Chapter 6

Request for Comments

6.1.1 NP 46-201 Escrow for Initial Public Offerings and Form 46-201F Escrow Agreement

NOTICE

PROPOSED NATIONAL POLICY 46-201 ESCROW FOR INITIAL PUBLIC OFFERINGS AND FORM 46-201F ESCROW AGREEMENT AND RECISSION OF ONTARIO SECURITIES COMMISSION POLICY 5.9

Effective today, the Commission, together with other members of the Canadian Securities Administrators (CSA), is publishing for comment National Policy 46-201 *Escrow for Initial Public Offerings.*

Background

The CSA believes that a simplified, uniform national approach to escrow promotes greater efficiency and places issuers, principals and public investors in different jurisdictions on a more level footing. As such, the CSA determined to develop a national escrow policy that would apply to initial public offerings by prospectus (IPOs). To achieve its objective, the policy would have to appropriately balance the regulatory objectives of facilitating capital formation in Canada and protecting investors. Further, it would have to be clear, consistent, understandable and administratively efficient.

The CSA considered the objectives and role of escrow requirements in the context of IPOs. The fundamental objective of escrow requirements is to encourage continued interest and involvement in an issuer, for a reasonable period after its IPO, by those principals whose continuing role would be reasonably considered relevant to an investor's decision to subscribe to the issuer's IPO. The CSA determined that many of the factors and assessments often associated with escrow such as controlling cheap stock are more properly addressed by underwriters appropriately exercising their responsibilities related to IPO pricing and timing.

In May 1998, the Commission, together with the other members of the CSA, published for comment a proposal for uniform terms of escrow applicable to IPOs ((1998), 21 OSCB 2927). After that time, issuers conducting IPOs could choose to follow either the proposed uniform escrow regime or the escrow policy in effect in their own jurisdictions.

On March 17, 2000, the CSA published CSA Notice 46-301 *Proposal for Uniform Terms of Escrow Applicable to Initial Public Distributions* describing a revised proposal for an IPO escrow regime and permitting issuers to use it at their option ((2000), 23 OSCB 1936). The 2000 proposal encompassed several fundamental changes to the 1998 proposal in response to comments which we received. The changes were identified in the Notice.

After publishing the 1998 and 2000 proposals, we received requests to approve amendments to existing escrow agreements to permit the release of escrow securities on the terms in those proposals. On June 15, 2001, we published CSA Notice 46-302 *Consent to Amend Existing Escrow Agreements* permitting, on certain conditions, escrow agreements which predate the 2000 proposal to be amended to reflect the release terms contained in that proposal.((2001), 24 OSCB 3583).

The proposed National Policy replaces CSA Notices 46-301 and 46-302.

Local Escrow Policies

In exercising his/her discretion under s. 61(2)(f) of the Act, the Director will permit an issuer to follow the proposed National Policy pending its adoption by the Commission. During this period, an industrial issuer may also follow OSC Policy 5.9 - *Escrow Guidelines - Industrial Issuers*. The Commission intends to rescind OSC Policy 5.9 at the end of this period and will request that the Lieutenant Governor in Council revoke section 79 and Forms 17 and 18 of the Regulation made under the Securities Act.

Certain other Canadian jurisdictions have maintained their local escrow policies on an interim basis while others have not. Therefore, until the National Policy is adopted on a permanent basis, the securities regulator in a particular province may permit issuers conducting IPOs in that province to rely on either the proposed National Policy or the province's local escrow policy. Please see each local notice announcing the publication of the proposed National Policy to determine whether a particular local policy is still in effect.

If an issuer wishes to follow a local escrow policy and proposes to offer securities in more than one jurisdiction, CSA members will apply mutual reliance principles.

National Policy

We, together with market participants, have considered the 2000 proposal since the publication of CSA Notice 46-301. The proposed National Policy contains substantially the same terms as the 2000 proposal. However, a limited number of changes have been made in response to comments we received on the 1998 proposal and on the basis of additional research which has been conducted since that time. The more important changes are set out below.

- The "exempt issuer category" has been expanded to include an issuer which has a market capitalization of at least $100 million on completion of its IPO. This change was made on the basis of significant research

which was conducted to ensure that the proposed National Policy does not impose any significant regulatory disadvantage on Canadian issuers relative to their U.S. counterparts. In conducting our research, we consulted with U.S. securities lawyers, U.S. state securities regulators, the North American Securities Administrators Association and the Pacific Exchange to get a clearer understanding of the resale restrictions and lock-up (or escrow) restrictions imposed on shareholders of companies that do IPOs in the U.S.

- Changes have been made to the category of "principals" whose securities are subject to escrow, including:

  - securities held by a principal that carry less than 1% of the voting rights attached to an issuer's outstanding securities immediately following its IPO are not subject to escrow; and

  - a principal's spouse and their relatives that live at the same address as the principal are treated as principals rather than all of the associates and affiliates of the principal being so treated.

- Escrowed securities may be transferred within escrow to a person or company that before the transfer holds more than 20% of the voting rights attached to an issuer's outstanding securities and to a person or company that after the transfer will hold more than 10% of such voting rights. The 10% holder after the transfer must also have the right to elect or appoint one or more directors or senior officers of the issuer or any of its material operating subsidiaries. This is in addition to the transfers within escrow that are permitted in the 2000 proposal.

- A person or company approved by a Canadian exchange to act as a transfer agent may be an escrow agent.

- Escrow agreements which predate the proposed National Policy may be amended to reflect the release terms contained in the proposed National Policy.

Summary of Written Comments

A summary of the written comments received on the 1998 proposal, the CSA's responses and a discussion of the changes incorporated in the National Policy is attached as Appendix "B" to this Notice. Appendix "A" contains a list of the commenters.

Regulations to be Revoked

The Commission will request the Lieutenant Governor in Council to revoke section 79 and Forms 17 and 18 of the Regulation made under the Securities Act.

Recission of Policies

The proposed National Policy and Form will result in the recission of OSC Policy 5.9. The text of the proposed recission will be as follows:

"Policy 5.9 is hereby rescinded."

Request for Comments

You are invited to comment on National Policy 46-201 and Form 46-201F. Please submit your comments in writing on or before November 20, 2001.

Please send us two copies of your comments, addressed as follows:

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Securities Commission
The Manitoba Securities Commission
Ontario Securities Commission
Office of the Administrator, New Brunswick
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Department of Government Services and Lands, Newfoundland and Labrador
Registrar of Securities, Government of the Northwest Territories
Registrar of Securities, Government of the Yukon Territory
Registrar of Securities, Nunavut

c/o Brenda Benham
Director, Policy and Legislation
British Columbia Securities Commission
PO Box 10142, Pacific Centre
701 West Georgia Street
Vancouver, British Columbia
V7Y 1L2
Fax: (604) 899-6506
Email: bbenham@bcsc.bc.ca

Please also send your comments to the Commission des valeurs mobilières du Québec as follows:

Denise Brosseau, Secretary
Commission des valeurs mobilières du Québec
Stock Exchange Tower
800 Victoria Square
P.O. Box 246, 22nd Floor
Montréal, Québec H4Z 1G3

If you are not sending your comments by e-mail, please send a diskette containing your comments (in DOS or Windows format, preferably Word).

We cannot keep submissions confidential because securities legislation in certain provinces requires that a summary of the written comments received during the comment period be published.

Questions

Please refer your questions to any of:

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September 21, 2001

APPENDIX "A"

LIST OF COMMENTERS

General

Swinton & Company, Barristers & Solicitors
Vancouver Stock Exchange
Scott & Aylen, Lawyers
Canadian Dealing Network Inc. (CDN)
Catalyst Corporate Finance Lawyers
Ogilvy Renault, Barristers & Solicitors
Union Securities Ltd.
Osler, Hoskin & Harcourt, Barristers & Solicitors
Montpellier & McKeen, Barristers & Solicitors
Prospectors & Developers Association of Canada (PDAC)
Davies, Ward & Beck, Barristers & Solicitors
Armstrong Perkins Hudson, Barristers & Solicitors
Investment Dealers Association of Canada (IDA)

Transfer Agents

Security Transfer Association of Canada (3 comment letters)
Equity Transfer Services Inc.
Pacific Corporate Trust Company
The Trust Company of Bank of Montreal
TD Trust Company

Venture Capitalists

Canadian Venture Capital Association (CVCA) (2 comment letters)
Davis & Company (on behalf of Ventures West Management Inc., Royal Bank Capital Corporation, Business Development Bank and Working Opportunity Fund)
Réseau Capital (2 comment letters)
Société Innovatech Québec et Chaudière-Appalaches
GrowthWorks Capital Ltd.
Bank of Montreal Capital Corporation
Mercator Investments Limited
Elnos Corporation
Royal Bank Capital Corporation
BCE Capital
Clairvest Group Inc.
Investissemenets Novacap Inc.
Saskatchewan Government Growth Fund
Les placements Telsoft Inc.
Hydro-Québec CapiTech
Whitecastle Investments Limited

APPENDIX "B"

SUMMARY OF COMMENTS RECEIVED AND RESPONSES OF THE CSA ON PROPOSAL FOR A NATIONAL ESCROW REGIME APPLICABLE TO INITIAL PUBLIC DISTRIBUTIONS

The CSA received submissions on the Proposal for a National Escrow Regime Applicable to Initial Public Distributions (the "initial proposal") from the 34 commenters listed in Appendix "A".

The CSA considered the submissions received in revising the initial proposal and preparing the National Policy. We thank all the commenters for providing their comments.

The following is a summary of comments received on the initial proposal, together with the CSA's responses, organized by topic. This summary is organized into three parts:

A. General Comments (comments on all aspects of the initial proposal, except the "passive investor" provisions and provisions directly affecting escrow agents)

B. Comments on passive investor provisions (including venture capital organizations' comments)

C. Escrow agents' comments

A. General Comments

1. Competition with United States Capital Markets

The paramount concern voiced by the commenters was that the proposed Canadian escrow regime continues to put the Canadian exchanges at a significant competitive disadvantage to United States exchanges and electronic trading systems. Many of the commenters raised this issue when commenting on specific aspects of the initial proposal. A few commenters raised the issue generally in support of suggestions that the Canadian escrow regime be abolished entirely or replaced with another regime that would be no more restrictive than United States resale restrictions. (See Abolish/Replace the Escrow Regime below.)

The CSA take this issue very seriously. We consulted with US securities lawyers, US state securities regulators, the North American Securities Administrators Association (NASAA) and the Pacific Exchange to get a clearer understanding of the resale restrictions and lock-up (or escrow) restrictions imposed on securityholders of issuers that do initial public offerings (IPOs) in the US.

Comparison of National Policy with US Regime

Offering size

US market participants and regulators advised that the regulatory and due diligence costs of a public offering in the US are quite high. Consequently, IPOs for less than US $20 million are not common. Very few US underwriters are interested in raising financing below this level. Most issuers that seek a listing on the Canadian Venture Exchange Inc. (CDNX) and many that seek a listing on The Toronto Stock

Exchange Inc. (TSE) raise less than this amount and, therefore, do not realistically have the option to conduct an IPO in the US. Smallcap and microcap companies in the US often obtain financing through private placements and semi-public offerings, delaying an IPO until later in their development cycles. By a "semi-public offering", we mean a public offering that is conducted under US state securities legislation that is basically equivalent to a private placement under US federal securities law.

Senior Issuers

While it is difficult to compare listing criteria, we found that the minimum original listing requirements of the TSE are lower than those of the Nasdaq National Market or the New York Stock Exchange (NYSE) and in the range of those of the American Stock Exchange (AMEX) and the Nasdaq Smallcap Market. Even the TSE's highest original listing criteria, those for its "exempt" issuer category, are, with one exception, generally lower than those of the Nasdaq National Market or the NYSE, although they are somewhat higher than those of AMEX.

Because exemption from escrow under the National Policy is tied to exempt listing status on the TSE, most issuers that would be exempt from escrow in the US because they qualify for listing on the NYSE or Nasdaq National Market would also be exempt from escrow in Canada under the National Policy. Indeed, some Canadian issuers that might be subject to escrow or lock-up arrangements if they conducted their IPO in the US could be exempt from escrow under the National Policy.

The one exception mentioned above is that an issuer can list on the Nasdaq National Market if it has a market capitalization of at least US $75 million after its IPO. This would not necessarily qualify it for listing in the TSE's exempt category. However, issuers with that market capitalization would also, at current currency exchange rates, be exempt from escrow under the National Policy because we have changed the category of "exempt issuer" under the National Policy to include issuers with a market capitalization of at least $100 million after their IPO.

