BY E-MAIL December 8, 2014

Cooperative Capital Markets Regulatory System

commentonlegislation@ccmr-ocrmc.ca

Dear Sirs/Mesdames:

Re: Comments on Proposed *Capital Markets Stability Act* ("CMSA") and *Provincial Capital Markets Act* ("PCMA")

We submit the following comments in response to the notice and request for comments published by the Cooperative Capital Markets Regulatory System (the "**CCMRA**") on September 8, 2014 related to the CMSA and PCMA (together, the "**Proposed Legislation**").

We have organized our comments below with reference to the relevant section of the CMSA and PCMA to which our comments relate. All references to parts and sections are to the relevant parts or sections of the applicable rule, policy or form. Where we use comparisons to current securities legislation, such comparisons are to the *Securities Act* (Ontario) (the "**OSA**"), the regulations and the National and Multilateral Instruments associated therewith.

Thank you for the opportunity to comment on the Proposed Legislation. This letter represents our general comments and are submitted without prejudice to any position taken or that may be taken by our firm on its own behalf or on behalf of any client.

1. General

a. *Adoption of National Instruments*

As a general comment, we do not believe that the introduction of the Proposed Legislation, and the PCMA in particular, should be used as an opportunity to introduce substantive changes to Canadian securities laws. This initiative represents a significant change to the regulation of capital markets. Therefore, to ease any regulatory challenges faced by market participants in any transition to this new framework, we would strongly suggest that any substantive changes be deferred so that market participants are able to focus and provide comments at the relevant time. Further, given that the PCMA would form a platform for regulation of the securities markets, and that in many cases (e.g., insider reporting, take-over bids, etc.) the specific rules governing such provisions are being deferred to the regulations, we would recommend that the current National and Multilateral Instruments be adopted in their current form with no changes as much as possible, so as to facilitate, among other things, harmonization of the Proposed Legislation with existing rules and regulations in the non-adopting jurisdictions. To the extent that existing rules

are supported by policy interpretations and/or staff notices, which may be national, multilateral or local only, we also suggest a mechanism be incorporated to ensure that they can be relied upon.

We appreciate that certain changes from the current regulatory regime may not appear to be substantive or otherwise problematic. However, in our view, many aspects of securities regulation are supported by market practice and judicial and regulatory interpretation over time. Therefore, even the slightest change in terminology or structure has the potential to result in a lack of certainty and confusion.

b. Definitions in CMSA and PCMA

We note that the defined terms used in the CMSA and the PCMA are not identical, with the same term having a different meaning in each act. For ease of application, we would suggest using the same definitions in both acts. In the alternative, if there is a compelling reason for using different definitions in each act, we ask that the reasoning be explained.

c. ***Transition***

We note that transition provisions have been intentionally omitted from the PCMA. Noting the complexity of such provisions, we urge that transition provisions be carefully drafted to take into consideration, among other things, the treatment of outstanding cease trade orders, prospectus and prospectus exempt offerings and bids currently in progress, resale restrictions, as well as exemptive relief orders and decisions. As an example of such provisions, we direct you to Appendix D of National Instrument 45-102 *Resale of Securities,* which outlines certain transitional and other provisions related to exemptions from the prospectus requirement in effect on March 30, 2004 (however, hopefully a simpler approach can be adopted in the case of the Proposed Legislation).

d. ***New Offences***

Sections 83 through 85 of the PCMA and sections 60 and 74 of the CMSA create several new offences (vicarious liability, aiding and abetting, conspiracy). These sections should be subject to a detailed request for comments.

e. ***Duplication of Provisions***

We query why certain provisions are replicated in both the CMSA and the PCMA, including, for example, the insider trading and tipping provisions (see section 67 of the CMSA and section 66 of the PCMA). To the extent possible, we suggest streamlining the Proposed Legislation and not duplicating provisions in the acts unless there is a compelling reason to do so.

