IN THE MATTER OF THE SECURITIES ACT,
S.A. 1981, CHAPTER S-6.1, AS AMENDED (THE "ASA")

AND

IN THE MATTER OF THE SECURITIES ACT R.S.B.C. 1996, c. 418
AS AMENDED (THE "BCSA")

AND

AND IN THE MATTER OF THE SECURITIES ACT,
R.S.O. 1990, CHAPTER S.5, AS AMENDED (THE "OSA")

AND

IN THE MATTER OF THE ROYAL HOST REAL ESTATE INVESTMENT TRUST

AND

IN THE MATTER OF CANADIAN HOTEL INCOME PROPERTIES
REAL ESTATE INVESTMENT TRUST

Hearing: **June 22,1999, Vancouver, British Columbia**

Panels:

William Hess, Q.C. **Alberta Securities Commission**	**Chair**
James E. Allard **Alberta Securities Commission**	
Douglas M. Hyndman **British Columbia Securities Commission**	**Chair**
Adrienne R. Wanstall **British Columbia Securities Commission**	
Morley P. Carscallen **Ontario Securities Commission**	
G. Patrick H. Vernon **Ontario Securities Commission**	

Counsel:	**Daniel J. McDonald, Q.C.** **Bill Maslechko** **Frederick Davidson**	**-**	**For the Royal Host Real Estate Investment Trust**
	J. L. McDougall, Q.C. **Jeffrey A. Read** **Michael D. Schafler**	**-**	**For Canadian Hotel Income Properties Real Estate Investment Trust**
	David F. C. Sheridan	**-**	**For the Staff of the Alberta Securities Commission**
	Patrick Robitaille **Brenda Leong** **Peter Brady**	**-**	**For the Staff of the British Columbia Securities Commission**
	Janet A. Holmes **Stan Magidson** **Tim Moseley**	**-**	**For the Staff of the Ontario Securities Commission**

REASONS FOR DECISION

This matter was conducted as a joint hearing by panels of the Alberta, British Columbia and Ontario Securities Commissions.

The Alberta Securities Commission adopts the reasons for decision delivered in this matter by the British Columbia Securities Commission dated November 24, 1999.

DATED at Calgary, Alberta, this 26th day of November, 1999.

"Original Signed By"
William Hess, Q.C.
Chair

"Original Signed By"
James E. Allard
Member

British Columbia
Securities Commission

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COR#99/322

IN THE MATTER OF THE SECURITIES ACT
R.S.B.C. 1996, c. 418

AND

IN THE MATTER OF ROYAL HOST REAL ESTATE INVESTMENT TRUST

AND

IN THE MATTER OF CANADIAN HOTEL INCOME PROPERTIES REAL ESTATE INVESTMENT TRUST

HEARING

PANEL: DOUGLAS M. HYNDMAN — CHAIR
ADRIENNE R. WANSTALL — MEMBER

DATE OF BEARING: JUNE 22, 1999

DATE OF DECISION: JUNE 22, 1999

DATE OF REASONS: NOVEMBER 24,1999

APPEARING:	DANIEL J. MCDONALD, Q. C. BILL MASLECHKO FREDERICK DAVIDSON	FOR ROYAL HOST REAL ESTATE INVESTMENT TRUST
	J.L. MCDOUGALL, Q.C. JEFFREY A- READ MICHAEL D. SCHAFLER	FOR CANADIAN HOTEL INCOME PROPERTIES REAL ESTATE INVESTMENT TRUST
	PATRICK ROBITAILLE BRENDA LEONG PETER BRADY	FOR COMMISSION STAFF

REASONS FOR DECISION OF THE COMMISSION

1. INTRODUCTION

On June 22, 1999, the British Columbia Securities Commission, the Alberta Securities Commission arid the Ontario Securities Commission jointly heard an application by Royal Host Real Estate Investment Trust ("Royal Host") in respect of a take over bid it had made for the units of Canadian Hotel Income Properties Real Estate Investment Trust ("CHIP").

Royal Host publicly announced on May 19, 1999, that it would make the bid for CHIP. On May 21, the trustees of CHIP adopted a unitholder rights plan, without the approval of the holders. Royal Host made the bid on May 31 and, on June 15, amended the bid so that it would remain open until June 25.

In its application to the commissions, Royal Host sought orders terminating the operation of the CHIP rights plan against its bid, specifically:

- orders cease trading the CHIP unit rights issued pursuant to the rights plan and any CRT units issued on exercise of the unit rights, and
- orders that certain exemptions not apply to any trades in securities issued by CHIP in connection with the distribution of the unit rights.

At the hearing on June 22, both Royal Host and CHIP called witnesses and made submissions. Staff of the British Columbia Commission made submissions on behalf of staff of all three commissions.

At the conclusion of the hearing, following a short adjournment, the Chair of the British Columbia Commission issued the following decision and advised that reasons would follow in due course:

> I am delivering this decision on behalf of the three Commissions that have participated in today's hearing. We have carefully considered all of the evidence and submissions we have received. It is our decision that, if Royal Host extends its take-over bid for the units of CHIP to expire no earlier than 7:00 p.m. Pacific Daylight Time on July 6, 1999, we will issue orders cease trading the CHIP [rights plan] unless CHIP issues a news release by noon, Pacific Daylight Time, on July 2 confirming that it has waived the [rights plan] as against the Royal Host bid.

These are our reasons for the decision.

2. BACKGROUND

Royal Host is an unincorporated closed-end investment trust that acquires and operates hotel properties. Its head office is in Calgary and it is governed by the laws of Alberta. The trust units of Royal Host are traded on The Toronto Stock Exchange.

