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# General Purpose of Securities Regulation

* Securities regulation is protective, not punitive, so broad definition is appropriate
  + Want to be looking forward, not retroactive
  + Wants to protect the *investing* public, not the public generally
* Regulation purpose is twofold

### Protect investors

* + - Doesn't mean protecting investors from losing their money (risk is correlated with return)
    - Just means make sure investors have access to the information they need to make an informed decision
    - Doesn't tell investors what to do
    - Premised on the idea that the market is going to a better job of indicating risk than a SR

### Foster fair and efficient markets

* + - The financial crisis was produced by the inability of regulators to control systemic risk
    - Three ways:
      * Registration of persons - there are a bunch of rules which apply
      * Regulations around issuers and securities - disclosure based (must provide information)
      * Anti-Fraud measures- provisions in securities acts to regulate fraud
* Regulatory regime can be divided into three branches:
  + Registration of Persons
  + Registration of Issuers and Securities
    - **An issuer or control block issuer must qualify an acceptable prospectus with the Commission for all *securities* being *distributed* to the public for the first time. After a *distribution*, RIs (but not control block issuers) must make a periodic and timely continuous disclosure about their affairs and management. Directors and officers must ensure proper disclosure and meet certain standards regarding personal *trades* in the issuer’s securities.**
  + Anti-fraud
* Twin Peaks regulator
  + One side is in charge of consumer protection
  + The other side is focused on safety and soundness, prudential
* Definitions are over broad to avoid excluding anything
  + Exclusions are set out in legislation - "catch-then-exclude" strategy

# Types of Securities

### Debt securities:

* + Debt based securities: commercial paper, bonds and debentures
    - Commercial paper- IOU, investor buys, agreed on maturity date to pay back with interest, no interest along the way, and is unsecured, and is usually short term (270 days)
      * Now it operates quite differently
    - Bond - Secured against some asset, company would need to talk to a credit rating agency since they are long term commitments, get fixed income along the way, good way of raising money
      * Government often sells bonds
      * Bond market is its own creature, they do not operate on exchange but through a broker
      * Bond indenture- investor has rights if company goes bankrupt, take pretty high up on the list
      * Convertible bond- bond that can turn into a share
      * Warrant- Option to buy shares at a certain price and certain time
    - Debenture - Unsecured, bigger interest returns
    - Bank Loan

### Equity securities:

* + - Investor is giving company money in hope that there will be future property
    - Take much greater risk than those buying debt based securities
    - Often retail investors (non-professionals instead of institutional investors)
  + **What is a share** - right to share in profits of dividends of the company
    - Proceeds upon wind-up or dissolution (after secured investors are paid)
    - Common shares
      * Right to vote
      * Right to dividends (or “stock dividends” – dividends paid in the form of shares of the company)
      * The Liquidation right –common shares are entitled to share pro rata any proceeds of the liquidation (after other claims)
    - Preferred shares - for the money partner, i.e. venture capitalists
      * May get better dividend or asset rights than common shares
      * Usually non-voting
        + Cumulative (vs. Non-cumulative) – if in a year dividends are either not declared or not sufficient to pay the full amount of the annual preferred dividend on the preferred shares, the amount unpaid carries over into the next year
        + Participating (vs. Non- participating) – participate in dividends beyond the specified preferred amount they are to receive in any given year.
        + Redemption/Call Provision – allows the company to buy back the shares from shareholders at some future date for a specified price (if want to refinance)
        + Retraction Rights – permits the shareholder to tender the share to the company and the company has to buy back at some priced specified in advance.
    - Restricted shares - restrictions on voting rights, transfer of the share
      * Have a right to pro rata share in dividends and on distribution of the proceeds of liquidation, but voting is restricted (used to raise money w/o giving up control)
  + **What is a right** - a right is a right of a shareholder to buy more shares in a particular offering
    - Holders of a specified number of rights will have the right to buy a share in the company for a predetermined price within a certain period of time
    - Rights to buy shares are normally tradable
  + REIT - Real estate investment trust, different structure where the trust sells units to unit holders
    - Used to be much less taxable, might still be at the corporate level, however there are different rights

### Derivative securities:

* + Can build them any way you can possibly imagine
    - Equity derivative
    - Debt Derivative

# “Security”, “Trade”, “Distribution” Definitions

#### **SECURITY** defined s.1 of *Act*

### An Instrument Commonly Known as a Security

* + - **"any document, instrument, or writing commonly known as a security"**
      * **Common knowledge is defined as knowledge that is common among securities professionals (*Re John T Gelderman & Co. Inc.*) or "knowledge that is common among members of those communities" *SEC v Glenn W Turner Enterprises***

### An evidence to title to or an Interest in Property

* + - Includes "document constituting evidence of title to or interest in the capital, assets, property, profits, earnings or royalties of any person or company"
    - Test- whether a "document" shows some form of investment or speculation
    - *Swain v Boughner*- One-half interest in a pair of breeding chinchillas was held to constitute a security
    - *Brigadoon*- receipts were held to be securities because they were bought and sold as an investment
    - No actual document needed
    - When considering franchises, the amount of control the franchisee has over its investment will likely determine the issue - *Re Century 21 Real Estate Corporation*
    - Whether or not the instrument creates a speculative interest or not

### An Option, a Subscription, or a Right

* + - "evidence of an option, subscription or other interest in or to a security"
    - An option is a form of derivative, and a contract that entitles but does not require its holder either to buy or sell a particular security on a particular date at a specified price
      * A "put" option entitles the holder to sell a security
      * A "call" option entitles the holder to buy a security
      * A "writer" creates the option and sells it to a buyer, who can in turn sell it to other investors
      * "Subscriptions" are "sign-up" forms for purchasing securities
      * "Rights" to purchase a specific number of additional securities for a specific price and time period. Exercise price is discounted from the prevailing market price at that time
      * "Warrant" are attached to bonds and give the warrant-holder the right to purchase a specific number of the corporation's equity securities at a specific price and during a specific time period

