

Saskatchewan Local Policy Statement 4.3

Escrow Guidelines

Introduction

An "escrow" of shares is the deposit, under a written agreement, by specified individuals, who are normally the principals of a company, of their shares in a specific company into the custody of a trustee. The trustee will hold their shares until such time as certain conditions have been fulfilled for their release. Shares being held in escrow cannot be sold without the prior approval of the Director of the Securities Commission.

The main reasons for placing shares in escrow are:

1. to protect a company's continued ability to raise money;
2. to act as an incentive for the principals of the company to remain involved with the company.

The company's principals, prior to a public offering, will frequently have received significant portions of the company's shares. These shares may have been issued at a lower price per share than the price to the public, or may have been issued for properties of unknown value. When a company turns to the public for capital to develop its operations or properties, without an escrow of shares, there could be a strong incentive for the principals to dispose of their holdings at the current issue price. Such actions could impair the success of the company's financing and be detrimental to new investors.

An escrow agreement also acts as an incentive for the principals to remain with the company, normally in a management or advisory capacity, after the security offering to the public. The expectation is that principals, knowing that they will participate in the appreciation of the value of the shares as a result of the successful operation of the company, will conduct the business affairs of the company in a manner that will benefit all shareholders.

Paragraph 70(2)(f) of *The Securities Act* states that:

"The Director shall not issue a receipt for a prospectus where, in his opinion:

- (f) an escrow or pooling agreement that the Director considers necessary or advisable with respect to securities has not been entered into;"

Paragraph 70(2)(f) has potential for very broad application.

This policy statement, prepared by staff of the Commission, sets out the circumstances in which the

Director will consider an escrow to be necessary. It also provides guidelines for the release and transfer of such securities.

The major portion of this policy relates to an unlisted company filing an initial prospectus. A distinction has been made between an unlisted company which is not yet a going concern and a going concern company.

This policy is applicable to security distributions by prospectus and by offering memorandum in accordance with the Commission's General Order # 1 - Venture Capital Qualification System.

Part I Definitions

For the purposes of this policy statement the following definitions have been used.

- (a) "Arms Length Transaction" means a transaction negotiated by unrelated parties each acting in its own interest.
- (b) "Equity Security" means any security of an issuer that carries the residual right to participate in the earnings of the issuer and in its assets on liquidation or winding up.
- (c) "Going Concern Company" means a company which over the past five years, or such shorter time period as will be considered by the Director, has demonstrated that it successfully carried out its business plans, met contractual commitments and demands of creditors, was profitable and had retained earnings. Profitability of the company and cumulative positive retained earnings will be the key determinants in assessing if the company is in fact, a going concern.
- (d) "Junior Mining Company" means a company involved in the exploration and development of natural resource properties, but generally lacking the abilities, financial and otherwise, to take a natural resource property to commercial production.
- (e) "Legal for Life Securities" are securities issued by well established companies with a proven track record and which are listed or have been conditionally approved for listing by a Canadian stock exchange and which in the opinion of a named legal counsel qualify as investments for insurance companies registered under the Canadian & British Insurance Companies Act (Canada) or for insurance companies licenced under the Saskatchewan Insurance Act, without resort to the "basket clauses".
- (f) "Mining Company" means a company with the demonstrated abilities, financial and otherwise, to take a natural resource property to commercial production.

- (g) "Net Tangible Asset per Equity Security" means the total net tangible assets of the issuer based on its latest financial statements, plus the proceeds of security sales made in the interim period from the date of the financial statements referred to above to the date of the current public issue prospectus, but not including the current public issue, minus the paid-up capital attributable to all securities ranking senior to the equity securities, divided by the number of equity securities outstanding prior to the closing of the distribution under the prospectus, provided that where there are outstanding currently exercisable rights to purchase, convert or exchange relating to the equity securities, such calculation shall be made on the basis that each such right, the exercise price of which is less than the offering price of the related equity security, has been exercised.
- (h) "Offering Document" means a prospectus filed under the provisions of The Securities Act or an offering memorandum filed under the Commission's General Order # 1 - Venture Capital Qualification System.
- (i) "Offering Price" means the price at which the securities offered by the offering document may be purchased by the public.
- (j) "Principal" of an issuer means
- (i) a promoter of the issuer
- (ii) an officer, director, or any member of their immediate family who hold directly, indirectly, or beneficially 5% or more of any class of equity securities, or
- (iii) any person or company who holds directly, or indirectly, or beneficially more than 10% of any class of equity securities of the issuer.
- (k) "Principals' Equity Securities" means the Equity Securities held by Principals of a company.
- (l) "Research & Development Company" means a company whose primary business purpose is research and development.
- (m) "Director" means the director or deputy director of the Saskatchewan Securities Commission.

