

Better Disclosure, Lower Costs

A Cost-Benefit Analysis of the
Continuous Market Access System

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October 31, 2002



A NEW WAY TO REGULATE
BRITISH COLUMBIA SECURITIES COMMISSION

About The Author

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Executive Summary

In June 2002 the British Columbia Securities Commission (BCSC) proposed a replacement for the current prospectus regime. The new regime is called Continuous Market Access (CMA). It would improve disclosure by requiring issuers to keep their material information up to date at all times, providing more timely and comprehensive information to investors than under the current system. It would enable issuers to complete an initial public offering (IPO) faster and to go immediately to market without having to prepare a prospectus and have it reviewed by a regulator. The proposal is contained in our June 5, 2002 paper entitled *New Proposals for Securities Regulation*, which is found on our website at bcsc.bc.ca/bcproposals.

We surveyed Canadian companies to find out how much they had spent on their recent capital-raising effort and how much they could expect to save using CMA. This is what we found:

- Issuers would save \$170 million in net present value over five years in reduced prospectus preparation and filing costs.
- Issuers could get to market up to 56% faster, reducing the risk of missing market windows.
- Prospectus costs for issuers listed on the Toronto Stock Exchange (TSX) are directly related to length – each page of additional prospectus disclosure costs a TSX issuer about \$29,000.
- Annual Information Form (AIF) costs would increase about 11%. This cost would be offset by the benefits of CMA if the issuer goes to market just once every 12 to 15 years.
- Issuers spend 87% of their securities law compliance time on areas of regulation that are already uniform across Canada.
- 77% of issuers surveyed support the CMA proposal.

These findings show that CMA would not only benefit investors by improving disclosure, it would also benefit issuers by significantly lowering their capital-raising costs.

The current system puts great emphasis on prospectus disclosure, but in fact most issuers rarely disclose to this standard – on average, issuers on the Toronto Stock Exchange file a prospectus only once every eight years (and issuers on the TSX Venture Exchange only once every 15 years).

CMA would bring the market the benefit of continuous, up-to-date disclosure of all material information about all issuers, all the time. The overall level of disclosure in the market would increase, and would be consistent among all issuers, whether or not they raised capital in a given year.

Methodology

The major challenge for anyone attempting cost-benefit analysis in the area of securities regulation is a lack of data. There is no comprehensive database of compliance costs in the securities industry, although this is now being addressed by research activities underway at the BCSC, the Ontario Securities Commission and elsewhere.

To gather data for our analysis, we developed two separate surveys. One was for issuers that had recently completed an initial public offering. The other was for those that had recently completed subsequent equity or debt offerings. We built a database of responses and added public information to complete our data set.

The survey

The survey asked issuers, among other things:

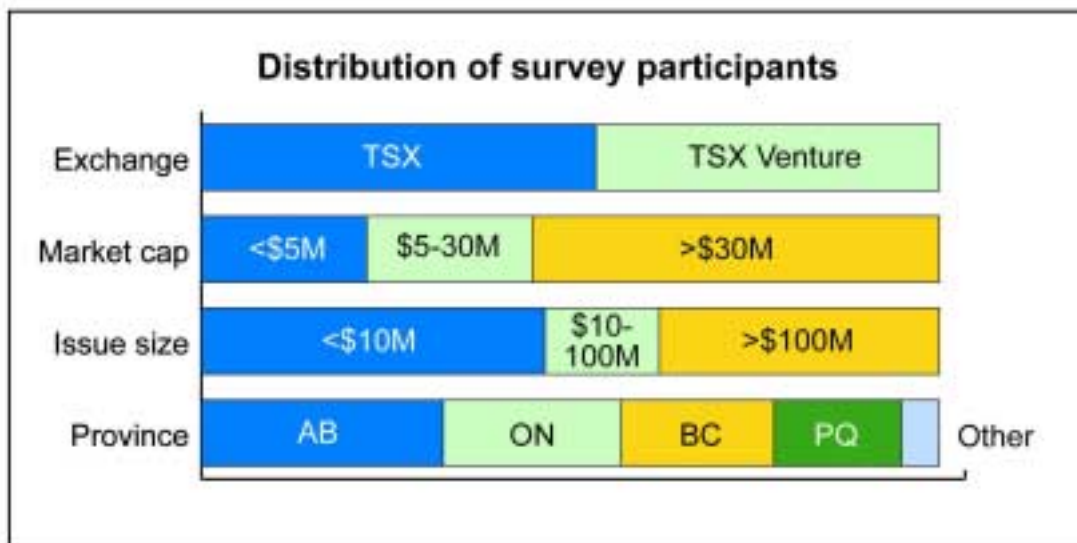
- How much it had cost them under the current system to complete a prospectus and, for subsequent offering filers, an annual information form (AIF). These costs were segmented into 10 categories of internal and external costs¹
- How their costs would change under CMA²
- When they had decided to go to market (which we later relate to the date they received final regulatory approval)
- How much they paid underwriters and their preferences for using underwriters for various capital-raising functions

The invitees

We surveyed 270 issuers that had financed through the public markets between December 2000 and June 2002.³ We intended to invite all issuers in this category to participate in the survey. To find these issuers, we used a database of new issues maintained by a large national news organization. We discovered later that our search on the database was incomplete. However, the 130 TSX issuers we unintentionally omitted had the same market cap distribution as our invitation list as well as a broad industry mix. For these reasons, we believe our sample is representative of the total. If the omission of these issuers has had any effect on our results, it has been to slightly understate the benefits of the CMA proposal.⁴

The respondents

We received 58 completed surveys, a 22% response rate. As shown on the chart on the following page, the respondents were distributed relatively evenly by exchange listing, market capitalization, issue size, and region.



Source: BCSC Public Offering Survey

Because costs were requested on a line-item basis, issuers were able to provide reliable cost estimates, thus minimizing our estimation error. The sampling error is +/- 10% nine times out of ten. We are satisfied that this response rate is sufficient to draw reliable conclusions from the data and that the conclusions drawn are still compelling with this degree of variability.

The analysis

To the survey data supplied by issuers, we added items such as market capitalization, prospectus filing dates, prospectus length, and regulatory filing costs.

A chart detailing sample sizes for each analysis appears in Appendix B.

Our analysis included:

- Calculating percentage responses to direct questions
- Deriving total costs from surveys, using the supplied hourly rates from the survey for internal time assignments and then totaling and averaging responses
- Quantifying cost savings using a model based on survey data and running Monte Carlo simulations (see Appendix A)
- Formulating reasonable assumptions using analyzed data to quantify time savings
- Estimating savings for industry as a whole
- Finding statistical differences between averages and performing regression analysis

The description of our analysis methodology is supplemented by the Notes.

Principal Findings

Finding 1: Under CMA, issuers would save \$170 million in net present value over five years in reduced prospectus preparation and filing costs.

This saving is distributed between issuers doing initial public offerings, who would save \$98 million, and issuers doing subsequent offerings of equity and debt, who would save \$72 million. The findings for IPOs and subsequent offerings are discussed separately below.

