



## **Local Policy 41-601**

### **NEW BRUNSWICK SECURITIES COMMISSION POLICY 41-601 CAPITAL POOL COMPANIES**

#### **Introduction**

The TSX Venture Exchange Inc. (the "TSX Venture") currently operates a capital pool company program (the "CPC Program") in each of Alberta, Saskatchewan, Manitoba, Ontario, Quebec, British Columbia, Nova Scotia and New Brunswick (the "CPC Jurisdictions"). The CPC Program was designed as a corporate finance vehicle to provide businesses with an opportunity to obtain financing earlier in their development than might otherwise be possible through a normal initial public offering (an "IPO"). The CPC Program permits an IPO to be conducted and a TSX Venture listing to be achieved by a newly created capital pool company (a "CPC") which has no assets, other than cash, and which has not commenced commercial operations. The CPC then uses this pool of funds to identify and evaluate assets or businesses which, when acquired (a "Qualifying Transaction"), qualify the resulting issuer (the "Resulting Issuer") for listing as a regular Tier 1 or Tier 2 issuer on the TSX Venture. The CPC Program will assist in harmonizing the ability of entrepreneurs to raise venture capital in the CPC Jurisdictions.

This Policy sets out the views of the New Brunswick Securities Commission (the "Commission") as to whether issuers participating in the CPC Program should be permitted to conduct public offerings in New Brunswick.

#### **Background**

In 1986, the Junior Capital Pool ("JCP") program, a predecessor to the CPC Program, was initiated in Alberta through the co-operation of the Alberta Securities Commission and The Alberta Stock Exchange. In 1997, the British Columbia Securities Commission and the Vancouver Stock Exchange adopted a similar program, the Venture Capital Pool ("VCP") program, for use in British Columbia. The current CPC Program, created following the merger of the Vancouver Stock Exchange and The Alberta Stock Exchange to form the Canadian Venture Exchange Inc. ("CDNX") in November 1999, replaced the existing VCP and JCP programs. Prior to the merger of the Winnipeg Stock Exchange with CDNX in November 2000 and the subsequent approval of the CPC Program by the Manitoba Securities Commission, a similar junior capital program, known as the Keystone Company Program, was previously available in Manitoba.

#### **Operation of the Program**

The CPC Program is currently governed by TSX Venture Policy 2.4 Capital Pool Companies ("TSX Venture Policy 2.4"). TSX Venture Policy 2.4 provides that an issuer wishing to participate in the CPC Program must file a preliminary prospectus and related supporting documents with the TSX Venture as well as with each of the securities regulatory authorities in whose jurisdictions the proposed distribution will be made.

A CPC prospectus that is filed in New Brunswick will be reviewed by the staff of both the TSX Venture and the Commission. Upon the issuance of a receipt for a final prospectus and the completion of its IPO, securities of a CPC will trade on Tier 2 of the TSX Venture. A CPC will have 18 months following its IPO to identify and complete a Qualifying Transaction. However, as soon as a CPC reaches an "agreement in principle" (as defined below) with respect to a proposed Qualifying Transaction, it must issue a comprehensive news release. The CPC Program requires each CPC to seek the approval of both the TSX Venture and a majority of its minority shareholders, in appropriate circumstances, prior to completing the Qualifying Transaction.

In connection with obtaining such shareholder approval, the CPC must prepare a comprehensive information circular containing full, true and plain disclosure concerning the CPC and the Qualifying Transaction. The information circular must contain the same information as a company would be required to disclose if it filed a prospectus. The information circular will be reviewed by the TSX Venture before it is mailed to shareholders of the CPC. The CPC Program will not be available to issuers if, prior to the completion of its IPO, an agreement in principle has been reached with respect to a proposed Qualifying Transaction. An "agreement in principle" includes any enforceable agreement or any other agreement or similar commitment which identifies the fundamental terms upon which the parties agree or intend to agree which:

1. identifies assets or a business to be acquired which would reasonably appear to constitute "significant assets", the acquisition of which would reasonably appear to constitute a Qualifying Transaction;
2. identifies the parties to the Qualifying Transaction;
3. identifies the consideration to be paid for the "significant assets" or otherwise identifies the means by which the consideration will be determined; and
4. identifies the conditions to any further formal agreements to complete the transaction, and in respect of which there are no material conditions to closing (other than receipt of shareholder approval and TSX Venture acceptance), the satisfaction of which is dependent upon third parties and beyond the reasonable control of the non-arm's length parties to the CPC or the non-arm's length parties to the Qualifying Transaction. Both TSX Venture and the securities regulatory authorities in the CPC Jurisdictions are of the view that if the issuer has reached an agreement in principle, it is able to, and should, prepare a regular prospectus.

