Cross-Border and International Agreements

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CROSS-BORDER AND INTERNATIONAL AGREEMENTS

by

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1. Introduction

Over the years, I have acted for Canadian clients who have expanded operations internationally primarily through strategic acquisitions. In initiating those transactions, Canadian clients are likely to consult their Canadian counsel to discuss the proposed transaction and the manner it can best be implemented, including the choice of counsel. This paper will review the manner in which Canadian counsel can play a significant role in negotiating and settling agreements in international or cross-border transactions entered into by Canadian clients.

One of the challenges and opportunities facing Canadian counsel to Canadian businesses that expand internationally is how best to serve the Canadian client in jurisdictions in which the Canadian lawyer is not licensed to practice law. Canadian clients may want to continue using their Canadian counsel for a variety of reasons which will include, among others, the Canadian lawyer's familiarity with the client's business and expectations, an understanding based on experience of the legal and business risks that are within the client's realm of tolerance and personal chemistry.

This paper will discuss the approach I have taken as a lawyer acting on behalf of Canadian clients in a variety of cross-border and foreign transactions. In addressing the challenges of negotiating and drafting agreements in an international context, this paper will use

* The author thanks Andrew Cooley for his assistance in updating this paper.
the model of negotiating and drafting private acquisition agreements – whether of assets or shares – as a paradigm. However, this discussion could relate equally to the negotiation of many other types of cross-border or international agreements, such as debt financings or other transactions that are, unlike securities transactions for example, not subject to extensive domestic regulation.

My approach here, in particular, will be to discuss, on a practical level, several of the limitations and challenges involved and how responsibility can be allocated between Canadian and foreign counsel in negotiating and drafting international and cross-border acquisition agreements. I have also added, at the end of this paper, a brief review of the significant differences in the approach to the regulation of related party financial assistance under Canadian law and the laws of virtually all other western legal systems, and how those differences must be considered in drafting and negotiating guarantees and other financial assistance agreements made by foreign affiliates of Canadian-based businesses.

2. Geographic Professional Limitations

a. The Restrictions on Advising Clients on Foreign Law

As Canadian lawyers qualified to practice law in specific provinces or territories we state, in qualifying each legal opinion we provide, that:

"We are solicitors qualified to practise law in the Province of ■ and we express no opinion as to any laws, or any other matters by any laws, other than the laws of the Province of ■ and the federal laws of Canada applicable therein".

Given that cardinal limitation on our professional licences – if not competence – we must, as a starting point, be wary of requests by Canadian clients to act on their behalf in the
negotiation and settlement of agreements governed by the laws of jurisdictions other than the laws of the jurisdiction in which we are licensed to practise law. Counsel for Canadian clients expanding their businesses internationally are often asked to do just that.

It is interesting to note in this regard that in 2010, LawPRO published an article specifically noting that the LawPRO Professional Liability Insurance Policy provides coverage to Ontario lawyers for the performance of professional services involving "the practice of the law of Canada, its provinces and territories". The article goes on to state the following:

With the Internet, easy international travel and a global economy, relationships and business transactions – and legal matters and disputes – frequently cross international borders. Handling matters that involve foreign law can increase the risk that you will face a malpractice claim, and can have important malpractice insurance implications that you should keep in mind… What will, or will not, be covered can be very fact-specific, but you should expect that you are not covered for work involving non-Canadian law.

The article also provides the following caution:

As much as you may want to help a client, don't be tempted to give even the most basic advice with respect to foreign law, even if you know for certain that the information is correct. Just telling a client about a foreign law deadline or commenting on a few words in an agreement governed by foreign law fully exposes you to a claim.

Whereas Alberta lawyers are covered under the ALIA's professional liability insurance policy for giving advice on non-Canadian law, Ontario lawyers are not similarly covered under the LawPRO policy.

This paper attempts to address how, based on my personal experience, I have responded to the challenge presented by requests from Canadian clients to act on their behalf in international and cross border transactions – and, in particular, in the negotiation and drafting of
agreements made in connection with such transactions while attempting to remain within the bounds of my own professional competence and, more particularly, my professional licence, which restricts me to practising law and advising on legal matters governed by the laws of the Province of Ontario, which is the jurisdiction in which I am licensed to practise law.

b. The Intra-Canadian Model and its Challenges

Traditionally, as members of the Bar of a Canadian province or territory, we act almost without hesitation in advising clients on various transactions, including, by way of example, the acquisitions of businesses or the making of loans, in provinces of Canada other than the province(s) in which we are licensed to practice law. In business acquisitions, for example, it is common to find Alberta lawyers advising their Alberta clients on acquisitions in British Columbia or Ontario and Ontario lawyers advising their Ontario-based clients on acquisitions in Alberta and British Columbia. Technically, the limitations on our professional capacity in respect of these matters is as severe in extra-jurisdictional Canadian transactions as it would be in foreign transactions. Our experience in navigating the frontiers of professional competence in these "cross-border" Canadian transactions can serve as a guide for how we might navigate the same limitations in non-Canadian extra-jurisdictional transactions.

