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À : lstreu@bcsc.bc.ca; Consultation-en-cours
Cc : CSA ACVM Secretariat
Objet : CSA comment period on rights offering regulatory changes

For the attention of: -

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority (Saskatchewan)
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon
Superintendent of Securities, Nunavut

Please find attached our comments on the proposed amendments to NI 45-106 Prospectus and Registration Exemptions, NI 41-101 General Prospectus Requirements, NI 44-101 Short Form Prospectus Distributions and NI 45-102 Resale Restrictions and Proposed Repeal of NI 45-101 Rights Offering. Our comments are being made on behalf of Scorpeo UK Ltd, our speciality being advising asset managers on corporate events, including rights issues.
As suggested by the CSA Secretariat we have outlined our comments following the specific questions, but would be happy to discuss further if points are unclear or require further depth.

With thanks in advance for your consideration.

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Questions relating to the Proposed Exemption

1. We propose that the exercise period for a rights offering under the Proposed Exemption must be a minimum of 21 days and a maximum of 90 days. These time periods are substantially consistent with those under the Current Exemption. Some market participants have told us that an exercise period of 21 days is too long. Others thought a longer exercise period is beneficial. Reasons cited for a longer exercise period are that at least 21 days may be necessary to reach beneficial security holders and foreign security holders and that institutional investors often need a longer period to receive approvals.

   (a) Do you agree that the exercise period should be a minimum of 21 days and a maximum of 90 days?
   No.

   (b) If not, what are the most appropriate minimum and maximum exercise periods? Why?

   In other jurisdictions, the minimum exercise period is 14 days (UK); similarly maximum periods are often restricted to 70 days (10 week maximum.) A two week period should be more than sufficient for shareholders to be notified of a rights issue and act accordingly. I would challenge why 3 weeks is necessary to reach beneficial security holders when in the UK 14 days is deemed sufficient and has become established without material problems. Similarly a 10 week period seems unnecessarily long. Having the option as an issuer to close the rights within 14 days removes material timing uncertainty. The reduction in timing risk reduces the cost of any underwriting fees to be paid.

   Should of course a corporate wish to extend a rights issue, or if for example a change to the terms in favour of shareholders is proposed (such as a reduction in exercise price), I would also suggest that an underwriter have the right to extend the period of exercise once for an additional 2 weeks, subject to the total subscription period being within the maximum timeframe. Again this would serve to protect the corporate issuer's shareholders, both in price paid and additionally reducing the possibility of otherwise having the underwriters own a large block of shares and creating a significant stock overhang. This capacity to extend in extremis would also reduce underwriting fees.

   I would also respectfully add that the trading period of rights should cease at least 3 business days prior to the end of the exercise period, to allow settlement of rights in good form for delivery to the agent.

2. We propose that the Notice must be filed and sent before the exercise period begins and that the Circular must be filed concurrently with the Notice. Do you foresee any challenges within this timing requirement?
   No.

3. Some market participants have suggested we consider requiring the issuer to only file and not send the Notice and the Circular. While we do not think that the issuer should have to send the Circular itself, it is our view that the issuer should send the Notice to ensure that each security holder is aware of the offering. We also understand that the issuer would have to send rights certificates to security holders in any event.

(a) Do you foresee any challenges with requiring the issuer to send a paper copy of the Notice?
No – a reasonable attempt should be made to contact smaller shareholders.

(b) Do you foresee any challenges with the Circular only being available electronically?
No, not if a Notice is sent pointing shareholders to where it can be found electronically (company website or CEDAR, etc.)

4. The required disclosure in the proposed Circular focuses on information about the offering, the use of funds available and the financial condition of the issuer. We do not propose to require information about the business in the Circular.

(a) Have we included the right information for issuers to address in their disclosure?
No – I would add additional information as per 4(b).

(b) Is there any other information that would be important to investors in making their investment decision in the rights offering?
I would also include any additional information that would reasonably be expected to impact the underlying share price throughout the rights offering, such as if quarterly results are due to be released during the rights offering or a dividend is due to go ex and details thereof, etc.

5. Under the Proposed Exemption, we would require the issuer to include certain information in their closing news release including the amount of securities distributed under each of the basic subscription privilege and the additional subscription privilege to insiders as a group and to all other persons as a group. Other required disclosure includes the aggregate gross proceeds of the distribution, the amount of securities distributed under any stand-by commitment, the amount of securities issued and outstanding as at the closing date and the amount of any fee or commission paid in connection with the distribution. This information will give investors a more complete understanding of who acquired securities under the rights offering.
Do you think that this disclosure will be unduly burdensome? If so, what disclosure would be more appropriate?
No, however disclosure should include all statistics on the result of the rights. Full disclosure of all details of the rights issue, including information such as what percentage of subscribing shares requested the additional subscription privilege (and not just the number subsequently distributed), are essential in establishing a true picture of demand by shareholders. Partial disclosure could allow obfuscation by management of the true pattern of shareholder demand.

