

THIS EXAMINATION CONSISTS OF **10 PAGES**
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THE UNIVERSITY OF BRITISH COLUMBIA
FACULTY OF LAW

FINAL EXAMINATION — APRIL 2022

LAW 463.002
LAW 576.002

SECURITIES REGULATION

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TOTAL MARKS: 100
TIME ALLOWED: 2 HOURS
and 15 minutes reading time

- NOTES:
1. This is an open book examination. Students are permitted to bring excerpts from the *Securities Act* (British Columbia), the regulations, policies and instruments thereunder, the Johnston, Rockwell and Ford, *Canadian Securities Regulation* textbook, and any personal notes. No other texts are permitted.
 2. THIS EXAMINATION CONSISTS OF **3 PARTS**.

ANSWER ALL PARTS.
 3. Each question is given an approximate time. **STUDENTS ARE CAUTIONED TO ALLOCATE THEIR TIME ACCORDINGLY.**
 4. All references to the Securities Act means the *Securities Act* (British Columbia).

PART ONE**(35 Marks Total)****(Approximately 40 minutes)**

You are an articling student at a well-recognized business law firm in Vancouver practicing in the securities law group. A partner in your firm informs you that the firm has been engaged by Lily (“Lily”), the founder and controlling shareholder of MindLinks Ltd. (“MindLinks”), a successful Vancouver-based tutoring company which operates an online platform that connects teachers and students from around North America, to assist with Mindlink’s capital raising plans. Unfortunately, the partner is leaving for vacation the next day, so she has asked you to meet with Lily in her place.

During the meeting with Lily, you learn that Mindlinks is targeting to raise between \$8 to \$10 million in equity financing in order to pursue its plans of expanding its online tutoring network into the European markets. Mindlinks is currently a private company, with Lily owning approximately 75% of the outstanding common shares of Mindlinks. The other shareholders of Mindlinks comprise of a couple of venture capital funds, current or former employees of Mindlinks, and friends, family and business associates, all of whom were early investors in Mindlinks. Mindlinks currently has a total of 65 shareholders, 10 of whom are current or former Mindlink employees,

In order to complete the capital raise, Lily tells you that she is considering several different options:

- Option #1: Lily has had some early discussions with two European-based private equity investment funds, each of whom is willing to complete an equity investment between \$4 to \$6 million into Mindlinks.
- Option #2: Lily believes that Mindlinks has a strong corporate brand and reputation amongst the public in British Columbia and has been recognized by the financial press as one of the fastest growing venture tech companies in the province. As a result, Mindlinks regularly receives unsolicited inquiries from members of the general public in British Columbia (from high net worth individuals to retail investors) about the potential of making an investment in Mindlinks. The investment amounts being offered varies, from as little as \$5,000 to as high as \$125,000. Based on the volume of these inquiries, Lily believes that there is potential to raise the total amount of capital required from British Columbia-based investors.
- Option #3: Lily has been approached by a slick investment banker working for a Toronto-based investment dealer, who believes that Mindlinks is ready to complete an IPO (initial public offering) in Canada and his firm could help raise the entirety of the \$10 million required under the IPO. The investment banker assures Lily that she could still retain a significant equity interest (55%) in MindLinks following the completion of an IPO.

Another objective that Lily desires to achieve as part of the capital raising process is to obtain liquidity for herself personally, as the vast majority of her net worth is tied up in the common shares of Mindlinks that she owns. It is important for Lily to retain voting control of Mindlinks following the completion of the capital raise.

Lily has a number of questions for you in relation to the capital raising process.

