# The Mergers & Acquisitions Review

Fourteenth Edition

**Editor**
Mark Zerdin

The Law Reviews

# THE MERGERS & ACQUISITIONS REVIEW

FOURTEENTH EDITION

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This article was first published in January 2021
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Published in the United Kingdom
by Law Business Research Ltd, London
Meridian House, 34–35 Farringdon Street, London, EC4A 4HL, UK
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Enquiries concerning reproduction should be sent to Law Business Research, at the address above.
Enquiries concerning editorial content should be directed
to the Publisher – tom.barnes@lbresearch.com

ISBN 978-1-83862-480-4

Printed in Great Britain by
Encompass Print Solutions, Derbyshire
Tel: 0844 2480 112

# ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following for their assistance throughout the preparation of this book:

AABØ-EVENSEN & CO ADVOKATFIRMA

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# PREFACE

While the previous edition of *The Mergers & Acquisitions Review* highlighted some causes for optimism for growth in the M&A market, the resilience of companies has been severely tested in 2020 in light of the covid-19 pandemic. Political uncertainty and economic shifts have taken a back seat to the wide-reaching global effects of the pandemic, which are leaving many jurisdictions and sectors in dire straits.

The figures for the first half of 2020 reflect this, as global deal value fell by 53 per cent and deal volume by 32 per cent (compared with the first half of 2019), while megadeals (over US$10 billion) were down by 48 per cent.[1] The global deal value figure is the lowest half-yearly total since the first half of 2010. The priority for many businesses in the wake of the crisis has been to conserve cash and protect their revenue streams rather than seeking to invest in M&A.

The Americas saw the largest fall in share of global M&A, as its value fell to 33.4 per cent from 52.8 per cent in 2019.[2] The US is facing not only political uncertainty with the upcoming presidential election and protests across the country, but also a sharp decline in economic productivity due to the lockdown enforced by the covid-19 crisis. M&A deal activity in the US fell to lower levels than the 2008 global financial crisis, with higher value deals particularly affected. Despite the bleak figures for the first half of 2020, though, there are signs that some sectors, notably the technology sector, are rebounding. This is perhaps unsurprising as the future of many industries will depend on technology services.

European M&A saw its lowest quarterly value since 2009 in the second quarter of 2020 of just US$83.6 billion. There was also a drop of 30.6 per cent in the value of European M&A in the first half of 2020 when compared with the figures in the first half of 2019. With economies beginning to open up towards the end of the first half of 2020, there are early signs as to where the focus of M&A activity will likely be in the aftermath of the crisis. Private equity buyouts have accounted for almost 20 per cent of deals targeting Europe, up from 18.9 per cent in 2019.[3] In Europe, as in the Americas, the tech sector is continuing to attract interest and reached a total of US$27.8 billion across 477 deals in the first half of 2020. By contrast, the consumer sector has been severely impacted and has fallen to its lowest value since 2009.

Looking forward to the remainder of 2020 and beyond, there are some reasons to be optimistic that the global M&A market will show some signs of recovery. There has already

1 Mergermarket, 'Global & Regional M&A Report 1H20'.
2 ibid.
3 ibid.

been a resurgence since the first half of 2020, with the third quarter seeing 36 deals worth US$5 billion-plus, making it the busiest third quarter on record.[4] The challenges caused by restricted international travel, less physical diligence and almost no face-to-face meetings are, for the most part, being surmounted. It is also anticipated that private equity funds will begin to put their dry powder to use as further clarity emerges on the duration and effects of the pandemic.

I would like to thank the contributors for their support in producing the 14th edition of *The Mergers & Acquisitions Review*. I hope the commentary in the following 42 chapters will provide a richer understanding of the shape of the global markets, and the challenges and opportunities facing market participants.

**Mark Zerdin**
Slaughter and May
London
December 2020

4 *Financial Times*, 'Dealmaking rebound drives busiest summer for M&A on record'.

**Chapter 10**

# CANADA

*Cameron Belsher, Robert Hansen, Robert Richardson, Debbie Salzberger and Mark McEwan*[1]

## I OVERVIEW OF M&A ACTIVITY

Canada saw 650 M&A deals announced in 2019 valued at US$112.6 billion overall.[2] These results represent the highest aggregate deal value since 2014 with an increase of 30 per cent on 2018 figures when 650 deals worth US$86.6 billion were announced.[3] For the first half of 2020, M&A activity in Canada was highly impacted by the covid-19 pandemic. M&A activity fell, with the number of deals, in first half of 2020, decreasing to 206 from 352 from the same period in 2019, and aggregate deal value decreasing from US$44.26 billion in 2019 to US$16.3 billion in 2020.[4]

The most active sectors by deal count in 2019 were, for a second year in a row, the technology, media and telecom industries with 119 deals announced during the year for US$9 billion.[5] Energy, mining and oil & gas were close behind, with 115 announced deals and for a market-leading US$40.7 billion or 36 per cent share of the total value.[6] Mining was the most active sector by deal value with US$23.6 billion,[7] with Newcrest Mining's acquisition of 70 per cent JV interest in the Red Chris copper and gold mine in British Columbia, Zijin Mining Group's acquisition of Continental Gold Inc and Evolution Mining's acquisition of the Red Lake gold complex from Newmont among the highlights. The 106 announced deals in industrials, manufacturing and engineering industries had an aggregate value of US$4.7 billion,[8] making it the second most active sector in 2019.