6. The Current Exemption permits the trading of rights and we propose to allow for the trading of rights under the Proposed Exemption. We have received mixed feedback from market participants on the costs and benefits of allowing rights to trade freely. On the one hand, the trading of rights adds complexity to a rights offering and could potentially add a few days to the timeline for an average rights offering. The trading of rights also allows the issuance of free-trading securities to new investors. On the other hand, the trading of rights may benefit issuers as it often puts the rights into the hands of holders who are more likely to exercise the rights. It allows for monetization, which means that security holders who are unable to exercise rights could receive compensation for the rights. It also benefits foreign

security holders as the issuer's transfer agent will typically attempt to sell the rights of ineligible security holders on the market.

(a) Should we continue to allow rights to be traded? If so, why?
No

(b) What are the benefits of not allowing rights to be traded?
Benefits are reducing cost to the issuing corporate / sponsoring bank. The proposed changes in timeline for rights exercise (Question 1.) will have a materially larger impact than the 'few days' additional to the timeline required for trading. Potentially the cost of trading in proportion to the size of the capital to be raised in the rights issue could be estimated to set a minimum size rights above which trading of rights should be expected. (CAD 250mm?)

(c) Should issuers have the option of not listing rights for trading?
Please see (b) above – an option should be available if the cost of trading is prohibitive relative to capital to be raised. In any extent the issuing company should ensure that the rights are transferable between entities to reduce settlement problems over ex. date.

7. When we looked at historic use of rights offerings by reporting issuers, we found that the time between the filing of the draft circular and the notice of acceptance was quite lengthy (an average of 40 days). As a result, we considered options to reduce the review period. One of the options was to conduct a more focused initial review in three days rather than 10 days prior to the regulators' acceptance of the offering. The review would focus on sufficiency of proceeds, stand-by commitments, use of proceeds, insiders, and other issues that raise significant investor protection or public interest concerns. We decided not to proceed with this option but instead to remove regulatory review prior to use. This is similar to other prospectus exemptions and it would significantly improve issuers' time to market. Certain jurisdictions are also proposing reviewing rights offerings on a post-distribution basis for a period of two years to assess the use of and compliance with the Proposed Exemption.

(a) Do you agree with our proposal to remove pre-offering review?
Yes

(b) Do the benefits of providing issuers with faster access to capital outweigh the costs eliminating our review?
Yes

(c) Post-distribution review would focus on sufficiency of proceeds, stand-by commitments, use of proceeds, insiders and other issues that raise significant investor protection concerns. Are there other areas that we should focus on?
That the capital raised is used for the prescribed purpose stated in the offering, to avoid management changing the use of proceeds without shareholder consent.

8. Currently, an investor in a rights offering has no statutory recourse if there is a misrepresentation in an issuer's rights offering circular or continuous disclosure record.

We propose that civil liability for secondary market disclosure provisions would apply to the acquisition of securities in a rights offering under the Proposed Exemption.

(a) Is this the appropriate standard of liability to protect investors given that there will be no review by CSA staff of an issuer's rights offering circular?
While an advance on the current situation it is still not ideal - please see below.

(b) Would requiring a contractual right of action for a misrepresentation in the circular be preferable? If so, what impact would this standard of liability have on the length and complexity of an issuer's offering circular, given that in order for the contractual liability to cover additional continuous disclosure record documents, the issuer may have to incorporate by reference those documents into the issuer's circular.
Yes, this is preferable – as it would ensure that both the corporate and sponsoring bank are liable for misrepresentation or fraud. This standard of liability should have no real impact on issuers who have, 'nothing to hide'.
If the circular is to be made available on SEDAR / company website, then including additional documents by reference to similar weblinks in our view does not materially add to any degree of complexity.

9. Given the potential size of rights offerings, there may be circumstances where it is desirable to mitigate the effect of the offering on control of an issuer. In this regard, CSA staff question whether security holders would benefit from separating the timing of the basic subscription and additional subscription privilege such that an issuer would announce the results of the basic subscription before commencing the additional subscription privilege period. An issuer's announcement of the results of the basic subscription may help security holders make more informed decisions about their participation under the additional subscription privilege.

(a) Would security holders benefit from knowing the results of the basic subscription before making an investment decision through the additional subscription privilege?

No. If all shareholders participate in their rights pro rata to their existing stakes, there will be no net change of control. We assume therefore that the relative participation in the basic subscription alone would have a larger impact on change of control than the (presumably) much smaller possible change as a result of any additional subscription on shares remaining post basic subscription. The decision to participate or not in the basic subscription is therefore a materially larger 'informed decision' than that in the additional subscription. The separation between basic and additional subscription results does not therefore in our view offer any material advantage to shareholders. It would however prolong the closure of the Rights issue, and therefore delay capital delivery to the issuer. Additionally, any extended period between basic and additional subscription close introduces market price risk, which increases underwriting costs to the issuer. Informing shareholders of the results of additional subscriptions post close of the offering should be required to be in a timely manner (Close of offer + 2 days?)

(b) Would security holders make a different investment decision through the additional subscription if the results of the basic subscription were announced? If so,

- Should the additional subscription privilege be inside or outside of 21 days?

