

# CHANGES EXPECTED TO LEAD TO RENEWED INTEREST IN TSXV'S CAPITAL POOL COMPANY PROGRAM

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On December 1, 2020, the TSX Venture Exchange (the “**TSXV**” or the “**Exchange**”) published a bulletin (the “**Bulletin**”) announcing certain changes to its Capital Pool Company (“**CPC**”) program (the “**CPC Policy Changes**”), which will become effective on January 1, 2021.<sup>[1]</sup> The CPC Policy Changes are the most significant amendments to the CPC program since 2010 and are expected to create renewed interest in the Exchange’s CPC program. The scope of these amendments address areas where the Exchange has received input from market participants and formalized a number of issues which had previously been dealt with by TSXV management on a case by case basis.

The TSXV CPC program is the predominant structure utilized for private companies going public in Canada as it provides high growth companies with ready access to public venture capital. As of September 30, 2020, there has been 2,600 CPCs created and approximately \$75 billion of equity capital raised by CPCs, since the formation of the CPC program.<sup>[2]</sup>

This article seeks to: (i) highlight the key policy changes addressed in the Bulletin; and (ii) provide further guidance for private companies exploring opportunities to list in Canada, or which are already listed, on the TSXV through the CPC program.

Capitalized terms not specifically defined in this article have the meanings ascribed to them in the Exchange’s Corporate Finance Manual,<sup>[3]</sup> including the amended policies and forms applicable to the CPC Policy Changes.<sup>[4]</sup>

## 1. Elimination of 24 Month Deadline for Qualifying Transaction

Under the current CPC policy published June 14, 2010 (the “**Current CPC Policy**”),<sup>[5]</sup> CPCs that do not complete a Qualifying Transaction within 24 months from listing face the prospect of either being suspended, delisted, or, subject to the approval of their Shareholders, moving their listing to the NEX board of the TSXV and canceling 50% of the pre-IPO Seed Shares.<sup>[6]</sup> This requirement has faced a lot of criticism, as it tends to disincentive the boards of directors of CPCs and their key stakeholders and has often resulted in CPCs completing a Qualifying Transaction in order to meet this 24 month deadline. The CPC Policy Changes will

eliminate the 24 month timing restrictions and any related penalties which previously existed. Accordingly, CPCs will gain flexibility to complete a Qualifying Transaction based on their preferred timing and will be better positioned to weather volatile capital markets.

## 2. Relaxation of Escrow Terms

The Current CPC Policy imposes restrictive escrow conditions on securities held by directors, officers, and other holders of Seed Shares acquired prior to the completion of a CPC initial public offering (“**IPO**”) at a discount to the IPO price. Securities held by these escrowed Shareholders are generally subject to restrictions on transfer until the completion of a Qualifying Transaction, after which these securities start to be released over an 18 month period for Tier 1 Issuers or (more commonly) a 36 month period for Tier 2 Issuers.

While not eliminating the escrow requirements, the CPC Policy Changes will significantly reduce the burden imposed by the current escrow regime of the CPC program. Notably, there will no longer be a tiered approach for determining the escrow timeframe. Following the completion of a Qualifying Transaction, all CPC escrowed securities will be subject to an 18 month escrow schedule (whereas the current rules provide a distinction between Tier 1 and Tier 2 Issuers), whereby 25% of the escrowed securities will be released on the date the TSXV issues a final bulletin for the CPC’s Qualifying Transaction (“**Final QT Exchange Bulletin**”) and 25% on each of 6, 12, and 18 months following such date. In addition, CPC stock options and shares issued on exercise of stock options will be released on the date the TSXV issues its Final QT Exchange Bulletin, unless such securities were granted before the IPO and at an exercise price less than the IPO price.

## 3. Lower Public Distribution Requirements

The CPC Policy Changes will align certain CPC distribution requirements to be closer to the requirements of the Canadian Securities Exchange, which has emerged, with the influx of primarily cannabis companies, as a viable alternative trading market to the TSXV. CPCs will be required to have a Public Float of at least 500,000 shares (decreased from 1,000,000 shares) and consisting of at least 150 Public Shareholders (decreased from 200 Public Shareholders), each owning at least 1,000 shares. However, Public Shareholders will need to collectively hold at least 20% of the outstanding shares (compared to 10% required by the Canadian Securities Exchange). In addition, certain restrictions on maximum ownership of IPO Shares will be loosened.<sup>[7]</sup>

## 4. Other Changes

In addition to the above amendments, the CPC Policy Changes include changes to, among other things:

- **Seed Capital and IPO Funds** – CPCs will be able to raise a maximum of \$1,000,000 in Seed Capital below the IPO price and a maximum of \$10,000,000 in aggregate funds (including under the IPO). These new amounts are double the previous allowances under the Current CPC Policy.

