of large acquisitions involving European companies, such as the Seagram Co. Ltd./Vivendi S.A./Canal Plus S.A. and Alcatel S.A./Newbridge Networks Corp. mergers, both completed in 2000.

2. What are the main means of obtaining control of a public company? (For example, public offer, legal merger, scheme of arrangement, etc.)

Public companies in Canada are generally acquired by way of takeover bid or in a merger transaction:

- Takeovers are the norm when the consideration offered is cash or securities in a Canadian issuer and for hostile acquisitions. No involvement by the target management is required in order to commence a takeover bid.
- Mergers can take many forms and are commonly implemented by way of a court supervised plan of arrangement. Plans of arrangement are generally only used in negotiated transactions, typically when a reorganisation of the target is required to achieve the business goals of the acquisition or to implement the acquisition on a tax efficient basis. A plan of arrangement facilitates a multi-step transaction by ensuring that the parties only enter into the transaction if completion of all steps in the transaction can be assured. They are also often used when a foreign acquirer wants to use its own securities as consideration.

In general, the time from the announcement of a plan of arrangement to completion is longer than for a takeover bid.
This chapter deals with the law and regulation of takeovers, unless stated otherwise.

3. Are hostile bids permitted? If so, are they common?

The majority of Canadian M&A transactions tend to be friendly transactions entered into with the approval of the target company’s board, typically on terms negotiated between the target and the acquirer. However, primarily hostile bids made directly to the target’s shareholders also occur. The success of a hostile bid depends on:

- The level of the premium offered on the pre-bid trading price.
- The strength of the target's takeover defences.
- Its ability to attract alternative suitors or create other options.

Many Canadian public companies have a controlling shareholder or one or more significant shareholders whose support is essential for a bid to succeed. This helps explain the predominance of friendly transactions. In addition, friendly acquisitions are generally more suitable for cross-border mergers where cooperation between the parties is desirable because of the complex structures which may be required.

4. How are public takeovers and mergers regulated and by whom?

Securities law

Each of Canada's ten provinces and three territories has its own securities legislation. While the legislation in the various jurisdictions is consistent in many respects, there are differences that may be important, depending on the particular circumstances of the transaction.

This article focuses on the securities legislation in the Province of Ontario. Ontario has the most comprehensive takeover regulatory regime and its securities legislation is almost invariably applicable in a Canadian acquisition due to the relative size of Ontario’s population.

In Ontario, takeovers are governed principally by Part XX of the Securities Act (Ontario) and by the accompanying regulations, rules and policy statements. The Securities Act is administered by the Ontario Securities Commission (OSC) (see box "Regulator contact details").

Corporate law

Corporations in Canada can be incorporated provincially or federally. The corporate law of the target's jurisdiction of incorporation governs the squeeze-out of minority shareholders after a successful bid and acquisitions by way of plan of arrangement.

Stock exchange rules

In general, Canadian stock exchanges do not specifically regulate takeovers. However, certain actions of listed companies that relate to business combinations require stock exchange approval, such as a proposed issue of securities, or the adoption of a shareholder rights plan by a target company. In certain circumstances, stock exchange approval may be made conditional on shareholder approval.
US securities laws
Many Canadian public companies have a significant number of US shareholders. For example, about 40% of the issuers listed on the S&P/TSX Composite Index maintain a listing in the US. It is imperative to determine as early as possible the extent to which US securities laws apply to a proposed M&A transaction involving a Canadian company. The US Securities and Exchange Commission has adopted exemptions to facilitate the extension of bids to the US security holders of Canadian and other foreign targets. For example, a bid for a Canadian "foreign private issuer" can be made to US holders of the target’s securities without complying with most US tender offer rules provided that all of the following are true:

- Less than 40% of the target's shares are held by US holders.
- The bid is not exempt from and complies with substantive Canadian rules governing takeovers.
- US security holders are entitled to participate on terms that are no less favourable than those offered to any other shareholder.

These exemptions do not exempt bidders from US anti-fraud and anti-manipulation rules, or from civil liability under US Rule 10b-5.

Merger control provisions
The takeover of a Canadian company can give rise to competition and foreign investment issues in Canada. Depending on where the target and the acquirer carry on business, there may also be merger control or antitrust issues in the US and in other jurisdictions (see Questions 29 and 30).

Result of non-compliance
Non-compliance by a bidder with Ontario securities law can result in the OSC issuing a variety of punitive orders, including a "cease trade" order or an order that exemptions contained in Ontario securities law do not apply to the offending corporation, or its directors and officers. A "cease trade" order can prohibit a bidder from acquiring securities of a target, including under its bid, or from disposing of securities already held. A compliance order can also be sought by the OSC in the Ontario courts. Violation of Ontario securities laws is an offence which is subject to a fine of up to C$5 million (US$3.4 million) and/or imprisonment for up to five years. Any misrepresentation made in a takeover bid circular gives rise to a right of shareholders to rescission or damages, subject to certain statutory defences.

Pre-bid

5. What due diligence enquiries will a bidder generally make before making a public bid? (What information will be in the public domain?)

Due diligence by the bidder
Whether a bidder can gain access to confidential information on the target depends on the circumstances. On hostile bids, access to non-public information is generally precluded. Even on a friendly bid, the investigation may be limited to high-level or "show-stopper" issues, since
extensive enquiries may compromise the confidentiality of the negotiations. For the same reason, a due diligence investigation typically involves only senior management and focuses on key aspects of the target's business. On friendly bids it is quite common for the target to establish a data room containing relevant information.