It is interesting to note, with respect to intra-Canadian "cross border" transactions, that recently, in an attempt to eliminate the costs to issuers of obtaining provincial agents' opinions in cross-Canada securities offers, certain law firms began developing the practice of rendering opinions on the laws of other provinces in which the securities were being offered. The practice is based on the ability of all Canadian lawyers under the 2002 National Mobility Agreement to practice on a temporary basis the laws of provinces in which they are not called.
The National Mobility Agreement has been signed by all of the legal governing bodies in Canada and implemented locally by the respective Law Societies or Bar Associations in each jurisdiction. The approach that has been adopted by some law firms, in the circumstances where opinions of counsel in other provinces would have otherwise been required, has been to qualify opinions as to the laws of the provinces other than Ontario in the following manner:

"we are solicitors qualified to practise law in the Province of Ontario and except for the opinions provided in paragraphs ■ and ■ as they relate to the Securities Laws of the provinces ■ and ■, which are provided by us pursuant to the National Mobility Agreement among certain members of the Federation of Law Societies of Canada, we express no opinion as to the laws of any jurisdiction or as to any matters governed by the laws of any jurisdiction, other than the laws of the Province of ■ and the laws of Canada applicable therein in effect on the date hereof."

Apparently, the view of those firms who accept or deliver such opinions is that, in principle, there is no problem with the use of the National Mobility Agreement for straight-forward corporate opinions such as extra-provincial registrations or corporate existence or for securities opinions based on National Instruments. Based on the LawPRO release cited above, it would seem that these types of opinions would be covered by the Law Society mandatory minimum insurance.

These intra-Canadian developments are interesting to note as a reflection of the attempt to eliminate, to the extent possible, intra-provincial barriers to trade and mobility. While they have no direct bearing on either the competence or insurability issues raised by the challenges of advising Canadian clients in their conduct of international or cross-border transactions, they are reflective of the overall global trend towards eliminating restrictions on trade and mobility.
3. Challenges to Canadian Counsel in Negotiating and Drafting Cross-Border Acquisition Agreements

a. Choice of Local Counsel

The choice of local counsel is often one that Canadian clients will leave up to their principal counsel. In the absence of pre-existing relationships with local counsel, referrals should be sought from other lawyers who have previously worked in the relevant jurisdiction.

b. Contract Formation

Until a formal agreement containing a choice of law clause is signed, neither party can rely on the laws of its own jurisdiction to govern issues of contract formation. Therefore, questions may arise as to whether a valid contract is formed under the laws of a particular foreign jurisdiction. In some cultures, a handshake may be sufficient to validate an agreement. Similarly, whether a "letter of intent" or "memorandum of understanding" is a binding contract or merely an agreement to negotiate depends on the rules of contract formation in the jurisdiction of the contracting parties. An agreement is binding at common law if both parties intended their agreement to be legally enforceable, assent has been reached on all of the essential terms of the agreement and all statutory formalities have been satisfied.

c. Enforceability

Generally speaking, purchase agreements entered into by Canadian clients in foreign jurisdictions with vendors in such jurisdictions – whether of shares or assets – will be

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governed by the laws of the local jurisdiction, and the parties will attorn to the jurisdiction of the local courts to adjudicate disputes arising out of the interpretation of the contract or the compliance by the parties with its terms. At the very least, local counsel will need to be retained to review the agreement for its enforceability and to provide any enforceability opinion that may be required on the closing of the transaction. If the Canadian business will be contracting directly using a Canadian entity, Canadian counsel will have to provide the corporate aspects of the closing legal opinion. Aside from the considerations of prudence and professional responsibility that would require Canadian counsel to retain local counsel, the practical necessity of obtaining a legal opinion at closing will provide a check on the Canadian counsel who might otherwise be tempted to act alone.

(i)  

*Governing Law*  

Although generally speaking, purchase agreements entered into by Canadian clients in foreign jurisdictions will be governed by the laws of the local jurisdiction, in some situations an issue may arise as to which law is chosen as the governing law of the contract. In jurisdictions where the legal system is insufficiently sophisticated to deal with complex transactional or commercial agreements, the governing law should be that of a jurisdiction with a more hospitable legal system and a close relationship to that jurisdiction in which the transaction is being conducted. For example, English law would be the appropriate law where transactions are conducted in former colonies or possessions of the United Kingdom and United States law may be appropriate for transactions in Central or South America.

If the governing law is not addressed in the contract it will be left to conflicts of law rules to determine which law governs the contract. Under our law, deference is given first to
the contractual choice of the parties, then to the implied choice of the parties and finally to the proper law of the contract. In some areas of law the proper law of the contract is predetermined. For example, in dealings with real property the governing law is the place where the property is located. In other areas, however, the test for the proper law of the contract is the "closest and most substantial connection" test enunciated in *Imperial Life Assurance Co. of Canada v. Colmenares.*² The closest and most substantial connection is determined by looking at a number of factors including the place of the contract, the place of the performance of the contract, the place of business of the parties and the nature and subject matter of the contract. The opinion of local counsel will be required as to the validity of the choice of law clause in the foreign jurisdiction.