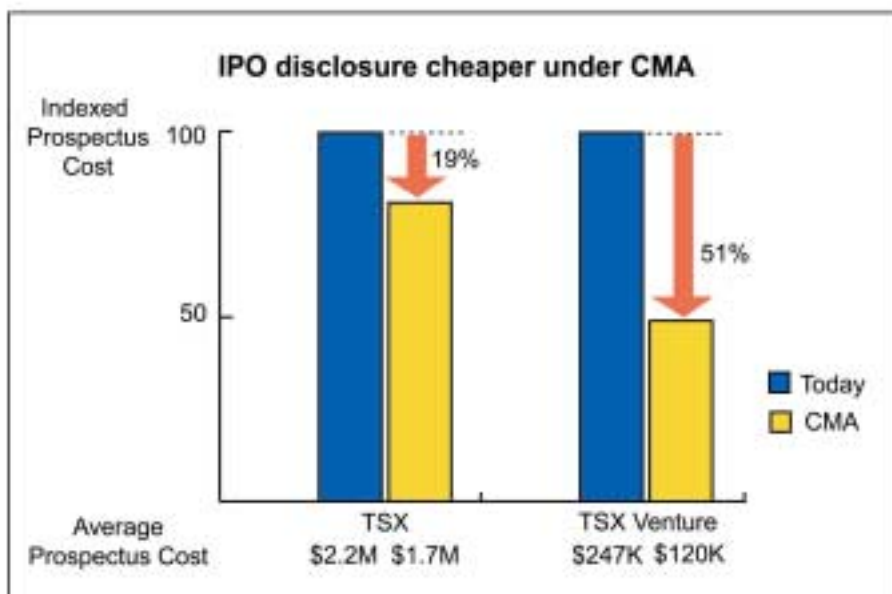
Initial public offerings

Under CMA, the current long form prospectus used for an IPO would be replaced by an initial AIF, a more streamlined disclosure document.

Each issuer was asked to estimate the cost of preparing the prospectus for a specific offer. We asked for a cost breakdown across 10 internal and external categories. This gave us information on today's costs.

The survey informed issuers about the relevant aspects of CMA and then asked them to estimate the differences in time and cost that they would expect to see under that system. This gave us information on costs under the CMA proposals.⁵

We found that for TSX issuers, average IPO disclosure costs would drop 19%, from an average of \$2.2 million under the current system to \$1.7 million under CMA.⁶ TSX Venture issuers would see a drop of 51%, from an average of \$247,000 under the current system to \$120,000 under CMA.⁷



Source: BCSC Public Offering Survey; Analysis

To estimate industry savings from these numbers, we calculated a five-year net present value based on the number of IPOs on the two exchanges in the recent past.⁸ The five-year net present value saving for IPOs totals \$76 million for TSX issuers and \$22 million for TSX Venture issuers.

These savings arise mostly from major differences between the current long form prospectus system and CMA:

- The prospectus form requires detailed disclosure of many items, whether or not they are material to the issuer's circumstances. Under CMA, issuers would have to address the same subject areas, but CMA is less prescriptive, so issuers could concentrate on disclosing information that is material to investors.
- The initial AIF and related guidelines are written in plain language (see discussion under "Other Findings" below).

Under CMA, investors in an IPO would get the same material information about issuers that they get today. But this disclosure would be clearer and easier to understand under CMA because issuers would be able to present their information on the basis of materiality and in plain language. CMA disclosure would not be cluttered by non-material information drafted in "legalese".

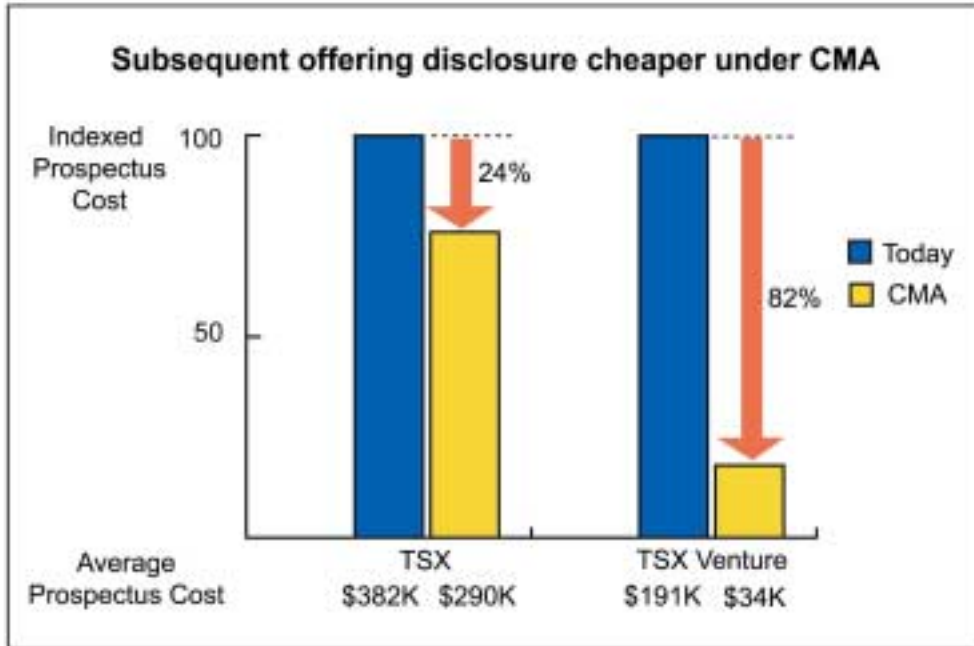
Subsequent offerings

Under CMA, the subsequent offering prospectus would disappear, along with the regulatory vetting period. However, all CMA issuers would be required to file an AIF annually and to comply with enhanced continuous disclosure requirements, similar to those CSA is developing.

Like the survey of IPO issuers, the survey of subsequent offering issuers collected data about internal and external costs. For issuers using a shelf prospectus, the base shelf prospectus was the relevant document. Using this data, we found that average disclosure costs for TSX issuers would drop 24%, from an average of \$382,000 under the current system to \$290,000 under CMA.⁹

Most of the TSX issuers in our sample reported using a short form prospectus under the Prompt Offering Qualification System (POP). This is not surprising since 80% of TSX issuers raising subsequent public capital in the 2001-2002 period were POP issuers. Even though POP issuers already have the least onerous disclosure requirements for subsequent offerings, they still benefit significantly under CMA.

TSX Venture issuers would see a cost saving of 82%, from an average of \$191,000 under the current system to \$34,000 under CMA.¹⁰



Source: BCSC Public Offering Survey; Analysis

Applying the same methodology used for the IPO segment, the five-year net present value saving for subsequent offerings totals \$46 million for TSX issuers and \$26 million for TSX Venture issuers.¹¹

These savings arise principally because issuers will not have to prepare a formal offering document under CMA. Because all material information about the issuer is available at all times, an offering document is not required to disclose new material information. CMA would only require the issuer to file a press release announcing its offering.