Junior Issuers

It appears that Canadian issuers conduct IPOs earlier in their growth cycles than those in the US. The feedback we have received suggests that issuers of the type listed on CDNX and certain of the junior issuers on the TSE would not be able to conduct an IPO in the US at all because of the significant costs. In the US markets, those types of issuers would often be restricted to private financing until they grow enough to list on a national securities exchange. If these junior issuers conducted a semi-public offering in the US, the majority of the state securities commissions would require the imposition of a lock-up either on the basis of NASAA policies or under their own state laws. Under the policies, a broader category of persons would be subject to escrow and the terms of release would generally be more onerous than would be the case under the National Policy. Issuers that are doing a registered offering with the US Securities and Exchange Commission and using Coordinated Review at the US state level are subject to escrow or lock-up under the NASAA policy regarding promotional shares.

Other

In addition to regulator-imposed lock-ups, US underwriters and market makers typically impose lock-up arrangements. Hold periods are also imposed under US federal securities law (Rule 144 under the Securities Act of 1933).

Conclusions

Many Canadian issuers are choosing to list in the US. Some are trading over-the-counter in the US without ever having conducted an IPO in either country. We acknowledge that this emigration of secondary market trading to the US may have important effects on the Canadian capital markets, but our research and analysis indicate that the National Policy should not be a factor in issuers' decisions on where to have their securities traded.

Changes to initial proposal to address competition concerns

We made significant changes to the initial proposal to ensure that an issuer that elects to list on a Canadian exchange is not subject to greater restrictions than are reasonable to accomplish the purpose of escrow. We narrowed the scope of the National Policy, applying it only to issuers that are not TSE exempt issuers or issuers with a market capitalization of less than $100 million after their IPO, cutting the escrow periods in half, and offering added flexibility to principals in dealing with their securities at the time of the IPO.

The following changes have been made to the initial proposal to address the competition concerns raised by some of the commenters:

- The class of exempt issuers has been broadened.
- The escrow period has been shortened:
  - for established issuers from 3 years to 18 months with 4 equal releases, starting on the listing date and then every 6 months from listing, and
  - for emerging issuers from 6 years to 3 years with 7 releases, 10% on listing and then 15% every 6 months from listing.
- The definition of principal has been narrowed:
  - The percentage equity interest that, alone, will subject a securityholder to escrow requirements has been increased from 10% to more than 20% of the voting rights attached to the issuer's outstanding securities.
  - A securityholder holding more than 10% but 20% or less of the voting rights attached to the issuer's outstanding securities will only be subject to escrow requirements if the securityholder selects, or has the right to select, one or more directors or senior officers of the issuer or a material operating subsidiary.
  - Percentage equity interest will be calculated after the issuer's IPO, instead of before.
- A de minimis exception has been added.

" A principal will not be subject to escrow requirements if the principal holds less than 1% of the voting rights attached to the issuer's outstanding securities, calculated after the issuer's IPO.

- Principals have been provided with an early liquidity opportunity. At the time of the issuer's IPO, principals may sell their escrow securities free of escrow restrictions in a secondary offering disclosed in the issuer's IPO prospectus.

" If the secondary offering is firmly underwritten, any principal may sell escrow securities.

" If the secondary offering is on a best efforts basis, only principals other than promoters, directors and senior officers of the issuer or any of its material operating subsidiaries, may sell their escrow securities, provided all or the specified minimum number of the securities offered by the issuer in the IPO are sold prior to the secondary offering.

2. Abolish/Replace the Escrow Regime

One commenter suggested that the escrow regime could be abolished altogether. In the commenter's view, the escrow regime is not needed to accomplish the stated purpose of escrow, i.e. to tie management and other key principals to the issuer, as current rules and market forces already accomplish this objective.

The CSA remain convinced that escrow continues to serve an important function in the Canadian marketplace. The CSA do not agree that current rules and market forces, without escrow, alone will be sufficient encouragement for management and other key principals to devote their time and attention to carrying out the issuer's IPO business plan.

A few commenters suggested that the Canadian escrow regime be replaced with resale restrictions closely replicating US Rule 144 limitations, or other rules that would be no more stringent than the escrow regime in place in the US. For the reasons discussed above, our research and analysis indicate that the National Policy should not be a factor in issuers' decisions where to have their securities traded.

Another commenter suggested an alternative approach. Principals would be prevented from selling into the open market for an 18-month period. After that, they would be required to provide 7 days prior notice before selling into the open market. We believe that the regime in the National Policy is preferable because shares are released on a staged basis, beginning on listing, and then every 6 months thereafter, and the length of escrow is related to the classification of the issuer. This approach provides greater predictability for market participants while offering principals earlier and increasing liquidity.

One commenter emphasized that Canadian escrow requirements should be easily understood and flexible so that Canadian issuers do not choose to go public in the US to avoid an onerous, complex regime.

One of the CSA's objectives in reviewing the initial proposal for revision was to ensure that the proposal would be easy to understand and apply so that compliance would be straightforward and administration would be efficient. We have made several changes to the initial proposal, including:

- adoption of exchange classifications for use in the National Policy,

- revisions to the definition of principal for persons and companies that are "principals" as a consequence of equity interest, basing the test for such principals on objective factors that are easily determined, eliminating the need for a definition of "passive investor" and a determination as to whether a particular securityholder is a "passive investor",

- basing escrow requirements upon completion of a take-over or other business combination on objective factors that are easily determined, and

- presenting the National Policy in plain language, addressing clearly and logically the questions most likely to arise.

3. Purpose of the Escrow Regime

While commenters generally concurred with the stated purpose of escrow, some of the commenters noted that there were other rationales for escrow that were not reflected in the initial proposal. One of these, "controlling cheap stock", prevents principals from selling securities that they acquired at a price that is significantly less than the IPO price into the market shortly after the issuer's IPO which depresses the trading price of the securities. Another rationale is to provide founders with a degree of control during the formative stages of an issuer.

The CSA considered and reconfirmed the stated purpose of escrow: to encourage the issuer's principals to remain with and devote their time and attention to the issuer for an appropriate period after the issuer's IPO to best enable the issuer to carry out the IPO business plan. In our view, the role of the issuer's underwriter includes dealing with valuation issues in the course of pricing the IPO.

4. Failure to Recognize Value

Several commenters expressed concern that value contributed to the issuer by principals was not recognized in the initial proposal. Commenters suggested that principals would be discouraged from providing value for their securities as a consequence of the initial proposal not making any distinction between securities issued for value, and securities issued for nominal or little consideration. A commenter suggested that principals are more committed if they have contributed value. Another commenter suggested that seed capital investors would be unwilling to become principals because they will not want their shares subjected to escrow requirements. Commenters raised US competition concerns, stating that principals that have paid fair value for their securities will choose to list where their contribution is recognized.

Commenters suggested several alternative models. Some suggested a formula tied to price paid, others also took dilution of the issuer's assets into account in the formula. Most of these commenters agreed with the elimination of property

valuations to support the issuance of free-trading shares to founders, although there was a commenter that disagreed.

The CSA are of the view that issues of value are better dealt with by underwriters in pricing the issuer's IPO, than by standard, mandatory escrow requirements imposed by the CSA. The CSA do not disagree with commenters that expressed the concern that principals should not be discouraged from contributing value to the issuer, but do not believe that the National Policy would have this result. However, the CSA do not agree that a seed capital investor's decision as to whether or how to participate in the management of an issuer will be governed by whether escrow requirements will apply to the investor, especially with the reduction in escrow periods and the opportunity for principals to participate in a permitted secondary offering at the time of the issuer's IPO.

5. Time-based Model vs. Performance-based Model

A commenter suggested that a performance factor should remain in the escrow release formula because this would align the interests of the public shareholders with the issuer's principals. The commenter's view was that in a purely time-based release formula, there is an incentive for the principals to take the issuer public prematurely, because the sooner the issuer goes public, the sooner their shares will be released from escrow.

The CSA do not agree that failure to include a performance factor in the release formula will have the result of an issuer going public prematurely. The timing of a particular issuer's IPO depends on many factors, especially the issuer's need for capital, and the comparative cost to the issuer of capital from available sources. Furthermore, the farther along the issuer's stage of development, the shorter the period of escrow, and for securities of issuers that are sufficiently developed to qualify as exempt issuers based on the TSE's criteria or significant market capitalization, no escrow will be required.

We believe that there are other mechanisms in place to align the interests of principals and shareholders, including fiduciary and statutory duties of principals, prospect of growth in personal holdings of the issuer's securities, stock options and conventional employment arrangements.

We do agree with this commenter that, in most cases, if principals have attracted a take-over bid for the issuer, the securities of the principals should be released from escrow, but not for the same reason as stated by this commenter. (See Release from Escrow – Release upon Take-over Bid below.)

6. Persons whose Securities are subject to Escrow Requirements (Definition of Principal)

A few commenters thought that the definition of principal was too broad and should be restricted to persons who are key to the issuer's success. A commenter suggested that it would be more appropriate to calculate percentage equity interest for the purpose of the definition after the issuer's IPO, rather than before. A few commenters suggested that directors and officers with nominal shareholdings be excluded from escrow requirements.

The CSA generally agree with these comments and have narrowed the definition of principal. We believe that whether a securityholder is subject to escrow requirements should be based on whether the securityholder has effective control over the issuer or a significant influence on management. Those that do should be subject to escrow requirements.

Therefore, we have made the following changes to the definition of principal that was contained in the initial proposal:

- The percentage equity interest that, alone, will subject a securityholder to escrow requirements has been increased from 10% to more than 20% of the voting rights attached to the issuer's outstanding securities, calculated after the issuer's IPO, rather than before.

- A securityholder holding more than 10% but 20% or less of the voting rights attached to the issuer's outstanding securities will only be subject to escrow requirements if the securityholder selects, or has the right to select, one or more directors or senior officers of the issuer or a material operating subsidiary. The percentage equity interest will be calculated after the issuer's IPO, rather than before.

We also agree that a de minimis exception is appropriate. Therefore we have added a provision to the National Policy that excludes from escrow securities held by principals that hold less than 1% of the voting rights attached to the issuer's outstanding securities. The percentage equity interest will be calculated after the issuer's IPO.

A commenter suggested that associates should be excluded from the definition of "principal". We agree that including all associates of the principal is too broad, and therefore have limited the associates that will be treated as principals to the principal's spouse and relatives who share the same home.

A commenter stated that a person who has acted as a promoter a long time prior to the issuer's IPO should not be subject to escrow. The CSA agree with this comment and have restricted the definition of principal to apply to persons that have acted as promoters of the issuer within two years of the issuer's IPO.

7. Escrow Periods

Several commenters stated that the length of the escrow period in the initial proposal was unnecessarily long. Some commenters made this comment in the context of competition concerns. One commenter pointed out that the proposed period was far longer than an issuer would generally need to carry out its IPO business plan. Another commenter noted that principals that cause their issuers to carry out IPOs for the purpose of creating greater investment liquidity would not do so if the escrow requirements are too onerous. A commenter noted that unreasonable escrow requirements could lead to management appointing nominee boards in order to attempt to evade the escrow requirements.

We agree that the escrow periods in the initial proposal were longer than necessary. We have made the following changes:

- The escrow period for emerging issuers has been shortened from 6 years to 3 years with 10% of a

principal's securities released on listing and the balance released in 6 equal instalments in 6 month intervals after listing.

- The escrow period for established issuers has been shortened from 3 years to 18 months with 25% of a principal's securities released on listing and the balance released in 3 equal instalments at 6 month intervals after listing.

- The class of exempt issuers has been expanded. An exempt issuer is now defined as an issuer that, upon completion of its IPO, is classified as an exempt issuer on the TSE or has a market capitalization of at least $100 million after its IPO. As a consequence of this change, approximately 20% of issuers that were subject to escrow in 1997 and 1998 would be exempt issuers under the National Policy.

The concept of an issuer changing its classification from emerging issuer to established issuer status has been retained. If an emerging issuer becomes an established issuer, there will be an automatic release of escrow securities equal to the amount of securities that would have been released to date as if it were an established issuer on its IPO, and any securities remaining in escrow will be released in accordance with the established issuer schedule.

8. Issuer Classification Thresholds

The CSA received several comments on thresholds. A few commenters stated that the threshold for exempt issuer status was too high. As noted above, we agree and have lowered the threshold for exempt issuer status by adopting the TSE category for exempt issuers.

