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Blaney McMurtry
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Blaneys on Business

"Business people often use the letter of intent (LOI) as an initial means of establishing a contractual relationship without having to commit themselves to legally binding obligations until the details of those obligations have been negotiated."

This newsletter is designed to bring news of changes to the law, new law, interesting deals and other matters of interest to our commercial clients and friends. We hope you will find it interesting, and welcome your comments.

Feel free to contact any of the lawyers who wrote or are quoted in these articles for more information, or call the head of our Corporate/Commercial group, Steve Popoff at 416.593.3972 or spopoff@blaney.com.

LETTERS OF INTENT: WHEN ARE THEY BINDING?

Sundeep Sandhu

Business people often use the letter of intent (LOI) as an initial means of establishing a contractual relationship without having to commit themselves to legally binding obligations until the details of those obligations have been negotiated.

But what happens when parties have entered into an LOI thinking that all the essential terms of their agreement have been hammered out?

In *Wallace v. Allen*, a 2007 decision of the Ontario Superior Court ("*Wallace*"), the vendors (Graham and Gayle Allen) and the purchaser (Kim Wallace) were friends and neighbours who entered into an LOI for the sale of the shares of the Allen companies – Graillen Holdings, Dickie Transport, Region of Huronia Environmental Services and Allens Acquisitions.

A clause in the LOI required that it be reduced to a binding agreement of purchase and sale within 40 days. Another stated the parties agreed that "there will be much legal work to be done… and that the wording of this agreement may alter somewhat." In other words, the agreement was subject to further legal work acceptable to both parties.

Negotiations ensued between the parties to address all the terms of the purchase and sale agreement.

It appeared from the negotiations and the conduct of the parties that everybody wanted the agreement to be concluded and the sale effected. The parties even went as far as to make emotional retirement speeches and introductions and announcements to business contacts and customers.

However, by the time the closing date rolled around, concerns over property taxes combined with an absence of communication and availability of the parties resulted in uncertainty about whether the deal would close. On the closing date, Mr. Wallace, the purchaser, failed to appear to execute the documents and no arrangement for the funds to close the deal had been made. As a result, the vendor, Mr. Allen, decided to terminate the transaction.

Mr. Wallace brought an action for a declaration that the LOI was binding on the parties. The court dismissed the action, finding that from the perspective of an objective reasonable observer considering (a) the circumstances giving rise to the LOI, (b) the wording of the document, and (c) the conduct of the parties, while the LOI contained all the essential terms, it did not constitute a binding contract.

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"When faced with a letter of intent (LOI), it is best to obtain advice from counsel as to whether it is, first, desirable to have a legally enforceable LOI and, second, whether the specific LOI in question is, in fact, a legally enforceable agreement."

Sundeep Sandhu is a member of Blaney McMurtry's corporate/commercial practice. A graduate of the University of Windsor Law School, where she was an award winner in business law and a volunteer case worker at Windsor Community Legal Aid and the university's mediation services. Ms. Sandhu was called to the bar in 2007. She is a member of the Law Society of Upper Canada and the Canadian Bar Association (Ontario).

Sundeep may be reached directly at 416.597.4878 or ssandhu@blaney.com

So, why did the court decide that the LOI was not a legally enforceable contract, even though it contained all of the essential terms of the agreement? The courts have historically refused to enforce agreements between parties where they have simply agreed to enter into a binding agreement at a later date, since the nature of these "agreements to agree" is to postpone any legal liability until the details of the final agreement have been negotiated.

A legally enforceable contract is formed when the parties have reached a consensus on all the essential terms of their bargain and they have shown that they actually intend to create binding obligations between them. In *Wallace* the parties had made the LOI conditional on entering into a binding agreement and obtaining further legal advice. They had merely entered into an agreement to agree and, as such, had not yet demonstrated that they intended to be bound by the LOI. As the parties did not sign the final form of the purchase and sale agreement they had negotiated, no final agreement had been made.

When faced with an LOI, it is best to obtain advice from counsel as to whether it is, first, desirable to have a legally enforceable LOI and, second, whether the specific LOI in question is, in fact, a legally enforceable agreement. ■

SECURITIES LAW HARMONIZATION: WE'RE MAKING PROGRESS BUT...

James Leech

As shareholders, bondholders, executives, managers, suppliers and many other stakeholders in Canadian public companies know only too well, senior levels of government in this country continue to struggle with the challenge of simplifying securities regulation and cutting the considerable business costs and aggravation that go with it.

Some jurisdictions, such as Ontario, are committed to establishing what would arguably be the most efficient and economic regime possible – a single national securities regulator. Unfortunately, at this point, a single national regulator is not a reality. In its absence, stakeholders welcome anything that can simplify the procedures and transaction costs that public companies face in navigating through 13 different securities regulatory regimes.

In that context, three new measures have come into force in the last six months that create greater harmonization in the securities regulatory environment in Canada. These three initiatives of the Canadian Securities Administrators (CSA) are Multilateral Instrument (MI) 11-102 - *Passport System,* National Instrument (NI) 41-101 - *General Prospectus Requirements*, and MI 62-104 - *Take-over Bids and Issuer Bids*

Passport System MI 11-102

The *Passport System* (**MI 11-102**) came into force March 17, 2008. It implements new national policies (NP) for the filing and review of prospectuses (**NP 11-202**) and exemptive relief applications (**NP 11-203**) in multiple jurisdictions. It also repeals the mutual reliance review (MRRS) policies.

The purpose of MI 11-102 is to implement a system that gives market participants the opportunity to access the capital markets in multiple jurisdictions by dealing only with one principal regulator – usually its local regulator – and meeting the requirements of one set of harmonized laws.