CHIP is also an unincorporated closed-end investment trust that acquires and operates hotel properties. CHIP owns 35 hotels in Canada and one in Washington. Each hotel, with a few exceptions, is held in a separate holding company. As of June 1999, CHIP had 66 wholly-owned subsidiaries, as well as an affiliated limited partnership that managed the hotels.

CHIP's head office is in Vancouver and it is governed by the laws of British Columbia. The trust units of CHIP are traded on The Toronto Stock Exchange. Pursuant to CHIP's Declaration of Trust, the standard of care required of the CHIP trustees is essentially the same as that required of directors under corporate legislation.

Representatives of Royal Host and CHIP first met in April 1998 to discuss the possibility of combining the two investment trusts. Over the course of the following year, several meetings were held, the last in March 1999.

On March 3 1, CHIP sent out a Manage ment Information Circular in anticipation of its annual general meeting on May 11. The CHIP trustees considered at that time adopting a rights plan and putting it to the unitholders for approval at the meeting, but decided not to do so. One of the reasons for their decision was that they did not think such a plan would be favourably received by CHIP's institutional unitholders.

On May 11, 1999, a Special Committee of independent trustees of CHIP was formed to review a proposed transaction under negotiation by CHIP and a third party hotel entity. Pursuant to those negotiations, CHIP had entered into a non-solicitation agreement with the third party, which prohibited CHIP from soliciting certain change of control transactions. Pursuant to the agreement, this prohibition would fall away if a formal bid was made for CHIP's shares.

On May 17, the chair of Royal Host wrote to the chair of CHIP requesting a meeting to present Royal Host's proposal for a combination of the two investment trusts. Later that day, after consulting CHIP's legal advisors and a number of the trustees, the chair of CHIP declined the request.

On May 19, Royal Host issued a press release announcing its intention to make a take over bid for all of the units of CHIP.

On May 21, the trustees of CHIP met to discuss Royal Host's proposed bid. They authorized the Special Committee to review the proposed bid, both on a stand-alone basis and relative to the proposed transaction that was already under negotiation. They also authorized the Special Committee to review any other unsolicited proposals received by CHIP and to advise the trustees as to which proposal would be in the best interests of the unitholders.

Later on May 21, the Special Committee met and unanimously recommended the adoption of a unitholder rights plan. The Special Committee considered a number of factors, including:

- the 22-day period that the proposed bid would be open for acceptance,
- the limitation imposed on CHIP by the non-solicitation agreement, which required CHIP to await Royal Host's formal bid before seeking alternative transactions;
- the complexity of CHIP and REIT structures generally;
- the likelihood of the proposed transaction under negotiation or an alternative transaction requiring a meeting of unitholders;
- the need to spend more time negotiating and developing the proposed transaction under negotiation, and
- the desire of the Special Committee to have the time necessary to consider all alternative transactions available.

The trustees adopted the plan that day. The rights plan authorized the trustees to issue one right in respect of each outstanding unit. The right entitled the holder to purchase additional units of CHIP at a significant discount ten business days after the public announcement or commencement of a take over bid that was not a "permitted bid". A permitted bid had to meet several requirements, including one that the bid remain open for acceptance for 60 days.

Also on May 21, the Special Committee appointed Ladner Downs as its legal counsel. On May 3 1, it retained TD Securities Inc. as its financial advisor.

On May 3 1, Royal Host mailed its bid to the CHIP unitholders. The bid was for all the outstanding CHIP units and was open for acceptance until June 24. The bid complied with all of the terms of a "permitted bid" under the CHIP rights plan, except the requirement that it be open for acceptance for 60 days. The bid was conditional upon, among other things, the CHIP trustees having redeemed the unit rights or waived the application of the rights plan, or a cease trade or court order having the same effect having been issued.

On June 1, the trustees of CHIP received a copy of Royal Host's bid, which released CHIP from the non-solicitation agreement connected with the proposed transaction negotiations. Accordingly, the trustees expanded the mandate of the Special

Committee to authorize it to initiate discussions with other parties and to pursue alternative transactions, with a view to maximizing value and benefits for CHIP and its unitholders.

Also on June 1, the Special Committee met with its legal and financial advisors to consider Royal Host's offer. The Special Committee expanded the mandate of TD Securities to authorize it to initiate discussions with third parties and advise on alternative transactions. The Special Committee also initiated interviews with other investment firms and, on June 6, retained Merrill Lynch & Co. to assist primarily in dealing with prospective third parties outside of Canada.

On June 2, Royal Host applied to the commissions for orders terminating the operation of the CHIP rights plan against the Royal Host bid. On June 7, CHIP also applied to the commissions for relief in connection with the bid, alleging that Royal Host's Offering Circular and certain of its public disclosure contained materially incorrect, inadequate and misleading information, which prejudiced the unitholders of CHIP in assessing Royal Host's bid.

During the first week of June, the Special Committee met on several occasions. With its legal and financial advisors, the Special Committee reviewed Royal Host's bid, considered a number of alternatives to the bid and reviewed financial, legal, strategic and other considerations relating to the bid. In addition, the Special Committee set up data rooms in Vancouver, Toronto and New York, and determined the basis on which confidential information would be made available to third parties. At one of these meetings, on June 6, TD Securities delivered its opinion that Royal Host's bid was inadequate, from a financial point of view, to unithholders of CHIP.

On June 7, the Special Committee delivered its report to the trustees. The report advised the trustees to recommend to the unitholders that they reject Royal Host's bid.