A few commenters stated that the categories resulted in inappropriate treatment for technology issuers that often have limited cash flow and profit. Other commenters pointed out inconsistencies in the treatment of research issuers once such issuers begin commercialization of product.

A commenter stated that the emerging issuer definition was confusing, and should be stated in positive terms. Another commenter made detailed suggestions as to certain elements of the natural resource category, in line with industry criteria and practice.

The CSA agree that the classifications set out in the initial proposal were not entirely appropriate, nor were they easily applied. In consultation with the Canadian exchanges, we adopted exchange categories for use under the National Policy.

In particular:

- TSE listed exempt issuers are be classified as "exempt issuers".

- Other TSE listed issuers and CDNX listed Tier 1 issuers are classified as "established issuers".

- CDNX listed Tier 2 issuers are classified as "emerging issuers".

- Issuers listed only on the Bourse de Montréal Inc. (Bourse) are classified based on the same criteria. If a Bourse-listed issuer meets the CDNX Tier 1 minimum listing criteria, the issuer is classified as an "established issuer". Otherwise the issuer is classified as an "emerging issuer".

In addition, to address competition concerns, issuers whose market capitalization after their IPO is at least $100 million are also exempt from escrow.

A few commenters suggested that more categories be created to allow for differences in treatment among issuers that are not exempt. We believe that these concerns are addressed by the significant reduction in escrow periods.

9. Treatment of Options

One commenter suggested that we broaden the definition of "option" to exclude from escrow options exercisable for cash, shares or a combination of both to allow issuers flexibility in designing compensation programs. We believe that broadening the exclusion may invite abuse.

A commenter stated that all options be excluded from application of the escrow regime. We disagree because options are no different from other securities. There is an exception for non-transferable incentive stock options issued to directors, officers or employees because these are governed by other policies.

Another commenter stated that issuers would avoid granting options to insiders until after the IPO is receipted in order to avoid the application of escrow. We do not see this as a problem because the exercise price of options must be at least equal to the market price of the securities on the day they are granted.

10. Change in the Issuer's Status after the IPO

A few commenters commented that established issuers should be allowed to become exempt issuers after their IPO, which would result in the immediate release of all escrow securities. There is no compelling need for this change since we reduced the length of the escrow period for established issuers. An18-month escrow period is too short a period to warrant a review. Therefore we have not included a provision for change in status from an established issuer to an exempt issuer.

11. Release from Escrow – Departure of Principals

A commenter stated that the securities of an officer who is terminated without cause should be automatically released from escrow, as the rationale for escrow no longer exists, although the commenter was of the view that voluntary resignation should not result in a release.

Another commenter stated that there should be an automatic release from escrow of the securities of any director or officer who leaves the position, whether voluntarily or involuntarily.

We disagree with the automatic release from escrow of the shares of departing principals, because this may encourage principals to depart prematurely. However, we agree that it would be beneficial to allow a departing principal to transfer

shares to a new principal, and to allow principals to transfer shares among themselves, to reflect re-arrangements of responsibilities. Therefore the National Policy allows transfers among principals at any time.

12. Release from Escrow - Release upon Take-over Bid

Several commenters questioned the rationale for requiring exchanged securities to be substituted for previously escrowed securities on completion of a take-over bid. The reasons stated included:

- Minority securityholders of the acquiror do not need or expect escrow protection.
- In an exchange bid, the participation of the initial principals will be diluted.
- Control of the issuer will in most cases shift away from the initial principals.
- Escrow continuation may artificially affect the consideration paid in the transaction and may reduce the value obtained by the shareholders of the target company.

Some of the commenters suggested that:

- Securities should be released if the principal will not be a principal of the successor issuer after completion of the take-over bid.
- Securities should be released if the successor issuer is an exempt issuer after completion of the take-over bid.
- The opportunity for change of status should be available to the successor issuer after completion of the take-over bid.
- Securities should be released from escrow if the principal's holding in the successor issuer is de minimis after completion of the take-over bid.

We agree. These changes have been made.

13. Release from Escrow – Release upon Death

A few commenters questioned the news release requirement upon the death of a principal, especially where the death does not constitute a material change. The CSA agree. The National Policy does not require a news release. In the event the death constitutes a material change in the affairs of the issuer, general disclosure requirements will apply.

14. Release from Escrow – Release upon Emerging Issuer Becoming Established Issuer

A commenter questioned the provision requiring released securities to be returned to escrow if the issuer did not meet the criteria for becoming an established issuer. We agree that this would have been a problem; however with the change to exchange classifications, there will be no doubt whether an issuer's classification has changed, and therefore this situation should not arise.

15. Transfers within Escrow – Transfers to Directors and Senior Officers

A few commenters questioned the propriety of requiring the issuer's board of directors to approve a transfer between directors and senior officers. While directors are required to act in the issuer's best interest, they note that these may not be the same as the shareholders or otherwise consistent with the purposes of escrow.

We disagree. At the time of the transfer, a decision made in the best interests of the issuer furthers the purpose of escrow. The transfer to a new director or senior officer or an existing director or senior officer will further the successful completion of the issuer's business plan.

A commenter notes that it is inconsistent to require all principals to escrow their securities and then restrict transfers to directors and senior officers. We agree. The National Policy permits the transfer of escrow securities to a 20% holder and to a person or company that will be a 10% holder with the right to appoint a director or senior officer after the transfer.

16. Transfers within Escrow – Transfers upon Bankruptcy or to Certain Plans

A commenter stated that the provision allowing transfers to RRSPs and RRIFs should be expanded to allow transfers to spousal RRSPs, to allow holders of escrow securities more latitude in tax planning, provided the securities remain in escrow on the same terms.

We agree. The National Policy allows transfers within escrow to any similar registered plan with a trustee, provided the beneficiaries of the plan are limited to the original principal, and his or her spouse, children and parents.

A commenter stated that RRSP trustees might be unwilling to sign the escrow agreements. We are not aware of this having been a problem in the past.

A commenter noted that if the principal goes bankrupt the trustee would need to sell the escrow securities. We have not made this change. The trustee will be subject to the same restrictions upon transfer of the escrow securities as applied to the principal. This result is consistent with the purpose of escrow and accurately reflects the value of the escrow securities.

17. Dealing with Escrow Securities – Prohibitions on Pledging Escrow Securities

Several commenters stated that the outright prohibition on pledging escrow securities was unduly restrictive, and that principals should be permitted to pledge their escrow securities as security for a loan. A commenter pointed out that the prohibition is particularly problematic for active business corporations that often charge assets in standard banking arrangements.

The CSA also took note of the fact that in certain Canadian jurisdictions, the pledge of escrow securities is common business practice. We balanced these comments against the anti-avoidance purpose of the prohibition and the concern that

a principal may be less committed to the issuer if the securities have been pledged, and would certainly be less committed if the securities have been realized upon by the pledgee.

The National Policy permits a principal to pledge, mortgage or charge escrow securities as collateral for a loan from a financial institution. If the financial institution realizes upon the securities, the securities will be subject to the same escrow conditions as they were in the hands of the principal. In addition, anti-avoidance provisions have been added to the National Policy and standard escrow agreement.

18. Secondary Offerings

A few commenters urged the CSA to consider the introduction of an automatic release mechanism for secondary offerings by way of prospectus. In support they pointed out that:

- Prospectus level disclosure exists.
- The sale demonstrates the favourable attitude of the market to the secondary offering.
- If a situation arises that securities regulators perceive as abusive, the securities regulators may refuse to give a receipt for the prospectus.
- Securities regulators have allowed releases in these circumstances in the past.
- It would weaken the US competitive advantage, as it would parallel the US policy allowing affiliates to sell their shares free of Rule 144 limitations by preparing a registration statement.

The CSA agree that it would be beneficial to permit principals to sell their escrow securities at the time of the issuer's IPO in a secondary offering that is disclosed in the IPO prospectus. Under the National Policy, if the secondary offering is underwritten, any principal may sell their escrow securities. If the secondary offering is on a best efforts basis, only principals that are not promoters, directors or senior officers may sell their escrow securities, provided all or the specified minimum number of securities offered by the issuer in the IPO are sold.

The National Policy restricts secondary offerings by principals to the time of the issuer's IPO. The IPO purchasers will have notice of the securities to be sold or proposed to be sold by principals, and will be able to form their decisions to purchase securities in the IPO based on full information.

19. Non-Compliant Arrangements

Two commenters stated that it was unduly burdensome not to assign responsibility for accepting non-compliant arrangements to only one jurisdiction. Securities regulators in each jurisdiction where the issuer's IPO prospectus is filed have jurisdiction over the escrow agreement and the escrow securities. The securities regulators will apply mutual reliance principles in administering the National Policy.

20. Transitional

A commenter suggested that the initial proposal be amended to include a mechanism for opting into the new regime. Another commenter requested clarification of the escrow requirements that will apply once the rule is adopted.

Section 8.1 of the National Policy permits, on the conditions set out in that section, amendments to escrow agreements made prior to the date of the National Policy to reflect the release terms in the National Policy.

21. Application to Reverse Take-Overs, Junior Capital Pool Companies and Similar Transactions

A commenter requested guidance on the terms of escrow that will apply to reverse take-overs, junior capital pool companies and similar transactions.

Another commenter suggested that the CSA should decline to make escrow requirements based on the initial proposal for reverse take-overs, junior capital pool companies and similar transactions. In the commenter's opinion, the terms of the initial proposal were not appropriate for these transactions and would be detrimental to the policy objectives of these initiatives.

We have worked in consultation with representatives of the Canadian exchanges in revising the initial proposal. We have deferred to the Canadian exchanges for escrow policies applicable to reverse take-overs, reorganizations, reactivations, junior capital pool companies, major acquisitions and similar transactions, and to direct listings. The policies of the Canadian exchanges are consistent and harmonious with the National Policy.

22. Additional Requirements if there is no Underwriter or Listing

Two commenters questioned the rationale for imposing additional escrow requirements if there is no underwriter involved in an IPO, or if an issuer's equity securities will not be listed on a Canadian exchange on completion of its IPO. They pointed out that underwriters do not generally require a lock-up for more than 180 days, and the securities held by pre-IPO shareholders would generally be subject to a one year hold period from listing under applicable legislation.

The National Policy continues to make it clear that securities regulators may impose additional or different escrow terms in these circumstances. This is because the function served by the underwriters when they price an IPO, effectively valuing the issuer, and the function served by a Canadian exchange in regulating the issuer are not present.

23. Application on a National Basis

Most commenters supported a national regime, although one commenter was of the view that different escrow arrangements are appropriate to allow for innovation and market segmentation. The commenter pointed out that each Canadian exchange has developed a different market segment and needs a framework that allows the specialization to continue.

The CSA believe that this commenter's concern has been addressed by the reorganization of the Canadian exchanges and the revisions to the initial proposal made in consultation with the Canadian exchanges.

24. Mergers and Amalgamations

A commenter suggested that an exemption from the initial proposal be available for an IPO of an amalgamated company. The CSA agree and made this change.

The CSA also noted that the initial proposal did not adequately deal with the escrow of securities of issuers resulting from business combinations (successor issuers). Section 5.3 of the National Policy addresses the escrow of securities of successor issuers.

B. Comments on Passive Investor Provisions and the Treatment of Venture Capital Organizations

Under the initial proposal:

- An investor holding more than 10% of the outstanding voting securities of an issuer (other than an exempt issuer) prior to the issuer's IPO was subject to escrow requirements, unless the investor was a "passive investor".
- An "institutional investor" was deemed to be a "passive investor" unless the institutional investor selected a director or senior officer or effectively controlled the issuer.
- Venture capital organizations were not included in the list of investors that were considered "institutional investors".
- An investor could apply to a securities regulator to be considered a passive investor. The initial proposal included a list of relevant factors.

The CSA received many comments from venture capital organizations and other commenters with respect to this aspect of the initial proposal.

Venture capital organizations stated that their securities should be exempt from escrow, citing the following reasons:

- There is no rationale that justifies imposing escrow on venture capital organizations because IPO investors do not look to them as principals responsible for carrying out the IPO business plan.
- Venture capital investments are generally designed for the medium term. The venture capital organization will have typically held the investment for 3 to 8 years prior to the issuer's IPO, and should not be denied an exit opportunity at the IPO stage.
- If venture capital organizations are forced to hold their investments in issuers for the additional length of time required by the initial proposal, they will decrease their investment in start-ups.
- IPOs by Canadian issuers in Canada will be less frequent because issuers will choose to conduct their IPOs in the US or will sell equity to strategic buyers.
- The delay of sales by venture capital organizations of their escrow securities will delay the recycling of venture capital funds into other pre-public issuers.
- Sources of capital for venture capital organizations will shrink, because investors in venture capital organizations will not want to receive escrow securities or a delayed return.

