Canadian Mergers and Acquisitions: Public M&A FAQs

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Blakes Means Business

Contents

01	Who regulates trading in securities in Canada?	03
02	How are Canadian public issuers typically acquired?	03
03	We're considering investing in a Canadian public issuer. At what stage would we have to publicly disclose our investment?	05
04	We're considering increasing our stake in a Canadian public issuer. At what stage would we have to make a public takeover bid?	05
05	What can we do to avoid triggering the takeover bid requirements?	05
06	If we approach a Canadian public issuer about a possible M&A transaction, when would that transaction need to be publicly disclosed?	06
07	Should we expect the target board to insist on an auction?	06
08	Are there special protections under Canadian securities laws for minority shareholders in Canadian M&A transactions?	06
09	Are defences to unsolicited takeover bids available to target boards?	07
10	Can a significant securityholder enter into an agreement to vote in favour of our plan of arrangement or tender to our bid? Can we offer any inducements to vote or tender?	08
11	When a friendly deal has been negotiated, what deal protection measures are commonly used in Canada?	08
12	What types of M&A transactions are subject to Canada's antitrust law?	09
13	If the transaction is subject to Canada's antitrust law review, what is the test for challenging the transaction?	10
14	Does Canada have rules restricting M&A transactions by non-Canadians?	10

Frequently asked questions about Canadian Public M&A

1. Who regulates trading in securities in Canada?

Trading in securities, including in M&A transactions, is largely regulated through securities legislation enacted by the individual provinces and territories. Each provincial or territorial securities act creates and empowers a provincial or territorial securities regulator to enforce such laws. These regulators have enacted a number of national, multilateral and local rules and policies that, among other things, seek to harmonize the application of certain aspects of securities laws across the country, including in relation to M&A transactions. In addition, companies whose securities are listed for trading on a stock exchange in Canada are subject to rules imposed by that stock exchange.

2. How are Canadian public issuers typically acquired?

Canadian public companies are typically acquired by way of either a plan of arrangement or takeover bid. A plan of arrangement is akin to a U.S. merger transaction with the addition of court supervision. "Friendly" M&A transactions are usually structured as plans of arrangement. While takeover bids can be carried out on a friendly basis with the target's support, they are principally used for unsupported or "hostile" transactions.

Plan of Arrangement

A plan of arrangement is a shareholder- and court-approved transaction governed by the target's corporate legislation. An arrangement practically requires the target's involvement and support but is subject to a less prescriptive regulatory regime than a takeover bid. Public company acquisitions supported by the target are most often effected via a plan of arrangement instead of a takeover bid.

The parties to a plan of arrangement generally enter into a definitive transaction document known as an "arrangement agreement," setting out the basis for the combination that is followed by an application to a provincial or territorial court for approval of the process for completing the transaction. The court order will require the calling of a target shareholders' meeting (typically held 45 to 90 days after an arrangement agreement is entered into), specify the approval threshold (typically two-thirds of the votes cast at the meeting) and provide for the grant of dissent rights to target shareholders. A meeting circular providing information regarding the transaction will then be sent to the target's shareholders. Where the offered consideration includes securities of the offeror, the circular must contain prospectus-level disclosure regarding the offeror's business and financial results. The meeting circular is not subject to any regulatory pre-clearance review.

Arrangements have more advantages than takeover bids. Most significantly, a plan of arrangement provides for the acquisition of 100% of the target's shares in a single step without the need for a second-step transaction and can facilitate dealing with multiple classes of securities (particularly convertible instruments) as part of the transaction. Also, if securities of the offeror are to be offered to U.S. shareholders of the target, it provides an exemption under U.S. securities laws from the requirement to register such securities.

Takeover Bid

Unlike plans of arrangement, takeover bids may be made with or without the agreement of the target. If the bid is successful, a "second-step" transaction is required to acquire 100% of the target shares (dissent rights would also be applicable).

Canadian securities legislation contains detailed procedural and substantive requirements applicable to non-exempt takeover bids governing certain elements of the bid, such as required disclosure, timing, conditionality, share purchases outside the bid and rules applicable to deposit, withdrawal, and take-up. The offeror must prepare a takeover bid circular that sets out prescribed information about the offer and the parties. This includes securityholdings and past dealings by the offeror and related parties in securities of the target, the nature of any financing relating to the bid, and prospectus-level disclosure regarding the offeror if the bid consideration includes offeror securities. Unlike a meeting circular for an arrangement, a takeover bid circular delivered to securityholders in Quebec must also be prepared in French. In addition, the target issuer's board of directors must also deliver a circular with its recommendation to target securityholders in response to the bid.

