All Things Canadian

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Canadian Securities Laws 101

The Regulators

- The Canadian Securities Administrators ("CSA")
  - securities regulation in Canada is provincial, not Federal
  - the Securities Commissions in the 13 provinces and territories administer securities regulation, with an increased level of co-operation through CSA

- Toronto Stock Exchange ("TSX")
  - regulates the conduct of listed companies
  - unlike NYSE and Nasdaq, it does not regulate corporate governance

- Investment Industry Regulatory Organization of Canada ("IIROC")
  - regulates the conduct of member firms (trading on debt and equity markets, investment dealers)
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Sources of Regulation

- The **Securities Act** of each province and territory, such as the Securities Act (Ontario), or “OSA”
- **Regulations** and **forms** made pursuant to the various Securities Acts
- **Rules** made by the Securities Commissions and in some cases adopted as National or Multilateral Instruments (force of law)
- **Policies** and **notices** issued by the Securities Commissions (no force of law)
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Prospectus Filing Requirement

- No person or company shall trade in (i.e. sell, not purchase) a security if the trade would be a distribution of the security unless: (i) a preliminary prospectus and prospectus have been filed and receipted by the applicable Securities Commission; or (ii) there is an exemption available

- Multiple exemptions available for sales to
  - accredited investors (Canadian definition)
  - financial institutions
  - private issuers

- Prospectus requirements - many similarities to U.S. requirements with additional certification obligations - issuer and underwriter
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Distribution/Delivery of Prospectus and Related Matters

- Preliminary prospectus distributed only after receipt issued by regulators
- Prohibition on pre-marketing communications (subject to bought deal rules and new Cdn IPO “testing the waters” exemption)
- Restricted interim period communications (no “free writing prospectus”)
- Investors have a right to withdraw from their agreement to acquire securities offered under prospectus until up to 2 business days following delivery of final prospectus to the purchaser
- Access does not equal delivery
- If a material change occurs in the information (after final but prior to completion of the distribution), the prospectus must be amended
- New prospectus “marketing” rules
New “testing the waters” exception for IPO issuers

- Permits solicitation of expressions of interest by non-reporting issuers to ascertain if there would be sufficient interest in an IPO

- Conditions (among others):
  - accredited investors only
  - through limited confidential communication by registered investment dealers only (i.e. cannot be solicited by issuer)
  - not available to foreign (SEC or other) public issuers, or if control person of issuer is a public issuer and the IPO would be a material fact or material change in respect of the control person
  - investor must confirm it acknowledges confidentiality and limited use in writing before any information is provided
  - dealer must keep written record of whom it solicits, of confidentiality confirmation and copy of written material provided
  - exemption cannot be used in 15 days prior to filing the preliminary prospectus (as the purpose is not to allow “pre-selling” of the deal)
Cross-Border Offerings
Multi-jurisdictional Disclosure System ("MJDS")

- Implemented by the CSA and SEC to coordinate regulatory review
- Eligible issuers may register an offering in the other country with offering documents prepared in accordance with the issuer’s home country’s requirements
Offerings by U.S. issuers into Canada

- Registered offering in the U.S. by a U.S. domestic issuer
- Concurrent public offerings
- Concurrent private placement into Canada
  - sell to “accredited investors” in Canada
  - Form S-1 or S-3 is “wrapped” to become a Canadian offering memorandum
  - sometimes subscription agreements
  - securities have an indefinite hold in Canada but will be freely tradable by non-control persons if the issuer is not a reporting issuer in Canada
- Using MJDS to extend rights offerings, take-over bids, issuer bids or business combinations to Canadian holders
Issues for U.S. offerings into Canada

Dual listed issuers

- Disclosure requirements similar, likely to satisfy both
- Exemptions from ongoing reporting for an “SEC foreign issuer”

Issues for U.S. underwriters

- Canadian affiliates
- Interaction with Canadian dealers
MJDS Offering Mechanics

- Canadian prospectus with a U.S. wrap registration form filed with the SEC to register the securities
- U.S. civil liability and anti-fraud rules apply to MJDS prospectuses
- All other usual U.S. requirements for public offerings also apply, e.g. prospectus delivery obligations, limitations on publicity during the offering period
Offerings by Canadian Issuers under a Shelf Prospectus - MJDS

