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December 22, 2008

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CALGARY • MONTREAL • OTTAWA • TORONTO • VANCOUVER • WATERLOO REGION

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Dear Mesdames and Sirs:

Re: Template Service Accountability Agreement

You have asked us to review the Template Service Accountability Agreement for use with Health Service Providers other than public and private hospitals. In this connection you have provided us with the draft multi-sectoral SAA template V3.1 (the "SAA" or the "Agreement").

In particular, you have asked us to provide an analysis of the risks to provider organizations and, in particular, the risks inherent in the termination provisions.

Terms capitalized in this letter and not otherwise defined shall have the meanings ascribed thereto in the SAA.

Background

The SAA is intended to be used with a variety of health service providers ("HSPs").

The Agreement purports to be a multi-year funding agreement which will provide for Funding for two years. The Agreement will be effective April 1, 2009 and terminate March 31, 2011.

The Agreement provides for Funding by the LHIN to the HSP and imposes various obligations upon the HSP.

You have not asked us to provide a "clause by clause" analysis of the various rights and obligations under the Agreement but rather to focus on an analysis of the risks to provider organizations under the Agreement.

Accordingly, we have reviewed the Agreement from that perspective and have considered the following issues:

1. Are the obligations imposed upon the HSP clear and certain such that the HSP will be able to identify what it must do in order not be in breach of the Agreement and to be able to determine its costs of complying with its obligations under the Agreement – is there a risk that the HSP will be subject to additional obligations and in particular obligations which increase the HSPs' cost of compliance?

2. Is the entitlement of the HSP to Funding from the LHIN certain – is there any risk that the LHIN will not be obligated to pay the agreed amount of Funding to HSP?
3. What will be the consequences to the HSP if the Agreement is terminated prior to the expiry of its term?

Certainty of Obligations

As a general principle, it is important that the obligations of parties under an agreement be set out with sufficient certainty that a party is able to determine what steps they must take in order to ensure that they not be in breach of the agreement.

In addition, any potential increase in the obligations imposed upon the HSP may increase the cost to provide the Services and therefore impact the degree to which the promised scope of Services can be provided within the available funding while maintaining the obligation for an “Annual Balanced Budget” (see Section 4.5 (iii) of the SAA).

There are a number of provisions in the Agreement where the HSP may be at risk of being required to comply with additional requirements:

- Sections 3.1 (a) (ii) and 10.4 (ii) require the Services be provided in accordance with, or in compliance with, “Applicable Law”. The definition of Applicable Law includes federal, provincial or municipal laws or regulations or “policies or standards of practice that are applicable to the HSP, the Services, this Agreement and the parties’ obligations under this Agreement during the term of this Agreement”.

While every corporation is at risk that a new law may be passed which may increase the costs of their operations, such laws are outside the control of either the LHIN or the HSP. We are concerned that the reference to “policies or standards of practice” may include policies or standards that are set by the LHIN and therefore would constitute additional contractual obligations unilaterally imposed by the LHIN on the HSP without any notice, negotiation, or mutual agreement.

- Section 3.4 contains an obligation to comply with any technical standard relating to architecture, technology, privacy and security for health service providers set by the MOHLTC or the LHIN. Once again there is a potential for new obligations to be imposed upon the HSP during the term of this Agreement. If such obligations create additional costs of compliance, there is no right to additional funding to offset such costs.

- Section 3.5 provides that the LHIN or the MOHLTC will give the HSP notice of amendments to “manuals, guidelines or policies identified in Schedule D”. While the Agreement does not expressly include a covenant that the HSP will comply with the manuals, guidelines and policies identified in Schedule D the definition of, and obligation to comply with, “Applicable Law’ as set out above likely amounts to such an obligation. This is therefore a provision where there is no mutuality of agreement and a potential risk of unilateral imposition of additional terms upon the HSP.
- Section 4.5 (c) entitles the LHIN to impose additional terms and conditions on the use of the Funding which it considers appropriate for the proper expenditure and management of the Funding. There is no requirement for prior notice before such terms or conditions are imposed and no contemplation that Funding will be adjusted if the HSP incurs additional costs to comply with such additional terms and conditions.

Certainty of Entitlement to Funding

There are a number of provisions in the Agreement which will entitle the LHIN to make an adjustment to the Funding without prior notice to, or the prior agreement of, the HSP.

In some circumstances, the provisions that entitle the LHIN to adjust Funding are matters that may, to some degree, be within the control of the HSP. For example, Sections 4.2 (i) and (ii) provide that the Funds will not be provided to the HSP if the Agreement is not fully executed by the HSP or if the insurance is not provided as required by the Agreement.

In addition, there are other provisions in the Agreement which may impact the amount of Funding. For example, Section 4.3 provides that Funding is conditional upon an appropriation of money from the Legislature and Sections 5.1 and 12.4 contain provisions with respect repayment of Funding in certain circumstances (default, misuse of Funding or surplus Funds). These provisions are fairly typical in governing funding agreements and generally speaking are either standard terms or are tied to circumstances that can be anticipated and to some degree controlled by the HSP.

There are numerous other provisions however which are more problematic in that they provide a unilateral right of adjustment or suspension of Funding by the LHIN without notice or any due process or dispute resolution:

- The LHIN is not required to continue to provide Funds in the event the HSP breaches any of its obligations under the Agreement (please note that this is not confined to a breach of a material obligation) – Section 4.2 (iii).

