"All the time in the world": Canadian securities regulators adopt fundamental changes to take-over bid regime

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The Canadian Securities Administrators (CSA) have announced the final adoption of fundamental changes to the take-over bid regime in Canada. These changes are substantially similar to a draft version of the amendments that the CSA published on March 31, 2015, which we previously reviewed.

The new rules will come into effect on May 9, 2016 (except that implementation may be delayed in Ontario until the applicable legislation is proclaimed into force). They represent the most significant changes to Canada's take-over bid regime in decades, and the consequences will be numerous and significant.

The three main changes to the take-over bid rules

The most significant changes to the take-over bid rules are the following three requirements, which will apply to all non-exempt take-over bids:

Minimum 105-day bid period

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The bid must remain open for a minimum deposit period of 105 days (under the existing rules, the minimum deposit period is only 35 days). However, there are two important exceptions to this new rule:

- **Voluntary reduction by target board***:* If the target board issues a news release in respect of a proposed or existing take-over bid which states that the board will accept a specified shorter deposit period for the bid (which is not less than 35 days), then the minimum deposit period for that bid only needs to be the shorter deposit period stated in the news release. However, if there are any *other* outstanding or subsequent take-over bids, those other bids would then also gain the benefit of the stated shorter minimum deposit period. In any event, no bid could stay open for less than 35 days.
- **Non-voluntary reduction for "alternative transaction"***:* If an issuer issues a news release announcing some type of "alternative transaction" such as a plan of arrangement, then the minimum deposit period for any then-outstanding take-over bid or any take-over bid subsequently commenced before the completion of such alternative transaction need only be at least 35 days.

In both of these exceptions to the 105-day rule, the bid would still need to remain open at least 10 days after the date of any notice of variation concerning the reduction of the deposit period.

Minimum tender condition

There will be a minimum tender condition of more than 50% of the outstanding securities of the class that are subject to the bid. The more than 50% tender condition will exclude securities beneficially owned, or over which control or direction is exercised, by the bidder or by any person acting jointly or in concert with the bidder. So, for example, if the bidder wishes to make a bid for all of the issued and outstanding common shares of Company A and the bidder already owns 25% of the common shares of Company A, more than 50% of the remaining 75% of the common shares must be tendered to the bid before the bidder can take up and pay for the shares.

10-day extension requirement

After the expiry of the initial deposit period (the 105-day period or the shorter period, if applicable), the bidder must extend its bid by an additional 10 days if: (a) all terms and conditions of the bid have been complied with or waived; and (b) the minimum tender condition is satisfied (more than 50% of the applicable securities have been tendered).

The key change from 2015 proposals: 105-day minimum deposit period rather than 120 days

Other than the change to the minimum deposit period, the final form of the amendments is mostly unchanged from the CSA's 2015 proposals. The CSA reduced the originally proposed minimum deposit period in order to ensure that bidders who make 105-day bids can extend their bids for the required 10-day period and still be able to complete their acquisition via the "compulsory acquisition" provisions which are contained in Canadian corporate statutes. Those provisions allow a compulsory acquisition (i.e., a forced sale of any remaining untendered shares) to occur if holders of 90% of the shares (except for shares held by the bidder) have accepted a bid within 120 days of the commencement of that bid.

How the new rules will affect Canadian public companies

Consequences of the new rules are expected to be numerous and significant. We highlight six of the most likely or possible results below.

Effect on hostile bids and bidders

The former 35-day minimum deposit period was perceived by most observers as giving hostile bidders a strategic advantage, by forcing target boards and shareholders to make rushed decisions (or at least essentially forcing them to implement shareholder rights plans – more on that below), and by not allowing adequate time for target companies to assess alternatives and find other "white knight" bidders. The prevailing view among industry

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observers at this point seems to be that hostile bids will now be a less attractive option and will be more difficult to carry out, given that such bids will now drag on longer, will be more expensive and will have less chance of success (because of the extended deposit period, which will presumably provide plenty of time for the target to drum up alternatives or other bidders). Accordingly, we would expect the number of hostile bids in Canada to decrease. Presumably, this situation will in turn lead potential acquirors to give greater consideration to alternative structures or strategies, such as launching proxy contests. In addition, one would also expect that there will be greater incentive to negotiate with a target rather than launching a hostile bid in the first place.

Effect on target boards and shareholders

The proposed amendments will give significantly more power and flexibility to target boards and their security holders in the face of hostile bids, because

(a) the required 105-day minimum bid period will give boards extra time to consider the bid (and possible alternatives, such as seeking a "white knight" bidder);

(b) the minimum tender requirement will have a roughly equivalent effect to requiring a shareholder vote; and

(c) the 10-day automatic extension will reduce the pressure that security holders may feel to tender early to the bid.

Effect on "poison pills"

The three main changes to the rules (a minimum tender condition, a 10-day automatic extension feature and a lengthened minimum deposit period) are all common and key features of Canadian shareholder rights plans (often referred to as "poison pills"). Therefore these changes can fairly be characterized as the legislative imposition of certain key features of shareholder rights plans on all Canadian public companies. What's more, the typical "permitted bid" minimum deposit period in a Canadian shareholder rights plan averages around 60 days, so in that sense, the new minimum deposit period is very generous to a target board of directors.

As a result of all this, a big part of the traditional rationale for adopting shareholder rights plans has now fallen by the wayside. This naturally raises the question: are shareholder rights plans on their way out in Canada? Time will tell, but it is reasonable to expect that the new take-over bid rules will result in fewer rights plans being adopted in Canada in the future.

A small lifeline for poison pills? "Exempt bids" are not covered by the new changes

It is important to note that these changes to the rules only apply to *non-exempt take-over bids*. So even with these changes in place, it will still be possible for third parties to acquire control of a target company via purchases which are exempt from the take-over bid rules such as through normal course purchases or the "private agreement" exemption (sometimes such incremental acquisitions are referred to as "creeping take-overs"). Alternatively, a third party can seek to acquire effective control of a public company by acquiring a large amount of the company's convertible debt. Another consideration for potential targets will be the recent advent in Canada of the so-called "voting pill," which is essentially a shareholder rights plan modified to cover off hostile proxy solicitations.

In light of these and other strategic reasons to keep a rights plan in place as a possible bargaining chip, we think that there will still be a role for shareholder rights plans to play, but they certainly will not continue to play the central role that they have historically played in contested take-overs in Canada.

More on poison pills – issuers will have some decisions to make

Over the last couple of decades, shareholder rights plans have been adopted by a large number of Canadian public companies. This means that these same companies are going to have to decide whether to retain these plans (albeit in amended form to take the new rules into account) or to terminate them – either proactively, or by just allowing them to lapse according to their terms. Some companies will have this decision forced on them sooner rather than later, for example if their rights plans are up for renewal at their next annual shareholder meeting.

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Effect on partial bids

The “more than 50%” minimum tender condition mentioned above will also apply to partial bids (i.e., bids made for less than all of the outstanding shares of a company). Therefore, more than 50% of the securities of the class that are subject to the bid will have to be tendered in order for the offeror to be able to complete the bid. This condition will make partial bids more difficult to complete, compared to the existing rules, where an offeror making a partial bid has the ability to pick up any securities tendered up to the maximum amount specified in the bid, regardless of how many holders actually tender their securities.

If you have any questions about this bulletin or if you would like further information about the new take-over bid rules, please contact the authors.

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