We asked issuers what type of disclosure documentation they would choose to prepare under the proposed CMA system. Options included: a press release only; a press release supplemented by a short marketing document summarizing key points from the issuer's continuous disclosure file; and a press release supplemented by a prospectus-style document. The survey participants responded as follows:¹²

- 32% would prepare only a press release
- 54% would prepare a short marketing document
- 14% would prepare a prospectus-style document

Finding 2: The CMA system would cut time to market 16% to 56%.

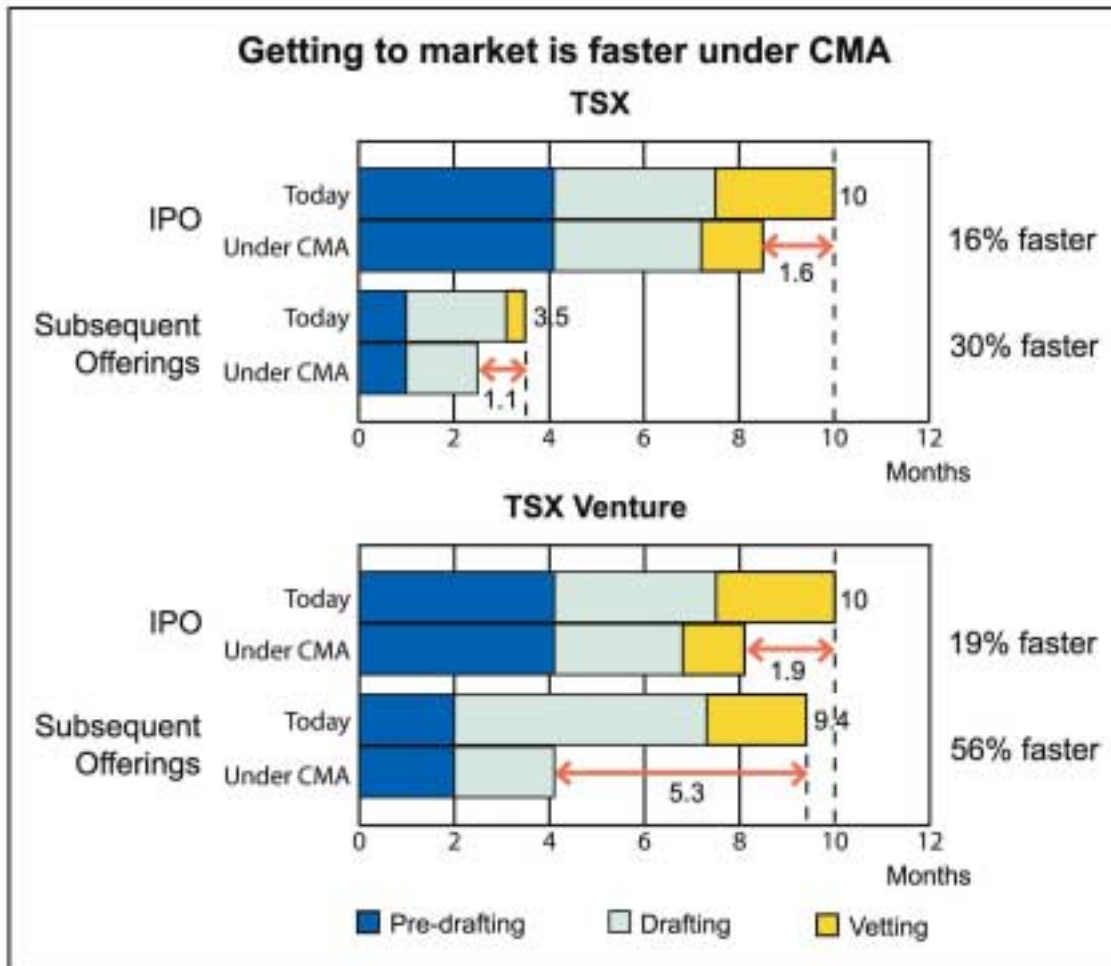
In our survey, we asked issuers to give us two dates; the date they decided to raise capital related to a specific prospectus and the date they began drafting that prospectus. To each response, we added the preliminary prospectus date and the final receipt date. These four dates defined the three phases of capital raising — pre-drafting, drafting, and vetting — and enabled us to calculate average time to market from start to finish.

For IPOs, the average time to market is about 10 months for both TSX and TSX Venture issuers. For subsequent offerings, the average is about 3.5 months for TSX issuers and nine months for TSX Venture issuers.¹³ The average period for TSX issuers is shorter because 90% of the TSX issuers surveyed used a short form prospectus or a pricing supplement.

We used a three-step process to estimate time savings:

1. We assumed that the pre-drafting time would remain unchanged.
2. We used the cost-savings data we had collected as an indicator of time savings. Not all costs saved could be attributed to reduced drafting time, because costs for activities other than prospectus preparation are incurred during the pre-drafting period. We assumed that IPO drafting time under CMA would be 10% shorter than under the current system for TSX issuers and 20% shorter for TSX Venture issuers. (TSX Venture issuers had indicated greater overall cost savings.) For subsequent offerings, we estimated a 30% reduction in drafting time for TSX issuers and a 60% reduction for TSX Venture issuers.
3. We estimated the change in regulatory vetting time. Under CMA, regulators would focus their review of the initial AIF on fundamentals, such as unsuitable directors or officers, significant non-compliance with AIF disclosure requirements, management integrity or competence issues, and public interest concerns, such as the viability or legality of the enterprise. We assumed that the average IPO vetting time would be cut in half under CMA. Vetting would not be required under CMA for subsequent offerings, so we eliminated that time for those issuers.

As shown in the chart on the following page, CMA would shorten the capital raising process between one and five months. All issuers, even those currently using short-form prospectuses, would save time under CMA.



Source: BCSC Public Offering Survey; Analysis

It is difficult to attach a dollar figure to these time savings. What issuers do with the time they save is up to them, but faster is better. Companies may choose to receive their capital 16% to 56% faster and benefit by investing more quickly in productive activities. Or they may choose to focus on running their business longer before initiating the capital raising process.

In some cases, issuers will hit market windows they otherwise would have missed. We asked survey respondents whether they had targeted a market window. If so, we asked whether they made it or missed it. If they missed it, we asked about the consequences in terms of money left on the table or time delayed in raising the capital.