f. ***Privilege***

We note that there are a number of provisions in the Proposed Legislation that may intrude upon privilege, including solicitor-client privilege. Examples of such provisions include sections 10 [*Duty to provide information*], 16 [*Duty to provide information etc. to auditor oversight organization*], 18 [*Duty to provide information*] and 189 [*Permission to disclosure to Authority*] of the PCMA and sections 9 through 17 [*Part 1 Information Collection and Disclosure*] and sections 54 [*Production order – names*] and 55 [*Order for production*] of the CMSA. Furthermore, some provisions (for example, sections 16(4) and 195 of the PCMA and section 55(3) of the CMSA) protect solicitor-client privilege, but not other forms of privilege, whereas other provisions do not (see, for example section 10 and 18 of the PCMA and sections 9 through 17 and 54 through 55 of the CMSA). We respectfully suggest that all forms of privilege should be protected and the protection of privileged information should apply in all cases of mandatory information sharing and compelled testimony.

g. *Collection of Personal Information*

We note that there are a number of provisions in the Proposed Legislation that provide the Authority with the right to require certain parties to provide personal information, including, for example, sections 12 [*Disclosure of personal information to Authority*] and 14 [*Disclosure of information*] of the CMSA. To the extent personal information can be compelled, it should be lawfully circumscribed and done so in accordance with existing privacy legislation requirements. We would also question whether personal information would be relevant to the Authority's systemic risk jurisdiction.

2. Capital Markets Stability Act

a. *Section 2 – Definitions*

i. *"capital markets intermediary"*

We believe that subsection (b) of the definition of "capital markets intermediary" in the CMSA is too broad and will capture entities such as holdings companies and private equity/venture capital funds. If the intention is to capture these broader types of pooled structures (beyond mutual funds and closed-end investment funds, as is currently the case under the OSA), this definition should be more specifically drafted to address such regulatory interest. As noted above, we believe that this would be an inappropriate substantive change.

b. *Section 10 – Request of Chief Regulator*

We believe that section 10 of the CMSA is drafted too broadly and will require that <u>any</u> person provide the Chief Regulator with records and information. This section should restrict the disclosure requirement to a limited subset of persons, like a "market participant" type of concept.

c. *Section 12 – Disclosure of Personal Information to Authority*

As noted above, to the extent personal information can be compelled, it should be lawfully circumscribed and done so in accordance with existing privacy legislation requirement. We would also question whether personal information would be relevant to the Authority's systemic risk jurisdiction.

d. ***Section 14 – Disclosure of information***

In our view, section 14 of the CMSA is overly broad. To the extent personal information can be compelled, it should be lawfully circumscribed and done so in accordance with existing privacy legislation requirement and not disclosed unless there is a compelling reason. Further, such a broad provision will have a chilling effect on capital market participants, including foreign issuers who may otherwise want to access Canadian markets. There should always be a heightened sensitivity around personal, confidential and/or commercially sensitive information and the onus should be on the party seeking to disclose collected information to show that the benefit of the disclosure outweighs the burden to the party to whom the information pertains, as seems to be the norm under current securities legislation. We also submit that persons subject to this provision should be granted protection of the right against self-incrimination.

e. ***Section 27 – Designation order – systemically important capital markets intermediary***

As currently drafted, section 27 of the CMSA appears to capture non-Canadian institutions. In the case of such non-Canadian institutions, we assume any order designating the institution as systemically important would be done in consultation with the institution's home jurisdiction.

f. ***Section 28 – Content of regulations***

As similarly noted above with regard to section 27, section 28 of the CMSA appears to capture non-Canadian institutions. In the case of such non-Canadian institutions, we assume any order designating the institution as systemically important would be done in consultation with the institution's home jurisdiction.

g. ***Section 65(1) – False information – benchmark***

We believe that section 65(1) of the CMSA, as currently drafted, is too broad. This section represents the introduction of a new "benchmark" concept. To the extent that new subject matter is to be regulated, the related provision should be carefully and specifically drafted and defined in the interest of certainty and to address the risk of over-broad application.

h. ***Section 84 – No destruction, etc.***

We query what "reasonably ought to know" means in the this circumstance and further query whether a person can "reasonably ought to know" that an

investigation "is likely to be conducted". We suggest that this section of the CMSA is too vague and too broad. A known current investigation should be used.

i. *Section 73 – Threats and retaliation against employees*

Section 73 of the CMSA creates a criminal offence respecting whistle-blowers, and among other things, seems to apply even where the whistle-blower in question is not acting in good faith. We also query whether this provision precludes customary confidentiality agreements and suggest that this section be subject to a detailed request for comments.