(ii) *Jurisdiction and Enforceability of the Contract*

If enforceability is at issue counsel may wish to consider use of an exclusive jurisdiction or forum selection clause. Traditionally, exclusive jurisdiction or forum selection clauses have been viewed negatively by Canadian courts. However, there has been a change over time in the Canadian judicial acceptance of such clauses, culminating in the Supreme Court of Canada's decision in *Z.I. Pompey Industrie v. ECU-Line N.V.*, where Justice Bastarache, writing on behalf of the Court, stated:

> [Forum selection] clauses are generally to be encouraged by the courts as they create certainty and security in transaction, derivatives of order and fairness, which are critical components of private international law... In the context of international commerce, order and fairness have been achieved at least in part

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by application of the "strong cause" test. This test rightly imposes the burden on the plaintiff to satisfy the court that there is good reason it should not be bound by the forum selection clause. It is essential that courts give full weight to the desirability of holding contracting parties to their agreements.\(^3\)

Accordingly, Canadian courts will generally give effect to exclusive jurisdiction or forum selection clauses unless the party challenging the clause can show "strong cause" for not doing so.

(iii)  **Dispute Settlement**

One way to reduce the risks associated with the enforceability of a contract made in a foreign jurisdiction is to agree to submit the dispute to arbitration. Arbitration has become the preferred dispute settlement provision in international business agreements. The benefits of arbitration include the ability of the parties to customize the process, the confidentiality of the arbitration process and the 1958 New York *Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, (the "Convention") signed by more than 100 States. The law in Alberta governing arbitrations is the *International Commercial Arbitration Act* (Alberta) (the "ICAA"), which incorporates the UNCITRAL Model Law on International Commercial Arbitration (the "Model Law"). To give force to an arbitration clause, there must be an express section, in writing, setting out the agreement to arbitrate either in the form of an arbitration clause or a separate arbitration agreement. The arbitration agreement is treated, pursuant to the ICAA and Model Law, as an agreement independent of the other terms of the contract and may

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survive if the contract is null and void, so long as there is a basis for arguing that an agreement was formed with respect to arbitration.

Article 34 of the Model Law provides limited reasons for when a court may grant recourse against an arbitral award:

An arbitral award may only be set aside if:

(a) the party making the application furnishes proof that:

(i) a party to the arbitration agreement was under some incapacity or the agreement is otherwise invalid;

(ii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceeding;

(iii) the award deals with a dispute not contemplated by the submission to arbitration or contains decisions on matters beyond the scope of the submission to arbitration; or

(iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with the provision of this Law from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Law; or

(b) the court finds that:
(i) the subject matter of the dispute is not capable of settlement by arbitration under a law of this State, or

(ii) the award is in conflict with the public policy of the State.

However, the finality of an arbitral award depends on the jurisdiction and, accordingly, the choice of governing law will influence the enforceability of the arbitral award. In China for example, arbitration awards are not open to review whereas in other countries the courts will readily review an award for errors in law. The position in Canada appears to be well captured in the following citation from Quintette Coal Ltd. v. Nippon Steel Corp. In dismissing an appeal from a judgment dismissing an application to set aside an arbitral award, Justice Gibbs of the British Columbia Court of Appeal stated:

The "concerns of international comity, respect for the capacities of foreign and transnational tribunals, and sensitivity to the need of the international commercial system for predictability in the resolution of disputes", spoken of by Blackmun, J. [of the Supreme Court of the United States in Mitsubishi Motors Corp. v Soler Chrysler-Plymouth, Inc., 473 US 614 at 629 (1985)] are as compelling in this jurisdiction as they are in the United States or elsewhere.

In addition to the need for a local view on the overall enforceability of the agreement, and the possible requirements for a closing legal opinion on the enforceability of the agreement pursuant to the governing local law, input from local counsel will be required with respect to many of the particular provisions of the purchase agreement because of the specialized

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4 Klotz, supra note 1 at 289.

or regulated nature of their subject matter. The following portions of this paper will review some of the key provisions of purchase agreements that will require such advice.

4. **Negotiated Purchase Agreements**

All commercial lawyers with any degree of practical experience in foreign jurisdictions will know that agreements governing negotiated purchase transactions are remarkably uniform across jurisdictional boundaries. This uniformity is driven primarily by the very nature of the subject matter of these agreements, and is reinforced by the advancements in technology that have reduced the world, in general, and the practice of commercial law, in particular, to a global village. As a practical matter, every purchase agreement must, of necessity, deal with the same issues, namely: the subject matter of the transaction (assets or shares), including a legally accurate description of such subject matter; the consideration to be paid for the assets or shares; the manner in which the consideration is determined, quantified, adjusted and paid; the liabilities, if any, to be assumed (on a asset purchase transaction in particular); and any expenses to be allocated between the parties. The contractual provisions relating to these matters tend to be substantially identical across the jurisdictional divide as their contents are determined primarily by commercial, rather than legal, factors.

