

The background features a dark red grid pattern on the left and a 3D bar chart on the right. The bar chart has five bars of increasing height, colored in shades of teal and blue. A large white arrow with a black outline points upwards and to the right, following the general trend of the bars. The overall composition is dynamic and suggests growth and progress.

Going Public: Getting Your Company Ready

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Going Public: Getting Your Company Ready

The going public process can be complex and time-consuming, with numerous issues to address within tight time frames. By addressing the matters listed below in advance while the company is still private, considerable effort, expense and time can be saved in the long run.

Prepare a Business Plan

A business plan prepared well in advance of going public can be useful for approaching potential underwriters and obtaining financing. In including a description of the business, an analysis of the company's market, a description of the products, corporate strategy, the management structure, financial information, and a description of the company's financial needs, a business plan can serve as a management tool, as well as constitute the forerunner of parts of the prospectus.

Prepare Audited Financial Statements

A prospectus is generally required to include income statements, statements of changes in equity and cash flow for three years and balance sheets for the previous two years. For financial periods beginning prior to January 1, 2011, these statements may be prepared in accordance with Canadian generally accepted accounting principles. For periods after that, the statements must generally be prepared in accordance with International Financial Reporting Standards. However, exceptions apply in both cases to permit preparation and audit in accordance with standards adopted by certain designated foreign jurisdictions and United States generally accepted accounting principles.

Although there are some limited exceptions from the requirement to provide a full three years of audited historical financial statements, by preparing financial statements that satisfy these requirements in the years preceding a decision to go public, the burden of redoing and obtaining audits at a later date can be avoided.

Auditor oversight

The auditors should preferably be the ones that are used once the company goes public. Under National Instrument 52-108 *Auditor Oversight*, financial statements of public companies can be audited only by a firm that is a participating audit firm and in compliance with any restrictions or sanctions imposed by the Canadian Public Accountability Board (CPAB). A participating firm is a public accounting firm that has entered into a "participation agreement" with the CPAB, under which the audit firm agrees to submit to CPAB oversight, including ongoing inspections.

Develop Appropriate Reporting and Control Systems

The more informal management reporting systems typically used by private companies will generally not be suitable for a public company. Appropriate reporting and control systems and procedures to support the financial and other reporting requirements for a public company should be developed and put into place before the company has gone public. As a public company, the chief executive officer and chief financial officer will be required to sign certificates attesting to the company's annual filings and its reporting and control systems and procedures (as discussed in detail under "Corporate Governance" in Section F – Life as a Canadian Public Company).

Select Advisers

Use of an accounting firm (and an audit partner) experienced in securities offerings facilitates the offering process and may reduce the time spent by lawyers on accounting matters relating to the prospectus. Early involvement of auditors can assist in planning a public offering, including assessment of the advantages and disadvantages of going public and consideration of other sources of financing. The auditors can also assist in developing reporting systems.

The law firm retained will play a major role in the preparation of the prospectus and other aspects of the going public process. Due to the extent of its involvement, a law firm with experience in public offerings and with broad experience in securities practice should be used.

For a private company not known to financial analysts, use of a financial public relations firm may be advantageous in order to establish a corporate image and to assist in preparing for a road show.

Creating a Corporate Image

Consideration should be given to creating a corporate image suitable for a public company that will accurately depict the state of the company's business. This should be done with caution and generally well in advance of going public due to limitations on priming the market in anticipation of a public offering.

Consideration should also be given to possible industry classifications of the company (e.g., according to the dominant types of customers, the technology used, the nature of the products) and the manner in which investors value different industries. Consideration should also be given to preparing a corporate brochure and to including securities analysts and the business press on mailing lists for newsletters. While a private company is generally allowed to keep its affairs confidential, there is no requirement that it do so.

Selecting an Underwriter

The appropriateness and interest of prospective underwriters could be affected by the size of the offering and the national/international/regional scope of the offering, and it may be useful to develop a relationship with one or more investment dealers well before going public, including for consideration of alternative methods of financing.

The following factors should be considered in evaluating the suitability of an underwriter, particularly a lead underwriter, for a particular offering:

- The reputation of the underwriter, particularly where the issuer is unknown, may be significant to potential investors as well as to other investment dealers that might be invited to join an underwriting syndicate or banking group to sell the securities;
- The underwriter must have, or be able to arrange for, adequate distributional capability, both for selling the requisite number of shares and for selling them to a sufficiently broad investor base. The retail or institutional focus of the underwriter should be considered in respect of the company's desired shareholder base;
- The specialization and reputation of the underwriter in a particular industry should be considered;
- The underwriter should have a research department with the capability and likely desire to follow the company after it goes public;
- It may be useful to establish a relationship with an underwriter that would be able to provide the company with further financial advisory services in the future; and
- Contacting other customers of a prospective underwriter might assist in evaluating these factors.

