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M&A drug wars

By Neill May

With the rapidly growing capitalization of publicly traded marijuana industry companies and the pace of consolidation in that space, a litigated M&A dispute between industry participants was fairly foreseeable, not just because of simple probabilities but because pot stocks likely get the munchies just like their customers, and competing pot companies are likely more satisfying for them to consume than Doritos. The temptation to make pot jokes about these matters is almost irresistible, but I will try to keep to the "high" road (see what I did there?).

The dispute that resulted from the unsolicited bid by Aurora Canada Inc. for CanniMed Therapeutics Inc. (which ultimately resulted in a consensual deal) was, therefore, in a general sense, predictable. The clash was also much watched as the first "poison pill" decision by Canadian securities regulators in the wake of the significant reforms to the rules governing takeover bids in 2016 and a high-profile test of some core elements of the new rules.

Aurora had announced its proposal to acquire CanniMed in mid-November 2017. Three days later, CanniMed entered into an agreement to acquire Newstrike Resources Ltd. by way of a corporate arrangement that would be subject to approval by the shareholders of both companies at meetings scheduled to be held in January 2018. Shortly afterward, Aurora formally commenced its takeover bid for Aurora, conditional on (among other things) not proceeding with the Newstrike deal. Holders of approximately 38 per cent of CanniMed's shares signed lockups committing to tender to the Aurora bid (even if a richer bid were made). CanniMed adopted a shareholder rights plan (or poison pill) that prevented Aurora from locking up any other shareholders (because any further commitments from its shareholders to Aurora would make the task of overcoming Aurora's committed support even more difficult or impossible).

Four issues came before the securities regulators (in this case, the Ontario Securities Commission and the Financial and Consumer Affairs Authority of Saskatchewan) at a joint hearing.

A key issue concerned CanniMed's shareholder rights plan. Prior to the takeover bid rule changes, issuers targeted by unsolicited bids had made frequent use of such plans to extend the time available to respond. A central element of the rule changes was to extend the old 35-day minimum bid period to 105 days, longer than regulators had historically tended to permit poison pills to endure. The (previously untested) widespread expectation was that regulators would have less tolerance for poison pills adopted in the face of hostile bids with the mandated longer bid period. The regulators fulfilled that expectation (and continued their traditional approach of not tolerating rights plans where the intention was simply to align the timing of competing deals) by cease trading CanniMed's plan. The regulators have not at the time of this writing released reasons; there will be much focus on the regulators' thinking about the use of a pill to prevent lockups in the course of a bid that might decide or profoundly influence the outcome.

Aurora also sought an order shortening the 105-day minimum period for its bid to 35 (so that it would expire at about the same time as the shareholder votes on the Newstrike deal). Aurora argued that the Newstrike deal was effectively similar to an "alternative transaction" (an acquisition transaction that is not a bid and which can, therefore, be completed more quickly), which allows a bidder to use a 35-day period. The regulators disagreed. On the other side, CanniMed also sought a tweak to the rules, asking the regulators to deny Aurora the right to buy up to five per cent of CanniMed's shares during the bid (which again, when combined with the locked-up shares, would have heightened the hurdle for CanniMed to resist the Aurora bid). The regulators refused to shorten the bid period and also declined to deny Aurora the five-per-cent purchase right, which may signal a regulatory bias to just let the new rules operate as written.

The most prurient aspect of the dispute concerned the allegations by CanniMed's special committee that the locked-up shareholders had been heavily involved with Aurora and others in orchestrating and facilitating the Aurora bid, such that the locked-up holders should be considered "joint actors" (this characterization would have significant disclosure implications and make the bid more difficult by excluding those shares from the 50-per-cent minimum tender condition and from any minority approval of a subsequent acquisition transaction). On this point, the regulators did not disclose their conclusion but ordered additional disclosure, which may have shed additional light on the process and relationships.

The regulators' unreleased reasons are anxiously awaited. Maybe the marijuana issuers have something to improve patience. The guidance in the reasons will be closely scrutinized as this initial marijuana dispute may have been a gateway deal to future harder contested deals. **CL**

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