3. Provincial Capital Markets Act

a. *Section 2 – Definitions*

i. *"investor relations activities"*

The PCMA includes a definition of "investor relations activities" that is separate and apart from the definition of "trade". In our view, the regulation of investor relations activities could imply that such activities are no longer considered to be trading (i.e., no longer captured under part (g) of the definition of "trade" – any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of a trade) but that such activities could potentially capture normal analyst activity, rating agencies and newspaper websites (which are frequently not paid for). We note that the addition of this definition and the related provisions of the PCMA (see section 74) should be the subject of a detailed request for comments and a cost/benefit analysis.

ii. *"market participant"*

Many elements of this definition are new and, we submit, extend the jurisdiction of the Authority in a broad manner over certain types of actors whose connection to Canadian capital markets is arguably too tenuous to justify such broad application. These include actors such as: an issuer who has filed a preliminary prospectus; a person engaged in investor relations activities; a person who is exempt from the requirement to be recognized under capital markets laws; and a person distributing or purporting to distribute securities in reliance on an exemption from section 27 or an exemption in an order made under section 94.

In particular we have specific concerns with respect to the exercise of such power over an issuer who has only filed a preliminary prospectus given that no public distribution of securities would have been made until a receipt for a final prospectus is issued, such an issuer may never become a "reporting issuer," and to the extent the Authority needs to exercise any power to obtain information from such issuer it can do so though the prospectus review process. We also do not believe that an issuer who relies on a prospectus exemption to distribute securities should be subjected to the power of the Authority to review books and records and compel information is the case for other types of market participants. Given that this

would include all sizes of private companies as well as foreign issuers (whose connection to Canadian capital markets may be as tenuous as, for example, relying on a prospectus exemption to issue stock options and underlying shares to employees), we question both the need and utility of subjecting such issuers to the jurisdiction of the Authority in this manner.

In addition, we note the expansion of the definition of "market participant" to include a reporting issuer's control persons. This expanded definition would now mean that control persons are, among other things, required to keep records necessary for the recording of their business transactions and financial affairs and other records required under capital markets law for a period of 6 years (section 54); provide such records to the Chief Regulator (section 54(3)); provide the Authority with any information, record or thing in the control person's possession in connection with the administration or enforcement of securities or derivatives laws or the regulation of the capital markets of another jurisdiction (section 102); and pay fees associated with certain reviews (section 103). In addition, the Tribunal would be permitted to make an order that the control persons submit to a review of, or make changes to, its practices and procedures (Section 89); and designated persons would be permitted to review the business and conduct of a control person, including to enter the control person's business premises (section 103). By including control persons in the definition of "market participant", large, yet passive, investors with little more knowledge about an issuer than other investors may be subject to a number of requirements with little benefit to the capital markets regime. In addition, we query whether persons whose only participation in capital markets is as an investor should be held to the same high standards as market participants. To the extent there is a compelling reason to include control persons in any of the provisions noted above, it should be done with respect to the specific provision and not by blanket inclusion of a control person through the use of a defined term. We once again note that substantive changes to the current regulatory regime should not be undertaken at this time and that even the slightest changes can have a significant effect on capital markets participants.

iii. "*marketplace*"

We note that the definition of "marketplace" in the PCMA is narrower than the definition of such term in the OSA in that it applies only to securities and query whether this is an intentional omission so as not to include marketplaces for derivatives trading in this definition. In this respect we also suggest that the term "exchange" (as used in section 8 and elsewhere) should be a defined term.

iv. "*misrepresentation*"

We note that under the OSA a "misrepresentation" includes "an untrue statement of material fact", whereas the PCMA includes "a false or misleading statement of material fact" which is arguably a broader definition. We note that even the seemingly slightest changes to this definition could have detrimental effects given that this is a term that has been subject to much scrutiny and interpretation over time.