### A Debt Security

* + - A "bond, debenture, not or other evidence of indebtedness" is a security
    - There is a rebuttable presumption that certain types of notes are securities, four factors are relevant in determining whether that presumption has been rebutted (*British Columbia (Securities Commission) v Gill*:
      * The motivations that would prompt a reasonable seller and buyer to enter into the transaction
      * The intended distribution of the instrument, - is it for common trading, speculation, or investment?
      * The reasonable expectations of the investing public
      * The existence of another regulatory regime
      * **Purpose of the indebtedness**

### A proportionate interest in a Portfolio of Assets/Mutual Funds

* + - "Any agreement under which the interest of the purchaser is valued for purposes of conversion or surrender by reference to the value of a proportionate interest in a specified portfolio of assets"

### Any profit-sharing agreement or certificate

* + - Not used very often any more as almost everything in this fits under (l)

### An Investment Contract

* + - Contains transactions that seem to involve a security but take an unusual form
    - ***Pacific Coast* is leading case, but substance was held to trump form, and US Jurisprudence was looked at. Common enterprise (Howey) and risk capital (Hawaii) are helpful, it is not strictly necessary that either be satisfied. What is necessary is finding the contract in question to be an investment contract would support and advance the policy goals of securities regulation generally. Is to be interpreted broadly and flexibly.**
    - Howey- **common enterprise test** 
      * Citrus grove in Florida
      * You could buy land in the citrus grove
      * Contract would be that they would take care of the trees for you, but you would buy the land
      * The produce would be pooled and sold under the caretakers name
      * Each investor would get their share of the profit
      * Attracted by the expectation of profit
      * Said that it is a "**contract, transaction or scheme, whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of a third party**"
      * **Two part test: 1) there must be a common enterprise 2) profits will come solely from the efforts of people other than the investors**
      * More than just buying an interest in land
* Hawaii Market Ctr 1971 - **risk capital test**
  + Focuses on the fact that you are putting capital into a risky thing
    1. Risk to investor is really what securities regulation is trying to take care of
  + They were going to open a retail store by recruiting "founder members"
  + Max 5000 members
  + Pay 320, get a 70 dollar appliance
  + Incentives every time you get someone else to join
  + It's trying to get money at the beginning and membership base
  + Argued that members are not expecting profits solely from the efforts of a third party
  + Court stated *Howey* definition was too narrow, need to look at the economic reality
    - **Test: 1) Offeree furnishes initial value 2) At least some of that money is risked by the enterprise 3) You are doing it based on the promises or representations that lead to a reasonable expectation of profit 4)No day-to-day managerial control by the investor**
* Pacific Coast - margin purchases were investment contracts
  + Selling silver coins
  + Inevitable increase in silver
  + Pacific coast got a commission whenever silver was bought or sold from them
  + You could only buy or sell your coins to or from them
  + Says that it is a security because this is about speculating the price of silver on the market
  + Don't need a horizontal structure for common enterprise, can be vertical
  + Laskin dissents:
    1. They don't control the value of silver
    2. If this is a security, too many things in the world will be a security
    3. The market is what determines the return of money, not pacific coast
* Lazerman- BCCA 1985
  + Silver bar exchange
  + Segregated one person's silver bars from the other
  + Didn't share common enterprise because they were each person's bars

### An interest in an Oil, Gas, or Mining Claim

* + "certificate of interest in an oil, natural gas or mining lease, claim or royalty voting trust certificate" and "oil or natural gas royalties or leases or fractional or other interest" in either

#### TRADE defined in s.1 of *Act*

* + The broker is the trader, pulls the broker into it and makes them liable (called registrant)

### A disposition of a security for valuable consideration

* + Includes "any sale or disposition of a security for valuable consideration", regardless of the method of payment, "but does not include a purchase of a security or… a transfer, pledge, or encumbrance of securities for the purpose of giving collateral for a *bona fide* debt". It is a trade to sell a security but not a trade to buy a security
  + A disposition of a security is not a trade if the transferee does not provide valuable consideration - *Re Anchor Machine & Manufacturing Ltd.*

### Entering into or Disposing of a Derivative (future)

* + "Entering into a derivative or making a material amendment to, terminating, assigning, selling or otherwise acquiring or disposing of a derivative"
    1. Includes acquisitions of derivatives
    2. Also contains no requirement that the disposition be for valuable consideration
    3. An act performed by a trader through a marketplace
  + "any participation as a trader in any transaction in a security…through the facilities of an exchange"
  + Captures activities of an agent or broker

Participation as a trader in a transaction in a security or exchange contract made on or through the facilities of an exchange or reported through the facilities of a quotation and trade reporting system

### A receipt by a dealer of an order

* + "receipt by a registrant of an order to buy or sell a security"
    1. Occurs when a broker *receives* the order

A transfer or pledge of securities from a control person's holdings for the purpose of giving collateral for a debt

* + Any "transfer, pledge or encumbrancing of securities of an issuer from the holdings of a control person for the purpose of giving collateral for a *bona fide* debt" is also a trade.
    1. A "**control person**" is a person who can materially affect the control of an issuer (or has more than 20 per cent of an issuer's voting rights).

### An Act in Furtherance of a Trade

* + Any "act, advertisement, solicitation, conduct or negotiation directly in furtherance of any of the other branches is itself a trade".
  + No actual trade need ever be completed for there to be a "trade" under this branch
  + Question of fact and context - *Re Costello*

### Geographical Limitations

* If the trade crosses provincial borders, then very often it is the buyer's jurisdiction, since it is largely based on consumer protection
* If trade crosses international borders, then the US will assert their jurisdictional laws
* A transaction that involves these is subject to the full range of securities regulation
* Definitions are over broad to avoid excluding anything
  + Exclusions are set out in legislation - "catch-then-exclude" strategy

#### DISTRIBUTION

* All distributions are trades, in that they have transfer of security for valuable consideration, but not all trades are distributions
* Only to primary market

Criteria:

* 1. a trade in securities that have not previously been issued (i.e., that are new to the market)
  2. a trade by the issuer in its own previously issued securities;
  3. a trade by a control block person in previously issued securities;
     + 20% shareholder, or less depending on situation (14.6% *Re Deer Horn Mines Ltd*)
  4. Resale of previously exempt securities
  5. any trade that is a distribution under the regulations; and
  6. any transaction involving a purchase and sale or a repurchase and resale during distribution or incidental to distribution.
* Must complete a prospectus before distributing shares
* Direct issue
  1. Issuer makes direct contact with the purchaser
  2. Rights offering is an example
  3. Or exempt offering

Underwriting arrangements:

* 1. "bought deal offering" (market deal) - underwriter commits to buy the entire issue at a set price before preparing the prospectus or canvassing interest among potential investors
  2. "marketed deal offering" - underwriter does not purchase until it has had a chance to assess market demand
     + Guarantee a floor, if there are unsold securities they will pick up that slack
  3. "best efforts" - risk remains with issuer, underwriter receives commission
  4. Can use "out clauses" to avoid risk due to unforeseen or drastic events
     + “material change out” “due diligence out” “tax changes out” etc.

