

# Securities Law Bulletin

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## Getting it Right: CSA Amends the Prospectus-Exempt Rights Offering Regime

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A rights offering is a granting of subscription rights to existing security holders of an issuer. The issuer raises capital when the subscription rights are exercised. As rights offerings constitute a distribution under securities laws, unless an exemption is available, issuers must undertake the offering by way of a prospectus. The Canadian Securities Administrators (the “**CSA**”) have noted that a rights offering can be “one of the fairer ways for issuers to raise capital as they provide existing security holders with an opportunity to protect themselves from dilution.”

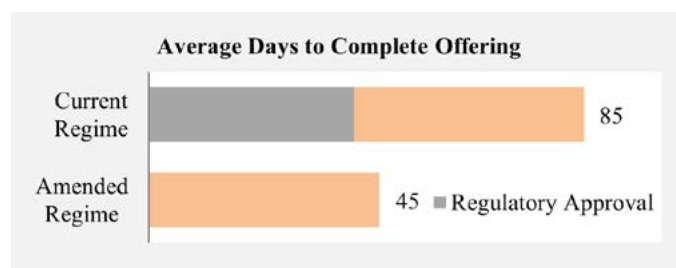
Thus, in seeking to encourage rights offerings, the CSA has provided notice of amendments that streamline the process for certain prospectus-exempt rights offerings (the “**Amendments**”). The Amendments, which will come into force on December 8, 2015, repeal National Instrument 45-101 *Rights Offerings* (“**NI 45-101**”) and amend the current prospectus exemption in National Instrument 45-106 *Prospectus Exemptions*.

### Benefits of Amendments

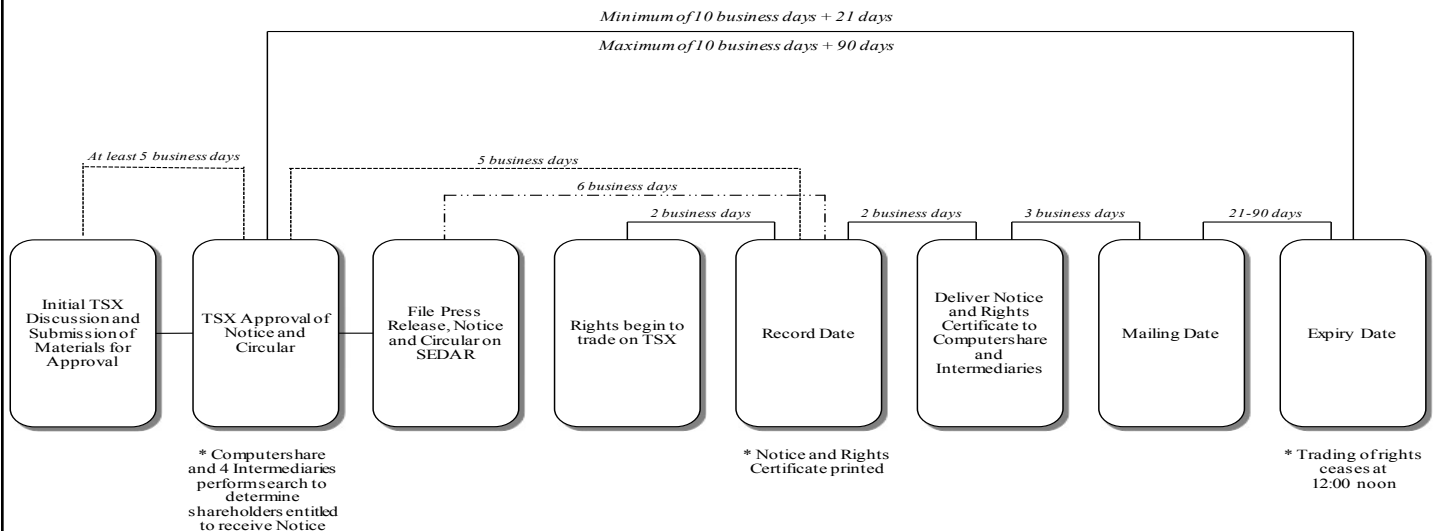
#### *Faster Offering Cycles*

The Amendments streamline the process for reporting issuers seeking to raise capital through prospectus-exempt rights offerings. Currently, the average length of time to complete a rights offering is 85 days, 40 days of which are typically spent obtaining the approval of securities regulators for the rights offering circular. This lengthy process increases the risks and costs associated with completing a rights offering and has historically limited the viability of rights offerings for Canadian issuers.

