IN FACT AND IN LAW

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Taking Your Company Public: Sounds Interesting?

By Johanne Duchesne and Josianne Beaudry

Is there a business owner who has never dreamed of taking his or her company public and having its shares listed on a stock exchange? Before embarking on the all-important process of transforming your private company into a public one, we suggest that you take certain steps. Whether you choose to carry out an initial public offering by way of a prospectus or to match your company with a capital pool company, the same steps are recommended in order to enable you to more easily transform your company into a public company by significantly reducing the delays, difficulties and costs for such an operation.

An Updated Business Plan

The preparation of a business plan, including financial forecast in support of the company's growth prospects, is essential. Such a business plan enables the securities dealers who participate in the offering to become more knowledgeable about - and to more adequately assess - your company. This plan is also a key document, which must be filed with the stock exchange in connection with the listing application. Moreover, a good business plan facilitates and speeds up the drafting of the prospectus, thus shortening the time needed for completion of the public offering.

A Solid Management Team

The skills of your senior management team and its knowledge of your company's industry are essential elements when it comes to having your company's securities listed. No longer can a founding shareholder concurrently hold the titles of president, chief executive officer and chief financial officer. He or she must be supported by experienced people of unquestionable integrity. If you have not already done so, you should reorganize your senior management team with a view to splitting up its various functions and hire qualified individuals to perform these newly redefined functions.

An Independent Board of Directors

Both the Toronto Stock Exchange and the TSX Venture Exchange strongly recommend that the board of directors of companies wishing to be listed be composed of a majority of independent directors. In addition to being independent, it is also strongly recommended that some board members be experienced in the workings of a board of a public company and that they be familiar with sound corporate governance practices. You most therefore seek out talented individuals who will complement the expertise of senior management members already who sit on the board.

Audited Financial Statements

The prospectus, information circular or registration statement of a company seeking to go public must contain audited financial statements for each of the company's three most recently completed financial years. A company that has been in existence for less than three years is only required to include its audited financial statements for the financial years completed since its incorporation. These financial statements must be prepared in accordance with Canadian Generally Accepted Accounting Principles. If your company does not have audited financial statements, you will need to take the necessary steps in order to comply with this requirement in due course.

Furthermore, effective March 30, 2004, the financial statements of a public company must now be prepared by an accounting firm that is a member of the *Canadian Public Accountability Board*, which may involve having to replace your auditors in anticipation of the initial public offering.

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Johanne Duchesne holds an MBA in Finance and acts as a special advisor in Securities

A Different Tax Treatment

An initial public offering often has tax consequences, which may not only affect the company itself but also its shareholders and subsidiaries. Proper planning will limit the negative impact of the loss of private company status. For instance, the company's shareholders should probably crystallize the $500,000 capital gains deduction applicable to their shares of the company before it goes public. It would also be profitable to take full advantage of some of the tax accounts of the company and its subsidiaries before the company loses its private company status. However, some tax repercussions cannot be avoided, such as the loss of the favourable tax rates on the revenue of an active business. These losses will need to be calculated in order to advise the company and help its management to make an informed decision.

A Well Chosen Securities Dealer

The choice of a securities dealer is crucial. In addition to establishing the value of the company, the dealer is actively involved in the drafting of the prospectus and organizing promotional tours. The dealer is also responsible for distributing the company's securities.

The following are elements to consider when selecting a dealer:

- its reputation and integrity;
- the size of its distribution network;
- its customer base;
- its partnerships with other securities dealers;
- its team of financial analysts.

Before making a final selection, it is greatly recommended that you meet with several dealers and invite them to submit a proposal to the company. You will then have a better idea of the company's value and of the type of financing that suits it best.

A Stock Option Plan for Employees and Management

One of the benefits of going public is that the company can use stock options as a form of remuneration for its senior officers and key employees. However, specific rules govern the stock option plans of public companies. It will therefore be necessary to either revise the existing plan or establish a new plan in accordance with the rules of securities regulatory authorities in anticipation of the transformation of the company into a public company.