- The LHIN may adjust the amount of funds it provides to the HSP based upon the LHIN's "assessment of the information contained in the Reports". No criteria is set out for the nature of the adjustment or the process that would be followed – Section 4.2 (iv).
- If Services are adjusted as a result of the "performance, management or system planning processes" (not defined), the LHIN may adjust the Funding, require the repayment of excess Funding or adjust the amount of any future Funding instalments accordingly – there is no requirement for prior notice, no process set out for how the adjustment of Funding would be calculated or what relationship it would bear to the adjustment of Services and no process to resolve a dispute between the LHIN and the HSP (Section 5.1 (d)).
- If the LHIN chooses not to terminate the Agreement in circumstances where it would have right to do so, the LHIN may take whatever corrective action it considers necessary and appropriate "including suspending Funding for such period as the LHIN determines" – Section 12.6.

Provisions in the Agreement that provide the LHIN with a unilateral right to alter Funding, without notice or due process, place the HSP at risk of having incurred financial obligations which it may not be able to honour with its available funds.

Termination

The LHIN has a right to terminate the Agreement in a number of circumstances:

- On sixty (60) days' notice at any time without cause – Section 12.1 (a).
- Where the LHIN did not receive the necessary funding from the MOHLTC – Section 12. 1 (b) [*query whether this provision should provide for a proportionate reduction of Funding rather than a termination of the Agreement in circumstances where the full appropriation is not received?*].
- Immediately for cause (Section 12.1 (c)). Cause includes a breach of a material provision of the Agreement, provision of false or misleading information or the HSP's inability to provide the Services.
- Failure to comply with the conflict of interest obligations set out in Section 3.3. [*Please note that this section of the Agreement is not the usual conflict of interest provision that we see in government funding agreements. Given the definition of "Conflict of Interest", it may be difficult to determine how an HSP is to comply with this section.*]

Where the HSP is in breach of the Agreement, the LHIN may, but is not obligated to give an opportunity to remedy the breach (Section 12.3).

If the LHIN chooses to terminate the Agreement the LHIN may, but is not obligated to allow the HSP to retain sufficient funds to pay the costs of “wind-down” of the Services. Section 12.4 (b) provides that if the LHIN has chosen to allow the HSP to retain to funds to wind-down the Services and if such retained funds are insufficient to pay the costs of the wind-down the LHIN will not provide additional monies to the HSP to wind-down the Services.

Accordingly, there is risk that the Agreement may be terminated in circumstances where the HSP has insufficient funds to satisfy its obligations to creditors and employees.

Where the HSP is a corporate entity, the general principle of limited liability will apply. The principle of limited liability provides that the directors and members/ shareholders are not personally liable for the corporate obligations. Persons who deal with the corporation are on notice that they may look only to the assets of the corporation to satisfy corporate obligations.

There are however some exceptions to the principle of limited liability. In certain circumstances, there may be potential personal liability to directors for corporate obligations. Potential personal liability in the context of an insolvent corporation is likely to arise in respect of non-payment of wages or failure to pay certain remittances.

- (i) Pursuant to the *Corporations Act*, directors are jointly and severally liable to employees and other wage earners for amounts owed not exceeding six (6) months' wages and twelve (12) months' accrued vacation pay. *[Please note for the purposes of this analysis, we have assumed that the HSPs would be corporations incorporated pursuant Part III of the Corporations Act (Ontario). If that assumption is not correct in the case of any particular HSP, they should consult their own legal advisers. There is similar liability for directors under the Employment Standards Act.]*

As a result of recent amendments to the *Bankruptcy Act* and the introduction of the *Wage Earner Protection Program Act*, certain protection is provided to employees which may reduce the potential liability of directors. The *Wage Earner Protection Program Act* is administered by the federal government and applies in the context of a bankruptcy or receivership of an employer. The purpose of the *Wage Earner Protection Program Act* is to make payments to employees for unpaid wages earned during the six (6) months before the employer's bankruptcy or receivership. The maximum payment that can be made to an eligible employee is capped at \$3,000.00 and there are certain exceptions as to which employees may receive Wage

Earned Protection Program ("WEPP") payments. Pursuant to the amendments to the *Bankruptcy and Insolvency Act* employees would be able to obtain the benefit of a super priority charge in respect of unpaid wages, salaries, commissions and compensations (which includes vacation pay but not termination or severance pay) for services rendered during the six (6) months before the employer's bankruptcy or receivership. The super priority charge creates a claim on the current assets of the bankrupt or insolvent debtor up to a maximum of \$2,000.00.

The *Wage Earner Protection Program Act* and the amendments to the *Bankruptcy and Insolvency Act* may mitigate the risk that directors may find themselves personally liable to employees for unpaid wages.

- (ii) Directors also have potential personal liability for various withholdings that the corporation is required to deduct, withhold and/or remit to the appropriate authorities (for example, income tax, pension and GST, etc.). In many cases, directors may be entitled to a due diligence defence if they can establish that all reasonable care, in the circumstances, were taken to ensure that a proper process was in place with respect to withholdings and remittances. What will constitute "all reasonable care" will depend upon the circumstances of each case and specific advice should be obtained.

Summary

1. There are various provisions in the Agreement that permit the LHIN to impose additional obligations upon the HSP.
2. The imposition of additional obligations may increase the cost to the HSP of providing the Services.
3. The Agreement permits the LHIN to adjust, reduce, or defer Funding in certain circumstances. No prior notice, due process or dispute resolution process applies.
4. If the Agreement is terminated in circumstances where insufficient Funds are provided to wind-down the Services there is a risk of insolvency and potential director liability.

We trust the foregoing is satisfactory.

Yours very truly,

A handwritten signature in black ink, appearing to read "Anne Corbett". The signature is fluid and cursive, with a long, sweeping horizontal line extending from the end of the name.

Anne C. Corbett
ACC:nb

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