v. *"related financial instrument"*

This definition incorporates the concept of an instrument whose market price, value, delivery obligations, etc., "vary materially" with the market price, value, delivery obligations, etc. of another security. This represents a departure from the definition of "related financial instrument" in National Instrument 55-104 *Insider Reporting Requirements and Exemptions* and incorporates the concept from the broader definition of security that is used for the purposes of the insider trading provisions of the OSA. In our view, this is an ambiguous concept that has caused a significant lack of certainly and difficulty with application given that there is no further interpretive guidance on what would be considered to be a "material variance." This gives rise to issues, for example, with respect to trading in or through indices, derivatives or other types of synthetic exposures where a subject reporting issuer's securities may represent a portion of the instrument that is actually traded and may disadvantage market actors from engaging in capital markets activities that do not otherwise offend the policy rationale underlying the prohibition.

vi. *"subsidiary"*

We question the broadening of the definition of "subsidiary" to include an issuer who is "controlled by *one or more other issuers*" [emphasis added]. Guidance on the application of this concept is required, particularly with regard to whether the other controlling issuers would have to act jointly, the percentage of securities each controlling issuer would need to hold to be considered in control of the issuer (i.e., if two issuers each hold 25% of another issuer but are not acting jointly, is the third issuer a subsidiary of each of the first two issuers?) and other indicia of control. We support the inclusion of a "jointly or in concert" concept.

vii. *"take-over bid"*

While we recognize that many of provisions of the PCMA will be included in regulation, the definition of "take-over bid" appears to capture any offer to acquire securities of an issuer, regardless of the number of securities being acquired. This is inconsistent with the current definition of "take-over bid" in the OSA and Multilateral Instrument 62-104 *Take-Over Bids and Issuer Bids* which both require that the securities subject to the offer, together with securities currently held by the offeror, constitute in the aggregate 20% or more of the outstanding securities of the issuer. As such, under the PCMA any offer to purchase a security could potentially trigger extensive compliance requirements. We assume the intent is not to change the current regulation and to keep the take-over bid threshold at 20%, but in our view, such a fundamental component of the take-over bid regime should be in the PCMA itself and not in the rules, and therefore subject to a more burdensome process of amendment.

b. *Section 28 – Restriction on distribution of information, record or thing*

We question the need for the prohibition under section 28 given that the prospectus requirement should be sufficient alone and particularly given the new range of "pre-marketing" exceptions that have been codified into National Instrument 41-101 *General Prospectus Requirements* and submit that to the extent the current intention is not to prescribe what will be prohibited, such a provision will only lead to ambiguity and lack of certainty.

c. ***Section 32 – Requirement to provide further information, etc.***

We believe that prior to imposing addition filing requirements or conditions on a prospectus offering, issuers should be given an opportunity to make representations and/or be heard. The receipt is a fundamental component of the prospectus process. As such, we recommend greater certainty in this process so as to avoid any actual or perceived exercise of the Chief Regulator's authority in an arbitrary manner. Regulatory certainty and consistency in these matters should always be the guiding principle.

d. ***Section 45 – Information from directors, etc.***

We query whether the type of information contemplated to be provided to the Chief Regulator in section 45 of the PCMA is similar to the information currently required by a personal information form and we submit that as currently drafted, this section is overly broad and open ended. While providing information in a personal information form is understandable, particularly as parties subject to the personal information form requirement are aware of the information to be provided in advance, under this section, the information required is unknown and such requirement may have a chilling effect on capital markets activities, particularly with regard to non-Canadian directors, officers, promoters and control persons. We further submit that information subject to privilege should not be compelled by the Authority.

e. ***Section 52 – Application to Tribunal – compliance orders***

With respect to section 52, we assume that the Tribunal will be informed by existing jurisprudence and expertise built upon the regulatory decisions of the major capital markets jurisdictions, especially in its early years of operation, in order to provide a certain level of consistency. We query whether the Authority may be the appropriate body to undertake this role.