1. If Lily's primary objective is to complete the capital raise as quickly as possible (ideally, in a couple weeks time), how would you advise Lily to proceed based on the financing options available to her. Please explain your reasoning. Please also explain what requirements or conditions must be satisfied under applicable BC securities laws in order to achieve this result. **(5 marks)**
2. Lily is interested in pursuing Option #2 but she is under the impression that it is not possible to sell securities to the general public without preparing and filing a prospectus document. At least that is what her previous lawyer told her when Mindlinks was completing her first round of financing for her business a couple years ago. Is Lily correct? Please explain your reasoning, including with reference to applicable BC securities regulations. **(4 marks)**
3. One of the European-based private equity investment funds that Lily is having dialogues with has indicated to her that they are willing to separately acquire a 5% equity stake in Mindlinks directly from Lily, which would give Lily the liquidity that she desires. Can this transaction be completed in compliance with applicable BC securities regulations? If so, explain how this can be achieved. **(4 marks)**
4. One of Lily's business mentors is a CEO of a publicly trading company which was recently listed on the Toronto Stock Exchange. Her mentor often tells Lily that "taking her company public was one of the hardest thing she has had to do in her business career and life as a public company is not always what it is cracked up to be". Lily does not fully understand what her mentor means by this. Please explain what an IPO would involve and what are the pros and cons of becoming a public company in Canada. **(12 marks)**
5. Assume that Lily has chosen Option #3. Lily would like to sell some portion of her shares in Mindlinks either at the same time as closing of the IPO or within a year after closing of the IPO. She does not want to sell any shares prior to the closing of the IPO. Please explain how Lily can sell her shares concurrent with the IPO and following the completion of the IPO. **(5 marks)**
6. Assume again that Lily has chosen Option #3. After the final prospectus was filed and receipted, but before closing of the IP and completion of the distribution, the Head of Corporate Development of Mindlinks tells Lily that he has learned that regulators in the European Union (EU) will be implementing new legislation which would require

Mindlinks to apply for a licence with EU regulators before it could make its online platform available to students based in the EU. Unfortunately, the Head of Corporate Development believes applying for this license would materially delay when Mindlinks could commence doing business in the EU and there is no guarantee that Mindlinks would be successful in its application. Lily is disappointed to hear this because Mindlinks has already expended a considerable amount of money and time on pursuing the IPO and does not want this “potential” bad news to curtail the process. Lily believes Head of Corporate Development is being overly pessimistic and doesn’t believe disclosure of this development is required in the prospectus document. What concerns should Lily be aware of for herself and Mindlinks. **(5 marks)**

PART TWO

(35 Marks Total)

(Approximately 40 minutes)

The CEO of HomeLending Inc. (“**HomeLending**”), a British Columbia incorporated company that is a reporting issuer in British Columbia and Ontario and the common shares of which are listed on the TSX Venture Exchange, has approached you for advice in relation to a new product offering that HomeLending is developing. HomeLending’s primary business to date focuses on offering a wide range of mortgage and lending products for both residential and commercial real estate properties in Canada.

The CEO of HomeLending has been reading about the unprecedented demand amongst major companies, brands, and early speculators who have been buying up “virtual land” in the metaverse (or virtual world). The CEO explains that ownership of “virtual land” in the metaverse is represented by a digital property deed which takes the form of a “non-fungible token” (NFT). Ownership of this NFT is then recorded on a blockchain ledger for everyone to see (much like the same way that if someone purchased a piece of real property in the physical world, their ownership over that piece of real property is recorded in the files of the land titles office). Similar to real property in the physical world, the owner of “virtual land” in the metaverse can build “virtual infrastructure” on the property (e.g., a home, a coffee shop, an art gallery, etc.). Ownership of “virtual land” can also easily be purchased and sold by way of transferring ownership of the underlying NFT on the blockchain ledger and there exists an active market of buyers and sellers for these “virtual land” NFTs.

HomeLending wants to leverage its experience and success in the mortgage lending business by offering a “virtual mortgage” to a prospective purchaser of a piece of “virtual land” (e.g. the “virtual land” NFT) which needs to finance a portion of the purchase price. While the concept is still in development, the CEO envisions that the “virtual mortgage” would work as follows:

- Under the terms of the “virtual mortgage”, HomeLending will provide a loan to a prospective purchaser (the “**Borrower**”) for up to 80% of the purchase price of the “virtual land” NFT, and the Borrower would be responsible for the remaining amount of the purchaser price by way of a down payment.
- In consideration for providing the loan to the Borrower, HomeLending will charge interest on the outstanding principal at a rate of 10% per annum. Much like a regular mortgage, the Borrower will be responsible for making monthly amortization payments to HomeLending payable in cash.
- As security for the loan, ownership of the “virtual land” NFT will be pledged by the Borrower in favour HomeLending until such time as the principal of the underlying loan is repaid in full by the Borrower to HomeLending. In order to facilitate the pledge, the

purchaser is required to transfer ownership of the “virtual land” NFT to HomeLending, such that HomeLending is the owner of the “virtual land” NFT on the blockchain over the entirety of the term of the loan. In return, HomeLending will provide the Borrower with rights to access, develop and use the “virtual land” in the metaverse as the Borrower’s sees fit, so long as the Borrower is not in default of the underlying loan.