**Part II New Companies and Companies which are
Not Yet Going Concerns**

Securities to be Escrowed

1. All Principals' Equity Securities of new companies or companies which are not yet Going Concerns, issued for cash at a price less than the Offering Price, will be subject to escrow, less that number determined to be free of escrow. The free number will be calculated by dividing the total cash paid for all Principals' Equity Securities by the public Offering Price per Equity Security in the issuer's Offering Document.
2. Equity Securities of new companies or companies which are not yet Going Concerns, issued:
 - a) to other than Principals;
 - b) within the twelve month period leading up to the filing of a preliminary Offering Document; and
 - c) for cash at a price less than the current Offering Price;

will be subject to escrow, less that number determined to be free of escrow. The free number will be calculated by dividing the total cash paid for Equity Securities by the public Offering Price per Equity Security in the issuer's Offering Document.

3. Equity Securities of new companies or companies which are not yet Going Concerns issued:
 - a) in an Arms Length Transaction;
 - b) in exchange with another party for services;
 - c) within the twelve month period before the filing of a preliminary Offering Document; and
 - d) where the party has received Equity Securities representing 10% or more of any class of Equity Securities of the issuer.

will be subject to escrow less that number of securities determined to be free of escrow. The free number will be calculated by dividing the total cash equivalent consideration paid for Equity Securities by the public Offering Price for each Equity Security in the issuer's Offering Document.

4. Equity Securities of a new company or a company which is not yet a Going Concern, issued:

- a) in an Arms Length Transaction;
- b) in exchange with another party for property;
- c) within the twelve month period before the filing of a preliminary Offering Document;
and
- d) where the party has received Equity Securities representing 10% or more of any class of Equity Securities of the issuer:

will be subject to escrow. Where the value of the property has been determined by an independent source, for example by an accredited independent appraiser or engineer, some Equity Securities may be free of escrow. The number of free Equity Securities will be calculated by dividing the appraised property value by the current public Offering Price for each Equity Security in the issuer's preliminary Offering Document.

Where the value of the property has not been determined by a recognized method of valuation by an independent source, all Equity Securities issued for the property will be subject to escrow.

- 5. All Equity Securities issued by new companies or companies which are not yet Going Concerns in a non-arms length transaction for services or property will be subject to escrow. Where the value of the property has been determined by an independent source some Equity Securities may be free of escrow. The number of free Equity Securities will be calculated by dividing the appraised property value by the current public Offering Price for each Equity Security in the issuer's preliminary Offering Document.

Release of Equity Securities covered by an Escrow Agreement

- 6. Equity Securities of a company other than a Junior Mining Company or Research and Development Company:
 - a) issued for cash to Principals and subject to escrow in accordance with the provisions of paragraph 1 of this Part; or
 - b) issued in exchange for services or property in a non-arms length transaction and subject to escrow in accordance with the provisions of paragraph 5 of this Part;

will be released on a pro-rata basis with the prior written approval of the Director. Such

approval will be given upon the proven demonstration of successful operation of the company. Successful operation will be considered to be two consecutive years of profitability as well as cumulative positive retained earnings determined in accordance with generally accepted accounting principles, as shown by then current audited financial statements of the company.

7. Equity Securities of a company

- a) issued for cash to other than Principals and subject to escrow in accordance with provisions of paragraph 2 of this Part; or
- b) issued in exchange for property or services in an Arms Length Transaction and subject to escrow in accordance with the provisions of paragraphs 3 and 4 of this Part;

will be subject to an automatic pro-rata release without application to the Director on the following basis:

- c) 30% pro-rata release of the escrowed securities on the first anniversary of the date of the final receipt for the Offering Document;
- d) 30% pro-rata release of the escrowed securities on the second anniversary of the date of the final receipt for the Offering Document;
- e) 40% pro-rata release of the escrowed securities on the third anniversary of the date of the final receipt for the Offering Document.