They claimed that the initial proposal contrasted sharply with the local policies under which venture capital organizations were operating.

Venture capital organizations and others had the following comments on the initial proposal:

- Venture capital organizations should be included in the list of institutional investors. One commenter questioned the distinction between the Business Development Bank of Canada and financial institutions that make investments directly (which were included in the list of institutional investors) and financial institutions that make investments through venture capital subsidiaries (which were not considered institutional investors).
- Venture capital organizations should not be precluded from being considered institutional investors as a consequence of having selected a director or senior officer of the issuer. Venture capital organizations often put a nominee on the issuer's board of directors as a means of obtaining information about the issuer. This is beneficial to the issuer as it provides the issuer with access to the venture capital organization's experience. Board representation is not synonymous with control or direction over the issuer and a test for de facto control would be more appropriate.
- Effective control should be determined at the conclusion of the issuer's IPO, not prior to the IPO.
- A discretionary relief provision should be added allowing a venture capital organization that is not otherwise exempt as an institutional investor to apply for a designation as an institutional investor, to avoid the necessity of applying on an investment-by-investment basis.
- Greater clarification should be made to the factors listed for consideration as a passive investor. Examples of factors requiring greater clarification include that the investor not be "involved in the management of the issuer", and not have a prior or existing "significant relationship" with a principal of the issuer.
- If the securities held by a venture capital organization are escrowed, a provision should be added permitting the distribution of the escrow securities to the beneficial owners of the venture capital organization.

In response, the National Policy:

- rationalizes the treatment of venture capital organizations with other significant investors and dispenses with the problematic concepts of "passive investor" and "institutional investor",
- ensures that the imposition of escrow on securities of significant investors is consistent with the purpose of escrow,
- ensures that the escrow regime is reasonable and will not unduly interfere with venture capital investment,
- makes the test for determining whether an investor's securities will be subject to escrow objective and straightforward, and
- eliminates the need for costly and time-consuming applications which can result in inconsistent treatment of investors.

We have redesigned the definition of principal as it relates to significant investors, so that:

- an investor will be considered a principal if the investor holds more than 20% of the voting rights attached to the issuer's outstanding securities after completion of the issuer's IPO, and
- an investor that holds more than 10% but 20% or less of the voting rights attached to the issuer's outstanding securities after the issuer's IPO will only be considered a principal if the investor selects or has the right to select a director or senior officer of the issuer or a material operating subsidiary.

The CSA are of the view that an investor holding more than 20% of the voting securities of a public issuer is likely to have effective control of or significant influence over the issuer.

The CSA are also of the view that if an investor holding more than 10%, but 20% or less of the voting rights attached to the issuer's outstanding securities has selected or has the right to select a director or senior officer of the issuer or of a material operating subsidiary upon the completion of the issuer's IPO, then it is likely that the investor is participating in the management of the issuer through the selection of a "corporate director". Accordingly, the investor's securities should be subject to escrow.

This approach is consistent with the purpose of escrow. The test is objective, straightforward and applies to all investors equally. We believe that it is fair and appropriate to subject the securities of a venture capital organization to escrow if it is participating in management of the issuer.

The CSA believe that changes made to other aspects of the initial proposal address the liquidity concerns expressed by the venture capital organizations. These include the following:

- We have expanded the class of exempt issuers.
- We have significantly reduced the escrow period from 3 years to 18 months for an established issuer, and from 6 years to 3 years for an emerging issuer.
- 75% of the venture capital organization's securities in an established issuer, and 40% of its securities in an emerging issuer, will be released within one year from listing.
- An emerging issuer may become an established issuer, resulting in an automatic release of securities no longer subject to escrow under the established issuer release schedule, and an accelerated release of any remaining securities.
- All of the venture capital organization's securities in an issuer may be sold at the time of the issuer's IPO in a secondary offering on a firmly underwritten basis or, subject to certain conditions, on a best efforts basis, so long as the secondary offering is disclosed in the IPO prospectus.

C. ESCROW AGENTS' COMMENTS

1. Trust Company as Escrow Agent

Several commenters disagreed with the initial proposal that only trust companies be permitted to act as escrow agents, and commented that transfer agents should be permitted to act as escrow agents. The following reasons were given in support:

- Transfer agents have control over registration of securities, and associated rights of ownership are in the transfer agent's hands.
- The initial proposal will not result in equality in treatment of companies that provide escrow agent services from province to province, as requirements for a trust company under trust legislation differ from province to province.
- The initial proposal is anti-competitive and will result in higher costs being paid by issuers.
- The requirement does not add to the protection of the investing public, as the escrow agency relationship is a contractual relationship, the escrow agent is not asked to exercise any discretionary trust powers, the escrow securities are in registered form, not readily fungible and are not covered by CDIC insurance.

We agree that the class of persons who could act as escrow agent under the initial proposal was too limited. The National Policy permits any person or company that a Canadian exchange has approved to act as a transfer agent to be an escrow agent.

Another commenter stated that the underwriter for the issuer's IPO and legal counsel should also be entitled to act as escrow agent. The CSA are of the view that trust companies and other persons and companies that act as transfer agents have

the appropriate relationship with the issuer and infrastructure in place to carry out escrow agent duties.

2. Indemnification of Escrow Agent

A few commenters stated that the indemnity of the escrow agent should be from the issuer and the securityholders, jointly and severally. This change was made.

A few commenters requested that language be added providing that the indemnity survives the release of all escrow securities and the termination of the escrow agreement. This change was made.

3. Drafting Comments

CSA received several technical drafting comments for the escrow agreement that we adopted.

4. Additional Provisions

A commenter suggested that a provision for the appointment of the escrow agent should be added to the escrow agreement. This change was made.

A commenter suggested that a provision be added to the escrow agreement directing the escrow agent to release escrow securities upon evidence of a decision of the appropriate securities regulators. To address this and other comments, we have added to the escrow agreement provisions noting the securities regulators with jurisdiction and requiring the consent of securities regulators to any amendments.

Commenters requested that the following provisions be added to the escrow agreement:

- The Escrow Agent shall not be responsible for the sufficiency, correctness, genuineness or validity of any securities deposited with it.
- The Escrow Agent shall be protected in acting upon any written document it receives, as to the document's due execution, validity and effectiveness, and the truth of its contents.
- The Escrow Agent may employ independent counsel and other advisors for the purpose of discharging its duties under the escrow agreement at the cost of the Issuer.
- The Escrow Agent shall have no duties or liabilities except those expressly set forth in the escrow agreement.
- The Escrow Agent shall not be bound by any notice of a claim or demand with respect thereto, or any waiver, modification, amendment, termination or rescission of the escrow agreement unless received by it in writing, and signed by the other parties, and, if the duties or indemnification of the Escrow Agent herein are affected, unless it shall have given its prior written consent.
- This is the entire agreement among the parties concerning the subject matter set out herein and supersedes any and all prior understandings and agreements.

We agree and added similar provisions to the escrow agreement.

We did not agree with the suggestion to add a provision stating that the Escrow Agent shall not be liable for any action taken or omitted by it, or any action suffered by it to be taken or omitted excepting only its own gross negligence or wilful misconduct. We do not agree that this is an appropriate standard of care. The appropriate standard of care is negligence.

NATIONAL POLICY 46-201
ESCROW FOR INITIAL PUBLIC OFFERINGS

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NATIONAL POLICY 46-201
ESCROW FOR INITIAL PUBLIC OFFERINGS

Securities regulators usually require an issuer making an initial public offering to enter into an escrow agreement with its principals and an escrow agent. We may also require an escrow agreement in connection with a prospectus when public investors are asked to finance a significant change of business and escrow has not been previously imposed on the issuer's principals in connection with that business.

Under an escrow agreement principals place their securities in escrow with an escrow agent. Principals are restricted from selling or dealing in other ways with the escrow securities until they are released from escrow according to the escrow agreement.

This Policy describes the circumstances where securities regulators consider an escrow agreement necessary or desirable and the terms of escrow we consider appropriate. Until recently, different provinces had different escrow policies. This Policy describes uniform terms for escrow agreements that will be used throughout Canada.

Part I – Purpose and Interpretation

1.1 What is the purpose of escrow?

(1) A public investor who buys securities in an initial public offering or an offering to fund a significant change of business relies on the issuer's management and principal securityholders to carry out the plans described in the issuer's prospectus. This is particularly true for issuers with a limited history of operations.

(2) An escrow agreement ties the issuer's management and its principal securityholders to the issuer by restricting their ability to sell their securities for a period of time following the issuer's offering. This gives them an incentive to devote their time and attention to the issuer's business while they are securityholders.

1.2 Interpretation

(1) When we refer to securities that a person or company "holds", we mean that the person or company has direct or indirect beneficial ownership of, or control or direction over, the securities.

(2) You should use common sense in applying this Policy to your own circumstances, as we will apply the Policy according to its purpose.

1.3 Will a Canadian exchange impose additional escrow terms?

A Canadian exchange may impose additional conditions or more stringent release terms.

Part II – Application of the Policy

2.1 When does this Policy apply?

This Policy applies when an issuer and/or one or more of its securityholders distributes shares or convertible securities (both defined in section 3.7) to the public by prospectus in one of the following ways (an **IPO**):

(a) an initial distribution by the issuer

(b) a distribution by one or more of the issuer's securityholders if it is the initial public distribution of the issuer's securities (e.g., a corporate spin-off)

(c) a distribution, other than an initial distribution, by a reporting issuer and/or one or more of its securityholders, if no escrow has been previously imposed by a securities regulator or a Canadian exchange on the issuer's principals in connection with its current business.

2.2 What are the exceptions?

(1) This Policy does not apply to a distribution by:

(a) an exempt issuer (defined in section 3.2);

(b) a capital pool company under Canadian Venture Exchange Inc. (CDNX) Policy 2.4;

(c) a Tier 3 issuer listed on CDNX; or

(d) an issuer that, following a business combination, is a successor to issuers whose principals have been subject to escrow requirements.

(2) This Policy generally does not apply when there is only a prospectus that does not offer securities to the public, such as a prospectus that an issuer files with a securities regulator only to become a "reporting issuer".

2.3 How does this Policy apply to special warrant prospectuses?

(1) Special warrants are convertible securities that a principal is required to place in escrow. The principal must also place the securities issued on conversion of the special warrants in escrow, even if the securities are qualified under the prospectus.

(2) A prospectus that only qualifies the securities issued on conversion of special warrants is generally not an IPO prospectus because there are no additional proceeds raised. However, if there is a market for the securities, the prospectus may be considered an IPO prospectus for the purpose of this Policy. Otherwise, the IPO prospectus will be the next prospectus of the issuer that makes a public offering.

2.4 Can securities regulators impose additional or different terms?

A securities regulator may impose additional or different escrow terms if:

(a) an underwriter has not signed the IPO prospectus;

(b) the issuer has not applied to have its securities listed on a Canadian exchange, or a Canadian exchange has not agreed to list the securities distributed under the IPO prospectus; or

(c) there are other exceptional circumstances.

Part III – Escrow Classifications

3.1 Escrow classifications

Issuers are classified as either exempt issuers, established issuers or emerging issuers. Whether or not an issuer's securities will be subject to escrow, and the schedule for release of escrow securities from escrow will depend on the classification of the issuer.

3.2 Exempt issuers

Securities regulators do not generally consider that escrow is necessary for an exempt issuer. An **exempt issuer** is an issuer that, after its IPO:

(a) has securities listed on The Toronto Stock Exchange (TSE) and is classified by the TSE as an exempt issuer; or

(b) has a market capitalization of at least $100 million. (In calculating market capitalization, multiply the number of the outstanding securities of the class of securities offered on the IPO, on completion of the IPO, by the IPO price.)

3.3 Established and emerging issuers

(1) Securities regulators generally consider that escrow is necessary for established and emerging issuers.

(2) An **established issuer** is an issuer that, after its IPO:

(a) has securities listed on the TSE and is not classified by the TSE as an exempt issuer;

(b) has securities listed on the CDNX and is a CDNX Tier 1 issuer; or

(c) has securities listed on the Bourse de Montréal Inc. **(Bourse)** and is eligible to be classified as a CDNX Tier 1 issuer.

(3) An **emerging issuer** is an issuer that, after its IPO, is not an exempt issuer or an established issuer.