Further information regarding the operation of the CPC Program can be found by consulting the TSX Venture Corporate Finance Manual and TSX Venture Policy 2.4.

### **Historical Concerns Versus Anticipated Benefits of the Program**

Historically, the Executive Director has been reluctant to issue a receipt for a prospectus where the prospectus revealed the issuer to have neither a business nor operations and no assets, other than cash. In Ontario, the Ontario Securities Commission (the “OSC”) has considered this issue in several decisions. In *Re Loki Resources Inc.* (1984), 7 OSCB 583, the OSC Director noted that where an issuer has neither assets to appraise nor business activities to evaluate, nor any present expectation of either assets or activities, meaningful information regarding an issuer cannot be provided to market participants. Accordingly, in such an instance, the benefits of “eporting issuer status”, including the ability of its securities to freely trade in the market following the expiry of any applicable hold period, should not be conferred upon the issuer. This approach was supported by the subsequent OSC decision in *Re Inland National Capital Inc.* (1996), 19 OSCB 2053.

While the concerns expressed in *Loki* and *Inland National Capital* remain relevant today, the Commission is aware that the implementation of the CPC Program in New Brunswick may also confer benefits upon New Brunswick's capital markets by providing entrepreneurs and emerging businesses access to the financial and other resources necessary for such enterprises to fully develop. Moreover, the Commission has also noted that the CPC Program provides certain investor protection provisions that were unavailable in the *Loki* and *Inland National Capital* cases, which, in the view of the Commission, help mitigate the potential for harm to investors identified in those decisions.

These provisions include the following:

1. management of a CPC is scrutinized by the TSX Venture to ensure that management has experience appropriate to the running of a public company and the completion of a Qualifying Transaction;
2. management's track record must also be disclosed in the CPC prospectus to allow potential investors a basis upon which to make an investment decision;
3. the risk of the investment is clearly and prominently disclosed throughout the CPC prospectus;
4. directors and officers of a CPC must contribute a minimum amount of cash prior to an IPO, and a CPC may raise only a limited amount of cash under the CPC prospectus;
5. furthermore, a CPC is subject to strict regulation of private placements prior to the completion of its Qualifying Transaction;
6. the amount that may be invested by any one individual during an IPO is limited to 2% of the shares issued under the CPC prospectus, and no more than 4% of the shares issued under the CPC prospectus may be purchased by an investor and his or her associates and affiliates during the IPO;

7. most shares held by non-arm's length parties of a CPC are escrowed until the completion of the Qualifying Transaction and then are released in stages;
8. when a CPC reaches an "agreement in principle" to acquire the business or assets that will be the subject of the Qualifying Transaction, trading in its shares is halted until a detailed press release describing the transaction is issued, a sponsor is retained (unless waived) and TSX Venture staff is satisfied that there are no obvious reasons why the Qualifying Transaction cannot be completed;
9. each CPC must file and distribute to its shareholders an information circular which is subject to review and which must provide prospectus level disclosure of the Qualifying Transaction and the Resulting Issuer in accordance with TSX Venture requirements;
10. TSX Venture staff will closely monitor secondary trading in securities of CPCs to help guard against insider trading; and
11. a CPC which fails to complete its Qualifying Transaction within 18 months may be suspended or de-listed and potentially subject to a cease trade order, thereby ensuring that secondary trading in shares of the CPC does not continue indefinitely.

In discharging its statutory duty, the Commission must have consideration for the purpose of the *Securities Act* (the "Act"). Section 2 of the *Act* states that the purpose of the *Act* is to provide protection to investors from unfair, improper or fraudulent practices and to foster fair and efficient capital markets and confidence in capital markets.

Upon considering the CPC Program and balancing the purpose and principles underlying the *Act*, the Commission has decided that it would not be prejudicial to the public interest to permit the operation of the CPC Program in New Brunswick.

#### **Availability of the Program in New Brunswick**

As the Commission has determined that it would not be prejudicial to the public interest to permit CPCs to conduct IPOs in New Brunswick, the Executive Director is generally willing to issue a final receipt for a CPC prospectus on the basis of the issuer's participation in the CPC Program.

On the basis of the *Loki* and *Inland National Capital* cases, however, it is unlikely that, in the absence of an issuer's participation in the CPC Program, the Executive Director will consider it to be in the public interest to issue such a receipt to a "shell issuer".

Issuers contemplating participation in the CPC Program should therefore be cautioned that the Commission will consider issuing a cease trade order in respect of the securities of a CPC if such CPC is de-listed on account of its failure to complete its Qualifying Transaction or otherwise comply with the Program.

#### **Review of the Program**

The Commission intends to monitor the functioning of the CPC Program to assess the benefits it confers upon New Brunswick's capital markets.