



Tech Futures:
August 22, 2003

By [Michael Volker](#)

Capital Formation, Bye Bye BBX - Hello CNQ, Easy Money, Recent Financings, and Updates

This month's column is mainly about accessing capital, some of the new funds and exchanges to help facilitate the raising of money, the rules associated therewith and finally, some recent financing deals.

Capital Formation

Just before the summer "recess", the **BCTIA Capital and Investment Committee** put out its final report of June 30, 2003 on improving access to capital for the BC Technology industry.

Venture capital formation in Canada has grown substantially in the past few years. As **Harry Jaako** pointed out recently in **Business in Vancouver**, approximately \$3.9 billion has been raised each year for the past three years - just over double the annual average for the three years prior - the so-called boom years.

Yet, as BC CEOs lament, and as noted in a recent **Financial Post** article, VC's are behaving more like bankers and Angel investors are behaving more like venture capitalists - taking fewer risks and investing at later stages of development.

Robin Louis of **Ventures West** commented that "we have to make sure that we are creating quality companies and then funding them well." However, to get to an appropriate level of quality, though, means providing early financial support to nascent firms so that they have a shot at becoming VC-fundable.

Indeed, we're very good in B.C. at creating new startups and we rank high in Canada and in the USA in this regard. The question raised posed in the FP article is this: Who's going to fund the next generation of startups?

I was recently asked by a business reporter why I was so bullish on the down-trodden tech sector and asked if technology still figures prominently in Canada's economic future. It got me thinking: if technology (broadly speaking) isn't in our future, what is? Canada's tech sector employs some 600,000 people and generates over \$125 billion a year ranking among natural resources and automobiles on our export list.

Obviously, the VC numbers show that there is faith in the sector's future.

In my previous column I stated that getting companies to the VC-ready stage is a completely different ball game than getting companies launched in the first instance. Although some VCs say that they are early stage or "seed", none actually do this.

Two new funds which *will* do this are the [BC Advantage Fund](#) and [WUTIF](#) - the **Western Universities Technology Innovation Fund**. Both of these are VCCs (Venture Capital Corps) that offer B.C. investors a 30% refundable tax credit and RRSP eligibility. This is the way to get in on the ground floor of the growing B.C. technology sector. These will begin their fund-raising efforts this fall and will appeal primarily to retail investors like you and me. Due to the tax leverage - i.e. almost four to one - that these offer, I'm optimistic that they'll sell fairly well in the coming months.

Between them, they could raise well in excess of \$50 million that will go towards developing the sought-after quality deals.

So the answer to the question as to who's going to fund the next generation of startups is *you and I*.

Bye Bye BBX - Hello CNQ and what's NEX?

For many months I've mentioned the pending formation of **NASDAQ's** new **BBX** stock market for junior companies. Well, it won't happen. NASDAQ's new management, led by President and CEO **Robert Greifeld**, recently concluded a strategic review of its business initiatives and, as a result of that review, has announced that it will focus solely on products and services that contribute to its mission to be the best stock market in the world for investors. As such, NASDAQ will discontinue its efforts to launch the **BBX**.

Here in Canada, the "**CNQ**" - the Canadian Trading and Quotation System started trading in its listed companies last month on July 25, 2003 after receiving recognition from the **Ontario Securities Commission** to operate a quotation and trade reporting system. This new equity market for emerging companies offers lower costs, a streamlined regulatory process and a unique market model that maximizes liquidity by offering the best features of both an auction market and a dealer market.

Meanwhile, the **TSX Venture Exchange** (TSX-V) announced the start of trading on its newest exchange, the "**NEX**" this past Monday. So what's **NEX**? Essentially, it's the leper colony of companies - that's where inactive shell companies will get bumped to if they no longer meet the standards of the **TSX-V**.

NEX, also called the "Inactive Board" will provide an (active?) trading forum in the form of a separate and distinct board of **TSX Venture** companies that have been listed on **TSX Venture** and have been declared inactive, or **CPCs** (Capital Pool Companies) that have failed to complete a Qualifying Transaction in accordance with **TSX Venture** requirements.