The Canadian private equity market continues to be a key driver of M&A activity, and enjoyed a record year by deal value. Aggregate deal value was C$62 billion, which was above 2018's high of C$57 billion, while deal volume experienced a modest dip to 356 from 381 in 2018.[9] Funds continue to fundraise actively, building on ever-increasing dry powder, and the market across Canada remains highly competitive, attracting interest from domestic and international investors. In 2019, the activity level in the healthcare and B2B sectors continued its positive trend while the materials & resources and energy sectors experienced

1 Cameron Belsher, Robert Hansen, Robert Richardson and Debbie Salzberger are partners and Mark McEwan is an associate at McCarthy Tétrault LLP.
2 Mergermarket, Deal Drivers Americas FY 2019.
3 Mergermarket, Deal Drivers Americas FY 2019.
4 Mergermarket, Deal Drivers Americas H1 2020.
5 Mergermarket, Deal Drivers Americas FY 2019.
6 Mergermarket, Deal Drivers Americas FY 2019.
7 Mergermarket, Deal Drivers Americas FY 2019.
8 Mergermarket, Deal Drivers Americas FY 2019.
9 Pitchbook Data, Inc.

a challenging year. The financial services sector saw a tightening of activity, while the IT and B2C sectors remained essentially flat. Both the deal value and the number of Canadian private equity exits were significantly down in 2019. Firms exited 69 companies for a total value of C$24 billion, representing a year-over-year decrease of 34 per cent and 30.3 per cent, respectively.[10]

## II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

### i Alternative transaction structures

In contrast to private M&A transactions in Canada, which are negotiated contractual arrangements set against a similar legal framework to the United States, public M&A transactions in Canada are subject to complex securities and corporate law regimes. Accordingly, Canadian dealmakers generally pursue one of two common methods to acquire control of a public company: a takeover bid or a plan of arrangement.

#### *Takeover bids*

A takeover bid is an offer made to a person in Canada to acquire outstanding voting or equity securities of a class of securities, which, if accepted, would result in the bidder (together with persons acting in concert with the bidder) owning 20 per cent or more of such class. Most commonly, a bidder will make an offer to all of the shareholders of a target company to buy their shares. Exactly the same offer must be made to all shareholders. This means that, subject to certain limited exceptions, it is not permissible to have collateral agreements with, for example, a controlling shareholder or a shareholder who is a senior officer that result in additional consideration flowing to that shareholder. The offer must remain open for shareholders to accept for at least 105 days (referred to as the bid period), subject to a target board's ability to reduce the bid period to not less than 35 days in prescribed circumstances.

Any takeover bid must be subject to a non-waivable condition that a minimum of more than 50 per cent of all outstanding target shares owned or held by persons other than the bidder and its joint actors be tendered and not withdrawn before the bidder can take up any shares under the takeover bid. The takeover bid must also be extended by the bidder for at least an additional 10 days after the bidder achieves the minimum tender condition and all other terms and conditions of the bid have been complied with or waived.

Certain takeover bids are, however, exempt from compliance with these requirements, including transactions involving the acquisition of securities from not more than five shareholders of the target company, provided that the price paid does not exceed 115 per cent of the prevailing market price (referred to as the private agreement exemption).

If the bidder succeeds in acquiring at least 90 per cent of the target's shares owned by third parties within 120 days of the commencement of the bid, then the bidder is typically able to effect a compulsory acquisition of the remaining outstanding shares pursuant to a process governed by Canadian corporate statutes. This process can take approximately 30 days, although timelines vary depending on the jurisdiction of incorporation of the target company. Alternatively, if the bidder acquires more than two-thirds of the outstanding shares, the bidder may call a meeting of all of the shareholders of the target company for the purposes of voting on an amalgamation with an affiliate of the bidder. This vote can be generally be

10 Pitchbook Data, Inc.

carried with two-thirds of the outstanding shares, and if approved can result in any remaining minority shareholders being squeezed out for the same consideration that was offered in the takeover bid. This second-step transaction takes longer than a compulsory acquisition because of the need to call a meeting of the shareholders of the target company.

***Plans of arrangement***

Most consensual acquisitions of Canadian public companies, however, are effected not by way of a takeover bid but through a statutory procedure under the target company's corporate statutes. These statutes generally provide that companies can be merged, and their outstanding securities can be exchanged, amended or reorganised through a court-supervised process known as a plan of arrangement. Under this process, the target applies for an initial court order directing the target to seek the approval of its shareholders and fixing certain related procedural requirements. A second court appearance will be scheduled for shortly after the shareholders' meeting for the court to consider the substantive fairness of a transaction, and at which any interested party may appear and object to the completion of the transaction. If shareholders vote to approve the transaction, typically by two-thirds of the votes cast at the meeting, and there are no meritorious objections from other interested parties, the court will approve and the transaction will proceed as intended. Plans of arrangement are often used to enable the shareholders of the target to exchange their shares for either cash or another form of consideration.

The plan of arrangement has two significant advantages in certain circumstances. One is that it allows for multiple transactions to happen simultaneously or in a specified sequence following shareholder and court approval. This is useful, for example, where there are multiple companies involved in the transaction, where several classes of equity and debt securities are outstanding, or where the sequencing of particular steps in the transaction is important to achieve an advantageous tax result. The other advantage to a plan of arrangement is that it will generally permit securities of the offeror to be issued to US holders of the target without requiring such securities to be registered in the US.