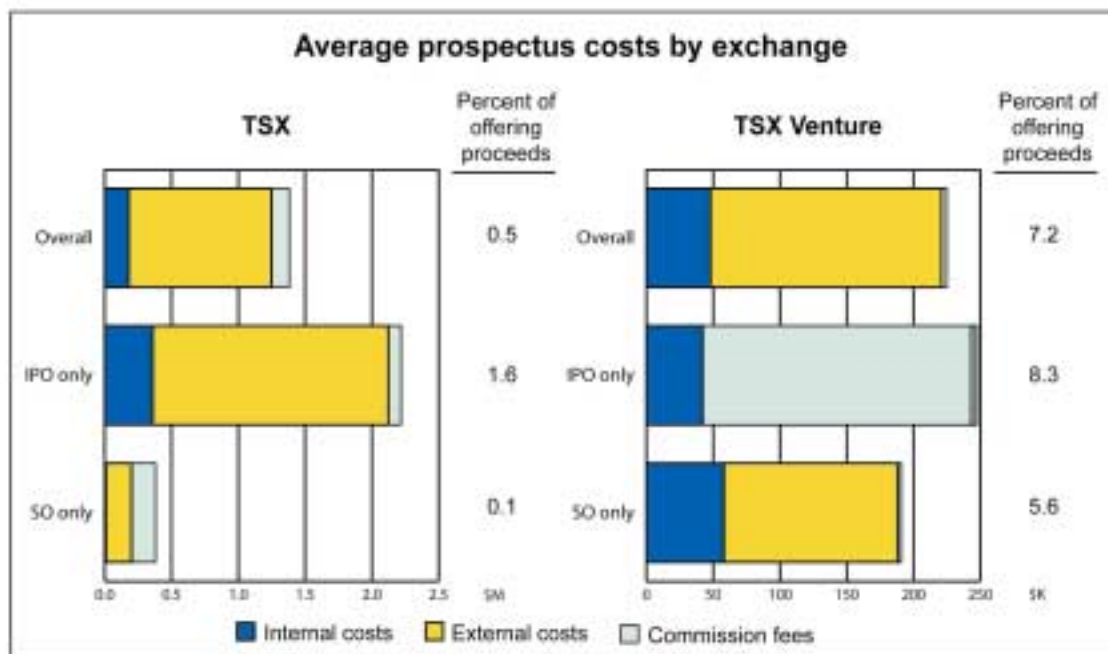
Only IPO respondents reported missing a market window.¹⁴ Of the 20 IPO issuers that had targeted a market window, eight reported missing the window. Four had already submitted a preliminary prospectus when their market window closed. Based on our time-saving estimates, these four would have made their windows under CMA. Three of them reported that they would have raised more money had they made their window.

With only a small data set for these findings, we cannot draw reliable conclusions about the types of offerings that miss market windows, nor about how many issuers could raise more capital if a faster process were available. However, eight such cases in a data set of 58 issuers suggests that the current system is an impediment to capital raising to at least some degree. CMA would eliminate this impediment.

Finding 3: Prospectus costs average \$1.4 million for TSX issuers and \$225,000 for TSX Venture issuers. For TSX issuers, prospectus cost is related to length – each page of additional prospectus disclosure costs a TSX issuer about \$29,000.

The discussion under Finding 1 describes the data we collected from issuers about internal and external prospectus preparation costs.

Prospectus costs averaged \$1.4 million for TSX issuers and \$225,000 for TSX Venture issuers. This table details these costs:



Source: BCSC Public Offering Survey; SEDAR; Analysis
 Note: CPC IPOs and financial special purpose instruments are not targeted in this analysis

Our TSX issuer data showed a strong correlation between prospectus length and cost: each page of a TSX issuer prospectus adds \$29,000 in cost.¹⁵ This has significant cost-benefit implications for rules that mandate specific disclosure. TSX issuers filed 833 prospectuses from 1997-2001. If each of these prospectuses had been one page shorter, industry would have saved a five-year net present value of \$21.5 million.

Finding 4: Under CMA, AIF costs would increase 11%. This cost is offset by CMA benefits even if the issuer goes to market just once every 12 to 15 years.

The AIF plays a pivotal role in the CMA system. It is the document used by an issuer to enter the system and to consolidate and update all its material information each year thereafter.

The AIF under CMA and the current AIF form require comparable disclosure. The proposed CMA AIF also requires disclosure of the following matters not covered by the current AIF:

- Marketing and objectives
- Risk factors
- Arrangements with senior management and others to tie them to the company
- Capital structure
- Escrow arrangements
- Head office address
- Transfer agent and registrar
- Interest of experts in the company
- Notice to investors of their rights to sue for misrepresentations

Despite the additional disclosure categories under the CMA AIF, the proposed form and related instructions are about the same length as the existing AIF.

We asked issuers for current costs to file an AIF, segmented in areas similar to our prospectus cost question. We then asked by what percentage the revised form of AIF would increase or decrease their effort relative to today's AIF completion cost.

Using this data, we estimated the additional AIF costs of CMA compared to the current system. Given a current average AIF cost of \$53,500, we found that the average cost of a CMA AIF would rise 11% to \$59,500.¹⁶

The absolute costs we identified are not entirely reliable as we had only a small number of responses on which to base our conclusions. We believe the cost increase is directionally correct, however, because this small subset of respondents replicated the average prospectus savings found in the larger sample.¹⁷

Issuers that currently file AIFs

To evaluate whether that cost increase was acceptable, we determined how many years would have to pass without an issuer raising capital before the incremental AIF costs outweighed the savings to be enjoyed when it did finally raise capital under CMA. We found that TSX issuers that currently file an AIF would enjoy a net benefit under CMA even if they did not raise capital for 12 years. A TSX Venture issuer could wait 15 years.¹⁸

Issuers that do not currently file AIFs

In a separate data-gathering effort, we found that 1,277 TSX Venture issuers do not file an AIF today (and would not have to under CSA draft National Instrument 51-102, *Continuous Disclosure Obligations*). These issuers would have to file one under CMA.¹⁹

We are unsure what the cost of filing an AIF would be for these issuers but the BCSC has some relevant experience.

When writing our CMA proposal, we retained counsel to write a sample initial AIF. In creating the sample, he also fulfilled the roles that internal management would normally play in the process. The value of his work was \$29,000. Based on our AIF survey data, we know that internal management costs and legal fees together account for about two-thirds of total AIF cost. This suggests that our initial AIF would have cost an issuer about \$44,000. In subsequent years, we would expect this cost to be at least halved. First, initial AIFs include details about the offering that do not apply in AIFs for continuous disclosure. Second, many small issuers have modest operations that do not change much year to year, so each year's AIF would have few changes from the previous year's.²⁰ Third, our cost of \$29,000 included legal time that in a small company would have been absorbed by internal employees, further reducing cost. Taking these AIF costs and assuming that today's cost is zero, CMA is attractive to smaller companies that issue a prospectus at least once every six years.²¹

Increased disclosure is a benefit to the market. The current system puts great emphasis on prospectus disclosure, but in fact most issuers rarely disclose to this standard – on average, issuers on the Toronto Stock Exchange file a prospectus only once every eight years, and issuers on the TSX Venture Exchange only once every 15 years.²²

CMA would bring the market the benefit of continuous, up-to-date disclosure of all material information about all issuers, all the time. The overall level of disclosure in the market would increase, and would be consistent among all issuers, whether or not they raised capital in a given year.

Finding 5: Issuers spend 87% of their time on securities regulation that is already uniform across Canada.

Issuers were asked to comment on whether they spent a lot, some, or little/no effort complying with securities regulations in nine areas.