Under the new regime, securities commission approval is not required for a rights offering circular, potentially cutting the expected time required to complete an offering in half. However, as discussed in greater detail below, the CSA has extended statutory civil liability for secondary market disclosure to the acquisition of securities under a rights offering. Further, where an issuer is listed on either the Toronto Stock Exchange (the “**TSX**”) or the TSX Venture Exchange (the “**TSXV**”), exchange acceptance is still required before the offering proceeds. The following graphic illustrates a potential timeline for a rights offering for a TSX issuer following the implementation of the Amendments.



### Minimum Timeline for Rights Offering



#### Greater Dilution Means Greater Capital Raising Possibilities

An important change reflected in the Amendments is an increase to the permitted dilution limit from 25% to 100% of issued and outstanding securities of the type offered under the rights offering in any twelve month period. This change should make the exemption a more attractive option for smaller issuers in particular. Instead of relying on a hard dilution cap to protect investors, the CSA has imposed *pro rata* requirements for both the basic and additional subscription privileges.

#### Disclosure Requirements when Conducting an Offering

The Amendments significantly revamp the disclosure required for both the notice and the rights offering circular.

##### Rights Offering Notice

Currently, notice requirements are satisfied by distributing a draft rights offering circular required under Form 45-101F *Information Required in a Rights Offering Circular* (“**Form 45-101F**”). The Amendments, in contrast, require a separate dedicated form of notice, Form 45-106F14 *Rights Offering Notice for Reporting Issuers* (“**Form 45-106F14**”), be distributed. The new form follows an investor-friendly Q&A format and the CSA has indicated that it expects a length of at most two pages.

##### Rights Offering Circular

Currently, issuers must submit the draft form of rights offering circular required under NI 45-101 to applicable securities regulators for approval before distribution to prospective investors. To be approved, the rights offering circular must meet the informational requirements set out in Form 45-101F. Further, as Form 45-101F requires disclosure of business information, mining issuers run the risk of triggering the technical report filing requirements under National Instrument 43-101 *Standards of Disclosure for Mineral Projects* (“NI 43-101”).

The new Form 45-106F15 *Rights Offering Circular for Reporting Issuers* (“**Form 45-106F15**”), as with Form 45-106F14, follows a reader-friendly Q&A format. Significantly, Form 45-106F15 no longer requires the disclosure of business information, meaning mining issuers will forego the risk of triggering costly compliance with NI 43-101 in connection with a rights offering. Also, unlike Form 45-101F, Form 45-106F15 need not be distributed directly to security holders. Instead, the new form of notice directs security holders to the issuer’s SEDAR website in order to access the final rights offering circular. Permitting the electronic publication of the rights offering circular in lieu of physical distribution should result in significantly reduced printing, legal and distribution costs for an issuer.

### Secondary Market Liability

As discussed above, as a result of the Amendments, a rights offering circular is no longer required to be reviewed and approved by securities regulators. In streamlining the disclosure and review requirements, the CSA has assumed that most investors who choose to exercise rights are already familiar with the issuer's continuous disclosure documents.

To balance the reduced investor protection resulting from the removal of regulatory review, the CSA has extended statutory civil liability for secondary market disclosure to the acquisition of securities under a rights offering. As such, and similar to the requirements for a prospectus, issuers will need to certify in the rights offering circular that the document contains no misrepresentations, and investors will have a right of action for misrepresentations in the rights offering circular and other continuous disclosure documentation. However, unlike contractual liability, secondary market disclosure liability does not provide investors with a statutory right of rescission.

Unlike contractual liability which applies only against the issuer, rights of action under the statutory market liability regime are enforceable against a broader group of persons, including directors, officers, control persons and experts. Also, when claiming damages suffered from a misrepresentation, the statutory market liability regime does not require that an investor prove reasonable reliance.

### Pricing and Insider Participation

The Amendments require that the subscription price of a security issued as part of a rights offering must be:

- For publicly traded securities, lower than the market price of the security on the day of the rights offering notice is filed; or

- For non-publicly traded securities, the lower of the fair value of the security on the day the rights offering notice is filed unless insiders are not permitted to increase their proportionate interest in the issuer through the offering.

This is similar to the current pricing and insider participation restrictions.