### ii Target board considerations

Under the Canada Business Corporations Act (and other Canadian corporate statutes are substantially the same in this regard), directors have a legal obligation to act honestly and in good faith with a view to the best interests of the corporation; and exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

In the context of a potential M&A transaction, Canadian boards typically seek to discharge these duties by overseeing a process relating to the sale of a company. It is not mandatory that Canadian public companies be sold by way of an auction, and many companies are sold pursuant to a process whereby the target negotiates confidentially with one third party and then issues a press release after a support agreement has been signed. It is customary for these support agreements to include 'fiduciary-out' termination provisions, similar to the practices in the US market. At this stage, the target company's board is recommending to its shareholders that they accept the transaction, but whether the bidder succeeds will depend upon the reaction of the shareholders. In the case of a takeover bid, the bidder will have to mail its takeover bid circular to target shareholders and its bid must be open for at least 35 days (provided the target company's board has agreed to reduce the bid period). In the case of a plan of arrangement, there is a period of approximately one month between the mailing of the target's management information circular and the date of its shareholders' meeting.

In either case, during that time, potential competing bidders may come forward and seek to make a superior proposal. Depending on the terms of the support agreement, there may be obstacles to another potential acquirer making a superior proposal, including the size of any break fee and whether there is a right to match in the support agreement. In addition, some target companies in Canada have signed support agreements with go shop provisions whereby the target puts the bidder on notice that it intends to actively solicit higher offers from third parties.

### iii Defensive measures

Any widely held public company with a depressed share price can be vulnerable to an unsolicited takeover bid. A target company will commonly react to a hostile takeover bid by initiating defensive measures. Although other potential responses may be available, two prominent defensive measures in Canada are shareholder rights plans and tactical private placements.

#### *Shareholder rights plans*

Until Canada's takeover bid rules were amended in 2016 to increase the minimum bid period from 35 days to 105 days, shareholder rights plans were frequently used to delay a hostile bidder so that the target board had more time to canvass alternatives. Unlike in the United States, they could not be used to stop a hostile bid indefinitely. Now that Canada has a 105-day minimum bid period (subject to two exceptions), the formerly accepted rationale for shareholder rights plans has diminished significantly.

Shareholder rights plans nevertheless remain a relevant tool for deterring creeping takeover bids. Any purchase in the market that takes a shareholder above 20 per cent ownership of a target company requires the bidder to make a formal takeover bid to all the target's shareholders on identical terms, subject to two key exceptions to the formal takeover bid rules. The first is a *de minimis* exemption that permits a shareholder to acquire shares in excess of the 20 per cent threshold through purchases of up to 5 per cent of the target's outstanding shares annually at market prices. The second is the private agreement exemption described above. Many Canadian public companies have shareholder rights plans that prohibit the use of these two exemptions to acquire control of a company without offering an appropriate premium to all shareholders, and to prevent the acquisition of a negative control block that could deter a bid that the target board and other shareholders would find desirable. A shareholder rights plan may also assist in deterring a hostile bidder from entering into hard lock-up agreements with shareholders or purchasing additional shares while its bid is outstanding.

#### *Tactical private placements*

There have been a small number of transactions in Canada in recent years where target companies have issued equity to friendly third parties at least in part to discourage hostile bids. Not only does the hostile bid become more expensive as a result, but the mandatory 50 per cent tender condition becomes harder to achieve.

Any private placement that impacts a hostile takeover bid may be challenged in court or before the securities regulators, or both. Relevant considerations in cases to date include:

*a* the timing of the private placement relative to a bid;

*b* whether the target required the financing;

*c* the impact of the private placement on the hostile bid or on a second bidder or locked-up shareholder; and

*d* whether the private placement was approved by shareholders.

### iv Financing

In Canada, unlike in the United States and some other jurisdictions, it is not permissible to make a takeover bid conditional on arranging financing. Before a bidder makes a cash takeover bid, it must have made adequate arrangements for its financing. Typically, the bidder will have signed a binding commitment letter with a bank or other source of funds prior to launching its takeover bid. The bidder will seek to have the conditions to the availability of its financing set out in the bank commitment letter as closely mirroring as possible the conditions in the takeover bid circular that is sent to the target company's shareholders. The law requires that the bidder must be confident that, if the conditions to the bid are satisfied, the financing will be available.

## III SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

### i Distressed transactions

The covid-19 pandemic has resulted in significant market disruption, including by creating perceived gaps between market prices and intrinsic values for public companies. This divergence can lead to significant challenges, as issuers may be reluctant to issue equity in disrupted markets and lenders may consider initiating creditor enforcement proceedings, but can also create opportunities for distressed transactions.

To that end, there are a variety of M&A processes available to acquire distressed Canadian companies. An insolvent company can look to the Companies' Creditors Arrangement Act (the CCAA) or the Bankruptcy and Insolvency Act (the BIA), both of which are federal statutes setting out insolvency processes that can help companies obtain protection from creditors and provide other restructuring tools. A solvent but distressed company can also avail itself of a plan of arrangement pursuant to either federal or provincial corporate statutes. Companies can also consider pursuing informal work-outs or soliciting a going-private transaction or a private placement investor.

#### *Plans of arrangement in distressed transactions*

As discussed above, most consensual acquisitions of Canadian public companies are effected by way a plan of arrangement. Plans of arrangement provide companies with the flexibility to undergo complex multistep transactions, potentially including:

*a* an exchange of securities of the company for money, new securities or property of company or a third party;

*b* a sale of all or substantially all of the assets of the company for money, securities or property of a third party;

*c* amendments to the company's articles of incorporation and share capital; and

*d* an amalgamation or going-private transaction.

Plan of arrangement proceedings can be useful in relation to distressed companies because they can be used to restructure a company's balance sheet, including by altering the share capital of the company through an issuance, exchange or cancellation of securities, including shares, warrants, bonds, and notes. A plan of arrangement can also result in an investor or

strategic partner making a major investment or acquiring all or a significant portion of the equity of the company. However, plans of arrangement are not typically used for operational restructurings or compromising bank credit facilities or trade debt.

