

Raising U.S. Funds Under Canada's New "Listed Issuer Financing Exemption"

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As many of our readers will have heard, the Canadian Securities Administrators ("CSA") has announced the adoption of a new prospectus exemption for certain reporting issuers listed on a Canadian stock exchange (the "Listed Issuer Financing Exemption"), effective November 21, 2022. To date, little attention has been given to the potential effect of the Listed Issuer Financing Exemption on the practices of Canadian listed companies raising funds from U.S. investors. In this post, we discuss those implications and suggest methods for relying on the Listed Issuer Financing Exemption while still preserving the ability to raise funds from U.S. investors.

Overview of the Listed Issuer Financing Exemption

The Listed Issuer Financing Exemption will allow certain reporting issuers listed on a Canadian stock exchange to complete a public offering of securities in Canada for cash to raise up to C\$5 million (up to C\$10 million for larger companies), with no investor qualifications, no legends or hold periods on the securities sold in the public offering, and no prospectus (an "Offering"). As such, the Listed Issuer Financing Exemption may become an important fundraising tool for Canadian public companies, especially those with smaller market capitalizations.

Many Canadian law firms have published summaries of the Listed Issuer Financing Exemption and its requirements. The most important requirements for our purposes are that the issuer publish a press release describing the Offering, and file and post on the issuer's website a completed Form 45-106F19 which outlines certain brief information about the Offering (the "Offering Document"). The intention of the CSA appears to have been to reduce the burdens on reporting issuers when conducting a relatively small Offering, as long as the issuer is current in its continuous disclosure requirements, meets certain other requirements, and publishes certain basic information about itself and the Offering.

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Overview of U.S. Private Placement Exemptions

The U.S. federal securities laws do not provide an equivalent exemption to the Listed Issuer Financing Exemption. Most Canadian public companies that offer and sell securities to U.S. investors as part of an Offering (a “U.S. Offering”) conduct the U.S. Offering either:

- In a fully underwritten offering, as resales by the underwriter to U.S. qualified institutional buyers in reliance upon Rule 144A under the U.S. Securities Act; or
- In non-brokered or agency offerings, as a sale by the issuer exclusively to U.S. accredited investors, without any general solicitation or general advertising, pursuant to Rule 506(b) of Regulation D under, or Section 4(a)(2) of, the U.S. Securities Act.

Therefore, outside of underwritten Rule 144A offerings, most U.S. Offerings by Canadian public companies are undertaken on the basis that no general solicitation or general advertising has been made in the U.S. Offering.

General solicitation and general advertising includes, without limitation:

- Any advertisement, article, notice or other communication published in any newspaper, magazine, or similar media or broadcast over television or radio; and
- Subject to limited exceptions, any seminar or meeting whose attendees have been invited by any general solicitation or general advertising.

As the internet became more prevalent, the SEC issued an interpretation confirming that the “use of an unrestricted, publicly available website to offer or sell securities constitutes a general solicitation and is not consistent with the prohibition on general solicitation and advertising ... if the website contains an offer of securities”.

Notwithstanding the foregoing, the SEC has published rules governing the purpose, content and use of press releases which, if complied with, provide a safe harbor under which a press release will not be deemed to be general solicitation or general advertising for a U.S. Offering.

Rule 506(c) of Regulation D under the U.S. Securities Act is an alternative exemption that allows an issuer to make sales to U.S. accredited investors in an Offering in which general solicitation or general advertising is employed, but only if the issuer takes certain steps that the SEC deems to be “reasonable” in verifying the accuracy of the investor’s claim of being an accredited investor. The SEC has provided some non-exclusive examples of steps that may be considered reasonable, include obtaining and reviewing an individual investor’s tax returns to establish net income, or obtaining a recent certification from the investor’s U.S. broker, lawyer or accountant. To date, this exemption has been used relatively rarely, due to the significant additional burden on issuers and investors of satisfying this due diligence requirement, and the risk that asking for this information will scare off investors who consider it an invasion of privacy.

Planning a U.S. Offering Under the Listed Issuer Financing Exemption

An issuer that consults with its U.S. counsel in advance should be able to ensure its ability to proceed with a U.S. Offering as a part of a broader Offering under the new Listed Issuer Financing Exemption. Whichever U.S. exemption will be used, the issuer's forms of offering documents will need to be updated. More importantly, issuers that intend to continue relying on the Rule 506(b) or Section 4(a)(2) exemptions must ensure that their use of the Listed Issuer Financing Exemption for the Offering will not involve any general solicitation or general advertising for purposes of the U.S. Offering. Of particular concern are the purpose, content and use of the mandated press release, the method of using and posting the Offering Document on the issuer's website, and the method by which U.S. investors are brought into the U.S. Offering. Issuers that intend to allow general solicitation and rely on the Rule 506(c) exemption must prepare new due diligence procedures.

To ensure compliance under the new rules, the following matters should be discussed with U.S. counsel in advance:

- The issuer's eligibility for, and selection of, the U.S. securities exemption for the U.S. Offering;
- The purpose, content and use of the press release announcing the Offering – in many cases, the names of underwriters or agents participating in the Offering may not be included in the press release;
- The approach toward posting the Offering Document on the issuer's website, including whether the issuer should employ geofencing or geoblocking technology, mandatory questionnaires or other means to prevent users in the United States from accessing the Offering Document on the website;
- The description of the U.S. Offering restrictions within the Offering Document and/or in a U.S. "wrap" around the Offering Document that is used for purposes of explaining the U.S. Offering;
- The portions of the subscription agreement to be completed by U.S. investors, or separate U.S. subscription agreement, if applicable;
- The response to any prospective U.S. investor that became interested in the U.S. Offering by viewing the press release or Offering Document, and how to reduce the risk of this occurring;
- In a Rule 506(c) offering, the method of verifying an investor's status as an accredited investor;
- Any underwriters, agents or finders, or the payment of fees or commissions to U.S. persons or for soliciting U.S. investors; and
- Any applicable U.S. notice filing or state securities law requirements.