

# **Confidentiality Agreements Fully Explained...But Don't Tell Anyone**

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**Goodmans<sup>LLP</sup>**

# Our Panelists

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Gesta Abols

Gesta Abols is a partner and counsels clients regarding mergers and acquisitions, securities offerings and business restructurings. Gesta graduated with First Class standing from Queen's University with a B.A. (Hons.) in economics. While studying for his J.D. at the University of Toronto, Gesta was awarded the Lionel Schipper Q.C. prize in advanced business law.

Gesta is a regular speaker at industry and professional conferences and has authored or contributed to a number of articles and surveys on mergers & acquisitions and corporate finance.



Neil Sheehy

Neil Sheehy is a partner in the Securities and Corporate Law Group at Goodmans. Neil's practice focuses on domestic and international mergers and acquisitions, corporate finance and private equity transactions. Neil has represented a broad range of clients on cross-border transactions in which he acts for clients purchasing or selling businesses in Canada as well as for issuers undertaking public offerings of securities in Canada. On an ongoing basis, Neil also advises many Canadian reporting issuers in connection with securities compliance and corporate governance matters.

Neil has delivered lectures on various securities and corporate law matters for the Canadian Bar Association, Insight and Osgoode Hall Law School.

# **Agenda**

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- **Introduction**
- **Key Definitions**
- **Permitted Use**
- **Acknowledgement of Securities Laws**
- **Legally Required Disclosure and Retention**
- **Remedies for Breach**
- **Non-Solicitation of Employees**
- **Standstill Provisions**
- **Term and Other Clauses**
- **Questions**

# Introduction

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- **First step in many commercial/business relationships and transactions**
- **Often in the form of a letter so that discussions begin on a less formal basis**
- **The discloser often prepares the first draft (their counsel or financial advisor)**
- **The recipient of information will want to avoid impractical restrictions and avoid restrictions that can easily result in “foot fault” violations**
- **Not a “one precedent fits all” document**
  - Need to recognize that immediate need for the document may need to apply to future uses (such as a staged transaction process)

# Key Definitions

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- **“Confidential Information” or “Evaluation Material”**
  - Typically very broadly defined and includes any work product that reflects information that could conceivably be provided
  - Consider if the scope ought to be limited or if it should only cover items specifically marked as confidential
  - Common exclusions include information that:
    - Is already in the recipient’s possession (provided that it is not subject to an obligation of confidence)
    - Is or becomes publicly available (other than through a breach of the agreement)
    - Becomes available from a source other than the discloser (provided that it is not subject to an obligation of confidence)
    - Is independently developed
  - If transaction related information is not captured in the definition, then an additional “transaction information” definition may be required

# Key Definitions (cont'd)

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- “Representatives”
  - Sets out the scope of persons with whom the recipient may share information (often on the condition that such representatives are also required to keep such information confidential and that the recipient, in most cases, agrees to be liable for their breach)
    - In certain cases, third party representatives are asked to agree to be bound by the terms of the Confidentiality Agreement
  - Typically includes the recipient’s directors, officers, employees, legal counsel and auditors
    - Consider if affiliates, financial advisors, financing sources (debt or equity) or consultants should be included as Representatives
    - Competition law concerns may require certain information only be shared with the recipient’s advisors
  - Consider if representatives should be restricted by all provisions (including any non-solicitation and standstill provisions) or a more limited set

# Permitted Use

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- **In an M&A situation, the use is generally limited to evaluating a potential transaction “involving”, “with” or “between” the parties**
  - In 2009, the Ontario Superior Court of Justice effectively ruled that RIM could not proceed with its hostile take-over bid for Certicom because the bid contravened the “permitted use” clause of confidentiality agreements between the companies
    - A take-over bid is not technically “between” the bidder and the target (it is made to shareholders)
    - The court ruled that the standstill provision is not a comprehensive code of when the party receiving information can make an unsolicited bid for the disclosing party
    - The standstill provision provides additional protection because the disclosing party does not have to prove that its confidential information is being misused, but the absence or expiry of a standstill provision does not mean that the disclosing party cannot insist that hostile take-over bids made with the benefit of its confidential information be stopped

