MAY 28, 2024

Taking AIM at the Mithaq Decision: A Critique

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The recent decision of the Ontario Capital Markets Tribunal to allow a defensive private placement amidst a battle for control places another nail in the coffin for hostile bids in Canada

In a perplexing decision, *Mithaq Canada Inc (Re)*, the Ontario Capital Markets Tribunal upheld a defensive private placement by a target corporation completed in the face of a hostile bid, effectively denying shareholders the opportunity to accept a premium offer. At the time of the bid the target company, Aimia Inc. (Aimia), had been locked in a bitter battle for control with its largest shareholder, Mithaq Capital S.P.C. (Mithaq), which began with a "vote no" campaign against Aimia's entire board in April 2023 and culminated in a hostile bid by Mithaq for Aimia in October of that year. In the midst of this battle, Aimia diluted its shareholders by 24.9% and placed shares in the hands of investors who had a stated intention of not tendering to Mithaq's offer. In a seemingly rigorous analysis of the facts and consideration of whether Aimia's private placement was an improper defensive tactic in accordance with the principles set out in *Re Hecla Mining Company (Hecla)*, the Tribunal reached a problematic decision that has significant implications for the future of unsolicited takeover bids.

Battle for Control

Aimia and Mithaq had a fraught history dating back to 2022 when Mithaq sought to communicate its concerns to Aimia management. Citing Aimia's disregard for the views of its shareholders, Mithaq launched a "vote no" campaign in April 2023 which set in motion the battle for control that culminated in the launch of its hostile bid in October.

Following Aimia's annual meeting of shareholders in April, Mithaq amended its early warning report to introduce, among other things, the explicit possibility of a takeover bid in respect of its investment in Aimia. In particular, Mithaq disclosed that it may "initiate or make public or private proposals or offers involving Aimia, including any takeover bid." Just over a month later on May 25, Mithaq increased its stake from 19.9% to 30.96% by way of a private share acquisition and filed an early warning report reiterating the possibility of a takeover bid.

Less than three weeks later, Aimia's management advised the company's board of directors in a report dated June 5 about a potential private placement that would "establish a strong moat to protect [Aimia] against the distracting attacks of opportunistic raiders." On June 6, Mithaq delivered a letter to Aimia which disclosed that it was contemplating a number of alternatives with respect to its investment in Aimia, including acquiring additional shares by way of a takeover bid. The following day, Aimia's board adopted a shareholder rights plan and publicly stated that it had done so as a direct response to Mithaq's "continued attempts to acquire effective control of Aimia."

From May to October, the parties initiated various legal proceedings against each other, including a proposed motion threatened by Aimia in May for an injunction to prevent Mithaq from taking any of the actions disclosed in its early warning report, including acquiring additional shares. On October 3, Mithaq announced its intention to make an all-cash offer for the outstanding common shares of Aimia and formally commenced the bid on October 5. On October 13, while the special committee of Aimia's board of directors (Special Committee) was still reviewing Mithaq's offer, Aimia announced that it intended to complete a private placement transaction. Aimia stated that the transaction was the result of a months' long negotiation followed by approval by the Toronto Stock Exchange on September 28.

On October 17, Mithaq brought an application to the Tribunal seeking, among other things, an order cease-trading the private placement on the basis that it was an improper defensive tactic intended to defeat Mithaq's offer. Following an expedited hearing held on October 19, the Tribunal allowed the private placement to proceed on an interim basis with an undertaking from Aimia to unwind the transaction if the Tribunal found it to be an improper defensive tactic.

The Tribunal's Findings

Despite finding that the private placement had a defensive character and materially interfered with Mithaq's ability to achieve the minimum tender condition under its bid, the Tribunal concluded that the private placement was permissible. It reasoned that although the private placement had a defensive character, its primary purpose was to meet Aimia's "serious and immediate" need for financing. This conclusion seems inexplicable in light of the evidence presented which, when viewed in the wider context of a battle for control of the company, more clearly suggests that the primary purpose of the private placement was to "build a moat" to defend against Mithaq as an "opportunistic raider" and had only the peripheral purpose of raising cash for unplanned future investment opportunities and to cover cash outflows over the next 24 months, but not to satisfy any immediate need for financing.