8. Equity Securities of a Junior Mining Company:

- a) issued for cash to Principals and subject to escrow in accordance with the terms of paragraph 1 of this Part; or
- b) issued in exchange for property or services in a non-arms length transaction and subject to escrow in accordance with paragraph 5 of this Part

will be released on a pro-rata basis with the prior written approval of the Director as follows:

- c) an annual release of 10% of escrowed securities to a maximum cumulative total of 40% of the original number of Equity Securities held in escrow upon providing the Director with:

- i) evidence that the issuer has carried out its exploration and development plan in the best interest of the shareholders, such plan having been detailed in the original Offering Document and having been amended where necessary.
 - ii) evidence of the funds actually spent on an annual and cumulative total basis for exploration and development of each of its properties; and
 - iii) a certificate signed by the chief executive officer and chief financial officer indicating that all of the company's properties are currently in good standing with the crown, where applicable, that all annual exploration expenditures required to keep the properties in good standing have been made, and that the properties are considered of sufficient merit to warrant the current and projected expenditures.
- d) a further 25% release of the escrowed securities upon providing the Director with:
- i) a written Arms-Length agreement with another Mining Company whereby the other Mining Company will bring a property to production; and
 - ii) a certified copy of the production decision notification of the other Mining Company;
- e) the release of the balance of the escrowed securities where the production decision has been made and the property is put into commercial production on providing the Director with;
- i) in the case of a straight Arms Length property sale, evidence that funds have been received by the Junior Mining Company from the other Mining Company;
 - ii) in the case where the Junior Mining Company retains a percentage of profits, evidence that an agreement has been entered into and the property has been put into commercial production; or
 - iii) in the case of a combination of the above, evidence that the funds have been received and property put into commercial production.
9. Equity Securities of a Research and Development Company:
- a) issued for cash to Principals and subject to escrow in accordance with the terms of

paragraph 1 of this Part; or

- b) issued in exchange for property and services in a non-arms length transaction and subject to escrow in accordance with the terms of paragraph 5 of this Part

will be released on a pro-rata basis with the prior written approval of the Director as follows:

- c) an annual release of 10% of the escrowed securities to a maximum cumulative total of 40% of the original number of Equity Securities held in escrow upon providing the Director with:
 - i) evidence that the company has carried out its research and development plan in the best interest of its shareholders, such plan having been detailed in the original Offering Document and having been amended where necessary;
 - ii) evidence of the funds actually spent on an annual and cumulative total basis for each of its individual projects; and
 - iii) a certificate signed by the chief executive officer and chief financial officer that the projects are considered of sufficient merit to warrant the current and projected expenditures;
- d) where the Research and Development Company has developed a commercially viable product:
 - i) the balance of the securities will be released upon providing the Director with evidence that the research technology has been sold to another company in an Arms Length Transaction which will pursue commercial production of the product and that funds have been received from the sale; or
 - ii) 25% of the escrowed securities will be released upon providing the Director with evidence that the company has commenced commercial production of the product, and the balance of the escrowed securities will be released on demonstration of at least one year's profitable operation determined in accordance with generally accepted accounting principles as shown on a current audited financial statement of the company, together with distribution of the commercial products; or
 - iii) 25% of the escrowed securities in escrow will be released upon providing the

Director with evidence of commercial production after transfer of the research technology to another company for equity securities in the second company or any combination of cash, profit sharing and equity securities in the other company, and the balance of escrow securities will be released on demonstration of at least one year's profitable operation (as determined in clause (ii).) and distribution of the commercial product.

Part III Going Concern Companies

1. In general, where a Going Concern Company has previously raised funds from the public by way of Offering Document, and where escrow provisions were required for that issue, the escrow requirements of this policy will not apply, where the original escrow requirements are determined to be adequate. This part of the policy is primarily directed at going concern companies which are attempting to raise funds from the public, by way of an Offering Document, for the first time.

Securities to be Escrowed

2. Securities Represented by Net Tangible Assets

All Principals' Equity securities in a Going Concern Company will be subject to escrow minus the number which may be deducted which are represented by net tangible assets. This will be calculated by deducting that number of Equity Securities obtained by multiplying the number of Principals' Equity Securities by the Net Tangible Assets per Equity Security and dividing that number by the Offering Price per security in the Offering Document.

