Cassels

GOING PUBLIC IN CANADA

OVERVIEW

The decision to become a reporting issuer and offer securities to be traded on a public exchange is a milestone for a company of any size. There are many advantages to going public, however, doing so brings new responsibilities for which a business must be prepared. Management is encouraged to carefully consider the following and then decide whether they are prepared to become, and operate as, a public company.

IS IT IN THE COMPANY'S BEST INTEREST TO GO PUBLIC?

Advantages

When a private company goes public, current shareholders benefit from the new market for their securities. Increased liquidity can raise the value of the shares and allow existing shareholders an opportunity to exit all or a portion of their position and realize gains. The company may also diversify its capital structure; access to public markets gives the company more flexibility in its capital structure as equity can be sold for cash or issued in satisfaction of debt. Going public can increase bargaining power when dealing with parties outside the business as public companies are seen as more secure than private companies; contractors and suppliers will deal more readily with a public company. Public companies are also regarded more highly by capital and labour markets. Employees can be offered stock options as part of their compensation package, allowing the company to attract and retain better talent and create an incentive to work toward a common goal.

Other considerations

There are a number of consequences to becoming a public company that must be carefully considered. To start, the company's management will lose a degree of control over the business. Managers and board members are accountable to a broader range of shareholders and must be able to justify their decisions to them. This means that maximizing shareholder value is a priority, creating pressure for short-term performance. A company must also be prepared for the requirements of increased transparency and the heightened level of scrutiny a public company receives. Business information that was formerly private, such as business strategy, financial performance and compensation of senior officers, is required to be revealed to the public, including to competitors. Additionally, material contracts are required to be made available publicly, subject to certain exceptions. The continuous disclosure obligations can be onerous and costly, and many judgment calls will require the assistance of outside professionals.

The initial cost of going public must be justifiable. A public offering will require the retention of lawyers, auditors and investment bankers, and sometimes other technical consultants. Further, costs for due diligence, printing the prospectus, "road shows," and listing fees can be substantial. Going public also exposes the company and its directors to potential liability. Compared to private shareholders, public shareholders will likely take a more

active interest in the business and may be more likely to sue. This risk is somewhat mitigated by the availability of director insurance; however, it only covers limited situations. Going public also increases the risk of a take-over bid.

CAN I GO PUBLIC?

Listing requirements

Even if a company feels it is prepared to deal with the risks and obligations of being a public company, it may not meet listing requirements set by one of the Canadian stock exchanges. There are three main stock exchanges in Canada, the Toronto Stock Exchange ("TSX"), the TSX Venture Exchange ("TSXV") and the Canadian Securities Exchange ("CSE"). The TSX is designed to provide senior issuers with a market for their securities, while the TSXV is designed to give early stage companies access to venture capital markets. The CSE is a cost-effective disclosure-focused exchange for smaller issuers. Companies initially listed on the TSXV or CSE may apply to graduate to the TSX when they meet the appropriate listing thresholds. The TSX has the highest thresholds in terms of listing requirements of the three exchanges.

Companies apply to be listed on one of the exchanges by submitting a letter request with certain required supporting documents to the desired exchange. Application documents include a listing application, listing agreement, personal information forms or declarations of all senior officers and directors and a prospectus, if the company is filing one.

TSXV applications must be sponsored by a TSXV member. This sponsor considers the expertise of senior management and directors, the integrity of the company's financial statements, the listing requirements and whether the company is suitable for a public listing. The sponsor also plays a role in determining how the company will go public.

For all applications, additional documents may be required depending on the industry in which the business operates. For example, mining companies will be required to submit geological reports in respect of material properties in compliance with NI 43-101 — *Standards of Disclosure for Mineral Projects*.

How do I go public?

In Canada, a company can go public by completing a prospectus offering (an "initial public offering" or "IPO"), through a reverse take-over or by completing a qualifying transaction with a capital pool company.

INITIAL PUBLIC OFFERING

An initial public offering is the most conventional way that private companies go public. An IPO requires the preparation of a prospectus, which provides investors with the information needed to make an educated investment decision. The level of disclosure needed for the prospectus is full, true and plain disclosure, the highest standard in securities law. As a result, creating a prospectus is a long and detailed process that requires the co-operation of management, securities lawyers, external auditors, investment bankers, investor relations professionals, and sometimes technical consultants.

A preliminary prospectus is publicly filed with each of the securities commissions of the provinces and territories where the securities will be offered and with the desired exchange. The preliminary prospectus is reviewed by the regulatory authorities and comments are sent to the company and its lawyers if any deficiencies or issues are identified. Once all comments have been satisfactorily addressed and settled, a final prospectus is filed and a final receipt is issued. The securities are then sold, the offering is closed, and the securities are listed on the applicable exchange.

WILL MY IPO BE SUCCESSFUL?