### Staggered Offerings Remain

As with the current regime, subscriptions for securities under a rights offering may be conducted following the implementation of the Amendments through a staggered process. This process begins with the basic subscription privilege, or the privilege to subscribe for a number of securities stipulated in the rights certificate acquired through the rights offering (the "**Basic Privilege**").

However, where issuers are seeking to ensure a basic level of subscription is completed, the issuer can also grant additional subscription privileges ("**Additional Privileges**"), so long as the additional subscription rights are granted to all holders of rights. Additional Privileges are granted to the holders of the rights and constitute privileges to subscribe for securities not subscribed for under the Basic Privilege.

And finally, where issuers want to guarantee a basic level of subscription, the issuer can enter into an agreement referred to as a stand-by commitment. In the stand-by commitment, the stand-by guarantor commits to acquiring the securities of an issuer not subscribed for under either the Basic Privilege or the Additional Privilege. Currently, and following the implementation of the Amendments, a stand-by commitment can only be entered into if Additional Privileges were granted.

### Table of Changes to the Prospectus-Exempt Rights Offering Regime

	Current Prospectus-Exempt Rights Offering Regime	Amended Prospectus-Exempt Rights Offering Regime
To whom exemption is available	<ul style="list-style-type: none"> <li>• Reporting issuers who have filed all applicable periodic and timely disclosure documents</li> <li>• non-reporting issuers</li> </ul>	<ul style="list-style-type: none"> <li>• Reporting issuers who have filed all applicable periodic and timely disclosure documents and who are not investment funds</li> </ul>
Form of rights offering notice	<ul style="list-style-type: none"> <li>• Draft Form 45-101F</li> <li>• Distribute to security holders</li> </ul>	<ul style="list-style-type: none"> <li>• Form 45-106F14</li> <li>• Q&amp;A format</li> <li>• Distribute to security holders</li> <li>• Up to 2 pages in length</li> </ul>

**Table of Changes to the Prospectus-Exempt Rights Offering Regime (continued)**

	<b>Current Prospectus-Exempt Rights Offering Regime</b>	<b>Amended Prospectus-Exempt Rights Offering Regime</b>
Form of rights offering circular	<ul style="list-style-type: none"> <li>• Final Form 45-101F</li> <li>• Distribute to security holders</li> <li>• Mining issuers may need to fulfill NI 43-101</li> </ul>	<ul style="list-style-type: none"> <li>• Form 45-106F15</li> <li>• Q&amp;A format</li> <li>• Publish electronically on SEDAR</li> <li>• Up to 10 pages in length</li> </ul>
Exchange review requirements	<ul style="list-style-type: none"> <li>• Acceptance by TSX/TSXV before offering proceeds</li> </ul>	<ul style="list-style-type: none"> <li>• Acceptance by TSX/TSXV before offering proceeds</li> </ul>
Securities commission review requirements	<ul style="list-style-type: none"> <li>• Review process typically takes 40 days</li> </ul>	<ul style="list-style-type: none"> <li>• No review process</li> </ul>
Maximum dilution	<ul style="list-style-type: none"> <li>• 25% of securities of type offered under rights offering in any 12 month period</li> </ul>	<ul style="list-style-type: none"> <li>• 100% of securities of type offered under rights offering in any 12 month period</li> </ul>
Exercise period for rights	<ul style="list-style-type: none"> <li>• Between 21 and 90 days*</li> </ul>	<ul style="list-style-type: none"> <li>• Between 21 and 90 days</li> </ul>
Basic Privilege	<ul style="list-style-type: none"> <li>• Must be offered to current security holders</li> </ul>	<ul style="list-style-type: none"> <li>• Must be offered on a pro rata basis to all security holders resident in Canada</li> </ul>
Additional Privilege	<ul style="list-style-type: none"> <li>• If offered, must be offered to all rights holders</li> </ul>	<ul style="list-style-type: none"> <li>• If offered, must be offered on a pro rata basis to all rights holders</li> </ul>
Secondary market liability	<ul style="list-style-type: none"> <li>• No</li> </ul>	<ul style="list-style-type: none"> <li>• Yes</li> </ul>
Seasoning period on resale**	<ul style="list-style-type: none"> <li>• Yes</li> </ul>	<ul style="list-style-type: none"> <li>• Yes</li> </ul>

\*for reporting issuers only; the period for non-reporting issuers is less than 60 days

\*\*securities will be immediately free-trading if the issuer has been a reporting issuer in good standing for at least four months

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