The takeover bid rules have been harmonized across Canada and, among other things, provide target boards with considerable time and discretion when responding to a takeover bid. A bid must remain open for at least 105 days unless the target board waives that minimum in favour of a shorter period (not less than 35 days) or unless the target enters into certain alternative transactions in response to the bid (in which case the period moves to 35 days).

3. We're considering investing in a Canadian public issuer. At what stage would we have to publicly disclose our investment?

There are two regimes that require disclosure of a holding in a Canadian public issuer: early warning reporting and insider reporting.

Under the early warning regime, the acquisition of or ability to exercise control or direction over 10% or more of a Canadian public issuer's voting or equity securities must be promptly publicly disclosed via press release and regulatory filing. Subsequent acquisitions or dispositions above the 10% threshold of 2% or more of the voting or equity securities must also be disclosed, including when ownership levels fall below the 10% reporting threshold. However, once below the 10% threshold, subsequent disclosure is required only where an acquisition again results in securityholdings at or above the 10% threshold. Notably, the early warning disclosure threshold is reduced to 5% for as long as a takeover bid or issuer bid is outstanding. Eligible institutional investors can avail themselves of an alternative reporting regime in which reporting is made at the end of the month when a change occurs.

In addition, upon acquiring or obtaining control or direction of 10% or more of the voting securities of a Canadian public issuer, the offeror becomes an "insider" of that issuer. As a result, the offeror must report in a publicly searchable database any of the issuer's securities it holds or subsequently trades.

Offerors must also be aware of Canadian "pre-bid integration rules," designed to ensure all of a target's securityholders are treated equally in the context of a takeover bid. The rules integrate an offeror's pre-bid purchases (other than qualifying purchases made over a stock exchange) by requiring, among other things, that consideration offered under any subsequent formal bid by the offeror be at least equal to and in the same form (e.g., cash) as the consideration paid in any such purchases made within the 90 days preceding the formal bid.

4. We're considering increasing our stake in a Canadian public issuer. At what stage would we have to make a public takeover bid?

Any offer to acquire outstanding voting or equity securities made to anyone in Canada that would result in the offeror holding 20% or more of the voting or equity securities of any class of a Canadian public issuer will constitute a takeover bid for Canadian securities law purposes. As a result, unless an exemption from the formal takeover bid requirements is applicable, the offer would be required to be made to all securityholders of the class in Canada on the same terms and conditions.

5. What can we do to avoid triggering the takeover bid requirements?

Exemptions from the takeover bid rules are available in certain circumstances. One of the most commonly used exemptions is the "private agreement" exemption, under which purchases may be made by way of private agreements with five or fewer vendors without complying with the requirement to make an offer to all securityholders of the class). Canadian laws exempt such purchases only if the purchase price (including brokerage fees and commissions) does not exceed 115% of the market price of the securities.

6. If we approach a Canadian public issuer about a possible M&A transaction, when would that transaction need to be publicly disclosed?

Canadian public issuers are required to promptly disclose any “material changes” in their affairs. Material changes are changes in an issuer’s business, operations or capital that would reasonably be expected to have a significant effect on the market price or value of any of its securities. This concept includes a decision by either the issuer’s board to implement such a change or senior management if they believe that approval of the board is probable.

Preliminary discussions and conditional proposals where material terms have not been agreed to are not generally viewed as disclosable. In most cases, public issuers do not announce a transaction until a definitive agreement regarding the transaction has been entered into. However, any determination of the existence of a material change is highly fact-specific and needs to be carefully considered in the context of a specific transaction.

7. Should we expect the target board to insist on an auction?

The board of a target company is not required to hold an auction before entering into an agreement for the sale of the company and often will enter into such agreements without an auction. However, a target board may determine that conducting an auction or a more limited market check before entering into an M&A transaction is in the corporation’s best interests and proceed on that basis.

8. Are there special protections under Canadian securities laws for minority shareholders in Canadian M&A transactions?

In addition to certain remedies available to minority target shareholders under Canadian corporate laws, securities regulators in some Canadian jurisdictions have adopted specific protections for minority target securityholders in certain categories of M&A transactions that can be abusive or unfair to minority shareholders, such as insider bids and related-party transactions. These protections include enhanced disclosure obligations. Subject to certain prescribed exemptions, they also include requirements to obtain a formal valuation of target shares (and any non-cash consideration to be provided) prepared by an independent valuator and a separate “majority of the minority” approval by target shareholders in shareholder-approved transactions such as arrangements. A subset of these categories of transactions that staff of the applicable securities regulators perceive as giving rise to material conflict of interest concerns are subject to enhanced regulatory scrutiny and expectations. This scrutiny includes staff review of such material conflict of interest transactions on a real-time basis to assess compliance. In addition, where a target board does obtain a fairness opinion for a material conflict of interest transaction, certain additional disclosure is expected by staff, including with respect to the financial advisor’s compensation arrangements. This applies even though the target board of directors and any special committee are responsible for determining whether a fairness opinion is necessary.