**Due diligence by the target**

On a friendly transaction, if the bidder is contemplating offering its securities as part of the consideration, the target may wish to undertake at least limited due diligence of the bidder and its business. This focuses on the bidder's financial and operational prospects.

**Confidentiality agreements**

Whether due diligence is one-way or two-way, the parties often enter into a confidentiality agreement. The party conducting due diligence covenants not to disclose any non-public information obtained through the due diligence process, nor to use such information other than for deciding on the terms of its bid. A confidentiality agreement typically includes "standstill" provisions that limit the potential bidder's ability to acquire target securities, or to undertake any transaction or other actions that have not been approved by the target's board, for a period of time after the due diligence period.

**Public sources**

The principal source of public information on a Canadian company is its filings with provincial securities commissions. Such filings are available on the internet via the System for Electronic Document Analysis and Retrieval (SEDAR) (www.sedar.com) and include:

- Audited financial statements.
- Management discussion and analysis of financial condition and results of operations.
- Annual information forms and annual reports, which contain a description of the company's business and operations.
- Prospectuses.
- Management proxy circulars and other shareholder meeting documents.
- Press releases and material change reports.

To ascertain the target's share capital structure the bidder can obtain copies of the target's articles of incorporation, which are publicly available. Depending on the business of the target and its assets, the bidder will want to search public records relating to:

- Patents and trademarks.
- Personal property security.
- Environmental matters.
- Real estate.

It may also search court records to determine if the target is involved in any significant litigation.

**6. Are there any rules as to maintaining secrecy, until the bid is made?**
There is no legal requirement that a proposed, unannounced transaction be kept confidential. However, in a friendly transaction both the bidder and the target share an interest in maintaining secrecy until an acquisition agreement has been signed, at which time the transaction generally must be announced immediately.

In a hostile bid, confidentiality is of the utmost importance to the bidder until it publicly announces the proposed transaction. If the target knows of a proposed hostile bid it may take defensive measures (see Question 23).

Rumours
Rumours of a proposed transaction may result in unusual trading activity in the target's shares. In such circumstances, Canadian stock exchanges may request the target to issue a press release commenting on the rumour, and may impose a trading halt on the target's shares until the release has been published. The press release must be accurate and may not be misleading. If the rumour is unfounded, the issuer ordinarily states that it knows of no corporate developments to account for the unusual market activity.

7. **Is it common to obtain a memorandum of understanding or undertaking from key shareholders to sell their shares? If so, are there any disclosure requirements or other restrictions on the nature or terms of the agreement?**

Before making an offer, a bidder is free to seek undertakings or "lock-up" agreements from shareholders to accept the bid. In fact, because many Canadian companies have a controlling shareholder or one or more significant (non-controlling) shareholders, the success of a bid may depend on securing their support. Lock-up agreements in Canada cover the whole spectrum, ranging from irrevocable undertakings to tender into a bid, to "soft" lock-ups where a shareholder agrees to tender but is free to withdraw if a higher competing bid is made. Institutional shareholders often agree to a soft lock-up but will not generally enter into an irrevocable one. Under certain circumstances, a bidder may be required to disclose the material terms of a lock-up agreement. In any event, in practice, the bidder will almost invariably disclose the existence and material terms of any lock-up agreement in the takeover bid circular.

A lock-up agreement may not confer a benefit on a shareholder that is not available to all shareholders of the target (see Question 17).

8. **If the bidder decides to build a stake in the target before launching the bid, what disclosure requirements, restrictions or timetables apply? Are there any circumstances in which shareholdings of associates could be aggregated for these purposes?**

The acquisition of a “toe-hold” position in the target’s securities before initiating a bid can be advantageous to a potential bidder, since the acquisition of a significant stake may discourage competing offers and the bidder’s total acquisition cost will normally be reduced. However, the bidder may find it difficult to dispose of the shares, other than at a loss, if the bid fails. This drawback is particularly true in Canada where the market for shares in Canadian companies tends to be relatively illiquid compared to other markets such as the US.

**Insider trading**
Stakebuilding by a potential acquirer is not an offence, nor does it give rise to civil liability under Canadian insider trading rules, unless the acquirer has knowledge of undisclosed material information concerning the target. However, the insider trading rules do apply to an insider of the potential acquirer (or a person in a similar relationship) who purchases shares of the target with knowledge of the proposed bid.

**Disclosure requirements**

Any person that acquires a stake of 10% or more in a Canadian public company must:

- Issue a press release immediately, and
- Within two business days file an "early warning" report,

in each case disclosing, among other things, the number of shares held and the acquirer's purpose in acquiring them, including any intention on the part of the acquirer to increase its beneficial ownership of the company in the future.

The shareholder is prohibited from acquiring any more shares until the expiry of one business day after the early warning report is filed. Further acquisitions of 2% or more trigger additional disclosure obligations.

If the target is a public company in the US, the acquirer is subject to similar disclosure obligations under US securities laws, but at a lower threshold of 5%.

**Aggregation with target securities held by certain persons**

Any securities acquired by persons acting “jointly or in concert” with a potential bidder will be aggregated with the bidder’s securities for purposes of determining whether the early warning thresholds are met. Whether a person is acting jointly or in concert is a question of fact, but the following persons will be presumed by statute to be acting jointly or in concert with a bidder:

- Every associate or affiliate of the bidder.
- Every person who, as a result of any agreement, commitment or understanding, formal or informal, with the bidder or any other person acting jointly or in concert with the bidder:
  - acquires or offers to acquire target securities of the same class as those acquired or sought to be acquired by the bidder; or
  - intends to vote target securities jointly or in concert with the bidder.

