ISEEE SMALL CAPITAL MARKET EXCHANGE DEVELOPMENT TASK FORCE

On-Going Progress Report
ISEEE SPRING 2015 MEETING
Intercontinental Hotel – Downtown Miami
March 22-25, 2015

Executive Summary

Summary Statement

- The focus of the Task Force is the consideration of developing a small capital market exchange in the USA or elsewhere globally for *Small to Medium Sized Enterprises* (SME)
- In doing so, it became apparent that SMEs can be very individualistic in their characteristics as well as their specific capital needs and preferences of ownership/management
- Therefore, to provide a balanced and holistic approach, many of the funding alternatives for SMEs are discussed in this report, in addition to the Task Force's primary focus, development of a small capital market exchange, which for reasons noted in this report, highlights Bermuda's BSX
- These alternatives may provide a SMEs sequential steps to being listed on a traditional national exchange or one or two of the alternatives may totally satisfy the SME's capital requirements, given its uniqueness and ownership/management preferences as well as current global economic and geopolitical conditions
- Often overlooked in both private and public SME funding, is that it must begin with creating market awareness and investor visibility to even create the "possibility" of a liquidity event for the funding and capital formation for startups, organic growth, expansion through acquisition or an exit strategy
- In essence, providing funding for an SME is more than just creating an exchange that accommodates such, mostly an operational and regulatory one, but is centered on the alternative that best meets the funding needs and ownership/management preferences of individual SMEs, the marketing needed to gain public and or institutional awareness and the current economic environment
- The final conclusion is that if an SME's need and goal is to IPO and list on a "traditional exchange" then the SEC currently considering a less regulated stock market on USA stock exchanges for SMEs to be called "Venture Exchanges" but the concept is currently under review and at this stage, only a possibility. A more near term reality may be the Bermuda Exchange (BSX) and the Singapore Exchange (SGX), which are potentially more viable choices in two strategic global locations and with additional enhancement, may become noted as premier global exchanges for SMEs, to include USA SMEs.

Tactical Actions to be considered

- Review and amend or approve the findings of the Task Force beyond that of the Luxemburg meeting, which approved of the findings presented
- Consider the likelihood and viability of the recent SEC consideration of "Venture Exchanges" as compared to off-shore exchanges, such as the BSX and potentially SGX

- Consider providing the BSX with the expertise found in the ISEEE membership as an assist in the full development of a viable exchange for SMEs at the BSX and other exchanges so designated by the ISEEE membership
- Consider the approaches that the ISEEE may educate SMEs on the funding alternatives available, guidelines for consideration and implementation, marketing approaches to create public and institutional awareness and investment desirability leading to a successful funding well before funding is sought and the promotion of one or more functioning SME friendly traditional exchanges, such as the BSX

TASK FORCE HISTORY AND PARTICIPANTS

- The Task Force was established some time ago by the effort of many of the distinguished ISEEE members, with its mission continuing to evolve into maturity and a focus to bring the effort to a conclusion and implementation
- Current task force members include: Steven Shelton (Chairman), David Franasiak (Vice Chairman),Tom Minney, Drasko Veselinovic, Hannes Takacs, Paul Bucha, Greg Wojciechowski, Peter Burnim, Cromwell Coulson, Scott Kaufman and David Scheckel

Small to Medium Sized Companies Financial Alternatives On and Off Exchange:

Brief Background of the Importance of Funding Small to Medium Companies for Growth and Exit Strategies Using On and Off Exchanges

- The U.S. government counts companies with fewer than 500 employees as “small businesses” for this calculation. That includes more than 99 percent of private employers.
- These small businesses make up:
  - 99.7 percent of U.S. employer firms
  - 64 percent of net new private-sector jobs
  - 49.2 percent of private-sector employment
  - 42.9 percent of private-sector payroll
  - 46 percent of private-sector output
  - 43 percent of high-tech employment
  - 98 percent of firms exporting goods, and
  - 33 percent of exporting value
  - (Source: U.S. Census Bureau, SUSB, CPS; International Trade Administration; Bureau of Labor Statistics, BED; Advocacy-funded research, Small Business GDP)
- Additionally, it is estimated that 20 million more business than ever before will come to market due to the baby boomers retiring
- Funding will most likely be needed for those wanting to buy these firms as the owners seek an exit strategy funding
- No funding….no exit strategy….as a result, the business is perhaps worth zero.