Reorganization of Capital

You will generally need to proceed with a stock split that will provide the company with a capital structure similar to that of other public companies. The shareholders' agreement, if any, will also need to be terminated, as all holders of a given class of securities will henceforth have equivalent rights.

Corporate Governance Practices

Going public brings important changes in the way a company is managed. Once a company has gone public, it will need to show a high level of transparency and accountability will become the guiding principle behind any communication with shareholders. It will therefore be essential that you put in place an infrastructure that enables you to meet these requirements.

In order to succeed, it is typically advisable to designate a person to be in charge of shareholder communications. In addition, an audit committee, composed solely of independent board members, will need to be created (except for companies listed on the TSX Venture Exchange).

Josianne Beaudry is a member
of the Québec Bar and
specializes in Securities Law

Once your company has reached a certain growth threshold, creating the following committees may help you adequately discharge your new responsibilities:

- a nominating committee;
- a management compensation committee;
- a corporate governance committee.

Information Control Systems

Due to the financial reporting requirements applicable to public companies, the company's senior management must implement systems and procedures to guarantee to the public the reliability of financial information disseminated into the market. However, since the *Enron* affair in the United States and the passing of the *Sarbanes-Oxley Act*, such systems and procedures no longer apply solely to financial information.

Canadian public companies are now required to implement controls and procedures that apply to any material information pertaining to the company's business and affairs. Management must therefore ensure that such information is communicated to the chief executive officer and the chief financial officer in a timely manner. In addition, beginning in 2005, the chief executive officer and chief financial officer will be required to perform an annual assessment of the efficiency of these controls and procedures and make public their conclusions in respect of such assessment.

Amendments to the Company's Articles of Incorporation

The company's articles of incorporation will need to be amended to provide for the transformation of the company from a private, or closed, company into a public company. The restrictions pertaining to the distribution of securities to the public, the 50-shareholder limit and the free transfer of shares will therefore have to be eliminated.

Put your Papers in Order

Finally, it is important that all corporate papers, particularly the following, be in order before the securities dealer performs its due diligence review:

- incorporating documents;
- amendments to incorporating documents;
- resolutions of the board of directors;
- material contracts.

It may also be advisable to consider entering into employment contracts with some of the company's key employees, as well as non-disclosure and non-competition agreements, in some cases.

The Role of Legal Advisors

Legal advisors play a dual role:

- they advise you and help you to achieve your objectives; and
- they act as intermediaries between the intervening parties (stock exchange, securities commissions, auditor, transfer agent) to ensure the success of the operation.

For more information on the steps necessary to take your company public and the estimated costs, please do not hesitate to contact a member of the Securities Law group.

Josianne Beaudry
(514) 877-3055
jbeaudry@lavery.qc.ca

Johanne Duchesne
(514) 877-3045
jduchesne@lavery.qc.ca

You can contact any of the following members of the Securities Law group in relation with this bulletin.

At our Montréal Office
Josianne Beaudry
Michel Blouin
René Branchaud
Georges Dubé
Martin Joyal
Isabelle Lamarre
André Laurin
Larry Markowitz
Jean Martel
Michel Servant
Sébastien Vézina

At our Québec City Office
Martin J. Edwards
Olga Farman
Jacques R. Gingras
Claude Lacroix
Jean-Philippe Riverin
Louis Rochette
Claude Thériault

Montréal
Suite 4000
1 Place Ville Marie
Montréal, Quebec
H3B 4M4

Telephone:
(514) 871-1522
Fax:
(514) 871-8977

Québec City
Suite 500
925 chemin Saint-Louis
Québec City, Quebec
G1S 1C1

Telephone:
(418) 688-5000
Fax:
(418) 688-3458

Laval
Suite 500
3080 boul. Le Carrefour
Laval, Quebec
H7T 2R5

Telephone:
(450) 978-8100
Fax:
(450) 978-8111

Ottawa
Suite 1810
360 Albert Street
Ottawa, Ontario
K1R 7X7

Telephone:
(613) 594-4936
Fax:
(613) 594-8783

Web Site
www.laverydebilly.com