We found that 87% of issuers' compliance time is spent on areas that are already largely uniform, such as prospectus disclosure and periodic and timely continuous disclosure (continuous disclosure requirements are generally uniform, with more harmonization currently proposed by CSA).²³

This has significant implications for the best way to improve the efficiency and effectiveness of securities regulation in Canada. It suggests that those who look solely to harmonization or national regulation to reduce the regulatory burden may be sorely disappointed if they get their way. If only 13% of regulatory compliance effort is spent on areas that are non-uniform, the efficiencies to be gained merely from harmonization are slim, especially considering that harmonization will not reduce that 13% to zero – the requirements will remain, albeit in a harmonized form.

Finding 6: 77% of issuers support the CMA proposal

At the end of our surveys we asked, “As a whole, would you take or leave the proposals described in this survey?” Of the 53 respondents (81%) who answered this question, 77% voted to take them. We segmented the issuers by type of capital raised, market capitalization, sector, and region to look for a segment that was not supportive. In no segment was the support less than 58%. The segmentation with the highest variation was by province, where support by segment ranged from a high of 89% (Alberta-based issuers) to a low of 58% (Ontario-based issuers).

Other Findings

Finding 7: 74% of issuers would interpret and apply securities rules on their own more frequently if they were written in plain language.

We were interested in whether issuers would self-advise on securities compliance if the rules were easier to understand. We asked, “Of the times over the last year that you needed to know something about securities requirements, what percentage required a call to a securities lawyer or other professional adviser?” 82% said they called a securities lawyer or other professional adviser more than half the time. Asked whether they would be more likely to act on their own understanding if securities law were simpler and written in plain language, 74% said yes.

We believe that there is a lot of room to make disclosure requirements more readable. You can find a sample of this plain language approach by looking at the form of AIF and related Guidelines in our June proposals, *New Proposals for Securities Regulation* (Appendices B and C). If the entire system of regulation were rewritten along the same lines, we believe issuers would be able to navigate the system with confidence and limit professional involvement to complex transactions.

Finding 8: Issuers are inclined to retain underwriters for due diligence and sales functions even if other options were available.

The CMA system proposes that, in addition to underwriters, other appropriate organizations be allowed to fulfill the gatekeeper, due diligence, and pricing functions. This means that non-registrant organizations, such as venture capital companies, law firms, accounting firms, or financial institutions, could perform these functions. A registrant would still be required for distribution of the securities; however, the registrant would not need to act as an underwriter.

We developed the idea of allowing others to perform traditional underwriting functions because junior market issuers told us that the cost of underwriters is often prohibitive relative to the benefits they provide. They told us:

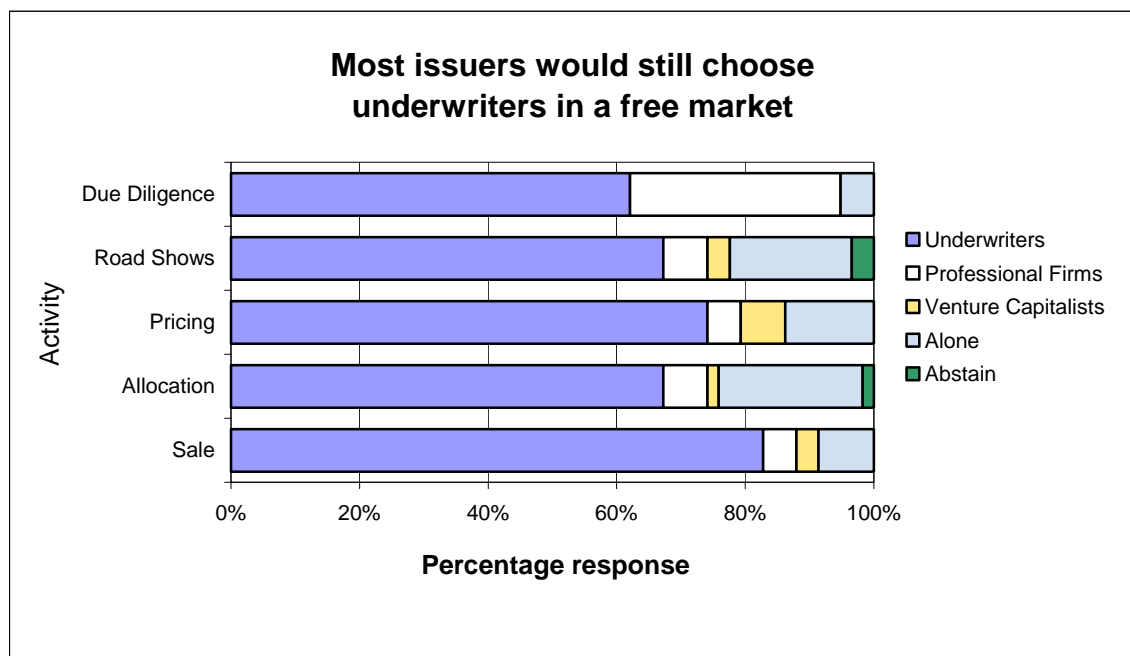
- the cost for an underwriter to conduct due diligence is not commensurate with the benefit it provides (this view is shared by some senior issuers as well)
- worthy issuers may not meet underwriters’ criteria and therefore never get to market
- underwriters typically expect junior issuers to arrange for the distribution of the major portion of the issue
- issuers have limited negotiating power so the negotiating of price is not between equals

To explore these assertions we asked issuers how they would complete five tasks in a competitive market of providers: Would they still have done their offering with an underwriter? Would they have used a venture capitalist instead, or another professional firm? Would they have preferred to do it on their own? The five tasks were:

- 1) Due diligence (“On my own” was not an option for this function)
- 2) Road shows and building the book
- 3) Pricing the offering
- 4) Assigning the initial allocation to investors
- 5) Selling the securities

We found that most issuers are comfortable with the underwriting system: 41% of respondents would have continued to use an underwriter for all five steps of the process. Another 21% said they would still use an underwriter in four of the five situations. That is a solid base of support for the expertise underwriters bring to the capital raising process. Of the remaining 38% of the issuers, 60% said they would perform due diligence with another professional firm. 60% said they would prefer to allocate the initial offering shares alone, and 50% said they would do their own road shows and build their own book.

The overall responses by activity for all 58 respondents are summarized in the following table:



Source: BCSC Public Offering Survey

Note: In our survey, we told issuers that “On my own” was not an option for due diligence, though it was still chosen by a few respondents

The strongest area of support for underwriters was in the sale of the securities, where 83% of all issuers said they would still have used an underwriter.

Those most inclined to seek other options are small-cap issuers. For share distribution, these issuers reflected the rest of the data set, with 62% preferring underwriters for this function. However, for due diligence, 62% preferred working with another professional firm. In doing the road shows, 54% would have done it themselves, compared to 31% that would have stayed with their underwriters.

We will consider this data carefully as we decide whether or not to proceed with the alternate due diligence provider proposal. There are practical issues. For example, under CMA, the sale of securities by a dealer does not carry any due diligence liability if another entity provides the due diligence function. In theory, the dealer's concern would only be the suitability of the investment for their investors. However, dealers may be unwilling to risk their reputations with their retail and institutional clients by distributing an offering in which they have had no role in due diligence and pricing.