Awareness and Marketing Considerations before Funding Alternative Considerations

- Regardless of the size of the SME nor the funding alternatives sought, Market Awareness and Investor Visibility is paramount to a successful funding strategy and full implementation of a properly constructed and researched SME business plan
- If institutional, retail or private investors as well as banks, friends and family are not aware of the SME, its product or service and its financial potential, then funding is greatly impaired, if at all possible
- Most often, IPO road shows are thought to be the only marketing in the funding process
- In reality, this is the last in a very long sequence of SME marketing activities to gain Market Awareness and Investor Visibility, for whatever funding alternative is targeted
- This function should be part of a fully developed SME business plan and may very well need the guidance and assistance of a professional or firm that will facilitate this marketing/public relations/investor relations function

Owner Financed Funding

- Owner financed funding is usually to a relative who they believe they can trust
- Another opportunity is to sell to a retiree who cannot retire, will put in some cash and expect the owner to finance the balance
- However, the business value is usually the owners retirement, so owner financing is an exit strategy of last resort

IN SUMMARY, WHY would an SME consider Owner Financed Funding? Answer: No other alternative except to close the doors and walk away empty handed, especially if there is an unexpected health or family issue!

Credit Cards and Friends and Family

- In the beginning of an SME lifecycle, funding options are very limited
- Friends and Family along with credit cards provide a classic first round of financing

IN SUMMARY: Why would a SME consider credit cards and or friends and family funding? ANSWER: It is the first and sometimes the final round of a funding for a new SME but can provide the runway to other alternatives, such as bank or Angel funding

Banks, Credit Unions

- A common misconception is to just go to a bank to get funding to expand or to fund an exit strategy (buy the business)
- According to one source, banks typically have done only 7% of all commercial and business lending
- In 2008, that dropped to 1%
- Today’s tighter capital requirements make bank lending even more difficult than in the past
- The real news is that the funding is being found somewhere else

- Credit unions on the other hand have a more positive perception when making loans
- The advantage of this debt approach is that one retains control of the company but expansion capability may be limited

IN SUMMARY, Why would an SME consider bank funding, given the hurdles for an approved loan? ANSWER: This may be the owners preferred first round of financing, especially if the entrepreneur has significant assets or friends and family are willing to co-sign, all with the intent to retain permanent control or alternatively, use the funding to develop the SME to positon it for PE or even OTCPINK

<u>Small Business Administration (SBA) Loans</u>

- SBA provides a number of financial assistance programs for small businesses that have been specifically designed to meet key financing needs, including debt financing, surety bonds, and equity financing
- SBA offers Guaranteed Loan Programs (Debt Financing)
- SBA does not make direct loans to small businesses
- Rather, SBA sets the guidelines for loans, which are then made by its partners (lenders, community development organizations, and micro-lending institutions)
- The SBA guarantees that these loans will be repaid, thus eliminating some of the risk to the lending partners
- So when a business applies for an SBA loan, it is actually applying for a commercial loan, structured according to SBA requirements with an SBA guaranty
- SBA-guaranteed loans may not be made to a small business if the borrower has access to other financing on reasonable terms
- However, it is common for all of the borrowers assets to be tied up, including ones home

IN SUMMARY, Why would a SME consider an SBA loan? ANSWER: Friends and family and credit cards may not be sufficient or even available. Thus the only way to get initial funding or more funding and retain control is an SBA loan; however, a major disadvantage is such a loan may tie up all assets

<u>The European Investment Bank (EIB)</u>

- EU's long-term lending AAA rated bank set up in 1958 by the Treaty of Rome, consisting of 28 EU member states
- Objective is to provide finance and expertise for sound and sustainable investment projects in support of EU policy objectives and may provide such for SMEs around the world
- Lending from ECU was 10bn in 1988, annual lending neared EUR 45bn in the mid-2000s before jumping to EUR 79bn in 2009 as a temporary response to the crisis; it was EUR 71.7bn in 2013 and EUR 77bn in 2014 with a goal of EUR 180 billion of additional investment across Europe during March 2015
- Capital increase in 2012 (by EUR 10bn) was for reinforcing the EIB **<u>countercyclical</u>** role in times of crisis
- Single largest policy priority of the EIB is support of SMEs as evidenced by providing EUR 18.5bn to SMEs in the EU and CPCs in 2013
- Main funding Product of the EIB aims at improving and enhancing access to finance for SMEs