Purchase agreements will always contain representations and warranties provided by both vendor and purchaser, generally with far more extensive representations and warranties being provided by the vendor with respect to the title, state and quality of the business and/or assets that are subject to the sale. The nature, substance and extent of the parties' representations and warranties will be driven principally by commercial considerations and will be designed primarily to address the major risks associated with the particular assets or business being
acquired, modified to reflect the relative bargaining strengths of the parties and the commercial practice and custom in the relevant jurisdiction. While partially informed by the legal idiosyncrasies of each jurisdiction, these factors, for the reasons mentioned above – primarily the globalization of the marketplace and the uniformity of legal practice that results therefrom – play a lesser role in the determination of the scope and content of the parties' representations and warranties.

Contractual rules governing the behaviour of the parties during the hiatus between the date on which the purchase agreement is signed, and the date on which the transaction is closed, will generally be codified through covenants of both parties that will apply during that period of time. The scope and content of these covenants, like the other principal provisions of the purchase agreement, will similarly be determined primarily by commercial factors. The same consideration applies to those provisions of the purchase agreement that govern the logistics and conditions of closing.

The one element of the pre-closing covenants and closing conditions that will vary between jurisdictions will be the identity of the particular regulatory consents, approvals or filings that will be required to be obtained in each jurisdiction prior to, and as conditions of, closing. However, the subject matter of such consents, approvals and filings, such as anti-trust or competition filings or consents, securities filings or consents, registrations or filings required to perfect security interests, etc., will generally be substantially similar and can generally be anticipated in principle, if not in the precise details, by experienced Canadian counsel.

Finally, the content and scope of the indemnity provisions of a negotiated purchase agreement, pursuant to which each party indemnifies the other for damages incurred as
a result of the indemnitor's breach of covenant or representations and warranties or for damages resulting from pre-closing (in the case of the vendor) or post-closing (in the case of the purchaser) conditions or events, will reflect the nature of the subject matter of the agreement, the relative bargaining strength of the parties, and only to a much lesser extent, the idiosyncrasies of local law and practice. (For example, the size of the indemnity and the extent of the "caps", thresholds and "tipping baskets" may vary slightly as a matter of practice between jurisdictions.)

Based on the foregoing summary overview of the subject matter of negotiated purchase agreements, one can begin to understand how an experienced Canadian counsel may effectively advise a Canadian client in the negotiation of such agreements, even when the agreements relate to foreign business acquisitions and are governed by foreign law. Given that the considerations which inform such negotiations are primarily commercial, the utility of a lawyer to his or her client will be driven much more by the lawyer's experience than by his or her knowledge of the local law. However, it is important that the Canadian counsel remain particularly sensitive to those contractual provisions that are more likely to be impacted by the non-Canadian law and that will require the input of foreign counsel. The ensuing portion of this paper will discuss some of those provisions.

a. Subject Matter

Generally speaking, the portion of a purchase agreement that deals with the subject matter of the acquisition will refer either to the assets (most of which will be described in schedules) or the relevant shares or other securities that are subject to the sale. In the case of a purchase of shares or other securities, it is always important to review carefully the description of the shares or other securities with local counsel to ensure that it accurately reflects the relevant
shares or securities, as they are described in the articles or other constating documents of the acquired corporate or other entity or in any other document that creates the relevant securities (e.g., a note indenture). Moreover, the advice of local counsel should be sought with respect to any restrictions on the transferability of the shares or other securities and with respect to any other contractual, statutory, common law or other restrictions on, or conditions that apply to, the transfer of the shares or securities or that otherwise encumber the ability of the vendor to effect the transfer.

Moreover, in the case of an asset purchase, local law may require certain acquired assets to be defined or described in a particular manner and it is important to ensure that local counsel has reviewed and is satisfied with the accuracy of the definition or description. For example, if intellectual property licences are to be included in the acquired assets (or assumed liabilities), it would be important for local counsel to review the description of the intellectual property licences to ensure its accuracy as well as its conformity to any aspects of local law that may impact on that description and/or other aspects of those licences, such as transferability.

b. Purchase Price

As noted above, the contents of the purchase price section of a purchase agreement are generally dictated by commercial – and not legal – considerations. However, local practice may differ from Canadian practice regarding the manner in which the purchase price may be adjusted and how the adjusting reviews or audits are to be conducted. Moreover, to the extent that the adjustment language reflects an application of accounting principles, advice should be sought from either local counsel, or perhaps more appropriately, the local office of the client's auditors (or local auditors in the event that a client is not using one of the international
auditing firms) to ensure that a description of any accounting principles or terms (e.g. description of inventory, goodwill, depreciable assets, etc.) that will impact on the price adjustment is accurately reflected in the purchase agreement and that the procedure set out in the agreement for conducting audits and valuations of the acquired assets is consistent with local practice.

In addition, to the extent that the purchase price includes shares or other securities, the advice of local counsel as to the proper description of such shares or securities and as to any issues regarding the transferability of such shares or securities will be required, just as it would be where the shares or securities are the subject matter of the acquisition.