These aggregation rules are expansive, and so any potential bidder should assess carefully its relationships with potential joint actors before acquiring target securities to avoid any party inadvertently exceeding the early warning thresholds.

**Effect of stakebuilding on bid consideration: pre-bid integration**

Under the pre-bid integration rule, if a bidder buys shares in the target during the 90 days before making a bid:

- The bid price must be at least equal to the highest consideration paid.
• The bid must be for at least the highest percentage of target shares purchased from the holdings of any seller.

There is an exemption from these rules for market purchases that comply with prescribed conditions. Non-compliance can have very serious consequences and any person contemplating acquiring a toe-hold should seek legal advice before doing so. This is particularly relevant if non-cash consideration may be offered on the bid or if the bid may be for less than all the shares in the target.

Requirement for an offer to be in cash
The pre-bid integration rule has been interpreted as requiring, in certain circumstances, that the consideration under a bid be entirely or partly in cash or that a cash alternative be offered.

Poison pills
If the target has previously adopted a shareholder rights plan, or “poison pill”, an acquirer will generally trigger the target’s poison pill if it crosses the specified ownership threshold. This may cause a significant dilution of the acquirer’s voting rights and economic interest. The ownership threshold depends on the specific terms of the pill, but for most Canadian companies it is 20% (the same as the threshold for a bid – see Question 11).

Effect on ability to buy out minorities
Shares acquired in the market before the launch of a bid do not count toward the 90% of the target's shares that the bidder must acquire to effect a statutory compulsory acquisition of the shares not deposited under the bid. Similarly, toe-hold shares are not counted as part of the minority for purposes of minority approval of a subsequent amalgamation or other form of squeeze-out transaction (see Question 20).

9. If the board of the target company recommends a bid, is it common to have a merger agreement between the bidder and target? If so, what are the main issues that are likely to be covered in the agreement?

In a friendly bid, the bidder and the target will typically negotiate an acquisition agreement setting out the terms and conditions of the bid before announcing the offer. The acquisition agreement will provide that the target’s directors will agree to recommend to the target’s shareholders that they accept the offer, provided the offer is made on the terms specified in the acquisition agreement. Such terms will generally include:

• The offer price including, where securities of the bidder are to be offered as consideration, the number of such securities per target share.
• The timing of the offer.
• Offer conditions, both to the bidder’s obligation to make the offer and to its obligation to take up target shares deposited to the offer (see Question 13).
• Termination provisions.
In some acquisition agreements, the target board’s obligation to recommend acceptance of the offer is made subject to another bidder making a “superior offer” (which would be a carefully defined term in the agreement). Other provisions which may be included in the acquisition agreement include:

- Access to non-public information concerning the target and, less frequently, the bidder.
- The waiver by the target’s board of any poison pill.
- The treatment of any outstanding stock options or other securities of the target which are not subject to the bid.
- A “no-shop” provision prohibiting the target, subject to certain exceptions, from actively soliciting, encouraging, providing confidential information to or negotiating with, a third party in respect of an alternative transaction. The target’s board is typically permitted to respond to unsolicited inquiries or proposals from third parties under certain circumstances.
- Break fees (see Question 10).
- The form of squeeze-out transaction to be used to purchase the shares of minority shareholders following a successful bid.
- The retention of management, directors or employees.
- The disposition of certain assets of the target or the bidder in accordance with competition or other regulatory requirements.
- Payment of costs and expenses.

10. **Is it common on a recommended bid for the target company to agree a break fee if the bid is not successful? If so, please explain the circumstances in which the fee is likely to be payable and any restrictions on the size of the payment.**

It is quite common in friendly bids, where an acquisition agreement has been entered into, for the target to agree to pay a break fee to the bidder under certain circumstances. These may include:

- The target’s board of directors withdrawing its recommendation that shareholders accept the offer.
- The target entering into an agreement for an alternative transaction with a third party.
- A material breach by the target of the terms of the acquisition agreement.

Break fees in Canadian transactions are typically seen in conjunction with “no-shop” clauses in which the target agrees, subject to certain exceptions, not to solicit or encourage alternative proposals from third parties (see Question 9). The no-shop covenant is typically subject to a “fiduciary out”. This enables the target’s board to terminate the acquisition agreement if its fiduciary duty to shareholders requires it to recommend acceptance of a higher bid, or to enter into a superior alternative transaction and, in such event, the break fee will become payable.

No break fee is generally payable simply because fewer than the minimum number of target shares are deposited under the bid, provided the target has not terminated or breached its obligations under the acquisition agreement and no alternative bid or transaction has been made or proposed.
In Canada, break fees typically fall within the range of 3% to 5% of the market capitalization of the target.

**Announcing and making the offer**

11. **How must the bid be made? Are there any official requirements (for example, notice to the target board; press announcement; notification to the regulator; filing the offer document with the regulator)?**

**Definition of a takeover bid**

A takeover bid is defined in the Securities Act (Ontario) as an offer made as follows:

- The offer is to acquire outstanding equity or voting securities of the target.
- The offer is made to a person in Ontario, or whose last address in the target’s books is in Ontario.
- The securities subject to the offer, together with the securities already held by the bidder and by any persons acting jointly or in concert with the bidder, constitute 20% or more of the outstanding securities of any class. Holdings of convertible and similar securities must be taken into account in determining whether the 20% threshold has been reached.

