DAVIES

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BY E-MAIL: comment@ccmr-ocrmc.ca

Dear Sirs/Mesdames:

Thank you for the opportunity to comment on the Revised Consultation Draft of the provincial and territorial Capital Markets Act (the "CMA" or the "Draft Act") and the draft initial regulations under the CMA (the "CMRA Regulations"), as well as the proposed changes to the existing national instruments and policies (the "Existing Instruments").

Our detailed comments are set out below and range from high level policy-oriented comments to drafting points. The comments on the CMA can be found under Part I below and the comments on the CMRA Regulations and the Existing Instruments can be found under Part II below.

The members of the Davies working group who participated in the comment process are listed at the end of this letter.

References herein to the "Commentary" are to the "Commentary on the Revised Consultation Draft of the Provincial/Territorial Capital Markets Act" or the "Draft Initial Regulations for the Cooperative Capital Markets Regulatory System", as applicable, each published on August 25, 2015.

GENERAL COMMENTS

While we still view the achievement of consensus among the several participating jurisdictions (the "CMR Jurisdictions") as a great accomplishment, we continue to have concerns with the extent to which the CMA introduces significant substantive changes into the law and the quality of consultation process. Specifically:

1. Many of our continuing comments and concerns flow from the initial decision made by the drafters of the legislation to model it on the *British Columbia Securities Act* (the "BC Act") and not the *Ontario Securities Act* ("Ontario Act"). The Ontario Act governs the largest portion by far of Canada's capital markets, and Ontario has a vigorous and involved securities bar and investment banking community, both of which have contributed over the years to a robust dialogue on the evolution of securities legislation. This is evident in the comment process on the Draft Act where the vast majority of the comments came from Ontario market participants. The choice to model the Draft Act on the legislation of British Columbia, where the capital market is comprised of smaller issuers and which has historically faced very different securities regulatory issues than Ontario, is very difficult to defend on a principled basis. By proceeding on the wrong foot from the outset, the drafters of the CMA will impose on Canada's key financial and capital markets legislation that will be disruptive to well-established transaction

mechanics and compliance practices and will impose significant costs on market participants to adapt to a new regime.

2. As we commented in our 2014 letter, the introduction of the new legislation should not be used as an opportunity to introduce major substantive changes to Ontario securities law unless the adoption of such changes is preceded by a thorough public consultation and study of the changes. We recommended at that time that the long established process of the Ontario Securities Commission (the "OSC") and the Canadian Securities Administrators in this regard ought to be followed here. That would require each change to be identified in the request for comments, and its implications explained and its necessity justified.

3. While we appreciate the effort to engage in a consultative process, we do not think the process was ultimately satisfactory. In many instances, where commenters provided thoughtful and detailed comments on the prior draft of the CMA, the response was simply to note that the draft was consistent with legislation in other jurisdictions without addressing the specific concerns raised. We do not consider that adequate justification for a change in law.

4. The Draft Act gives broad and sweeping powers to the capital markets regulatory authority (the "Authority"). For example, as discussed in more detail below, the Authority can require directors, officers, promoters and control persons of an "issuer" to hand over any "information, record or thing" in the person's possession or under their control that relates to the administration or enforcement of capital markets laws or the regulation of capital markets. This power of the Authority extends not only to reporting issuers and market participants but to any person that has issued or proposes to issue securities, from the tiniest private entity to the largest publicly held one. No case has been made for the broadening of powers of the regulator to the point of divorcing them completely from the traditional focus of securities regulation, namely, public securities markets. The CMR Jurisdictions defended the power on the basis that it exists under the BC Act without providing an explanation as to the policy rationale for its inclusion.

5. It appears that the general bias of the drafters of the CMA was to adopt the most expansive prohibition from among the existing provincial securities acts. By way of illustration, although Ontario law was seldom the reference point for the Draft Act, the drafters did decide to follow Ontario's unique approach and regulate non-resident investment fund managers.

6. The Draft Act significantly extends the extra-territorial reach of Canadian securities law. Under the Draft Act, the Authority has extended its jurisdiction and the application of the CMA to Canadian corporations, partnerships and trusts listed only on foreign exchanges that have not sought and are not seeking to access Canadian capital markets. This approach to regulation is not only inconsistent with the stated purposes of the CMA, it is

also intrusive and costly. At the same time, the Draft Act proposes to regulate sales of securities by Canadian issuers to foreign investors, adopting a British Columbia approach that is both dated and impractical and will be an impediment to access by Canadian issuers to the US and other international capital markets.

7. A number of sections of the Draft Act take a "catch and release" approach to regulation where conduct is prohibited or persons are caught within a class of regulated persons unless exempted by regulation. For example and as discussed below, the Draft Act defines the term "market participant" broadly to catch a larger universe of persons and entities than does the Ontario Act and then contemplates exemptions by regulation from specific obligations applicable to market participants generally. As a general principle, we believe this is not an appropriate approach to securities regulation; nor is it consistent with the approach of the Ontario Act.

8. The Draft Act vests in the Authority substantial discretion. The Authority has significant power to designate persons as members of a "prescribed class" or to otherwise "prescribe circumstances" where persons will become subject to the regulation of the Authority and the application of the CMA. The circumstances in which the regulator may make such determinations are not delineated in the legislation. For example, the Authority will have the ability to require all registrants to meet such standards "as may be prescribed". The Authority will have the power to require issuers to obtain a receipt for a "prescribed offering document" in addition to requiring a receipt for a prospectus. The Authority also has the ability to deem a person to have control over another person in any "prescribed circumstance". This vesting of substantial discretion in the Authority, coupled with the platform approach to the legislation itself which leaves vast sections of the law to regulation, together undermine one of the key features of a sound capital market, namely, stability and predictability in the legal and regulatory regime which allows for transaction planning.

Our specific comments on selected provisions of the Draft Act and Regulations are set out below.

PART I – CAPITAL MARKETS ACT

INTERPRETATION

Reporting Issuer

Clause (c)

We had previously commented that clause (c) of the definition of "reporting issuer" should be drafted to exclude an exchange that is temporary in nature or is made merely to effect an internal reorganization. We further noted that clause (c) is missing certain language from the clause on which the current legislation is modelled. We had suggested language in our prior comment

letter to address these concerns. In response to these issues, the ministry and regulatory staff of the CMR Jurisdictions ("Staff") have noted in the responses filed on October 20, 2015 that this language is substantively the same as the BC Act and that excluding an internal reorganization or temporary transaction would fall within the Authority's regulation-making powers. It appears as though Staff is accepting the position that internal reorganizations and temporary transactions should not be captured by clause (c) of the definition yet these transactions have not been excluded from the definition pursuant to CMRA Regulation 11-501. We would suggest that CMRA Regulation 11-501 be revised accordingly.

Section 3- Affiliation

References throughout the Draft Act to affiliated persons are by reference to an "affiliate", not a person that is "affiliated". Accordingly, the introduction to this section should be revised to provide that a person "is an affiliate of" another person.

PROSPECTUS REQUIREMENTS

Section 28 - Restriction on distribution of records

In order to properly limit the conduct that might be prohibited by the regulations, language should be added to the effect of this italicized language - "must not, *in furtherance of that distribution,…*". This limitation is consistent with existing prohibitions on marketing materials are a function of the prospectus requirement, which is premised on a "trade".

Section 29 - Preliminary prospectus requirements

The reference at the end of this Section to "prospectus" should be replaced with "preliminary prospectus" or, consistent with the Ontario Act, separate provision should be included here to be clear that a preliminary prospectus can exclude certain pricing and other information that will not be included until the final version of the prospectus.

Section 32 – Requirement to Provide Further Information, etc.

In response to our concerns regarding this Section, Staff has noted that circumstances under which the Chief Regulator would not rely on Section 30(2) but instead impose additional requirements under Section 32 will be an "operational decision". It is unclear to us what this is intended to address. Giving the Chief Regulator virtually unfettered discretion to demand information beyond that required by the statute or the regulations will create uncertainty and further impediments to access to the public markets in Canada. The suggestion in the Staff response that a party affected has an opportunity to have a hearing on the issue is of little practical utility in the context of a live financing. The window to raise capital is typically limited and issuers seek certainty when accessing the capital markets. Section 32 of the CMA and Section 2(1)(i) of CMRA 41-501 (discussed in more detail below) create an unnecessary level of uncertainty in this regard. We therefore recommend deleting these Sections.

Section 34 - Permitted activities under preliminary prospectus

Currently, Section 34 only provides an exception for permitted marketing activity during the waiting period. It fails to account for permitted marketing activities *prior* to the issuance of the preliminary receipt (e.g., bought deal, testing the waters).

Section 36(4) - Duty to comply

We submit that, as a practical matter, the duty to cease distribution can only be effective upon receipt of the relevant order. The recipient will not be on notice of the order at the time it is sent. In addition, the following language is missing after "Chief Regulator" – *"for that prospectus or prescribed offering document, as applicable*".