- Standardized product reaches a very large and diversified number of SME's via over 700 financial intermediaries (e.g. commercial banks, leasing companies, public promotional institutions, etc.)
- EIB has involvement in the business development cycle to include early seed stage, venture capital, expansion/development capital and mezzanine financing with the ultimate goal public markets as the primary exit strategy
- In essence, the complex EIB is the European Union's bank and the only bank owned by and representing the interests of the European Union Member States which work closely with other EU institutions to implement EU policy. EIB is the largest multilateral borrower and lender by volume, providing finance and expertise for sound and sustainable investment projects which contribute to furthering EU policy objectives. More than 90% of their activity is focused on Europe but they also support the EU's external and development policies.

Why would a SME consider the EIB? Answer: If a firm (typically in EU Zone) has a project that is closely aligned with EIB's counter-economic cycle role which is to invest in innovation and skills as well as to provide access to finance for SMEs which support climate action and strategic infrastructure, then firms may receive lending (guarantees, microfinance, equity investing and so on), blending of other sources of funding and advisory regarding administration and project management…which tends to lead to a public offering exit strategy

<u>Equity-Based Crowdfunding</u>

- If we realize that today was yesterday's future, the evolving state of crowdfunding becomes more probable as a SME funding alternative
- Crowdfunding has earmarks of a concept that may radically change funding in the future assuming it continues on the path to maturity and acceptance
- It is but an extension of that time when the internet was AOL and dial ups were novel but now the internet based companies are competing with brick and mortar worldwide firms with the attributes of immediacy, transparency, mobility, low overhead and much more
- It is no longer about non-for-profits or just a site but it's about the platforms that are being created globally and therefore opening up funding from global sources
- Most germane crowdfunding offering for this task force is Equity-based crowdfunding: the backer receives unlisted shares of a company, usually in its early stages, in exchange for the money pledged
- The company's success is determined by how successfully it can demonstrate its **viability and visibility**
- Equity-based crowdfunding is the collective effort of individuals to support efforts initiated by other people or organizations through the provision of finance in the form of equity
- In the United States, legislation that is mentioned in the 2012 JOBS Act will allow for a wider pool of small investors with fewer restrictions, following the implementation of the Act

IN SUMMARY, Why would a company consider Crowdfunding? Answer: While it provides a low cost means to raise capital and may have great potential in the future, however, the amount able to be raised in the USA is only $1mm per deal. There are unanswered legal issues and the SEC has yet to clarify the rules.

Credit-based Crowdfunding known as Shadow Banking

- In the U.S., credit-based crowdfunding from non-banks became more prominent as a form of crowdfunding in 2012, with the launch of the Lending Club, which had advanced more than US $500 million in loans via its website by April 2012
- Prospective borrowers of the Lending Club first submit their requirements and are then matched with pools of investors who are willing to accept the credit terms
- Platforms such as the Lending Club gained popularity, as banks increased interest rates or reduced their level of lending activity
- Another credit based platform, Prosper.com, was established in 2006 and had funded nearly $325 million in personal loans by April 2012

IN SUMMARY, Why would a company consider Credit Crowdfunding? Answer: For the same reasons as equity based crowed funding, however, there are fewer legal hurdles as opposed to equity crowdfunding

Private Equity (PE) Types or Stages

- PE is an alternative asset class that consists of equity securities and debt in operating companies that are not publically traded on an exchange
- PE investments tend to be made by private equity firms, venture capital firms and angel investors
- Each of these have their own set of goals, preferences and investment strategies
- However, all provide working capital to a target company to nurture expansion, new-product development or restructuring of the company's operations, management or ownership
- Explanations of these stages and investing PE firms are noted below

Micro-Cap:

- Deals are under $5 million dollars but typically under $2 million dollars
- Requires a business broker or private equity banker who specializes in these small deals
- Special assistance is needed for valuation, pricing, deal structuring, marketing and capital sourcing

Angels:

- Defined as a private investor or group of private investors who typically provides capital at high rates/return for an early stage or start up, usually in exchange for ownership equity
- The arrangements are less formal and less involved than most PE deals, especially venture capital firms
- As many Angels are business experienced, an advisory role is quite common and may be very beneficial to the small company
- It is common for an Angel investment to be made as a second round, after the first round of friends and family but before Venture capitalists
- Many Angels, well networked, look for an agreed to exit strategy, such as a mandatory buyout

