

How to participate in a distressed M&A environment

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Meet our presenters



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How to participate in distressed M&A

Considerations for the purchaser

- Practical considerations
 - Don't buy it just because its on sale.
 - Understand the problem and have a solution and the ability to fix it
 - Knowledge of the product, industry and market
- Prepare
 - War chest
 - Engage your team

The Pengrowth Deal – A case study example

- Pengrowth Energy Corporation was on the precipice of bankruptcy
 - Failed to renegotiate credit facility amid plummeting oil prices
 - Credit facility and senior notes all matured within 6 months (\$740M in total debt)
 - Lender placed company in special loans
 - Strategic review process
- Process and negotiation of final deal took several months
- Creative Solutions to maximize stakeholder value
 - Shareholders were issued cash at a 75% discount to the trading price
 - Contingent benefit rights
 - Assumption of Credit Facility and repayment / settlement of Notes
- Board and Institutional Shareholder Services (ISS) supported the deal and recommended shareholders approve the deal

Consider legal structure

- Negotiated M&A
 - Target and Purchaser negotiate a deal
 - Court approved Plan of Arrangement
 - Mergers (amalgamation, 3-corner amalgamation)
 - Share Purchase Agreement
 - Take-over Bid (exempt?)
 - Negotiate an Asset Deal ??
 - Creative legal and business structuring
 - Force a negotiated deal through fiduciary process.
- Hostile M&A
 - Purchaser makes take-over offer directly to Target's Stakeholders
- Benefits and timing considerations

**Opportunity to be
Aggressive**

Securities law considerations

- Corporate governance considerations
- Due diligence
 - Assess the business
 - Uncover upsides/downsides
- Other considerations
 - Disclosure requirements
 - Purchasing stock with stock
 - Listing matters
 - Reporting issuer considerations

Thank you



Alex Farcas, Partner
Toronto

Director duties in Canada

- General duties
 - Duty to manage and supervise
 - Fiduciary duty
 - Duty to exercise care, due diligence and skill that a reasonably prudent person would exercise in comparable circumstances
- Fiduciary duty is owed to the **corporation**, not shareholders
 - Includes interests of stakeholders (i.e. shareholders, creditors, employees, etc.)
- Business judgment rule will generally protect decisions made honestly, prudently, in good faith and on reasonable grounds
- Oppression remedy
 - Liability for acts that are “oppressive or unfairly prejudicial”
 - Reasonable expectation of stakeholders is a key consideration

Director duties in Canada – Change of control (Friendly)

- General director duties continue to apply
- Discharging fiduciary obligations requires proper process
 - Form independent committee
 - Retain experts (financial / legal / specialty)
 - Attempt to negotiate a higher price
 - Launch an auction or canvass the market
 - Consider doing so pre-emptively
 - Obtain court approval (where practical)
- Impact of impending insolvency
 - Valuation considerations
 - Practical considerations
- Does a friendly deal make sense?

Director duties in Canada – Change of control (Hostile)

- Duty to respond: 15 days (public companies)
 - No duty to negotiate and no Revlon duty
- Process is important
 - Form independent committee
 - Directors must inform themselves regarding transaction (financial advisors, legal advisors, other experts)
 - Consider alternatives
- Defensive tactics
 - Subject to fiduciary duties
 - Tactical defenses are not widely used
 - Require demonstrable business purposes
 - Regulatory framework for public companies: NP 62-202

Preparedness

- Recommended to adopt a strategy
 - Consult early and often with advisors
 - Set up a special committee
 - Conduct frequent and regular meetings to evaluate situation
 - Due diligence preparedness: consider and understand approach to likely issues
- Understand the needs of stakeholders
- Consider leverage – without cash, the company has no leverage and cannot delay insolvency proceedings
 - Can company raise money?
 - Bridge loan may not be practical
 - Related party considerations

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The landscape

- Overleverage
- Mismanagement
- Supply chain disruption
- Loss of revenues/voluntary or required closures
- Defaults by customers/tenants
- Uninsured or legacy liabilities
- Disadvantageous contracts or leases
- Industry challenges long-term
- Industry challenges short-term
- General or regional economic problems

Key distressed acquisition structures using court process

- Purchase from Debtor-in-Possession Restructuring Process
 - Sale
 - Plan of arrangement or proposal
 - Purchase debt/loan to own
- Purchase from receivership, bankruptcy, or foreclosure proceedings
- Key difference: who drives the bus – the vendor company or a court or statute-appointed third party

Strategic considerations for sellers (1 of 2)

- Type of proceeding (debtor-in-possession or not) - control
- Fiduciary duty to stakeholders
- Support of major lenders
- Sale and investment solicitation process
- Restructuring support agreement or stalking horse bidder
- Preservation of tax NOL carryforwards in plan or proposal
- Funding of process and operations
 - Cost of process
 - New or existing lender?

Strategic considerations for sellers (2 of 2)

- Guarantees
- Can avoid required equity holder approvals or vote
- Application of proceeds and any arguable “diverted” proceeds
- Buyer possibly hiring some existing management
- Recent dividends or distributions being subject to possible claw back
- Opportunity to address class actions
- Compromise third party claims or claims against directors and officers
- Potential stay of regulators

Strategic considerations for buyers (1 of 2)

- Type of process
 - Who has control?
 - Potential costs and delays related to different types of processes
- Ways to exert control over process
 - Become interim lender
 - Buy existing debt – secured or unsecured
 - Credit bidding
 - Stalking horse purchaser – bid protections
- Asset or share acquisition possible
- Vesting order to ensure effective acquisition of assets free and clear of legacy obligations
- Shed existing liabilities, unprofitable business lines, excess employees

Strategic considerations for buyers (2 of 2)

- Availability of pre-closing due diligence – “as is, where is”
- Successor liability
- Environmental, especially for ongoing owned and operating real properties
- Need for lien releases, consents to assignments of contracts, leases, IP licenses
- Whether any assets are owned by insiders or affiliates
- Union and pension
- Post-closing cooperation may be illusory
- Subsequent fraudulent transfer attacks by unpaid creditors or bankruptcy trustee

Thank you



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