# Primary vs. Secondary Market

**Primary Market**

* Primary market transaction is a **distribution** of securities, from an issuer directly to the public
  1. See definition of distribution above
  2. Done through IPOs
* **Private placement** is when the issuer sells securities directly to specific investors, usually institutional investors, under a specific head of exemption

**Secondary Market**

* Securities bought and sold without any involvement of the issuer (unless it is repurchasing)
* First submarket is registered stock exchanges (TSX)
* Second submarket is the unlisted market
* Third market is “face to face” or “computer to computer” trading of *listed* securities between institutional investors
  1. Smaller, less liquid, less transparent
* Fourth market – same as third but without dealers

# Materiality

* Material Fact - when used in relation to securities issued or proposed to be issued, a fact that would reasonably be expected to have a significant effect on the market price or value of the securities (*BCSA* s.1) – **market impact test**
  + Key element in prospectus –“full true and plain disclosure” of all “material facts”
* Material Change - A change in the business operations, capital of the issuer, that would reasonably be expected to have a significant effect on the market price or value of a security of the issuer (*BCSA* s.1)
* Material fact is static and broad, a change is a difference in something and narrower
* NP 51-201 s.4.2 provides guidance on materiality
  + Factors relevant to materiality: nature of information itself, price volatility of the issuer’s securities, prevailing conditions in the market and the size and nature of the issuer itself
  + Material includes:
    - Acquisitions and dispositions
    - Changes in Credit Arrangements
    - Changes in Financial results
    - Changes in capital structre
  + Material does not include:
    - External Political, Economic and Social Developments (no disclosure required)
* Pezim(1994) – Leading case
  + First set of mining survey results suggested a lot of gold were in the hills
  + Second survey indicated that there wasn't as much gold in the hills
  + They sell their shares before revealing the second results
  + Don't have to disclose material facts, only material changes
  + This is a material change since in the mining industry mineral property is constantly being assessed by investors
* Siddiqi(2005)
  + At what point do negotiations crystallize into a material change
  + **They were material as soon as there was a sufficient degree of certainty that the transaction would be completed**
    - In this case a hand shake deal
* Kerr v Danier Leather(2007)
  + Danier issues a prospectus on a new class of securities
  + There was warmer weather than expected, and the internal analysts expected less sales than normal
  + Danier decided it wasn't a material change
    - Didn't reveal change during distribution period
  + Prospectus is a snapshot in time, must disclose all material facts at the time of the prospectus
    - There is an implied expectation of reasonableness in the assumption
    - It was just a forecast, not an actual change in the business
  + The business judgment rule doesn't get you out of your legal obligations
* Re Donald(2012)
  + RIM VP purchased securities of Certicom with knowledge of MNPI while in a special relationship
  + Was proposing to make a take-over bid for Certicom
  + Information given at the dinner was “non-specific, conjectural, full of opinion and publicly available”
  + Evidence was that RIM had not made a decision as to purchase of Certicom at time shares were bought by Donald
  + Wasn't at proposing stage yet
  + For the proposing requirement to be met “there must have been some significant level of involvement and approval of the process at the highest corporate levels of RIM”
  + Court held there wasn't a special relationship at the time

# History/Future/*Reference Re Securities Act*

* Canada is the only industrialized nation without a national securities regulator
* *Hawkin* recommended unilateral federal action in a federal statute
  + Led to Canadian Securities Transition Office
  + Had the job to draft a national statute
* May 2010, fed. Gvt. Referred the Proposed Act to the SCC

## Reference Re Securities Act

* The federal claim was under s.91(2) general trade and commerce
  + Five part test for whether something falls within fe
    - Is the impugned law part of a general regulatory scheme? Yes
    - Is the scheme part of a general regulatory agency? Yes
    - Whether leg is concerned with trade as a whole rather than a particular industry? No
      * Took up too much provincial space
    - Could the provinces acting together do this or would they be incapable? Partial win for the feds
      * The act covered more things than it should have
    - Whether the failure to include one part would jeopardize the operation of the others? Maybe
      * Again, overreaching
* Opposition stated:
  + Enforcement is poor
  + Risk for Canadian companies that it might be a fraudulent company due to lack of enforcement
  + Therefore, if you have an identical company in Canada and US, Canada company might be worth less
* Anti-regulation arguments:
  + If you have 13 bodies working on regulating securities you get parallel learning experiences
    - One jurisdiction can learn from others
  + The provinces are diverse
  + Economies and politics are different across the country
  + There is no problem that a national regulator could solve that a provincial regulator couldn’t
* Even if national regulator had been created, it would have been concurrent
  + Would have had 14 regulators
* Ended up with a cooperative federalist model
  + The provinces continued to have jurisdiction over day-to-day operation of the markets
  + The feds get jurisdiction over monitoring systemic risk and data collection
  + Systemic risk are things that provinces can't control
  + The proposed federal act allows the feds to designate something as systemic risk

### Passport system (MI 11-102, Passport System and Companion Policy 11-102CP)

* Principle regulator (usually in place of headquarters) and host regulator (where business is occurring)
* Does not include Ontario
* Ongoing questions about what harmonization looks like
  + What about if a national instrument is enforced differently in different provinces
* Memorandum of agreement covers the nuts and bolts of how it is going to work
* If it is to pass, there will be a uniform provincial securities act
  + Covers day-to-day operations of the markets
  + Agrees to delegate enforcement to Canadian Capital Markets Regulator (CCMR) or Capital Markets Regulatory Authority (other name) (CMRA)
* Idea is that it is eventually going to be self-funding
* Proposal moves towards bifurcation