Securities legislation in most other Canadian provinces contains a similar definition of a takeover bid. In addition, there is a general requirement that a bid made to security holders in any province or territory must be made in all provinces and territories (*National Policy No. 62-201*).

**Formal commencement**

A takeover bid may be formally commenced in one of two ways:

- By mailing a takeover bid circular to all registered holders of the target's securities in the jurisdictions where the bid is being made. The circular is generally also sent to non-registered shareholders through their brokers or other nominees. The circular must be filed with securities regulators as soon as practicable after mailing.
- By publishing a newspaper advertisement containing a brief summary of the terms of the bid. A bidder using this method must file the complete takeover bid circular with the securities regulators and deliver a copy to the target’s principal office on or before the date the advertisement is published. This method of commencing a bid is generally used in hostile situations where the bidder does not want to alert the target to the impending bid by requesting a list of the target’s shareholders. On a hostile bid, the bidder will typically requisition a shareholder list from the target on the same day as the advertisement. The corporate statutes in most Canadian jurisdictions require that this list be delivered within ten days. The bidder is required to mail the circular to shareholders within two business days of its receipt of the shareholder list.
However, these requirements (and other requirements applicable to bids generally) do not apply to certain exempt transactions, including:

- Purchases at market price of not more than 5% in any twelve month period.
- Purchases from not more than five persons, provided the consideration does not exceed 115% of the market price (as determined in a prescribed manner).

**Announcement of the bid**

Other than as described above, there are no rules governing the timing or content of the announcement of a bid.

Friendly transactions are normally announced immediately after the acquisition agreement negotiated between the bidder and the target is signed. The announcement typically sets out:

- The principal terms of the offer.
- The expected timing of its formal commencement or completion.
- An indication of the bidder's intentions for the target.

In friendly transactions the target board's recommendation is also disclosed. If a bidder is a "reporting issuer", and thus subject to Canadian continuous disclosure obligations, it must ensure that the announcement discloses all material information from the perspective of its own security holders.

**12. Please set out brief details of the offer timetable. (Consider both recommended and hostile bids.) Is the timetable altered if there is a competing bid?**

There is no single timetable applicable to all transactions. However, below are some guidelines on key dates and deadlines that apply to all bids, hostile or friendly.

**Offer period**

The offer must stay open for a minimum of 35 days from the date of formal commencement. Generally, if there is a variation in the terms of the bid, or a material change in the information contained in the takeover bid circular, a notice of variation or change must be sent to the target's shareholders. The bid must be extended for at least ten days from the date the notice is mailed.

**Directors' circular**

The target board of directors must mail to shareholders a directors’ circular responding to the bid no later than 15 days after the date of commencement (see Question 14). If the board needs more time to consider the bid, the circular can advise shareholders of this. In this event, a supplementary circular containing the board's recommendation must be mailed out at least seven days before the expiry date of the bid.

On a friendly bid, the target directors' circular is usually mailed to target shareholders at the same time (and in the same envelope) as the bidder's takeover bid circular.
Competing offers
Competing offers do not alter the legal time periods that apply to bids. However, a superior offer by a competing bidder may dissuade target shareholders from accepting the initial bidder's offer, and may force the initial bidder to extend and increase its offer. There is no maximum time period after which an offer must be withdrawn.

Regulatory delays
A bid may be subject to pre-notification under the Competition Act (Canada) and to approval under the Investment Canada Act (see Questions 29 and 30). Additional regulatory approvals may be required if the target's business is in a regulated industry, such as broadcasting or telecommunications, or if the target is a financial institution, securities dealer or airline. The effect of these approval processes on timing depends on the particular approval required.

Translation requirement
Shareholders in the province of Quebec must be provided with a French version of the takeover bid circular (Securities Act (Quebec)). A discretionary exemption from this requirement may be obtained from the Quebec Securities Commission if there are only minimal shareholdings in Quebec. If the exemption does not apply, the time involved in translating the circular can cause delays in the transaction timeline and add to the bidder's expenses.

Poison pill
The adoption by the target of a poison pill will delay completion of a hostile bid. However, unlike in the US, a poison pill cannot be used to delay a hostile bid indefinitely. Canadian securities regulators will not permit a poison pill to be used to deny shareholders the opportunity to make their own decision with respect to a bid. Therefore, they will terminate a poison pill if the target is unable to demonstrate that it is actively pursuing alternative transactions or if there seem to be no prospective alternative bids.

Based on decided cases, the OSC is generally willing to consider removing a poison pill 35 to 45 days after the commencement of the bid.

13. **What conditions are normally attached to a takeover offer?**

The following conditions are commonly attached to the offer, and must be satisfied or waived by the bidder before the expiry of the offer:

- Valid deposit under the offer, at or before its expiry, of such number of target shares as will enable the bidder to acquire the remaining outstanding target shares under a compulsory acquisition or squeeze-out transaction. The relevant level of acceptance will depend on how the bidder intends to acquire the remaining shares and the number of shares already held (see Question 20). Ontario securities law imposes no minimum acceptance threshold on takeover bids generally.
- There having been no material adverse change in the business or affairs of the target before expiry of the offer.
• The obtaining of all necessary governmental or regulatory consents or approvals on terms satisfactory to the bidder, including the expiry of any applicable waiting periods under competition, merger control or other similar laws.
• No action or proceeding having been taken before any court, tribunal or other regulatory authority, and no law or regulation having been enacted or proposed, which would have a material adverse effect on:
  
  o the target; or
  o the bidder’s ability to complete the offer, acquire any remaining target shares in a compulsory acquisition or squeeze-out transaction, or exercise rights of ownership in the target shares.