The data leads us to question whether the current system is sufficiently "broken" to need fixing. We do not know whether the cost of these services will decrease if others can provide them. We do not know whether others would enter the business.

If we implement this proposal, we will have to design a system and create new rules to deal with the solvency and proficiency of the new service providers. Experience has shown us that these kinds of rules tend to be complex. They also require considerable administrative resources to enforce. We will have to weigh these costs against the benefits of having such a system in place.

Conclusion

The strong interest in our Continuous Market Access proposal indicates that issuers see the promise of savings in this streamlined system. The results of this cost benefit analysis confirm their perception.

Continuous Market Access builds on a familiar tool, the AIF, to improve the quality and timeliness of disclosure. Even a more efficient prospectus-based system would not bring the market the benefit of continuous, up-to-date disclosure of all material information about all issuers, or provide these kinds of savings for issuers.

The acknowledged inefficiencies of the prospectus system have spawned a host of regulatory alternatives and issuers use them whenever the rules say they can. While some of these alternatives have no doubt reduced costs for issuers and saved them time, the benefits identified in this analysis, even for POP issuers, show that much potential remains.

By moving from the current prospectus-based system to CMA, we would gain:

- Continuous, up-to-date disclosure of all material information about all issuers, all the time, whether or not they are raising capital
 - Lower capital raising costs for issuers, which means more of the capital raised can be invested in the issuer's business
 - Time savings for issuers, which means management can be more productive
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APPENDIX A

Monte Carlo Analysis – An Example

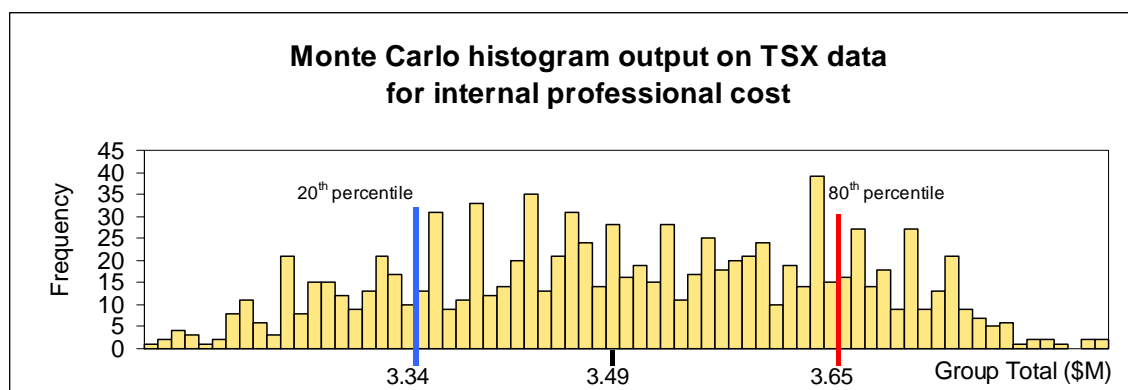
Monte Carlo analysis was used to test the reliability of our findings for IPO and AIF cost changes under CMA. The mean costs listed in our study for IPO costs under our proposals are the means resulting from a Monte Carlo simulation of the model that calculated the cost savings. A Monte Carlo simulation is designed to show how much variation is in “the bottom line” due to uncertainty in critical assumptions of the data model.

This is an example of one data set – internal professional times for TSX respondents – to show how these means were calculated.

Fourteen TSX respondents gave estimates for internal professional expense involved in the prospectus. Their estimates of how that cost would change under CMA are:

CHANGE	NUMBER OF RESPONDENTS
Decrease over 50%	1
Decrease 26% - 50%	4
Decrease 6% - 25%	2
Decrease 5% to increase 5%	4
Increase 6% - 25%	2
Increase over 50%	1

Each cell that held the assumption used to calculate the cost savings or increase was then defined in the model to vary between the minimum and maximum of the responses with an equal probability. So for each of the four respondents who responded “decrease 26% to 50%,” a run of the Monte Carlo simulation randomly picked separate numbers between 26% and 50% and put it in those cells. The simulation records the total expense and does another run. This was repeated 1,000 times. The chart below shows the distribution of the responses and the variability.



Source: BCSC Public Offering Survey; Analysis

As a result, we can see that the mean of the sample for internal professional costs on the TSX is \$3.49 million across the 14 issuers. In 20% of the cases, the cost was under \$3.34 million. In 80% of the cases, the cost was under \$3.65 million. In the report, we used the average savings of 19%, although the data could be legitimately interpreted to suggest savings of anywhere from 16% to 23%.

In this case, the Monte Carlo analysis shows that the savings do not vary much even if respondents meant different things by “decrease (or increase) costs 26%-50%”.

The savings we identified for IPO and AIF costs change only two percentage points to reach their 20th and 80th percentiles. This means the cost savings we state are strongly supported by the survey responses.

Appendix B: Participant subsets for our analyses

Analysis	Number of issuers participating	Reconciliation to 58	Note
Prospectus costs	50	<ul style="list-style-type: none"> No response for prospectus cost (5) No response for initial AIF cost (2) Data outlier for several fields (1) 	The outlier accounted for up to 33% of some total costs across 21 issuers. Because issue size and prospectus length was in line with other issuers, we dropped this point.
AIF costs	12	<ul style="list-style-type: none"> IPO survey did not ask this question (33) Do not file an AIF(5) No response on AIF costs or savings to costs (7) Data outlier for several fields (1) 	
Time required to raise capital	49	<ul style="list-style-type: none"> Raised capital off a shelf prospectus (6) Illogical answers (2) Dataset incomplete (1) 	Illogical answer example: the date on which the issuer decided to raise capital was after the date document drafting began.
Underwriter preferences	58	Not applicable	
Regulatory time	35	<ul style="list-style-type: none"> Subsequent offering flow by-passed this page (17) No assignment of percentage (6) 	
Plain language	40	<ul style="list-style-type: none"> Subsequent offering flow by-passed this page (17) No response (1) 	
Proposal support	53	<ul style="list-style-type: none"> No response (5) 	

Notes

¹ Each issuer estimated hours for:

- Senior management time
- Internal finance time
- Internal legal time
- Internal expert time
- Clerical time

Because, earlier in the survey, we asked each issuer for standard salaries for each of these positions, we were able to attach a cost to the survey responses.

Issuers also provided costs for:

- Auditors
- External legal
- External expert
- Printing and administrative
- Holding board meetings to approve the prospectuses

To complete prospectus costs, we also looked up through SEDAR the filing fees incurred for that prospectus. For issuers who did not file their prospectus with the BCSC, we used the fee schedule from the province of filing (generally these cases were single-province filings).

² To quantify the costs of moving from a long form IPO prospectus to an initial AIF under CMA, and of moving from today's AIF to the proposed AIF under CMA, we asked companies to estimate how their costs would vary relative to today's cost. Issuers were asked to provide this data in ranges (for example, "would external legal costs increase or decrease by +/- 5%, 6%-25%, 26%-50% or 50%+"). To quantify the costs of moving from a prospectus for a subsequent offering to the press release approach, we asked for new data in each of the ten areas. We also asked for an estimate of the time the CMA press release process would take to prepare.