3.4 When is an issuer classified for escrow purposes?

An issuer is classified based on its circumstances immediately after completion of its IPO. If an emerging issuer becomes an established issuer at a later point, it may have the release schedule changed. See section 4.4.

3.5 Whose securities are subject to escrow?

(1) Securities regulators generally require principals of an emerging or established issuer to place their securities in escrow under an escrow agreement.

(2) A **principal** of an issuer is:

(a) a person or company who acted as a promoter of the issuer within two years before the IPO prospectus

(b) a director or senior officer of the issuer or any of its material operating subsidiaries at the time of the IPO prospectus

(c) a **20% holder** – a person or company that holds securities carrying more than 20% of the voting rights attached to the issuer's outstanding securities immediately before and immediately after the issuer's IPO

(d) a **10% holder** – a person or company that

(i) holds securities carrying more than 10% of the voting rights attached to the issuer's outstanding securities immediately before and immediately after the issuer's IPO and

(ii) has elected or appointed, or has the right to elect or appoint, one or more directors or senior officers of the issuer or any of its material operating subsidiaries.

(3) In calculating these percentages, include securities that may be issued to the holder under outstanding convertible securities in both the holder's securities and the total securities outstanding.

(4) A company, trust, partnership or other entity more than 50% held by one or more principals will be treated as a principal. (In calculating this percentage, include securities of the entity that may be issued to the principals under outstanding convertible securities in both the principals' securities of the entity and the total securities of the entity outstanding.) Any securities of the issuer that this entity holds will be subject to escrow requirements.

(5) A principal's spouse and their relatives that live at the same address as the principal will also be treated as principals and any securities of the issuer they hold will be subject to escrow requirements.

3.6 Are any principals exempt from escrow requirements?

A principal that holds securities carrying less than 1% of the voting rights attached to an issuer's outstanding securities immediately after its IPO is not subject to escrow requirements. (In calculating this percentage, include securities that may be issued to that principal under outstanding convertible securities in both the principal's securities and the total securities outstanding.)

3.7 What types of securities are subject to escrow?

3.7.1 Escrow securities

(1) The following securities are subject to escrow **(escrow securities)** if a principal holds them immediately before the issuer's IPO:

(a) **shares** – equity securities that carry the right to participate in earnings and assets remaining on winding-up or liquidation, including common shares, restricted voting shares, subordinate voting shares, multiple voting shares and non-voting shares

(b) **convertible securities** – securities that allow the holder to acquire shares or other convertible securities (such as warrants, special warrants qualified under the IPO prospectus, convertible shares, convertible debentures, rights and options), except for non-transferable incentive stock options issued to principals of the issuer to purchase securities solely for cash at a price equal to or greater than the IPO price

(2) Securities will be released from escrow if they are sold in a "permitted secondary offering" which is defined in section 3.8.

3.7.2 Additional escrow securities

Shares and convertible securities that a holder of escrow securities acquires in relation to securities that are in escrow at the time:

(a) as a dividend or other distribution;

(b) on the exercise of a right of purchase, conversion or exchange, including securities received on conversion of special warrants;

(c) on a subdivision, or compulsory or automatic conversion or exchange; or

(d) from a successor issuer in a business combination, if this is required under Part V

(additional escrow securities) must be placed in escrow by the holder.

3.8 What is a permitted secondary offering?

(1) A principal may sell its securities in the issuer in the issuer's IPO free of escrow in the following circumstances **(a permitted secondary offering)**:

(a) the sale is conducted on a firmly underwritten basis; or

(b) the sale is conducted on a best efforts basis after completion of the sale by the issuer of all or the specified minimum number of its securities offered in the IPO (if any), if the principal is not a promoter, director or senior officer of the issuer or any of its material operating subsidiaries.

(2) The permitted secondary offering must be disclosed in the IPO prospectus.

3.9 Is there a standard form of escrow agreement?

The terms of escrow are set out in a written escrow agreement among an emerging issuer or an established issuer, an escrow agent and the issuer's principals whose securities are subject to escrow. The standard form of escrow agreement is attached as an Appendix to this Policy. An issuer must file a copy of the signed escrow agreement with securities regulators in the jurisdictions where the issuer files its IPO prospectus.

3.10 Who may be an escrow agent?

A person or company approved by a Canadian exchange to act as a transfer agent may be an escrow agent.

Part IV – Release of Escrow Securities from Escrow

4.1 When are escrow securities released from escrow?

(1) The release of escrow securities from escrow will vary depending on the escrow classification of the issuer that issued the securities. Principals of established issuers will have their escrow securities released from escrow over an 18-month period. Principals of emerging issuers will have their escrow securities released over a three-year period. The timing of escrow release will also be affected if a securityholder dies, if an emerging issuer becomes an established issuer, or if an issuer is party to a business combination.

(2) The escrow agreement sets out release procedures for escrow securities.

4.2 Release schedule for established issuers

4.2.1 Usual case

A principal's escrow securities in an established issuer are released as follows:

On the date the issuer's securities are listed on a Canadian exchange **(the listing date)**	25% of the escrow securities
6 months after the listing date	25% of the escrow securities
12 months after the listing date	25% of the escrow securities
18 months after the listing date	25% of the escrow securities

4.2.2 If there is a permitted secondary offering

(1) If a principal has sold in a permitted secondary offering more than 25% of that principal's escrow securities, the principal's escrow securities are released as follows:

For delivery to complete the issuer's IPO	All escrow securities sold in the permitted secondary offering
6 months after the listing date	33 1/3% of the unsold escrow securities
12 months after the listing date	33 1/3% of the unsold escrow securities
18 months after the listing date	33 1/3% of the unsold escrow securities

(2) If a principal has sold in a permitted secondary offering 25% or less of that principal's escrow securities, the principal's escrow securities are released as follows:

For delivery to complete the issuer's IPO	All escrow securities sold in the permitted secondary offering
On the listing date	25% of the escrow securities less the escrow securities sold in the permitted secondary offering
6 months after the listing date	25% of the escrow securities
12 months after the listing date	25% of the escrow securities
18 months after the listing date	25% of the escrow securities

4.2.3 Additional escrow securities

If a holder of escrow securities acquires additional escrow securities, they are released in equal portions on the remaining release dates.

4.3 Release schedule for emerging issuers

4.3.1 Usual case

A principal's escrow securities in an emerging issuer are released as follows:

On the date the issuer's securities are listed on a Canadian exchange **(the listing date)**	10% of the escrow securities
6 months after the listing date	15% of the escrow securities
12 months after the listing date	15% of the escrow securities
18 months after the listing date	15% of the escrow securities
24 months after the listing date	15% of the escrow securities
30 months after the listing date	15% of the escrow securities
36 months after the listing date	15% of the escrow securities

4.3.2 Alternate meaning of "listing date"

The **listing date** is the date the issuer completes its IPO if:

(a) the issuer's securities are not listed on a Canadian exchange immediately after its IPO; or

(b) the issuer's securities are listed on a Canadian exchange immediately before its IPO.

4.3.3 If there is a permitted secondary offering

(1) If a principal has sold in a permitted secondary offering more than 10% of that principal's escrow securities, the principal's escrow securities are released as follows:

For delivery to complete the issuer's IPO	All escrow securities sold in the permitted secondary offering
6 months after the listing date	16 2/3% of the unsold escrow securities
12 months after the listing date	16 2/3% of the unsold escrow securities
18 months after the listing date	16 2/3% of the unsold escrow securities
24 months after the listing date	16 2/3% of the unsold escrow securities
30 months after the listing date	16 2/3% of the unsold escrow securities
36 months after the listing date	16 2/3% of the unsold escrow securities

(2) If a principal has sold in a permitted secondary offering 10% or less of that principal's escrow securities, the principal's escrow securities are released as follows:

For delivery to complete the issuer's IPO	All escrow securities sold in the permitted secondary offering
On the listing date	10% of the escrow securities less the escrow securities sold in the permitted secondary offering
6 months after the listing date	15% of the escrow securities
12 months after the listing date	15% of the escrow securities
18 months after the listing date	15% of the escrow securities
24 months after the listing date	15% of the escrow securities
30 months after the listing date	15% of the escrow securities
36 months after the listing date	15% of the escrow securities

4.3.4 Additional escrow securities

If a holder of escrow securities acquires additional escrow securities, they are released in equal portions on the remaining release dates.

4.4 What happens if an emerging issuer becomes an established issuer after its IPO?

(1) An emerging issuer becomes an established issuer if it:

(a) lists its securities on the TSE;

(b) becomes a CDNX Tier 1 issuer;

(c) has its securities listed on the Bourse and become eligible to be classified as a CDNX Tier 1 issuer; or

(d) lists or quotes its securities on an exchange or market outside Canada that its "principal regulator" under National Policy 43-201 Mutual Reliance Review System for Prospectuses and Annual Information Forms or, if the issuer has only filed its IPO prospectus in one jurisdiction, the securities regulator in that jurisdiction, is satisfied has minimum listing requirements at least equal to those of CDNX Tier 1.

(2) If an emerging issuer becomes an established issuer 18 months or more after its listing date, all escrow securities will be released immediately.

(3) If an emerging issuer becomes an established issuer within 18 months after its listing date, all escrow securities that would have been released to that time, if the issuer was an established issuer on its listing date, will be released immediately. Remaining escrow securities will be released in equal instalments on the day that is 6 months, 12 months and 18 months after the listing date.

4.5 Release of escrow securities on death of holder

If a holder of escrow securities dies, the holder's escrow securities will be released from escrow.

4.6 Release of escrow securities

Once escrow securities are released from escrow, they are no longer escrow securities for the purpose of this Policy.

Part V – Business Combinations

5.1 When does this Part apply?

This Part applies to business combinations. A **business combination** is:

(a) a formal take-over bid
(b) a plan of arrangement
(c) an amalgamation
(d) a merger
(e) any other similar transaction

5.2 Can a holder of escrow securities tender them in a business combination?

(1) Yes, a holder of escrow securities can tender them in a business combination. The tendered escrow securities will be released from escrow and delivered under the business combination if the terms and conditions of the business combination have been satisfied or waived.

(2) The escrow agreement contains special procedures for tendering escrow securities.

5.3 If the holder receives securities of another issuer in exchange for the holder's escrow securities, will the new securities be subject to escrow?

If the holder receives securities of another issuer (successor issuer) in exchange for the holder's escrow securities, the new securities will be subject to escrow, if immediately upon completion of the business combination:

(a) the successor issuer is not an exempt issuer (defined in section 3.2);

(b) the holder is a principal (defined in section 3.5) of the successor issuer; and

(c) the holder holds more than 1% of the voting rights attached to the successor issuer's outstanding securities. (In calculating this percentage, include securities that may be issued to the principal under outstanding convertible securities to both the principal's securities and the total securities outstanding.)

5.4 If the new securities are subject to escrow, when will they be released?

(1) If the new securities are subject to escrow, the escrow agent will hold the new securities in escrow on the same terms and conditions, including release dates, as applied to the escrow securities that were exchanged.

(2) However, if the issuer is an emerging issuer, the successor issuer is an established issuer, and the business combination occurs 18 months or more after the issuer's listing date, all escrow securities will be released immediately.

(3) If the issuer is an emerging issuer, the successor issuer is an established issuer and the business combination occurs within 18 months after the issuer's listing date, all escrow securities that would have been released to that time, if the issuer was an established issuer on its listing date, will be released immediately. Remaining escrow securities will be released in equal instalments on the day that is 6 months, 12 months and 18 months after the issuer's listing date.

Part VI – Dealing with Escrow Securities

6.1 Can a holder of escrow securities vote and receive distributions on the escrow securities?

A holder of escrow securities may vote and receive distributions on the holder's escrow securities.

6.2 Restrictions on dealing with escrow securities

Escrow restricts the ability of holders to deal with their escrow securities while they are in escrow. The standard form of escrow agreement sets out these restrictions. Except to the extent that the escrow agreement expressly permits, a principal cannot sell, transfer, mortgage, enter into a derivative transaction concerning, or otherwise deal in any way with the holder's escrow securities or the related share certificates or other evidence of the escrow securities. A private company, controlled by one or more principals of the issuer, that holds escrow securities of the issuer, may not participate in a transaction that results in a change of its control or a change in the economic exposure of the principals to the risks of holding escrow securities.