For there to be a public offering of securities, the company must first find underwriters who are confident the securities will sell. Underwriters will consider the company's potential for growth and whether the funds raised can be used to increase the value of the company. The company's past earnings and future prospects, as well as the abilities and previous experience of the management team and board of directors will also be considered. A public company needs a management team and board of directors with experience operating public companies.

WHY DO AN IPO?

An IPO allows for a wide distribution of securities. From a marketing perspective, the company is given more publicity as more potential investors become aware of the offering. Unlike a reverse take-over, an IPO does not involve dealing with another company that may have potential liabilities, issues or obligations attached to it that would be inherited or assumed by the entity that continues forward following the reverse take-over.

WHAT FINANCIAL STATEMENTS ARE REQUIRED?

Generally, both the preliminary and final prospectus must include:

- A statement of comprehensive income, a statement of changes in equity and a statement of cash flows for each of the three most recently completed financial years ended more than 120 days before the date of the prospectus; and
- A statement of financial position as at the end of the two most recently completed financial years ended more than 120 days before the date of the prospectus.

There are special rules for quarterly reports and possible exceptions to the above requirements in certain very specific situations. A company preparing to go public also needs to be aware that additional financial statements are required if a "significant acquisition" has been completed in the most recently completed financial year (or the company proposes to complete one). All annual financial statements included in a prospectus must be audited. Audits are required to be prepared in accordance with International Financial Reporting Standards ("IFRS"). Audit reviewed financial statements for the most recently completed interim period may also be required.

WHAT ARE THE STEPS AND TIMING?

Timeline for an IPO in Canada	
Timing	Task
Weeks 1-2	• Management confirms the current board of directors and management team will meet the regulatory requirements of a public company • Management chooses and engages professional advisors: underwriters, securities lawyers, external auditors and investor relations professionals • Meeting with auditors and other advisors to discuss financials and, if applicable, technical reports (such as NI 43-101 compliant reports for mineral properties) and commence preparation of same • Internal documentation organized to ensure due diligence and preliminary prospectus preparation are completed efficiently • Underwriters begin due diligence review • Drafting of preliminary prospectus commences
Weeks 3-4	• Preparation of exchange listing application • Attend to exchange listing requirements (i.e., application for CUSIP number) • Have officers and directors fileepersonal information forms

Timeline for an IPO in Canada	
	• Legal and business due diligence to continue • Commence preparation of marketing materials • Arrange for financial printers
Week 5	• Oral due diligence session with the company's management and auditors and company's and underwriters' legal counsel • Finalize preliminary prospectus • Board meeting to approve preliminary prospectus (including financial statements and technical reports, if any) • Preliminary prospectus and supporting documents, including financial statements, filed with the exchange and applicable provincial and territorial securities regulators
Weeks 6-9	• "Waiting period" begins: the company and the underwriters are permitted to solicit interest in securities by forwarding copies of preliminary prospectus to prospective investors • Underwriters' counsel distributes draft underwriting agreement • Provincial and territorial securities regulators and the exchange review preliminary prospectus and advise applicant issuer and professional advisors of any deficiencies • Applicant issuer (with aid of securities counsel) to address deficiencies and file necessary amendments to prospectus with securities regulators • Underwriters begin marketing efforts • Listing application filed with the applicable exchange
Weeks 10-11	• Marketing complete and expressions of interest solicited • Hold update due diligence session with company's management and auditors and company's and underwriters' legal counsel • Resolve any outstanding comments from the securities commissions on the preliminary prospectus • Finalize terms of offering (i.e., price, size, etc.) • Finalize final prospectus • Hold board meeting to approve final prospectus and any other ancillary matters • File final prospectus with relevant securities commissions • Issue press release • Print commercial copies of final prospectus for distribution to subscribers
Weeks 12-13	• Expiry of statutory withdrawal rights in Canada • Pre-closing meeting to settle and sign all closing documentation • Closing occurs • Issue press release • Securities begin trading

WHAT ARE THE COSTS OF AN IPO?

Common expenses in completing an IPO in Canada include:

- Auditor fees
- Prospectus filing fees (paid to Canadian securities regulators in provinces and territories where securities are offered)
- Legal fees
- Listing fees (paid to the applicable exchange)
- Marketing costs
- Printing costs
- Transfer agency fee
- Translation costs (if any part of the offering is made in Quebec)
- Underwriter fees and costs (generally includes their legal fees)

REVERSE TAKE-OVER

Another way for a private company to become a public company is for it to be acquired by an existing public company listed on an exchange, known as a “reverse take-over” or “RTO.” An RTO occurs when a public listed shell company acquires or merges with a private company, and the owners of the private company become the majority owners of the publicly listed company. The shell company will not have an operating business and will typically have few, if any, assets. The acquisition of the private company may be achieved through a number of means, including by merger of the two companies, asset acquisition or share acquisition. The structure of the RTO will depend on numerous factors including tax considerations. The acquisition generally requires the preparation of materials for a meeting of shareholders to approve these transactions which contain prospectus level disclosure on both the listed company and the private company.