Venture Capital:

- These funds provide equity capital to very select start-ups and companies in the early stages of growth
- These venture companies tend to have a specific focus such as technology, healthcare or green technologies
- These companies tend to exhibit high levels of growth, with potential to become profitable businesses
- The immaturity of these businesses means that some will inevitably fail
- However, within a successful capital fund, any failures will typically be counterbalanced by a number of extremely profitable investments
- Often the business may have to agree to one or all of following: give up a large percentage of business profits, a cap on the entrepreneurs salary, more than 50% ownership in the company, seat(s) on the board of directors, venture capital personnel on site management/business advice and an agreed to exit strategy
- The deals may be structured in many ways to include outright ownership interest, convertible preferred stock, debt or debt and equity combination

Growth Capital:

- These funds provide expansion capital to enable a company to scale a business
- Investments tend to be made after the early stages of a company's life
- Returns are largely dependent upon cash flow growth
- The negotiated structure can result in the PE firm owning more than 50% along with board membership and management input

Buyout:

- These funds provide equity capital to mature firms in need of capital or ownership transition.
- Transactions tend to have a layer of debt in their financing
- Small and mid-sized buyout transactions tend to have lower proportions of debt in their capital structure relative to their large and mega-sized counterparts
- This approach gained great popularity in the leveraged buy-out era

Special Situations:

- These funds tend to invest in mezzanine or mid-layer debt capital, which provides more protection than equity financing in the event of default
- These funds can aim to achieve equity-like returns via the use of warrants and equity-like features
- Mezzanine debt tends to exhibit lower risk and return features than other, purely equity based, private equity stages

- The term “special situations” also includes distressed debt and funds specializing in energy and turnaround investments

Generalists:

- These funds invest in a variety of different stages

IN SUMMARY: Why do firms use private equity/ Venture funding? ANSWER: The benefit of raising capital, having access to a network of experts and veteran funders of smaller firms. The downside is the loss of some or most control, and operational flexibility. The company’s path to an IPO, if contemplated, will be guided by the PE/ Venture equity investors

<u>OTC Markets</u>

OTC Markets tend to be a precursor or alternative to an accelerated IPO, the “Slow PO”:

- **OTC Markets is an Alternative Trading System** (**ATS**) which is a US regulatory term for a non-exchange trading venue that matches buyers and sellers to find counterparties for transactions
- **Similar to the ATS, the Multilateral Trading Facility** (**MTF**) is an European regulatory term for a non-exchange electronic financial trading venue which was introduced by the Markets in Financial Instruments Directive (MiFID) and intended to be an alternative to traditional exchanges
- USA’s Alternative trading systems (ATS) are typically regulated as broker-dealers rather than as securities exchanges
- For regulatory purposes, an alternative trading system is an organization or system that provides or maintains a market place or facilities for bringing together purchasers and sellers of securities, but does not set rules for subscribers (other than rules for the conduct of subscribers trading on the system)
- OTC markets provides management with more resources to focus on growing the business rather than meeting externally-imposed financial targets and time pressures of a traditional IPO
- Builds investor confidence in the quality of the company’s management and financials as the market in its shares expand
- Enables companies to grow liquidity organically through a slower entry to the public markets
- Allows companies to choose the market visibility and reporting status that best fits their needs whether SEC-reporting or Alternative Reporting Standards
- Ability to list off exchange at a much lower expense than the traditional national exchange IPO
- A Slow PO enables companies to enter public markets by making previously restricted shares available for public trading: Potential to raise capital in private or restricted offerings; makes shares tradable after registration or seasoning; and enables broker-dealers to quote shares on OTC Link ATS
- OTC Markets provide many non-traditional off exchange alternatives to meet the specific needs of public and private enterprises seeking listing as described below

OTCQX:

- A recognized marketplace with qualified companies world wide
- Designed for investor-focused companies that meet high financial standards, are current in their disclosure, and receive third party advice
- The companies found on OTCQX are distinguished by the excellence of their operations and diligence with which they convey their qualifications
- An example of listed companies include: Roche Holding Ltd, Volkswagen AG, AXA, Allianz SE, BNP Paribas and others for a total of 361
- Select attributes: $1.7 Trillion in market Capitalization, $29.5 Billion in annual dollar volume and $78 Million in average annual volume security
- Investors can see prices and access market data: OTCM sets the best price standard by broadly distributing market data through multiple channels, including Bloomberg, Thomson Reuters, and other leading market data distributors
- Investors can access company information: OTCM's suite of Corporate Services empowers public companies and their advisors to improve visibility and availability of information
- Investors can trade through the broker of their choice**:** OTCM's technology enables investors to buy and sell securities through the institutional, retail, or online broker-dealer of their choice, making the trading experience nearly identical to that of trading NYSE or NASDAQ securities