Modifications to Corporate Structure

Rather than taking the whole corporate group public, it may be desirable to take public only certain operating units in the group. This may depend in part on the historical financial performance and growth prospects of the various units, and the view taken by the financial markets of the different industries in which they operate. For this purpose, it may be necessary to reorganize the corporate structure or transfer assets among entities in the corporate group, bearing in mind that the public company should be capable of being a viable entity on its own, without needing to rely extensively on private companies in the corporate group for its operation.

Consideration should be given to the tax and accounting consequences of taking public either a holding company or other unit. If the existing corporate structure of the private company has been developed with a view to minimizing corporate taxes, a corporate restructuring may be necessary. The transfer of assets could potentially require valuations by independent third parties.

Similarly, for tax related reasons, the share capital structure of a private company will often involve complexities unsuitable for a public company. Simplification of the share capital structure to create a single class of common equity is often a requirement of the underwriters. It may be desirable for additional classes of shares to be authorized (e.g., preferred shares), even if there is no intention to issue other classes of shares in the near future.

If the shareholders of the private company historically have taken little or no profits from the company, it could be appropriate for the company to pay them a significant dividend before it goes public, which might be done by incurring a reasonable amount of debt. Further, it will typically be necessary and desirable to eliminate loans between shareholders and the company before a company goes public.

The articles and by-laws of the company should also be reviewed with a view to their suitability for a public company. At a minimum, “private company” restrictions will need to be removed.

Appointment of Independent Directors

A certain number of directors who are independent, namely persons who have no direct or indirect material relationship with the company, will need to be appointed to the board once the company has gone public. Directors’ and officers’ liability insurance will generally also be required.

A uniform corporate governance disclosure rule, National Instrument 58-101 *Disclosure of Corporate Governance Practices* and the associated National Policy 58-201 *Corporate Governance Guidelines* provide guidance on what the securities regulators consider to be optimal standards of corporate governance for publicly listed companies. This National Instrument and National Policy are also discussed in more detail in Section F - Life as a Canadian Public Company. It is generally regarded as good corporate governance to have a majority of directors on the board comprised of independent directors. Audit committees are required, subject to certain exceptions, and nominating and compensation committees are also recommended, to be set up with specified terms of reference and be composed entirely of independent directors. It may also be desirable for a company to adopt a code of business conduct and ethics for its directors, officers and employees.

Preparation of New Contracts

Certain types of contracts may need to be entered into, while other types of contracts may need to be revised, upon going public:

- A company that relies on technological expertise or innovation may require confidentiality and other agreements with certain employees;
- Consideration should be given to entering into employment agreements with particular employees regarding their compensation and related arrangements. Appropriate compensation levels will need to be established for shareholder

managers that previously may have set salary and bonus levels primarily with a view to minimizing the overall tax burden rather than with a view to paying competitive remuneration. Conversely, various “income-splitting” arrangements established by an owner-manager with family members may no longer be appropriate in a public company and may need to be wound up;

- If there will be an ongoing business relationship between the new public company and its related companies, these entities should enter into written contracts. By doing so before the company goes public, the company will have documented its relationship with related parties and thereafter be in a better position to avoid subjecting itself to the valuation and minority approval requirements for material related party transactions that may be applicable to it as a public company under Multilateral Instrument 61-101 *Protection of Minority Security Holders in Special Transactions* (which apply to Ontario and Quebec); and
- Consideration might also be given to revising certain supply, sales or lease agreements, loan agreements, and agreements with or among shareholders to ensure that they are appropriate and workable for a public company. For example, buy-sell arrangements between major shareholders may need to be revised or terminated in order to avoid the possibility of inadvertently triggering the requirement to make a take-over bid to all shareholders. Removal of change of control, termination or approval rights may also be desirable, as well as the insertion of confidentiality provisions or other mechanisms to address material contract disclosure requirements after the IPO.

Establishment of Share Incentive Plans

One of the advantages of going public is the ability to establish stock option and other types of share incentive plans for directors, officers, employees and consultants. These plans may include an option component, a purchase component or a bonus component. Administrative requirements regarding share incentive plans may be facilitated by setting up the plan before a company goes public, being mindful of equity compensation arrangement requirements that may be imposed by the relevant exchange.

About the Firm

When Heward Stikeman and Fraser Elliott first opened the firm's doors in 1952, they were united in their pledge to do things differently to help clients meet their business objectives.

In fact, they made it their mission to deliver only the highest quality counsel as well as the most efficient and innovative services in order to steadily advance client goals.

Stikeman Elliott's leadership, prominence and recognition have continued to grow both in Canada and around the globe. However, we have remained true to our core values.

These values are what guide us every day and they include:

- Partnering with clients – mutual goals ensure mutual success.
- Finding original solutions where others can't – but they must also be grounded in business realities.
- Providing clients with a deep bench of legal expertise – for clear, proactive counsel.
- Remaining passionate about what we do – we relish the process and the performance that results from teamwork.

A commitment to the pursuit of excellence – today, tomorrow and in the decades to come – is what distinguishes Stikeman Elliott when it comes to forging a workable path through complex issues. Our duty and dedication never waver.

This is what makes Stikeman Elliott the firm the world comes to when it counts the most.

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