On June 9, the trustees issued their Trustees' Circular in which they recommended rejection of Royal Host's bid. They gave the following reasons for, their recommendation:

- The bid was inadequate from a financial point of view.
- The bid was inadequate and unfair for unitholders.
- The combination with Royal Host would result in a weaker balance sheet, expose unit holders to significant refinancing risk and reduce financial flexibility.
- The combination with Royal Host might result in a downgrade of CHIP's credit rating.
- Royal Host's hotel portfolio was dominated by smaller, limited-service hotels, which are more susceptible to new competition.
- Royal Host's claimed cost savings and synergies were significantly overstated.

- The exchange of CHIP units for units of Royal Host would result in tax being payable by some unitholders.
- The bid was coercive and highly conditional to the benefit -of Royal Host.
- The Offering Circular contained defective and incorrect information.
- In response to the efforts of the Special Committee and its financial advisors, a number of industry participants and other parties had expressed interest in pursuing an alternative transaction with CHIP.

On June 14, Royal Host issued a Notice of Change and Extension of its bid. The Notice of Change corrected and updated the financial information contained in its Offering Circular and extended the bid by one day, to June 25. On June 20, after reviewing the Notice of Change, CHIP withdrew its application to the commissions of June 7.

The hearing was held on June 22. CHIP called two witnesses: J. Thomas English, Q.C., a trustee of CHIP and chair of the Special Committee; and Joel A. Kazman, Managing Director and head of Mergers and Acquisitions Advisory Services at TD Securities. Both testified that there was a "reasonable possibility" that a competing bid or an alternative transaction, offering terms superior to those of Royal Host's bid, would be forthcoming within the 60 days provided for in CHIP's rights plan. Kazman provided the following reasons for this assertion:

- Twenty-three information packages concerning CHIP, together with confidentiality agreements, had been delivered to potential offerors or parties to alternative transactions, and data rooms in New York, Vancouver and Toronto had been established.
- Thirteen interested parties had entered into confidentiality agreements with CHIP and it was anticipated that additional parties would sign confidentiality agreements.
- Certain of these parties had attended in data rooms in New York, Vancouver and Toronto, had conducted property tours and had engaged in general discussions with CHIP's advisors regarding the type of transaction involving CHIP they would be prepared to consider.
- The parties who had expressed an interest in CHIP were generally significant participants in the hotel and lodging industry with businesses similar to or complementary with that of CHIP, and had the financial resources to be able to make a competing bid for or be party to an alternative transaction with CHIP, superior to Royal Host's bid.
- TD Securities, in conjunction with Merrill Lynch, continued to be actively engaged in bringing additional prospective parties into the process by executing further confidentiality agreements, and assisting prospective parties who had signed confidentiality agreements to complete their investigation of CHIP.

Kazman also testified that, although there was a reasonable possibility of a superior competing bid or alternative transaction, more time was required than was available under the Royal Host bid, for the following reasons:

- CHIP's structure is complicated and a prospective third party would require more time than usual to familiarize itself with that structure.
- Each of CHIP's hotels can be viewed as a discrete business operating in a distinct market; as their hotels are spread across Canada, with one in Washington, a third party would require significant time to conduct adequate due diligence.
- As the total market capitalization of publicly traded American hotel entities is more than ten times higher than that of their Canadian counterparts, CHIP's financial advisors had been soliciting extensively outside of Canada; typically, a foreign third party would require more time to deal with the local business and legal issues.
- A transaction involving a foreign third party would have to be carefully structured to ensure retention of CHIP's favourable status under the Income Tax Act, a process which would be extremely time consuming.

English testified that the third party with whom CHIP had been negotiating the proposed transaction was taking a "wait and see" approach. He also testified, however, that three parties had visited the data rooms and that one of these parties had toured 20 of CHIP's 36 properties.

Also in his testimony, English alleged that Royal Host's bid was substantially unfair and coercive, for the following reasons:

- Royal Host's-Offering Circular contained serious material deficiencies, which were not corrected until Royal Host delivered its Notice of Change.
- Royal Host's Offering Circular threatened CHIP unitholders who did not tender to the bid with adverse tax consequences.
- Royal Host's Offering Circular provided that if at least 66 2/3% of CHIP units were tendered, Royal Host would acquire the untendered units through either a "Compulsory Acquisition" or a "Subsequent Transaction Acquisition". However, the Offering Circular did not indicate which alternative was more likely or what the impact of either alternative would be for unitholders who did not tender. This created a material element of uncertainty which made it virtually impossible for a unitholder to arrive at a fully informed decision as to whether to tender.

Finally, English testified that several institutional investors supported retention of the rights plan. He tendered letters from five such investors, holdings 22.6% of the units.

Royal Host called one witness: Darryl Squires, Vice-President of Nesbitt Bums Inc. Nesbitt Bums was retained by Royal Host as a financial advisor and soliciting dealer-manager in connection with the bid.

Squires testified that, having regard to all the circumstances, by the expiration of Royal Host's bid on June 25, CHIP would have had a considerable period of time within which to evaluate the bid and to seek alternatives to it. He gave the following reasons for his opinion:

- The Trustees' Circular disclosed that, at the time the bid was announced, CHIP, with the assistance of financial advisors, had been in discussions with a third party relating to a potential strategic transaction. A proper review of strategic alternatives should have included an assessment of the value of CHIP and its assets, the organization of data and the identification of potential transactions.
- The fact that CHIP had entered into a non-solicitation agreement indicates that the proposed transaction was significant and that the negotiations were relatively advanced.
- At the expiry date of Royal Host's bid, June 25, CHIP's process of review or negotiation would have been ongoing for at least three months and the bid would have been in the marketplace for 36 days.
- CHIP's value is almost entirely attributable to its real estate assets. Developed real estate assets and hotel properties in particular are not unusually complex to value. Their value is highly predictable based upon past performance and forward looking assumptions respecting a relatively limited number of variables. The methodology is relatively straightforward and generally accepted.
- CHIP's properties and its property manager were acquired within the last two years. Therefore, a reasonably up-to-date valuation and information file should exist for each property.
- The timing of Royal Host's bid made CHIP easier to evaluate. The bid was made shortly after the publication of CHIP's annual audited financial statements and its quarterly financial statements for the first three months of 1999, and the filing of its annual information form.
- CHIP, its advisors and other market participants would have benefited from the knowledge garnered by the marketplace from the recent sale of Unihost, a hotel Company of similar size and with similar operations to CHIP. In particular, the Unihost experience would have helped to identify the universe of potential purchasers, both domestically and internationally.
- The number of potential purchasers for an enterprise like CHIP is relatively limited and readily identifiable.
- Real estate investment trusts have been common in Canadian capital markets for a number of years and there have been a number of mergers and acquisitions involving REITs. The REIT structure does not make CHIP more difficult to evaluate, nor does it make a transaction with CHIP more difficult to implement, than if CHIP were a corporation.

Squires observed that it appeared to him that CHIP, TD Securities and Merrill Lynch had canvassed a wide group of prospective buyers and had been able to get the serious parties well advanced in their reviews. He expressed the view that, given a desire to move towards a transaction, those parties would be able to negotiate the principles of a transaction with CHIP within ten days. (At the date of the hearing, Royal Host's bid was scheduled to expire in three days.)

In response to English's allegations that the Royal Host bid was coercive, Squires testified that uncertainties with respect to either adverse tax consequences or the form of a subsequent acquisition transaction are generally not significant considerations for an investor in evaluating a bid.

Finally, Squires testified that if CHIP were to be permitted to keep the plan in place for another ten days, he would not recommend that Royal Host withdraw the bid.

3. ANALYSIS

The starting point for our analysis of whether we should terminate the operation of the CHIP fights plan against the Royal Host bid is National Policy 62-202, Take-Over Bids - Defensive Tactics, which came into force on August 4, 1997. It replaced the substantially identical national policy statement, National Policy 38, adopted in 1986. National Policy 62-202 sets out our goal in regulating take over bids as follows:

> The primary objective of the take-over bid provisions of Canadian securities legislation is the protection of the bona fide interests of the shareholders of the target company. A secondary objective is to provide a regulatory framework within which take-over bids, may proceed in an open and even-handed environment. The take-over bid provisions should favour neither the offeror nor the management of the target company, and should leave the shareholders of the target company free to make a fully informed decision. The Canadian securities regulatory authorities are concerned that certain defensive measures taken by management of a target company may have the effect of denying to shareholders the ability to make such a decision and of frustrating an open take-over bid process.

National Policy 62-202 summarizes our general position on these defensive measures as follows:

> The Canadian securities regulatory authorities appreciate that defensive tactics ... may be taken by a board of directors of a target company in a genuine attempt to obtain a better bid. Tactics that are likely to deny or limit severely the ability of the shareholders to respond to a take-over bid

or a competing bid may result in action by the Canadian securities regulatory authorities.

Over the past decade, the four major Canadian securities commissions have issued a series of decisions respecting applications to terminate the operation of rights plans, or .,poison pills", adopted as defensive tactics.

The first of these was *Re Canadian Jorex Limited and Mannville Oil & Gas Ltd.* (1992), 15 OSCB 257. Jorex adopted a rights plan, without shareholder approval, nine days after Mannville made an offer to acquire all of Jorex's shares. A rival bid was made shortly thereafter by Canadian Trans-Arctic & Southern International Corp. Jorex subsequently waived its plan in respect of Trans-Arctic's bid, but not Mannville's. Mannville complained to staff of the Ontario Commission that the plan was contrary to the public interest and should be stopped. The hearing was the result of that complaint.

In the reasons for its decision, the Ontario Commission refused to consider whether the Jorex board had acted in good faith, whether the board should have adopted the rights plan in the first place or whether the board should have taken steps to seek shareholder approval of the plan before making it operative. The Commission identified the sole issue before it, at page 263, as follows:

> That issue was quite simply whether, at the time of the hearing, it was in the public interest for us to make an order that would have the effect of putting an end to the operation of the Jorex rights plan as against the Mannville bid, and thus of allowing the Mannville bid to proceed for consideration by the shareholders of Jorex along with the rival bid from Trans-Arctic. Put the other way around, the only question we really had to decide was whether the rights plan had served its purpose in facilitating an auction for Jorex, and so ought to be discontinued as against the Mannville bid to let the shareholders decide which bid they preferred (if, indeed, they wished to accept either one). All seemed to agree, as Commissioner Blain put it early on in the hearing, that "there comes a time when the pill has got to go". The only real issue before us, then (again, as succinctly framed by Commissioner Blain), was "when does the pill go".

After considering the facts of the case, the Commission concluded that the time had come for the pill to go. They observed at page 266:

> Underlying our conclusion was our view of the public interest in matters such as this. As is amply reflected in National Policy 38, the primary concern of the Commission in contested take-over bids is not whether it is appropriate for a target board to adopt defensive tactics, but whether those tactics "are likely to deny or severely limit the ability of the

> shareholders to respond to a take-over bid or a competing bid" (paragraph 6) or "may have the effect of denying to shareholders the ability to make a [fully informed] decision and of frustrating an open take-over bid process" (paragraph 2). If so, then as National Policy 38 clearly indicates, the Commission will be quite prepared to intervene to protect the public interest as we see it. For us, the public interest ties in allowing shareholders of a target company to exercise one of the fundamental rights of share ownership -- the ability to dispose of shares as one wishes -without undue hindrance from among other things, defensive tactics that may have been adopted by the target board with the best of intentions, but that are either misguided from the outset or, as here, have outlived their usefulness.