9. Are defences to unsolicited takeover bids available to target boards?

A target facing an unsolicited takeover bid has a number of options available to it in responding to the hostile bid. In fact, Canadian securities regulators have provided guidance that supports using defensive tactics in appropriate circumstances (e.g., when a target board takes over in a genuine attempt to obtain a better bid). That said, Canadian securities regulators believe that unrestricted auctions produce the most desirable results in change -of -control contests. They have also indicated that tactics that could deny or severely limit the target securityholders' ability to decide whether to accept an offer may result in regulatory action.

Poison Pills

Historically, one of the most common defensive tactics employed by Canadian target boards was a securityholders' rights plan (commonly known as a "poison pill"). Securities regulators did not generally allow a target's poison pill to remain operative indefinitely while it remained operative (typically for a period of approximately 60 days following the date of the takeover bid). However, a poison pill effectively prevented a bidder from acquiring any target shares under its bid without the target's approval. Before changes in 2016 to the bid regime that increased the minimum period during which a hostile bid must remain open from 35 to 105 days, poison pills were used to provide target boards additional time beyond the 35-day minimum period to respond to a hostile bid. The 2016 changes to the bid regime are generally seen as providing target boards sufficient time to identify and explore other value-maximizing alternatives. As such, poison pills have not played a meaningful role in Canada as a defensive tactic in response to hostile bids since 2016.

Private Placements

Another defensive tactic available to a target facing a hostile bid is a "tactical" private placement. As a result of the 2016 changes to the bid rules, a bidder is not permitted to acquire shares under a takeover bid unless more than 50% of all outstanding target shares (other than those held by the offeror and its joint actors) have been tendered to the bid. A significant private placement of target shares to a shareholder that is friendly to the target, particularly by an issuer with a low market capitalization, can reduce the likelihood that this minimum tender requirement will be satisfied.

Not surprisingly, private placements with material dilutive impact undertaken in the face of hostile bids have been subject to increased scrutiny by Canadian securities regulators. When reviewing such transactions, the regulators consider and balance competing factors, including the extent to which the private placement serves as the target's bona fide corporate objective and the principle of facilitating shareholder choice in an open and even-handed bidding process. When balancing these factors, the regulators will often afford significant deference to the business judgment of target boards. In other words, the mere fact that a substantial private placement is undertaken in the face of a hostile bid will not necessarily result in the securities regulators concluding that the placement is an impermissible defensive tactic.

10. Can a significant securityholder enter into an agreement to vote in favour of our plan of arrangement or tender to our bid? Can we offer any inducements to vote or tender?

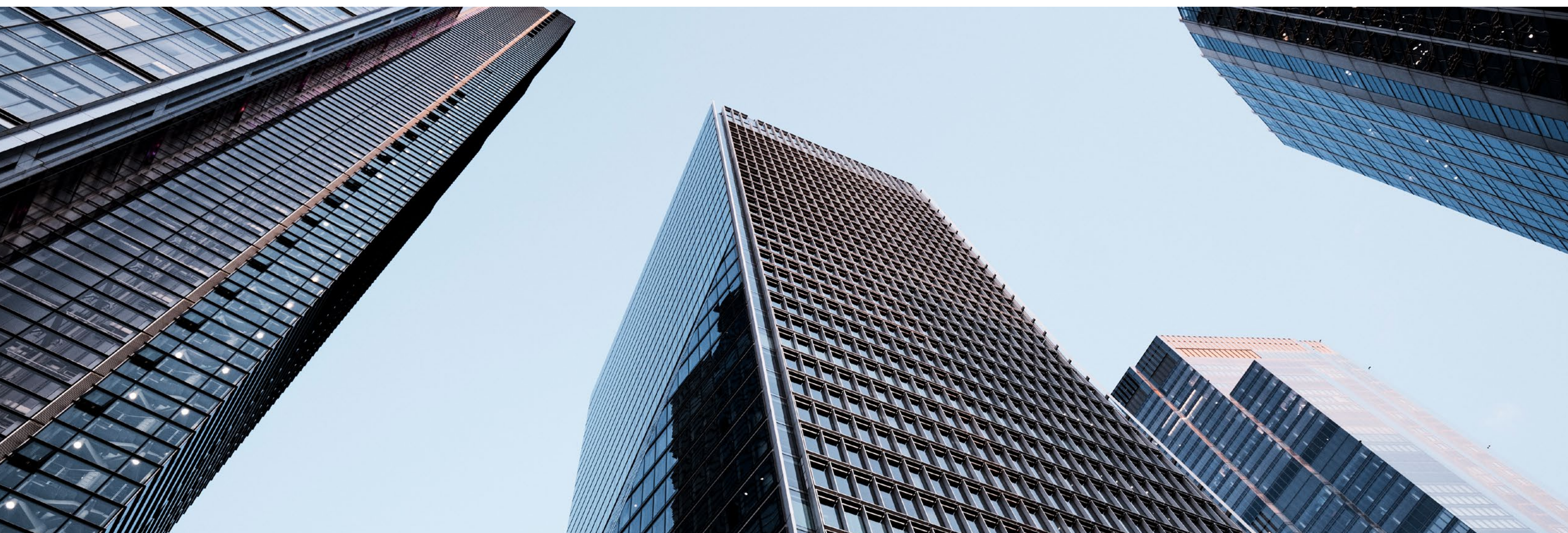
Offerors commonly enter into support agreements with significant target securityholders or target management and directors whereby such securityholders agree to support the transaction, including by voting in favour of a plan of arrangement or tendering to the offeror's takeover bid.