# Prospectus Requirements

* NI 41-101 s.7 *General Prospectus Requirements*, Form 41-101F1 sets out requirements
  + RI can apply to principal for local jurisdiction requirement exemption (MI 11-102)
* Absent exemptions, a prospectus must be registered in the Canadian jurisdiction in which the issuer wishes to distribute the securities (s.61 *BCSA*)
* Should be capable of being read by investors generally
* Full, true, and plain disclosure of all material facts (s.63 *BCSA*, NI 41-101 s. 7.02)
  + Full- made of facts sufficient to permit investors to make an informed decision
  + True- accurate and not misleading, and does not omit a fact
  + Plain- must be understandable to investors and in plain language
* First prospectus is an IPO
  + It is then a reporting issuer in that jurisdiction
  + Long Form Prospectus
* Underwriters due diligence efforts are essential to its potential liability
* Auditors and creditors must provide certificates
* Prospectus must disclose consent from any third party information (lawyers, engineers etc.) and if they have an interest or position with the issuer
* Executive director retains some discretion

### Procedure

* Preliminary "red herring" prospectus
  + Contains essentially all the information that will be in the final prospectus, except price of securities and related matters
* Waiting Period - time between when the issuer receives a receipt for preliminary prospectus and a receipt for its final prospectus, makes comments and revisions
  + **Executive Director holds discretion to issue receipt,** “shall” issue unless it appears not to be in the “public interest to do so” (s.65 *BCSA*)
  + Investment dealers can provide a significant amount of information to all investors during the waiting period
    - "road shows" (NI 41-101 13.9)
    - "Green Sheets" - ten page summaries of preliminary prospectus
    - Must contain cautionary language (NI 41-101 s. 13.7(1)©
* Final Prospectus
  + Revamped and approved preliminary prospectus
  + Must include a blacklined copy to show changes from preliminary prospectus
  + Once an issuer obtains a receipt for its final prospectus, it can begin distributing securities under it
  + Signatories must sign a paper document and file it with SEDAR within three business days after electronic filing
    - Issuer: CEO, CFO, and any two other directors must certify that the “prospectus constitutes full, true, and plain disclosure of all material facts” (45-101 ss.5.3-4)
    - Underwriter: same, but prefaced with “to the best of our knowledge, information, and belief” (45-101 s. 5.9)
  + Liability is attached to final prospectus
  + When a dealer obtains an order to purchase, it must send the prospectus to the prospective purchaser either before entering the purchase agreement, or within two business days
  + Purchaser then has two "cooling off days"
* Principle Regulator (jurisdiction)
  + Criteria:
    - Location of the issuer's management
    - Location of assets and operations
    - Location of trading market or quotation system
    - Location of the securityholders
  + Will issue a final receipt if:
    - All comments have been resolved
    - OSC's actions (opting out or indicated on SEDAR)
    - Filer must have filed acceptable materials
    - Fees have been paid and no cease trade orders

Re Cycomm (1993) – Director had concluded that an officer’s past conduct meant that Cycomm would not operate with integrity. **Standard of proof for proving conduct was BoP.**

# Continuous Disclosure Requirements

* Every RI has an ongoing obligation to disclose certain information to the Commissions and its securityholders, which ensures **equal footing** for investors
* Harmonized through NI 51-02 *Continuous Disclosure Obligations*
* Two broad categories of continuous disclosure obligation
  + **Periodic disclosure** - must be made at regular, set intervals
    - Annual and interim financial statements fall into this category
    - Information circular (Sent before AGMs)
  + **Timely disclosure** - triggered by a material change in the issuer's affairs
    - Issuer may or may not have control over the timing
* Designed to create a level playing field where investors have access to the same information and all pricing and investment decisions are made from the same starting point
* Financial statements need contain only significant (material) matters
* Issuers that wish to use US GAPP or other exemptions from NI 51-102 may request exemptions (NI 51-102 s.13.1(1))
  + Commission will perform a cost/benefit analysis with the public interest in mind
* CD advances investor protection by ensuring that all investors have sufficient information to make rational investment decisions -> boosts investor confidence -> increased participation -> increases market efficiency

#### Periodic Disclosure (annual and interim quarterly statements)

* Requires financial disclosure, MD&A, AIFs, certification, compensation disclosure, and proxy and information disclosure (for an AGM)
* Delivery of Periodic Disclosure
  + NI 54-101 ensures that beneficial owners receive periodic disclosures to which they are entitled
  + Beneficial Owners:
    - Intermediaries (registered owners) must keep records
    - NOBOS - non-objecting beneficial owners - those who don't mind having their name revealed
    - OBOs (objecting beneficial owners)
  + NP 11-201 recommends that the deliverer obtain advance consent to deliver documents electronically
  + A deliverer should have evidence that the document was delivered to the recipient
  + Could be inferred from a consent form if the document was sent in accordance with its terms
* Venture issuer: one with no securities listed in most markets (NI-52-109, s.1.1)

### Financial Disclosure

### Accounting Standards

* RI must make financial disclosure that is accurate and timely
* As of 2011 financial statements must be prepared according to International Financial Reporting Standards (IFRS) (NI 52-107)
  + Set by the International Accounting Standards Board (IASB) in a principle based approach, as a rule-based approach allows for more loopholes

### Annual Financial Statements

* A non-venture reporting issuer must file audited annual financial statements within 90 days of its year-end
* A venture issuer has 120 days (NI 51-102, s.4.2)
* Investment fund's 90 days (NI 81-106, ss. 2.1-2.2)
* Must compare the current year's results to the previous year's
* Comprehensive income, statement of changes, statement of financial position as at the end of the financial year

### Interim financial statements (NI 51-102, s.4.3)

* Periods ending nine, six, and three months before the end of its financial year
* Due within 60 days of the end of the interim period for venture issuers
* 45 days for non-venture issuers and investment funds

### Auditor's Report (NI 52-107, s.3.3)

* All annual statements (not interim statements) must be audited in accordance with the fair presentation framework of IFRS (interim statements are only subject to audit)

