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Ontario Court Decision Highlights Importance of Termination Rights in Bought Deal Letters

By Toby Allan and Dan Shea

A recent decision of the Ontario Superior Court in *Stetson Oil & Gas Ltd. v. Stifel Nicolaus Canada Inc.*¹ highlights the importance of including termination rights in bought deal letters and other engagement letters used in capital markets transactions.

The case involved Stifel Nicolaus Canada (then Thomas Weisel Partners) refusing to close a private placement of subscription receipts after executing a bought deal letter with Stetson Oil & Gas Ltd. in July of 2008.² Following an unsuccessful marketing process, Stifel refused to proceed with the transaction, including failing to negotiate a definitive underwriting agreement.

The bought deal letter contained the following customary condition (the "**underwriting agreement condition**") that Stetson and the underwriters negotiate in good faith an underwriting agreement containing certain standard termination rights:

The definitive terms of this agreement will be governed by a formal underwriting agreement to be entered into prior to closing of the purchase by Thomas Weisel (the "Underwriting Agreement") in respect of the Offering. The Underwriting Agreement will be negotiated in good

¹ 2013 ONSC 1300.

² Although the court and this article refer to the engagement letter as a "bought deal letter", the deal was a private placement and, accordingly, did not involve the bought deal procedures under National Instrument 44-101.

faith between the Company and Thomas Weisel, on behalf of the Underwriters, and will contain ... termination provisions (including, without limitation standard "due diligence-out", "disaster-out", "material adverse change-out" , and "regulatory-out" rights) customary in agreements of this type ... (Underlining Added.)

The termination rights were not, however, specifically included in the bought deal letter itself.

After confirming the bought deal letter established a binding obligation on Stifel to close the transaction, the court considered whether any termination rights were available to Stifel. Focusing on the absence of termination rights in the bought deal letter and the failure to negotiate and execute a definitive underwriting agreement, the court concluded that the termination rights referenced in the underwriting agreement condition were not available to Stifel. In other words, the mere reference to the termination rights in the underwriting agreement condition was not sufficient to permit Stifel to rely on them absent the execution of a definitive underwriting agreement actually containing the termination rights.

This decision serves as a useful reminder of the importance of specifically including termination rights in bought deal letters and other forms of engagement letters to ensure underwriters have flexibility to terminate or renegotiate transactions if the events covered by the agreed-upon termination rights arise prior to execution of a definitive underwriting agreement.

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