In considering support agreements in a takeover bid, Canadian securities laws provide that all holders of a target's securities must be offered identical consideration in that bid. Those holders must also prohibit an offeror from entering into a separate agreement that provides greater consideration to a securityholder for its securities than that offered to the other securityholders (subject to certain limited exceptions). Offering non-identical consideration can also introduce additional complexity in the context of a plan of arrangement and would need to be carefully considered in the context of a specific transaction before extending any such offers.

11. When a friendly deal has been negotiated, what deal protection measures are commonly used in Canada?

In a public M&A transaction in Canada, a target will generally have the right to terminate the transaction if it receives a financially superior proposal to the agreed-upon transaction. There are several deal -protection measures commonly used by buyers to reduce the likelihood that the target will terminate the transaction in order to accept a superior proposal, including the following:

- **No shop.** Offerors typically obtain a "no-shop" covenant that prohibits the target board from soliciting or encouraging competing bids from other buyers.
- **Right to match.** The offeror is frequently granted an opportunity to match any superior proposal during a limited period after the target receives the superior proposal.
- **Break fees.** When break fees payable by a target to a buyer are in connection with the target's termination of the transaction with the buyer, those fees generally range between 2% to 5% of the target's equity value. Reciprocal or reverse break fees, pursuant to which an offeror is obligated to pay a fee to the target if the transaction fails for specified reasons, are common in Canada, including in mergers of equals, transactions with significant regulatory issues or sponsor-backed deals.



12. What types of M&A transactions are subject to Canada's antitrust law?

Canada's antitrust law is set out in the *Competition Act*, which is administered and enforced by the Competition Bureau and led by the Commissioner of Competition (Commissioner). Two parts of the *Competition Act* apply to M&A transactions: the pre-merger notification provisions, which apply to all transactions, and the substantive merger review provisions, which apply to transactions exceeding certain thresholds.

Because all M&A transactions are subject to the *Competition Act*, parties to a transaction must plan early to determine whether competition concerns are raised in order to consider matters such as risk allocation and closing conditions. Completing a transaction that is subject to pre-merger notification is a criminal offence unless the applicable statutory waiting period has expired, been waived or terminated early.

A transaction is notifiable if the target has an operating business in Canada and each of the following tests for pre-merger notification is exceeded:

- **Size of parties test.** The parties to the transaction, together with their affiliates, have aggregate assets in Canada with a book value or aggregate gross revenues from sales in, from or into Canada in excess of C$400-million.
- **Size of transaction test.** The target and its subsidiaries' aggregate value of the assets in Canada or aggregate gross revenues from sales in, from or into Canada generated from the assets in Canada (or, in the case of an asset transaction, from the assets being acquired) exceeds C$93-million (2024). Notably, a separate test applies to an amalgamation, and the target must own or control an operating business in Canada. In an asset transaction, the assets being acquired must be from an operating business.
- **Equity interest test.** The transaction would result in the offeror having more than 20% of the voting shares of a public target (35% in the case of a private entity). This would apply if the offeror already holds in excess of such applicable ownership threshold at launch (but less than a majority), then the threshold is whether the contemplated acquisition would result in the offeror having more than 50% of the target's voting shares.