WHY DO A REVERSE TAKE-OVER?

The benefit of pursuing a reverse take-over is that the public parent has a pre-existing shareholder base that will satisfy the exchange’s public float requirement. Therefore, it may not be necessary to attract as many new investors or hire a team of underwriters to distribute stock.

Although an IPO may establish a stronger retail distribution, an RTO provides a historical retail base thereby reducing the requirement to market to retail investors. In certain circumstances, the shell company can provide the company with commercial advantages such as cash, qualified resident Canadian directors and a compatible asset.

OTHER CONSIDERATIONS

This method of going public does not eliminate the work or expense involved in taking a company public. The new company, on a post-transaction basis, must still meet listing requirements and the transaction is subject to regulatory approval. The company performing the reverse take-over will still need to conduct extensive due diligence and prepare the disclosure documents associated with the transaction. The fees associated with going public this way are still substantial.

The time required to complete an RTO varies, however it usually takes between four months and six months from the time the owners of the private company identify the shell company. The key determining factors with respect to timelines include statutory requirements for the holding of shareholder meetings, the time required by regulators for review of materials and the receptiveness of the market to any proposed financing.

The issuer which results from the RTO must meet the original listing requirements of the exchange that the public company is listed on and the transaction will be subject to the approval of that exchange.

The RTO must be approved by shareholders of the shell company, which requires that an information circular be mailed and filed, and a shareholder meeting be held. Holding a shareholder meeting adds time and expense to the transaction. The shell company would have separate legal and accounting advisors which also adds delay and expense.

As indicated above, the shell company will have some prior history which means that there is greater potential for actual or contingent liabilities that would be inherited by and continue with the entity resulting from the RTO. For the reasons noted above, including the requirement for a shareholder meeting in Canada, additional advisors and preparation of meeting materials, an RTO may be more time consuming, and potentially more costly, than an IPO.

WHAT ARE THE STEPS AND TIMING?

Timeline for an RTO in Canada	
Timing	Task
Weeks 1-3	• Identify and commence negotiations with shell company • Parties to commence due diligence process on each other • Determine stock consideration ratio or range • Consider whether a financing is required in connection with the RTO • Commence drafting of NI 43-101 compliant technical reports for mineral properties, if applicable • Prepare financial statements for inclusion in information circular for shareholder meeting of shell company
Weeks 4-6	• Announce transaction with shell company • Commence preparation of meeting materials • Continue preparation of financial statements and technical reports • Legal and business due diligence to continue • Select management and board of directors of resulting issuer
Week 7	• Deliver initial draft documentation to the exchange (i.e., information circular, financial statements, technical reports, listing application) • Have officers and directors file personal information forms • Publish record date for shareholders meeting (at least 7 days prior to the record date)
Weeks 8-11	• Record date for shareholders meeting (must be at least 30 days prior to meeting date) • Obtain conditional listing approval of the applicable exchange • Printing and mailing of meeting materials for shareholders meeting (must be at least 21 days prior to the meeting date)
Weeks 12-13	• Hold shareholder meeting and obtain shareholder approval • Filing of post-shareholder approval documents with the applicable exchange (i.e., scrutineer's report, legal opinion, balance of filing fees) • Closing of RTO • Exchange issues final exchange bulletin (evidencing final listing approval) • Common shares of the resulting issuer commence trading

QUALIFYING TRANSACTION WITH A CAPITAL POOL COMPANY

A "qualifying transaction" is similar to a reverse take-over except it is done using a "Capital Pool Company" or "CPC."

A CPC is a particular kind of TSXV listed public shell company that is very limited in terms of what it can do until it completes a "Qualifying Transaction" by acquiring or merging with an operating private company or acquiring a qualifying asset.

The CPC program is offered by the TSXV in an attempt to provide smaller businesses with alternative access to capital markets. Shareholders of the private company become shareholders of the CPC. Once the CPC completes the transaction its shares continue to be traded on the TSXV.

WHY CHOOSE A CPC?

A private company may choose to do a qualifying transaction with a CPC to allow the private company to go public where it is not otherwise ready to have its securities very widely held, or if the market is not strong

enough for a successful IPO. Because a CPC is a recently incorporated shell company with little history, there is typically a much lower volume of due diligence than for a regular reverse take-over.

The CPC program provides an alternative route to accessing capital that may allow the company founders to retain a higher ownership than through a traditional IPO or RTO. A qualifying transaction with a CPC provides a going public process that has greater flexibility, more certainty, and allows for more control by the companies involved. In general, it takes some of the risk out of the going public process.