OTCQB:

- A Venture Stage Marketplace for early and developing U.S. and international companies
- Companies are required to meet eligibility standards aimed at improving the information available to investors
- OTCQB will include Real-Time Level 2 quotes and the OTC Disclosure & News Service to help companies improve the information experience for their investors
- To be eligible for OTQBC, U.S. and international companies must be current in their reporting, meet a minimum bid test of $0.01, and undergo a new annual verification and management certification process
- OTCQB also has initial and ongoing requirements for SEC reporting companies, Bank reporting companies, and International reporting companies
- International Reporting companies listed on a Qualified Foreign Stock Exchange are now eligible for OTCQB
- Banks that do not file disclosures on EDGAR will be required to post their regulatory filings on otcmarkets.com
- Securities of companies that do not either meet the OTCQB standards or qualify for OTCQX will likely continue to be traded by broker-dealers on OTC Pink and continue to provide additional information on officers, directors, and controlling shareholders
- Included in the 2,054 Companies that list here are: Anheuser-Busch Inbev Ord, Ameren Illinois, Alabama Power, AXIM Biotechnologies and Bank First National Corp WI

OTCPINK:

- Is an Open Marketplace with Variable Reporting Companies
- The OTC Pink® marketplace offers trading in a wide spectrum of equity securities through any broker
- This marketplace is for all types of companies that are there by reasons of default, distress or design, which is why they are further segmented based on the level of information that they provide
- If a company does not provide high quality information, investors are warned to be extra careful and cautious
- Investors are strongly advised to thoroughly and carefully research companies before making any investment decisions
- OTC Pink provides a base level of trading efficiency, electronic trading (through institutional, retail and online brokers) and transparent prices
- Classification of companies is based on the variable levels of disclosure and information availability. Provides access to all types of U.S. and global companies (including ADRs, penny stocks, shells, bankruptcies, and minimally engaged companies)
- Because companies on OTC Pink are variable in their reporting, OTC Markets Group further segments them based on the quantity and quality of information they provide to investors: Current Information, Limited Information, No Information, Caveat Emptor
- Included in the 7,051 companies listed are: Aberdeen Asset Management ADR, ACCOR SA, and Air Canada Inc

Other OTC or Grey Market:

- "Other OTC" or "Grey Market" is a security that is not currently traded on the OTCQX, OTCQB or OTC Pink marketplaces. Broker-dealers are not willing or able to publicly quote these OTC securities because of a lack of investor interest, company information availability or regulatory compliance.
- Companies in this segment total 8,618

IN SUMMARY: Why would a firm choose to be a part of OTC MARKETS? ANSWER: Many large European firms use OTC MARKETS as opposed to an exchange in the USA to lower their cost of complying with Sarbanes-Oxley (SOX) and exchange listing requirements. Small firms, especially in the USA, use it as a bridge towards listing on an exchange. Others never get past the OTCMARKETS "listing" as they do not want to nor perhaps need to, as they have met their firm's specific and unique quantitative and qualitative objectives and goals.

Exchange Initial Public Offering (IPO) – the primary focus of the Task Force is the development of small capital exchange

- An initial public offering (IPO), also known as a stock market launch, is when shares of a company become available for the public to buy – converting a private company into a public company
- Companies use IPOs as a means of raising capital

- After going public, shares of a company are traded in the financial marketplace
- Most IPOs require an investment bank to act as the underwriter. The underwriter helps assess the value of shares and establishes an initial sales price

<u>**Global Exchange IPO Trends Year ending 2014 – Ernst & Young 2014 4th Quarter**</u>

Global Exchange IPO statistics in US Dollars:

- "Globally, 2014 was a very strong year with IPOs outperforming global indices by around 12.3% on average; it was a good year but not an EPIC year", Ernst & Young 2015
- 1,206 deals globally, a 35% increase over 2013
- $256.5bn in capital raised, a 50% increase over 2013
- PE and VC accounted for 27% of global IPOs, 323 deals but 48% by proceeds
- Leaders: Healthcare 193 deals for $21.8bn, Technology 167 deals for $50.2bn, Industrials 142 deals for $19.9bn
- 161 deals withdrawn or postponed, compared to 121 in 2013
- 87% of exchange IPOs priced within or above expectations
- Top Exchanges: NYSE 116 deals for $73.4bn, NKEx -87 deals for $30bn, NASDAQ 173 deals for $21.7bn, LSE 40 deals at $19.4bn, ASX 75 deals at $16bn and Euronext 26 deals at $12.4bn
- Deal volume by country: USA 222, China 206, UK 92, Australia 68 and India 44
- Global funds raised on exchanges: USA 37%, Asia Pacific 32%, Europe 24%
- Cross border listings were 11% of global IPOs, compared to 9% in 2013
- Rapid Growth markets represented 47% of global IPO volume as compared to 53% developed markets

USA Exchange IPO Statistics:

- 288 deals, 27% more than 2013
- $95bn in capital raised, 54% increase from 2013
- PE and VC accounted for 63% of deals for 181 deals and 72% of proceeds for $68.2bn
- Leading sectors; Healthcare 111 deals for $9.9bn, Technology 47 deals for $36bn and Financials 29 deals for $15.7bn
- IPO price: 19.3% first average return, 27.8% increase in offer price vs 3 December 2014, $390m post IPO market cap
- 2014 deals: NYSE 116 deals for $73.4bn, NASDAQ 172 deals for $21.7bn
- 2013 deals: NYSE 116 deals for $45.8bn, NASDAQ 109 deals for $15.8bn
- Cross Border Activity to USA; China 16 deals for $29.4bn, Europe 26 deals for $6.8bn, Israel 12 deals for $2bn and another 8 countries with 13 deals for $2.5bn
- Rationale for 2014 strength: cheap money, Quantitative Easing (liquidity), few alternative to invest and need to exit for deals done in 2006-2007 at high valuations
- Outlook for 2015: concerns regarding rising interest rates, abating USA QE and increasing global economic uncertainty; 2014 proceeds may be invested in USA or global equity markets

Some of the steps toward an IPO are:

- Develop an impressive management and professional team
- Grow the company's business with an eye to the public marketplace
- Obtain audited or auditable financial statements using IPO-acceptable accounting principles
- Clean up the company's act
- Establish antitakeover defenses
- Develop good corporate governance
- Create insider bail-out opportunities and take advantage of IPO windows
- Hire an investment bank and security law firm to assist in the process to include establish value, set price, roadshow management, put together a selling syndicate, insure after-market support and more

The advantages of going public on an exchange:

- Cheaper access to capital
- Increased exposure
- Diversifying equity base
- Ability to retain better management
- More financing opportunities
- Facilitating acquisitions

Disadvantages of going public on an exchange:

- It is expensive, especially on US exchanges
- A company is required to disclose all its financial information
- Ongoing costly and time consuming state and federal regulations to be complied with to include "SOX"
- The risk that funding targets will not be met
- Loss of control
- Potential shareholder activism

IPOs for SMEs on USA and other world exchanges

- The seminal ISEEE report, *"Opening the World's Equity Markets to Small, Medium Size Companies"* is most definitive
- For those SMEs opting to raise capital on an exchange, a SME's unique situation, characteristics and requirements have been neglected, thus raising capital has been dampened

- Changes are needed to lower disclosure requirements yet keep markets regulated and fair
- The report proposed an exchange carve out framework especially formulated for SMEs
- However, given the regulatory history and economic climate, especially in the USA, such an innovative concept has not been acceptable until recent SEC consideration of a “Venture Exchange” as outlined in following commentary
- Given the increased need for funding and capital raising in up and down markets, as noted in prior sections of this report, a potentially more likely and timely approach is to locate a situs and an exchange that would welcome and foster SME capital raising for those seeking a traditional exchange IPO and listing

<u>SEC Considering Less-Regulated Stock Markets for Small Companies – A Recent Development</u>