Unlike the current practice, **NEX** companies will not face delisting if they fail to reactivate within a prescribed time. They will be designated as such by the addition of an ".H" suffix to their trading symbol.

NEX's real purpose is to clearly separate ventures without an active business from those with active operations, and to provide them with a listing/market alternative with a reduced compliance burden.

At the same time, investors will know that all companies on the **TSX-V** are real, active and alive unlike some of the living dead that trade there now.

CPCs that have not completed a Qualifying Transaction within the prescribed time frame will be eligible to transfer to **NEX** provided that they have received shareholder approval to do so. If a **CPC** has not completed a Qualifying Transaction within the prescribed time, the **CPC** shareholders will have a choice to either delist the **CPC**, cancel the principals' shares and redistribute the remaining cash to shareholders, or cancel the principals' shares and transfer the **CPC** to the **NEX** Board. I'm not sure what the logic is behind getting the principals to cancel their shares - shares that they've paid for. Why the rush to do a **QT** anyway? I can tell you from first hand experience that many **CPCs** I know haven't done **QTs** simply because they couldn't find acceptable deals.

On the plus side, **NEX** does demonstrate the **TSX Group's** (**TSX-X**) commitment to providing a home for the smallest (including inactive shells) to the largest Canadian public firms and between **Toronto Stock Exchange**, **TSX Venture Exchange** and **NEX**, **TSX Group** thus facilitates the raising of capital for companies at every stage of development.

According to **TSX Venture Exchange** Senior Vice-President **Kevan Cowan**, "**NEX** provides a valuable contribution to the process of capital formation for emerging companies. The nature of growth companies and venture funding is that many don't achieve their objectives with their first attempt. **NEX** has been designed as a place with simplified rules where companies can trade while they seek additional funding to pursue their business plans or reinvent themselves."

For more information on **NEX**, see www.tsx.com and click on the **NEX** button on the home page.

Getting back to the new CNQ market, how does it compare with the TSX-V?

The TSX Venture Exchange has evolved a set of rules and regulations that is very complex and expensive to deal with. The costs and time delays associated with getting exchange approval of certain business transactions, not to mention the exchange's ongoing maintenance fees, have made a TSX-V listing more of a burden than a benefit for many companies.

There are well over 1,000 Canadian public companies that do not trade on any stock exchange. They may, at one time, have been listed on the TSX-V or a predecessor exchange, but for various reasons are now not trading and no longer meet the listing requirements of a Canadian exchange. Or, it may be too costly for them to do so.

More importantly, though, there are many startups that might be able to raise capital from many small investors if they can get listed on an exchange such as the CNQ with minimal fuss and bother. Then, if they fail, they can be dissolved rather than preserved as public shells. After all, the main reason for keeping a shell company is the value it carries by having a public listing.

Some of the main benefits of listing on the CNQ, as opposed to the TSX-V, are:

1. Lower Fees- indeed, much lower, perhaps less than half in some cases. The CNQ charges a one-time fee (<\$10K) and a monthly fee whereas the TSX-V has a complex fee schedule that's tied to number of shares and financing activity.
2. Fewer Regulations - CNQ listed companies need to comply with the relevant provisions of the Company Act and/or Securities Act. The CNQ will *not* impose its own layer of additional rules - such as the TSX-V has, which effectively tell a company how to run its business.
3. No Sponsorship Required - Companies can save an estimated \$15,000 to \$50,000 in fees by not having to get under the wing of a broker/dealer.
4. Hybrid Market to Increase Liquidity - One of the interesting features of the CNQ is the fact that it will operate as a hybrid between an auction market and a dealer market. Like the TSX-V, the CNQ will post the highest bid and lowest offer on each stock, plus market depth information. However, issuers will have the option of retaining an IDA member to act as market maker on the stock. If an investor wants to buy or sell shares at a price between the bid and the ask, then the investor's broker will contact the market maker who will have a choice of either making the trade or posting the investor's bid or offer.

Easy Money

It's tough enough to get investors interested in a deal without having to fuss with all the securities rules and regulations that have to be followed by companies accessing capital.