### Future Predictions

* NI 51-102 divides predictions into 3 categories:
  + Forward-looking information (broadest, includes FOFI and FO)
    - Disclosure regarding possible events, conditions or financial performance that is based on assumptions about future economic conditions and courses of action
  + Future oriented financial information (FOFI)
    - Information with respect to prospective financial performance, financial position or cash flows that is presented either as a forecast or a projection
    - Presented in the format of a historical statement of financial position, statement of comprehensive income, or statement of cash flows
  + Financial outlook (FO)
    - When presented in any other format
* **Must have a reasonable basis for the forward-looking information** (s. 4A.2)
  + FOFI implies a material fact that the forecast is obj. reasonable at time made
* "Safe harbour" where an issuer makes a FOFI, must state date on which management approved the FOFI, explain its purpose and caution investors that the information may not be appropriate for other purposes

### MD&A- Management Discussion and Analysis

* **Must be filed with every annual and interim financial statement (s.5.1(1))**
* Narrative explanation, through the eyes of management from the issuer's management of the most important aspects of the issuer's position and condition (51-102F1, s.1(a))
* Only material information must be disclosed (51-102F1, s.1(e))
* Includes overall performance, operations, quarterly results, liquidity, capital resources, off-balance sheet arrangements, transactions between related parties, proposed transactions and changes in accounting policies

### Annual Reports

* Glossy documents sent to securityholders summarizing the past fiscal year
* Contain a letter from the issuer’s chairperson or CEO outlining projects and problems
* Typically accompany annual financial disclosure, **not required by law**

### Annual Information Forms (AIFs)

* Extensive and important disclosure documents that must be prepared annually by **all non-venture reporting issuers**
* Material information about a company and its business at a point in time in the context of its historical and possible future development, operations, prospects, risks, and external factors
* Must be filed within 90 days of the end of an issuer's fiscal year (NI 51-102 ss 6.1-2)
* Contains much of the information that would ordinarily be found in a prospectus
* Only material information need be disclosed
* 18 items - including a description of capital structure and dividends, information on the directors and officers and their interest in material transactions or contracts

### Certification Requirements (NI 52-109 pt. 4)

* CEOs and CFOs are required to execute certificates attached to the primary CD documents
* Must certify financial statements, and the board of directors (or auditor) must also
* Applies to both annual and interim filings
* Makes the issuer's top management accountable

### Proxy and Information Circular Disclosure (Part 9 of NI 51-102)

* Proxy - another person to attend and act for the securityholder on his behalf (NI 51-102 s.1.1)
* Must vote as directed by the securityholder
* Proxy regulation today is contained in Part 9 of NI 51-102
  + If a RI is incorporated, organized, or continued under another jurisdiction the issuer may comply with those requirements instead
* Proxy solicitation is mandatory to prevent management from avoiding proxy rules
  + **Proxy solicitation** 1) “requesting a proxy whether or not the request is accompanied by or included in a form of proxy” 2) “requesting a securityholder to execute or not to execute a form of proxy or to revoke a proxy”… page 266 (s.1(1)(a-d)
  + Information circulars must contain information to enable securityholders to make informed decisions on proxy votes
* Form of proxy - form that when completed and executed, appoints a proxy (s.1.1)
  + States that any person can be nominee for proxy
  + Must allow the securityolder to vote separately on each matter or group of related matters
* Issuer generally bears the costs of proxy solicitation, since it enables securityholders to make intelligent decisions on corporate policies, and this benefit outweighs the costs
* **Management circular** –normal matters: election of directors, auditor renumeration
* **Dissident circular** –when an outside shareholder is soliciting proxies for more than 15 shareholders for votes, usually kicking out shareholders
* Norcan Oils Ltd *v Fogler* (1964) SCC
  + Court has no power to set aside a consummated amalgamation
  + Must do so before the certificate of amalgamation is issued
* Garvie *v Axmith* (1961) OHC
  + Court held that there is right to receive information sufficient to enable an “intelligent conclusion”
  + Circular did not disclose how the valuation of assets had been reached
  + Court found that shareholders could not form an intelligent decision without this information

### Executive compensation disclosure

* Includes directors and Named Executive Officers (NEOs) - CEO, CFO, each of the three most compensated executive officers other than the CEO and CFO who received more than $150,000 in compensation, even if they were not an executive officer at the end of recent financial year (i.e. management consultants)
* Must include any compensation paid, awarded, granted, given, directly or indirectly, etc. (s.1.3(1) of Form 51-102F6)
* Broadly defined throughout
* Contains a compensation discussion and analysis section

#### Timely Disclosure

* Proxy and information circulars (outside of the AGM)

### Material Change Reports (MCRs)

* Disclosure document intended to inform Commissions, market participants, and the public about certain important changes in an issuer's affairs
* Must file an MCR "as soon as practicable" and within 10 days of any material change (NI 51-102 s.7.1), however this is rarely relied upon for civil liability reasons
* Must also **immediately** issue and file a news release
* **Triggered by a material change** (market impact test)
* May be confidential where immediate disclosure would be "unduly detrimental" to its interests (pursuing a specific strategy) (NI 51-102, s.7.1(2)(a))
  + Or where a decision by its senior management amounts to a "material change" and is awaiting probable board approval (s.71(2)(b))
  + Issuer must still file the information within 10 days, it is marked confidential and not released to the public
  + Always temporary
  + Cannot trade securities before information is disclosed to public

### Business Acquisition Reports (BARs)

* Must be filed when a "significant acquisition" occurs within 75 days (NI 51-102, s. 8.2)
* An MCR must be filed within 10 days if it is also a material change (51-102CP, s. 8.1)
* “Significant acquisition” tests (must satisfy any one)(NI 51-102CP, s.8.1):
  + Asset test – Do assets exceed 20 percent of the issuer’s total assets after the acquisition
  + Investment test- do the investments and advances exceed 20 percent of assets as of the last day of its most recently completed financial year
  + Profit or loss test- If the acquired businesses’ profit or loss exceeds 20 percent of the profit of loss of the issuer over the last completed financial year