Similarly, to the extent that the price or economic cost of the transaction involves the assumption of the vendor's obligations and/or liabilities (which may include encumbrances, governmental permits, environmental liabilities or lease obligations) such assumed obligations and liabilities may be creatures of local law and thereby affected, both in their description and substance, by the vagaries of such law. While the initial drafts of a purchase agreement prepared by Canadian counsel will more often than not "get it right", one is compelled to rely on the advice of local counsel in ensuring that no obligation or liability is improperly described and assumed and that any protection that would otherwise be available to a Canadian purchaser is not lost because of Canadian counsel's ignorance of local law and practice. This consideration is particularly relevant to the transfer of licences and government permits, the assumption of mortgages or other forms of security and the assumption of liabilities that are subject to local statutory regulation, such as environmental liabilities, or that are themselves the creatures of such regulation, such as tax liabilities.
If a Canadian business is selling assets to a foreign purchaser, the financial risk associated with any currency fluctuations that may arise can be mitigated by ensuring that payment is made in Canadian or U.S. dollars or Euros. Letters of credit can be used to reduce the risk of non-payment and risk of non-enforcement associated with international purchase agreements. The use of a letter of credit substitutes the credit of the purchaser's bank for that of the purchaser. Its usefulness in business transactions is based on the principle of the autonomy of the credit. Regardless of any subsequent dispute between the parties, the bank that issued the letter of credit to the purchaser is obliged to pay upon receipt from the vendor of the requisite documentation. The only circumstance in which a letter of credit will not be honoured is where a fraud has been perpetrated by the beneficiary of the credit and the fraud has been brought to the knowledge of the bank before payment.  

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**Bulk Sales Law**

While most Canadian jurisdictions have discarded their bulk sales rules which require creditor consent to a "sale in bulk" asset transaction, this is not the case in many foreign jurisdictions. Accordingly, the advice of local counsel must be obtained as to the proper description of any applicable bulk sales rules and as to the conventional practice adopted by commercial parties in the relevant jurisdiction for dealing with such restrictions. (Such practices can include obtaining judicial or statutory exemptions, contractual indemnities and waivers or other mechanisms for addressing the potential liabilities created by bulk sales legislation).

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**d. Tax Issues**

Many jurisdictions impose transfer taxes on the transfer of real estate and other specified classes of assets. It is critical, in preparing any agreement governing the acquisition of a foreign business, that local tax counsel or other tax advisors review the purchase agreement with a view to advising on all transfer taxes that may apply to the transaction and as to the local commercial practice in allocating liability for such taxes between the parties.

The variety of tax regimes globally will encourage Canadian businesses entering into transnational business relationships to structure their foreign investments and transactions in a manner that utilizes tax efficiencies to maximize returns. For example, consider the following hypothetical situation. A partnership, established in the United States with a Canadian partner and a U.S. partner, receives funds from the Canadian partner and invests in assets within the United States. The income earned by the partnership is subject to U.S. tax but if the net after tax return is distributed to the Canadian partner who then, under Canadian tax law, claims a foreign tax credit in respect of the U.S. tax paid, the Canadian partner will not be taxed on the distribution received by it. In addition, under U.S. tax law, the U.S. partner is entitled to deduct the distribution paid to the Canadian partner and thereby in effect receives a tax refund.

The advice of local counsel is crucially important to help structure the transaction in the most tax efficient manner. The same transaction can produce different effects in two jurisdictions as a result of differing characterizations. Take for example a situation where a Canadian company enters into an acquisition agreement to acquire goods from an American company. The deal may be structured such that for Canadian tax law purposes the Canadian company is viewed as the owner of the goods and therefore entitled to claim capital cost
allowance. For United States tax purposes the transaction is viewed as a lease from a U.S. company and therefore the U.S. company is also entitled to claim capital cost allowance.

e. **Representations and Warranties**

As noted above, most representations and warranties will reflect the risks associated with the particular assets or business being acquired. Therefore, Canadian counsel with knowledge of his or her client's business, risk tolerance and negotiating leverage, and with prior experience in acquisitions of this nature, will be in the best position to draft and negotiate the representations and warranties on behalf of the Canadian client. However, in preparing the representations and warranties, Canadian counsel will require input from local counsel as to legal matters which will have an impact on such representations and warranties, and as to conventional practice in the local jurisdiction which may inform the bargaining approach of the local party to the transaction.

(i) **Status**

By way of example, in an acquisition by a Canadian purchaser of the shares of a foreign corporation, local counsel's input will be important in assisting the purchaser's Canadian counsel in preparing the representations and warranties as to the due organization, existence and good standing of the foreign corporation and the appropriate representations and warranties to be obtained in connection with the qualification of the corporation to do business in the foreign jurisdictions in which it conducts its business. In both share and asset purchase transactions, the appropriate language of the title representation will be prepared or reviewed by local counsel. In my experience, as a general matter, the format used in Canadian precedents can be applied, almost without revision, in most foreign transactions, but that format may require some
modification from jurisdiction to jurisdiction based on legal advice as to local practice and terminology.

(ii) **Permits, Licences and Filings**

Local counsel's input will be important in determining the identity, nature and proper description of any approvals, permits and licences required to be obtained, or filings required to be made, under local law to enable the transaction to be effected in the manner contemplated in the agreement, and the issues that should be addressed in any representations and warranties concerning such approvals, permits, licenses and filings.