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James Leech is an associate in Blaneys corporate/commercial group. His practice includes securities, mergers and acquisitions and general corporate law. He has worked on debt and equity financing, initial public offerings, brokered and non-brokered private placements, asset and share purchase transactions, reverse take-overs, and corporate governance matters.

James may be reached directly at 416.596.2893 or jleech@blaney.com

The OSC has elected not to adopt M11-102. It has stated that the passport system does not sufficiently address its objectives for securities regulatory reform, namely to:

- strengthen Canada's capital markets and improve the country's competitive position by eliminating fees, costs and duplication arising from 13 provincial and territorial securities regulators;
- promote consistency in regulatory decision-making to ensure fairness and a level playing field for all market participants;
- lead to better and more effective enforcement across Canada resulting in greater investor protection.

Beyond that, the Ontario government has indicated it is not prepared to participate in the passport system without a roadmap, with reasonable timelines, to get to a common securities regulator. It has therefore declined to introduce the statutory amendments that would grant the OSC the rule-making powers that it would need to be a passport member. The government has also indicated it has no plans to introduce such statutory amendments.

Although the passport system may add incremental administrative improvements and efficiencies to the current regulatory process, it does not resolve the need to modernize Canada's securities regulatory structure. Under the passport system, market participants are obliged to deal with only one of 13 regional securities regulators. In addition, when a regulator applies the law and makes regulatory decisions, its decision will have legal effect in other passport jurisdictions. The historic safeguards that promote consistency in regulatory decision making within the CSA, however, would no longer be in effect. Finally, market participants would, for the most part, continue to pay fees to all securities regulators.

While the Ontario Securities Commission (OSC) has decided not to adopt MI 11-102, it can still be a principal regulator under the instrument. This will give market participants in Ontario access to the capital markets in all passport jurisdictions (every province and territory except Ontario) through their dealings with the OSC.

Harmonized Prospectus Requirements

The second major CSA initiative that has come into force this year is National Instrument 41-101 - *General Prospectus Requirements* (**NI 41-101**), which also took effect on March 17, 2008. NI 41-101 creates a comprehensive, seamless, and transparent set of national prospectus requirements for all issuers, including investment funds, except mutual funds, which would continue to file prospectuses under NI 81-101.

The CSA states that NI 41-101 is based on three general principles:

- to harmonize across Canada and consolidate the general prospectus requirements among Canadian jurisdictions;
- to substantially harmonize the general prospectus requirements with the continuous disclosure and short form prospectus disclosure regimes;
- to take into consideration changes in the principles underlying the general prospectus requirements that the CSA has identified as a result of regulatory reviews, applications for exemptive relief, and public comment and consultation.

NI 41-101 is largely based on the requirements set out in former OSC Rule 41-501, *General*

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Prospectus Requirements and Québec's Regulation Q-28 *Respecting General Prospectus Requirements* (**Rule 41-501**). There are a number of substantive differences, however, that are beyond the scope of this article.

A number of other national instruments build on the foundation of NI 41-101, or make reference to requirements in it. They have been amended to harmonize their requirements with those of NI 41-101.

Take-Over Bid Rules

The third major initiative implemented by the CSA in 2008 has been the adoption of MI 62-104 - *Take-over Bids and Issuer Bids* (**MI 62-104**). This came into force on February 1, 2008, and governs take-over bids and issuer bids.

A take-over bid is an offer to acquire voting or equity shares of any class of securities offered by an issuer (including convertible securities) which, if acquired, would result in the purchaser holding 20 per cent or more of the target securities. Persons who hold 20 per cent or more of the securities of a company are considered control persons, and are required to make certain public disclosures of any proposed acquisitions or dispositions of their shares.

Under this new initiative, unless a take-over bid is exempt under the instrument, the offeror must comply with the formal bid requirements of the Bid Regime. This involves filing a take over bid circular (with prospectus-level disclosure) and compliance with stringent notice requirements.

There are a number of circumstances where a take-over bid is exempt from the formal bid requirements:

- Normal course purchases – purchases of not more than 5 per cent of the target securities of the target issuer in any year, made on the open market and not at a premium;
- Private Agreements - purchases from not more than 5 persons, with a maximum premium of 15 per cent of the market price;
- Non-reporting Issuers – the target company is not a reporting issuer, there is no market for the securities, and the company has less than 50 shareholders;
- Foreign take-over bids – if less than 10 per cent of the shares of the target company are held by shareholders in Canada;
- Any company having less than 50 shareholders.

All of the provinces and territories in Canada except Ontario have implemented MI 62-104. The OSC and the Ontario government elected to harmonize Ontario's take-over bid regime through amendments to Part XX of the *Ontario Securities Act* by implementing OSC Rule 62-504 - *Take-over Bids and Issuer Bids* (**Rule 62-504**).

The result is that take-over bid and issuer bid requirements are substantially harmonized across Canada. Although the new bid regime is not a significant departure from the former regime, many commentators have criticized the position taken by Ontario and have expressed disappointment that the regulation of take-over bids and issuer bids has not proceeded by way of a single national instrument. ■

Blaneys on Business is a publication of the Business Law Department of Blaney McMurtry LLP. The information contained in this newsletter is intended to provide information and comment, in a general fashion, about recent cases and related practice points of interest. The information and views expressed are not intended to provide legal advice. For specific legal advice, please contact us.

We welcome your comments. Address changes, mailing instructions or requests for additional copies should be directed to Chris Jones at 416 593.7221 ext. 3030 or by email to cjones@blaney.com. Legal questions should be addressed to the specified author.

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Blaney McMurtry
BARRISTERS & SOLICITORS LLP

2 Queen St. East, Suite 1500
Toronto, Canada M5C 3G5
416.593.1221 TEL
416.593.5437 FAX
www.blaney.com