- The USA media has reported that the U.S. Securities and Exchange Commission (SEC) is reviewing whether to allow USA stock exchanges to start less-regulated markets that will make it easier for small companies to raise money
- The SEC calls this less regulated market, “Venture Exchanges”, a possible boost to investors’ interest in stocks with low market values, which tend to trade less frequently than other equities and attract less interest from market makers
- In essence, the SEC is attempting to discern if such an effort would improve or deepen the liquidity of the securities of small companies
- The SEC has stated it’s too early to tell what exactly they will do, if anything, but indicate they are very seriously taking a deep look at such
- As described, “Venture Exchanges” could offer incentives for small companies to go public, such as lighter disclosure requirements, if so allowed by the SEC
- Additionally, regulators may have to exempt “Venture Exchanges” from some of the agency’s rules, including a mandate that trades occur at the best price available on ANY public market
- A senior SEC official has indicated it’s too early to say how the SEC will move forward or when
- If the SEC moves ahead with “Venture Exchanges” on USA stock exchanges, will they be comparable to an ATS, such as OTC Markets, which is less regulated, easier to enter, and a less complex environment for venture markets, thus lowering costs for issuers and enhancing innovation for the differing types of companies and their lifecycle position.

<u>IPO Alternative by listing on an off-shore Exchange, such as Bermuda (BSX) and Singapore (SGX)</u>

In example: Current listing environment and requirements for IPO/Listing on the BSX for a SME:

- New company or established company can list, minimum market capitalization size $500,000.
- Trading restricted to “Qualified Investors” OR general public trading both possible
- BSX approved Listing Sponsor, prospects, and complete listing application required
- Very commercial and responsive listing process, short time to market

Future BSX plans and potential enhancement for SMEs IPO/listing on BSX:

- Linkages to international settlement and security services (i.e. Euroclear)
- Expansion of trading member/brokerage network
- Expansion of BSX brokerage analysis, coverage and support of listed SME securities
- Ensuring the BSX listing regulatory environment matches and supports SME companies and the risk tolerance of their investors

Steps to be taken for a SME to IPO/list on the BSX:

- Appoint BSX approved Listing Sponsor and if needed, other corporate financial or legal advisors
- Develop a prospectus (see BSX Listing Regulations for content requirements) and submit for review
- Submit listing application with supporting documents (see BSX Listing Regulations for document requirements)
- Ensure management is aware of the company's ongoing Listing Requirements
- Introduce company to the market (generally done through third party support using road shows and public relations exercises to create awareness, stimulate interest and expand demand)

Disadvantages Currently for an SME listing on BSX but subject to change:

- Initially not a USA registered security
- Lack of market coverage at the moment but may be addressed as need arises
- Like many exchanges, limited liquidity for SME but being a smaller exchange this may be addressed as needed
- Limited external access to the BSX market (given newness of product platform)
- Limited access to cross border settlement mechanisms (given newness of product platform)

Advantages for an SME listing on BSX:

- Listed on an internationally recognized stock exchange that is a full member of the World Federation of Exchange (not so with USA OTC platforms and other offshore exchanges)
- BSX is a fully deployed electronic/modern stock exchange platform. Vertical silo, trading, settlement and depository services are owned and controlled by the BSX
- Listing on a recognized stock exchange permits greater access to professional investors which require target securities for investment to be listed (fiduciary responsibility)
- Raises company profile via BSX information dissemination sources (BSX feeds Bloomberg real time data and news)
- Naked short selling not allowed
- BSX located in a jurisdiction whose regulator is well known and respected and whose financial platform is substantial (i.e. 3rd largest reinsurance market globally)

IN SUMMARY AND CONCLUSION: Why is BSX a viable SME alternative as compared to a USA or other global exchange when considering an IPO and listing? ANSWER: For an SME that wants to lPO and list on a traditional exchange then BSX offers the following …..

- Bermuda is not bound by Western Hemisphere or European regulatory frameworks (i.e. SOX and EU Directives).
- BSX offers a listing on a recognized exchange NOT a posting on an electronic trading platform which is unregulated (i.e. OTC and Pink Sheets)
- BSX is a fully deployed stock exchange platform
- Principle based regulatory framework based upon internationally accepted standards
- Due to size and history, BSX is commercial, nimble and niche focused
- 700 listed securities with a combined aggregate market capitalization of over $450 bn.
- Management and staff are open to work with those individuals and groups to enhance an environment for SME's seeking exchange funding

<u>Details and actions regarding a focus on SME IPOs and listings that may be taken by the Singapore Exchange (SGX) are under consideration and will be provided as received at a later date</u>