### Insider Trading Reports (ITRs)

* Under legal insider trading, where a special relationship person does not know any MNPI about the RI, the person may trade freely in the RI’s securities, HOWEVER –if the person is a “reporting insider”, the reporting insider must file an ITR (NI 55-104 s.3.1)
* Filed on SEDI within ten days of becoming an RI, any further changes within 5 days
* Reporting insider defined in NI 55-104 and on page 350 full list
* There are exemptions –automatic securities purchase plans, issuer events, issuer grants as compensation, Insiders of US issuers, mutual funds –and discretionary power of the commission

#### Selective Disclosure

* Accidental or intentional dissemination to a select group of individuals of information about an issuer that is not yet publicly available
* If a RI discloses some material information it should make an immediate public announcement and request exchanges to halt trading until that announcement is disseminated (NP 51-201, s.3.6)
* CSA views it unfavourably due to need for level playing field
* Concerns about regulating selective disclosure since it might have a “chilling effect” between RIs and their analysts

# The Exempt Market

* Exempt market securities are subject to different conditions and rules than public securities
* Subject to certain resale rules (i.e. hold periods to restrict securities from being freely traded)
* Private placement - offering made using an exemption (proper name is exempt distribution)
* **Avoid prospectus requirement and CD obligations**
* Two types of exemptions: mandatory and discretionary
* Mandatory exemptions have objective qualifications under the legislation NI 45-106
  + Onus is on claimant - **Issuer must take the steps reasonably necessary in the circumstances to ascertain that an exemption applies, and must have a reasonable basis for considering that the exemption applies**

* Discretionary exemption - regulators have considerable discretion to grant exemptions
* Disadvantage of exempt market is restricted secondary trading, securities can only be re-sold if:
  + Qualified under a prospectus
  + The resale rules must be satisfied (NI 45-106 s.9.06)
  + Or they must be allowed to trade under some other exemption
* Also less liquid and riskier, so issue price may be discounted
* System was implemented in 1979
* **Must have either a prospectus or an exemption (closed system) – catch-then-exclude** 
  + Prevents a security from being traded freely without information
* Hold period- securities held until the issuer has become a reporting issuer and can then be traded freely –can be used to allow information about the securities to be built up

#### Reasons to Use Exempt Market

* Prospectus takes time, effort, expenses
  + Three types of costs:
    - Direct - out of pocket (commission to underwriter, fees etc.)
    - Indirect- searching for underwriter and marketing, road shows
    - Intangible (shares immediately start trading above issuing price)
* If only offering to a narrow range of investors
* Commission not approving prospectus or issuer unable to satisfy prospectus disclosure requirements
* Not able to find a registered dealer
* Doesn't want to become a RI

#### Types of Exempt Markets

Familiarity (no need to know)- The purchaser is already **familiar** with the issuer, the securities, or both

* Founder, directors, executive officers and their immediate families, employees
* Includes rights offerings- right of existing securityholders to purchase more securities
  + Slight discount from prevailing market price in proportional ownership share
    - Issuer must provide written notice to regulator, who then has 10 days to raise any objections (NI 45-101) –no more disclosure is needed

### Dividend Distributions and Reinvestment Plans

* Dividend distribution - issuer giving out securities instead of cash (NI 45-106 s. 2.31)
* Reinvestment plan - agreement between an issuer and securityholders to reinvest their cash dividends automatically
* Reinvestment plan is automatic (rights offering isn’t), idea for this, dividend distr, and RO, is that the securityholder since they already hold securities and possess or have access to information

### Conversion Exchange or Exercise

* Converting other instruments into securities or vice versa (i.e. convertible securities or warrants)

### Family, Friends, Business Associates

* "close business associates"
* NI 45-106 s.2.5(1) describes exhaustively who qualifies as a family member (page 310 ftnote 54)
* "close personal friend" is one who has known the person in question long enough to be in a position to assess that person's capabilities and trustworthiness, and a direct relationship
  + Must be a direct relationship
* "close business associate" is one who has had sufficient prior business dealings with a director, executive officer, founder or control person of the issuer to be in a position to assess that person's capabilities and trustworthiness, a direct relationship
  + Must be a direct relationship (NI 45-106CP, ss 2.7-2.8)
  + A signed statement has no impact (s.1.9)

### Affiliate

* If one company is a subsidiary of the other, or controlled by the same person (NI 45-106 s. 1.3)
* Unlikely for an issuer to take advantage of its affiliates, and they share information regularly

### Employee, EO, Director and Consultant

* Distribution by an issuer of its own securities (or by a control person) to an employee, executive officer, director or consultant (NI 45-106, ss.2.22-2.29)
* Permits employee stock options and similar programs
* Must be voluntary action by the securityholder
* Creates alignment of economic interests

### Investment Funds – (NI 45-106 ss 2.18-2.21)

* Reinvestment actions
* Additional investments (initial acquisition was $150k)
* Private investment club- small number of retail investors to pool
* Private investment fund -loan and trust pools- trust company

### Private issuer exemption –(NI 45-106 s. 2.4)

* A distribution by a “private issuer” to an accredited investor or a person who has a close relationship with the issuer (“close relationship”, page 314 ftnote 74)
* Not “to the public” –common bonds test is included in “close relationship”
* Private Issuer- An issuer which is not a reporting issuer or an investment fund, has 50 or fewer securityholders, and whose constating document restricts the right of securityholders to transfer its securities
* No commission or finder’s fee may be paid

### Sophistication or Able to Protect Itself (no need to know #2) -The purchaser does not need prospectus-level disclosure because it is sophisticated, or has incentive to do own research

### Accredited investors (NI 45-106 s.2.3)

* Could be corporate entities or individuals
  + Individuals - "financial assets test" - own more than 1m in assets before tax
    - "net income test" pre-tax income in each of past two years of more than $200k, or combined income with spouse of more than $300k and who reasonable expects to exceed that level in the current year
    - "net asset test" - alone or with a spouse has assets of at least 5M
    - A person created or used solely to purchase or hold securities as an accredited investor cannot use the exemption
    - Requires a report in BC and must be within 10 days

### Minimum amount investment (NI 45-106 s.2.10)

* Acquisition cost of at least 150k
* Pays in cash for first 150k
* Must report to commission within 10 days

### Investment is especially safe (No need to know #3) – Canada savings bonds, municipal bonds etc.

* Also includes guaranteed instruments, approved debt securities of foreign jurisdictions, instruments issued by “permitted supranational agencies”, and short term debt that is not convertible
* Not subject to resale rules
* NI 45-106 s.2.34