³ We contacted the CEO or CFO of each issuer about the survey. We sent the invitations by e-mail and administered the surveys online. We re-sent the invitation by physical mail, and two weeks later we mailed a postcard reminder. Some issuers requested a paper version of the survey and we supplied them with one. We made follow-up calls to all invitees. The survey ran from the beginning of July through the end of August 2002.

⁴ This is because issuers using the Prompt Offering Qualification System (POP) are over-represented in our respondents. POP issuers account for 90% of our sample, but make up only 80% of all subsequent equity and debt issuers on the TSX. POP issuers would enjoy lower cost savings under CMA than non-POP issuers, so the over-representation of POP issuers in our sample lowers the overall savings identified in our report.

⁵ Because the answer was a range, and not a specific number, we ran Monte Carlo simulations to understand both the mean savings of each group of numbers and the variability in those numbers. The Monte Carlo simulations showed us that the savings variation overall even if respondents mean different things by, for example, "decrease (or

increase) costs 26%-50%". The overall average is within two percentage points of both the 20th and 80th percentile cases. A description of the Monte Carlo simulations is in Appendix A.

⁶ This table shows the breakdown of these cost savings:

COST ITEM	REDUCTION
Internal professional	19%
Internal clerical	8%
External legal	13%
Other external professional	12%
Board meetings	50%
Printing and admin	75%
Regulatory fees	None

The last three categories of costs were reductions we assumed:

- The cost of holding board of directors meetings would drop by 50%. Boards currently have to sign off twice with a prospectus: at the preliminary stage and at the final stage. Under CMA, offerings are a one-stage process.
- Printing costs would be one-quarter of current costs. Issuers would do smaller print runs because distribution of physical copies of the prospectus would not be required under CMA. Printing set-up costs would decrease because most formatting could be done in house and not at the printer. Initial AIFs would likely be significantly shorter than current long form prospectuses (our sample AIF was 32 pages, versus 74 pages from our sample of IPO issuers).
- Regulatory filing fees could change under CMA but we have not assumed that. We have included filing fees to round out the picture by showing that regulatory fees are part of the cost.

⁷ This table shows the breakdown of these cost savings:

COST ITEM	REDUCTION
Internal professional	63%
Internal clerical	60%
External legal	50%
Other external professional	45%
Board meetings	50%
Printing and admin	75%
Regulatory fees	None

⁸ We used five years of actual data for TSX and three years of actual data together with two years of averaged data for TSX Venture. To be conservative, our count excludes special-purpose investment vehicles on TSX (had we included them, the five year net present value would rise from \$76 million to \$116 million). Our count also excludes CPCs on TSX Venture. We used a discount rate of 4.22%, the Government of Canada's 5-year benchmark bond yield on October 10, 2002.

⁹ This table shows the breakdown of these cost savings:

COST ITEM	REDUCTION
Internal professional	39%
Internal clerical	47%
External legal	46%
Other external professional	43%
Board meetings	50%
Printing and admin	75%
Regulatory fees	None

¹⁰ This table shows the breakdown of these cost savings:

COST ITEM	REDUCTION
Internal professional	87%
Internal clerical	89%
External legal	81%
Other external professional	88%
Board meetings	50%
Printing and admin	75%
Regulatory fees	None

¹¹ See note 8.

Whether an offering by a TSX issuer was done using a pricing supplement was not always apparent; the pricing supplement offerings we could identify were not included in this valuation. TSX Venture issuers that were former Capital Pool Companies were included.

¹² Issuers also believed it would take 2.8 weeks, on average, to prepare the level of disclosure they chose.

¹³ These three averages were created by comparing long form and short form offerings and by comparing IPOs and subsequent offerings.

Long form vs. short form

Significant differences show up between segment means when we break out short form issuers from long form issuers, regardless of the type of capital being raised. A short form took 3.7 months while a long form took 9.6 months. This 5.9 month difference is allocated as follows:

- 2.4 months in the pre-drafting period
- 1.5 months of drafting the prospectus
- 2 months of vetting

We compared each subsegment's average and the standard deviation of that average with the same information for the other subsegment. As a result, we concluded that each of these segment averages is statistically distinct.

IPO vs subsequent offerings

The statistical significance of differences in the data for subsequent offerings depends on whether the subsequent offering is for equity or debt. The debt average of 3.6 months is close to what we saw with the short form average, since all but one offer was done off a short form. The long form average splits into a longer period for IPO issuers (10 months) and a shorter period for subsequent equity offers (8 months). While the two-month difference looks substantial, the drafting time difference of one month is not statistically different. However, both the pre-drafting and vetting times are, and were used in our report.

In our report, the IPO times for both exchanges are the same because the means of the two separate averages were not significantly different. The subsequent offering averages were separated because of the short form dominance on TSX.

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40% of IPO issuers who targeted a market window missed it		
Percent of sample who responded:	IPO	Subsequent capital
Did not target a market window	40%	56%
Targeted a window and made it	36%	44%
Targeted a window and missed it	24%	0%
Total	100%	100%

Source: BCSC Public Offering Survey

¹⁵ We ran regressions to see whether we could explain prospectus costs based on other observable variables by issuer, such as offering size, market capitalization, number of past offerings, number of provinces filed in, and prospectus length in pages. We also looked at dummy variables, marking fields for TSX/TSX Venture, debt/equity, IPO/subsequent offers, industry, and long form/short form.

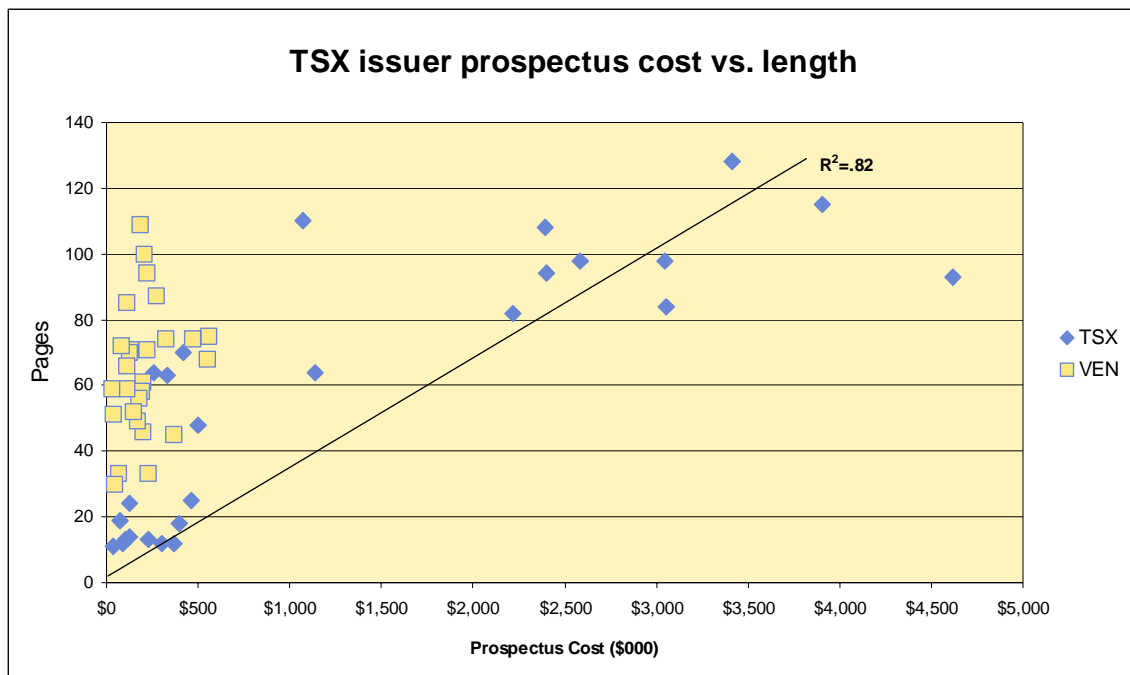
Many of these variables are highly related to one another. For example, TSX issuers tend to be filed in 10 to 13 provinces, while TSX Venture issuers tend to be filed in 2 or 3 provinces. All short form issuers are on TSX. Number of pages is a more detailed cut of a long or short form prospectus dummy.

