Cassels

Canadian Capital Markets: The Next Stop for German Cannabis Operators

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Canada has garnered a reputation for its expertise in capital markets, particularly within highly regulated industries. While mining serves as a prime example of international companies seeking to list in Canada, similar trends have been observed in the cannabis sector, which we anticipate will continue. We foresee comparable developments in healthcare as well as emerging technologies.

For German Cannabis operators, recent changes to Germany's Cannabis legislation to remove cannabis from the German Narcotics Act provides a significant opportunity for local operators to rapidly develop and expand their business to expand market share in Europe's largest legal cannabis market. As the German and broader European market grows, owners and operators will need access to capital while existing shareholders will also seek liquidity opportunities.

As the second country in the world and first G20 nation to legalize cannabis for recreational purposes, Canadians are extremely familiar with the industry and the highs and lows of cannabis investment. As a result, Canadian investment banks, securities commissions and stock exchanges are extremely well versed in the complexities associated with such a highly regulated product and this capital markets expertise makes Canada a unique marketplace for German companies that may opportunistically look to Canada's bustling marketplace and consider going public on a Canadian stock market.

Canadian markets are well situated, stable and provide easy access to capital and greater liquidity options than in other international jurisdictions. In particular, as discussed below, the TSXV (as defined below) may serve as an advantageous entry point for companies seeking to go public on a smaller scale compared to other international jurisdictions such as the New York Stock Exchange or Nasdaq in the United States or the London Stock Exchange in the United Kingdom. The TSXV also allows for capital raising and liquidity without significant market capitalization, offering a simplified graduation program to the TSX (as defined below) once the business has matured.

Canadian Stock Exchanges

Toronto Stock Exchange (the TSX)

The TSX is Canada's largest senior stock exchange. The minimum listing standards on the TSX for

industrial, technology and research & development companies include:

- All issuers require sufficient working capital to carry on their business; 1 million free trading public shares; $4 million held by public shareholders; 300 public shareholders each holding a board lot; and sponsorship, except as noted below.
- Issuers forecasting profitability require pre-tax earnings of at least $200,000 for the current or next fiscal year; pre-tax cash flow of at least $500,000 for the current or next fiscal year; and net tangible assets of at least $7.5 million.
- Profitable issuers require pre-tax earnings of at least $200,000 in the last fiscal year; pre-tax cash flow of at least $500,000 in the last fiscal year; and net tangible assets of at least $2 million.
- Industrial companies require pre-tax earnings of at least $300,000 in the last fiscal year; pre-tax cash flow of $700,000 in the last fiscal year, with an average of $500,000 for the past two years; and net tangible assets of at least $7.5 million but no sponsorship requirement.
- Technology issuers require funds to cover planned opportunities for one year; $10 million cash in treasury; evidence of advanced stage of development or commercialization of a business or technology; experienced management and board, including public company experience; at least two Canadian independent directors; a $50 million market capitalization; and $10 million held by public shareholders.
- Research and development issuers require funds to cover planned opportunities for two years; adequate working capital; $12 million cash in treasury; a minimum two-year operating history that includes research and development; experienced management and board, including public company experience; and at least two Canadian independent directors.

TSX Venture Exchange (the TSXV)

The TSXV is a venture issuer for early-stage companies, typically those that do not meet the requirements of the TSX. The initial listing requirements for industrial, life sciences and real estate companies are split into Tier 1 and Tier 2 Requirements and include:

- All issuers require adequate working capital; management, including the board of directors, should have adequate, relevant and public company experience; at least two independent directors; 20% of the issued and outstanding shares held publicly; and sponsorship may be required.
- All Tier 1 issuers require sufficient resources to carry out their business plans for 18 months or $200,000 of unallocated funds; a public float of 1 million shares; and 250 public shareholders each holding a board lot with no resale restrictions.
- All Tier 2 issuers require sufficient resources to carry out their business plans for 12 months or $100,000 of unallocated funds; a public float of 500,000 shares; and 200 public shareholders each holding a board lot with no resale restrictions
- Tier 1 industrial, technology and life sciences issuers require $5 million in net tangible assets or revenue (in the event of no revenue, issuers requires a two-year plan demonstrating a reasonable

likelihood of revenue within 24 months); a significant interest in a business or a primary asset used to carry on the business; and a history of operations or validation of the business.
- Tier 2 industrial, technology and life sciences issuers require $750,000 in net tangible assets or $500,000 in revenue or a $2 million financing (in the event of no revenue, issuers require a two-year plan demonstrating a reasonable likelihood of revenue within 24 months); a significant interest in a business or a primary asset used to carry on the business; and a history of operations or validation of the business.
- Tier 1 real estate issuers require $5 million in net tangible assets; a significant interest in real property but no prior expenditures or work program requirements.
- Tier 1 investment issuers require $10 million in net tangible assets; and a disclosed investment policy.
- Tier 2 real estate issuers require $2 million in net tangible assets or a $3 million financing; a significant interest in real property but no prior expenditures or work program requirements.
- Tier 2 investment issuers require $2 million in net tangible assets or a $3 million financing; a disclosed investment policy; and 50% of available funds must be allocated to at least two specific investments.