Section 37 - Obligation to Send Prospectus, etc.

We disagree with Staff 's interpretation that the change in language from "dealer" to "a person who trades in securities" does not broaden the delivery obligations from those existing under the Ontario Act. On a technical read of this Section, together with Section 3(2) of CMRA Regulation 41-501, the issuer is "trading in securities" when involved in a distribution and therefore is responsible to deliver a prospectus. This represents a departure from Ontario law and imposes an obligation on an issuer that it might not be capable of satisfying. For example, in the context of an underwritten or bought deal public offering of securities, it is the dealer that enters into the purchase agreement with the investor, not the issuer. As a result, currently dealers ensure that the prospectus is delivered to investors, which are clients of the dealer. However, now, as a matter of law, the issuer will be held responsible if the dealer fails to deliver the prospectus. This is an untenable situation for issuers and an unnecessary "doubling up" of responsibility.

Separately, there should be an exception if the required documents were previously sent. This exception is currently provided in Section 71 of the Ontario Act.

While not the subject of this comment process, in future rulemaking initiatives we urge Staff to consider the benefits of introducing an 'access equals delivery' model for prospectus delivery.

<u>DISCLOSURE AND PROXIES</u>

Section 45 – Information from Directors, etc.

Section 45 introduces a sweeping new open ended power for the Chief Regulator to require a director, officer, promoter or control person of an issuer to give the Authority any information, record or thing in the person's possession or under the person's control that relates to the administration or enforcement of capital markets law. There are several troubling aspects to this provision:

(a) While contained under Part 7 of the CMA, the obligation is not limited to the disclosure of information. The power is drafted broadly enough to authorize the Chief Regulator to effectively confiscate property, even property that does not belong to the person but is in the person's control.

(b) The Draft Act does not impose any procedural safeguards with respect to this power and references no regulations that would impose any restrictions or protocols around such demands.

(c) Although the information, records or things demanded by the Chief Regulator must relate to the administration or enforcement of "capital markets law", the obligation extends to directors, officers, promoters or control persons of issuers that are neither reporting issuers nor registrants. No explanation is given for why the provision should apply to private companies or control persons of issuers whether or not reporting issuers or registrants.

(d) Section 45 is both broader and more vague than similar provisions, such as Section 54 of the Draft Act.

For the reasons stated above, we previously suggested deleting Section 45 of the Draft Act. In response, Staff has advised that Section 45 is consistent with securities legislation in British Columbia, without providing an explanation as to the policy rationale for the inclusion of the Section and without addressing the concerns we have raised.

MARKET CONDUCT

Section 54 - Requirement to Keep Records

The definition of market participant remains overly broad and captures issuers relying on exemptions from the prospectus requirements, including the private company exemption, as well as issuers "purporting" to rely on exemptions from the prospectus requirements, whether or not a trade occurs. Canadian issuers that do not access Canadian capital markets are also deemed to be market participants pursuant to CMRA Regulation 51-105, discussed below. We had previously commented that the definition of market participant is too broad and that it was inappropriate to require certain of these market participants to be subject to the record keeping and other requirements of the CMA. Section 54(1.1) of the CMA has been added to address these concerns and allow the Authority to exempt a class of market participants from the record keeping provisions of the CMA. For clarity, the exception included in Section 54(1.1) of the CMA should be expanded to cover all of Section 54, including the duty to provide records under Section 54(3).

Although the Commentary suggests that Section 5.4(1.1) allows the Authority to exempt control persons, issuers and other market participants from the requirements of Section 54(1), no such prescribed class has been excluded pursuant to the CMRA Regulations. It is unclear whether an

application to the Authority requesting relief from Section 54(1) will be required in such circumstances or whether the Authority will pass regulations on its own accord to exempt this prescribed class. Details of the criteria that will be applied by the Authority in making these decisions have been omitted from the draft legislation.

Section 55 - Duty to Client

As we noted in our prior comment letter, Section 55 of the Draft Act extends the duty of good faith and fair dealing from that imposed by OSC Rule 31-505 on dealers and advisors to underwriters, notwithstanding the prevailing view and practice that underwriters do not owe such a duty to their issuer clients. As we previously suggested, a quasi-fiduciary duty is potentially incompatible with underwriters' statutory liability to the persons to whom their clients' securities are sold and inconsistent with the securities commissions' articulated expectation that underwriters will stand in an adversarial role *vis a vis* their clients in respect of due diligence and disclosure. We had recommended that such a significant change should not be adopted without a full understanding of the implications and a process of consultation. In response to these comments, Staff has noted that this provision is consistent with securities legislation in British Columbia, Alberta and New Brunswick, without commenting on whether it is the intention of Staff to modify the current view of the relationship between an underwriter and its issuer client. We re-iterate once again that such a significant change to existing legislation in Ontario should not be adopted without a better understanding of the implications.

Not only is the duty of fair dealing currently owed by dealers now extended to all registrants under Section 55 of the CMA, the Authority will also have the ability to require all registrants to meet such other standards "as may be prescribed", providing the Authority with significant regulation-making power to further alter the duty of a registrant, including, as noted in the Commentary, to adopt a "best interests" standard. The definition of such a standard will be highly disputed and should only be adopted after significant consultation with affected parties. We urge Staff to consider adopting any additional registrant standards as part of the CMA itself, rather than through regulation.

Section 60(4)- Prohibited Representations – Listing on an exchange

We submit that this prohibition on listing representations be removed from capital markets laws. It is an antiquated provision unique to Canadian jurisdictions that results in unnecessary cost and delay without any concomitant benefit to Canadian investors.

Section 62 - Market Manipulation

We note that several commenters suggested that this Section should mirror the language in Section 126.1 of the Ontario Act such that the person engaging in the conduct must know or ought reasonably to know that the conduct would result in market manipulation. The prohibition should only apply to wilful or reckless conduct. In response, Staff has thanked commenters for their comments but has not changed the Section and has not provided any explanation for

disregarding these comments. Similar comments were made in respect of Section 63 and a similar response from Staff was provided. Given the consequences for a breach of Section 62 or Section 63 (which may include imprisonment), we believe that an element of *mens rea* is necessary.

Section 66(1)- Insider Trading

In our earlier comment letter, we expressed a concern that the term "publicly traded" is not defined in the CMA. In response, Staff has noted that "publicly traded" is used but not defined in the secondary market liability framework (a statement which is not entirely accurate, as noted below) and the insider trading framework in all CMR Jurisdictions.

We note that the Ontario Act was amended only this year to include trading in securities of issuers whose securities are publicly traded for purposes of the insider trading framework. This change was made without any public consultation as far as we are aware and presumably to align the insider trading regime in Ontario with the regimes found in the other CMR Jurisdictions.

The term "publicly traded" is not in fact used in the same open-ended and undefined way in the secondary market liability framework in the CMR Jurisdictions. Under Section 138.1 of the Ontario Act and similar provisions in the CMR Jurisdictions the notion of a "publicly traded" non-reporting issuer is limited to one with a real and substantial connection to Ontario.

A similar limitation should be applied to the insider trading regime in the CMR Jurisdictions. Where an issuer has a substantial connection to a CMR Jurisdiction, it is defensible to regulate trading in the securities of that issuer to ensure that all investors in that jurisdiction have access to the same information before making an investment decision. If there is no real and substantial connection to a CMR Jurisdiction, then the CMA should not apply. To extend the application of the insider trading and tipping prohibitions extra-territorially is particularly problematic where the conduct may be lawful in the foreign jurisdiction, a risk which is especially acute in the insider trading and tipping area where Canada's laws are more stringent than those in the United States and other jurisdictions. The stated purposes of the CMA are to provide investor protection, to foster fair, efficient and competitive capital markets and to contribute to the stability and integrity of the Canadian financial system. None of these purposes is served by extending the insider trading regime to securities of all publicly traded issuers, irrespective of the connection or lack thereof, to a CMR Jurisdiction.

The insider trading prohibition has also been extended well beyond the current prohibition in the Ontario Act against purchasing or selling a security to prohibit the purchase or "trade" of a security and the entering into of a transaction involving a security including a termination or material amendment of a pre-existing obligation with respect to a security or any related financial instrument. Such an extension of the well-settled insider trading law in Ontario should not be included in the new legislation without a full airing of the purpose of the change and a full appreciation of the implications. This approach is even more troubling in light of the fact that Ontario amended the insider trading provisions of the Ontario Act just a few months ago to bring

it generally into line with the insider trading provisions in other provinces but specifically did not expand the range of prohibited conduct beyond the purchase or sale of a security. Presumably, the recent amendments to the Ontario Act reflect the legislature's recently considered view of the appropriate scope of the prohibition.

Section 66(2) – Tipping

We had recommended reverting to "in the necessary course of business" in this Section of the CMA. Instead, Staff has indicated that several jurisdictions use the words "'necessary in the course of business". It would be helpful if Staff could confirm that the change in wording is not intended to alter the tipping provisions from those found in the Ontario Act and National Policy 51-201, notwithstanding the change in language.