Distressed companies remain in control of their operations throughout the plan of arrangement proceedings, subject to any negotiated covenants on the conduct of the business, and are in some circumstances able to obtain a stay of proceedings to preserve the status quo while pursuing a potential transaction. Companies are generally required to be solvent in order to avail themselves of plan of arrangement procedures, but this requirement has been interpreted broadly by courts.

***Formal insolvency proceedings***

A company that is not solvent, meaning that it cannot satisfy its obligations generally as they become due because or that the realisable value of its assets is not sufficient to satisfy its liabilities, can restructure under one of Canada's two main insolvency regimes: the CCAA and the BIA. Because of its flexibility, the CCAA is the most commonly used regime for larger companies or complicated restructurings. The CCAA applies only to debtor companies with more than $5 million in debt. Companies with less than $5 million in debt or more straightforward restructurings may use the proposal sections of the BIA.

The CCAA and the BIA provide companies with an array of tools to help them restructure their operations and finances. These tools, which may be ordered by the supervising court in appropriate cases, include familiar insolvency tools, like stays of proceedings, as well as structured proceedings for asset sales or transactions involving changes to a company's capital structure. For example, under the CCAA, courts have authority to approve transactions and sale processes, including:

*a* A sale of all or substantially all of a debtor's assets, either as a means to finance a restructuring or as a final, creditor-approved outcome of the court-supervised restructuring process. Such asset sales can in some cases proceed without having received the approval of shareholders, which is generally otherwise required by Canadian corporate statutes.

*b* The issuance of new shares to a buyer or investor, in exchange for cash, debt or equity securities of the buyer or investor, or a combination thereof, in some cases, without shareholder approval. In addition, cash and equity securities can also be distributed and offered to the company's creditors pursuant to the plan of arrangement, so long as the value provided to creditors through such distribution represents an improvement over the recovery that could be achieved through conventional liquidation proceedings.

Sale processes approved under the CCAA (often called a sale and investment solicitation process) facilitate obtaining court approval of transactions to be implemented at a later date, and have features that are similar to traditional M&A processes, including: a two phase process, minimum requirements for letters of intent and binding bids, and forms of key agreements, including confidentiality, purchase and sale, or investment agreements.

A transaction that receives approval under the CCAA can also yield certain advantages for buyers, as this approval can also provide for 'vesting order', which enables a transaction to occur free and clear of secured claims and other encumbrances, and may, among other things, permit the debtor company to assign contracts without counterparty consent.

To exit CCAA proceedings, each applicable category of creditors must approve the arrangement or proposal under a 'double majority', consisting of more than 50 per cent by

number of voting creditors representing at least two-thirds of the value of the claims of voting creditors. The classification of creditors can be an important factor. Courts generally weigh several factors when considering a proposed transaction, including: whether the process was reasonable in the circumstances; whether a court appointed monitor approved the process and believes that the outcome of the process is better than a liquidation in a bankruptcy scenario; the extent to which creditors were consulted and the effect of the sale on the creditors of the company; and whether the consideration is fair and reasonable.

### ii Private equity and pension funds

In Canada, domestic and international private equity firms and Canadian pension funds continued to have a major impact on both inbound and outbound transactions in 2019. Marquee transactions included Brookfield Infrastructure's and GIC's US$8.4 billion acquisition of Genesee & Wyoming, Cortland Partners' US$1.2 billion acquisition of Pure Multi-Family REIT and JP Morgan's acquisition of Billy Bishop Airport.

#### *Private equity exits: dual-track processes*

The parallel pursuit by equity sponsors of both an M&A exit and an initial public offering (IPO) is not a new development. Recent examples in Canada include GFL Environmental Inc opting for a sale to BC Partners in April 2018 over a go-public transaction, followed by their IPO in 2019 and the dual-track processes of Kinder Morgan Canada Limited and Neo Performance Materials Inc that culminated in IPOs respectively. However, private equity sponsors facing potentially volatile markets may rely on the dual-track process more heavily in the future to help increase valuations and to hedge against the risk of a failed or significantly delayed IPO. The US market has recently seen a significant uptick in dual-track processes, much of which has been driven by private equity sponsors, and many dealmakers expect such processes to become more common for significant sponsor exits in future years.

While a dual-track process may enhance valuations and pricing tension in certain circumstances, concerns may arise that a contemporaneous IPO is little more than a distraction from a sale process or an elaborate pricing exercise. These concerns, however, can be managed or moderated in a number of ways:

*a* Concerns relating to distractions, skepticism of bidders, market perceptions and confidentiality may be alleviated by a company making a 'quiet filing' with Canadian securities regulators. While the US Jumpstart Our Business Startups Act and recent policy changes from the US Securities and Exchange Commission allow for companies to file a registration statement confidentially, a similar blanket policy is not available for Canadian companies (other than in certain limited circumstances). As a result, confidential filings have not been a common practice in Canada until recently. In certain limited situations (including in certain dual-track processes), Canadian securities regulators may allow a preliminary prospectus to be filed on a confidential basis and allow a company to advance an IPO process to a certain point without any public disclosure. This permits the company to address comments from the securities regulators without having disclosed the prospectus to the public. If the company then ultimately pursues a sale process, it can terminate the IPO. Prior consultation with the principal securities regulator is required in these circumstances to ensure that the regulator is aligned on the case for a quiet filing.

*b* Bidders' concerns regarding the commitment of a company to an auction process running alongside an IPO process can be alleviated by offering break fees or expense

reimbursements to a preferred bidder in a dual-track process. It is also important to note that the Canadian convention for underwritten IPOs is for the issuer to pay the expenses of the underwriters, including the fees of underwriters' counsel (often up to a cap). If a company significantly advances an IPO but ultimately pursues the M&A track, the company will in most cases be required to reimburse the underwriters for their expenses (which can be significant, depending on the stage of the IPO). This is a significant difference from the convention in the US where underwriters typically pay the fees of their own counsel.