# Acknowledgement of Securities Law

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- **Prohibition on tipping**
  - Ontario securities laws prohibit a reporting issuer, or any person in a special relationship with a reporting issuer, to inform, other than in the necessary course of business, another person of a material fact or material change before such information has been generally disclosed
- **Prohibition on trading**
  - Ontario securities laws prohibit a person in a special relationship with a reporting issuer to sell or purchase securities of the reporting issuer with the knowledge of a material fact or material change that has not been generally disclosed
    - Note that in the context of a Confidentiality Agreement, the disclosure of certain information to a recipient can create a *de facto* standstill

# Legally Required Disclosure and Retention

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- **Exception to allow disclosure of confidential information as required by law**
  - Consider how broadly “law” should be defined (rules, policies, notices, stock exchange rules, professional / supervisory authorities)
  - Consider what procedural protections the discloser should have:
    - Advance notice of the requirement or request
    - Advice or opinion of counsel confirming
    - Narrowing the scope of the disclosure
    - Agreement to challenge or obtain confidential treatment
  - Consider the legitimate practical concerns of the recipient (and its representatives)
- **Exception to allow the retention of information as required by law or policies**
  - Consider technical challenges of destroying information received electronically and internal document retention policies (whether based on legal requirements or prudent risk management)

# Remedies for Breach

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- **Generally include language that facilitates injunctive relief**
  - Consider if one agrees to the actual remedy or the “seeking” of such a remedy
  - Monetary damages can be difficult to prove or inadequate (for example, breaching a standstill provision with a premium bid)
  - Expense reimbursement (we already have a “loser pays” system) and indemnification provisions less common

# Non-Solicitation of Employees

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- **Prohibition on soliciting (and hiring) employees**
  - Consider:
    - How long should the prohibition last (typically between six months and two years)?
    - To whom should it apply (i.e., the recipient or the recipient and all/some of its representatives)?
    - Who should be covered (i.e., all employees, senior management or those met during the process)?
    - Any reasonable exceptions (for example, general solicitations (including advertisements and search firms), persons who approach on their own initiative, persons whose employment has been terminated)?

# Standstill Provisions

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- **Broad prohibition on acquiring securities or assets, engaging in proxy solicitation, acting jointly with others to purchase securities or other actions that could put the discloser “in play”**
  - Consider:
    - How long should the prohibition last (typically between six months and 18 months)?
    - To whom should it apply (i.e., the recipient or the recipient and all/some of its representatives)?
    - Fall-away provisions?
    - Requirement to “snitch”?
    - MFN provisions (particularly when fall-away provisions are not included)?

# Standstill Provisions (cont'd)

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- **Recent Case Law**

- In 2007, the Ontario Court of Appeal upheld a decision declaring that Sunrise was precluded by its support agreement with Ventas from considering a superior hostile bid submitted by HCP as it was required to enforce its standstills (which clause was not subject to a fiduciary out)
- A recent US federal appeals court decision upheld a \$102 million damage award to Ventas in a related case against HCP
  - From a target's standpoint, be careful what you ask for
  - Subsequent parties to a deal may demand you enforce all standstills

# Term and Other Clauses

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- **Term typically between one and three years**
  - Consider the nature of the information in the context of the term (some information, such as trade secrets, may warrant longer protection)
  - In certain situations, lesser terms may be warranted
  - Ensure term of agreement does not get confused with term of specific clauses like non-solicit or standstill provisions

# Term and Other Clauses (cont'd)

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- **Other important clauses to consider:**
  - Choice of law/forum
  - Privilege
  - No representations and warranties
  - No obligation to transact
  - Point person and other restrictions on communications (including customers and suppliers)
  - Entire agreement
  - Assignment and waiver
  - Counterparts

# Questions?

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