Securities for Which Consideration is Sufficient

In addition to any deduction permitted above, in calculating the number of Equity Securities to be escrowed, the following may be deducted:

- a) all Equity Securities which were acquired by a Principal more than one year prior to the preliminary receipt date for consideration equal to at least 60% of the Offering Price.
- b) all Equity Securities which were acquired by a Principal more than two years prior to the preliminary receipt date for consideration equal to at least 45% of the Offering Price.
- c) all Equity Securities which were acquired by a Principal more than three years prior to

the preliminary receipt date for consideration equal to at least 25% of the Offering Price.

Release of Equity Securities covered by an Escrow Agreement

3. Equity Securities which are Legal for Life Securities subject to escrow in accordance with the terms of paragraph 2 of this Part will be subject to an automatic pro-rata release without application on the following basis:
 - a) 10% of the escrow securities on the expiration of 9 months after the date of the final receipt for the Offering Document; and
 - b) 45% of the escrowed securities on the first and second anniversaries of the date of the final receipt for the Offering Document.

4. Equity Securities that are other than Legal for Life Securities and subject to escrow in accordance with the terms of paragraph 2 of this Part will be subject to an automatic pro-rata release without application on the following basis:
 - a) 10% of the escrowed securities nine months after the date of the final receipt for the Offering Document;
 - b) 20% of the escrowed securities on the first, second and third anniversaries of the date of the final receipt for the Offering Document; and
 - c) 30% of the escrowed securities on the fourth anniversary of the date of the final receipt for the Offering Document.

Part IV Venture Capital Corporations

1. Single Investment Venture Capital Corporations

Venture capital corporations incorporated in Saskatchewan with the intent of becoming registered under the Venture Capital Tax Credit Act, are often initiated by the Principals of existing small businesses in need of capital.

The intent of the arrangement is for the venture capital corporation to raise equity capital, and then reinvest all, or most of the proceeds of the issue into the small business. In return, the venture capital corporation received a minority voting position in Equity Securities of the small

business.

When such an arrangement is contemplated, the Equity Securities of the Principals in the small business, into which the venture capital corporation will be investing, will be subject to the escrow requirements in Part II of this policy. The investors in the venture capital corporation will not be subject to any escrow requirements.

Venture capital corporations in these circumstances may wish to further protect their interests and investments in the small business through contractual arrangements with the small business such as a unanimous shareholders' agreement, in addition to the escrow requirements of the Commission.

Multiple Investment Venture Capital Corporations

2. Venture Capital Corporations may be incorporated in Saskatchewan for the purpose of investing and maintaining a portfolio in numerous small businesses.

The Principals of the small businesses into which these venture capital corporations invest will not be subject to any escrow requirements.

The venture capital corporations in these circumstances may protect their interests and investment in the small businesses through contractual arrangements with the small business such as a Unanimous Shareholder's Agreement.

Those Principals owning Equity Securities of the venture capital corporation will be subject to the applicable escrow and release requirements in Part II of this policy.

Part V Holding Companies

One of the reasons for an escrow arrangement is to act as an incentive for the Principals to remain with the company after the security offering to the public. The expectation is that Principals, knowing that they will participate in the appreciation in the value of the shares as a result of their efforts and the successful operation of the company, will conduct the business affairs of the company in a manner that will benefit all shareholders.

If the holding company were to purchase equity securities of the issuer, an escrow of only the shares held by the holding company would not serve the intended purpose. The Principals of the holding company could sell their Equity Securities in the holding company to other parties, thereby circumventing the intention of the escrow provisions.

Where equity securities of an issuer are held through a holding company, the staff of the Commission will look to the substance of the arrangement rather than to its form. In general, the following will apply:

1. Equity securities of an issuer held by a holding company will be subject to the applicable provisions as to escrow and release in Part II of this policy.
2. Principals' Equity securities in the holding company will be subject to the applicable provisions as to escrow and release in Part II of this policy.