*c* Canadian securities laws provide for certain limited testing the water activities prior to the public filing of a preliminary prospectus (subject to a cooling-off period). These activities may allow for a company to confirm whether an IPO is a viable exit path before making a public filing as part of a dual-track process.

***Representations and warranties insurance***

While M&A representations and warranties insurance (R&W insurance) has become widespread in the US market, particularly in large or mid-market private equity deals, the Canadian market has been relatively slower in its adoption. Insurance brokers and dealmakers have, however, predicted over the past few years that it was only a matter of time before R&W insurance became increasingly prevalent in Canadian transactions. In 2019, this expectation became a reality. R&W insurance is now widely used by private equity firms and certain strategic acquirers in Canadian transactions.

A number of factors have led to the embrace of R&W insurance in Canada:

*a* Dispositions of Canadian assets are increasingly being managed through structured auction processes with the assistance of a financial adviser. In previous years, buyers would use R&W insurance (in lieu of, or as a supplement to, traditional indemnification) to competitively differentiate their bids. However, sophisticated sellers and financial advisers that are conducting robust auctions are now including, as part of the formal process, the requirement that any prospective buyer obtain an R&W insurance policy.

*b* Over the past year, R&W insurance policy terms have continued to become more attractive. Competition among underwriters has created downward pressure on premiums, which are now typically between 2.5 and 4 per cent of policy coverage. Retention amounts have also decreased significantly, with a retention amount of 1 per cent of the enterprise value now becoming standard.

*c* Just a few of years ago, policies contained numerous broad exclusions from coverage including in areas like tax, environmental matters, cybersecurity, pension funding and compliance with certain laws. This naturally led to specific or supplemental indemnities being negotiated in purchase agreements to ensure buyers still had recourse for these exclusions, which partially defeated the purpose of R&W insurance. As underwriters have become more sophisticated and have faced greater competition from new entrants into the market, the number and scope of exclusions have decreased considerably.

*d* Buyers have naturally been reluctant to shift from traditional indemnification to a relatively new insurance product due to concerns about claims recovery. In an effort to increase adoption of the product and alleviate this concern, various prominent global underwriters have published reports that set out historical information promoting their claims coverage to build confidence in the effectiveness of the product among users.

*e* R&W insurance brokers are becoming increasingly focused on the Canadian market. Many global insurance brokers have established permanent offices and staff in key Canadian markets to help market and place R&W insurance.

There is no question that there is growing acceptance of R&W insurance in the Canadian M&A landscape, especially where private equity firms are involved. Buyers and sellers are now seeing the transformative impact of R&W insurance on deal negotiation dynamics and post-closing relationships. As dealmakers become more familiar with the product, and in particular in a generally seller-friendly environment where underwriters seek to demonstrate that R&W insurance policies may provide more effective means of recovery than traditional indemnification, there is every reason to expect that the product will be further embraced in 2019, and that adoption rates will converge with those in the US in coming years.

### iii Strategic private investment in public entity or financing and acquisition transactions

Although they have long been popular among junior mining, gaming and cannabis companies, strategic private investment in public entity (PIPE) transactions have become increasingly common in Canada among a wider variety of issuers. A strategic PIPE transaction has features commonly associated with both corporate financings and takeovers, sometimes being referred to as a financing and acquisition (F&A) transaction.

In an F&A transaction, a publicly traded issuer will raise money by issuing equity or equity-linked securities, usually at the market price or at a premium, to an investor who may also receive warrants entitling the holder to acquire additional securities, giving the investor a path to control the issuer. Some notable examples of PIPE transactions include:

*a* CITIC Africa's C$725 million investment to acquire a 19.9 per cent interest in Ivanhoe Mines, together with ancillary governance rights;

*b* Rhône Capital's US$500 million investment to acquire a 21.8 per cent interest in Hudson's Bay Company, together with ancillary governance rights;

*c* Constellation Brands' C$5.1 billion investment to acquire an additional interest of approximately 30 per cent in Canopy Growth, together with ancillary governance rights and share purchase warrants entitling Constellation to acquire (upon payment of an additional C$4.5 billion) further shares that would result in aggregate holdings of approximately 55 per cent;

*d* Altria Group's C$2.4 billion investment to acquire a 45 per cent interest in Cronos Group, together with ancillary governance rights and warrants entitling Altria to acquire (upon payment of an additional C$1.4 billion) additional shares that would result in aggregate holdings of approximately 55 per cent; and

*e* Brookfield Renewable Partners' C$750 million investment in preferred shares and convertible debentures of TransAlta Corporation, which shares and debentures are exchangeable for equity in a TransAlta subsidiary using an exchange ratio derived from a multiple of the subsidiary's future adjusted EBITDA.

From the issuer's perspective, a PIPE transaction offers equity financing at an attractive price (since public offerings and private placements are typically completed at a discount to the market price), often accompanied by an ancillary commercial relationship that may be perceived by market participants as a form of commercial sponsorship by the investor. The F&A transaction may be an especially attractive form of financing for a capital-intensive business

that is not earnings positive or is operating in a challenging capital markets environment, or both. Provided that the securities issuance is completed as a private placement, the F&A transaction does not require a prospectus or other offering document.

The market disruption unleased by the covid-19 pandemic has led many issuers and investors to contemplate PIPE transactions, with issuers looking at them as an attractive financing alternative and some investors looking at them as a form of supercharged toe-hold that may facilitate a later going-private transaction or secondary sale.