Meaning of "Immediate" Need for Financing

In evaluating the private placement as an improper defensive tactic, the Tribunal was required to consider whether the transaction was designed primarily to meet Aimia's "serious and immediate" need for financing. Unlike in *Hecla* where the issuer was in "desperate financial shape" and had insufficient funds to remain a going concern, or in *AbitibiBowater Inc. c Fibrek Inc.* where a dilutive private placement was cease-traded because the issuer failed to demonstrate a "pressing need" for capital, here, the Tribunal concluded that "immediate" does not imply urgency; it simply means that a need "currently" exists, reasoning that an issuer may look 12 to 24 months into the future in assessing whether it has a serious and immediate need for financing.

While the Tribunal rightfully considered the nature of Aimia's business as an investment holding company, it attributed disproportional weight to this consideration. This seemingly muddied the Tribunal's ability to consider the private placement in the broader context, a continuum of events which constituted a contest for control of the company. In fact, Aimia had closed the last of its two pending acquisitions in May of 2023, ahead of management's June 5 report which contemplated establishing "a strong moat" and described one of the purposes of the private placement as eliminating Mithaq's "distracting" behaviour to enable the company, at a later time, to raise debt should any opportunities to transact arise.

Although it might have been preferable for Aimia to have additional cash on hand in order to seize on unexpected investment opportunities, it is difficult to characterize this preference as a serious and immediate need for financing, particularly when compared with the *Hecla* standard. In particular, by the time Aimia began negotiations in respect of the private placement, it had $64 million of cash on hand, of which $7 million was immediately available at the parent level, more than twice the amount Aimia required for the $3 million in cash outflows over the succeeding 12 months.

Reason to Believe Bid Might Be Imminent

In looking at whether Aimia had "reason to believe that a bid might be imminent," the Tribunal articulated the correct test prescribed by National Policy 62-202 *Take-Over Bids – Defensive Tactics* (NP 62-202), but then proceeded to apply a different one. Curiously, the Tribunal considered the circumstances in which a board would have reason to believe that a bid *is* imminent, rather than when a board would have reason to believe that a bid *might* be imminent. (The decision is rife with references to "was" and "is" in this context.) As a result, the Tribunal concluded that it was not until October 3, 2023, when Mithaq announced its intention to make a takeover bid, that Aimia's board had sufficient reason to believe that a bid *was* imminent. The Tribunal seemingly never considered the point at which Aimia's board would have reason to believe that a bid *might* be imminent.

This finding permitted the Tribunal to conclude that Aimia's board could not have had reason to believe that Mithaq's bid might have been imminent, and therefore that the principles of NP 62-202 were not engaged, during the period beginning from Mithaq's early warning report filed in April (which introduced a takeover bid as an option that Mithaq might explore); or from June, when management presented a report to Aimia's board proposing that a private placement would protect Aimia from "opportunistic raiders"; or when Mithaq reiterated the possibility of a takeover bid in its letter to Aimia dated June 6; or when Aimia adopted a poison pill explicitly in response to Mithaq's "continued attempts to acquire effective control of Aimia." Notwithstanding the Tribunal's conclusions, the foregoing appears to provide ample evidence that the board had reason to believe that a bid might have been imminent prior to Mithaq's public announcement on October 3. Interestingly, although by June Aimia was referring to Mithaq's "continued attempts to acquire effective control of Aimia," the Tribunal declined to consider the continuum of events that constituted the battle for control of Aimia.

The Tribunal also noted that the four months between Mithaq's June 6 warning letter to Aimia and the commencement of its takeover bid was too long to support a conclusion that a bid was imminent. It is irresistible to point out the incongruity between a finding that, in the financing context, "immediate" means any time up to 24 months whereas "imminent" in the context of NP 62-202 means a period of less than four months.