The Ontario Commission applied National Policy 38 and the principles set out in *Jorex* in the reasons for its decision in *Re Lac Minerals Lid and Royal Oak Mines Inc.* (1994), 17 OSCB 4963, where it observed at page 4963 that: "All parties agreed that the critical issue that the Commission had to decide was is it time for the poison pill to go?"'

The Lac shareholders had approved the adoption of a rights plan in May 199 1. In July 1994, both Royal Oak and American Barrick Resources Corporation made offers for all of the shares of Lac. In considering the application by Royal Oak and American Barrick, the Commission characterized the issue before it, at page 4968, as follows:

> The Commission will only make an order under section 127 of the Act to cease trade securities when in its opinion it is in the public interest to do so. In considering whether to make an order in this case, the real issue the Commission had to determine was whether, the extent to which, and when the Commission should interfere with the conduct of the Lac Board, professed to be directed at maximizing shareholder value, in the interests of allowing the shareholders of Lac to respond to one of the two outstanding take-over bids.
>
> This issue involved interesting questions about the relationship between securities law and corporate law. It raised the tension between (i) the board's duty to manage the corporation honestly and in good faith with a view to the best interests of the corporation; and (ii) the shareholders' "right" to decide whether to sell their shares in response to a take-over bid.

The Commission then referred to *Jorex* and continued at page 4969:

> In a case such as this, the Commission's main concern is the interests of the shareholders of the target company. Would the interests of the Lac shareholders be prejudiced by the continued operation of the Lac

Rights Plan in the face of the outstanding bids by Royal Oak and American Barrick?

After reviewing the evidence, the Commission concluded at page 4970:

> In our view, unless it was made clear to shareholders that the Lac Rights Plan would cease to operate in respect to each of the Revised Royal Oak Offer and the American Barrick Offer if the conditions of the subject bid were met, the existence of the Lac Rights Plan could well have impeded their decision to tender to the bid. Accordingly, we decided that it was in the public interest to indicate that in those circumstances, should the Lac Board not do so, we would make an order cease trading any securities issued or to be issued in connection with the Lac Rights Plan in respect of that bid.

On the same day the Ontario Commission released the reasons for its decision in *Lac*, it also released the reasons for its decision in *Re MDC Corporation and Regal Greetings &Gifts Inc.* (1994),17 OSCB 4971.

As in *Lac*, Regal had adopted and obtained shareholder approval of its rights plan before MDC publicly announced its intention to make a bid. However, in this case, shareholder approval was obtained only shortly before MDC's announcement.

Again as in *Lac*, the Commission applied National Policy 38 and the principles in Jorex and identified the only real issue before it as "when does the pill go". At page 4979, the Commission set out a test to be applied in answering that question:

> It is true chat Jorex teaches that "there comes a time when the pill has to go". However, this is not to say that, once a take-over bid has been made, a shareholder rights plan can have no effect, and that it must automatically be struck down by the Commission so as to allow the bid to proceed at the stated expiry date of the acceptance period of the bid. If there appears to be a real and substantial possibility that, given a reasonable period of further time, the board of the target corporation can increase shareholder choice and maximize shareholder value, then, absent some other compelling reason requiring the termination of the plan in the interests of shareholders, it seems to us that the Commission should allow the plan to function for such further period, so as to allow management and the board to continue to fulfil their fiduciary duties.
>
> In our view, our determination of where the public interest lies required us, in this case, to consider two principal questions.

1. If the Plan is permitted to remain in effect for a reasonable further period, is there, on the evidence, a reasonable possibility that a better offer will come along during the period so that, whether or not this results in MDC raising its bid, the shareholders of Regal will be advantaged?

2. If the Plan is not terminated prior to the end of the current period for the acceptance of the bid, is it likely that [MDC] will not extend the period for acceptance for such "reasonable further period", and thus deprive the Regal shareholders of the opportunity to decide whether they wish to accept the [MDC] bid?

After reviewing the evidence, the Commission concluded that there was a reasonable possibility that a better offer would come along if the rights plan was permitted to remain in effect for a further three weeks and that MDC was likely to extend its bid for some reasonable period if it was likely that the operation of the plan would be terminated by the end of that period.

After reaching these conclusions, the Commission continued at page 4980:

> Having answered the two principal questions, there remained a further fundamental question which we had to consider, namely, what were the wishes of the Regal shareholders as regards the Plan? It is all very well for us to conclude that there is a real possibility that shareholder value will be increased as a result of our deciding that the "time has not yet come", but we would not have been prepared to do so if it was clear to us that the shareholders of Regal felt otherwise.

The Commission observed that Regal's shareholders had approved the plan. They also observed that around 80% of Regal's shares were held by 15 or 16 institutional shareholders, who were not unfamiliar with rights plans. Finally, they observed that no shareholders, other than MDC, were seeking termination of the plan. They concluded that they had no reason to believe that Regal's shareholders, other than MDC, wanted the Commission to terminate the plan as against MDC at the time of the hearing.

The Commission concluded at page 4981:

> For the reasons above stated, we were not prepared at the conclusion of the hearing to interfere with the attempts being made by the Regal board to maximize value for shareholders. We, like the majority in Lac, were reluctant to interfere with or usurp the responsibilities of the board. Accordingly, we were not then prepared to grant MDC the relief

requested in its application, In the circumstances, we concluded that the Lac "less is more" approach was the appropriate one.

> However, based on the evidence which had been presented to us at the hearing, we would have been prepared to issue a cease trade order as requested if the Regal board had not waived the Plan, as regards the MDC bid, or redeemed the rights issued thereunder, prior to September 30, 1994. In the interim, if any new evidence came to the attention of the parties that would have justified bringing the matter back on before then, we would have been prepared to hear it. In particular, this would have included evidence that the holders of a majority of the outstanding Common Shares wished the Plan terminated as regards the [MDC] bid.