From the investor's perspective, an F&A transaction offers an opportunity to acquire a substantial, non-controlling equity foothold in a company, usually accompanied by board nomination rights, shareholder approval rights, anti-dilution and preemptive rights and an option to acquire a controlling interest. Unlike an acquisition of securities effected under the private agreement exemption from the takeover bid requirement, there is no statutory limit on the premium payable in a private placement by an issuer. The F&A transaction can be structured using common shares, preferred shares or convertible debentures. Convertible debentures or preferred shares may be especially attractive for an investor that is evaluating an early stage issuer or an issuer that is experiencing financial difficulty, where there can be a real benefit to being higher up in the issuer's capital structure before becoming an equity holder. An F&A transaction permits an investor to monitor (and often influence) its substantial investment before determining whether to acquire control (and consolidate the investee company) by exercising its path-to-control warrants.

As a type of PIPE, an F&A transaction is subject to securities laws and stock exchange requirements. The issuance of securities will be completed under an exemption from the prospectus requirement, usually in reliance upon the accredited investor exemption. An accredited investor includes an institutional investor having net assets of at least C$5 million. Securities acquired under the accredited investor exemption will generally be subject to statutory resale restrictions for four months following the closing of the private placement, except where the investor is a control person, in which case additional restrictions will apply. If the investor acquires 10 per cent or more of the issuer's voting shares, it will become an insider subject to insider reporting obligations.

In addition, if the investor acquires 10 per cent or more of the voting or equity securities of any class (or convertible securities entitling the investor to be issued 10 per cent or more of such class), the investor must promptly issuer a press release and, within two business days, file an early warning report (similar to a Rule 13D filing) with the Canadian securities regulators. Any issuance of equity securities by a listed issuer (or securities exercisable, convertible or exchangeable for equity securities) will usually require stock exchange approval. In the case of securities listed on the TSX or TSX Venture Exchange, the stock exchange will usually require disinterested shareholder approval if the securities being issued would result in a new 20 per cent shareholder or dilute the company's existing shareholders by 25 per cent or more. In addition, depending on the strategic investor's pro forma ownership in the issuer, the F&A transaction may trigger approval requirements or pre-merger notifications under the Competition Act (Canada) and, if the investor is a non-Canadian, under the Investment Canada Act.

F&A transactions are completed pursuant to a negotiated form of subscription agreement, which, in addition to the customary provisions found in share purchase agreements for private placements, will include some or all or the following provisions that are more typically reserved for M&A transactions:

*a* a non-solicit with a fiduciary out;

*b* deal protections, such as the payment of a termination fee and a right-to-match, in favour of the investor; and
*c* a standstill provision, restricting the investor's ability to acquire securities of the investee company, or to propose a merger, prior to closing.

These provisions are customary because, in an F&A transaction, the investor is acquiring a meaningful equity position in the investee company that, even if not accompanied by path-to-control warrants, puts the investor in a good position to launch a takeover bid or merger proposal. Moreover, prior to signing the subscription agreement, the investor will have had an opportunity to complete a due diligence investigation and may have gained access to material information that has not been publicly disseminated. If the investor elects to commence a takeover bid or make a merger proposal, depending upon the investor's ownership interest, the takeover bid could be subject to insider bid rules, and any merger could be subject to minority approval and formal valuation requirements under Multilateral Instrument 61-101: Protection of Minority Security Holders in Special Transactions.

The scope of ancillary contractual rights that accompany the investment in an F&A transaction is subject to negotiation in the context of the parties' relative bargaining power and prevailing market conditions. Often, these rights are set forth in an investor rights agreement, which may contain some or all of the following provisions:
*a* Board nomination rights allowing the investor to enjoy the right to nominate an agreed number of persons for election as directors. The actual number of nomination rights will usually be a function of the investor's percentage ownership. The agreement will usually place restrictions on the company's ability to change the size of its board, and may prescribe how the chair will be selected.
*b* Top-up rights allowing the investor to subscribe for additional shares, at an agreed price or formula price, to maintain its percentage shareholding following the issuance of dilutive securities, including shares issued as acquisition currency or pursuant to employee compensation plans. Top-up rights can, however, create complexity for compliance with stock exchange anti-dilution policies, and can inadvertently be an unnecessary administrative burden for the investee company.
*c* Preemptive rights allowing the investor to have conventional preemptive rights to participate rateably in any public offering or private placement.
*d* Shareholder approval rights allowing the investor to have the benefit of restrictive covenants, which will require the investee company to obtain the investor's prior approval before, inter alia, amending its articles, entering into an agreed list of material transactions and declaring an extraordinary dividend. Notably, the investor is not subject to any common law fiduciary obligation to the investee in exercising shareholder approval rights. The scope of these shareholder approval rights may be taken into account by a stock exchange or a regulator in assessing whether they confer de facto control on the investor.
*e* The investee company may want to ensure that it has an opportunity to use the proceeds obtained from the F&A transaction to pursue its business plan before the investor is able to acquire control of the company or take it private. As such, the investor rights agreement may limit the strategic investor's ability to acquire additional securities or propose a going-private transaction with a standstill provision that applies for a period following closing, or for as long as the investor holds an agreed minimum percentage of shares, except with the prior approval of the investee company's board.

*f* The investee company may seek to align the strategic investor with the company for some minimum period following closing to prevent the investor from flipping its investment to a competitor of the company, or divesting all or part of its interest in a manner that places undue negative pressure on the market price of the company's shares. These resale restrictions may contain springing provisions, entitling the investor to tender its shares to a third-party takeover bid.

*g* Conventional piggy-back rights or demand registration rights, or both.

