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Canada/Cross-Border

Canadian Capital Markets Lure Small and Mid-cap Clean-Tech

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With more than 3,600 listed companies, the Toronto Stock Exchange (TSX) and the TSX Venture Exchange (TSX V) rank second among the world's stock exchanges. In recent years they have emerged as the world's leading exchanges for listing clean-tech companies. In 2010, clean-tech companies raised over Cdn$1.3 billion on both the TSX and the TSX V.

An increasing number of U.S. clean-tech companies are exploring the Canadian capital markets because they are too small for listing on the Nasdaq. For example in December, 2010, Global Water Resource Corp., a Phoenix-based water resource management company, raised approximately $65 million through an initial public offering on the TSX.

Currently, there are approximately 160 U.S. companies listed on the TSX exchanges. International clean-tech companies are also gravitating towards the exchanges. In 2009, China Wind Power International Corp. listed on the TSX V. In 2011, Nesscap Energy Inc. (a South Korean based clean-tech company) listed on the TSX V.

This article provides an overview of why a U.S. company should consider listing on the TSX exchanges, and the various options available for taking a company public in Canada.

> The exchanges are leveraging their traditional strengths in listing gas and exploration companies. As a result, there is a pool of investment bankers and investors who understand renewable energy.

THE TWO EXCHANGES

The TSX is the senior exchange. It has listing standards for well established businesses and management teams with experience in public markets. The TSX V is the junior exchange. It has adopted listing standards which are tailored towards emerging companies or smaller financings, and it has more flexible listing standards.

A U.S. company could initially list on the TSX V, then graduate to the senior TSX once it has reached its business milestones. A streamlined regulatory protocol fosters this process. Thirty percent of clean-tech companies that initially listed on the TSX V have successfully graduated to the TSX.

The TSX exchanges currently list approximately 130 clean-tech companies, with an aggregate market capitalization of approximately Cdn$19 billion. One of the main reasons there are so many clean-tech listings is the abundance of entrepreneurial capital in Canada. The traditional strength of the exchanges has been gas and fuel exploration companies, which has resulted in a pool of investment bankers and investors who understand energy.

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In March 2010, the TSX launched the S&P/TSX Clean Technology Index. It measures the performance of listed companies that generate over 50 percent of their revenue from products or services focused on eliminating negative ecological impacts, while utilizing natural resources productively and responsibly.

BENEFITS OF LISTING

The costs associated with going public in Canada tend to be less than those in the United States. Legal, audit and accounting costs on a small offering range between Cdn$200,000 and $500,000. Larger, more complex offerings cost up to $1,000,000. The lower costs are attributable in large part to the differences between the regulatory environment in Canada and the United States, differences that also translate into lower ongoing compliance costs. For example, under Canadian securities law, the obligations of auditors are not as stringent as requirements under Sarbanes-Oxley.

Investors in Canada are notably interested in small and mid-cap companies, and analysts cover them comprehensively. Approximately 86 percent of companies listed on the TSX V have a market capitalization of Cdn$50 million or less. About 31percent have a market capitalization between $50 million and $250 million.

In 2010, there were more than 100 financings completed by clean-tech companies listed on both exchanges, with more than 3.5 billion shares trading. That represented approximately $7.3 billion in value.

Twenty-five international brokers are trading members of the exchanges, including, Goldman Sachs, JP Morgan, Citigroup and Merrill Lynch. Collectively they account for 40 percent of daily trades.

The process for going public in Canada is similar to the U.S. process. Typically it takes three to six months. It may be quicker to file and get a prospectus finalized with Canadian regulators in comparison with the SEC. (This process can sometimes be completed within 60 days.) It also may be quicker for a U.S. company to list on the TSX or the TSX V by way of a qualifying transaction or a reverse-takeover (both discussed below), because a prospectus is generally not required.

There is no requirement for a U.S. company to establish a Canadian office. However, foreign companies often designate a party resident in Canada to manage investor relations.

OPTIONS FOR GOING PUBLIC

One option is a traditional IPO, similar to an IPO in the U.S. market. The process includes preparing and clearing a prospectus with the applicable Canadian regulators, undertaking the requisite due diligence and conducting a road show.

Corporate structure and jurisdiction of incorporation are important considerations for a U.S. company considering an IPO in Canada. These structuring choices are often driven by a thorough analysis of U.S. securities and tax law in light of an IPO in Canada.

The reverse-takeover, or backdoor option, permits a private U.S. company to immediately obtain a listing by taking over an existing listed company. These transactions are generally achieved either by way of statutory amalgamation or through a share exchange between the target listing company and the private company.

Irrespective of how the transaction is executed, the successor company formed as a result would need to meet the listing standards of either the TSX or the TSX V. An information circular is required for review by either exchange, and shareholder approval is required.

The Capital Pool Company Program (CPC) was created by the TSX V to allow seasoned directors and officers with no commercial operations to raise capital in order to acquire an operating business. This program consists of two-phases: creating and capitalizing a CPC through a prospectus filed and reviewed by Canadian securities regulators, and identifying at closing a qualifying transaction with an operating business that meets the listing standards, within a two year time-line.

The qualifying transaction is usually accompanied by concurrent financing conditional on closing. The CPC is subject to several requirements, including a minimum number of public shareholders and a limit on the amount of capital which it can initially raise.

Some of the key advantages of the CPC are that it provides an alternative route to accessing capital for a company that is not ready for a traditional IPO; it doesn't entail the risk of an IPO; and a qualifying transaction can be completed quickly in comparison to an IPO because a filing statement or information circular is required to be filed and reviewed by the TSX V in lieu of a prospectus.

Since the establishment of the CPC more than 2,000 capital pool companies have been established, and approximately 80 percent of them have completed qualifying transactions. The CPC has been successfully utilized by a number of clean-tech companies to go public in Canada.

U.S. clean-tech companies considering their financing options should consider the TSX or the TSX V as a viable alternative to other public and private options, given the clear leadership that these exchanges have demonstrated. ■

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