Fortunately for companies, the rules (at least in some jurisdictions) are making life easier. In an attempt to harmonize regulations across the country, securities regulators delivered good news to companies who are looking to raise money when they decided to adopt a new version of what they refer to as "Multilateral Instrument 45-103 Capital Raising Exemptions (MI 45-103)". MI 45-103 means that companies in most Canadian jurisdictions can raise money without having to meet the very onerous and costly prospectus and dealer registration requirements. In other words, there are new exemptions to these requirements.

MI 45-103, which has been adopted in B.C., provides for the following exemptions:

1. Private Issuer Exemption

(Note - regulators and lawyers like to use the term "issuer" instead of "company" to refer to an entity that can issue securities, i.e. shares to investors.)

A "Private Issuer" is a company that is not a reporting issuer, a mutual fund or a non-redeemable

investment fund whose shares are (i) subject to restrictions on transfer that are contained in the issuer's incorporating documents or security holders' agreements, and (ii) are beneficially owned, directly or indirectly, by not more than 50 persons or companies. A Private Issuer can only distribute its shares only to certain types of people including:

- (a) directors, officers, employees, founders or control persons;
- (b) a spouse, parent, grandparent, brother, sister or child of a director, senior officer, founder or control person;
- (c) close personal friends, or close business associates of a director, senior officer, founder or control person;
- (d) current shareholders;
- (e) accredited investors (see below);
- (f) companies of which a majority of the voting securities are beneficially owned by, or a majority of the directors are, persons or companies listed in (a) to (e) above; and
- (g) people that are "not the public";

A close personal friend is an individual who has known the director, senior officer, founder or control person for a sufficient period of time to be in a position to assess the capabilities and trustworthiness of the director, senior officer, founder or control person.

A close business associate is an individual who has had sufficient prior business dealings with the director, senior officer, founder or control person to be in a position to assess the capabilities and trustworthiness of the director, senior officer, founder or control person.

2. Family, Friends and Business Associates Exemption

Any company can use this exemption, even companies that don't have the 50-shareholder limitation of a private issuer. This exemption is similar to the Private Issuer exemption. The purchaser must be either:

- (a) a director, senior officer, or control person;
- (b) a close relative, close personal friend, or a close business associate of a director, senior officer, founder or control person;
- (c) a close relative of the spouse of a founder;
- (d) a company of which a majority of the voting securities are beneficially owned by, or a majority of the directors are, persons or companies listed in (a) to (c); or
- (e) a trust or estate of which all of the beneficiaries or a majority of the trustees are persons or companies listed in (a) to (c).

If a company is relying on either the Private Issuer exemption or the Family, Friends and Business Associates exemption, then it should ensure that each investor completes and signs a subscription agreement that sets out in detail the relationship of the investor to a director, senior officer, founder or control person of the issuer. No commission or finder's fee may be paid to any director, officer, founder or control person in connection with a trade under this exemption.

3. Accredited Investor Exemption

An "Accredited Investor" includes the following:

- a person or company registered under the securities legislation ... as a representative of an adviser or dealer (e.g., a stockbroker);
- an individual who, either alone or jointly with a spouse, beneficially owns financial assets (i.e., cash and securities) having an aggregate realizable value before taxes, but net of any related liabilities, exceeding \$1,000,000;
- an individual whose net income before taxes exceeded \$200,000 in each of the last two years or whose net income before taxes combined with that of a spouse exceeded \$300,000 in each of the last two years and who, in either case, reasonably expects to exceed that net income level in the current year.

If a company is relying on this exemption, then the purchaser's subscription agreement should specifically state how the purchaser meets the definition of an Accredited Investor.

4. Offering Memorandum Exemption

Under this exemption, the company delivers an offering memorandum (drafted in accordance with Form 45-103 F1) to each purchaser, and has each purchaser sign a risk acknowledgement form. If the company is a qualifying issuer, then there is a different format for the offering memorandum. If a material change occurs in the company's affairs prior to closing of the offering, then the company will need to give each purchaser an updated offering memorandum. The purchaser's subscription agreement should include an acknowledgment by the purchaser that he or she has received a copy of the offering memorandum.