OTHER CONSIDERATIONS

As with the other methods for going public, a strong management team with experience operating public companies is needed. Additionally, a suite of professional advisors including securities lawyers, external auditors, investment bankers and technical consultants are required to be involved in the transaction. The company also needs to ensure that it has a long-term strategy for growth as a public company and engage financial advisors to ensure that the company's message is communicated to potential shareholders and that there is investor support for the company's shares following the going public transaction.

The steps involved and time to complete a qualifying transaction are similar to those for a reverse take-over.

LIFE AFTER LISTING

WHAT HAPPENS ONCE THE COMPANY GOES PUBLIC?

It is important for businesses to give serious consideration to the obligations associated with being a public company. Companies are required to provide both periodic and timely disclosure and the continuous disclosure requirements can be onerous and costly. Periodic disclosure means that there will be regular reporting of financial statements, including auditor's reports, management's discussion and analysis, annual meeting materials, business acquisition reports for "significant acquisitions," technical reports (if applicable) and an annual information form (which is optional if the company is listed on the TSXV or the CSE). These items require significant resources to prepare, review and file. The timely disclosure regulations may also be onerous, as companies are required to report material changes by press release immediately and to file a material change report within 10 days of the material change. Deciding what constitutes a material change requires careful consideration by the board of directors and often the assistance of an experienced securities lawyer. The consequences of failing to disclose a material change can be severe.

One benefit to the continuous disclosure regime is the reduced cost and increased speed with which subsequent prospectus offerings can occur. If a company is up-to-date with its filings it may qualify to use the short-form prospectus regime. The short-form prospectus rules allow a company to incorporate documents by reference and is a much faster prospectus process than for a long-form prospectus.

CORPORATE GOVERNANCE REQUIREMENTS

There are important corporate governance matters to consider when going public, including ensuring that the company's board and management are constituted in accordance with Canadian governance standards and that residency requirements for directors are met if the company is, or after going public will be, incorporated in Canada.

The TSX requires a minimum of two independent directors in order to meet minimum listing requirements. Three independent directors who possess knowledge and understanding of financial matters, are necessary in order to have a properly constituted audit committee.

To be considered "independent," a director:

- Must not currently be an executive officer or employee of the issuer (or have fulfilled such a role in the last three years)
- Must not receive compensation from the issuer other than payment for acting as a member of the board and have no other direct or indirect material relationship with the issuer

The TSX also requires at least one director with North American public company experience, and that management and the board have experience in the issuer's business/industry.

The above audit committee requirements do not apply to TSXV-listed companies, provided there is at least one independent director.

US issuers that have securities listed or quoted on a US marketplace are exempt from certain audit committee requirements if they comply with the audit committee requirements of the US marketplace.

Residency requirements for Canadian companies vary from province to province. For example, companies incorporated in Alberta or Ontario are required to have resident Canadian directors comprising at least 25% of the total number of directors, while there are no Canadian residency requirements for directors of companies incorporated in British Columbia or Quebec. Boards of directors of companies existing under the *Canada Business Corporations Act* are also required to be comprised of at least 25% Canadian resident directors.

ABOUT US

Cassels Brock & Blackwell LLP is a Canadian law firm focused on serving the transaction, advocacy, and advisory needs of the country's most dynamic business sectors.

Cassels offers one of the largest business law practices in Canada, advising clients from start-ups to multi-national organizations – across the street and around the world – and we are consistently cited as market leaders by such authorities as *Chambers*, *Lexpert*, and *Best Lawyers*.

We are dedicated to staying on the leading edge of trends in law and business to offer practical and flexible solutions to your legal challenges, and our lawyers are proud to serve leadership roles in business, civic, charitable, and cultural organizations in community, national, and international organizations.

At Cassels, your success is our priority.

SELECT KEY INDUSTRIES AND AREAS OF PRACTICE

- Aboriginal
- Banking & Specialty Finance
- Business
- Cannabis
- Class Actions
- Competition & Foreign Investment
- Construction
- E-Discovery & Information Governance
- Emerging Companies
- Employment & Labour
- Energy
- Entertainment & Sports
- Franchise
- High Growth & Venture Capital
- Hospitality
- Information Technology & Data Privacy
- Infrastructure
- Insurance & Reinsurance
- Intellectual Property
- International Trade
- Litigation
- Mergers & Acquisitions
- Mining
- Municipal, Planning & Environmental
- Private Equity
- Product Liability
- Real Estate & Development
- Regulatory
- Restructuring & Insolvency
- Securities
- Securities Litigation
- Taxation
- Universities & Colleges

This document, and the information in it, is for illustration only and is subject to changes in the law and its interpretation. It does not constitute, and is not a substitute for, legal or other professional advice. For advice on the matters discussed in this document, please consult legal counsel.