Section 66(4) – Recommending

In our prior comment letter, we had noted that in the course of marketing a private placement an issuer or agent may need to disclose material non-public information to a potential investor, which it does under the "necessary course of business" exception. This has been a practice that has been accepted by the Canadian securities regulators as reflected in National Policy 51-201- Section 3.3(4). The marketing efforts of the issuer or agent under these circumstances could also be seen to include recommending or encouraging the investor to participate in the private placement and should be excluded from this prohibition in the same fashion that the disclosure is excluded from the tipping prohibition. We had also suggested giving consideration to whether other ordinary course business activities that involve recommending an issuer's securities (such as investor relations activities, non-deal road shows, etc.) should be excepted.

In response to these comments, Staff has noted that the ability to prescribe circumstances where a person does not contravene the CMA is within the Authority's regulation-making power if the policy need for inclusion of a defence is established. We think our comment has raised a policy need for inclusion of a defence, a concern which has not been disputed by Staff.

Section 68(6) – Defence to tipping

An equivalent defence should be afforded for recommending in contravention of Section 66(4).

ORDERS, REVIEWS AND APPEALS

Section 88(1) – Cease-trade order – non-compliance

We submit that, in order to properly balance the discretion afforded in this Section with the wrongdoing it is intended to address, the following italicized language should be added to the first line- - "The Chief Regulator may, *if it considers that it is in the public interest to do so,* without giving…".

Section 89 – Orders of Tribunal – General

General Comment

We continue to be concerned about the uncertainty introduced by the current draft of this provision. As explained previously, we accept that the Chief Regulator should be entitled as a matter of right to commence proceedings before the Tribunal to seek relief under this Section. The more difficult issue, which is not addressed in the CMA is *when*, and *if*, it is ever appropriate for a private litigant to commence proceedings before the Tribunal seeking relief (and to advance its personal interests) under this Section.

We appreciate that this Section is consistent with current securities legislation. The problem, however, is that the OSC and British Columbia Securities Commission have reached inconsistent results in how to interpret analogous provisions. In *Severstal Gold NV (Re)*, 2010 BCSECCOM 181, the British Columbia Securities Commission held that a takeover bid under Section 114 of the B.C. *Securities Act* constituted the "only circumstances under which the Commission has made orders under Section 161(1) as a result of an application by a member of the public" (para. 30). By contrast, in *In the Matter of MI Developments Inc*. (2009), 32 OSCB 126, the OSC concluded that "such applications should be able to be brought as of right only by Staff" (para. 108), and that leave to bring such an application should only be granted to a private party where "the order sought is future looking and prophylactic and not in the nature of simply an enforcement sanction" (para. 109).

We continue to believe that the CMA should eliminate the uncertainty and litigation that would inevitably surround this issue, and clarify private party standing to seek an order under Section 89 as follows:

(a) the Chief Regulator may commence proceedings before the Tribunal for relief under Section 89 as of right;

(b) private litigants may commence proceedings before the Tribunal for relief under Section 89 only with leave of the Tribunal; and

(c) the Tribunal shall grant leave to private litigants only in circumstances where:

  (i) the relief sought is future-looking, and not regulatory or enforcement in nature;

  (ii) the private litigants have a direct interest in the outcome (for example, as a bidder or target shareholder in a poison pill or other defensive tactics hearing); and

(iii) the Tribunal, considering any other matters it deems relevant, including the Chief Regulator's reasons for not commencing the proceedings, is satisfied that it is in the public interest to grant leave.

Section 89(4) – (7) – Order Without Delay

We accept Staff's comments with respect to procedures for extension of a temporary order. However, we continue to be concerned regarding the scope of the types of temporary orders currently authorized in Section 89(4). Given the almost unfettered discretion granted to the Chief Regulator to make orders that imply a finding of breach (e.g. Section 89(1)(a) (m) – an order that a person comply with the CMA or submit to an audit, respectively); or have potentially significant ramifications to a person's livelihood (e.g. Sections 89(1)(h), (i), (j), (k) and (l)); we continue to believe that it would be appropriate to carve paragraphs 89(1)(a), (h), (i), (j), (k), (l) and (m) out of Section 89(4).

Section 91 – Freeze Order

We recognize the CMA's comment that Section 91 of the Draft Act follows current securities legislation in British Columbia rather than Section 126 of the Ontario Act. However, we respectfully submit that further consideration is warranted given the intrusiveness of a freeze order, and the apparently low standards (when compared to the test for a *Mareva* injunction) for issuing such an order. We believe that there should be a requirement to have such an order reviewed by a court and any extension of such order should be made subject to court approval, as in Section 126(5) of the Ontario Act, rather than simply by order of the Tribunal if it is satisfied that an extension is not prejudicial to the public interest.

Our concerns are heightened by the new Section 91(1)(d), which permits the Tribunal to make an order, without notice or a hearing, that a person must "liquidate or otherwise dispose of [another person's] derivatives and retain the proceeds of the liquidation or other disposition." Unlike Sections 91(1)(a) to (c), Section 91(1)(d) is a mandatory order, not a prohibitory one. It is irrevocable and therefore inconsistent with the purpose of Section 91 of maintaining the status quo. Indeed, Section 91(6) provides that an order under Section 91(1) expires after 15 days, and Section 91(7) requires an order after a hearing to extend a freeze order. Where the "freeze order" requires liquidation of another person's derivatives, the order is effectively permanent and an extension is irrelevant.

CIVIL LIABILITY

Section 117(1) – Actions Relating to Prospectus or Prescribed Offering Document

Section 117(1) provides for a right of action where the prospectus or prescribed offering document contains a misrepresentation "at the time of purchase". These words are not found in Section 130(1) of the Ontario Act and it is not clear to us whether this change is directed at the *Danier* decision. *Danier* confirmed that the time of filing is the appropriate time to assess

whether a prospectus contains a misrepresentation. This is a very significant change in the law and one that will require substantial and costly changes in underwriting practices relating to the timing of due diligence, opinions, expert reports and similar matters. As previously noted, we are of the view that substantive changes should not be introduced into the Draft Act without an appropriate explanation of the policy rationale and an opportunity to fully canvass the implications of the change. The only explanation provided by Staff is that the change is consistent with the statute in British Columbia and New Brunswick.

Section 122(1) – Actions Relating to Prescribed Disclosure Document

This provision creates a new statutory right of action against directors of the issuer. As we have previously noted, this represents an expansion from Section 130.1(1) of the Ontario Act which limits the statutory right of action to claims against the issuer and a selling security holder. In our view this is another example of a significant change in the substantive law that should not be enacted in the absence of the articulation of a persuasive policy rationale and extensive consultation with market participants. In the Commentary, Staff has not provided the rationale for expanding the class of defendants. A discussion of the necessity and desirability of expanding the class of potential defendants should precede this change, which will impose significant costs on issuers accessing the exempt market. The purpose of the exempt market is to provide issuers with faster and less costly access to capital provided by investors with sophistication or resources to find for themselves. Canadian regulators have worked to balance this objective with investor protection by limiting the class of investors and/ or the size of investments in exempt offerings. In our view, layering on additional liability for directors only serves to undermine the utility of the exemptions in circumstances where there is no suggestion that the current framework for recourse is flawed.

In addition, we submit that the introductory language to this Section be amended as follows: "If, *during the period of distribution*, a person purchases securities offered *to it* by a prescribed disclosure document …". The first edit is consistent with Section 130.1(1) of the Ontario Act. The inclusion of "to it" is to clarify that this right is available only to purchasers to whom the offer was made.

Section 129(1) – Action for Damages – Insider Trading, etc.

This provision of the Draft Act represents a major substantive expansion of the existing insider trading liability regime under the Ontario Act. Section 129(1) expands exponentially the category of plaintiffs to whom damages are payable. Under Section 134(1) of the Ontario Act, a person who purchases or <u>sells</u> in contravention of the rule is liable to compensate the <u>seller or purchaser of the securities</u>. However, under Section 129(1) of the Draft Act, damages would be payable to <u>every person</u> who purchases or <u>trades</u> in a security of the issuer during the period from the time the contravention occurred to the time when the material change or material fact is generally disclosed.

Accordingly, damages would be payable to every single person who purchased or traded during the relevant time period, not just persons who traded with the defendant. Section 129(1) also provides that there would be liability not only in respect of purchases and "sales", but purchases and "trades". As a result, any person who engaged in any act directly or indirectly in furtherance of, among other things, a sale of a security, would be subject to insider trading liability. This formulation appears to expand the scope of insider trading liability, but creates uncertainty as to its application due to the inherent subjectivity of applying the definition of "trade".

Staff's response to our prior comments fails to address this concern which we believe is valid and a potential unintended consequence.