Approximately three years after *Regal,* National Policy 38 was replaced by National Policy 62-202. Subsequently, each of the four commissions participated in one or both of two hearings respecting the validity of "tactical" rights plans, namely plans implemented by a target company without shareholder approval in the face of a hostile take over bid. Those two decisions have been interpreted as imposing a different test from that established in Regal.

In *Re CW Shareholdings Inc. and WIC Western International Communications Ltd.*, (1998), 21 OSCB 2899, the Ontario, Alberta and British Columbia Commissions considered a rights plan that had been adopted by WIC in the face of a take over bid by CIA' Shareholdings without shareholder approval. In that case, the bid was effectively for only non-voting shares and would not have affected control. The controlling shareholder had, shortly before the bid, disposed of control in a private transaction at a substantial premium to the market. The commissions found that the bid was in no way coercive and that there were only two other potential bidders, neither of whom would need much time to make a bid. The commissions decided- that they would issue cease trade orders if the rights plan was not removed in respect of the bid within one week after the hearing. Reasons for the decision were issued by the Ontario Commission and concurred in by the 'others. In its reasons, the Ontario Commission observed at page 2908:

> The Rights Plan was put into place in the face of the Bid and without a vote of shareholders. In such circumstances, it is, at the very least, necessary for the target company to demonstrate that it was necessary to do so because of the coercive nature of the Bid or some other very substantial unfairness or impropriety, This was not done by WIC in this case.

In *Re Ivanhoe III Inc. and Cambridge Shopping Centres Limited*, (1999), 22 OSCB 1327, the Ontario and Quebec Commissions let stand a rights plan adopted by Cambridge without shareholder approval in the face of a partial bid by Ivanhoe. The

reasons issued by the two commissions were, in substance, identical. In its reasons, the Ontario Commission referred to the above quoted paragraph from 97C and applied a two step procedure, as described at page 1329:

> The two principal issues which had to be considered by the Commission were:
>
> 1. in view of the facts that the Plan had been adopted in the face of the Bid and had not received shareholder approval, should it be permitted to stand; and
>
> 2. if the Plan was permitted to stand, had the time come for it to be terminated by the Commission.

With respect to the first issue, the Commission found that the bid was coercive. They based this finding on their conclusions that the market for the shares was relatively illiquid (given the large institutional shareholdings) and would become more so if the bid were successful and that, in such circumstances, the effect of the partial bid would be to put pressure on shareholders to dispose of whatever shares they could before being locked into a minority position, there being no assurance that Ivanhoe would ever bid for the remaining shares. In making this finding, the Commission observed at page 1329:

> Had we not concluded that the Bid was coercive, we would have immediately cease traded the Plan, since we agree with the Commission's determination in WIC that, if a rights plan is put into place in the face of a bid and without a vote of shareholders, it is, at the very least, necessary for the target company to demonstrate that it was necessary to do so because of the coercive nature of the bid or sortie other very substantial unfairness or impropriety.

The Commission then turned to the second issue and applied the *Regal* test in determining whether the time had come to terminate the rights plan. It found that there -tk as a reasonable possibility that a better offer would come along and that there was every reason to believe that Ivanhoe would extend its bid, if the plan was to remain in place until its expiry. Accordingly, the Commission denied the application but stated that it would terminate the operation of the plan if the trustees amended it to remain in effect after its original expiry date.

Shortly after *Cambridge*, the Alberta Commission issued the reasons for its decision in *Re Samson Canada, Ltd cod Highridge Exploration Ltd.* (1999) 8 ASCS 1791. The shareholders of Highridge had approved a rights plan almost two years before Samson publicly announced its intention to make a bid for all of the Highridge shares.

In its decision, the Commission noted that both parties had agreed that the relevant test was that set out in *Regal.* In applying the *Regal* test, the Commission observed at page 1794:

> The Highridge Plan was initially approved by shareholders two years ago and effectively re-ratified during the currency of Samson's Offer. Samson presented no evidence to suggest that the shareholders' views had changed, or that 45 days was unreasonable, Shareholder approval of the Plan is powerful, but not necessarily conclusive, evidence of how the shareholders want their collective interests to be protected in a take-over bid situation. Because all take-over bid situations are factspecific, the Commission must consider all of the particular circumstances of each case, including shareholder approval or lack thereof, in deter-mining whether either parry has met their burden under the Regal test. Here, the 45-day period appeared to be reasonable under all the circumstances and not merely because it was approved by the shareholders.

The Commission concluded that Highridge had shown a real and substantial probability that a better offer could be generated within the 45 days provided for in the rights plan and that Samson had not suggested that it would withdraw its offer or allow it to lapse if the plan remained in place.

The Commission then considered Highridge's allegation that the Samson offer was coercive because it was "opportunistic in timing" in that, although the offer price was at a premium to the current trading price, the shares were so undervalued that the offer was still a "low-ball bid". The Commission agreed that the offer was opportunistic but that that, in and of itself, did not make it coercive. The Commission continued at page 1795:

> Whether an offer is coercive is only one factor to be considered in assessing a shareholder rights plan. Like prior shareholder approval, coerciveness is a powerful but not necessarily conclusive factor to be considered in applying the *Regal* test. The recent decisions of the Ontario Securities Commission in *Cambridge*, and of the Ontario, Alberta and British Columbia Securities Commissions in *Re CW Shareholdings Inc. and WIC Western International Communications Ltd.* (1998), 21 O.S.C.B. 2988; (1998), 7 A.S.C.S. 1452 ("WIC") may appear to place a particular emphasis on this factor in the context of so-called "tactical pills" -- shareholders' rights plans that are put into place in the face of a takeover bid and without a vote of shareholders. Each of those cases involved unique facts and, in our view, each should be interpreted as consistent with

the fundamental application of Regal test in the manner we have described.