• The target will not have materially breached the terms of any acquisition agreement with the bidder.
• No target shareholder will have materially breached the terms of any lock-up agreement with the bidder.

Other deal-specific conditions may also be attached to the offer depending on the circumstances. A takeover bid cannot be made conditional on the bidder obtaining the necessary financing (see Question 17).

14. What documents will target shareholders receive on a recommended and hostile bid? (Briefly describe the purpose, main terms and responsibility for each document.)

The documents required to be sent to shareholders on a bid are the same whether the bid is friendly or hostile. They include the takeover bid circular and the directors' circular.

**Takeover bid circular**
This comprises the offer (which sets out the terms of the bid), and an offering circular containing prescribed information concerning the bidder and the offer. The disclosure required in the offering circular is not onerous on a cash-only bid. When securities are being offered as consideration for target shares, the offering circular must contain prospectus-level disclosure concerning the issuer of such securities. This includes financial statements of the issuer and, depending on the size of the target relative to the issuer, *pro forma* financial statements giving effect to the acquisition. These financial statements must generally be prepared in accordance with (or reconciled to) Canadian generally accepted accounting principles.

Acceptance documentation, which is required to be completed by shareholders who accept the offer, is mailed with the takeover bid circular, and consists of:

• A letter of acceptance and transmittal for shareholders who hold their shares in certificated form.
• A notice of guaranteed delivery for shareholders whose share certificates are not immediately available.

**Directors' circular**
This is prepared by the board of directors of the target and must include either a recommendation to accept or reject the bid, or a statement that the board is not making a recommendation. It must state the board's reasons for its decision. The directors' circular must correct any incorrect or misleading information contained in the takeover bid circular.

In a negotiated transaction, the directors' circular recommending acceptance of the bid is typically mailed to target shareholders in the same envelope as the takeover bid circular. In a hostile transaction, target shareholders receive these documents in separate mailings.

Each of the takeover bid circular, the directors' circular and any notice of change or supplementary circular must contain a certificate signed on behalf of the issuing company's board of directors as to the accuracy and completeness of the information contained in the document.

15. **Is there a requirement to make a mandatory offer? If yes, when does it arise?**

Unlike in certain jurisdictions, there is no requirement in Ontario to make a mandatory bid when certain ownership thresholds are passed.

16. **Please state key shareholding thresholds. At what point is effective control deemed to occur?**

Key thresholds are:

- **10%**. Filing of press release and early warning report required *(see Question 8)*.
- **20%**. Bidder is required to make a takeover bid to all shareholders of the target *(see Question 11)*.
- **33 1/3%**. Ability to block special resolutions *(see below)*.
- **50%**. Control of a corporation is conclusively obtained when a shareholder acquires voting securities carrying more than 50% of the votes required for the election of directors, although effective control of a widely held company can be obtained at lower levels of share ownership.
- **66 2/3%**. Special resolutions of a corporation’s shareholders require the approval of two-thirds of the votes cast under most Canadian corporate statutes (for corporations incorporated under the British Columbia Company Act, 75% approval is required). Matters that require approval by special resolution include, for example:
  - significant amendments to the company’s articles of incorporation;
  - amalgamations other than with subsidiaries;
  - continuance or re-incorporation of the company to the laws of another jurisdiction; and
  - dissolution.
- **66 2/3% of all shares plus 50% of shares held at the date of the bid by shareholders unrelated to the bidder**. Generally permits bidder to squeeze out minority shareholders. *(see Question 20)*.
- **90% (other than shares held by the bidder at date of the bid)**. A bidder may take advantage of compulsory acquisition procedures *(see Question 20)*.
Consideration

17. What form of consideration is commonly offered on a public takeover? Are there any limitations on the type of consideration that can be offered?

Generally, there are no restrictions on the form of consideration that can be offered on a takeover. Target shareholders may be offered a choice, for example, cash or shares in the bidder. This is often subject to limits on the aggregate amount of each form of consideration offered.

Identical consideration

All shareholders must be offered identical consideration. Where there is a choice of consideration, they must all be offered the same choice on a pro rata basis. Exemptions from the identical consideration requirement can be obtained in limited circumstances, generally in connection with multi-jurisdictional bids where offering a certain form of consideration in a foreign jurisdiction produces delays or burdensome ongoing reporting requirements.

Prohibition on collateral agreements

A bidder may not enter into a collateral agreement with a target shareholder that has the effect of offering greater value for that shareholder's shares than for the shares of others. This prohibition is interpreted broadly and encompasses virtually all forms of agreements that might be entered into with a shareholder in connection with a takeover, including:

- Employment agreements.
- Supply agreements.
- Sales of assets.
- Rights of first refusal.

If the agreement is essential to the acquisition, the bidder must apply to securities regulators for a ruling confirming that the agreement is for valid business reasons other than to increase the value of the consideration to be paid for the other party’s shares.

No financing condition

If cash forms part of the consideration, the bidder must ensure the necessary funds are available before commencing the bid. Generally, a firm letter of commitment from the bidder's lenders satisfies this requirement.

