

TSX provides guidance regarding the pricing of acquisition financing transactions

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Some market participants may not be aware that the Toronto Stock Exchange (the TSX), for a number of years, has been scrutinizing the practice of launching and announcing both an acquisition and an equity financing at the same time. Issuers, underwriters and their advisors need to be mindful of the TSX's recent Staff Notice on prospectus offerings, private placements and concurrent acquisitions, which provides guidance as to when the TSX will allow a concurrent equity financing by an issuer to be priced prior to the time at which the issuer publicly discloses a material transaction. The issuer and its advisors need to be satisfied that the issuer would not have agreed to the acquisition or other transaction without having a firm commitment for the equity financing at a specific price and offering size.

Background

When a public company in Canada announces a material transaction such as a major business acquisition, it will often simultaneously announce the financing arrangements for the acquisition in the same press release describing the acquisition itself. This is the case even where the acquisition is being partially or fully financed by an equity bought deal or committed private placement entered into at the same time as the announcement of the acquisition.

The TSX has been scrutinizing this practice for some time, and is particularly focused on the implications of pricing the equity financing prior to the time at which the details of the acquisition or other material transaction have been disseminated to the market. As a general matter, the TSX believes it is not appropriate to price an equity offering prior to the public announcement of undisclosed material information, since the market price of the issuer's securities may not accurately reflect the current business and affairs of the issuer.

Where an acquisition is being financed in whole or in part with the proceeds of an equity bought deal or committed private placement, the prevailing practice in Canada has been to enter into the bought deal bid letter or subscription agreement at the time of announcing the acquisition and to disclose both the acquisition and the financing terms, including the offering price, at the same time. If the details of the acquisition constitute undisclosed material information with respect to the issuer, the TSX has historically allowed the issuer to price the financing contemporaneously with the acquisition announcement if the issuer was able to demonstrate that the acquisition would not have been approved by the issuer's board of directors without the agreement for the financing (e.g., a signed bid letter for a bought deal or signed subscription agreements). The TSX refers to this accommodation as the "pricing exception," and views this as an exception to the general rule that prohibits an issuer from pricing an equity financing where there is material information about the issuer that

has not yet been disclosed. In recent years, the TSX has generally required evidence, in the form of an officer's certificate from the issuer, confirming the facts that support reliance on the pricing exception. This requires the issuer and its advisors to be satisfied that the issuer would not have agreed to the acquisition without having a firm commitment for the equity financing at a specific price and offering size – reflecting the fact that the financing commitment was integral to being able to enter into the acquisition agreement.

New TSX guidance

The TSX Staff Notice formalizes the TSX's historic practice of requiring an officer's certificate from the issuer confirming that the issuer would not have entered into the agreement for the acquisition without also having entered into the agreement for the financing. The TSX's form of officer's certificate also requires the officer to certify that the proceeds from the financing are intended to be used primarily in connection with the acquisition.

The new TSX guidance gives two examples where the TSX may have concerns about issuers announcing a material acquisition and financing at the same time and relying on the pricing exception:

- the net proceeds of the financing significantly exceed (e.g., by 30% or more) the cash consideration for the acquisition plus related expenses, or
- the financing provides for significant participation by insiders, such as officers and directors and any significant shareholders above the 10% level.

In either of these circumstances, the TSX may conclude that the dependency of the acquisition on the financing is not sufficiently strong to support the issuer's reliance on the pricing exception, and could require the issuer to reduce the gross proceeds of the offering, price the offering after the acquisition has been disclosed, or obtain shareholder approval of the offering. The TSX has stated that listed issuers unable to provide the required officer's certificate may, in exceptional circumstances, be able to successfully make alternative submissions in support of the use of the pricing exception. In these cases, the issuer and its advisors should discuss any submissions well in advance of the launch of any equity financing.

Conclusion

Equity bought deals and private placement transactions will continue to be a common source of financing in Canada for major acquisitions by TSX-listed issuers. We do not expect the new TSX guidance to result in a major change to the relatively common Canadian practice of announcing an acquisition and a committed and priced equity financing at the same time. However, issuers and their advisors should be more focused on ensuring that the issuer will meet the conditions for relying on the TSX's pricing exception. This requires those involved to be satisfied that the issuer would not have agreed to the acquisition without having a firm commitment for the equity financing at a specific price and offering size, and that the issuer will be able to provide an officer's certificate to that effect. Issuers should also consult with the TSX in advance of launching an equity offering if the net proceeds of the offering would exceed the cash consideration for the acquisition plus related expenditures by 30% or more, or if the financing would involve significant participation by insiders. These considerations will apply whether the issuer is undertaking an offering of straight equity, convertible debentures or subscription receipts.