

## Corporate Securities Law

December 1, 2015

### BCSC Permits Private Placement in Face of a Hostile Bid

The British Columbia Securities Commission (BCSC) has released its reasons in an application brought by Red Eagle Mining Corporation (“**Red Eagle**”) alleging improper defensive tactics by CB Gold Inc. (“**CB Gold**”). Red Eagle had applied to the BCSC to cease trade both CB Gold’s shareholder rights plan and a private placement to Batero Gold Corp. (“**Batero**”), which had also entered into a support agreement with CB Gold in connection with an offer by Batero for all of CB Gold’s shares (the “**Batero Agreement**”). The BCSC cease traded the rights plan. However, it allowed the private placement, highlighting the difficulties bidders face in overcoming certain defensive tactics by application to the securities regulator.

#### Background

In June of 2015, Red Eagle, which had earlier engaged in unsuccessful discussions with CB Gold about a possible transaction, launched a share exchange take-over bid for CB Gold. At the time of Red Eagle’s offer, CB Gold was running short of cash, and knew that a proposed related party transaction was not going to be approved by its shareholders. CB Gold’s shareholders had earlier approved the adoption of a shareholder rights plan.

In July of 2015, CB Gold announced it had entered into the Batero Agreement and, in connection with that agreement, completed a private placement to Batero. The announcement did not disclose that the principal shareholder of CB Gold was a significant shareholder of Batero. The TSX Venture Exchange made inquiries as to whether the private placement was a defensive tactic, but ultimately granted conditional approval for the private placement after CB Gold provided evidence that it needed the proceeds to continue as a going concern.

#### The Rights Plan

In considering Red Eagle’s challenge to CB Gold’s rights plan, the BCSC applied the rules and principles developed under the current takeover bid regime, not the Proposed Amendments. In concluding that CB Gold’s rights plan had outlived its usefulness, the BCSC determined that, among other things:

- the rights plan was not facilitating a robust auction (in fact, the rights plan was constraining the competitive process by preventing shareholders from tendering to the Red Eagle bid);
- the Red Eagle bid was not coercive, despite the fact that the 50% minimum tender condition had been waived (the Proposed Amendments will require that all bids be subject to a 50% minimum tender condition); and
- on expiry of the Red Eagle bid, it would have been open for a significant amount of time, even if less than the 120-day minimum required under the Proposed Amendments.

#### The Private Placement

In considering an order to unwind the private placement, the BCSC noted that reviewing a private placement in the context of a hostile bid is more challenging from a regulatory perspective than reviewing a rights plan. In particular, in the words of the BCSC, it “scrambles together” different regulatory and legal regimes and issues. In the BCSC’s view, the review engages securities laws relating to improper defensive tactics, corporate laws relating to the target board’s decision to complete a private placement and regulatory matters relating to the approval by the target’s stock exchange.

While the BCSC confirmed that its public interest power is broad enough to encompass the unwinding of a private placement, it emphasized that such power should only be exercised conservatively, and only where there is “clear abuse of the target shareholders

# Goodmans<sup>LLP</sup> Update

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and/or the capital markets.” The BCSC found that because CB Gold required financing to remain a going concern, the private placement had a legitimate business purpose and was not primarily a defensive tactic. It also found that because Red Eagle had waived its minimum tender condition, Red Eagle’s bid was not frustrated by the private placement. The private placement, therefore, was not “abusive”.

In its reasons, the BCSC also commented on other factors that can arise in the consideration of defensive tactics. Specifically:

- notwithstanding the breadth of its public interest powers, the remedies available to the BCSC were constrained by practical limitations in unwinding the transaction; for example, the proceeds of the private placement may have been spent;
- the BCSC was reluctant to overturn a transaction that had been approved by a stock exchange, expressing concern that doing so could lead to different standards of review and undesirable “regulatory arbitrage”; and
- altering the dynamics of the auction to require the correction of technical deficiencies in disclosure would cause greater prejudice than not intervening.

## Lessons for Participants in M&A Transactions

The Red Eagle decision provides the following guidance to M&A participants:

- Pending implementation of the Proposed Amendments, securities regulators will continue to apply the current approach to rights plans (see our December 1, 2015 Update, *ASC Strikes Oil Compromise - COSL Rights Plan Allowed to Stand for an Additional 30 Days*).
- The standard for securities regulatory intervention in defensive tactics other than rights plans is “clear abuse”, a high threshold for acquirors to overcome. Even potentially unfair private placements that do not meet the threshold of “abusive conduct” will not be unwound by the regulator.
- Securities regulators will consider the decisions of other regulators involved in the transaction, including stock exchanges, and acquirors should consider all avenues of recourse against defensive tactics.
- Technical breaches of disclosure requirements will only hinder an auction if intervention to correct them causes less harm than the breaches themselves.

Please contact any member of our Corporate Securities Group to discuss defensive tactics, take-over bids or other matters relating to public M&A generally.