6.3 When can a holder of escrow securities transfer them within escrow?

(1) A holder may transfer escrow securities within escrow:

(a) to existing or, upon their appointment, incoming directors or senior officers of the issuer or any of its material operating subsidiaries, if the issuer's board of directors has approved the transfer;

(b) to a person or company that before the proposed transfer holds more than 20% of the voting rights attached to the issuer's outstanding securities;

(c) to a person or company that after the proposed transfer

(i) will hold more than 10% of the voting rights attached to the issuer's outstanding securities, and

(ii) has the right to elect or appoint one or more directors or senior officers of the issuer or any of its material operating subsidiaries;

(d) to a trustee in bankruptcy or another person or company entitled to escrow securities on the bankruptcy of the holder;

(e) to a financial institution on the realization of escrow securities pledged, mortgaged or charged by the holder to the financial institution as collateral for a loan; or

(f) to or between a registered retirement savings plan (RRSP), registered retirement income fund (RRIF) or other similar registered plan or fund with a trustee, where the beneficiaries of the plan or fund are limited to the holder and his or her spouse, children and parents.

(2) The escrow agreement sets out transfer procedures for escrow securities.

(3) Securities laws and other legislation may impose additional restrictions on transfer. (See section 7.4.)

6.4 Can a holder pledge, mortgage or charge escrow securities as collateral for a loan?

A holder can pledge, mortgage or charge escrow securities to a financial institution as collateral for a loan. The loan agreement must provide that the escrow securities will remain in escrow if the lender realizes on the escrow securities to satisfy the loan.

6.5 Can a holder exchange or convert convertible escrow securities?

A holder of a convertible security that is in escrow may exchange or convert the security within escrow. Securities acquired on conversion or exchange of convertible escrow securities are additional escrow securities and remain in escrow.

Part VII – General Provisions

7.1 Amendments to escrow agreement require regulatory approval

The securities regulator in each jurisdiction where the issuer files its IPO prospectus has jurisdiction over the escrow agreement and escrow securities of the issuer. No amendment to an escrow agreement is valid unless the securities regulators that have jurisdiction have approved it.

7.2. Will mutual reliance principles apply to escrow filings?

Yes, the securities regulators will apply mutual reliance principles in administering this Policy.

7.3 What happens if an issuer does not complete its IPO?

If an issuer does not complete its IPO and becomes a reporting issuer in one or more jurisdictions because it has obtained a receipt for its IPO prospectus, its escrow agreement will remain in effect until the securities regulators in those jurisdictions order that the issuer has ceased to be a reporting issuer.

7.4 Do local resale restrictions still apply to escrow securities after they are released from escrow?

Although this Policy may permit the release of escrow securities from escrow or permit a holder to transfer or deal in other ways with escrow securities, other restrictions imposed by securities legislation, securities regulators and Canadian exchanges will still apply.

Part VIII – Amendment of Release Terms in Escrow Agreements Made Prior to this Policy

8.1 Can the release terms of escrow agreements made prior to this Policy be amended?

(1) The securities regulators consent to amendments to escrow agreements made prior to the date of this Policy **(existing escrow agreements)** to reflect the release terms of this Policy on the following conditions:

(a) The issuer's board of directors must have approved the amendment.

(b) All parties to the existing escrow agreement, except parties whose securities are no longer in escrow, must have agreed to the amendment.

(c) The issuer must have obtained any approval by a Canadian exchange required by the existing escrow agreement.

(d) The amendment must have been approved by a majority vote of the securityholders of the issuer, or consented to by securityholders holding a majority of the securities of the issuer, excluding in each case escrow securityholders and their affiliates and associates.

(e) The amendment to the release terms must apply to all escrow securities.

(f) Once the escrow agreement has been amended and these conditions have been met, the issuer must issue a news release at least 60 days before the first release of escrow securities under the amended escrow agreement notifying the market of the amendment and the new release terms.

(g) The issuer's classification as an exempt, established or emerging issuer must be determined at the date of the news release.

(h) The news release must set out the date of the first release of escrow securities under the amended escrow agreement. The first release date must be at least 60 days after the news release and that date will take the place of the listing date for purposes of the appropriate release schedule under this Policy.

(i) If the issuer is an exempt issuer, all escrow securities may be released no earlier than 60 days after the news release, subject to the 10% limit in (k) below.

(j) If the issuer is an emerging or an established issuer, the new release schedule must be the schedule included in this Policy for that class of issuer, subject to the 10% limit in (k) below.

(k) The number of escrow securities to be released at any one time may not exceed 10% of the issuer's outstanding securities at the time of release. Securities remaining in escrow after the last scheduled release will continue to be released from escrow at 6-month intervals until all escrow securities have been released.

(l) Escrow securities must be released on a pro rata basis, with each holder of escrow securities receiving the same percentage of the escrow securities that are released as the percentage of total escrow securities held by the holder.

(m) The issuer must file with the securities regulators in the jurisdictions where it filed its IPO prospectus:

(i) a copy of the amended escrow agreement, and

(ii) a certificate of a director or senior officer of the issuer confirming that the escrow agreement has been amended in accordance with this Part.

(2) The parties to an existing escrow agreement may amend the agreement by entering into an agreement in the form of Form 46-201F Escrow Agreement.

(3) Our consent does not limit the right of a Canadian exchange to impose additional conditions or more stringent release terms.

Part IX – Effective Date

This Policy takes effect on September 21, 2001.

This is the form required for escrow arrangements under National Policy 46-201 Escrow for Initial Public Offerings.

APPENDIX

FORM 46-201F
ESCROW AGREEMENT

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ESCROW AGREEMENT

THIS AGREEMENT is made as of the _____ day of _____, _____

AMONG:

(the "**Issuer**")

AND:

(the "**Escrow Agent**")

AND:

EACH OF THE UNDERSIGNED SECURITYHOLDERS OF THE ISSUER
(a "**Securityholder**" or **"you"**)

(collectively, the "**Parties**")

This Agreement is being entered into by the Parties under National Policy 46-201 Escrow for Initial Public Offerings (the **Policy**) in connection with the proposed distribution by the Issuer, an [established/emerging] issuer, of [describe securities] by prospectus (the **IPO**) and/or a proposed distribution by certain Securityholders, namely [names of Securityholders], of [specify number of securities distributed by each Securityholder and what percentage of each Securityholder's securities that number represents] (the **permitted secondary offering**).

For good and valuable consideration, the Parties agree as follows:

PART 1 ESCROW

1.1 Appointment of Escrow Agent

The Issuer and the Securityholders appoint the Escrow Agent to act as escrow agent under this Agreement. The Escrow Agent accepts the appointment.

1.2 Deposit of Escrow Securities in Escrow

(1) You are depositing the securities **(escrow securities)** listed opposite your name in Schedule "A" with the Escrow Agent to be held in escrow under this Agreement. You will deliver to the Escrow Agent any share certificates or other evidence of these securities you receive.

(2) If you receive any other securities **(additional escrow securities)**:

(a) as a dividend or other distribution on escrow securities;

(b) on the exercise of a right of purchase, conversion or exchange attaching to escrow securities, including securities received on conversion of special warrants;

(c) on a subdivision, or compulsory or automatic conversion or exchange of escrow securities; or

(d) from a successor issuer in a business combination, if Part 6 of this Agreement applies,

you will deposit them in escrow with the Escrow Agent. You will deliver to the Escrow Agent any share certificates or other evidence of those additional escrow securities. When this Agreement refers to **escrow securities**, it includes additional escrow securities.

(3) You will deliver to the Escrow Agent any replacement share certificates or other evidence of additional escrow securities issued to you.

1.3 Direction to Escrow Agent

The Issuer and the Securityholders direct the Escrow Agent to hold the escrow securities in escrow until they are released from escrow under this Agreement.

PART 2 RELEASE OF ESCROW SECURITIES

2.1 Release Schedule for an Established Issuer

2.1.1 Usual case

If the Issuer is an **established issuer** (as defined in section 3.3 of the Policy) and you have not sold any escrow securities in a permitted secondary offering, your escrow securities will be released as follows:

On _____, 2___, the date the Issuer's securities are listed on a Canadian exchange **(the listing date)**	25% of your escrow securities
6 months after the listing date	25% of your escrow securities
12 months after the listing date	25% of your escrow securities
18 months after the listing date	25% of your escrow securities

2.1.2 If there is a permitted secondary offering

(1) If the Issuer is an established issuer and you have sold in a permitted secondary offering more than 25% of your escrow securities, your escrow securities will be released as follows:

For delivery to complete the Issuer's IPO	All escrow securities sold by you in the permitted secondary offering
6 months after the listing date	33 1/3% of your unsold escrow securities
12 months after the listing date	33 1/3% of your unsold escrow securities
18 months after the listing date	33 1/3% of your unsold escrow securities

(2) If the Issuer is an established issuer and you have sold in a permitted secondary offering 25% or less of your escrow securities, your escrow securities will be released as follows:

For delivery to complete the Issuer's IPO	All escrow securities sold by you in the permitted secondary offering
On the listing date	25% of your escrow securities less the escrow securities sold by you in the permitted secondary offering
6 months after the listing date	25% of your escrow securities
12 months after the listing date	25% of your escrow securities
18 months after the listing date	25% of your escrow securities

2.1.3 Additional escrow securities

If you acquire additional escrow securities, those securities will be released in equal portions on the remaining release dates.

2.2 Release Schedule for an Emerging Issuer

2.2.1 Usual case

(1) If the Issuer is an **emerging issuer** (as defined in section 3.3 of the Policy) and you have not sold any escrow securities in a permitted secondary offering, your escrow securities will be released as follows:

On _____, 2____, the date the Issuer's securities are listed on a Canadian exchange **(the listing date)**	10% of your escrow securities
6 months after the listing date	15% of your escrow securities
12 months after the listing date	15% of your escrow securities
18 months after the listing date	15% of your escrow securities
24 months after the listing date	15% of your escrow securities
30 months after the listing date	15% of your escrow securities
36 months after the listing date	15% of your escrow securities

(2) The **listing date** is the date the Issuer completes its IPO if:

(a) the Issuer's securities are not listed on a Canadian exchange immediately after its IPO; or

(b) the Issuer's securities are listed on a Canadian exchange immediately before its IPO.

2.2.2 If there is a permitted secondary offering

(1) If the Issuer is an emerging issuer and you have sold in a permitted secondary offering more than 10% of your escrow securities, your escrow securities will be released as follows:

For delivery to complete the Issuer's IPO	All escrow securities sold by you in the permitted secondary offering
6 months after the listing date	16 2/3% of your unsold escrow securities
12 months after the listing date	16 2/3% of your unsold escrow securities
18 months after the listing date	16 2/3% of your unsold escrow securities
24 months after the listing date	16 2/3% of your unsold escrow securities
30 months after the listing date	16 2/3% of your unsold escrow securities
36 months after the listing date	16 2/3% of your unsold escrow securities

(2) If the Issuer is an emerging issuer and you have sold in a permitted secondary offering 10% or less of your escrow securities, your escrow securities will be released as follows:

For delivery to complete the Issuer's IPO	All escrow securities sold by you in the permitted secondary offering
On the listing date	10% of your escrow securities less the escrow securities sold by you in the permitted secondary offering
6 months after the listing date	15% of your escrow securities
12 months after the listing date	15% of your escrow securities
18 months after the listing date	15% of your escrow securities
24 months after the listing date	15% of your escrow securities
30 months after the listing date	15% of your escrow securities
36 months after the listing date	15% of your escrow securities

2.2.3 Additional escrow securities

If you acquire additional escrow securities, those securities are released in equal portions on the remaining release dates.

2.3 Delivery of Share Certificates for Escrow Securities

The Escrow Agent will send to each Securityholder the share certificates or other evidence of that Securityholder's escrow securities released from escrow as soon as reasonably practicable after the release. The share certificates or other evidence of the escrow securities will be sent to the Securityholder's address on the Issuer's share register unless the Securityholder has advised the Escrow Agent in writing otherwise before the escrow securities are released from escrow.

2.4 Replacement Certificates

If, on the date a Securityholder's escrow securities are to be released, the Escrow Agent holds a share certificate or other evidence representing more escrow securities than are to be released, the Escrow Agent will deliver the share certificate or other evidence to the Issuer or its transfer agent and request replacement share certificates or other evidence. The Issuer will cause replacement share certificates or other evidence to be prepared and delivered to the Escrow Agent. After the Escrow Agent receives the replacement share certificates or other evidence, the Escrow Agent will send to the Securityholder or at the Securityholder's direction, the replacement share certificate or other evidence of the escrow securities released. The Escrow Agent and Issuer will act as soon as reasonably practicable.

2.5 Release upon Death

(1) If a Securityholder dies, the Securityholder's escrow securities will be released from escrow. The Escrow Agent will deliver the share certificates or other evidence of the escrow securities to the Securityholder's legal representative.