Section 129(2) – Amount of damages and Section 129(3) Loss incurred by plaintiff

Subsections 129(2) and (3) refer to "the loss incurred by the plaintiff as a result of the contravention" as the basis for calculating damages. This formulation appears to be based on the premise that the plaintiff's loss was caused by defendant's contravention. However, there is no such causal relationship. The plaintiff's loss does not result from the defendant's contravention of insider trading rules, but rather the fact that the plaintiff happened to decide to trade (a decision unrelated to the activities of the defendant) during the relevant period following the defendant's violation of insider trading laws.

This lack of causality is in our view a further reason not to pursue the expansion of the category of plaintiffs to whom damages are payable (see our previous comment). However, if you insist on adopting this approach it would appear that these provisions as currently drafted do not accurately describe the circumstances giving rise to the plaintiff's loss and the related calculation of damages.

Section 130(1) – Payment of Benefit – Insider Trading, etc.

As we noted in our prior comment letter, the reference to "the person and all other persons" should be changed to "such person" in order to ensure that the remedy (which is of a restitutionary nature) is tied to the contravention. In response, Staff has noted that the Section is consistent with securities legislation in British Columbia without commenting on the merits of our suggestion that the remedy should be tied to the contravention.

Section 130(2) – Payment of Benefit – Front-running

Same comment as above regarding Section 130(1).

Section 145 – Intervention by Chief Regulator

We remain of the opinion that providing the Chief Regulator with a statutory right of intervention in a proceeding to enforce a right or obligation created by Part 12 constitutes an unjustified intrusion by the Chief Regulator into the private, civil liability regime created under

the Draft Act. The Chief Regulator's purpose is deterrence while the policy objective underlying civil liability is compensation and deterrence. To this end, we are of the opinion that providing an unqualified statutory right to intervene may compromise the Authority's role as an independent regulatory body.

CIVIL LIABILITY FOR SECONDARY MARKET DISCLOSURE

Section 165(1) – Liability Limit

Section 165 prescribes liability limits for actions brought under any of Sections 149-152. For responsible issuers and influential persons that are not individuals, the first value in the formula for calculating the applicable liability limit is 5% of the market capitalization of the issuer or influential person in question. "Market capitalization" is defined in Section 23(2) of CMRA Regulation 11-501, which is identical to Section 249 of Regulation 1015 to the Ontario Act. The definition involves, among other things, performing the following calculation for each class of equity securities for which there is a published market: the average number of outstanding securities for the 10 trading days before the day on which the misrepresentation was made or the failure to make timely disclosure first occurred is multiplied by the trading price for the securities for the 10 trading days before the day on which the misrepresentation was made or the failure to make timely disclosure first occurred.

In a case involving a single misrepresentation or a single failure to make timely disclosure of a material change, calculating the applicable market capitalization is relatively straightforward in concept. However, we are concerned that in cases involving multiple misrepresentations or multiple failures to make timely disclosure of material changes, it is unclear how the applicable market capitalization is to be calculated. The Draft Act does not specify whether, in such cases, the applicable market capitalization is: (i) based on the first misrepresentation or failure to make timely disclosure; (ii) the sum of the market capitalization in respect of each of the misrepresentations or failures to make timely disclosure, divided by the number of misrepresentations or failures to make timely disclosure; or (iii) to be calculated in some other manner. To our knowledge, no Canadian court has considered this issue.

We believe that, in view of the importance of the liability limits to the overall scheme of the legislation and the increasing prevalence of cases involving allegations of multiple misrepresentations or failures to make timely disclosure, now is the opportunity to resolve this uncertainty. We would therefore suggest adding language, either in Section 165 of the Draft Act or in Section 23 of Regulation 11-501, to clarify that where multiple misrepresentations or instances of failure to make timely disclosure are established, the applicable market capitalization is the average of the market capitalizations in respect of each of the misrepresentations or failures to make timely disclosure.

<u>**REGULATIONS, FORMS AND POLICIES**</u>

Section 197- Publication of notices, etc. by Authority

In our view, it is important to clarify how and where any prescribed notice, regulation or form must be "published" or made "accessible to the public" for purposes of this Part. Market participants should not be required to make themselves aware of changes in the law that are published or are otherwise made available to the public in an inconsistent and ever-changing manner. We suggest that market participants be entitled to rely on a single source of information from the Authority for informing themselves of all regulations made by the Authority and all forms and policy statements issued by the Chief Regulator. We suggest that this single source be the public website maintained by the Authority rather than "through an electronic medium as suggested by Section 197. The possibility that additional or contrary information may, at any time, become available through an indeterminate source will lead to market confusion. Further, any notice or statement should be published in a consistent and predictable manner reasonably designed to put any affected person on notice of its contents.

Section 202(4) – Regulate or prohibit

It may be prudent to include a clarification that a regulation may exempt certain persons, securities, trades, distributions, bids or other transactions from a requirement of Parts 2 to 9 where the CMA provides that the requirement be performed "in accordance with the regulations" or "subject to the regulations". Consider whether this clarification is properly included in Section 202(4).

Sections 203 and 215 – No finding of guilt or administrative sanction

With respect to Section 203(3) and Section 215, we submit that it is not sufficient that the relevant regulation or other material be "otherwise accessible". In each, the word "accessible" should be replaced with "published in accordance with Section 197". To the extent the regulation (or the material incorporated in a regulation, as applicable) is not published in the manner usually required, a person should not be liable for any contravention in respect of that regulation (or that portion governed by the incorporated material, as applicable). This recommendation will be more effective if coupled with the implementation of our comment above in relation to the single, public source for all published information and regulation.

Sections 205 and 211.1 – Notice of proposed regulation; Forms

In our view, it is in the public interest that all proposed regulations <u>and forms</u> be published in advance and be subject to comment by capital market participants, except in the limited circumstances set out in Section 205(4). Accordingly, we submit that Section 205 and Section 211.1 should be revised to be clear that notice of any proposed form must be given in the same manner, and will be subject to the same comment period, as any proposed regulation.

Section 205(4) – Exception to publication

Consider whether a class order may be extended by way of a temporary regulation per Section 96(1)(b) only where that temporary regulation is necessary to afford time to publish and allow for comment on regulation that will give permanent effect to the matters addressed in that order / temporary regulation similar to the condition to extending a temporary regulation under Section 210(2).

Section 210 – Automatic Revocation of Certain Regulations

Some clarification is required in Section 210(2) to allow for the revocation of the temporary regulation prior to the 36 month outside date. Absent this clarification, the temporary regulation would continue for longer than the Authority intended and may overlap with a permanent regulation that is to replace it. Clarification is also required in this Section to distinguish between the temporary regulation that is being extended and the more permanent regulation to replace it that is proposed pursuant to Section 205(1). Absent these clarifying changes the more permanent regulation will be read to be the same regulation as the earlier, temporary regulation and, among other things, would be revoked after 36 months.

We submit that the statement required by Section 210(4) should be accompanied by the full text of the relevant regulation consistent with the advance notice required under Section 205(2). As currently drafted, Section 210(4) requires only a description, among other things, of the regulation. Market participants cannot properly govern their affairs based only on a description of a regulation to which they are to adhere. If the full text of the regulation is not included with the notice, the notice should at least note that it is accessible to the public (with reference to that public source). On a minor, typographical note, Section 210(4) should be 210(3).

Section 212 – Guidance from the Authority

We submit that a minimum comment period be required by Section 212(4) for proposed changes to a policy statement that are material. While a policy statement will not have the force of law, to ensure efficient capital markets, it remains important that market participants have an opportunity to comment. Further, in determining the length of any comment period, it is unclear why the CMA would distinguish between a new policy statement and material changes to an existing policy statement. In fact, the latter might require more consultation because it would involve a change to existing interpretations relied upon by market participants.

Section 213 – Public access to regulations, etc.

See our earlier comment as to a single public source for accessing all of these materials.

PART II – REGULATIONS

GENERAL COMMENTS

We are pleased to see that many of the Existing Instruments will be adopted by the Authority without substantive changes. We had limited comments on some of the changes to these instruments. We are concerned however with the introduction of new substantive law in the Province of Ontario through the adoption of certain Multilateral Instruments. We also have some concerns with the new proposed CMRA Regulations.

NATIONAL POLICY 12-203 - *CEASE TRADE ORDERS FOR CONTINUOUS DISCLOSURE DEFAULTS*

Appendix B- *Lists of Defaulting Reporting Issuers* includes a draft note that the Authority does not intend to carry forward OSC Policy 51-601. The Ontario local policy has some additional detail on the process that the OSC follows in determining whether to add/remove an issuer from their list. It is unclear whether the decision to abandon Policy 51-601 signals a change in the process that will be followed.