f. ***Section 58 - Conflicts of interest – offeror, etc.***

Section 58 of the PCMA introduces new obligations in respect of various transactions, some of which are undefined, and some of which do not correspond with similar definitions in MI 61-101 (e.g. going private transaction). For example, how could an offeror making an insider bid "manage" its conflict of interest and what does this mean? This section should be subject to a detailed request for comments and cost/benefit analysis.

g. ***Section 60(4) – Prohibited representation – exchange***

We recommend that this prohibition (on making such representations as to listing) would more properly be codified in the rules as opposed to the PCMA. This could then permit for flexibility with respect to, for example, foreign issuers who are permitted to make such listing representations, do not fall within the prescribed exceptions and are routinely required to apply for exemptive relief from such a prohibition.

h. ***Section 62 – Market manipulation***

Currently, the OSA requires that, in order to be in contravention of the market manipulation prohibition, a person must "know or ought to know" that his, her or its conduct results in or contributes to a misleading appearance of trading activity. In our view, the PCMA should include such a knowledge qualifier in section 62. We would suggest adding the work "knowingly" after "must not" in section 62(1).

i. ***Section 63 – Unjust deprivation, fraud***

Section 63 appears to create an offence of "negligent fraud". As similarly noted above with regard to section 62, we submit that in order to partake in fraud, a person must have scienter. Fraud has generally been seen to require *mens rea.* We would suggest adding the word "knowingly" after "must not" in section 63(1) and further suggest that this section should be subject to a detailed request for comments and a cost/benefit analysis.

j. ***Section 66(1) and (2) – Insider trading and tipping***

As currently drafted, the insider trading prohibition in the PCMA has been significantly expanded from what is currently found in the OSA and other provincial securities laws and includes trades in securities of both reporting and non-reporting issuers (who securities are publicly traded) and "entering into transactions" with related financial instruments (a concept which may be less than an actual trade in a security). In addition, section 66 extends the prohibition to a "purchase or trade" of a security as opposed to a "purchase or sale." In our view, given the expansive definition of trade, we do not agree that it is the proper term to use in this context as it unduly expands the restriction and will lead to issues with interpretation and application. It is also not clear why the prohibition has been expanded apply to an issuer "whose securities are publicly traded" which, in our view, creates further ambiguity. Similarly, the prohibition on tipping includes a restriction on non-reporting issuers. Given that the insider trading and tipping prohibitions are a fundamental part of securities legislation with a large body of judicial and regulatory interpretation, we would recommend maintaining the regime as it currently exists.

k. ***Section 66(4) – Recommending***

Section 66(4) of the PCMA introduces a new restriction into securities law as compared to the current regime under the OSA. As previously noted, substantive changes to securities laws may result in significant and burdensome effects on capital markets participants and should be carefully drafted and given proper consideration (with a specific request for comments) prior to implementation.

l. ***Section 67(2) – Connection to investor***

The definition of "connected to an investor" found in section 67(2) of the PCMA is overly broad and should exclude an issuer's personnel as well as persons engaged in a distribution.

m. ***Section 68 – Defences***

We do not agree that the defences to insider trading and tipping should be codified in the PCMA. Capital markets trading activity continues to grow in terms of its sophistication and complexity. The defences that have been included, particularly sections 68(3) and (4) are, in our view, no longer reflective of the types of trading that may be "automatic" and/or carried out through an agent and give rise to significant issues with interpretation and application to trading activities that do not amount to insider trading. We further submit that in this respect, capital markets laws need to be flexible and adaptive to change in order to remain relevant and to provide the proper framework for trading activities. We therefore strongly urge the CCMRA to consider a more flexible approach that allows for these provisions to be more easily adapted as capital markets activities continue to evolve.

n. ***Section 76 – Obstruction***

We query what "reasonably ought to know" means in the this circumstance and further query whether a person can "reasonably ought to know" that an investigation "is likely to be conducted". We suggest that this section of the PCMA is too vague and too broad. A known current investigation should be used.

o. ***Section 81(3) – Onus***

Section 81(3) of the PCMA seems to create a new reverse onus provision whereby a person who wishes to rely on the exception to the rule must prove that they did not know that he/she/it had made a false or misleading statement. This section should be subject to a detailed request for comments.