Where a transaction is notifiable and the parties file a formal notification, a waiting period commences and runs for an initial 30 days. At the end of the waiting period, the parties are legally entitled to close their transaction, even if the Commissioner's review is ongoing, unless the Commissioner issues a supplementary information request (SIR) to the parties. A SIR is similar to a second request under the U.S. *Hart-Scott-Rodino Antitrust Improvements Act*, 1976. If a SIR is issued, the parties cannot lawfully close their transaction until 30 days after the day on which both parties have complied with the SIR. A SIR is issued in relatively rare cases involving significant competitive overlap between the parties (approximately 10% of notified transactions). There are special provisions for unsolicited offers and filing requirement, designed to prevent a target from delaying the start of the waiting period by having the waiting period start upon receipt of the offeror's provision of information, rather than both parties.

While the parties to a notifiable transaction are generally free to complete their transaction following the expiry of the statutory waiting period, the Commissioner's review can, and often, takes longer than the statutory waiting period. The Commissioner has the statutory right to review and challenge any M&A transaction within one year after closing unless an advance ruling certificate is issued. Alternatively, the Commissioner may issue a "no-action" letter, indicating that he does not intend to challenge the M&A transaction at that time but retains the right to challenge the transaction at any time before or within one year following its substantial completion. As a practical matter, however, we are not aware of any situation in which the Commissioner has challenged a transaction post-closing after issuing an unqualified no-action letter.

13. If the transaction is subject to Canada's antitrust law review, what is the test for challenging the transaction?

Whether an M&A transaction is subject to notification or not, the test applicable to any transaction is whether it prevents or lessens or is likely to prevent or lessen competition substantially. The analysis has historically taken place in the context of a relevant market that is defined based on product and geographic dimensions. The *Competition Act* provides a non-exhaustive list of factors that may be considered when assessing the competitive impact of an M&A transaction.

14. Does Canada have rules restricting M&A transactions by non-Canadians?

A non-Canadian that directly acquires control of a Canadian business and exceeds the applicable review threshold cannot complete the acquisition until the responsible minister under the *Investment Canada Act* has reviewed the investment and declared or is deemed to have declared that the investment is likely to be of net benefit to Canada. An acquisition of more than 50% of the voting securities of a corporation or non-corporate entity is deemed to be an acquisition of control. The acquisition of one-third to one-half of the voting securities of a corporation creates a rebuttable presumption that control has been acquired. In contrast, subject to certain exceptions, the acquisition of less than one-third of the votes of a corporation or less than a majority of the votes of a non-corporate entity is deemed not to constitute an acquisition of control for these purposes.

Notwithstanding the above, the *Investment Canada Act* provides that the responsible minister under the act can determine that control will be or has been acquired, even below the previously noted thresholds, in the following circumstances:

- The acquisition of a Canadian cultural business (as such term is defined)
- The acquisition by a state-owned enterprise (SOE) (as such term is defined)
- Where the acquisition could be injurious to Canada's national security

If control of a non-cultural Canadian business is directly acquired by an investor ultimately controlled in a World Trade Organization (WTO) member country, the acquisition is subject to review. This applies where the Canadian business, along with any businesses it controls, has (1) for non-SOE investors, an enterprise value of C$1.326 -billion (2024) or more, or (2) for SOE investors, a book value of C$528 -million (2024) or greater. For non-WTO investor transactions, or where the Canadian business qualifies as a cultural business, the review threshold is exceeded where the Canadian business has a book value of assets of C$5-million or more.

Other than cultural businesses, if the Canadian business is being acquired indirectly, and the WTO investor rule is met, or if the applicable review threshold is not exceeded, the transaction is subject only to a post-closing notice requirement.

Reviewable transactions require the approval of the responsible minister. The initial waiting period is up to 45 days after the investor submits an application for net benefit review. The minister can unilaterally extend this period by 30 days and, thereafter, only with the consent of the responsible minister and investor.

All investments involving a Canadian entity, whether or not the investment is direct or indirect and whether or not control will be acquired, are subject to possible review on grounds of whether an investment is likely to be injurious to national security. There are broad powers under the national security provisions of the *Investment Canada Act* to direct parties not to implement an investment or implement it with conditions. Where a review occurs after closing, such powers include the right to require the divestiture of control or impose terms and conditions on the investment.

In addition to the *Investment Canada Act*, other federal statutes regulate and restrict foreign investment, particularly in industries and sectors such as transportation, telecommunications, broadcasting, newspapers and financial institutions.