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Termination Provisions in Securities Offerings – Impacts of COVID-19

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The increasing global spread and uncertainty of the COVID-19 pandemic has produced significant legal consideration of force majeure clauses and the law of frustration as they relate to commercial agreements. In brokered equity offerings that are conducted on an underwritten or agency basis, a similar concept is applicable; the underwriting or agency agreement, as the case may be, will include rights of the underwriter or agent to terminate its obligations under the agreement, including “material adverse change out,” “market-out” (for non-bought deal offerings) and “disaster-out” clauses. Such clauses can take many forms, but are generally drafted so that the underwriter or agent can terminate its obligations under the agreement in an offering if, in its sole determination, an event, action, law, condition, circumstance, etc. develops or comes into existence that has a significant or material adverse effect on financial markets or the business or operations of the issuer.

Historically, such clauses have (thankfully) not enjoyed much recognition due to, generally speaking, both the rarity of such material adverse effects on the state of the market for securities, and the short time frame between the signing of offering agreements and the closing of the offerings. Such clauses are often only operative for a matter of days up to a few weeks. Therefore, the likelihood of an event material enough to trigger the “market-out” clause arising in such a short time frame is limited. Additionally, once an offering has been priced and the underwriting or agency agreement signed, the underwriters/agents are incentivized to close the deal.

Notwithstanding the rarity of termination of offerings, the current COVID-19 pandemic has caused at least one planned bought-deal offering to terminate. On March 11, 2020, Silvercrest Metals Inc. (“**Silvercrest**”) entered into an underwriting agreement with a syndicate of underwriters led by a well-known Canadian Bank (the “**Bank**”) for a bought-deal offering to raise approximately $75 million. The offering was scheduled to close on April 3, 2020. One week after signing, on March 18, 2020, Silvercrest issued a press release (the “**Press Release**”) announcing that it had received notice that the Bank was invoking the “disaster-out” provision to terminate the offering, citing extreme financial turmoil due to COVID-19. In the Press Release, Silvercrest made it clear that they did not agree with the Bank invoking the “disaster-out” provision because the COVID-19 pandemic was well known on the date of signing (in fact, the World Health Organization formally labelled COVID-19 as a ‘pandemic’ on March 11th) and the parties’ expectation was “that the precious metals market would respond positively to this known risk.” The Press Release also announced that Silvercrest’s view was that the underwriting agreement created a binding legal obligation on the Bank to complete the offering and that Silvercrest intends to pursue legal remedies against the Bank for breach of the agreement.

Subsequent to the Silvercrest offering, there has been at least one new offering that has attempted to address the potential offering risk created by COVID-19. On March 30, 2020, Orla Mining Ltd. (“**Orla Mining**”) entered into an underwriting agreement (the “**Orla MiningAgreement**”) with a syndicate of underwriters (the “**Underwriters**”), which included a provision to expressly exclude COVID-19 as a cause for termination of the offering. The provision states that “any related interruption to the business, affairs or financial condition of [Orla Mining], or any event, action, state or condition or financial occurrence related directly or indirectly to the COVID-19 Outbreak (whether now known or unknown or whether foreseeable or unforeseeable in the future), including any adverse effect on the financial markets generally” will not be considered an event or occurrence that will enable the Underwriters to terminate the Orla Mining Agreement. While relatively uncommon prior to COVID-19, carve-outs such as the one in the Orla Mining Agreement should become an important point of consideration for issuers and underwriters/agents during the COVID-19 crisis and beyond.

The pandemic is a fluid situation and outbreaks could wax and wane for months. COVID-19 has led to border closures, travel restrictions and declarations of states of emergency. These measures, among many other market interruptions, have profoundly impacted the Canadian and global financial markets, and have made typical offering activities such as in person roadshows impossible.

Issuers and underwriters/agents will need to consider how further efforts by governments to curb COVID-19 or future resurgences of the virus could impact offerings. The likelihood of completing a successful offering should be considered before launching a brokered offering, particularly if the proceeds of such offering are intended to be used to complete an acquisition or other transaction. It will be important for the documents governing the acquisition or transaction to include a corresponding right of termination for the issuer in the event the offering cannot be completed due to a termination event.

A determination of whether “out” clauses can be invoked during, or as a result of, COVID-19 necessarily involves an analysis of the specific contract in question and the timing of the termination, and will depend on how Canadian courts interpret these clauses given the novelty of this type of global event.

When thinking about an offering, issuers and underwriters/agents should consider the following before proceeding:

1. **Proper Disclosure of Risk Factors**. All prospective offering materials should contain all potential risks related to the current state of COVID-19 and other material risks that could impact the issuer or the offering.

2. **Negotiating the Scope of Termination Provisions.** In the context of many offerings and in other market circumstances, “out” clauses may not be given the consideration that they deserve. However, in the current climate, issuers and underwriters/agents should carefully consider and negotiate “out” provisions to ensure they accurately reflect the expectation of the parties as to when underwriters/agents may terminate the offering. For issuers, this may mean limiting the scope of the provision so that it is not drafted so broadly as to allow underwriters/agents to terminate the offering based on the impact of COVID-19, or other circumstances already known on the date of signing. An example of such a limitation is seen in the Orla Mining Agreement noted above. For underwriters/agents, this may mean considering the potential impact of COVID-19 on an issuer’s business or the financial markets in advance of entering into an underwriting or agency agreement, as the case may be.

In the end, termination provisions may or may not reference specific risks, such as the current state of the pandemic, but in all cases should reflect the expectation of the parties as to when and in what circumstances the offering may be terminated.

The Capital Markets Group at Aird & Berlis can advise on offering documents and termination proceedings. For more information, please visit our Capital Markets webpage.

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