NATIONAL INSTRUMENT 41-101 – *GENERAL PROSPECTUS REQUIREMENTS AND RELATED POLICY AND FORMS*

Special Warrants/Converting Securities

We have concerns with respect to the proposed amendments to Section 2.8(3) of 41-101CP which reads as follows:

> In a CMR Jurisdiction, Section 14 [Converting security prescribed for Part 12 of the Act] of CMRA Regulation 11-501 *Definitions, Procedure, Civil Liability and Related Matters* prescribes the securities that are converting securities for the purposes of Part 12 [Civil Liability] of the *Capital Markets Act*. Section 118 [Actions relating to prescribed converting securities] of the *Capital Markets Act* provides a right of rescission in connection with prescribed converting securities offered under a prospectus or prescribed offering document. As well, the reference to a person who "purchases securities offered by a prospectus" found in the statutory right of action for damages contained in Section 117(1) [Actions relating to prospectus or prescribed offering document] of the *Capital Markets Act* includes a person who receives common shares qualified by a prospectus on conversion of special warrants. [emphasis added]

In the Commentary, the Authority suggests that the underlined language clarifies how the right of action contained in Section 117(1) of the CMA works, and has specifically asked for comments on whether such language in fact clarifies how such right of action will operate.

We appreciate the additional clarity that the Authority is striving to provide; however, we believe that additional precision is needed. As drafted, the amount recoverable under Section 117(4) of the CMA pursuant to the statutory right of action is limited to "the price at which the securities were offered under the prospectus". In a special warrant transaction, no consideration is paid by the holder of the special warrant on the conversion of the special warrant to receive the underlying common shares. So, arguably, nothing is recoverable by the investor pursuant to the statutory right of action. In addition, an investor should not be permitted to double-up the amounts recoverable pursuant to a multiplicity of statutory rights of action. If an issuer sells an investor a special warrant pursuant to a prescribed offering document (e.g., an offering memorandum), Section 122 of the CMA provides the investor with a statutory right of action for damages or rescission if the prescribed offering document contains a misrepresentation. If the issuer then qualifies by prospectus the common share underlying the special warrant, and the prospectus contains the same misrepresentation, the investor would also, presumably, have a separate right of action under Section 117. While, as a policy matter, an investor may be able to benefit from the resetting of a limitation period by virtue of being entitled to multiple statutory rights of action, an investor should not be entitled to double-recovery.

OTC Derivatives

Companion Policy 41-101 provides that OTC derivatives are being treated as securities for purposes of the prospectus requirements found in the CMA until a comprehensive regulatory regime is implemented for OTC derivatives. We urge the CMR Jurisdictions to implement the OTC derivatives regulatory regime simultaneously with the implementation of the CMA. In the alternative, we strongly suggest that OTC derivative transactions involving sophisticated counter-parties be exempt from the prospectus requirements under the CMRA Regulations, similar to the proposed exemption for registration proposed by the Authority in National Instrument 31-103.

NATIONAL POLICY 47-201 – *TRADING SECURITIES USING THE INTERNET AND OTHER ELECTRONIC MEANS*

The proposed changes to Section 2.3 import the approach currently used in British Columbia to all CMR Jurisdictions. We believe the proposed changes to Section 2.3 are inappropriate for the reasons set out below in our commentary on proposed CMRA Policy 71-601 – *Distribution of Securities to Persons Outside CMR Jurisdictions*.

NATIONAL INSTRUMENT 51-102 – *CONTINUOUS DISCLOSURE OBLIGATIONS* ("NI 51-102")

According to the Commentary, the second paragraph in the definition of "Recognized Quotation and Trade Reporting System" has been removed, on the basis that in CMR Jurisdictions, a quotation and trade reporting system would be recognized and regulated as an exchange, making the need for an additional definition unnecessary. However, as this explanation is not provided in the actual instrument, it would be clearer to make this definition consistent with the definition of

"Recognized Quotation and Trade Reporting System" in National Instrument 21-101 – *Marketplace Operation* ("NI 21-101"), by replacing the second paragraph with the following, rather than deleting it: "in a CMR Jurisdiction, a quotation and trade reporting system recognized by the securities regulatory authority under the *Capital Markets Act* as an exchange." In addition to removing any ambiguity about how a "Recognized Quotation and Trade Reporting System" is defined in a CMR Jurisdiction for purposes of NI 51-102, this approach would ensure this term is defined consistently in NI 51-102 and NI 21-101, which is clearly the intent.

The proposed instrument includes a note to draft stating that the language requirement in Section 3.1(2) of NI 51-102 has been replaced by the broader requirement in Section 183 of the CMA. However, both Section 3.1(2) of NI 51-102 and Section 183 of the CMA seem to effectively require that versions of a document in a particular language are to be filed once they are actually delivered (i.e., if a document is initially filed in French, it does not have to be filed in English until the English version of the document is actually delivered). If the intention is that all linguistic versions of a document must be filed, regardless of which versions are sent to securityholders, this could present a significant additional cost to reporting issuers who currently only generally file documents in one language, given their base of investors. Such issuers typically translate documents in limited situations, such as in connection with a public offering, and requiring them to file all documents in English and French would be of questionable benefit to investors.

MULTILATERAL INSTRUMENT 51-105 - *ISSUERS QUOTED IN THE U.S. OVER-THE-COUNTER MARKETS* ("MI 51-105")

MI 51-105 is the product of an initiative from the British Columbia Securities Commission to address the harm caused by market participants that engage in abusive activities in Canada through the OTC markets in the United States. The stated objective of MI 51-105 is to discourage the manufacture and sale of U.S. OTC traded "shell companies" that can be used for abusive purposes.

The issue with MI 51-105 is that it is overly broad and has unintended consequences for legitimate issuers (both Canadian and foreign) that are not engaged in abusive activities. Moreover, the alleged harm that MI 51-105 seeks to address can already be adequately addressed by other provisions in securities laws. We therefore recommend that MI 51-105 be repealed and not carried forward as a CMRA Regulation.

In general, MI 51-105 deems any issuer a "reporting issuer" in each of the CMR Jurisdictions if (a) the issuer does not already have any class of securities listed or quoted on certain "designated exchanges", (b) the issuer has a class of securities that have been assigned a ticker symbol by FINRA for use on any U.S. OTC market and (c) the issuer's business is directed or administered in one or more of the CMR Jurisdictions or the issuer, or someone acting on its behalf, has carried on "promotional activities" in or from any CMR Jurisdiction.

The first problem with this is that an issuer cannot always control when FINRA issues a ticker symbol for a class of its securities. We understand that if the securities have been issued a CUSIP number, any U.S. broker-dealer can take the necessary steps to have the securities trade OTC in the United States, without the issuer's knowledge or consent.

Second, while MI 51-105 is targeted at a very specific type of abusive behaviour, the instrument makes no account for this in its operative provisions. Any issuer, legitimate or not, is simply forced into becoming a reporting issuer just by virtue of the fact that its securities happen to trade OTC in the United States. The underlying assumption in the rule is that if securities of an issuer with some nexus to a CMA Jurisdiction trade in the United States and the issuer is not listed on a "designated exchange", then it must have been created for an improper purpose. We do not believe this assumption is appropriate.

Consider the following example: a large private company in Canada carries out a private placement of shares to a small group of accredited investors in Canada and the United States. One of the U.S. investors happens to be a broker-dealer and takes the necessary steps to have the shares issued a ticker symbol by FINRA in order to create a small grey market for possible future trades to "qualified institutional buyers" in the United States. This company is now a reporting issuer in Canada. Through no fault of its own, and solely because it raised money in the Canadian exempt market, it is now fully subject to Canadian reporting requirements. Not only is this an extremely unfair result for the company, but it does absolutely nothing to protect investors in Canada.

While we acknowledge the exemptions provided in Section 18 of MI 51-105 (which are currently included in various blanket orders across the country), these only provide limited relief where the investors are all "permitted clients" or where the issuer has securities listed on certain designated exchanges. However, given that the Authority has ample power elsewhere in the CMA to address the alleged harm at which MI 51-105 is aimed, we recommend that it be repealed in its entirety.

MI 51-105 targets illegal "pump and dump" schemes whereby fraudsters use OTC-traded shell companies to defraud investors in Canada. This behaviour is in clear violation of a number of securities laws. It is not necessary for the issuer to be deemed to be a reporting issuer in order for securities regulators to take action against these individuals. Moreover, individuals engaged in this type of behaviour clearly are not concerned about compliance with securities laws and are unlikely to comply with the obligations imposed on OTC reporting issuers under MI 51-105. It is not clear to us what benefit is gained by deeming issuers such as these to be reporting issuers. In any event, to the extent there is a benefit, the Authority has the power under Section 95(2) of the CMA to designate any issuer to be a reporting issuer. It could use this power if circumstances warrant. This would be a much more tailored response to address the behaviour of a particular issuer, rather than creating unnecessary obstacles to legitimate behaviour, as MI 51-105 does.

We strongly urge the CMR Jurisdictions to reconsider the need for this Multilateral Instrument.