We ran these regressions against the total cost minus regulatory filing fees. This is because we already know what drives the filing fees: they are fixed, until the offering triggers volume-based tariffs.

The degree to which a regression explains the underlying data can be summarized on a high level by three outputs: the R^2 , F-statistic, and p value. The higher the R^2 , the better the fit between the regression line and the actual data. The F-statistic helps determine how valid the overall regression is, regardless of the coefficients on individual variables. In the regressions we ran, we are generally looking for a number higher than 3. The

p value is a significance level test for individual variables. If the p value is under .1 (or under .05 for the more conservative), we can say that variable is statistically different from zero, and hence does help explain the regression. When the regression cannot tell to what degree two or more variables are singularly responsible for the movement of what it is trying to explain, these variables are collinear. That is why we can say both variables contribute to explaining the regression even when one or both variables has a high p value.

An initial analysis of the entire data set showed that the regression with the best fit involved three variables: the issuer's exchange, whether the prospectus was an IPO, and prospectus length. This regression had an R^2 of 0.82 and a F-statistic of 33.5. Due to multicollinearity between the exchange and IPO variables, their coefficients had a low p value. However, when we charted the prospectus length against its cost, we saw very clearly that the regression for the entire set could not be applied to issuers on TSX Venture. This plot is shown in the chart below. This chart shows that prospectus costs for TSX issuers rise with prospectus length. The same correlation does not apply to prospectus costs for TSX Venture issuers.



Source: Analysis; Issuers' prospectuses

In fact, when we divide the two groups and run the same regression on each part, the two regressions give dramatically different results. For TSX issuers, the R^2 is 0.84 with a F-statistic of 28. However, the IPO dummy does not contribute to the accuracy of the regression. In fact, when it is dropped, the R^2 only falls to 0.82 and the regression has a

F-statistic of 51. This means that an IPO prospectus is not significantly more expensive for TSX issuers by virtue of being the first: all long form prospectuses are expensive and their price is related to their length. The regression result is:

$$\text{Cost of the prospectus} = (\$29,000 \times \text{number of pages}) - \$373,000$$

Because the intercept of \$373,000 has a high p value (and so is not statistically significant), and because adding an IPO dummy to the equation did not result in a better explanation of the data, the best interpretation of the regression is simply that each page of the prospectus adds \$29,000 in cost. As mentioned, the TSX Venture data did not hold this relationship. Neither was there an IPO premium in the TSX Venture data.

¹⁶ This table shows the breakdown of these cost increases:

COST ITEM	INCREASE
Internal professional	15%
Internal clerical	8%
External legal	10%
Other external professional	10%

No special board meetings or printing costs were associated with the AIF as it would be part of a routine year-end process.

Because the issuers gave us ranges of cost savings, we ran Monte Carlo simulations to test the sensitivity of our data to variations in the percentage increase or decrease we applied to each response. This exercise showed very little variation, with an outside low cost estimate of \$58,500 per issuer's AIF and an outside high cost estimate of \$60,400.

¹⁷ The analysis is done off a sample of 12. This sample replicated the average cost savings found in the prospectus analysis (42%). The prospectus cost savings of this smaller subset reflected what we saw in the larger group (25% savings on the TSX, versus 24% in this report, and 78% on the TSX Venture, versus 82% in this report). So the 11% increase in AIF costs comes from a sample of companies who reflected the same scale of change we saw in other costs. However, we still view the results from the AIF analysis as merely directional. We are looking forward to seeing the AIF cost data the OSC is collecting in a survey to refine our analysis.

¹⁸ We built a simple model that showed total dollars spent on both the AIF and prospectus costs over a series of years. One line was today's cost scenario and the other was cost under CMA. We determined how many years a company would need to wait to file a prospectus in the scenario before CMA costs were more expensive than the current costs, on a net present value basis.

¹⁹ Among 2,179 trading TSX Venture issuers we counted 826 that had filed an AIF in the last year and another 76 that would have to file an AIF under the proposed CSA National Instrument. The remaining 1,277 that do not file an AIF today and are not included in the CD rule would have to file one under CMA.

²⁰ Only 6% of the issuers who do not file AIFs have assets or sales over \$10 million.

²¹ We used the model described in note 18 for this analysis. Because the cost for a year with no prospectus is zero for issuers in the current system, the NPV cost for the current system declines over time as the cost for the prospectus is pushed further out.

²² In 2001 there were 1,147 issuers listed on the TSX, excluding investment funds. Of these, only 142 filed a prospectus. That implies that issuers are filing prospectuses every 8 years. Over 5 years, 610 distinct issuers have filed a prospectus, or 53% of the currently-trading issuers. If issuers truly filed every eight years, we would expect 60% to have issued a prospectus in the last five years.

In 2001 there were 2,307 companies trading on the TSX Venture exchange and 153 of them filed a prospectus. This translates into filing a prospectus every 15 years.

²³ Issuers were asked to comment on whether they spent a lot, some, or little/no effort complying with securities regulation in nine areas. We asked issuers to estimate the percent of regulatory effort they spend in the top three of those areas. 85% of issuers' total effort was accounted for by their top three answers. We allocated the remaining 15%, based on the number of companies who rated the task as a lot or some work but did not assign a percentage, and weighted it by the importance other issuers placed on that activity.

Compliance time by regulatory activity		
Regulatory activity	Compliance time (percent)	Substantially uniform?
Preparing prospectuses	39	Yes
Preparing routine continuous disclosure (annual and quarterly requirements)	28	Yes
Preparing material change reports and related press releases	11	Yes
Complying with exchange requirements	5	Yes
Reporting insider trades	4	Yes
Tracking regulatory changes	7	No
Preparing exempt market documents	3	No
Responding to requests by commissions (i.e. continuous disclosure reviews, investigations)	2	No
Applying for exemptions and orders	1	No
	100	

Source: BCSC Public Offering Survey; Analysis