(iii) **Securities and Competition Filings**

Although most Canadian transactional lawyers are familiar with the securities and competition filings required in the United States it is imperative that U.S. counsel be retained to advise on and effect such filings.

Under the United States *Hart-Scott-Rodino-Anti-Trust Improvements Act* ("HSR"), parties or transactions that meet certain minimum thresholds must comply with the reporting requirements and wait at least 15 to 30 days before completing any asset transfer. During this period the Department of Justice's Antitrust Division will review the transaction for anti-competitive effects in the United States market. If the transaction qualifies for reporting, failure to comply may result in civil penalties of up to US$16,000 per day. Three criteria must be met for HSR to apply. First, the transaction must affect commerce in more than one state or with another country. Second, one party must have total assets or annual net sales of at least US$126.9 million and the other party must have total assets or annual net sales of at least
US$12.7 million. Third, as a result of the transaction, the acquiring person must hold an aggregate amount of stock and assets of the acquired person valued at more than US$63.4 million. HSR will apply regardless of the foregoing in transactions where the aggregate amount of stock and assets acquired is valued at more than US$253.7 million.

In Europe, the Merger Regulation (Council Regulation 139 of 2004) (the "Merger Regulation") gives the European Commission the exclusive power to investigate mergers and acquisitions with a "community dimension". Mergers or acquisitions in which the combined aggregate worldwide turnover of all the entities concerned is more than Euro 5,000 million and the community turnover of each of at least two of the entities is more than Euro 250 million must be notified to the commission for approval, unless each of the entities concerned achieves more than two-thirds of its aggregate community turnover in one and the same member state. Mergers and acquisitions below these thresholds, along with those that meet the two-thirds rule, remain in the exclusive jurisdiction of the member states.

(iv) Property and Encumbrances

The description of title to real estate and the encumbrances thereon, including the description of any encumbrances that ought to be assumed as "Permitted Encumbrances", will similarly require input from local counsel. Canadian counsel can continue to lead the negotiation as to the scope and intensity of the representations and warranties as to title, as a commercial matter, based on the purchaser's risk tolerance, the practice, the industry and the relative negotiating leverage of the parties. However, the scope and definition of the encumbrances, and the agreement as to which encumbrances should properly be assumed, will be informed by local law, custom and practice.
(v) **Employees and Employee Benefits**

Canadian counsel would be well-advised to delegate totally to local counsel the area of employment benefits regulation which, especially in United States jurisdictions, is a complex area of regulated federal law practised by highly specialized counsel. This also applies to any acquisition of a business whose employees are unionized. In such a case, the negotiation of the provisions related to the assumption of collective bargaining agreements and the associated representations and warranties should be with the exclusive purview of specialized labour counsel, subject to instruction as to business issues by the client with input of Canadian counsel only to the extent the client desires such input.

(vi) **Environmental/Intellectual Property**

While environmental and intellectual property issues are also generally the subject of specified regulation in every jurisdiction, Canadian counsel can play a significant role in negotiating the provisions regarding these issues, because the nature of the risks, and the substance of the relevant legislation, is often virtually identical across jurisdictions. Although local input is critical in ensuring that the particular rules of the local regulatory regimes are reflected, and the relevant assets, liabilities and risks are accurately described, Canadian counsel with experience in these areas, and in acquisitions generally, will be competent to advise the Canadian client on the manner in which the risks can best be allocated on a basis acceptable to the client, based on such counsel's understanding of the legal and practical risks involved, and his or her understanding of the client's risk tolerance. However, the registration of intellectual property with the appropriate local regulator should be left to local intellectual property counsel.
f. **Covenants**

Generally, where an acquisition transaction involves a delay between execution of the purchase agreement and closing, there will be covenants that govern the behaviour of the parties between those two dates. These covenants may deal with, among other matters, the conduct of the business during the period, the access of the buyer to the premises of the acquired business, the treatment of employees, the obtaining of third party consents and regulatory compliance and environmental matters, such as the conduct of environmental investigations.

The manner in which these issues will be addressed will be strongly influenced by the risks associated with the conduct of the business by the vendor during a period in which the economic result of such conduct may directly accrue to the purchaser (if the effective date of the transaction precedes the closing date) or may, at the very least, have a significant effect on the acquired business from and after the closing date. As a result, the purchaser will have a strong commercial interest in monitoring, if not controlling, the conduct of the business during that interim period. This is a purely commercial concern with which Canadian counsel to the purchaser will be familiar. That counsel will therefore be best able to negotiate the terms of these interim period covenants without much substantive input from local counsel. Local counsel's input will be necessary to advise on any particular regulatory compliances which must be addressed during the interim period (e.g., the consents, permits, licences and approvals that must be obtained, and the filings that must be made, so that the purchaser can continue to operate the business from and after closing). In addition, local advice will be necessary in drafting and negotiating the covenants of the parties as to the allocation of liabilities that arise under any highly regulated regimes, such as tax or employee benefit legislation and regulations.
The full description of the procedure to be adopted by the parties in respect of the allocation of environmental risk (e.g., the conduct of various environmental investigations and the allocation of liability to address the conditions identified by such investigations) can be negotiated primarily by Canadian environmental counsel with input from local counsel to address the particularities of local legislation.