p. ***Section 90(2) – Compensation or restitution***

Section 90(2) of the PCMA creates a new restitution/compensation power for the Tribunal. Given the existence of other penalties, which may include compensation (see for example, ss. 115, 129, 130(2) and 132 of the PCMA), this may lead to inappropriate penalties. There are also no parameters to this new power, such as regarding indirect, consequential, punitive or other damages. This section should be subject to a detailed request for comments.

q. ***Section 96(1) – Duration of class orders***

Given that section 97 of the PCMA does not appear to apply to Part 10 of the PCMA, we query whether section 96(1)(b) of the PCMA is intended to create a hard 36 month maximum and further query whether this is a desirable outcome.

r. ***Section 103(6) – Review of Market Participant – Authority to inquire***

As currently drafted, section 103(6) of the PCMA authorizes designated persons with administrative or enforcement power to make inquiries of persons under review or its employees, agents, officers, directors or control persons concerning business or conduct that reasonably relates to the review. We question whether there is a compelling reason to include control persons in this provision and whether persons whose only participation in capital markets is as an investor should be held to the same high standards as market participants.

s. ***Section 105 – Duty to assist***

As currently drafted, section 105 of the PCMA authorizes designated persons with administrative or enforcement power to make inquiries of persons under review or its employees, agents, officers, directors or control persons concerning business or conduct that reasonably relates to the review. We question whether there is a compelling reason to include control persons in this provision and whether persons whose only participation in capital markets is as an investor should be held to the same high standards as market participants.

t. ***Section 122(1) – Actions relating to prescribed disclosure document***

The expansion of liability in section 122(1) of the PCMA to "every person who, on the date of the prescribed disclosure document, was a director of the issuer" and to "every person who signed the prescribed disclosure document" represents a significant change from the provincial capital markets legislation in many provinces, including Ontario (in, for example, expanding the liability associated with an offering memorandum to all directors of the issuer). As set out above, we not agree that such substantive changes should be made via implementation of the PCMA without a proper opportunity for review and comment.

u. ***Section 129 – Action for damages – insider trading , etc.***

We believe that section 129 of the PCMA is too broad and captures damages to anyone who purchases or trades within the time period regardless of whether the trade was with the person who contravened section 66 of the PCMA (the insider trading, tipping and recommending provision). This section represents an extreme expansion of liability from that currently in the OSA. Such expansion should not be undertaken without the proper opportunity for consultation.

v. ***Section 130 – Payment of benefit – insider trading, etc.***

In our view, section 130 of the PCMA is too broad and captures damages to anyone who purchases or trades within the time period regardless of whether the trade was with the person who contravened section 66 of the PCMA (the insider trading, tipping and recommending provision). This section represents an extreme expansion of the current related provision in the OSA. Such expansion should not be undertaken without the proper opportunity for consultation.

w. ***Section 200 – Collection from third party***

We query whether section 200 of the PCMA overrides the rights of secured creditors, unsecured creditors, employees, trust beneficiaries, etc. Our view is that this section should be subject to a detailed request for comments.

x. ***Section 201 – Immunity from proceedings for damages***

Section 201 of the PCMA (unlike section 106(2) of the CMSA) does not grant immunity to persons intending to comply with securities laws as is currently provided in section 141(2) of the OSA, a provision which assists greatly in enabling compliance with laws. We recommend continuing the status quo in this regard and including a similar provision in the PCMA. Section 201 of the PCMA also provides immunity to SROs and other private parties, which, given their substantial powers, is a substantial change to Ontario securities law and should be subject to a detailed request for comments.

y. ***Section 203 – Incorporation by reference***

Our view is that public access to materials incorporated by reference pursuant to section 203 of the PCMA should be without cost.

z. ***Section 205 – Notice of proposed regulation***

Our view is that access to proposed regulations pursuant to section 205 of the PCMA should be without cost.

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Thank you for the opportunity to comment on the Proposed Legislation. Please do not hesitate to contact any of the undersigned if you have any questions in this regard.

Yours truly,

Laura Levine
Simon A. Romano