Payment for the securities must be held in trust for a two-day "cooling-off period" during which the purchaser has the right to cancel his or her investment. In Alberta, Manitoba, Saskatchewan, Newfoundland & Labrador, P.E.I., N.W.T, and Nunavut, unlike B.C. and Nova Scotia, if an investor wants to subscribe for more than \$10,000 worth of securities, he or she must qualify as an "eligible investor". In Saskatchewan, N.W.T., and Nunavut, no commission or finder's fee may be paid to anyone other than a registered dealer in connection with a trade, under this exemption, to a purchaser in that jurisdiction.

Filing Requirements

If a company has raised funds pursuant to one of the exemptions set out in sections 2, 3, or 4 above, it will need to file with the applicable securities regulatory authorities a report of exempt distribution (Form 45-103F4) and, if applicable, a copy of the offering memorandum, within 10 days after the closing of the offering.

The bottom Line - yes, it is easier - a lot easier now. These four "exemptions" open a lot of doors. For example, by using the offering memo, a company in B.C. can readily sell its shares to almost any willing investor.

Recent Financings

Yes, B.C. firms are raising capital. Here's a sampling of some recent financings:

QLT INC. completed its previously announced offering of US \$172.5 million aggregate principal amount of 3.0% convertible notes due 2023.

AVCORP INDUSTRIES INC. has closed its Private Placement for 15,000,000 units at a price of \$0.30 per unit for gross proceeds of \$4.5 million before expenses and commissions.

FORBES MEDI-TECH announced that Phyto-Source, LP has closed its US\$3 million term loan facility and US\$1.5 million line of credit with Southwest Bank of Texas and has made the US\$3 million advance loan payment to Forbes.

CONTEC INNOVATIONS has completed a third close of its private placement offering of 2,881,800 units at 25 cents per unit for gross proceeds of \$720,450.

WESTPORT INNOVATIONS INC. announced that it has entered into a bought deal financing agreement with a syndicate of investment dealers led by Raymond James Ltd.

SMARTIRE SYSTEMS INC. announced that it has closed two financings representing \$16.7 million.

AZURE DYNAMICS CORPORATION has announced the completion of its previously announced financing of \$2.21 million in secured convertible debentures, of which proceeds \$1.0 million is immediately available to the company.

EXTREME CCTV has closed a previously reported private placement financing of 2,666,700 special warrants

at a price of \$3 per special warrant for gross proceeds of \$8,000,100.

PHOTON CONTROL has completed the third and final closing of the private placement announced June 9, 2003. In this closing, a total of 283,000 units were issued for gross proceeds of \$84,900.

QI SYSTEMS has entered into a non-brokered private placement for gross proceeds of \$250,000 (U.S.), consisting of 1.65 million units at a price of 15 U.S. cents per unit.

STOCKGROUP INFORMATION SYSTEMS has closed its short form offering reported on May 12, having raised a total of \$1,384,836.

INEX PHARMACEUTICALS announced the closing of its offering of 4,600,000 Common Shares at a price of \$5.45 per share, in connection with the previously announced agreement with an underwriting syndicate led by BMO Nesbitt Burns Inc.

INFOWAVE SOFTWARE announced the completion of the second and final tranche of \$1.1 million of its brokered private placement of units. The first tranche was US\$2.8 million.

NXTPHASE CORPORATION announced that it has closed a convertible debt financing, to be issued in 2 tranches in the aggregate amount of US \$7 million, with an option for an additional US \$3 million.

INFORETECH WIRELESS TECHNOLOGY announced that it has reached an agreement to retire \$1.25 million in convertible debt obligations to Augustine Fund, LP.

NEODYM TECHNOLOGIES has arranged a private placement for gross proceeds of \$81,800 in units of the company at a price of 10 cents per unit.

AXONWAVE SOFTWARE INC., formerly **Gavagai Technologies**, an **SFU** spin-off, a provider of content intelligence solutions for unstructured information, announced the completion of a \$(US) 2.3 Million second round of financing.

