M&A Building Blocks

Dealing with Public Disclosure

Acquisitions or divestitures of public companies or by public companies in Canada may trigger disclosure obligations under applicable securities laws. The nature and timing of disclosure is an important aspect of the overall implementation strategy of a successful transaction.

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Key Issues/Process Points

1 Disclosure Framework

A reporting issuer is required under Canadian securities laws to make timely disclosure to the public of a "material change" and, in the case of a Toronto Stock Exchange or TSX Venture Exchange listed issuer, "material information". When public disclosure is made, a reporting issuer must ensure that it is accurate and complete and does not contain a misrepresentation.

In addition, a person "in a special relationship with a reporting issuer" who has knowledge of a material fact or material change that has not been generally disclosed cannot disclose the information to another person ((i.e. "tipping") except in the necessary course of business. This would include directors and officers as well as persons proposing to make a take-over bid for the issuer, or other significant transaction.

2 Statutory and Regulatory Definitions[1]

Disclosure requirements are centred on the concept of "materiality". The fundamental question in determining whether a change or fact in relation to an issuer is a "material change" or "material fact" is, broadly speaking, whether the change or fact results in or would reasonably be expected to result in a significant change in the market price or value of the issuer's securities. "Material information", the disclosure standard of the TSX and TSXV, includes both material facts and material changes.

3 Timely Disclosure Obligations

If a material change[2] occurs, the reporting issuer must:

- Immediately issue and file a news release and
- File a material change report as soon as possible, but no later than 10 days after the change.

There is a temporary exemption from the obligation to disclose certain material confidential information:

- if disclosure would be unduly detrimental to the interests of the reporting issuer, or
- if the material change consists of a decision by management to implement a change, management believes the board of directors will confirm the decision, and there is no reason to believe that persons with knowledge of the material change have made use of that knowledge in purchasing or selling securities of the reporting issuer. To utilize the exemption, the issuer must file a confidential material change report with the securities authorities and renew the report every 10 days until public disclosure is made.

4 Best Practices

In the context of an M&A transaction, where confidentiality and timing are often vital, compliance with disclosure obligations without compromising the success of the transaction is a key element in deal management. Best practices in this regard include:

- Obtaining confidentiality agreements from potential counterparties to the proposed transaction.
- Reviewing disclosure obligations at each stage of the deal.
- Establishing at the outset strict confidentiality and "need to know" protocols in relation to the transaction.
- Ensuring Board minutes accurately refer to the status of negotiations between the parties and review by the Board so that it is clear that board approval is not given until it has been deliberately and finally given.
- Establishing "blackouts" on trading in the issuer's securities by board members, senior management and, if a transaction appears imminent, other employees.
- Monitoring trading activity in the issuer's securities for unusual activity which might indicate a leak.

Note that an issuer may be required to issue a press release earlier than planned if information is leaked and the issuer has reasonable grounds to believe its securities are being purchased or sold with knowledge of undisclosed material information. This is one reason why enforcing confidentiality and managing the process can be so important.

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1 Summarized from the *Securities Act* (Ontario).

2 TSX or TSXV policies require disclosure if material information arises.

5 When to Disclose?

- Disclosure will generally be required at the time of Board approval and signing of a definitive agreement.
- Disclosure may also be required earlier in the process, for example upon the adoption of a sale process, depending upon the certainty surrounding the decision and the risk of leaks.
- In some circumstances, disclosure obligations may not be triggered, but one or more parties may wish to disclose for strategic reasons.

6 What to Disclose?

The press release announcing an agreed-upon transaction should include:

- All information considered material, such as:
  - Price
  - Principal conditions
  - Timeline
  - Required shareholder, creditor and regulatory approvals
  - Deal protection provisions
  - Other material deal terms
  - Financial metrics
    - » Premium to market price
    - » Impact on purchaser
- Involvement of related parties, if any, and any valuations or fairness opinions obtained or required.
- Process followed by the Board and/or special committee.
- Other information material to security holders.

7 Contingency Planning and Dealing with Leaks

Issuers are sometimes called upon by regulators to respond to rumours and/or unusual trading activity in their securities.

- Issuer may choose to be proactive and put out an announcement in response to such activity.
- In certain cases IIROC (Investment Industry Regulatory Organization of Canada), which monitors securities trading for unusual activity, may require disclosure.

In response to an inquiry from IIROC, an issuer must be truthful, but it also may not yet be in a position to announce a “deal”. It may be sufficient to comment publicly on the process generally, where there is no deal to announce. In such cases, it may be appropriate to emphasize the lack of certainty.

Before making an announcement to address market rumours, it may be necessary to refer to any applicable confidentiality agreement to determine whether consent of another party is required.

8 Disclosure Documents

Once an M&A deal is announced, there will usually be one or more disclosure documents which must be issued. While the press release announcing the deal (and the related material change report which must also be filed) will contain the key points in relation to the deal, subsequent disclosure documents will contain much greater detail. In the case of a take-over bid, the key disclosure documents are the take-over bid circular prepared by the party making the bid, and the directors' circular prepared by the issuer. In the case of a transaction implemented by way of plan of arrangement or amalgamation, the key disclosure document is the management information circular (or proxy circular) prepared by the issuer. Important considerations in relation to the disclosure contained in these documents include:

- Follow the forms carefully, but not narrowly.
- Purposive disclosure is expected by regulators and investors, especially in the case of "material conflict of interest transactions".
- Failure to comply with disclosure requirements leaves the deal subject to attack (for example by way of application to the OSC to compel additional disclosure).
- There is heightened scrutiny associated with "material conflict of interest transactions", including disclosure of process and benefits to related parties. In this regard:
  - Disclosure documents are reviewed by Ontario Securities Commission, Autorité des marchés financiers (Québec), Alberta Securities Commission, Manitoba Securities Commission and New Brunswick Securities Commission
  - The form requirements are open to interpretation – but the market wants to know who stands to benefit; failure to disclose may result in shareholders and regulators asking questions
  - Disclosure is required regarding background and process, including:
    - » Reasoning and analysis of the board and any special committee
    - » Desirability and fairness of the transaction
    - » Reasonably available alternatives, including status quo
  - Include a detailed summary of the background to the transaction and of the board's process and financial analysis
  - Regulators will also look at the analysis underpinning any exemptions the parties seek to rely upon

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