The Commission decided that if Samson extended its bid to expire no earlier than 45 days from the date of the offer, the Commission would cease trade the rights plan unless it was waived by Highridge.

Within days of the release of Samson, the British Columbia Commission released the reasons for its decision in Re BGC Acquisition Inc. and Argentina Gold Corp. [1999] 6 B.C.S.C. Weekly Summary 23. In that case, Argentina Gold had implemented a lights plan without shareholder approval during a take over bid by Barrick Gold Corporation through BGC. In the reasons for the decision, the Commission reviewed Jorex, Regal and WIC; it did not consider Cambridge as the reasons for that decision had not been released at the time of the Argentina Gold hearing. The Commission observed at page 54:

> In determining whether a poison pill should stay or go, there is a natural tension between the objectives of letting the shareholders decide for themselves, as described in Jorex, and of letting management and the board fulfill what they see as their fiduciary duties, as set out in Regal. Striking a balance between these objectives in any particular case is highly dependent on the specific facts. Relevant factors include: whether shareholder approval was obtained; whether broad shareholder support is evident; when the poison pill was adopted; the nature of the bid, including whether it is coercive or unfair to the target company shareholders;- the size and complexity of the target company and the number of potential, viable offerors; the likelihood of the existing bid or bids falling away if the pill is not removed; and the likelihood that, if given further time, the target company can find a better offer.

The Commission then applied these factors to the case at hand, noting at page 54:

> In the hearing, Barrick focused considerable attention on the fact that the pill was adopted long after the bid was announced. While it was unusual, we did not place much weight on that fact. What was relevant to us was the situation at the date of the hearing. Argentina Gold had, for seven weeks, been strenuously fighting the Barrick bid and seeking other offers. It was a relatively straightforward company, with some mineral properties, albeit in a remote part of the world, one of which was showing some very promising exploration results. The other potential offerors were a handful of international mining companies, that are in the business of assessing and acquiring successful junior exploration companies, often on short notice and in an auction environment. Newmont had looked closely

at the property and had apparently forgone the opportunity to make a bid. Another major company had visited the property in mid December and had yet to launch a bid. Scotia McLeod had recently been brought in to seek other bidders but most had already been contacted by Argentina Gold's management and, although some site visits were in the offing, there was nothing that could be described as real and substantial interest. Barrick held other properties close by and, as the joint venture partner, was a natural offeror for Argentina Gold. Despite Argentina Gold's efforts to solicit a show of shareholder support for the pill, the support provided in evidence was extremely meagre. Barrick's bid was simple -- a cash bid for all the shares -- and, despite the assertions made by Argentina Gold, there was nothing coercive or unfair about the bid. Similarly, there was no evidence or analysis to support Argentina Gold's claim that Barrick's was an insider bid.

In the final analysis, Argentina Gold's directors opposed the bid because they thought it was too low and that, if given further time, Argentina Gold could produce more positive exploration results and generate an auction in order to obtain a higher bid, from Barrick or someone else. In effect, Argentina's Gold's directors wanted the wow shareholders to reject a current cash offer and speculate that future developments would bring a higher price. They emphasized their view that Barrick would not go away, given its natural interest in the property. That, in our view, was not a decision for the directors to make on behalf of the shareholders.

The Commission applied the test in Regal and decided to immediately terminate the operation of the rights plan on the basis that the only bid on the table was about to expire and that there was no evidence of a real and substantial possibility of another bid within a reasonable period of time.

We now turn to the issue raised by Royal Host's application. That issue was whether it was in the public interest for us to make orders that would terminate the operation of the CHIP rights plan against the Royal Host bid and thus allow the bid to proceed for consideration by the unitholders of CHIP. In other words, was it time for the CHIP pill to go?

The general principles we applied in making that determination are set out in National Policy 62-202 and have been interpreted in the series of decisions reviewed above. In the policy, we emphasize that the primary objective of the regulatory scheme governing take over bids is the protection of the bona fide interests of the shareholders of the target company. We recognize that the board of a target company facing a hostile bid may adopt defensive tactics in a genuine. attempt to increase shareholder value.

However, we also confirm that we will step in if their tactics appear likely to deny or severely limit the opportunity of the shareholders to respond to the bid.

In applying these principles to the determination of the public interest in a particular case, the challenge we face is finding the appropriate balance between permitting the directors to fulfill their duty to maximize shareholder value in the manner they see fit and protecting the right of the shareholders to decide whether to tender their shares to the bid. We can make this determination only after considering all of the relevant factors in that particular case. While it would be impossible to set out a list of all of the factors that might be relevant in cases of this kind, they frequently include:

- whether shareholder approval of the rights plan was obtained;
- when the plan was adopted;
- whether there is broad shareholder support for the continued operation of the plan;
- the size and complexity of the target company;
- the other defensive tactics, if any, implemented by the target company;
- the number of potential, viable offerors;
- the steps taken by the target company to find an alternative bid or transaction that would be better for the shareholders;
- the likelihood that, if given further time, the target company will be able to find a better bid or transaction;
- the nature of the bid, including whether it is coercive or unfair to the shareholders of the target company;
- the length of time since the bid was announced and made;
- the likelihood that the bid will not be extended if the rights plan is not terminated.

This is the approach that was taken in *Jorex* and that served as the starting point for the analysis in the subsequent decisions. However, a number of those decisions *Regal*, *WIC* and *Cambridge* - have attempted to refine this approach by focusing on certain of these factors and using them as the basis for specific tests to be applied in determining whether it is time for the pill to go.