Redundancy or Dual Regulation –Prospectus-level information is available from another source or required by another regulator

* Equivalent information is available from another source, or regulated under another regime

### Take-over bid or Issuer Bid (NI 45-106 s.2.16)

* A distribution made in connection with a take-over bid or an issuer bid
* “In connection with” can be interpreted very broadly
* Since accompanied by a bid circular

### Business Combination and Reorganization (NI 45-106 s.2.11)

* In amalgamations or mergers since securityholders already know from approval
  + Must be made under statutory procedure
  + Described in information circular and then approved by securityholders, or
  + A dissolution or winding-up

### Acting as underwriter(NI 45-106 s.2.33)

* A distribution between a person and a purchaser acting as an underwriter or between or among persons acting as underwriters
* Distributions are only for the purpose of moving toward a distribution to the public, so no prospectus necessary

Cost/Benefit Analysis – Ensuring Smaller Issuers and Not-for-Profits can Access Capital Markets

* Ability to access capital markets would not happen with costs of prospectus-level disclosure

### Offering Memorandum (OM)(NI 45-106 s.2.9)

* Is similar to prospectus
* Not reviewed or accepted by commission, but does attract liability
* If transaction is over 10k, only “eligible investors” can use OM exemption
  + Eligible investor: accredited investor, family-friends-business-associates, those “obtain advice regarding the suitability of the investment” from a registered eligibility adviser.
* Two prescribed forms for an OM - one for qualifying issuers and one for all other issuers
  + Qualifying issuer- is one that files its CD documents on SEDAR, never been in default of CD obligations, and filed an AIF for most recent year
* OM must contain a statement of purchaser’s rights, a signed certificate, risk acknowledgement statement
* Must be filed within 10 days of distribution

### Isolated Distribution (NI 45-106 s.2.30)

* Isolated distribution in its own securities
* Requires two conditions to be met:
  + Must not be part of a series of similar continued and successive transactions
  + Must not be by a person whose usual business is trading securities
  + Must report to commission within 10 days

### Asset acquisition (NI 45-106 s. 2.12)

* A distribution made as consideration for the acquisition of assets owned by the purchaser
  + If assets are worth over 150k
  + Must report within 10 days
  + Give securities instead of cash

### Not-for-Profit Issuers (NI 45-106 s.2.38)

* No securityholder may benefit from the distribution, and no commission or remuneration be paid associated with the distribution

### Discretionary Exemptions (*Canada Business Corporations Act*, s. 241)

* Commission has the ultimate discretion
* Cannot be appealed
* Cannot be "prejudicial to public interest"
* Typically granted when an issuer meets most, but not all, requirements for mandatory exemption
  + *Re Teck Cominco Ltd*, 2006
* Made to suit specific situations
  + *Re Uranium Focused Energy Fund*
* Applies to its principal regulator
* Passport system applies

#### Resale Rules (NI 45-102 s.22-2.7)

* Allow a third means to distribute securities (aside from exemptions and prospectuses)
* Impose hold periods of 4 months
* Two types: restricted periods and seasoning periods
  + Hold period securities are less liquid and more risky
* Once hold period expires they are freely tradable
* Hold periods are 4 months pursuant to NI 45-102
* Private issuers, or issuers that aren’t reporting issuers, may be subject to indefinite hold period (but could be traded under another exemption)
* Restricted Periods
  + Applies to any exemption listed in Appendix D of NI 45-102
  + Deemed to be a distribution unless the restricted period has been observed
  + Seven conditions must be met, page 332
* Seasoning Period
  + Applies to exemptions listed in Appendix E of NI 45-102
  + Also applies to the first trade of securities by private companies
  + 5 criteria set out - page 333
  + For a Control Person, additional burden to provide advance notice to sell one week before trade executed

# Registration

* Highly regulated area of market
* Can be an individual or a corporation
* Includes:
  + "Dealers" engage in the business of trading in securities and acting as underwriters
  + "Salespersons" are individuals employed by a dealer, and are also registrants
  + "Advisors" - a person engaging in advising securities
  + "investment fund managers" - registrants who direct business, operations or affairs investment funds
* Registration rules are contained in NI 33-109
* Registration requirement is intended to protect investors from unfair, improper or fraudulent practices
* **Cannot act as a dealer unless registered**
* Must register in different categories, may need to register in more than one category

#### Dealers and Advisers

* Triggered if the person or company holds himself as engaging in the business of trading or advising in securities
* Business trigger- trading for business purpose (does not apply for investment fund managers)
  + Engaging in typical registrant activities
  + Intermediating trades
  + Carrying on the activity with repetition, regularity, or continuity
  + Expecting to be remunerated or compensated
  + Directly or indirectly soliciting
* **Was it an opinion or a recommendation?**
  + Reciting facts is not advising, but recommending an investment or opining on the investment merits of an issuer or security is
* **Did the purported adviser offer the recommendation in a way that reflected the business purpose?**
  + Disclaimer has no impact
* One-time trading or advising activities are not considered to be in the business of trading or advising
* Business purpose may not be found if the trading or advising activities are incidental to a primary business
* Types of dealers p478 (NI 31-103 s.7.1(1)):
  + Investment (largest scope) – any security and members of IIROC
  + Mutual fund
  + Scholarship plan
  + Exempt market dealers
  + Restricted
* Types of adviser categories (NI 31-103 s.7.1(2)):
  + Portfolio managers – act as advisers in respect of any security
  + Restricted portfolio managers –in accordance with terms, conditions etc. applied to registration
* Investment fund manager category (NI 31-103 s.7.3))
  + Criteria to decide are pg480

### Individual Applications – individuals as sole proprietors or within a firm must register

* Individuals must be “fit for registration”, based on criteria in NI 31-103 and From 33-109F4
* Three fundamental criteria for assessing an individual applicant
  + Proficiency -requires that individual applicants have the education, training and experience that a reasonable person would consider necessary to perform the activity competently (Part 3 of NI 31-103)
  + Integrity -requires honest character
  + Solvency - requires that applicants be in sound financial condition
* Must register under one or more categories
* Individuals can be dealing representatives,
  + Must be an "approved person" by IIROC (or MFDA if mutual fund dealer)
* Advising representatives and associate advising representatives
  + Apprentices
* Ultimate Designated Persons and Chief Compliance Officers (UDP)
  + IIROC member firms the UDP must be the CEO

