Cassels

New TSXV Security Based Compensation Rules to Keep in Mind for Upcoming Proxy Season

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On November 24, 2021, the TSX Venture Exchange amended its Policy 4.4 – *Incentive Stock Options* and renamed it *Security Based Compensation*. While the amendments are comprehensive and wide-ranging, here are the most significant changes from the previous Policy 4.4, which may be relevant to our TSXV-listed issuer clients as we head into proxy season.

1. Expanded the forms of security-based compensation;
2. Added the hybrid plan and the fixed 10% plan;
3. Added the concepts of "cashless exercise" and "net exercise" for stock options; and
4. Permitted the issuance of certain types of securities as compensation.

Expanded Forms of Security Based Compensation Recognized

The TSXV now has a formal policy that recognizes additional forms of security based compensation that can be governed by a security based compensation plan. In addition to traditional stock options, Policy 4.4 governs including deferred share units, performance share units, restricted share units and stock appreciation rights.

New Plan Types

The traditional "rolling 10%" and "fixed 20%" plans remain in effect but now allow the inclusion of the additional types of securities as set out above. The TSXV has added two new types of plans aimed at providing TSXV issuers with greater flexibility:

1. The "rolling up to 10% and fixed up to 10%" plan (referred to as a hybrid plan) allows issuers to issue stock options and other securities. Under a hybrid plan, an issuer may issue (a) stock options on a rolling basis provided they do not exceed 10% of the issued shares at the date of issuing any stock options, and (b) additional securities (excluding stock options) on a fixed basis provided they do not exceed 10% of the issued shares at the time of implementing the plan (provided such plan does not include the issuance of stock options). Issuers will require shareholder approval (a) to implement and amend a hybrid plan, and (b) on an annual basis to maintain a hybrid plan.

2. The “fixed stock option plan up to 10%” (referred to as a fixed 10% plan) allows issuers who only wish to issue stock options to not have to seek shareholder approval on an annual basis. A fixed 10% plan effectively operates in the same manner as a fixed 20% plan; however, a fixed 10% plan is applicable to stock options only. Although such a plan does not require shareholder approval to implement or on an annual basis, it does require shareholder approval to amend.

The TSXV may require disinterested shareholder approval for either a hybrid plan or a fixed 10% plan if the issuance of the securities could result in insiders holding greater than 10% of the issuer’s shares at any time and in certain other circumstances. In addition, the TSXV has added the requirement that disinterested shareholder approval be obtained for any security based compensation plan (including a hybrid plan or a fixed 10% plan) if any amendment to the plan will result in a benefit to an insider of the issuer.

“Cashless Exercise” and “Net Exercise”

The addition of the concepts of “cashless exercise” and “net exercise” are designed to give issuers greater flexibility in facilitating the exercise of stock options. Previously, TSXV-listed issuers could only settle stock options via a cash payment. Issuers may now settle stock options through (a) a “cashless exercise” whereby a holder of stock options receives a loan from a broker arranged by the issuer to exercise stock options and receives the balance of cash/shares minus any costs, or (b) a “net exercise” whereby a holder of stock options exercises without a cash payment and receives a number of shares determined by dividing: (A) the product of the number of stock options being exercised multiplied by the difference between the five day volume weighted average price of the shares and the exercise price of the stock options; by (B) the five day volume weighted average price of the shares. These mechanisms have often been used by issuers listed on the Toronto Stock Exchange but, to date, have not been available to TSXV-listed issuers.

Securities Issued as Compensation

The TSXV has also clarified that an issuer may issue additional types of securities as compensation to arm’s length parties for services provided on condition that the issuer, among other things, obtains TSXV acceptance in circumstances where the issuance of the securities is not captured by a security based compensation plan, the value of the securities paid is specified based on its dollar value, the securities are issued after the services have been provided and the issuer provides adequate disclosure to the TSXV and the public following the issuance of the listed shares.

In circumstances where the recipient is a non-arm’s length party, the issuer will only be able to issue listed shares. However, the TSXV has increased the maximum value of listed shares that may be issued to non-arm’s length parties to $5,000 per month per person and $10,000 per month for the issuer. Previously, an issuer could only issue an aggregate of $2,500 per month worth of listed shares to non-arm’s length parties.

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Transition

All security based compensation plans that were filed with the TSXV prior to November 24, 2021 will remain in full force and effect in accordance with their existing terms until they are put before shareholders for approval (including annual approval of a “rolling” plan or approval of an amendment to the security based compensation plan). The amendments will only apply to security based compensation plans that are implemented, amended or re-approved after November 23, 2021.