After reviewing these decisions and the fact patterns on which they were based, vie have come to the conclusion that it is fruitless to search for the "holy grail" of a specific test, or series of tests, that can be applied in all circumstances. Take over bids are fact specific; the relevant factors, and the relative importance to be attached to each, will vary from case to case. As a result, a test that focuses on certain factors to the exclusion of others will almost certainly be inappropriate in some of the cases to which we attempt to apply it.

Therefore, in determining whether it was time for the CHIP pill to go, we simply considered all of the relevant factors rather than attempting to establish and apply a comprehensive and conclusive test.

The first of these factors was that CHIP had had an opportunity to put a rights plan to its unitholders for approval last May, but chose not to do so. One of the reasons for this decision was that the trustees did not think that a plan would be favourably received by the institutional unitholders. In other words, it appears that there would not have been a great deal of unitholder support for the implementation of the plan.

Second, CHIP was able to provide little evidence of unitholder support for the continued operation of the plan. By the time of the hearing, institutions holding only 22.6% of the units had provided letters in support.

Third, on the basis of the evidence and the submissions, we concluded that if CHIP was allowed some additional time, there was a reasonable possibility that it could bring forward an alternative bid or transaction superior to the Royal Host bid. The question was, how much additional time would be reasonable in the circumstances? CHIP argued that it needed the 60 days provided for in the rights plan (which would give it 38 days from the date of the hearing) because it had been unable to solicit alternative offers or transactions until June 1, due to the non-solicitation agreement, because its structure is complicated, which would increase the time required for a third party to do due diligence, and because most of the potential third parties were outside of Canada, making them more difficult to locate and any resulting transaction more difficult to structure. Royal Host, on the other hand, argued that CHIP should be given only an additional ten days from the date of the hearing. In support of this, Squires had testified that CRT had been negotiating a proposed transaction or reviewing strategic alternatives for at least three months, that CHIP was not unusually complex to value, that reasonably up-to-date valuation and information files should have been available, that it is no more difficult to implement a transaction with a REIT than with a corporation, and that the potential purchasers for an enterprise like CHIP are limited in number and readily identifiable. Ultimately, we were of the view that the additional time should be much closer to the ten days suggested by Royal Host than the 3 8 days requested by CHIP.

Fourth, by the June 25 expiry date of the bid, it would have been open for acceptance for 25 days. This exceeded the minimum deposit period of 21 days currently required under the securities legislation administered by the four major commissions. However, all four commissions have taken steps to implement the recommendations of the July 30, 1996 Report of the IDA Committee on Take-over Bid Time Limits (chaired by Adam Zimmerman), which proposed that this minimum deposit period be extended from 21 to 35 days from the date the bid was commenced, and that an offeror be able to commence a bid by placing an advertisement, containing prescribed information, in the newspaper and subsequently mailing the bid. Although the legislative amendments

necessary to implement these recommendations have not been brought into force in any of the jurisdictions, all four commissions have clearly indicated support for the 35 day period. Had these amendments been in force when Royal Host announced its bid on May 19, and had Royal Host taken out an advertisement containing the prescribed information on that date, CHIP presumably would have been released from the non-solicitation agreement at that time. In fact, CHIP was not released from the agreement until it received the Royal Host bid on June 1. Under the circumstances, we considered it appropriate that the CHIP trustees have at least 35 days from that date to seek alternatives to the bid.

Fifth, Royal Host's financial advisor, Squires, testified that, if CHIP was permitted to keep the rights plan in place for a further ten days, he would not recommend that Royal Host withdraw the bid.

Finally, despite CHIP's argument that the Royal Host bid was coercive and unfair, we were satisfied that there was nothing coercive, unfair or improper about it. The deficiencies in Royal Host's Offering Circular were corrected by Royal Host's Notice of Change; the potential adverse tax consequences and the uncertainty with regard to the form of a subsequent acquisition transaction were fully disclosed in the Circular; and the bid complied with all of the terms of a "permitted bid" under the CHIP rights plan, except the requirement that it be open for acceptance for 60 days.

4. CONCLUSION

After considering all of these factors, we were of the view that it would not be in the public interest to make orders terminating the operation of CHIP's rights plan against the Royal Host bid at the conclusion of the hearing. However, we were also of the view that the plan should cease to operate against the bid in the event that Royal Host kept the bid open for at least 35 days, which would be an additional 13 days from the date of the hearing. Therefore, we decided that, if Royal Host extended its bid for the units of CHIP to expire no earlier than 7:00 P.M. Pacific Daylight Time on July 6, we would issue orders terminating the operation of the CHIP rights plan unless CHIP issued a news release by noon Pacific Daylight Time on July 2, confirming that it had waived the rights plan against the Royal Host bid.

5. POSTSCRIPT

Following the hearing, Royal Host extended its bid until July 6. On July 2, CHIP announced that it had waived the application of the rights plan to the Royal Host bid. Royal Host later extended the bid several times and increased its offer. On July 20, CHIP announced that it had agreed to a $100 million, two part transaction with BII Acquisition Limited Partnership, an affiliate of Belkorp Industries Inc. Under the transaction, CHIP was to issue 5,000,000 units at $10 per unit to BII Acquisition and BII Acquisition

proposed to acquire a further 5,000,000 units pursuant to a cash take over bid at $10 per unit. This transaction was later approved by CHIP unitholders and closed on September 3. Later on September 3, Royal Host announced the withdrawal of its bid.

DATED at Vancouver, British Columbia, on November 24, 1999.

FOR THE COMMISSION

"Original Signed By"
Douglas M. Hyndman
Chair

"Original Signed By"
Adrienne R. Wanstall
Member