NATIONAL INSTRUMENT 55-104 – *INSIDER REPORTING REQUIREMENTS*

The definition of "economic interest" states that for CMR Jurisdictions, this term has the same definition as in securities legislation. The Commentary also notes that the term "economic interest" has been incorporated into the definition of "related financial interest" in Section 2 of the CMA. We would suggest that the definition of "economic interest" in National Instrument 55-104 – *Insider Reporting Requirements* make explicit reference to the definition of "related financial interest" under the CMA by including a statement such as the following: "in a CMR Jurisdiction, an economic interest is considered a related financial interest" in order to avoid confusion about how "economic interest" is defined for purposes of the CMA and ensure consistency among CMR Jurisdictions.

In Part 10 of the Companion Policy, the reference to "late filing fees" in sub-paragraph 2 has been placed in square brackets, likely as this is being considered as part of the fee project. In order to ensure harmony in the insider reporting requirements and related provisions across all provinces and territories, we would suggest adopting this instrument without substantive change, including with respect to the regime for dealing with failure to comply with the insider reporting requirements.

NATIONAL INSTRUMENT 58-101 – *DISCLOSURE OF CORPORATE GOVERNANCE PRACTICES* ("NI 58-101")

We suggest two changes to reflect recent amendments to NI 58-101 that came into force on November 17, 2015. First, the definition of "venture issuer" in Section 1.1 should include "Aequitas NEO Exchange Inc." after "Toronto Stock Exchange." Second, Section 1.3 should be amended by replacing paragraph (c) with "an exchangeable security issuer or credit support issuer that is exempt under Section 13.3 or 13.4 of NI 51-102, as applicable; and".

NATIONAL INSTRUMENT 71-101 ("NI 71-101") - *THE MULTIJURISDICTIONAL DISCLOSURE SYSTEM* ("MJDS")

Generally, we are of the view that offerings of securities to purchasers outside of the CMR Jurisdictions should be governed by the laws of the purchasers' local jurisdictions and not the CMA or the CMRA Regulations. In particular, we do not believe that issuers undertaking a southbound-only offering under MJDS should be subject to the prospectus requirements under the CMA or the CMRA Regulations. For example, an issuer filing a prospectus with the Chief Regulator for an MJDS southbound-only offering should be allowed to omit information that is not relevant or material to purchasers in the United States. In addition, issuers and underwriters involved in southbound-only MJDS offerings should not be required to comply with the marketing material requirements, statutory rights of recission (whether or not they are available under US securities laws), trust indenture requirements, delivery requirements or statutory rights of action or civil liability.

Our view is premised on the general view that offerings made to offshore investors should be conducted in accordance with, and investors should be entitled to only the protections afforded to them under, offshore securities laws. By capturing these offerings as "distributions" that are subject to the prospectus and registration requirements of the CMA, the Authority is subjecting these issuers to additional and potentially conflicting rules which ultimately render these offerings more costly and difficult to implement with no corresponding benefit to or protection of investors in the CMR Jurisdictions. MJDS southbound-only is available to a limited number of medium-to-large cap Canadian reporting issuers. As such, we see no harm to offshore investors by maintaining the Ontario approach to these offerings under Part 4 of the Companion Policy to NI 71-101. Moreover, no justification has been offered for the fundamental shift in the regulatory approach prevailing in Ontario and other provinces to adopt the British Columbia approach which regulates offshore distributions as if they were local distributions.

CMRA REGULATION 11-501 – *DEFINITIONS, PROCEDURE, CIVIL LIABILITY AND RELATED MATTERS*

Part 1 – Definitions and Interpretations

Section 2 – Persons Prescribed Not to be a Clearing Agency

We are supportive of the exclusion of certain prescribed persons in this Section from the definition of "clearing agency" in Section 2 of the CMA.

Section 3 – Persons Prescribed to be a Market Participant

Given the concerns mentioned in our prior comment letter and repeated above about the wide reach of the definition of "market participant," we are of the opinion that this Section of the regulation should prescribe certain persons, such as foreign and domestic non-reporting issuer, private companies and control persons not to be market participants.

Generally, the Authority's discretion to designate a person to be a market participant should be limited to persons who perform roles similar to those of the enumerated market participants in the CMA.

Section 4 – Persons Prescribed Not to be a Market Place

We are supportive of the exclusion of "inter-dealer bond broker" from the definition of "market place" in Section 2 of the CMA, as it is consistent with the Ontario Act.

Section 5 – Persons Prescribed to be a Reporting Issuer

We are supportive of this Section to the extent that it provides that issuers that are reporting issuers in any CMR Jurisdiction immediately prior to the CMA launch date will continue as CMA issuers in all CMR Jurisdictions.

In our prior comment letter and again above, we noted our concern about the undue breadth of clause (c) of the definition of reporting issuer in Section 2 of the CMA. As noted above, we believe that this Section of the regulation should narrow clause (c) of the definition of reporting issuer in the CMA by excluding an exchange that is temporary in nature or is made merely to effect an internal reorganization.

Section 7 – Voluntary surrender of reporting issuer status

We note that this Section imports the voluntary surrender provisions of BCI 11-502, which are akin to the 'simplified procedure' in CSA Staff Notice 12-307, to apply for a decision that an issuer is no longer a reporting issuer. While we are supportive of providing for a regulation that allows for an automatic surrender of one's reporting issuer status in lieu of a cumbersome application process, we submit that, consistent with the 'simplified procedure', there should not be a minimum notice period. Likewise, we suggest that the 'modified approach' from CSA Staff Notice 12-307 also be codified within the regulations for issuers reporting and listed in the U.S. or other jurisdictions identified within the regulation whose securities law or exchange requirements will mandate adequate disclosure.

Proposed Provision - Persons Prescribed for the Purpose of Record Keeping

We note that in the Commentary, the Authority proposes to add a provision to this regulation prescribing that certain record keeping requirements required under Section 54(1.1) of the CMA will not apply to certain persons (such as control persons of reporting issuers and persons providing record-keeping services to a registrant.) While we are supportive of this proposed exclusion, we are concerned about timing. We are of the opinion that this exclusion should be included in this regulation at this time, given the resources that will need to be expended to seek and obtain an exemption from the Authority under Section 54 of the CMA until such exclusion is in the regulations.

<u>Part 2 – Procedures</u>

Section 9 – Execution and Certification of Documents

We note that the Ontario rule which provides the Director has authority to permit agents or attorneys to file records without a power of attorney has not been incorporated into this regulation. While your stated rationale is that Section 94 of the CMA will permit the Authority to provide an exemption from the power of attorney requirement, we are of the opinion that this procedure would impose an unnecessary burden on agents and attorneys and the Authority and that the Ontario rule should be carried forward.

<u>Part 3 – Administration and Enforcement</u>

Section 12 – Profit Made and Loss Avoided

We believe that the detailed formulas for "profits made" and "loss avoided" set out in this Section for the purpose of calculating fines under Section 115(3) of the CMA should not be introduced as they result in substantive changes without the benefit of thorough consultation and

input from market participants. While your stated intention is to provide for consistency with the approach for calculating damages for civil liability for secondary market disclosure, there may be valid policy reasons to differentiate between the calculation of fines, which have an underlying rationale of deterrence, and the calculation of damages, which have an underlying rationale of compensation. In our opinion, the Ontario rule should be carried forward until a discussion of the necessity and desirability of consistent formulas in these two parts is had.

<u>Part 5 – Civil Liability</u>

Section 15 - Disclosure Document Prescribed for Section 122(1) of the Act

Section 15 prescribes the disclosure document under Section 122(1) of the CMA (Actions relating to prescribed disclosure documents). The concept of a prescribed disclosure document is similar to the definition of "offering memorandum" under the Ontario Act, with some notable differences. The Ontario Act definition of offering memorandum is "a document… purporting to describe the business and affairs of an issuer …". A disclosure document under the CMA for purposes of 122(1) is a document "that provides information, including information about the business or affairs of an issuer, and that has been prepared primarily…to assist the prospective purchaser in making an investment decision ". This is a broader definition and captures any document that provides any information that has been prepared primarily to help a purchaser to make an investment decision. It is unclear why documents that describe information other than the business or affairs of an issuer would need to be considered a prescribed disclosure document. As a result of these changes, issuers will now have to accept statutory liability for misrepresentations in any document delivered to prospective investors and existing investors. This seems to us to be over-reaching. This change also casts doubt on the long-established practice of making private placements to institutional investors using term sheets only. Term sheets, because they contain no information pertaining to the business and affairs of the issuer, are not considered "offering memoranda" under existing Ontario law. This has allowed for time and cost-efficient offerings to be made to institutional investors without the documentation and procedures necessary in an offering that attracts statutory liability. Absent some case being made that these transactions are abusive or otherwise problematic, it seems unjustifiable to now regulate them in a significantly different manner.