(2) Prior to delivery the Escrow Agent must receive:

(a) a certified copy of the death certificate; and

(b) any evidence of the legal representative's status that the Escrow Agent may reasonably require.

PART 3 EARLY RELEASE ON CHANGE OF ISSUER STATUS

3.1 Becoming an Established Issuer

If the Issuer is an emerging issuer on the date of this Agreement and, during this Agreement, the Issuer:

(a) lists its securities on The Toronto Stock Exchange;

(b) becomes a Canadian Venture Exchange (**CDNX**) Tier 1 issuer;

(c) if the Issuer's securities are listed on the Bourse de Montréal Inc., becomes eligible to be classified as a CDNX Tier 1 issuer; or

(d) lists or quotes its securities on an exchange or market outside Canada that its "principal regulator" under National Policy 43-201 Mutual Reliance Review System for Prospectuses and Annual Information Forms or, if the Issuer has only filed its IPO prospectus in one jurisdiction, the securities regulator in that jurisdiction, is satisfied has minimum listing requirements at least equal to those of CDNX Tier 1,

then the Issuer becomes an **established issuer**.

3.2 Release of Escrow Securities

(1) When an emerging issuer becomes an established issuer, the release schedule for its escrow securities changes.

(2) If an emerging issuer becomes an established issuer 18 months or more after its listing date, all escrow securities will be released immediately.

(3) If an emerging issuer becomes an established issuer within 18 months after its listing date, all escrow securities that would have been released to that time, if the Issuer was an established issuer on its listing date, will be released immediately. Remaining escrow securities will be released in equal instalments on the day that is 6 months, 12 months and 18 months after the listing date.

3.3 Filing Requirements

(1) Escrow securities will not be released under this Part until the Issuer does the following:

(a) at least 20 days before the date of the first release of escrow securities under the new release schedule, files with the securities regulators in the jurisdictions in which it is a reporting issuer

(i) an officer's certificate stating

(A) that the Issuer has become an established issuer by satisfying one of the conditions in section 3.1 and specifying the condition, and

(B) the number of escrow securities to be released on the first release date under the new release schedule, and

(ii) a copy of a letter or other evidence from the exchange or quotation service confirming that the Issuer has satisfied the condition to become an established issuer; and

(b) at least 10 days before the date of the first release of escrow securities under the new release schedule, issues and files with the securities regulators in the jurisdictions in which it is a reporting issuer a news release disclosing details of the first release of the escrow securities and the change in the release schedule.

(2) If escrow securities remain in escrow after the first release under the new release schedule, then within 10 days after the date of the first release, the Issuer will deliver to the Escrow Agent and file with the securities regulators in the jurisdictions in which it is a reporting issuer an amended copy of this Agreement (with amendments indicated).

3.4 Amendment of Release Schedule

This Agreement will be deemed to be amended to reflect the new release schedule after the Escrow Agent receives an officer's certificate

(a) stating that the Issuer has become an established issuer by satisfying one of the conditions in section 3.1 and specifying the condition;

(b) stating that the release schedule for the Issuer's escrow securities has changed;

(c) stating that the Issuer has issued a news release at least 10 days before the first release date under the new release schedule and specifying the date that the news release was issued; and

(d) specifying the new release schedule.

3.5 First Release under New Schedule

(1) The Escrow Agent will release your escrow securities in accordance with the amended Agreement.

(2) The share certificates or other evidence of a Securityholder's escrow securities will be sent to the Securityholder's address on the Issuer's share register unless the Securityholder has advised the Escrow Agent in writing otherwise before the escrow securities are released from escrow.

PART 4 DEALING WITH ESCROW SECURITIES

4.1 Restriction on Transfer, etc.

Unless it is expressly permitted in this Agreement, you will not sell, transfer, mortgage, enter into a derivative transaction concerning, or otherwise deal in any way with your escrow securities or the related share certificates or other evidence of the escrow securities. If a Securityholder is a private company controlled by one or more principals (as defined in section 3.5 of the Policy) of the Issuer, the Securityholder may not participate in a transaction that results in a change of its control or a change in the economic exposure of the principals to the risks of holding escrow securities.

4.2 Pledge, Mortgage or Charge as Collateral for a Loan

You may pledge, mortgage or charge your escrow securities to a financial institution as collateral for a loan. The loan agreement must provide that the escrow securities will remain in escrow if the lender realizes on the escrow securities to satisfy the loan.

4.3 Voting of Escrow Securities

You may vote your escrow securities.

4.4 Dividends on Escrow Securities

You may receive a dividend or other distribution on your escrow securities, and elect the manner of payment from the standard options offered by the Issuer. If the Escrow Agent receives a dividend or other distribution on your escrow securities, other than additional escrow securities, the Escrow Agent will pay the dividend or other distribution to you on receipt.

4.5 Exercise of Other Rights Attaching to Escrow Securities

You may exercise your rights to exchange or convert your escrow securities.

PART 5 PERMITTED TRANSFERS WITHIN ESCROW

5.1 Transfer to Directors and Senior Officers

(1) You may transfer escrow securities within escrow to existing or, upon their appointment, incoming directors or senior officers of the Issuer or any of its material operating subsidiaries, if the Issuer's board of directors has approved the transfer.

(2) Prior to the transfer the Escrow Agent must receive:

(a) a certified copy of the resolution of the board of directors of the Issuer approving the transfer;

(b) an officer's certificate stating that the transfer is to an existing or, upon his or her appointment, an incoming director or senior officer of the Issuer or a material operating subsidiary and that any required approval from the Canadian exchange the Issuer is listed on has been received;

(c) an acknowledgment in the form of Schedule "B" signed by the transferee;

(d) copies of the letters sent to the securities regulators accompanying the acknowledgement; and

(e) a transfer power of attorney, duly completed and executed by the transferor in accordance with the requirements of the Issuer's transfer agent.

(3) At least 10 days prior to the transfer, the Issuer will file a copy of the acknowledgement with the securities regulators in the jurisdictions in which it is a reporting issuer.

5.2 Transfer to Other Principals

(1) You may transfer escrow securities within escrow:

(a) to a person or company that before the proposed transfer holds more than 20% of the voting rights attached to the Issuer's outstanding securities; or

(b) to a person or company that after the proposed transfer

(i) will hold more than 10% of the voting rights attached to the Issuer's outstanding securities, and

(ii) has the right to elect or appoint one or more directors or senior officers of the Issuer or any of its material operating subsidiaries.

(2) Prior to the transfer the Escrow Agent must receive:

(a) an officer's certificate stating that

(i) the transfer is to a person or company that the officer believes, after reasonable investigation, holds more than 20% of the voting rights attached to the Issuer's outstanding securities before the proposed transfer, or

(ii) the transfer is to a person or company that

(A) the officer believes, after reasonable investigation, will hold more than 10% of the voting rights attached to the Issuer's outstanding securities, and

(B) has the right to elect or appoint one or more directors or senior officers of the Issuer or any of its material operating subsidiaries

after the proposed transfer, and

(iii) any required approval from the Canadian exchange the Issuer is listed on has been received;

(b) an acknowledgment in the form of Schedule "B" signed by the transferee;

(c) copies of the letters sent to the securities regulators accompanying the acknowledgement; and

(d) a transfer power of attorney, duly executed by the transferor in accordance with the requirements of the Issuer's transfer agent.

(3) At least 10 days prior to the transfer, the Issuer will file a copy of the acknowledgement with the securities regulators in the jurisdictions in which it is a reporting issuer.

5.3 Transfer upon Bankruptcy

(1) You may transfer escrow securities within escrow to a trustee in bankruptcy or another person or company entitled to escrow securities on bankruptcy.

(2) Prior to the transfer, the Escrow Agent must receive:

(a) a certified copy of either

(i) the assignment in bankruptcy filed with the Superintendent of Bankruptcy, or

(ii) the receiving order adjudging the Securityholder bankrupt;

(b) a certified copy of a certificate of appointment of the trustee in bankruptcy;

(c) a transfer power of attorney, duly completed and executed by the transferor in accordance with the requirements of the Issuer's transfer agent; and

(d) an acknowledgment in the form of Schedule "B" signed by the trustee in bankruptcy or other person or company legally entitled to the escrow securities.

(3) Within 10 days after the transfer, the transferee of the escrow securities will file a copy of the acknowledgment with the securities regulators in the jurisdictions in which the Issuer is a reporting issuer.

5.4 Transfer Upon Realization of Pledged, Mortgaged or Charged Escrow Securities

(1) You may transfer escrow securities you have pledged, mortgaged or charged under section 4.2 to a financial institution as collateral for a loan within escrow to the lender on realization.

(2) Prior to the transfer the Escrow Agent must receive:

(a) a statutory declaration of an officer of the financial institution that the financial institution is legally entitled to the escrow securities;

(b) a transfer power of attorney, duly executed by the transferor in accordance with the requirements of the Issuer's transfer agent; and

(c) an acknowledgement in the form of Schedule "B" signed by the financial institution.

(3) Within 10 days after the transfer, the transferee of the escrow securities will file a copy of the acknowledgment with the securities regulators in the jurisdictions in which the Issuer is a reporting issuer.

5.5 Transfer to Certain Plans and Funds

(1) You may transfer escrow securities within escrow to or between a registered retirement savings plan (RRSP), registered retirement income fund (RRIF) or other similar registered plan or fund with a trustee, where the beneficiaries of the plan or fund are limited to you and your spouse, children and parents.

(2) Prior to the transfer the Escrow Agent must receive:

(a) evidence from the trustee of the transferee plan or fund, stating that, to the best of the trustee's knowledge, the beneficiaries of the plan or fund do not include any person or company other than you and your spouse, children and parents;

(b) a transfer power of attorney, duly executed by the transferor in accordance with the requirements of the Issuer's transfer agent; and

(c) an acknowledgement in the form of Schedule "B" signed by the trustee of the plan or fund.

(3) Within 10 days after the transfer, the transferee of the escrow securities will file a copy of the acknowledgment with the securities regulators in the jurisdictions in which the Issuer is a reporting issuer.

5.6 Effect of Transfer Within Escrow

After the transfer of escrow securities within escrow, the escrow securities will be held in escrow and released from escrow under this Agreement on the same terms that applied before the transfer.

PART 6 BUSINESS COMBINATIONS

6.1 Business Combinations

This Part applies to the following (**business combinations**):

(a) a formal take-over bid
(b) a plan of arrangement
(c) an amalgamation
(d) a merger
(e) any other similar transaction

6.2 Delivery to Escrow Agent

You may tender your escrow securities to a person or company in a business combination. At least three business days prior to the date the escrow securities must be tendered under the business combination, you must deliver to the Escrow Agent:

(a) a written direction signed by you that directs the Escrow Agent to deliver to the depositary under the business combination either

(i) share certificates or other evidence of the escrow securities, or

(ii) if you have provided the Escrow Agent with a notice of guaranteed delivery or similar notice of your intent to tender the escrow securities to the business combination, that notice,

and a duly completed and executed cover letter or similar document and, where required, transfer power of attorney duly completed and executed for transfer in accordance with the requirements of the depositary, and any other documentation specified or provided by you and required to be delivered to the depositary under the business combination; and

(b) any other information concerning the business combination as the Escrow Agent may reasonably require.

6.3 Delivery to Depositary

Immediately after the Escrow Agent receives the documents and information required under section 6.2, the Escrow Agent will deliver to the depositary, in accordance with the direction, the documentation described in 6.2(a), and a letter addressed to the depositary that

(a) identifies the escrow securities that are being tendered;

(b) states that the escrow securities are held in escrow;

(c) states that the escrow securities are delivered only for the purposes of the business combination and that they will be released from escrow only after the Escrow Agent receives the information described in section 6.4;

(d) if share certificates or other evidence of the escrow securities have been delivered to the depositary, requires the depositary to return to the Escrow Agent, as soon as practicable, the share certificates or other evidence of escrow securities that are not released from escrow into the business combination; and

(e) where applicable, requires the depositary to deliver or cause to be delivered to the Escrow Agent, as soon as practicable, share certificates or other evidence of additional escrow securities that you acquire under the business combination.

6.4 Release of Escrow Securities to Depositary

The Escrow Agent will release from escrow the tendered escrow securities when the Escrow Agent receives a declaration signed by the depositary or, if the direction identifies the depositary as acting on behalf of another person or company in respect of the business combination, by that other person or company, that:

(a) the terms and conditions of the business combination have been met or waived; and

(b) the escrow securities have either been taken up and paid for or are subject to an unconditional obligation to be taken up and paid for under the business combination.