- General eligibility criteria for a Canadian issuer to use MJDS:
  - incorporated or organized in Canada
  - must be a “foreign private issuer” under U.S. securities laws
  - must not be an “investment company” under U.S. laws
  - must have been a “reporting issuer” in Canada for 12 months
  - public float must be U.S.$75M or more (when using F-10 (instead of F-3))
    - US FINRA review has higher thresholds
  - alternative tests if selling certain debt or preferred shares (when using F-9)
  - MJDS filers cannot take advantage of WKSI benefits

- Canadian issuers can make a U.S. public offering using a Canadian shelf prospectus

- Can be made in connection with a contemporaneous Canadian prospectus offering or on a U.S.-only basis
Foreign Private Issuer Definition

- A foreign non-governmental issuer unless
  (1) more than 50% of outstanding voting securities are directly owned of record by U.S. residents; and

(2) any of the following:
  (a) majority of directors or executive officers are U.S. citizens or residents; or
  (b) more than 50% of assets in the U.S.; or
  (c) business administered principally in the U.S.
Offerings by Canadian Issuers under a Shelf Prospectus - 10b-5 Opinions

- When offering securities in the U.S. (even with Canadian prospectus), prevailing practice is for underwriters to obtain a 10b-5 negative assurance letter from counsel
- Provides support for the underwriters’ due diligence defense
- No equivalent of 10b-5 under Canadian securities laws
- Canadian law firms generally provide “Canadian-style” 10b-5 opinions indicating they have no reason to believe there is a “misrepresentation”, as defined in Canadian securities laws
- Underwriters generally obtain a second U.S.-style 10b-5 opinion from U.S. counsel
Popular Canadian and U.S. Deal Forms

- Bought Deals
- Wall-crossed/Pre-marketed offerings under shelf prospectus
- Registered Directs
- At-the-Market
Bought Deals

- Primary means by which eligible issuers raise equity capital in **Canada**
  - examples of debt “bought” deals are limited

- Underwriter makes an up-front “firm” commitment to buy securities from an issuer for subsequent resale
  - subject to standard outs (“disaster” or “material adverse change”) but no “market” out

- After offering has been announced by press release, underwriters may solicit indications of interest during the 4 business day period prior to filing preliminary prospectus

- Commission typically 4% to 5% of gross proceeds for equity

- Securities typically bought at a discount to market
Public Bought Deals — Eligible Issuers

An eligible issuer must:

- be a SEDAR filer (similar to EDGAR)
- be a “reporting issuer” in at least one province or territory
- be in compliance with timely/periodic reporting requirements
- have current annual financial statements and a current annual information form (similar to a Form 10-K or 20-F)
- must be listed on a short-form eligible exchange (TSX or TSX Venture), provided that
  - principal assets are not its exchange listing and/or cash or cash equivalents
  - its operations are still active
Bought Deals—Offering Process

- Issuer and underwriter enter into a binding bid letter fixing terms of distribution (business day 1)
- Issuer commits to file a preliminary short form prospectus within 4 business days of signing binding bid letter
- Issuer issues a press release announcing offering
- Underwriters immediately solicit expressions of interest
- Issuer files preliminary prospectus (business day 5)
- Preliminary prospectus delivered to all who expressed interest
- Lead Securities Commission provides comments on preliminary prospectus in 3 business days
- Receipt for final prospectus provided within 5 business days of filing (business day 10)
- Underwriting agreement signed and final prospectus filed
- Purchase orders confirmed
  - Purchaser has right to withdraw until 2 business days after the purchaser or its dealer receives final prospectus
- Closing - 15 business days (sometimes T+3)
Canadian Public Offerings - Form of underwriting agreements

Indicative Timing Comparisons

- Bought Deal
- Overnight Marketed
- Short Form Marketed
- Long Form Marketed (IPO)

- Prospectus Preparation
- Marketing
- Initial Comment Period
- Resolving Comments
- Time to Closing
- Prospectus Filings
- Underwriting Commitment
Bought Deals—Practical Concerns

Underwriter

- Time prior to launch for lead or co-lead can be 48 hours
- Time to agree to co-manage can be short - 30-40 minutes
- Due Diligence
  - most business due diligence done subsequent to announcement
  - Canadian underwriters hold formal question and answer due diligence
  - some issuers have designated underwriters’ counsel
- No Rule 10b-5 in Canada
  - disclosure opinion not normally given unless a substantial U.S. component is involved under MJDS
- Translation
Cross-Border Bought Deals

Combining Bought Deals and MJDS Offerings

- Difficult because of difference in timing requirements and U.S. prohibition on “gun jumping”