- **Use of Proceeds** – Under the Current CPC Policy, non-Qualifying Transaction expenses (e.g. general and administrative expenses) are limited to the lesser of 30% of the gross proceeds raised by the CPC and \$210,000 over the CPC’s lifetime. This requirement, which CPCs are typically unable to comply with after having been in existence for a couple of years, will be replaced with a requirement that general and administrative expenses will be limited to \$3,000 per month. Through the CPC Policy Changes, the TSXV has also expanded guidance on permitted uses of proceeds and payments to Non-Arm’s Length Parties and codified the practice of permitting loans by CPCs to a target company in a Qualifying Transaction on terms similar to what is permitted for reverse takeover transactions (up to a maximum of the greater of \$250,000 or 20% of the CPC’s working capital).
- **Concurrent Financings and Bridge Financings** – CPCs are generally only permitted to issue common shares pursuant to financings completed prior to a Qualifying Transaction. The CPC Policy Changes will codify existing Exchange practice to also allow CPCs to complete a Concurrent Financing or Bridge Financing involving the issuance of subscription receipts or special warrants that convert into listed shares, or listed shares and warrants, on completion of a Qualifying Transaction.
- **Agents, Pro Groups, and Finders’ Fees** – The CPC program will become more attractive to Agents, Pro Group members, and eligible finders, as incentives will be implemented to benefit these stakeholders. Examples of such changes include, among others: finder’s fees may be paid to Non-Arm’s Length Parties to a CPC under certain circumstances; the maximum term of Agent’s options will be 5 years (rather than 2 years); shares issued to Pro Group members as part of the Qualifying Transaction will not be subject to a four month hold period unless required by law; and shares acquired by the Pro Group at or above the IPO price will not be subject to escrow.
- **Directors and Officers** – International directors will be permitted and one person may act as CEO, CFO, and corporate secretary of a CPC.
- **Stock Options** – CPCs will be permitted to adopt 10% rolling option plans (based on number of shares outstanding at the time of grant) instead of being limited to 10% fixed option plans based on the number of shares outstanding on closing of the IPO. Further, the minimum exercise price for stock options granted before an IPO will be the lowest Seed Share issue price, removing the existing restriction which prohibits stock options being issued with an exercise price lower than the IPO price.

## 5. Transitional Provisions

The CPC Policy Changes include transitional provisions that will allow companies that, as of January 1, 2021, are CPC applicants, current CPCs, or former CPCs that have already completed a Qualifying Transaction (“**Resulting Issuers**”) to take advantage of certain of the CPC Policy Changes.

### a. CPCs in the Application Process

If a company has filed its CPC Prospectus, but has not yet completed its IPO, it may elect to comply with the CPC Policy Changes, provided that it files the final CPC Prospectus and CPC Escrow Agreement under the new forms. Alternatively, the company may file its final CPC Prospectus and complete its IPO in accordance with the Current CPC Policy and be governed by the Current CPC Policy (with the ability to comply with the transition provisions below).

#### **b. Existing CPCs**

Existing CPCs can implement certain changes without Shareholder approval, including increasing maximum aggregate gross proceeds raised by the CPC to \$10,000,000; adopting the new requirements concerning use of proceeds; and issuing new Agent's options in connection with a Private Placement.

Adopting certain other changes will require disinterested Shareholder approval, including removing the consequences of failing to complete a Qualifying Transaction within 24 months of listing; extending the term of pre-existing Agent's options or permitting payment of a finder's fee to a Non-Arm's Length Party to the CPC; and adopting new escrow terms and/or a 10% rolling stock option plan.

#### **Resulting Issuers that have Completed a Qualifying Transaction**

Resulting Issuers can amend their existing CPC Escrow Agreement to track the escrow terms permitted under the CPC Policy Changes, provided that they first obtains disinterested Shareholder approval.

#### **Conclusion**

Overall, the CPC Policy Changes overhaul the CPC program to make it a more competitive candidate for earlier stage private companies looking to 'go public' in Canada. We anticipate these changes to be welcomed by market participants and to renew interest in the CPC program.

Companies are encouraged to contact us for further information concerning the CPC Policy Changes and other alternatives for going public in Canada.

by Mark Neighbor, Rajeev Dewan, Marina Tran, Gavyn B. Backus and Ashley E. Brown.

[1] [TSX Venture Exchange Bulletin RE Policy 2.4 – Capital Pool Companies \(December 1, 2020\)](#).

[2] [TSX Venture Exchange, "Capital Pool Company Program" \(2020\)](#).

[3] [TSX Venture Exchange, "Corporate Finance Manual" \(as at October 29, 2019\)](#); also see [TSX Venture Exchange, "Policy 1.1 – Interpretation" \(as at July 26, 2019\)](#).

[4] [TSX Venture Exchange, "Policy 2.4 – Capital Pool Companies" \(effective as of January 1, 2021\)](#); [TSX Venture Exchange, "Form 3A – Information Required in a CPC Prospectus" \(effective as of January 1, 2021\)](#); [TSX Venture Exchange, "Form 2F – CPC Escrow Agreement" \(effective as of January 1, 2021\)](#); and [TSX Venture Exchange,](#)

[“Form 3B1-3B2 – Information Required in an Information Circular for a Qualifying Transaction / Information Required in a Filing Statement for a Qualifying Transaction” \(effective as of January 1, 2021\).](#)

[5] [TSX Venture Exchange, “Policy 2.4 – Capital Pool Companies” \(as at June 14, 2010\);](#) [TSX Venture Exchange, “Form 3A – Information Required in a CPC Prospectus” \(as at June 14, 2010\);](#) [TSX Venture Exchange, “Form 2F – CPC Escrow Agreement” \(as at June 14, 2010\);](#) and [TSX Venture Exchange, “Form 3B1-3B2 – Information Required in an Information Circular for a Qualifying Transaction / Information Required in a Filing Statement for a Qualifying Transaction” \(as at June 14, 2010\).](#)

[6] NEX is a separate board of TSXV that provides a trading forum for listed companies that have fallen below the Exchange's ongoing listing standards.

[7] The Current CPC Policy places restrictions on a person's (and their affiliates', as applicable) percentage of ownership of the total IPO Shares. The CPC Policy Changes will change the ownership limitation from all IPO Shares to “75% of the IPO Shares”.

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#### **A Cautionary Note**

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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