*h* In some transactions, although not the majority of them, path-to-control warrants allowing the strategic investor to acquire, on exercise, a sufficient number of additional securities to give the investor a controlling interest (or negative control) in the company. These warrants are usually priced at a further premium, above the premium paid by the investor for its front-end investment in the common shares, and may be subject to specified vesting limitations and other conditions.

The path-to-control control aspect of this type of transaction might seem curious to persons familiar with the *Revlon* doctrine,[11] which is a shareholder primacy model of jurisprudence espoused by Delaware courts and followed in many other jurisdictions. Under the *Revlon* doctrine, in the context of a transaction involving a potential change of control, directors' fiduciary duties are automatically transformed from focusing on the long-term interests of the corporation to maximising shareholder value in the near term. More specifically, the role of the board, when faced with the possibility of a change of control, changes from 'defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company'.[12]

However, a number of Canadian courts have declined to follow *Revlon* in the context of change of control transactions, with one even going so far as to declare that 'Revlon is not the law in Ontario'.[13] In *BCE Inc v. 1976 Debentureholders*,[14] the Supreme Court of Canada had an opportunity to weigh in on the topic in the context of a proposed C$52 billion leveraged buyout. In *BCE*, the Supreme Court's main focus was to consider whether the company's debenture holders were being oppressed in a proposed plan of arrangement that had been approved by an overwhelming majority of common shareholders. While the Court did not expressly reject Revlon, it reiterated a finding in its earlier decision in *Peoples*[15] that, under Canadian corporate law, the fiduciary duty of directors is always owed to the corporation and not to any particular stakeholder or group of stakeholders. As such, under Canadian law, an informed board that is free of conflicts of interest has wider latitude to exercise its business judgment, even in the context of a prospective change of control, than may be the case in jurisdictions that follow the *Revlon* doctrine. In Canada, not every potential, or even prospective, change of control requires a board of directors to auction the company.

11 *Revlon, Inc v. MacAndrews & Forbes Holdings, Inc*, 506, A.2d 173 (Del. 1986).

12 *Revlon*, at 182.

13 Including *Maple Leaf Foods Inc. v. Schneider Corporation* (1999), 42 O.R. (3rd) 177 (C.A.).

14 [2008] 3 SCR 560.

15 *Peoples Department Stores (Trustees of) v. Wise*, [2004] 3 SCR 461.

## IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

In recent years, the review thresholds under the Investment Canada Act's net benefit regime have increased significantly. Two of the three thresholds that will apply to most direct acquisitions of control of a Canadian business by non-state-owned enterprise investors[16] from World Trade Organization (WTO) Member States have increased significantly: the private sector trade agreement investors threshold increased to C$1.613 billion (2020) in enterprise value of the target, and the threshold for investors from other WTO Member States increased to C$1.075 billion (2020) in enterprise value of the target.[17] These increased thresholds have contributed to a decrease in the number of transactions subject to a net benefit review (falling from 22 in the 2016–2017 fiscal year to nine in both the 2017–2018 and 2018-2019 fiscal years).[18]

While these increased thresholds represent a shift in the government's emphasis away from net benefit reviews (focused on economic benefits to Canada), national security is increasingly in the spotlight. The national security review regime applies to any investment that involves a non-Canadian, regardless of size and whether control was acquired. Certain industries are likely to attract greater scrutiny, such as tech, critical infrastructure and defence. The government's Guidelines on the National Security Review of Investments set out a non-exhaustive list of activities that may relate to national security. Although these guidelines provide some insight as to when a national security review may occur, there are notable gaps, and foreign investors often receive limited transparency during the national security review process. If the government believes that a transaction may be injurious to national security, the transaction can be blocked, subjected to conditions, or if already implemented, subject to remedies that can include divestiture. Since 2012,[19] four transactions have been blocked, and various others have been subjected to conditions or were abandoned.[20] The majority of the national security reviews that have been ordered were in respect of investors from China (14 orders). In response to the pandemic, the government has extended the timelines for national security screening, and applied the national security screen to a broader range of investments, including those relating to public health.

16 The threshold for direct acquisitions of Canadian businesses by state-owned investors from WTO Member States is C$428 million (for 2020) in gross book value assets.

17 The threshold for the direct acquisition of control of a Canadian business that carries on a cultural business by a non-state-owned enterprise investor from a WTO country remains the same: C$5 million in asset value of the target.

18 Annual Report, Investment Canada Act, 2018–2019, 27 December 2019.

19 Aggregated statistics regarding the national security review process were first published in 2012.

20 Since the implementation of a formal national security review process in 2009, 22 national security review orders were issued between 2012 and 2019. In all but three cases, the transaction was blocked, abandoned or subjected to conditions.

## V COMPETITION LAW

Certain types of transactions that exceed prescribed thresholds require pre-merger notification under Canada's Competition Act. Such transactions cannot be completed until notice has been given to the Canadian Competition Bureau and the statutory waiting period has expired or, alternatively, has been terminated early or waived by the Bureau. Generally, pre-notification of such transactions is required if both:

*a* the parties to the transaction (together with their affiliates) have combined aggregate assets in Canada, or combined gross revenues from sales in, from and into Canada, exceeding C$400 million; and

*b* the aggregate assets in Canada of the target (or of the assets in Canada that are the subject of the transaction), or the annual gross revenues from sales in or from Canada generated by those assets, exceeds C$96 million (2020; this threshold is typically adjusted annually).

Equity investments are also notifiable if the financial thresholds are met and the applicable equity thresholds are exceeded (more than 20 per cent in the public company context, more than 35 per cent in the private or non-corporate entity context or an acquisition of more than 50 per cent of a public company voting shares or private entity equity if a minority interest is already owned by purchaser).