The Ontario Act definition of offering memorandum excludes "a document setting out current information about an issuer for the benefit of a prospective purchaser familiar with the issuer through prior investment or business contacts". There is no such exclusion in Section 15 of the CMRA Regulation. We believe this exception should be carried forward in this regulation, as the exception is reasonable and does not undermine the goal of investor protection. In addition, by removing the exception considerable uncertainty is created as to the scope of the definition of "disclosure document" which, by its terms, arguably does exclude such documents as they would not in fact have been prepared primarily for sending to and review by a prospective purchaser to assist the prospective purchaser in making an investment decision about securities being sold in an exempt distribution.

Section 16 – Disclosure document prescribed for subsection 128(c) of the Act

For consistency with the delivery timeframe required in respect of prospectuses, we submit that the obligation in Section 16(b) be revised to require that the prescribed disclosure document be sent "not later than midnight on the second business day...".

Section 22 – Liability in Margin Contracts

Section 47 of the Ontario Act addresses the harm of a dealer speculating with a client's security; We note that Section 22 of this regulation imposes new, more detailed requirements; the dealer "must immediately disclose" the facts giving rise to the ability to void the contract; and the client may void the contract by sending written notice within 30 days of the dealer's disclosure. We question the need for introducing these new requirements particularly without the benefit of consultation and input from dealers, investor and other market participants.

Part 6 – Civil Liability for Secondary Market Disclosure

Section 23 – Definitions

While the definition of "equity security" in this regulation is the same as in Section 89(1) of the Ontario Securities Act, we suggest this fundamental definition should be in the CMA as opposed to a regulation.

Conversely, we suggest that the definition of "principal market" should be contained in this regulation as opposed to the CMA. This would parallel the current structure where the definition of principal market is contained in Section 250 of the Regulations to the Ontario Act.

CMRA REGULATION 41-501 – *PROSPECTUS REQUIREMENTS AND EXEMPTIONS AND RELATED POLICY*

Part 1 – Prospectus Requirements

Pursuant to Section 2 of CMRA Regulation 41-501, the Chief Regulator has the ability to refuse to issue a receipt for a final prospectus if *the directors and officers of the issuer lack the knowledge and expertise necessary to conduct the business of the issuer in the best interests of the security holders of the issuer*. We do not believe that the Chief Regulator would be in a better position than security holders or investors to make this determination. We understand that issues may arise during background checks performed by the Authority or other regulators which could raise concerns regarding the suitability of directors and officers. However, a determination of the relevant knowledge and expertise of a director or officer should be left to shareholders and the board, respectively.

Part 2 – Publication of Research Reports During Distributions

Part 2 of CMRA Regulation 41-501 includes provisions dealing with the publication of research reports during distributions, which provisions are similar to those found in OSC Rule 48-501. We understand that the balance of OSC Rule 48-501 will not be carried forward on the basis that similar requirements are imposed on "dealer-restricted persons" under Rule 7.7 of UMIR.

However, OSC Rule 48-501 deals with permitted activities and restrictions applicable to "issuer-restricted persons". Was it the intention of the Authority that these restrictions would not be carried forward under the new legislation?

Part 3 – Trust Indentures

Part 3 of CMRA Regulation 41-501 regulates trust indenture requirements for public offerings of debt securities. The provisions of Part 3 are similar to the current corporate law requirements applicable under the *Ontario Business Corporations Act* (the "OBCA") with a few notable exceptions. We understand that these Part 3 requirements are intended to replace existing trust indenture legislation under the OBCA and other corporate statutes governing indentures for publicly offered securities. We submit that these Part 3 requirements should not replace existing corporate trust indenture legislation and should apply only where corporate trust indenture legislation is not applicable, particularly if the effect any such replacement is that the exemption in Rule 4d-9 of the *United States Trust Indenture Act of 1939* (the "TIA") will no longer be available to Canadian corporate issuers (as their indentures will no longer be subject to the trust indenture legislation referred to in Rule 4d-9). Alternatively, if the SEC will allow for the Rule 4d-9 exemption to apply to indentures subject to the requirements of Part 3 of CMRA Regulation 41-501, we submit that these new requirements should apply only to indentures that are entered into after Regulation 41-501 is effective. The relevant terms of existing shelf indentures for public debt securities will conform to existing trust indenture legislation, where applicable, and may not contemplate amendment (without consent of existing debt security holders) to conform to the changes proposed in Part 3. For issuers with these indentures it would be impractical to require them to obtain the necessary consent for the retroactive application of these new Part 3 requirements.

The OBCA provides that the OSC may exempt an issuer from the trust indenture requirements. Historically, the OSC has granted relief to issuers from the OBCA requirements (including the requirement to appoint a Canadian resident trustee) where the issuer proposes to offer debt securities under an indenture subject to the TIA. We assume that the Authority will continue to grant similar relief following implementation of the CMA and the CMRA Regulations and, in particular, that such requirements will not apply to debt securities that are issued pursuant to MJDS southbound only offerings (see our comments above).

Sections 7(8)-(12) of CMRA Regulation 41-501 outline the procedures for requesting information from a trustee. Section 7(8) requires a trustee to provide a list of certain enumerated information within 25 days after the trustee receives the request. By contrast, the OBCA imposes a 10 day response period from the date that the person requesting the information delivers such request to the trustee. We see no reason why a trustee would need 25 days to respond to such a request. Often this information is being sought in the context of a consent solicitation or change of control transaction and the additional timing requirement could have an adverse impact on the solicitation or transaction. The 10 day period found in the OBCA is similar to the timing requirements for a reporting issuer to deliver a NOBO list under Part 6 of National Instrument 54-101.

CMRA REGULATION 51-501 – *DISCLOSURE AND PROXIES*

Part 2 - Disclosure

Section 3(2) requires Canadian entities that are not reporting issuers but have securities listed or quoted on foreign exchanges to file with the Authority the documentation filed in furtherance of the foreign listing or quotation. We see no reason why the Authority or the public should be entitled to receive this documentation. Section 3(3) deems these Canadian entities to be market participants. We do not believe there is any policy rationale for extending the jurisdiction of the Authority and the application of the CMA to entities that have not accessed Canadian capital markets. These issuers will already be subject to regulation in the jurisdictions in which their investors reside and where their securities are listed.

Part 3 – Meeting Information and Voting

Section 4(2) and 4(4) of CMRA Regulation 51-101 deal only with the distribution of materials "received from the issuer or its agent". This contrasts with Section 49 of the Ontario Act which contemplates that materials may be sent by any "person or company" and not only the issuer. This is an important distinction. Among other things, as drafted, Sections 4(2) and 4(4) would not impose any obligation on a custodian or registrant to forward on to beneficial holders copies of materials provided to the custodian or registrant by other shareholders of the issuer, for example in connection with a dissident proxy contest.

CMRA POLICY 71-601 – *DISTRIBUTIONS OF SECURITIES TO PERSONS OUTSIDE THE CMR JURISDICTIONS*

Distributions-Out

In Ontario, the distribution concept is used to identify the types of offerings where a prospectus or an exemption from the prospectus requirements is necessary in connection with an offering. It is intended to (and should) capture only those circumstances where investors in the applicable Canadian jurisdiction are making an investment decision with respect to securities sold from treasury or by a control person or within a hold period. Accordingly, we submit that the term "distribution" under capital markets law should only capture offers of those securities that are made, directly or indirectly, in a CMR Jurisdiction. The term "distribution" should not capture offers made outside of the CMR Jurisdictions (provided they are not indirect offers within a CMR Jurisdiction) because affording protection to non-resident investors is outside of the scope and purpose of the prospectus requirements. Consistent with the purposes of the CMA, the prospectus requirements are focused on providing protection to investors from unfair, improper or fraudulent practices. The separate objective of protecting the integrity of the capital markets of the CMR Jurisdictions is properly, and adequately, achieved through the broad public interest powers afforded under the CMA – not prospectus requirements.

Where the securities come to rest

To determine whether an offer is made in or outside of a CMR Jurisdiction should be a question of where the subject securities are intended to come to rest. Connections to a CMR Jurisdiction that do not bear on this question should be irrelevant in the context of defining a distribution. Accordingly, at a minimum, we submit that the proposed CMRA Policy 71-601 be revised to:

- remove the 'distribution from / out' provisions (in Section 1 of Part 2) imported from BC Interpretation Note 72-702; and
- replace the 'indirect distribution' provisions (in Section 2 of Part 2) with a guiding principle that, where reasonable steps have been taken in an offshore offering to ensure that the subject securities come to rest outside of a CMR Jurisdiction, that offering is deemed to be outside of the CMR Jurisdictions for purposes of the "distribution" definition.

This is consistent with the guiding principle in OSC Interpretation Note 1.

Consequences of Proposed Approach

Not only is it inappropriate and unnecessary to expand the interpretation of "distribution" beyond the principle established in OSC Interpretation Note 1, it is also impractical. An overly broad definition of "distribution" will lead to conflicts with the securities laws and capital markets practice in other jurisdictions, unnecessary costs and a lack of certainty. As a result, this overly broad approach fails to meet the express purpose of the CMA of fostering fair, efficient and competitive capital markets. The “catch and release” approach proposed by 71-601 leads to a dangerous exercise of attempting to address all of the negative, unintended consequences that arise from an unnecessarily expansive interpretation of "distribution" through exceptions and clarifications - while it is possible to foresee some of these consequences, there will necessarily be other, unforeseen consequences. It is also a wasteful and inappropriate exercise, as any purpose served by an expansive interpretation goes beyond the purpose of the capital markets law expressed in the CMA.