- The CEO expects that many early speculators of “virtual land” who would be interested in financing their purchase by way of a “virtual mortgage” will not be sophisticated or experienced with “virtual land” development with no intention of using or developing the “virtual land” (e.g., they are only interested in the potential capital appreciation of the “virtual land”). For this group of Borrowers, HomeLending will offer an optional service, whereby HomeLending will be permitted to offer the pledged “virtual land” for lease to third parties that are interested in using the “virtual land” on a rental basis. HomeLending will be solely responsible for engaging with and managing the rental arrangements with these third parties. A portion of the profits earned by HomeLending from the rental fees charged to these third parties will be “shared” with the Borrowers and credited towards the interest owing under the loan with HomeLending. This “credit” would effectively decrease the rate of interest payable by the Borrower under the loan. The CEO expects that a large portion of Borrowers will take advantage of this optional service.
- HomeLending plans to market this “virtual mortgage” broadly and its marketing department is working on a large social media campaign to introduce this innovative product to the world.

The CEO also shares with you that HomeLending' entry into the “virtual mortgage” business will represent a significant shift in HomeLending’s business focus. The CEO is of the view that HomeLending needs to pivot away from its traditional real estate mortgage and lending business, where growth will likely stagnate in the future, and instead put all of its efforts behind the “virtual mortgage” business. In fact, the CEO, together with his senior management team, has already devised a new business plan which will result in HomeLending completing a restructuring of its business operations , such that its primary business will be focused on pursuing the “virtual mortgage” business and the traditional real estate mortgage and lending business will be slowly phased out. The CEO will be presenting this new business plan to HomeLending’s board of directors for approval at the end of the week, and he fully expects that the board of directors will approve this plan. However, HomeLending plans to announce this change in business focus in a couple of months time, so that it coincides with its public roll-out of its “virtual mortgage” product, in order to maintain HomeLending’s first mover advantage in the “virtual mortgage” business, as the CEO is not aware of any other company that is offering a similar product currently. The CEO is concerned that announcing the change before the public roll-out will result in competitors jumping-in and starting to offer a competing product.

The CEO is very keen on HomeLending's new "virtual mortgage" business, but is unsure whether it raises any legal concerns. He has asked you to prepare a short memo to address the following questions:

1. When you consider the entirety of the product offering as a package, is the proposed "virtual mortgage" a "security" for purposes of the *Securities Act* (British Columbia)? The CEO sees the "virtual mortgage" as no different than a conventional real estate mortgage and HomeLending has never had to engage a securities lawyer in connection with these transactions, but he would like your advice. Please explain your reasoning. **(10 marks)**
2. The CEO has asked you to explain the consequences to HomeLending if the "virtual mortgage" are found to be "securities". Please explain the consequences and the potential requirements that may be triggered under applicable British Columbia securities regulation. Please explain your reasoning. **(10 marks)**
3. The CEO would like to know what are the likely outcomes or ramifications if the "virtual mortgages" are found to be "securities", but HomeLending fails to comply with applicable securities law requirements. **(5 marks)**
4. The CEO would like to know whether you have any thoughts on the proposed timing on announcing the change in HomeLending's business focus? Please provide your reasoning. **(10 marks)**

PART THREE**(30 Marks Total)****(Approximately 40 minutes)**

You are a corporate and securities lawyer in a law firm which acts for a B.C. company called Cascadia Gold Inc. (“**Cascadia**”). Cascadia is a TSX Venture Exchange listed company which owns a 49% interest in an advanced exploration stage property in northwestern British Columbia, known as the Cassiar Gold Project, as well as a 100% interest in a relatively undeveloped exploration property located in the Kootenay region.

Late one Friday afternoon, you receive a telephone call from the CEO of Cascadia advising that he just had an unexpected visit from the CEO of Canadian Mining Corp. (“**CMC**”), a large TSX listed company which owns several producing gold mines and which also owns the remaining 51% interest in the Cassiar Gold Project. CMC has the exclusive right to manage the Cassiar Gold Project pursuant to the joint venture agreement relating to the project. In addition, CMC owns 19.9% of the issued and outstanding shares of Cascadia, which it acquired in a private placement that closed concurrently with the acquisition of its 51% interest in the Cassiar Project. CMC’s CEO is a director of Cascadia, nominated by CMC pursuant to a nomination right contained in the subscription agreement under which CMC acquired its Cascadia shares.