- Should the split timing for basic subscriptions and additional subscriptions always be required or only required in circumstances where there may be an impact on control?

Potentially, security holders would make different investment decisions in the additional subscription if the results of the basic subscription are known. The price of the underlying shares will in all probability react to the result of the basic subscription results. (Or indeed as a result of wholly exogenous market movements.) If the market rallies, then the value of subscription rights will increase and additional subscription become more attractive; or vice versa.

- **Additional subscription privilege should be along with, or at a very short time after the basic subscription**
- **Please see 9(a) – no split timing in our view is required. (There is no such split results release timing for example in most of the European markets.)**

(c) What are the costs and benefits of having a two-tranche system for security holders?

Please see 9(a), in our view, costs of delay, increased risk and underwriting costs outweigh the 'benefits' – which as described above *if* available cannot be separated from market directional movements.

Questions relating to the repeal of the Current Exemption for use by non-reporting issuers

10. We propose repealing the Current Exemption for use by non-reporting issuers. There is very little use of the Current Exemption by non-reporting issuers. We also have concerns that existing security holders of non-reporting issuers do not have access to continuous disclosure about the issuer and the rights offering circular contains very limited disclosure about the issuer and its business. Accordingly, there may not be sufficient disclosure upon which an investor can make an informed investment decision.

(a) If we repeal the rights offering prospectus exemption for non-reporting issuers,

- Would this create an obstacle to capital formation for non-reporting issuers?
- Do you foresee any other problems?
- Would repealing the Current Exemption cause problems for foreign issuers that do not meet the Minimal Connection Exemption? If so, should we consider changes to the Minimal Connection Exemption? Please explain what changes would be appropriate and the basis for those changes.

(b) Do you think we should consider changes to the Current Exemption instead of repealing it? If so, what changes should we consider?

- If you think we should change the disclosure requirements, please explain what disclosure would be more appropriate.
- Should non-reporting issuers be required to provide audited financial statements to their security holders with the rights offering circular if they use the exemption?

(c) If the Current Exemption is repealed, non-reporting issuers could continue to offer securities to existing security holders under other prospectus exemptions such as the offering memorandum exemption, the accredited investor exemption, and the family,

friends and business associates exemption. Are there other circumstances in which non-reporting issuers need to rely on the Current Exemption? If so, please describe.

(a) The proposed regulations would in our view adequately replace the Current Exemption for non-reporting issuers, and if liability as in 8(b) is introduced offer increased protection to the investor in the Rights. Similarly for foreign issuers, if they are by 8(b) required to have the support of a local Canadian bank (who also take final liability) the problem would be one of establishing credit worthiness between the issuer and bank. (No comment on part b or c.)

Questions relating to the Stand-by Exemption

11. We propose that the securities distributed under the Stand-by Exemption to a stand-by guarantor who is not a current security holder or who is a registered dealer will be subject to a four-month hold period. We understand that stand-by guarantors are often either insiders of the issuer or registered dealers.

(a) Should stand-by guarantors be subject to different resale restrictions depending on whether or not they are security holders of the issuer on the date of the notice?

If the stand-by guarantor has a board seat due to their stake size, or is otherwise privy to internal information not available to external minority shareholders then our opinion is there should be additional caveats on their stake. This should equally apply to both existing shareholders and new shareholders if their stake would enable them to seek board representation. If there is no potential insider status then our view would be not to impose a requirement for a resale restriction.

(b) What challenges would there be for issuers trying to find a stand-by guarantor that is not already a security holder?

This will depend upon the time sensitivity of the need for the capital being raised and available information on the company (analyst coverage etc.) If a very tight time requirement on a poorly followed stock it could be very difficult indeed to both find and educate a potential guarantor.

12. We are considering whether securities distributed under the Stand-by Exemption to a stand-by guarantor that is an existing security holder should also be subject to a four month hold.

(a) If the stand-by guarantor is an existing security holder, should we require a four month hold? Why or why not?

Please refer to answer 11 above – a four month hold should only be required in our view if the stake size confers any additional rights such as board representation or insider status.

(b) We understand that in many cases, a stand-by guarantor receives a fee for providing a stand-by commitment. Should a stand-by guarantor that receives a fee and is a current security holder be subject to a restricted period on resale when other security holders are not subject to the restricted period?

Please see the answer to 12 (a) above – the payment of a fee for being a guarantor should not influence the resale restrictions, only I our view the impact of any purchase commitment would have on access to internal information.

(c)What challenges do you foresee if we require a four-month hold?

To both regulate and police that the guarantor does not use any other means to effect a sale prior to the expiry of the hold period – e.g. by purchasing puts or other OTC transactions.

Question relating to the Minimal Connection Exemption

13. We are considering whether we should require the filing of materials with the regulator through SEDAR as part of the Minimal Connection Exemption. Most issuers using the Minimal Connection Exemption would be foreign issuers. We understand that some, but not all, of these issuers use local counsel to file the materials. Do you anticipate challenges if we require that materials for the Minimal Connection Exemption be filed on SEDAR?

No – filing on SEDAR for equal dissemination to all stakeholders should be mandatory