Clarifications in 71-601

We recommend that 71-601 be revised to clarify (i) that the first trade of securities acquired in an offshore offering that is not a "distribution" will not be a "distribution" under capital market law (other than a first trade from a control person's holdings), (ii) Canadian marketing rules apply only with respect to marketing activities to purchasers in a CMR Jurisdiction, and (iii) there is no requirement to include any disclosure in a report of exempt distribution with respect to foreign resident purchasers.

What constitutes a "distribution" should be clearly defined in capital markets laws in order to foster fair, efficient and competitive capital markets. The importance of this concept (and

corresponding consequences) demands a level of transparency and certainty that cannot be achieved through subjective policy measures. In addition to specific regulation establishing appropriate 'safe-harbours' and prospectus exemptions for offshore offerings, as stated above there should be a general deeming regulation that a trade of the type identified as a "distribution" within the meaning of the CMA is a "distribution" for purposes of capital markets law only where it is made within a CMR Jurisdiction and shall be deemed not to be a "distribution" if it is made outside of the CMR Jurisdictions. U.S. federal securities laws limit application of their prospectus requirements through an equivalent general principle established under Rule 901 of Regulation S of the U.S. Securities Act. This general principle is in addition to separate 'safe-harbours' (deeming a trade to be made outside of the jurisdiction and therefore not a distribution subject to the prospectus requirements) established through Rules 903 and 904 of Regulation S.

Responses to Questions for Comments on CMRA Policy 71-601

Our responses to these questions are in the context of the use of a prospectus (via MJDS or otherwise) to qualify an offshore offering that may constitute a distribution (due to a risk that the securities will not come to rest outside the CMR Jurisdictions) but apply equally should the CMR Jurisdictions adopt a “distribution out” approach which, as we stated above, we think is the wrong result. Overall, we believe that all of the exemptions from the prospectus requirements of the type identified in your questions for comment on 71-601 would be necessary. In contrast with your proposals, we believe these exceptions should apply with respect to all foreign purchasers (not just U.S. purchasers) and all foreign underwriters (not just U.S. underwriters or those registered as dealers in the few "foreign jurisdictions" identified in 71-501) that are selling exclusively to foreign purchasers. In addition, these exceptions should not be conditioned on foreign purchasers being provided with substantially equivalent information and rights as would be afforded them if they were a Canadian purchaser in a Canadian prospectus offering, or on the issuer or underwriter complying with applicable foreign requirements in respect of the offshore offering. These limits and conditions are inappropriate as they would only be for the purpose of protecting foreign investors, which is outside of the purpose of the CMA.

Question 1(a) Obligation to Deliver a Canadian Prospectus

We see no benefit to providing foreign purchasers with both a Canadian prospectus and the foreign offering document. This is not only costly for issuers but also confusing for purchasers receiving two disclosure documents.

Question 1(b) Marketing Rules

We submit that issuers and foreign dealers should not be required to comply with Canadian marketing rules in connection with offshore offerings. Regulating marketing activity is intended to provide investor protection. Issuers conducting foreign offerings in accordance with foreign securities laws should only be required to follow local marketing rules, if any. Forcing issuers to comply with two sets of marketing rules, which may be inconsistent, is costly and could impede an issuer from implementing the offering.

Question 1(c) and (d) Statutory Rights of Withdrawal/Civil Liability

Statutory rights of withdrawal do not exist in many jurisdictions outside of Canada. As a result, Canadian offerings are often completed on a longer timeframe (T+5) to allow for the "cooling off" period to expire. Introducing a cooling off period for foreign purchasers will create confusion and may impede current practices for foreign offerings. As stated above, foreign investors should only be entitled to the protections afforded to them under the foreign rules governing the offering. No additional protections, such as rights of damages or recission, should be extended to these purchasers under the CMA.

Question 2 Clarifications Needed

As stated above, the relevant regulations or CMRA Policy 71-601 should clarify that the offshore offering may be qualified by such a 'flow back' prospectus such that any offered securities initially sold to foreign purchasers that 'flow back' into CMR Jurisdictions will be freely tradeable in the CMR Jurisdictions (other than a first trade from a control person's holdings). In addition, there should be an exemption (like the one provided in subsection 4(3) of proposed CMRA Regulation 71-501) from the requirement to include a certificate page in that prospectus for any foreign underwriters of the offshore offering.

Question 3 Dealer Registration

We see no reason why foreign dealers offering securities outside of the CMR Jurisdictions should be required to register under the CMA and corresponding regulations. Imposing such requirements is not only inconsistent with the stated purposes of the CMA but also inconsistent with the current practice in Ontario. Such a requirement would have a chilling effect on the ability of issuers to raise capital in foreign jurisdictions.

Question 4 Imposing 4 Month Hold

Conducting a public offering in one or more foreign jurisdictions by way of a Canadian prospectus exemption is not a viable approach in many circumstances. For example, where equity securities are offered that are to be listed on a foreign stock exchange, it is not commercially viable to apply the Canadian four month hold period to any resale. We submit that this concern is appropriately addressed through the regulatory framework for offshore offerings suggested above. This framework properly limits the definition of "distribution" to offers that are made, directly or indirectly, in a CMR Jurisdiction and affords issuers the ability to use a Canadian prospectus to qualify any offering for which there is a real and substantial 'flow back' risk. Offshore offerings that do not constitute a "distribution" are not made pursuant to a prospectus exemption (as they are not subject to the prospectus requirements) and, therefore, any first trade of the offered securities (other than a first trade from a control person's holdings) would not be subject to a four month hold.

CMRA REGULATION 71-501 – *INTERNATIONAL ISSUERS AND SECURITIES TRANSACTIONS WITH PERSONS OUTSIDE THE CMR JURISDICTIONS*

In addition, while we support the introduction of prospectus exemptions for offshore offerings of the type contemplated in subsections 4(1) and 4(4) of proposed CMRA Regulation 71-501, they are not alone sufficient to address the aforementioned concerns. Even if the 4 month restricted period were the only requirement of 4(1), it is not a workable solution in many circumstances. For example, applying this restriction to securities offered in a public offering conducted concurrently in Canada and offshore (whether in US or elsewhere), or a public offering being conducted exclusively offshore, will mean the securities are not fungible with those already traded over the relevant exchange. However, with some modification, the exemptions proposed subsections 4(1) and 4(4) of 71-501 could afford market participants certainty where offering restrictions are implemented to provide reasonable assurance that the subject securities will come to rest outside of the CMR Jurisdictions but an issuer safe-harbour is not available and qualifying the offshore offering by a prospectus is not a practical option. Key among these modifications is removing the requirement to file a report of exempt distribution or, if required, clarifying that no fees are payable with respect securities purchased by foreign residents and amending the required disclosure for that report such that personal information with respect to foreign resident purchasers need not be included (consistent with current practice). Requiring public disclosure of this private information raises a number of issues, including privacy concerns (the issuer and any underwriter may be prohibited from providing personal information with respect to purchasers under foreign privacy legislation) and commercial concerns (foreign underwriters will not voluntarily reveal their client lists for competitive reasons). Accordingly, if required, it would have a significant chilling effect on foreign purchasers participating in financings using these exemptions. Further, it is unclear what purpose would be served in requiring this disclosure. Notably, there is no equivalent requirement in a public offering. In addition, to accommodate debt or exchangeable security offerings or offerings by subsidiary issuers, condition (d) of subsection 4(1) (having listed equity on a "qualified market") should be removed. This is not necessary in light of the other offering restrictions imposed (particularly the restricted period) and, in many cases, is irrelevant to the 'flow back' risk that should be the focus of this exemption.

For our comments with respect to subsection 4(3) of proposed CMRA Regulation 71-501, please see our comments above with respect to CMRA Policy 71-601.

In addition to our specific submissions above with respect to CMRA Regulation 71-501 and CMRA Policy 71-601, we recommend that the CMR Jurisdictions consider, in consultation with the securities regulators of each other Canadian jurisdiction and Canadian capital market participants, a comprehensive, national framework for governing offerings that are, in whole or in part, made outside of Canada. The Canadian regulatory scheme in respect of offshore offerings requires an overhaul to make Canada's capital markets more transparent, efficient and competitive and bring them in line with more modern approaches applied in other jurisdictions.

The current proposals in 71-601 and 71-501 fall well short of this goal and, worse yet, will make Canadian capital markets considerably less competitive.

We thank you again for the opportunity to comment on the Draft Act and regulations.

Yours very truly,

(signed) Davies Ward Phillips & Vineberg LLP

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