Choice of consideration

In Canada, the use of securities as consideration does not cause undue delay to completion of the transaction:

- No regulatory approval is required for securities exchange transactions. In contrast to the position in the US, securities offered as consideration on a bid in Canada are not required to be qualified by a securities regulatory authority. The takeover bid circular must contain prospectus-level disclosure concerning the issuer, but it is not subject to mandatory review by a securities regulator (but see Question 19).
• A securities exchange bid takes slightly longer from the decision to proceed than a cash bid because of the time needed to compile the additional information required in the takeover bid circular. The minimum length of time that the bid must remain open is 35 days, the same as for cash bids.

**Foreign bidders: exchangeable shares**
Exchangeable share structures are commonly used to avoid the disadvantages that arise when foreign bidders offer their own securities as consideration in M&A transactions in Canada. Exchangeable shares are issued by a Canadian-incorporated subsidiary of the foreign bidder and are exchangeable for shares in the parent at the shareholder's option. Exchangeable shares are the economic equivalent of shares in the parent, and confer dividend and voting rights that mirror those attaching to the parent shares. Often, both the exchangeable shares and the parent company's shares are listed on a Canadian stock exchange.

Exchangeable shares are issued by a Canadian corporation and therefore offer the following tax advantages:

• Subject to certain conditions, Canadian shareholders receive exchangeable shares on a tax deferred, or "rollover" basis. By contrast, a receipt of shares in the foreign acquirer would be an immediately taxable transaction.
• For the purposes of foreign property holding limits, listed exchangeable shares do not count as "foreign property" for Canadian tax deferred plans or for tax exempt entities, such as certain pension funds.
• Dividends paid on exchangeable shares are generally subject to taxation in the hands of the holder of the shares at a lower rate than dividends paid by foreign corporations.

Nevertheless, exchangeable shares are often treated as "preferred shares" for Canadian income tax purposes. They are therefore most suitable in cases where the Canadian target is a taxable entity and can reclaim tax paid on preferred shares, or where the foreign acquirer does not pay dividends.

Exchangeable share structures are technically complicated and their use may increase the preparation time for a transaction.

18. **Are there any regulations that provide for a minimum level of consideration?**

Other than the pre-bid integration rule (see Question 8), there is no legal requirement that a bid meet any minimum level of consideration.

19. **Are there any restrictions on the form of consideration that a foreign bidder can offer to shareholders in your jurisdiction? Please state any restrictions/ filing requirements etc.**

There are no restrictions on the form of consideration that may be offered by a foreign bidder.
Newly issued securities of a foreign issuer are subject to resale restrictions unless the issuer is a "reporting issuer" in Ontario. Bidders that are not reporting issuers can apply to the OSC for a discretionary exemption order. This will generally be granted if the OSC is satisfied that the takeover bid circular meets the disclosure requirements of a prospectus. The exemption can normally be applied for and obtained within the offer period and generally does not affect the bid timetable.

Also, exchangeable share structures are commonly used to avoid the disadvantages that arise when foreign bidders offer their own securities as consideration (see Question 17).

Post-bid

20. Can a bidder compulsorily purchase the shares of outstanding minority shareholders?

There are two basic ways in which a successful bidder can acquire the shares held by non-tendering shareholders. In most cases, if the bidder acquires 50% or more of the target shares held by unrelated shareholders in the course of the bid, and holds 66 2/3% or more of the total outstanding shares, it can buy out the remaining shareholders. However, this is not always the case, and the appropriate analysis needs to be made before the bid and accounted for in the bid's minimum acceptance condition. The way in which this acquisition of the minority's shares can be achieved depends on the acceptance level of the bid.

Compulsory acquisition provisions

If the bid is accepted by the holders of 90% of the target's shares (excluding shares held by, or on behalf of, the bidder), the bidder can use the compulsory acquisition provisions in the target's governing corporate statute. The bidder sends a notice of acquisition to the non-tendering shareholders, and pays the offer consideration to the target to hold in trust. Depending on the target's jurisdiction of incorporation, the compulsory acquisition may take from a few days to 35 days or more after completion of the bid.

Other squeeze-out methods

If the compulsory acquisition provisions cannot be used, the remaining shares can be acquired in a second step amalgamation or other form of squeeze-out transaction. A squeeze-out has to be approved by at least 66 2/3% of the votes cast at a meeting of the target's shareholders (for corporations incorporated under the British Columbia Company Act, 75% approval is required). Ontario and other provinces have enacted rules that ensure that minority shareholders are treated fairly in transactions of this nature by, for example, requiring minority shareholder approval. Generally, but not always, shares acquired from public shareholders in a takeover count towards the minority approval in a second step transaction, provided the same consideration is offered. A second step transaction typically takes 45 to 55 days to implement.

Regardless of the method chosen, non-accepting shareholders are entitled to demand payment of "fair value" for their shares, as determined by the court.
21. **Are there any rules protecting the target from a further bid by the same bidder if the initial bid fails?**

There are no rules in Canada that prevent an unsuccessful bidder from making another bid.

22. **What action is required to de-list a company?**

A company listed on the Toronto Stock Exchange (TSX) may apply to have its securities of any class voluntarily de-listed from the TSX. The application takes the form of a letter to the exchange outlining the reasons for the proposed de-listing. The de-listing must be approved by a resolution of the company’s board of directors. Although de-listing is subject to approval by the exchange, the TSX will generally not object to a proposed de-listing which follows a successful takeover bid.

The TSX Venture Exchange, Canada’s other principal stock exchange which mainly lists junior issuers, has similar rules governing voluntary de-listing.