Cascadia’s CEO informed you that in their meeting earlier in the afternoon, CMC’s CEO delivered an offer letter which provides that: (i) CMC will buy all of the shares of Cascadia that it doesn’t already own at a 30% premium to their latest trading price, (ii) the purchase price for the Cascadia shares will be paid in shares of CMC, (iii) the transaction will be structured as a plan of arrangement under the British Columbia Business Corporations Act, (iv) the transaction will be conditional on usual conditions for transactions of this nature, including satisfactory due diligence, the execution of a definitive arrangement agreement by CMC and Cascadia and support agreements with each of Cascadia’s directors and officers, and the receipt of a unanimous recommendation in favour of the transaction from the board of directors of Cascadia, (v) Cascadia would pay a break fee of 4% to CMC in certain circumstances, if the transaction doesn’t complete, and (vi) the definitive arrangement agreement will contain customary representations and covenants for a transaction of this nature, including deal protection provisions in favour of CMC. The letter also stated that the above offer is open for acceptance until 5:00 p.m. on the upcoming Sunday and, if not accepted by Cascadia by that time, CMC will issue a news release before the opening of trading on Monday announcing that it intends to launch a take-over bid for Cascadia on similar terms.

In your conversation with Cascadia’s CEO, he further advised that (i) CMC had previously expressed interest in buying 100% of the shares of Cascadia, which the board of directors of Cascadia rejected as the offer price was too low and in the view of the board didn’t reflect the true value of the company, (ii) Cascadia is disappointed with the manner in which CMC has been

managing the Cassiar Gold Project, as CMC doesn't appear to be spending either the time or money required to develop the project in a timely manner, (iii) CMC has not been providing Cascadia with regular reports on the progress and status of the Cassiar Gold Project, making it impossible for Cascadia to keep its shareholders fully informed and resulting in a lack of interest in Cascadia's shares and a depressed share price, (iv) CMC's directors and officers collectively own a total of about 10% of the outstanding shares of Cascadia, (v) Cascadia has two independent shareholders who each own between 5% and 10% of the outstanding shares of the company, and (vi) he believes that unless a better offer is received a majority of the shareholders of Cascadia would likely approve or accept the offer presented by CMC, if given the opportunity to do so, as they are frustrated with the lack of progress in the development of the Cassiar Gold Project and the depressed trading price of Cascadia's shares.

At the end of your telephone call, Cascadia's CEO advised you that he intends to reject CMC's offer and let it know that his board will take all steps necessary to ensure that CMC doesn't "steal" the company. The CEO has requested your advice with respect to the following questions:

1. What duties do the directors and officers of Cascadia have with respect to CMC's offer and the take-over bid which it has threatened to launch if Cascadia doesn't accept the offer? In particular, can Cascadia "just say no" to CMC? **(4 marks)**
2. What steps and actions do you recommend that the board and management of Cascadia take before responding to CMC's offer? In particular, is Cascadia under any legal obligation to make public disclosure of CMC's offer? **(4 marks)**
3. Can Cascadia's CEO contact the two independent shareholders referred to above to discuss CMC's offer and determine their views regarding same before responding to CMC? **(3 marks)**
4. What steps are available to the board and management of Cascadia to defeat the hostile take-over bid by CMC? In particular, Cascadia's CEO has asked whether or not CMC's possible breaches of the Cassiar joint venture agreement (including the mutual confidentiality covenants contained therein) or CMC's position as an insider of Cascadia, might assist Cascadia in resisting CMC's hostile bid and, if so, how. **(7 marks)**
5. What steps is CMC likely to take once Cascadia announces actions to defend against the take-over bid? In particular, is it legally possible for CMC to acquire or otherwise "lock-up" the shares held by the two independent shareholders prior to launching a take-over bid and, if so, how would CMC accomplish this? **(5 marks)**
6. If, after CMC launches its hostile take-over bid and Cascadia announces steps to defend against the same, CMC and Cascadia reach agreement on a purchase price that both find acceptable, how would you recommend that they structure that agreement? **(4 marks)**

7. Are CMC and its insiders legally permitted to buy shares of Cascadia after CMC's hostile take-over bid has been announced and before it is completed? Assuming that CMC's take-over bid is successful, how soon after the completion of the bid will former Cascadia shareholders be able to sell the CMC shares issued to them pursuant to the bid? **(3 marks)**

— **END OF EXAMINATION** —