- Use an “accelerated filing” process:
  - sign underwriting agreement and file preliminary prospectus concurrently in Canada and the U.S. after the close or before the opening of markets
  - immediately commence marketing

- To be eligible, an MJDS issuer must:
  - have a definitive form of underwriting agreement, form of Canadian prospectus and MJDS registration statement prepared in advance
  - have auditors that qualify as independent
  - all ancillary exhibits (consents, audit reports, etc.) must be ready

- FINRA timing concerns
Post Receipt Pricing

- Issuers permitted to price public offerings of securities following receipt for the final prospectus
- Avoids having to wait for receipt following pricing
- Permits greater integration with U.S. registration statement regime where no receipt is required for final
- Size of the distribution disclosed in the prospectus may be increased or decreased by up to 20%
Registered Direct Offerings by Canadian Issuers under a Shelf Prospectus—Overview / Advantages

- Private placements of securities in Canada require a 4 month hold period
- Offering under a shelf prospectus provides investors with freely tradable securities
- Shelf allows issuers and agents to continuously market the offering
- MJDS shelf prospectus reviewed and cleared by Securities Commissions, generally not reviewed by SEC
- Prospectus supplement with offering terms not subject to any pre-clearance by Securities Commissions or SEC
Shareholder Approval?

- TSX will treat shelf offerings to a small number of investors as a “private placement”

- Permitted discount rules:
  - C$0.50 or less - 25% discount
  - C$0.51 to C$2.00 - 20% discount
  - Above C$2.00 - 15% discount

- Shareholder approval required for offering if
  - at a price below the permitted discount rate
  - materially affects control (creates a new 20% holder)
  - more than 25% dilutive to existing shareholders and issued below market price
At-the-Market Distribution—Overview

- An “at-the-market”, or ATM, offering allows exchange-listed companies to sell newly issued shares into the trading market through a broker-dealer at prevailing market prices in amounts and at the times the company chooses.

- Used by companies eligible to file a shelf prospectus under National Instrument 44-102 (Canadian equivalent of Rule 415 made under the Securities Act of 1933).

- Used in a wide variety of industry sectors in the U.S., much less commonly used by Canadian issuers.
At-the-Market Distribution—Overview

Examples of at-the-market distributions

– Midway Gold Corp (TSX-V and NYSE-AMEX listed): U.S.-only offering
– Calloway Real Estate Investment Trust (TSX listed): Canada-only offering
– Artis Real Estate Investment Trust (TSX listed): Canada-only offering
– Royal Gold Inc. (TSX and Nasdaq listed): U.S.-only offering
– Aeterna Zentaris Inc. (TSX and Nasdaq listed): U.S.-only offering
ATM—Key Timing Requirements

- Exemptive relief needed from prospectus form and delivery requirement for Canada only or Canada/U.S. ATM program
- Obtain receipt for base shelf prospectus
- Sign equity distribution agreement
- Once program established, some dealers may require 2 business days notice prior to sales (for due diligence purposes)
- Some issuers preclude sales during earnings blackouts
- French translation of prospectus supplement can impact timing
ATM — TSX Requirements

- Conditional Listing Approval for shares under ATM program required
- The number of shares sold on TSX on any particular day cannot exceed 25% of the trading volume on the TSX on that day
- Reporting requirement - within 7 days following the end of each month in which sales made on TSX, must report on SEDAR:
  - Number and average price of shares distributed over the TSX
  - Gross proceeds, commissions and net proceeds of sales during that month
  - Quarterly disclosure of sales in MD&A and notes to financial statements
- Report sales to TSX each month
ATM — Legal Restrictions

- Market value of equity securities distributed under equity distribution agreement cannot exceed 10% of market value of securities under Canadian shelf rules

- Market Value determined as at the last day of the month immediately preceding the first trade under the ATM distribution

- Market Value for these purposes excludes equity securities held by 10% holders

- Dealers prohibited from over-allotting or from stabilizing or maintaining the market price
ATM — Other Considerations

- Due diligence: generally quarterly auditor’s comfort letters and legal opinions
- Restriction on research if issuer not highly liquid
- Restriction on TSX normal course issuer bids
- Fees and set-up costs
  - Legal/Auditors
  - TSX
  - Filing fees
New Prospectus Exemption Proposal - Crowdfunding in Canada

- Ontario Securities Commission Proposal
  - Qualification criteria
  - Offering parameters
  - Investment limits
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