Flawed Special Committee Process and an Unusual Opinion

The Tribunal was critical of the Special Committee's process, observing that its "work was not as comprehensive as it might have been." In particular, the Tribunal noted the Special Committee's failure to consider the data provided by its financial adviser about the extent to which the private placement might *affect*, as opposed to *eliminate*, shareholder choice and whether there were ways in which the private placement could be amended to make it compatible with Mithaq's bid.

However, the Tribunal reasoned that it was required to tread carefully in its scrutiny of the Special Committee's work, noting that *Hecla* requires the Tribunal to afford significant deference to directors who are following appropriate governance processes. Despite reasoning earlier in its decision that the board's failure to consider or record any material need for financing near the beginning of 2023 would not be "satisfying from a corporate governance perspective," the Tribunal concluded that the deficiencies in the Special Committee's and board's work were not sufficiently consequential to weigh on its decision in this respect.

It should also have been noteworthy that the Special Committee did not obtain a financial advisory opinion to the effect that Aimia *required* additional capital (as the Aimia board had done by obtaining the Clarus opinion). The Special Committee's financial adviser only concluded in its opinion that a "capital injection was *warranted*." While the Tribunal concluded that this opinion corroborated a pre-existing need for financing, the opinion might be better read as saying nothing more than that the financing was defensible or justifiable as opposed to being required or essential.

How Did Shareholders Benefit from the Private Placement?

In considering whether the private placement was "clearly abusive," the Tribunal applied the tests set out in NP 62-202, including "whether the private placement would benefit Aimia's shareholders" and concluded, without much analysis, that the private placement would be a benefit to shareholders.

The Tribunal acknowledged that a flow of capital to an issuer will not always be of benefit to shareholders, perhaps because it results from an issuance of shares that causes excessive dilution. It found in this case that, on balance, the private placement was beneficial to Aimia's shareholders, but did not provide any detail on how shareholders stood to benefit. Instead, it focused nearly exclusively on rejecting Mithaq's submission that the private placement was not beneficial to shareholders because the shares were being issued at a discount to market price. The Tribunal sensibly noted that it was not necessary for a private placement to be issued at or above market in order to be of benefit to shareholders, but it stopped its analysis short and relied on unspecified benefits in coming to the conclusion that the negative impact of the private placement on bid dynamics was justified because "the impact was outweighed by the benefit to Aimia shareholders."

Calling for a New Public Interest Standard

The Tribunal signalled that *Hecla* may have applied an incorrect standard in respect of the Tribunal's public interest power. While *Hecla* provides that a private placement may be blocked only where there is "a clear abuse of the target shareholders and/or the capital markets," the Tribunal suggested that, in light of the 1994 amendments to the *Securities Act* (Ontario), which introduced the purpose of the legislation as protecting investors against "unfair" practices and to foster "fair" capital markets, it might be appropriate to change the applicable standard used in the evaluation of private placements as improper defensive tactics. Because neither party argued that an alternative standard should be applied, the Tribunal left it open for future bidders to submit that the standard under *Hecla* ought to be reduced from the "clear abuse" standard that the Tribunal was ultimately required to apply in this decision.

The Tribunal's unprompted commentary on the appropriate standard suggests that it may have felt hamstrung by the "clear abuse" standard in making its decision. But its hand-wringing here is misplaced. Arguably, it was unnecessary for the Tribunal to even ask the question whether the private placement should be judged against the standard of "clearly abusive" or the standard of "fairness." That

question has already been answered by securities regulators in NP 62-202. That policy says, in effect, that an issuance of securities representing a significant percentage of the outstanding securities of the target company when a bid might be imminent *is abusive* if it is likely to result in shareholders being deprived of the ability to respond to a bid. That was the finding here, but *Hecla* tells us that in the financing context, this is not the end of the analysis. The adjudicator must balance the impact on shareholder choice against the corporate objectives of the private placement. But once that is done, there is no need to rerun the abuse analysis. The Tribunal's job is done once the balancing exercise has been completed.

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