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Weed Wars Part III: The Joint Actor Issue

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In the recently released joint reasons of the Ontario and Saskatchewan securities commissions in *In the Matter of Aurora Cannabis Inc.* in respect of the unsolicited takeover bid by Aurora Cannabis Inc. for all the shares of CanniMed Therapeutics Inc., the commissions considered when a bidder and target company shareholders might be considered "joint actors." Read our previous communications on this case from January 3 and March 20.[1]

Background

At the hearing, CanniMed argued that four of its shareholders (collectively, the Locked-Up Shareholders) who had signed "hard" lock-up agreements with Aurora committing them to tender their shares to the Aurora offer should be considered to be acting jointly or in concert with Aurora in respect of the bid. As evidence of a joint actor relationship, CanniMed pointed to the terms of the hard lock-up agreements, which committed the Locked-Up Shareholders to vote against other acquisition proposals or actions that might frustrate Aurora's bid and to vote against CanniMed's proposed acquisition of Newstrike Resources Ltd. CanniMed also argued that because the Locked-Up Shareholders approached Aurora to solicit the bid and conveyed to Aurora material non-public information (including the fact that CanniMed was contemplating an acquisition of an unspecified cannabis company and key details relating to the status of negotiations and the timing of the CanniMed board's deliberations), the Locked-Up Shareholders became active participants in assisting Aurora in planning its bid and were therefore joint actors. The Locked-Up Shareholders had access to this information because three of them had representatives on the CanniMed board.

The finding of a joint actor relationship would have had significant negative consequences for the bidder, among them the exclusion of the locked-up shares in determining whether Aurora satisfied the statutory 50% minimum tender condition, and the recharacterization of Aurora's bid as an insider bid subject to the valuation and other requirements of Multilateral Instrument 61-101, *Protection of Minority Security Holders in Special Transactions*.

Commissions Decline to Deem Locked-Up Shareholders as Joint Actors

Peculiarly for such a fact-dependent inquiry, no one called the Locked-Up Shareholders as witnesses. So, as the securities commissions noted, the evidentiary record with respect to the interaction between the Locked-Up Shareholders and Aurora was limited. On the basis of this limited record, the securities commissions held that a joint actor relationship was not established. As discussed below, the reasons of the securities commissions centred on the effects of the lock-up agreements and the conduct of the Locked-Up Shareholders and Aurora.

Lock-Up Agreements

The takeover bid rules state that an agreement or understanding to tender securities to a bid does not, in and of itself, lead to a determination of acting jointly or in concert. The statute does not distinguish between hard and soft lock-ups, and the mere fact that the commitment to tender is "hard" did not allow the commissions to conclude that the Locked-Up Shareholders are joint actors with the bidder.

The securities commissions considered the effect of the presumption that persons who intend to exercise voting power together by virtue of an agreement, commitment or understanding are joint actors and concluded that the presumption can be rebutted when voting rights are tailored to be consistent with, and otherwise support, permissible commitments to tender securities to a bid. On these facts, the securities commissions noted that the effect of the lock-up agreements would have been substantially "watered down" if the Locked-Up

Shareholders were able to vote in favour of the Newstrike transaction and "thwart" the Aurora offer. Moreover, the lock-up agreements did not extend to requiring the Locked-Up Shareholders to vote in accordance with Aurora's instructions or transfer voting entitlements to Aurora.

Underlying this analysis is the view of the securities commissions that lock-up agreements are well-established in mergers and acquisitions practice and assist in improving deal certainty for a bidder and facilitating value-enhancing transactions. This rationale is especially applicable in the context of the 105-day bid period and 50% minimum tender condition under the takeover bid rules, where the potential of an interloping bidder can be high. According to the reasons, there is nothing objectionable in a shareholder seeking to enhance its liquidity in an investment and obtain a higher price for its securities through entering into a lock-up agreement.

Conduct of the Locked-Up Shareholders and Aurora

The securities commissions were clearly more concerned with the conduct of the Locked-Up Shareholders in conveying material non-public information to Aurora, information that was "extremely valuable" to Aurora in formulating its bid. However, this behaviour was not sufficient to ground a finding by the securities commissions of joint actor status, since the Locked-Up Shareholders were all sellers acting in their own financial interests to maximize the value and liquidity of their investments while Aurora was the only potential buyer in the transaction. As the securities commissions point out, Aurora and the Locked-Up Shareholders remained "on fundamentally different sides of the transaction" and the Locked-Up Shareholders' transfer of material non-public information to Aurora (while raising other concerns) was not inconsistent with the Locked-Up Shareholders' desire to see the Aurora offer succeed, given their self-interest as sellers. It was no doubt also a significant fact to the securities commissions that Aurora did not use the information to make toehold purchases.

Two Clear Takeaways

- It is difficult to envision situations in which shareholders who enter into hard lock-up agreements with a hostile bidder, without more, will be deemed to have a joint actor relationship.
- Voting provisions in lock-up agreements will not lead to a joint actor finding if the voting provisions are consistent with the permissible objectives of a selling shareholder – namely, price, liquidity and success of the bid.

Leaving the Door Open

Although the securities commissions did not find that the facts of this case gave rise to a joint actor relationship, the reasons assist in demarcating the boundary between parties on opposite sides of a transaction and shareholders and bidders coordinating to bring about a planned result. The reasons leave the door open for a different outcome in a number of scenarios. For example:

- **Content of Information.** The securities commissions left open the possibility that the transfer of material non-public information could support a joint actor finding. If such a transfer is "clear and extensive, it could suggest a level of cooperation that would mean that the shareholders are 'under the tent' with the bidder and are participating in the planning of the bid beyond appropriately seeking to maximize the price and liquidity of their shares."
- **Competing Bids.** Equally important as the content of material non-public information that is conveyed are the circumstances of its transfer. If tipping a bidder provides the bidder with a timing advantage when there are two or more competing bids or prevents an auction process from being feasible or otherwise denies shareholders a choice among alternatives, the securities commissions will be significantly more likely to grant remedies to level the playing field.
- **Special Benefits.** Evidence of any benefits to the Locked-Up Shareholders beyond increased price and liquidity that create a misalignment of interests between the Locked-Up Shareholders and the other shareholders may be relevant to a joint actor determination (in addition, of course, to being relevant to a "collateral benefit" analysis under MI 61-101). This represents a new consideration in the joint actor analysis, and it will be interesting to see how it is applied in future decisions.

- **Impact of Lock-Ups.** Despite endorsing lock-up agreements as an established part of mergers and acquisitions practice, the securities commissions reserved the right in future cases to apply its public interest jurisdiction to the terms of lock-up agreements or the context in which they are used. It therefore remains an open question whether lock-up agreements with off-market or unusually onerous provisions or which effectively transfer voting entitlements to the bidder could be used to support a joint actor finding.

[1] See Davies bulletin dated January 3, 2018, titled *Weed Wars: Securities Commissions Weigh In on Aurora/CanniMed Hostile Bid* and Davies bulletin dated March 20, 2018, titled *Weed Wars Part II: Tactical Poison Pills and Lock-up Agreements in Hostile Bids*.

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