**Target response**

23. **What actions can a target’s board take to defend a hostile bid (pre-and post-bid)?**

**Initial response**

It is normal for the target to issue a press release acknowledging the proposed bid shortly after the bidder announces its intention to make a hostile bid. The announcement usually informs shareholders that the directors are studying the available information concerning the bid, and advises them not to tender their shares into the bid until the target's board evaluates and recommends acceptance or rejection of the bid. This is sometimes referred to as a "stop, look and listen" press release.

**Defensive measures**

Subject to directors’ fiduciary duties, a target may take various actions to defend itself against a hostile takeover. However, the courts have held that once it is apparent that there will be a sale of the target's equity and/or voting control, the duty of the target board is to act in the best interests of the shareholders as a whole. It should not block the sale, but take active and reasonable steps to maximise shareholder value. These steps could include conducting a market canvas to assess the likelihood of superior bids, or initiating an auction of the target.

Canadian securities regulatory authorities scrutinise the defensive tactics adopted by a target and take action if they consider that the defensive measures frustrate an open bidding process or deny shareholders the ability to decide whether or not to accept an offer.

There are numerous reasons why a target may contest either the bid itself, or the behaviour of the hostile bidder. It may be trying to buy time to enable competing offers to surface, or to distract and divide the energies of the bidder, or to block an unfavourable transaction entirely. Since it is difficult to gauge the efficacy of any single defensive tactic in advance, the target generally adopts different tactics in combination. These may include:
• Adopting a poison pill. This action does not initially require shareholder approval so can be taken swiftly.
• Initiating securities regulatory proceedings. The target can allege, for example, unlawful pre-bid stake-building, inadequate or misleading disclosure in the takeover bid circular, or deals with shareholders that contravene the collateral agreement prohibition.
• Initiating litigation in the courts. The target can allege wrongful conduct on the part of the bidder by, for example, challenging the proposed takeover on antitrust or other statutory grounds.
• Seeking an alternative bid from a “white knight”.
• Seeking a friendly “white squire”. The target may place a substantial block of shares with a third party, or enter into a significant joint venture or co-operative transaction with it.
• Seeking a sale of strategic assets that the bidder is known to be interested in acquiring.
• Making an acquisition that makes the takeover too expensive for the bidder, or presents the bidder with competition problems.

Some defensive measures employed in the US, such as creating a staggered board, or limiting shareholders’ rights to requisition shareholder meetings, are unavailable or have little practical efficacy for Canadian companies.

Tax

24. Are any transfer duties payable on the sale of shares in a company that is incorporated and/or listed in your jurisdiction? Is there any way in which payment of transfer duties can be avoided?

No transfer duties are imposed on the transfer of securities in Canada.

25. Is tax potentially payable on gains arising on the sale of shares by individuals/companies that are tax resident in your jurisdiction?

A shareholder that is resident in Canada who disposes of target shares under a takeover bid may realize a capital gain on the disposition. The capital gain is generally measured as the amount by which the net proceeds of disposition realized by the shareholder exceed the shareholder’s adjusted cost base of the target shares. 50% of any such capital gain will be included in the shareholder’s income for the year of disposition and taxed at the shareholder’s ordinary rates.

If the consideration for the acquisition includes shares of a taxable Canadian corporation, including exchangeable shares (see Question 17), target shareholders who are resident in Canada may, under certain circumstances, receive the consideration shares on a tax-deferred, or rollover basis. Certain rollover provisions require the shareholder and the purchaser to file a joint tax election with the tax authorities.

26. If a bid vehicle is incorporated in your jurisdiction, are there any restrictions on the capital structure of the bid vehicle from a tax perspective (thin capitalisation rules)?

There are no general restrictions on the capitalisation of a bid vehicle. However, if the bid vehicle is owned by a non-resident person, the Canadian thin-capitalisation rules may apply.
These rules establish a 2:1 debt-to-equity ratio for debt from related non-resident persons. A bid vehicle will be disallowed the deduction of interest on its debts to related non-resident persons to the extent the outstanding amount of these debts exceeds two times the aggregate of the corporation’s retained earnings and its contributed surplus and paid-up capital in respect of shares held by related non-resident persons.

27. **If a bid vehicle is incorporated in your jurisdiction to purchase a target company in your jurisdiction, can interest costs incurred by the bid vehicle be set off against profits of the target company for tax purposes?**

Without some planning, interest costs incurred by the bid vehicle cannot be set off against profits of the target company for tax purposes. The bid vehicle and the target must be combined through an amalgamation or winding-up, or they must engage in an income-shifting transaction (that is, income of the target company would be effectively transferred to the bid vehicle).

28. **What is the tax treatment of dividends and interest paid by a company that is tax resident in your jurisdiction to a foreign shareholder?**

Dividends and interest paid by a corporation that is resident in Canada to a person that is a non-resident of Canada are subject to Canadian withholding tax at a rate of 25% of the amount of such payments. Such rate is subject to reduction under one of Canada’s bilateral tax treaties.

**Other regulatory restrictions**

29. **Please give a brief overview of antitrust regulation relating to the acquisition of a company in your jurisdiction. In particular:**

- **What are the thresholds for investigation?**
- **Is notification mandatory or voluntary?**
- **What is the substantive test?**
- **What is the time limit for a decision and is there an obligation to suspend?**

- **Thresholds for investigation.** A merger transaction must be pre-notified to the Canadian Competition Bureau if both:
  - the combined assets in Canada, or the combined gross revenues from sales in, from or into Canada, of the bidder and the target (as shown on their last audited financial statements), together with their affiliates, exceed C$400 million (US$270 million).
  - the assets or revenues of the target’s business in and from Canada exceed C$35 million (US$23.6 million). This threshold is expected to rise to C$50 million (US$33.8 million) in 2003.

