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When to pay your financial advisors

By Neill May

Getting paid for doing nothing is a classic dream. Sure, maybe it's not spiritually fulfilling, and there's not yet a Nobel Prize for it, but there are some pretty obvious advantages to being compensated for doing nothing. For the young and unambitious, it's "Freedom 25." In fact, at an earlier age, I would have ranked payment for nothing high on my bucket list, along with having my name mean something in common parlance ("He's sort of charming, I suppose, but he can't Neill a party") and/or having my superpower be the ability to think of the perfect comment five minutes earlier when it would have been funny.

The issue of an unclear connection between a claim for payment and services rendered was at the heart of the recent Ontario Superior Court of Justice decision in *RBC Dominion Securities Inc. v. Crew Gold Corporation*. The case involved a financial services arrangement with relatively typical terms, including a success fee component and a "tail" fee feature (pursuant to which the success fee is payable if the triggering event occurs within a short period following termination of the agreement), though the facts of the case were somewhat unique.

It started when Crew Gold retained RBC to advise the company concerning strategic alternatives. RBC's advice to the company's board outlined strategic choices that generally involved some form of *en bloc* sale of shares, the disposition in whole or part of Crew's assets or some form of strategic partnership. Meanwhile, the company completed a restructuring pursuant to which Crew's debenture holders were issued shares representing 95 per cent of Crew's outstanding equity in exchange for their debt (with one debenture holder, GLG Partners, receiving shares constituting almost 32 per cent).

RBC continued to advise Crew. Notably, both RBC and Crew believed that any purchaser for GLG's 32-per-cent position would need to deal with Crew (for example, to undertake due diligence), which could be used by the company as leverage to protect its strategic objectives. They were mistaken. Endeavour Financial Corp. (which has not been on RBC's proposed list of purchasers for Crew stock) purchased the GLG position and that of another investor, totalling approximately 38 per cent of Crew's outstanding shares, without dealing with the company. After Crew terminated its agreement with RBC, there was a contest between Endeavour and OAO Severstal to increase their respective stakes in Crew shares. Ultimately, Severstal increased its shareholdings to just more than 50 per cent, with Endeavour holding approximately 43 per cent. Endeavour then sold its remaining interest in Crew, and Severstal acquired the rest of the Crew shares under a plan of arrangement. With the exception of the arrangement, all of the acquisitions were done in the secondary market without any involvement by Crew.

RBC claimed a success fee on the basis of the language of its engagement letter, which entitled it to the fee on completion of a "transaction" that was very broadly defined to include, among other things, any investment by a third party that results in a change of control and any sale of all or a substantial portion of the Crew shares, during the term of the engagement or in the year following termination. The agreement did not expressly require that RBC be involved in the transaction to be entitled to payment.

The court found in favour of Crew, interpreting the contract to reflect the parties' intention that the financial advisor be entitled to a success fee only in the event of a transaction that was connected to the financial advisory services provided. The court concluded that there had to be some causal link between its activities and the transaction that was completed.

The logic generally expressed for the breadth of financial advisory engagement letters is that neither the issuer nor the advisor can foresee or control the future or how transactions might unfold (or not). Sometimes, the benefits of the financial advisory work may not tie in in obvious or direct ways to the ultimate outcome; and on other occasions, the outcome may frustrate what the parties had sought to accomplish.

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I cannot predict the future either (if I could, I wouldn't need the referenced superpower as I could plan my humorous comments in advance), but I expect it's safe to assume that the result of this decision will be some clarifying expansionary drafting changes to forms of financial advisory engagement letters. Some of this drafting may be genuinely clarifying, and some of it will foreseeably be, to some degree, repetitive, redundant, superfluous, unnecessary, verbose and tedious; you know, really Neilling it up. **CL**

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