

Righting a Wrong: Canadian Regulators Improve the Rights Offering Regime



By Samuel Li and Paul Fornazzari on February 16, 2016

The various Canadian regulatory authorities recently overhauled how prospectus exempt rights offerings are to be conducted going forward, including allowing for larger financings to be completed in a shorter time frame with less extensive offering documents. As a result of these amendments (**Amendments**) which came into force on December 8, 2015, reporting issuers in Canada may now have a more viable avenue to raise funds from existing shareholders.

Rights offerings are viewed favourably by the regulators because they allow the then current securityholders of an issuer, who are often retail investors, to participate in a financing which typically offers securities at a discount to the market price, and avoid dilution. For issuers, a prospectus exempt rights offering should be less costly than other forms of financing because brokers are not usually involved and a prospectus is not required to be filed. However, historically, prospectus exempt rights offerings prior to the Amendments have been uncommon and have been characterized as financings of last resort. In large part, issuers have chosen not to rely on prospectus exempt rights offerings because of limitations on the size of the financing (securities offered were limited to 25% of the issuer's issued and outstanding securities) and the length of time required to complete the offering (the average time to complete a prospectus exempt rights offering was 85 days including 40 days between the filing of a draft circular and the acceptance by the regulators). This delay combined with the normally deeply discontinued right exercise price tends to result in the share price drifting down to the right exercise price so without a stand-by guarantor, there is a real possibility that few rights would be exercised. Further, certain foreign issuers have been unable to offer Canadian residents the ability to participate in rights offerings because the Canadian exemption was so limited when compared to other jurisdictions.

The major changes to the rights offering prospectus exemption include: •increasing the potential rights offering size to allow for an offering of up to 100% of the issued and outstanding securities, •no longer requiring regulatory approval of offering documents, and •simplifying the offering documents required, thereby significantly decreasing the time and cost required to complete a rights offering financing.

Although the exemption is now limited to reporting issuers, the Amendments appear to have created a useful equity financing alternative. In particular, an issuer which is having difficulty raising funds under the current economic conditions can consider seeking financing from its own securityholders under the rights offering exemption with a far reduced time and cost commitment.

Changes from the Proposal

While the Amendments adopted were substantially in the form provided for in the proposed amendments published by the Canadian Securities Administrators on November 27, 2014 as summarized in “A New National Rights Offering Exemption”, some minor changes were made based on comments received regarding the proposal.

The prospectus exemption created for securities issued to a stand-by guarantor as part of a prospectus exempt rights offering required such securities to be subject to a restricted hold period under the proposals, unless the guarantor was an existing securityholder. Under the Amendments as adopted, the securities issued to the stand-by guarantor will not normally be subject to a hold period (only a seasoning period on resale is applicable).

The “minimal connection exemption”, whereby the prospectus requirement would not apply to rights offerings where the number of securities and beneficial securityholders in Canada, and in a local jurisdiction, was minimal, was amended to remove the local jurisdiction requirement meaning the use of the exemption no longer requires that less than 5% of the beneficial securityholders reside in the local jurisdiction or that less than 5% of the number of securities are held by securityholders residing in the local jurisdiction. The exemption will be available if less than 10% of the beneficial securityholders reside in Canada and less than 10% of the number of securities are held by them.

A requirement was included in the Amendments that an issuer must disclose in the required circular related to a prospectus exempt rights offering any material facts and material changes that have not yet been disclosed and a statement that there are no undisclosed material facts or material changes.

Toronto Stock Exchange and TSX Venture Exchange Guidance

On January 18, 2016, the Toronto Stock Exchange (**TSX**) and the TSX Venture Exchange (**TSXV**) each issued additional guidance in light of the adoption of the Amendments (**Exchange Guidance**). While it is intended that the TSX Company Manual (**TSX Manual**) and the TSXV Corporate Finance Manual (**TSXV Manual**) will be formally amended in the future, the TSX and the TSXV have each issued Exchange Guidance in the interim to direct issuers.

The Exchange Guidance confirms that TSX or TSXV approval, as applicable, of the offering documents is still required prior to finalization despite no longer being subject to securities regulatory approval. The TSX requires filing of the offering documents five trading days prior to finalization while the TSXV does not provide a timeline.

Prior to the adopting of the Amendments, each of the TSX Manual and the TSXV Manual required issuers to resolve all issues raised by the TSX or the TSXV at least seven trading days prior to the record date. The Exchange Guidance has lowered the advance notice requirement to five trading days.

The TSXV indicates that it proposes to amend the TSXV Manual to lower the minimum subscription price to \$0.01 for each security acquired on the exercise of rights. Until such amendment, the TSXV notes in the Exchange Guidance that it will grant waivers to the current \$0.05 minimum rights subscription price requirement upon application provided the subscription price is not less than \$0.01. The TSXV also proposes to amend the TSXV Manual to expressly provide that the rights are not required to be listed for trading and, until such amendment, issuers may apply for a waiver of the listing requirement.

Finally, the TSXV specifies that it is proposing to amend the TSXV Manual such that shareholder approval of the creation of a new control person of an issuer through a rights offering standby commitment will generally not be required provided the rights are listed for trading on the TSXV and the rights subscription price is equal to or less the market price minus the maximum allowable discount for private placements. The TSXV will also require the filing of a personal information form of a person providing a standby commitment if it may lead to such person

owning or controlling, beneficially or as nominee, directly or indirectly, securities representing over 10% of the voting rights attached to outstanding voting securities of the issuer.

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