The Competition Commissioner can review and challenge all mergers, whether they are notifiable or not, within one year of closing. Recent developments may increase the number of transactions that are subject to review. From a legislative perspective, recently expanded affiliation rules subject previously non-notifiable transactions to mandatory notification by extending the same control and affiliation principles to all entities, including corporations, partnerships, sole proprietorships, trusts or other unincorporated organisations, which in turn expands the net of relevant entities for the size of parties calculation. From an enforcement perspective, the Bureau has announced an increasing focus on non-notifiable transactions via an expanded intelligence-gathering mandate for the Merger Intelligence and Notification Unit. Furthermore, as part of the Bureau's overall enforcement prioritisation of the digital economy, the Commissioner recently stated that the Bureau is going to be more vigilant about monitoring the acquisition of small firms by big tech. All of this serves to reinforce the importance of conducting substantive competition analysis of transactions of any size that may give rise to competition issues in Canada.

## VI OUTLOOK

M&A in Canada will continue to be heavily impacted by the covid-19 pandemic. The volume of transactions is expected to continue to be robust in those industries perceived to be least impacted, or even enhanced, by the pandemic environment. Distress transactions will continue in bricks and mortar industries directly impacted by ongoing social distancing and government mandated regulation or shut downs. In Canada, the mining sector is anticipated to be a considerable source of activity given the current pricing environment.

**Appendix 1**

# ABOUT THE AUTHORS

## CAMERON BELSHER

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Cameron Belsher is the leader of McCarthy Tétrault's M&A group. He focuses his practice on public and private M&A, corporate finance and private equity, frequently advising on international and cross-border deals. A senior member of the firm's business law group, Cam is one of the most sought-after corporate lawyers in Canada and the relationship partner for some of McCarthy Tétrault's key clients.

Cameron is a former member of the Toronto Stock Exchange (TSX) Listings Advisory Committee, which is composed of individuals representing legal, brokerage and securities-related industries, and provides feedback on TSX listings initiatives. He has lectured extensively on M&A and public corporation matters and is a former adjunct professor at the Faculty of Law, University of British Columbia. He received his LLB from Osgoode Hall Law School in 1987, and was called to the British Columbia Bar in 1988.

Cameron is ranked among Canada's top business lawyers by a multitude of publications, including *Chambers and Partners*, *The Legal 500*, *Lexpert*, *Best Lawyers in Canada*, *Who's Who Legal* and *IFLR1000*.

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Robert Hansen is a partner in McCarthy Tétrault's business law group. His practice focuses on the purchase and sale of shares and assets of public and private companies, with additional experience in continuous disclosure and corporate governance matters. Recognised as a skilled dealmaker, Robert has acted as lead counsel in a range of complex transactions, providing strategic advice and innovative insight on some of Canada's most high-profile deals while successfully pursuing his clients' objectives.

Robert is on the faculty of the Directors College, Canada's first university accredited corporate director development programme, founded by the Conference Board of Canada and the DeGroote School of Business at McMaster University. He also teaches an advanced securities law seminar at the University of Windsor and Western University. Robert received his LLB from Osgoode Hall Law School in 1997, and was called to the Ontario Bar in 1999.

Robert is recognised as a leader in corporate law, securities, M&A and private equity by *Chambers and Partners*, *Lexpert* and *IFLR1000*. In 2008, he was named a 'Rising Star' by *Lexpert*, an accolade given to Canada's top 40 lawyers under 40.

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Robert (Bob) Richardson is a partner in McCarthy Tétrault's M&A, and financial services groups. A seasoned securities lawyer and former senior banking executive, Bob's clients include a variety of deal participants on both sides of the table.

After spending several years near the beginning of his career at McCarthy Tétrault, he led the legal teams at CIBC World Markets Inc, and, later, Canadian Imperial Bank of Commerce (CIBC) where he managed the legal aspects of almost all of CIBC's strategic transactions globally. He served on the board of directors of CIBC's Canadian and European investment banking subsidiaries, and was a member of most of CIBC's key governance and deals committees, including CIBC's fairness opinions review committee. He returned to McCarthy Tétrault in 2018 and focuses on public M&A transactions and corporate governance matters.

Bob is an adjunct professor at Osgoode Hall Law School and the Western University Faculty of Law. He received his LLB and LLM from Osgoode Hall Law School, and was called to the Ontario Bar in 1993.

Bob has been recognised by *Lexpert* as a 'Top 500 Lawyer in Canada', and was a 'Rising Star (Top 40 Lawyers under 40)' in 2004.

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Deborah (Debbie) Salzberger is a partner in McCarthy Tétrault's Competition/Antitrust & Foreign Investment Group. She acts for clients in domestic and multinational mergers and acquisitions with respect to competition/antitrust law and foreign investment review matters. She also regularly provides competition law compliance advice in respect of criminal cartel matters and reviewable practices, including joint ventures, resale pricing, advertising and distribution issues.

Debbie is the current chair of the Canadian Bar Association Competition Law Section's Foreign Investment Review Committee and the co-chair of the American Bar Association's Insurance and Financial Services Committee. Debbie is editor of the "International Price Discrimination" chapter of the ABA Price Discrimination Handbook. She received her LLB from the University of Toronto in 2000, and was called to the Ontario Bar in 2002.

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Mark McEwan is an associate in McCarthy Tétrault's business law group. He practices in the areas of corporate finance, M&A, corporate governance and private equity. He works alongside clients and senior partners on complex domestic and international matters.

In 2019, Mark completed a six-month secondment with a global private equity firm, and gained experience on a variety of transactional, investment and regulatory matters,

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ISBN 978-1-83862-480-4