g. Logistics and Conditions of Closing

The logistics of closing are virtually uniform in all jurisdictions and, except for the regulatory consents and filings that are particular to a given jurisdiction, will not need much input or review by local counsel and can be negotiated fully and virtually exclusively by Canadian counsel.

h. Indemnities

As a general matter the cross indemnities of vendor and purchaser are the result of a commercial negotiation that is informed, only to a minor extent, by local law and practice, such as any applicable statutes of limitation or other prescription periods that may affect the survival periods of the various indemnities. However, the fundamental deal issues associated with any indemnity, which generally concern the survival period of the indemnity, the appropriate threshold of damages that must be incurred before the indemnitee can assert a claim against the indemnitor, and the maximum aggregate liability that an indemnitor will have pursuant to its indemnity (i.e., the "cap" on the indemnity) are all commercial matters. Experienced Canadian counsel, with knowledge of the business and understanding of the relative bargaining power of the parties, will be in a good position to advise the Canadian client as to such matters.
i. **Summary Regarding Cross Border Purchase Agreements**

Based on the foregoing overview, Canadian counsel has a very significant – but not exclusive – role to play in advising Canadian clients who pursue business acquisitions in foreign jurisdictions. However, it would be nothing short of professional negligence for a Canadian lawyer to attempt to pursue any such acquisition in the absence of competent local legal assistance. Most business acquisitions are driven fundamentally by commercial considerations and experienced counsel with knowledge of the client and its business will be in the best position to advise the client on acceptable risks and the appropriate resolution of risk allocation issues that arise in negotiated acquisitions transactions. However, that counsel will inevitably require the input of its foreign counterpart to ensure, at the very least, that technical aspects of the transaction governed by local law are properly addressed and that local practice is considered when negotiating otherwise "standard" provisions.

In preparing agreements in U.S. jurisdictions, it is especially helpful to resort to the model share and asset purchase agreements prepared with commentary by the Negotiated Acquisitions Committee of the American Bar Association's Business Law Section as a helpful starting point in understanding the American approach to these transactions and the suggested resolution of issues that may arise in their negotiation.

5. **Financial Assistance Provided by Foreign Affiliates of Canadian Businesses**

a. **The Requirement for Foreign Affiliate Financial Assistance**

In the course of establishing an international presence, Canadian business entities will generally conduct their businesses in foreign jurisdictions through legal entities formed
under the laws of those jurisdictions. Creditors of a business entity formed in any given jurisdiction may reasonably want to look at the assets of the global enterprise to satisfy the debts being incurred, especially where credit is being made available to newly formed entities in those foreign jurisdictions. To that end, creditors will seek credit support by way of guarantees or other financial assistance agreements from entities affiliated with their principal debtor. Such entities will, by the very nature of the international enterprise, be found in many different jurisdictions.

One of the anomalies I have encountered in acting for Canadian-based multinational enterprises, is the radical distinction between the laws regulating financial assistance in Canada and the comparable laws in other jurisdictions. This dichotomy in the treatment of financial assistance presents interesting challenges in the preparation and negotiation of guarantees and other financial assistance agreements involving multi-jurisdictional businesses.

b. The Canadian Position Regarding Financial Assistance Provided by Affiliate

Under Canadian corporate law, the financial restrictions that formerly limited the ability of Canadian corporations to provide guarantees for the indebtedness of their parents or other affiliates have been repealed and replaced, in the case of the Business Corporations Act (Alberta) by a disclosure requirement (Section 45 of the ABCA) that applies only to financial assistance provided to a prescribed category of persons that includes shareholders of affiliates of the financial assistance provider or associates of such prescribed category of persons. The Canada Business Corporations Act contains no restrictions, procedural or substantive, on the provision of financial assistance.
While Canadian common law restrictions relating to the exercise by a board of directors of its fiduciary obligations to the corporation may continue to be applied on a factual case-by-case basis to restrict the provision of guarantees or other financial assistance in certain relatively narrow circumstances, the elimination of the legal restrictions formerly contained in Canadian corporate statutes has removed the most fundamental barriers that previously prevented Canadian-based corporations from providing guarantees or other financial assistance to related entities.

c. The U.S. Regime

Unfortunately, the liberal Canadian position has no apparent equivalent under the laws of any of the major foreign jurisdictions in which Canadian companies are likely to carry on business. By way of example, under applicable United States law, the enforceability of upstream guarantees by subsidiaries will be tested under the United States Bankruptcy Code as well as under State-enacted laws such as the Uniform Fraudulent Conveyance Act (the "UFCA") and the Uniform Fraudulent Transfer Act. Guarantees provided by a United States subsidiary of the liabilities of its parent – including its Canadian parent – may be rendered unenforceable under the Bankruptcy Code if the guarantee is an obligation incurred by the guarantor at less than a "reasonably equivalent value" at a time when the guarantor was insolvent, or rendered insolvent, by incurring the obligation under the guarantee. Similarly, under the UFCA the test is whether the guarantee was incurred "without a fair consideration" and the mere fact that a subsidiary is a wholly-owned subsidiary does not provide a safe harbour for its enforceability as it would have even under the previously more restrictive Canadian legislation.
d. **English Rules**