Part VI General

1. Multi Jurisdiction Filings

Where Saskatchewan is not the principal jurisdiction for the security filing, the security issuer has complied with the principal jurisdiction's escrow requirements, and the escrow agreement adequately protects the public interest in Saskatchewan, the Director will not normally impose any additional escrow requirements.

2. Listing on the Toronto Stock Exchange

Where the security issuer has applied for listing on the Toronto Stock Exchange and the issuer has entered into an escrow agreement pursuant to the Toronto Stock Exchange Founder Stock Policy Statement, the Director will normally not impose any additional escrow requirements, where the escrow agreement adequately protects the public interest in Saskatchewan.

In both of the above cases, the alternate escrow agreement will be required to be submitted to the Director for review to determine its acceptability.

3. Information to be Filed

To assist the Commission staff in determining the terms of an escrow, the following information is to be provided at the time of filing the preliminary Offering Document with the Commission:

- a) the names and addresses of all persons or companies who own beneficially, directly or indirectly, Equity Securities of the issuer;
- b) the number of securities of each class of the issuer held by the persons or companies referred to in (a);

- c) the dates of acquisition of all securities referred to in (b);
- d) the purchase price or consideration received for the acquisition of all securities referred to in (b) above and how the value was determined in each case.

Executed escrow agreements, as required by this policy, must be filed with the final Offering Document submitted to the Commission. A final receipt will not be issued until the executed agreements have been received.

4. Discretionary Releases

Application may be made to the Director in exceptional circumstances for release of securities from escrow on terms other than those outlined in this policy. The security holder and issuer must both advise the Director in writing of the unusual circumstances which lead them to believe that a release of all or part of the escrowed securities is appropriate, together with a copy of the escrow agreement. Upon review of the information submitted, a decision will be made as to whether the discretionary release is appropriate.

When dealing with the application, the Director will consider the following:

- a) the nature of the escrow, the reason for its creation, and its history, including the reasons for any transfer of shares within escrow and the basis of any consent given to such transfer;
- b) the interests of the applicant for release;
- c) the interests of the company;
- d) the interests of the then current shareholders of the listed company where those interests may differ from those of the listed company and its management; and
- e) the interests of the investing public generally; i.e. of those who might become shareholders in the future.

5. Extended Application of Escrow Policy

As all of the situations in which an escrow would be appropriate cannot be foreseen, the Director may require additional or alternate escrow requirements that are reasonable in the circumstances.

6. Appeals to the Chairman

Any issuer requested to comply with escrow requirements by the Director, may, where it considers the requirements unduly harsh or onerous, may request a hearing on the matter by the Commission. The Commission, after giving the parties an opportunity to be heard, will then make a determination on the matter in question, and refer the matter back to the Director for final consideration under Subsection 70(1) and 70(2).

7. Forms

Wherever an escrow of securities is required, the issuer and equity security holder should enter into a written agreement which may be in accordance with the regulations to the Act or may be prepared in another form which incorporates the provisions of this policy and is acceptable to the Director.

An example of a sample escrow agreement is attached:

- a) Form 16 Escrow Agreement

Adopted by the Commission

Effective June 21, 1988

Amended Effective November 7, 1988

"Marcel de la Gorgendière"

Marcel de la Gorgendière, Q.C.

Vice-Chairman

FORM 17

ESCROW AGREEMENT

THIS AGREEMENT is made as of the ____ day of _____, 19__

BETWEEN:

(hereinafter called the "Escrow Agent")

OF THE FIRST PART

AND:

(hereinafter called the "Company")

OF THE SECOND PART

AND:

THE UNDERSIGNED SHAREHOLDERS IN _____
(hereinafter individually called "Shareholder" and collectively
called the "Shareholders")

OF THE THIRD PART

WHEREAS:

- A. The Shareholders have acquired or are about to acquire shares of the Company and have agreed to enter into this escrow agreement on the terms and conditions hereinafter provided;
- B. The Escrow Agent has agreed to undertake and perform its duties according to the terms and conditions hereof;

NOW THEREFORE this Agreement witnesses that in consideration of the aforesaid agreements and of the sum of one dollar (\$1.00) now paid by the parties hereto, each to the other (receipt of which sum the parties do hereby respectively acknowledge each to the other) the shareholders jointly and severally covenant and agree with the Company and with the Escrow Agent and the Company and the Escrow Agent covenant and agree each with the other and with the Shareholders jointly and severally as follows:

1. In this Agreement:
 - a) "Shares" shall mean the shares of each Shareholder set opposite their signature at the end of this Agreement, together with any additional shares issued by way of a dividend paid in shares which accrues to the shares, and the certificate or certificates representing such shares;
 - b) "Director" shall mean the Director or any Deputy Director of the Saskatchewan Securities Commission;
2. Each Shareholder hereby places and deposits in escrow with the Escrow Agent the Shares of the Company referred to opposite his or her name as set out at the end of this Agreement and agrees to deliver forthwith to the Escrow Agent those Shares (including any replacement shares or certificates if and when issued) to the Escrow Agent for deposit in escrow.
3. The parties hereby agree that the Shares and the beneficial ownership of or any interest in them shall not be sold, assigned, hypothecated, alienated, released from escrow, transferred within escrow, or otherwise in any manner dealt with, without the express consent in writing of the Registrar being first obtained except as may be required by reason of the death or bankruptcy of any Shareholder, in which case the Escrow Agent shall hold the Shares subject to this Agreement, for whatever person, firm, or corporation shall be legally entitled to be or become the registered owner thereof.
4. The Shareholders hereby direct the Escrow Agent to retain their Shares including any replacement shares or certificates, and not to do or cause anything to be done to release the same from escrow or to allow any transfer, hypothecation, alienation, sale, assignment or release thereof except with, and as directed by, the written consent of the Director. The Escrow Agent hereby accepts the responsibilities placed on it hereby and agrees to perform the same in accordance with the terms hereof and in accordance with the written consent of the Director.
5. If, during the period in which any of the Shares are retained in escrow pursuant hereto, any dividend, other than a dividend paid in shares of the Company, is received by the Escrow Agent in respect of the Shares, such dividend shall be paid or transferred forthwith to the respective Shareholders entitled thereto. Any shares received by the Escrow Agent by way of dividend in respect of the Shares shall be dealt with as if they were Shares hereunder.
6. All voting rights to the Shares may at all times be exercised by the respective registered owners thereof.

7. The Company hereby acknowledges the terms and conditions of this Agreement and agrees to take all reasonable steps to facilitate its performance.
8. The written consent of the Director to a release from escrow of all or part of the Shares shall terminate this Agreement only in respect to those Shares so released. For greater certainty, a transfer within escrow is not a release from escrow.
9. It is acknowledged by the parties that if the Company meets certain conditions over time, the Shareholders shall be entitled to a partial or full release by the Director of the Shares from the terms of this Agreement from time to time in accordance with the policies of the Saskatchewan Securities Commission.
10. The parties hereto agree and acknowledge that the Shares subject to escrow shall be released on the following terms: (detail the applicable release provisions of the policy).
11. Notice of any consent of the Director shall be given by the Escrow Agent to all persons or parties affected thereby at their last known address.
12. The Shareholders do hereby jointly and severally covenant and agree to keep harmless and fully indemnify the Escrow Agent from and against all loss, costs, suits, demands, claims, damages, and expenses which the Escrow Agent may at any time or times hereafter suffer as a result of compliance in good faith with the terms hereof.
13. If the Escrow Agent should wish to resign, it shall give at least six months' notice to the Company, which may, with the written consent of the Director, by writing appoint another Escrow Agent in its place and such appointment shall be binding on the Shareholders and the New Escrow Agent shall assume and be bound by the obligations of the Escrow Agent hereunder.
14. This agreement may be executed in several parts in the same form and such parts as so executed shall together form one original agreement, and such parts, if more than one, shall be read together and construed as if all the signing parties hereto had executed one copy of this Agreement.
15. This Agreement shall enure to the benefit of and be binding upon the parties hereto, their and each of their heirs, executors, administrators, successors, and permitted assigns.

IN WITNESS WHEREOF the parties hereto have executed these presents the day and year first above written.

SIGNED)	Signature	Number and	Certificate
)		Type of	Number
)		Shares	
)			
)			
in the presence of:)	_____	_____	_____
)			
)			
_____)	_____		
)	Print Name		

SIGNED)			
)			
)			
)			
in the presence of:)	_____	_____	_____
)			
)			
_____)	_____		
)	Print Name		