Canadian Securities Exchange (the CSE)

The CSE is an independent and alternative exchange in Canada used for micro-cap and emerging companies. The CSE uses simplified listing regulations and its minimum listing requirements include sufficient development of the business; minimum $100,000 in working capital; sufficient public shareholder distribution; at least $1 million freely tradeable securities and 150 public shareholders each holding a board lot.

Cboe Canada (Cboe)

Cboe (previously known as the NEO Exchange) is an alternative senior stock exchange in Canada that is associated with international Cboe marketplaces. All issuers on Cboe require $10 million market value of public float; $1 million publicly held securities; and 150 public security holders, each holding a board lot.

In addition, listed issuers must satisfy one of the following categories:

- Equity: $5 million in shareholder’s equity.
- Net Income: $750,000 from continuing operations in the last fiscal year or two of the last three fiscal years.
- Market Value: $50 million in listed securities.
- Assets and Revenues: $10 million in total assets and revenues in the last fiscal year or two of the last three fiscal years.

Additionally, issuers are typically required to provide a two-year operating history and must demonstrate adequate working capital for 12 months and a $100,000 budget for investor relations for their first year after listing.

Ways to Go Public

There are two main ways to go public in Canada – an initial public offering (IPO) or a reverse take-over (RTO).

Initial Public Offerings

An IPO, known as the “conventional” way of going public, involves the sale of new securities of an existing company (and/or securities held by existing shareholders) to the public for the first time under a long form prospectus along with a concurrent listing on a stock exchange. The prospectus is a comprehensive selling document that describes, in detail, the company, its business and its holdings, capitalization and financial status, future plans and details on the uses of the proceeds of the offering.

Reverse Take-Overs

An RTO occurs when a publicly listed entity, typically an entity with minimal assets, known as a shell company, acquires a private company and the owners of the private company become the owners of the majority of shares of the public entity. The TSXV has established a program whereby a capital pool company (“CPC”) can list on the exchange without any business interest other than for the purpose of acquiring an active business through a qualifying transaction (“QT”) for an RTO. Its intention is to provide an alternative method for completing IPOs at earlier stages in the company’s development and to gain access to public markets without significant upfront costs that come with traditional IPOs.

As a result of a RTO, the owners and operators of a private company typically take over as directors and officers of the public entity and the business of the private company continues to operate as a direct or indirect wholly owned subsidiary of the public entity.

The CPC program is similar, in many ways, to more well-known SPAC (Special Purpose Acquisition Company) transactions, which are also available in Canada but far less common. The main difference is that shareholders of a CPC do not have redemption rights in connection with the RTO and therefore, while CPCs typically have far less cash than SPACs, the cash is guaranteed on closing as opposed to a SPAC transaction where it is unknown how much cash will remain in the business.

One particular benefit of an RTO is that the transaction is regulated by a stock exchange only whereas an IPO will require clearance from a securities commission in Canada in addition to approval of the desired

stock exchange.

Additional Considerations

Corporate Laws and Financial Statements

Non-Canadian companies should expect to have their listing documentation scrutinized according to Canadian corporate law standards. In addition, financial reporting must comply with the International Financial Reporting Standards ("IFRS") for annual audited financial statements and quarterly interim financial statements. The IFRS provides specific requirements for reporting fair value of growing cannabis plants.

Presence in Canada

There are no specific presence requirements for listing on a Canadian stock exchange, however, federally incorporated entities in Canada may have specific requirements to consider some of which are not applicable for provincially or foreign incorporated entities. For instance, there are no director residency requirements for directors of corporations governed by statues of Alberta, British Columbia or Ontario.

If you or your business have questions regarding the Canadian capital markets, the process for going public or what options in Canada may be right for you to list on a Canadian stock exchange, please contact a member of the Cassels Cannabis Group.

For more on this topic, read "Cannabis in Germany: The Time is NOW to Seize Opportunities in the Emerging Market," by guest author Franziska Katterbach of Oppenhoff.

This publication is a general summary of the law. It does not replace legal advice tailored to your specific circumstances.