The financial assistance provisions under English law were recently repealed and replaced by the *Companies Act 2006*. The principal effect of the changes, which came into effect on October 1, 2008, is that private companies are no longer prohibited from giving financial assistance for the purpose of the acquisition of their shares (or the shares of their private company parent). The "whitewash procedure" for private companies was also repealed. However, subject to some exceptions, it remains unlawful for a public company to give financial assistance using the assets of the subsidiary "for the purpose" of acquiring the shares of that subsidiary, either concurrently with the acquisition or after the acquisition in order to redeem or discharge a liability incurred for the purpose of the acquisition.

So, for example, under English law, where financial assistance is provided, not for the purpose of an acquisition, but merely as an incidental part of a larger purpose of the company and is given in good faith or, where the principal purpose in giving the assistance is not to reduce a liability incurred for the purpose of acquiring the shares but is an incidental part of a larger purpose and given in good faith, the guarantee can be saved.

The consequences of violating the prohibitions against unlawful financial assistance in England are grave. Unlawful financial assistance is a criminal offence and a company found to be in violation of such rules, and any of its officers in default, are liable to a fine and/or imprisonment. Moreover, a transaction entered into in breach of the financial assistance restrictions can be void and any guarantee or security given is unlikely to be enforceable.
e. **Continental Europe**

The comparable legal regimes in continental Europe present even greater challenges to the enterprise of supporting liabilities through a leveraged acquisition of assets or shares. In France, for example, companies may only use their assets and credit in their own corporate interest or in the corporate interests of the corporate group to which they belong. Directors who authorize corporate actions in breach of this principle may not only be held personally liable civilly towards the company or its creditors, but may also be subject to criminal prosecution for misuse of corporate assets. In my experience with acquisitions in France, French counsel have consistently taken the view that upstream guarantees provided by French companies in connection with their acquisition by foreign companies could, if made "without true and sufficient consideration", be considered to be against the corporate interests of the French company given the potential exposure to increased financial risks without the provision of comparable economic benefit.

Similarly, in Italy, Germany and Switzerland, the validity of the guarantee or other financial assistance will be analyzed on a stand-alone basis, without regard for the similar cross-guarantees provided in favour of the locally incorporated company by the foreign affiliates of that company. If, on the basis of that simple analysis, the contingent liability assumed by the local company exceeds its assets in any material way, the guarantee may be declared void by a court and directors who approved it may be subject to extensive civil, regulatory and occasionally criminal liability.
f. **Impact on Cross Border Financings Entered by Canadian Corporations and their Foreign Affiliates**

The disparity in approach to the enforceability of financial assistance agreements requires Canadian counsel involved in the preparation and negotiation of such agreements to consider the impact of these restrictions on the foreign affiliates of a Canadian business entity in negotiating the terms of "standard form" guarantees that are intended for use by all affiliates of the Canadian business world-wide (e.g., the form of subsidiary guarantee negotiated in any credit facility intended for use by the borrower in financing all of its operations, including those outside Canada).

g. **Drafting Solutions**

The following are some of the drafting approaches that can be adopted to address these restrictions:

(i) include in the guarantee a limitation on the liability of the subsidiary guarantor to "such maximum amount that can be incurred without rendering the guarantee, as it relates to the guarantor, avoidable under any mandatory and non-waivable provisions of applicable law relating to fraudulent conveyance or fraudulent transfer and not for any greater amount" which should address the enforceability issue under the United States fraudulent conveyance/fraudulent transfer restrictions;

(ii) provide, where necessary, (and this would apply under the applicable financial assistance rules in certain jurisdictions in continental Europe) that the guarantee is capped at a maximum amount;
(iii) provide for a cross-indemnity by the parent or other affiliates of the foreign guarantor so that the foreign guarantor is indemnified by the parent or such affiliates for any liability that it may incur in excess of the maximum liability imposed on it under applicable local law;

(iv) clarify in the guarantee that it is joint and several to all other guarantees provided by all other affiliates of the principal obligor;

(v) provide in the guarantee for guarantee fees or other similar features that enhance the arms' length nature of the guarantee; and

(vi) ensure that the terms on which the foreign guarantor can access the financing which creates the liability of the subject of the guarantee is better than the terms that it could otherwise negotiate on a stand-alone basis in the foreign jurisdiction (this may enhance the enforceability of the guarantee in certain continental European jurisdictions).

**h. Conclusion**

Canadian counsel advising clients who are acquiring or establishing businesses in foreign jurisdictions that will involve the provision of inter-corporate financial assistance must be attuned to the radical distinction between the treatment of such financial assistance under Canadian law and most foreign legal systems, and must ensure that guarantees that are negotiated with Canadian creditors, in particular, and intended for global use, can be adapted to reflect the restrictions imposed on financial assistance by those foreign jurisdictions.