6.5 Escrow of New Securities

If you receive securities (**new securities**) of another issuer (**successor issuer**) in exchange for your escrow securities, the new securities will be subject to escrow in substitution for the tendered escrow securities if, immediately after completion of the business combination:

(a) the successor issuer is not an **exempt issuer** (as defined in section 3.2 of the Policy);

(b) you are a **principal** (as defined in section 3.5 of the Policy) of the successor issuer; and

(c) you hold more than 1% of the voting rights attached to the successor issuer's outstanding securities (In calculating this percentage, include securities that may be issued to you under outstanding convertible securities in both your securities and the total securities outstanding.)

6.6 Release from Escrow of New Securities

(1) The Escrow Agent will send to a Securityholder share certificates or other evidence of the Securityholder's new securities as soon as reasonably practicable after the Escrow Agent receives:

(a) an officer's certificate from the successor issuer

(i) stating that it is a successor issuer to the Issuer as a result of a business combination,

(ii) containing a list of the securityholders whose new securities are subject to escrow under section 6.5, and

(iii) containing a list of the securityholders whose new securities are not subject to escrow under section 6.5; and

(b) if the Securityholder's securities are not subject to escrow under section 6.5, a notice from the Securityholder that the Securityholder wishes to receive share certificates or other evidence of the Securityholder's new securities.

(2) The share certificate or other evidence of a Securityholder's new securities will be sent to the Securityholder's address on the Issuer's share register unless the Securityholder has advised the Escrow Agent in writing otherwise before the new securities are released from escrow.

(3) If your new securities are subject to escrow, the Escrow Agent will hold your new securities in escrow on the same terms and conditions, including release dates, as applied to the escrow securities that you exchanged.

(4) However, if the Issuer is

(a) an emerging issuer, the successor issuer is an established issuer, and the business combination occurs 18 months or more after the Issuer's listing date, all escrow securities will be released immediately; and

(b) an emerging issuer, the successor issuer is an established issuer, and the business combination occurs within 18 months after the Issuer's listing date, all escrow securities that would have been released to that time, if the Issuer was an established issuer on its listing date, will be released immediately. Remaining escrow securities will be released in equal instalments on the day that is 6 months, 12 months and 18 months after the Issuer's listing date.

PART 7 ESCROW AGENT

7.1 Escrow Agent Not Responsible for Genuineness

The Escrow Agent will not be responsible or liable in any manner whatever for the sufficiency, correctness, genuineness or validity of any escrow security deposited with it.

7.2 Escrow Agent Not Responsible for Furnished Information

The Escrow Agent will have no responsibility for seeking, obtaining, compiling, preparing or determining the accuracy of any information or document, including the representative capacity in which a party purports to act, that the Escrow Agent receives as a condition to a release from escrow or a transfer of escrow securities within escrow under this Agreement.

7.3 Escrow Agent Not Responsible after Release

The Escrow Agent will have no responsibility for escrow securities that it has released to a Securityholder or at a Securityholder's direction according to this Agreement.

7.4 Indemnification of Escrow Agent

(1) The Issuer and each Securityholder jointly and severally:

(a) release, indemnify and save harmless the Escrow Agent from all liabilities, actions, costs (including legal costs, expenses and disbursements), charges, claims, demands, damages, losses and expenses resulting from or arising out of the Escrow Agent's performance of its duties under this Agreement in good faith and without negligence;

(b) agree not to make or bring a claim or demand, or commence any action, against the Escrow Agent in respect of its performance of its duties under this Agreement in good faith and without negligence; and

(c) agree to indemnify and save harmless the Escrow Agent from all costs (including legal costs, expenses and disbursements) and damages that the Escrow Agent incurs or is required by law to pay as a result of any person's claim, demand or action in connection with the Escrow Agent's performance of its duties under this Agreement in good faith and without negligence.

(2) This indemnity survives the release of the escrow securities, the resignation or termination of the Escrow Agent and the termination of this Agreement.

7.5 Additional Provisions

(1) The Escrow Agent will be protected in acting and relying reasonably upon any notice, direction, instruction, order, certificate, confirmation, request, waiver, consent, receipt, statutory declaration or other paper or document (collectively referred to as "**Documents**") furnished to it and signed by any person required to or entitled to execute and deliver to the Escrow Agent any such Documents in connection with this Agreement, not only as to its due execution and the validity and effectiveness of its provisions, but also as to the truth or accuracy of any information therein contained, which it in good faith believes to be genuine.

(2) The Escrow Agent will not be bound by any notice of a claim or demand with respect thereto, or any waiver, modification, amendment, termination or rescission of this Agreement unless received by it in writing, and signed by the other Parties and approved by the securities regulators with jurisdiction as set out in section 9.6, and, if the duties or indemnification of the Escrow Agent in this Agreement are affected, unless it has given its prior written consent.

(3) The Escrow Agent may retain such legal counsel and advisors as it may reasonably require for the purpose of discharging its duties or determining its rights under this Agreement and may rely and act upon the advice of such counsel or advisor. The Escrow Agent will give written notice to the Issuer as soon as practicable that it has retained legal counsel or other advisors. The Issuer will pay or reimburse the Escrow Agent for any reasonable fees, expenses and disbursements of such counsel or advisors.

(4) In the event of any disagreement arising under the terms of this Agreement, the Escrow Agent will be entitled, at its option, to refuse to comply with any and all demands whatsoever until the dispute is settled either by a written agreement among the Parties or by a court of competent jurisdiction.

(5) The Escrow Agent will have no duties or responsibilities except as expressly provided in this Agreement and will have no duty or responsibility arising under any other agreement, including any agreement referred to in this Agreement, to which the Escrow Agent is not a party.

7.6 Remuneration of Escrow Agent

The Issuer will pay the Escrow Agent reasonable remuneration for its services under this Agreement. The Issuer will reimburse the Escrow Agent for its expenses and disbursements.

7.7 Resignation of Escrow Agent

(1) If the Escrow Agent wishes to resign as escrow agent, the Escrow Agent will give written notice to the Issuer.

(2) If the Issuer wishes to terminate the Escrow Agent as escrow agent, the Issuer will give written notice to the Escrow Agent.

(3) If the Escrow Agent resigns or is terminated, the Issuer will be responsible for ensuring that the Escrow Agent is replaced not later than the resignation or termination date by another escrow agent that is acceptable to the securities regulators having jurisdiction in the matter and that has accepted such appointment, which appointment will be binding on the Issuer and the Securityholders.

(4) The resignation or termination of the Escrow Agent will be effective, and the Escrow Agent will cease to be bound by this Agreement, on the date that is 60 days after the date of receipt of the notices referred to above by the Escrow Agent or Issuer, as applicable, or on such other date as the Escrow Agent and the Issuer may agree upon (the "resignation or termination date"), provided that the resignation or termination date will not be less than 10 business days before a release date.

(5) If the Issuer has not appointed a successor escrow agent within 60 days of the resignation or termination date, the Escrow Agent will apply, at the Issuer's expense, to a court of competent jurisdiction for the appointment of a successor escrow agent, and the duties and responsibilities of the Escrow Agent will cease immediately upon such appointment.

PART 8 NOTICES

8.1 Notice to Escrow Agent

Documents will be considered to have been delivered to the Escrow Agent on the next business day following the date of transmission, if delivered by fax, the date of delivery, if delivered by hand or by prepaid courier, or 5 business days after the date of mailing, if delivered by mail, to the following:

[Name, address, contact person, fax number]

8.2 Notice to Issuer

Documents will be considered to have been delivered to the Issuer on the next business day following the date of transmission, if delivered by fax, the date of delivery, if delivered by hand or by prepaid courier, or 5 business days after the date of mailing, if delivered by mail, to the following:

[Name, address, contact person, fax number]

8.3 Deliveries to Securityholders

Documents will be considered to have been delivered to a Securityholder on the date of delivery, if delivered by hand or by prepaid courier, or 5 business days after the date of mailing, if delivered by mail, to the address on the Issuer's share register.

The share certificates or other evidence of a Securityholder's escrow securities will be sent to the Securityholder's address on the Issuer's share register unless the Securityholder has advised the Escrow Agent in writing otherwise before the escrow securities are released from escrow.

8.4 Change of Address

(1) The Escrow Agent may change its address for delivery by delivering notice of the change of address to the Issuer and to each Securityholder.

(2) The Issuer may change its address for delivery by delivering notice of the change of address to the Escrow Agent and to each Securityholder.

(3) A Securityholder may change that Securityholder's address for delivery by delivering notice of the change of address to the Issuer and to the Escrow Agent.

8.5 Postal Interruption

A party to this Agreement will not mail a Document if the party is aware of an actual or impending disruption of postal service.

PART 9 GENERAL

9.1 Interpretation - "holding securities"

When this Agreement refers to securities that a Securityholder "holds", it means that the Securityholder has direct or indirect beneficial ownership of, or control or direction over, the securities.

9.2 Further Assurances

The Parties will execute and deliver any further documents and perform any further acts necessary to carry out the intent of this Agreement.

9.3 Time

Time is of the essence of this Agreement.

9.4 Incomplete IPO

If the Issuer does not complete its IPO and has become a reporting issuer in one or more jurisdictions because it has obtained a receipt for its IPO prospectus, this Agreement will remain in effect until the securities regulators in those jurisdictions order that the Issuer has ceased to be a reporting issuer.

9.5 Jurisdiction

The securities regulator in each jurisdiction where the Issuer files its IPO prospectus has jurisdiction over this Agreement and the escrow securities.

9.6 Consent of Securities Regulators to Amendment

Except for amendments made under Part 3, the securities regulators with jurisdiction must approve any amendment to this Agreement and will apply mutual reliance principles in reviewing any amendments that are filed with them.

9.7 Governing Laws

The laws of [insert principal jurisdiction] and the applicable laws of Canada will govern this Agreement.

9.8 Counterparts

The Parties may execute this Agreement by fax and in counterparts, each of which will be considered an original and all of which will be one agreement.

9.9 Singular and Plural

Wherever a singular expression is used in this Agreement, that expression is considered as including the plural or the body corporate where required by the context.

9.10 Language

This Agreement has been drawn up in the [English/French] language at the request of all Parties. Cet acte a été rédigé en [anglais/français] à la demande de toutes les parties.

9.11 Benefit and Binding Effect

This Agreement will benefit and bind the Parties and their heirs, executors, administrators, successors and permitted assigns.

9.12 Entire Agreement

This is the entire agreement among the Parties concerning the subject matter set out in this Agreement and supersedes any and all prior understandings and agreements.

9.13 Successor to Escrow Agent

Any corporation with which the Escrow Agent may be merged or consolidated, or any corporation succeeding to the business of the Escrow Agent will be the successor of the Escrow Agent under this Agreement without any further act on its part or on the part or any of the Parties, provided that the successor is recognized as a transfer agent by the Canadian exchange the Issuer is listed on (or if the Issuer is not listed on a Canadian exchange, by any Canadian exchange) and notice is given to the securities regulators with jurisdiction.

The Parties have executed and delivered this Agreement as of the date set out above.

[Escrow Agent]

_____
Authorized signatory

_____
Authorized signatory

[Issuer]

_____
Authorized signatory

_____
Authorized signatory

If the Securityholder is an individual:

Signed, sealed and delivered by)
[Securityholder] in the presence of:)
)
_____)
Name)
)
_____)
Address)
)
_____)
)
)
_____)
Occupation)

_____
[Securityholder]

If the Securityholder is not an individual:

[Securityholder]

_____
Authorized signatory

_____
Authorized signatory

Schedule "A" to Escrow Agreement

Securityholder

Name:

Address:

Signature:

Securities:

Class or description	*Number*	*Certificate(s) (if applicable)*

Schedule "B" to Escrow Agreement

Acknowledgment and Agreement to be Bound

I acknowledge that the securities listed in the attached Schedule "A" (the "escrow securities") have been or will be transferred to me and that the escrow securities are subject to an Escrow Agreement dated _____ (the "Escrow Agreement").

For other good and valuable consideration, I agree to be bound by the Escrow Agreement in respect of the escrow securities, as if I were an original signatory to the Escrow Agreement.

Dated at _____ on _____.

Where the transferee is an individual:

Signed, sealed and delivered by)
[Transferee] in the presence of:)
)
_____)
Name)
)
_____) _____
Address) **[Transferee**]
)
_____)
)
)
_____)
Occupation)

Where the transferee is not an individual:

[Transferee]

_____
Authorized signatory

_____
Authorized signatory