VRB POWER SYSTEMS INC. announced that it has negotiated, subject to regulatory acceptance, a non-brokered convertible debenture for \$850,000 CAD.

ANGIOTECH PHARMACEUTICALS INC took in \$67.4 million from 102 purchasers in a private placement.

XILLIX TECHNOLOGIES CORP raised \$1 million from 4 investors.

DYNAMOTIVE ENERGY SYSTEMS CORP received \$386K from 16 purchasers exercising warrants.

D-WAVE SYSTEMS INC. raised U\$7.1 million in a venture capital round led by - get this - California based **Draper Fisher Jurveston**, it's first-ever Canadian investment (in its 18 year history). DJF took up \$4.5 million with the rest divided among **GrowthWorks Ltd.**, the **Business Development Bank of Canada** and various local angel investors. D-Wave is generating a bit of a buzz with its work on quantum computing. **Questair Technologies Inc** received \$9.6 million from **Technology Partnerships Canada**.

SMARTIRE SYSTEMS INC raised \$325k from 6 purchasers.

CV TECHNOLOGIES raised \$200K.

PALCAN FUEL CELLS raised \$143K from one investor.

ZOOLINK CORP raised \$88K from 10 purchasers.

WEBTECH WIRELESS got 3 investors to pony up \$41K. Hey -itain't nothing!

Capital Pool Corporation (CPC) Update

In this column, I've kept track of Capital Pool Corporation ("CPC") companies as defined by the **TSX Venture Exchange** (the former CDN) because they may provide funding and management to, and in the process acquire, technology companies. They provide companies with an alternative to traditional venture capital financing. It lets the public investor get into the game

An introductory article explaining CPCs may be found at <http://www.bctechnology.com/statics/mvolker-jun0200.html>.

These CPCs are not as popular as they used to be and their future is somewhat uncertain. Therefore, I'm not going to continue to track them although I'll periodically provide readers with an update.

The most recent update - thanks to **David Ing** of **Pacific International Securities** - can be found by clicking on: [Capital Pool Corporation chart](#).

VEF UPDATES

The [Vancouver Enterprise Forum](#) is taking a break for the summer. The next event will be held late in September.

A complete calendar of local technology events can be found on [T-Net's Events page](#).

Footnotes

If you're an entrepreneur looking for a place to get your company started; there's some great space available at Harbour Centre downtown. The **New Media Innovation Centre** (NewMIC) and **SFU's TIME Centre** have teamed up to provide not only office space but also access to various resources, e.g. tech advisors, access to capital, mentors, etc. Worried about the high cost of being downtown? Well, not to worry - they'll even reduce the fees and take some payment in the form of equity. Check www.sfu.ca/time for contact info.

A reminder: SFU's TIME Centre is open for business - business folks, that is. TIME is an acronym for **Technology, Innovation, Management, and Entrepreneurship**. TIME supports the growth and development of the tech industry in B.C. TIME features a "BusinessCentre" (looks like an airport business lounge) which is open to technology entrepreneurs and business people to use as a drop-in downtown office facility. Need to plug-in? Make some calls? Do some work? Hold a meeting? There are some great facilities for holding your company's AGM. Why hang out at MacDonald's when you can work productively at the TIME Centre? Drop by and check it out! It is located at SFU's downtown campus at 515 West Hastings St.

Michael Volker, a technology entrepreneur, is Director of the University/Industry [Liaison Office](#) at Simon Fraser University, Chair of the B.C. Advanced Systems Institute, Chair of the [Vancouver Angel Network](#) and past Chair of the [Vancouver Enterprise Forum](#). He owns shares in many of the companies he writes about. Copyright, 2003.

[What Do You Think? Talk Back To Mike Volker](#)

Tech Futures is a bi-weekly column that focuses attention on new and emerging BC publicly listed technology companies.

Click for a [Printable Version](#).

Contact: risktaker@volker.org

[Tech Futures Archive](#)

[B.C. High Tech Links](#)