- **Notification.** For merger transactions that meet both the above thresholds, notification is mandatory.

- **Substantive test.** The Bureau is likely to challenge any transaction which will have the effect of substantially lessening competition in Canada. The Bureau has the right to challenge an anti-competitive merger even if pre-merger notification is not required.
• Time limit and obligation to suspend. The transaction cannot be completed until the notification is filed and the applicable waiting period has expired. This is normally 14 days for a "short form" notification, but can be extended by the Bureau by 42 days if a "long form" notification is requested.

Normally, the bidder does not close the transaction until the Bureau completes its review and notifies the parties that it will not challenge the merger. The review process can be as short as two weeks but can extend to five months or more for transactions that give rise to complex competition issues.

A bidder would apply for an advance ruling certificate (ARC) for transactions that do not give rise to substantive competition issues. The issuance of an ARC is discretionary. It precludes challenges to the merger by the competition authorities during the three years following completion of the merger, when such a challenge may otherwise be made.

30. Are there restrictions on foreign ownership of shares (generally and/or in specific sectors)? If yes - what approvals are required for foreign ownership and from whom are they obtained?

Foreign ownership of shares generally
There are relatively few statutory limitations on foreign ownership of shares in Canadian companies. Those that do exist apply primarily to:

- Banks.
- Insurance companies and other financial institutions.
- Securities dealers.
- Airlines
- Telecommunications and broadcasting companies.

Limitations include absolute percentage limits on foreign ownership (often 25% or 33% in the aggregate), and prohibitions against foreign entities having “control in fact”.

Investment Canada Act
A transaction may require approval under the Investment Canada Act (ICA) if both:

- A non-Canadian entity acquires control of a Canadian business.
- The gross book value of the assets of the target business exceeded certain thresholds at the end of its most recent financial year.

The acquisition of more than 33 1/3% of the voting shares of a Canadian business gives rise to a rebuttable presumption that control has been acquired.

Generally, if the acquirer is a company controlled in a country that is a member of the World Trade Organization (WTO investor), the proposed transaction is subject to review under the ICA
if the Canadian target has assets of C$223 million (US$143 million) or more. This threshold rises every year in accordance with an inflation index.

If the acquirer is not a WTO investor, the review threshold is C$5 million (US$3.2 million). The lower threshold also applies to WTO investors where the target's business is in certain industries including:

- Uranium production.
- Transport.
- Financial services.
- Cultural businesses (publishing books and other printed media, production and distribution of film, television, radio or music).

If a direct acquisition of a company carrying on a Canadian business is subject to review by the ICA, approval must be obtained before the transaction is completed. An application must be filed with Industry Canada, containing factual information concerning:

- The acquirer.
- Its controlling shareholders.
- The target.
- The acquirer’s plans for the business.

The minister responsible for the ICA must decide whether or not the proposed acquisition is likely to be of "net benefit to Canada" within 45 days.

The review process may include negotiating undertakings with Industry Canada relating, for example, to:

- Business plans.
- Levels of employment.
- Capital expenditures.
- Research and development after the acquisition.

If the Minister is unable to reach a decision within 45 days, he may extend the time limit by an additional 30 days, or longer if the acquirer agrees. If the Minister concludes that the transaction is not of net benefit to Canada, the acquirer has a further 30 days to make additional submissions and submit undertakings in order to obtain approval.

If an acquisition of control is not subject to review under the ICA, a simple notification of the acquisition must nevertheless be filed within 30 days of completion.

31. Are there any restrictions on repatriation of profits or exchange control rules for foreign companies?
Canadian law does not impose exchange or investment controls on foreign companies. Depending on the way in which profits are proposed to be repatriated, there could be tax consequences.

**Reform**

32. **Are there any proposals for the reform of takeover regulation in your jurisdiction?**

There are currently no proposals being actively considered by securities regulators that would substantially alter takeover bid regulation in Canada.

**Regulator contact details**

**Name.** Ontario Securities Commission  
**Address.** Suite 800, 20 Queen Street West, Toronto, Ontario M5H 3S8  
**Tel.** +1 416 597 0681  
**Fax.** +1 416 593 8122  
**Website.** www.osc.gov.on.ca  
**Area of competence.** Administration and enforcement of Ontario securities laws.  
**Head of authority.** David Brown (Chair).  
**Obtaining information.** The OSC website provides a wide range of information, including the text of the *Securities Act* (Ontario), the accompanying regulations, rules and policies, and the status of enforcement proceedings. It has links to securities regulators in the other provinces.

**Name.** Toronto Stock Exchange (TSX)  
**Address.** The Exchange Tower, 130 King Street West, Toronto, Ontario M5X 1J2  
**Tel.** +1 416 947 4700  
**Fax.** +1 416 947 4547  
**Website.** www.tsx.com  
**Area of competence.** Administration and enforcement of TSX rules and policies.  
**Head of authority.** Barbara G. Stymiest (President and Chief Executive Officer).  
**Obtaining information.** The TSX website provides a wide range of information, including the complete *TSX Company Manual*. It also serves as the website for the TSX Venture Exchange, which lists more junior issuers.