### Registration Obligations

* Investment dealers are subject to additional requirements of IIROC
* Mutual fund dealers are subject to additional requirements of MFDA
* Firms registered with IIROC/MFDA are exempt from certain requirements of NI 31-103 as long as they oblige IIROC MFDA rules
  + IIROC exemptions for KYC, suitability and disclosure when recommending the use of borrowed money)
  + MFDA (suitability and disclosure when recommending the use of borrowed money)
* Registrants must have and use policies and procedures to establish a **system of controls** and supervision
* Required to maintain records to accurately record its business activities**, financial affairs**, and client transactions for seven years (NI 31-103 s.11.5(2))
* Must keep "**working capital**" available pursuant to Form 31-103F1
* **Collect Know Your Client information** (KYC)
  + Identity, insider of any reporting issuer, creditworthiness
  + Must have sufficient information about investment needs and objectives, finances, risk tolerance
  + Must keep the information current
* **Know your Product** (KYP)
  + Structure, features, and risks of each security the individual recommends to a client
  + Take reasonable steps to ensure that the purchase or sale is suitable for a client
* **Referral Arrangements**
  + Registrants can accept or pay a referral fee
  + Must take reasonable steps to ensure that a person or company is appropriately qualified
* Must document and respond to every **complaint** made to a registered firm about any product or service offered by the firm or its representative

# Insider Trading/Tipping

* There is illegal (administrative and criminal) and legal IT
* **Illegal IT** is based on a person having knowledge of undisclosed material facts or changes about the reporting issuer - "material non-public information" (MNPI)
  + Occurs when (1) a person in a special relationship with a reporting issuer (2) trades (lay person, not securities def.) in the issuer's securities (or, effectively, a derivative) (3) with knowledge of a material fact or change (4) that has not been generally disclosed. (*BCSA* s.57.2(3))
* **Legal IT** is when they disclose their trades, and do not use material non-public information
  + Argument that legal material-non-public information insider trading should be allowed as it is most efficient and follows fiduciary duty towards the corporation, securities reg is just extra
  + Legal IT is for a “reporting insider” (pg. 350), so long as the insider is not in possession of material non-public information and files an insider trading report (ITR) *see* ITR in CD
* **Difference between illegal/legal depends on state of knowledge a the time of the impugned activity**
* IT prohibition is based on a theory of "equal access to information"
* **Prove each element of an illegal IT allegation on a balance of probabilities** 
  + Re Suman (2012 OSC) - Inferences may be drawn based on circumstantial evidence that includes proof of the ability and opportunity to acquire the information combined with evidence of well-timed, highly uncharacteristic, risky and highly profitable trades. The more facts and evidence supporting an inference, the stronger and more compelling the inference will be
  + Re Holtby – inferences as circumstantial evidence as to motive, as circumstantial evidence as to certain habit or practice, and as circumstantial evidence of after-the-fact conduct that could reflect consciousness as to guilt

Methods of prevention of liability National Policy 51-201 sections 6

* Establish a policy
* Train employees
* Sign confidentiality agreements
* Try and show that it was just a "bad apple" and not the entire company
* Handling rumours, chat rooms, bulletin boards, emails etc.

#### Persons in Special Relationships with the RI

### Insiders, Affiliates and Associates (Special Relationship)

* Both insiders and people in special relationships can be held liable for IT
* A person or company is in a special relationship with a reporting issuer if:
  + **An insider, affiliate, or associate of the RI itself**
  + An insider, affiliate or associate of a person proposing to make a take-over bid for the reporting issuer's securities; or
  + An insider, affiliate or associate of a person proposing either to enter into a business combination with the reporting issuer or to acquire a substantial portion of the reporting issuer's property
* "affiliate" - if one issuer is a subsidiary of the other or if each is controlled by the same issuer
* "associate" - if they are relatives (living in the same home) or partners, if a person "has a substantial beneficial interest" in or is trustee for a trust, or if one person owns or controls more than 10 per cent of second's voting securities
* "insider" - broad in the number of parties that it captures but precise in that those parties are well-defined by position or percentage of securities held (in s.1(1)of *BCSA*)
  + **Directors and officers** are insiders (defined by capacity to act, not necessarily title)
  + **A person with Ownership of or Control** or Direction over 10 percent of the Voting Securities
    - Includes beneficial ownership (*Re Holtby*)
    - Prevents insiders from avoiding the regulations by arranging for legal ownership by another
    - "control or direction" means more than legal ownership
  + **The Issuer itself**
  + **A person designated** as an insider by the Commission

### Business or Professional Activity

* A person who has engaged in, is engaging in or proposes to engage in any business or professional activity with or on behalf of the reporting issuer, a proposed take-over bid person or a proposed business combination person is in a special relationship with it (*BCSA* s.3(b))
* Includes suppliers, bankers, lawyers, accountants, underwriters, geologists etc.

### Directors, Officers and Employees

* Directors, officers, and employees are in a special relationship if they are (s.3(c))
  + Part of the reporting issuer itself
  + Engaging in or proposing to engage in any business or professional activity with or on behalf of the RI
  + Any person proposing to make a take-over bid for the RI
  + Any person proposing to enter into a business combination with the reporting issuer or to acquire a “substantial portion’ of it

### Persons with a Past Relationship

* Past special relationships continue to be a special relationship so that they cannot remove themselves from a situation (s.3(d))

### Tippees/Tipping

* **Tipping** is when (1) a person in a special relationship with a reporting issuer (2) with knowledge of a material fact or change (3) that has not been generally disclosed (4) informs another person of that information, other than in the necessary course of business (s.57.2)
  + Tipper is liable regardless of the tippee's conduct. A tippee who does not act on the information is not liable
  + Proportionality is used to determine the damages in relation to the offence
  + Recommending is separate (ss. 5)
* Tippee (section 3(e))
  + A tippee is a person who learns of a material fact or material change from a person in a special relationship with the issuer
  + They are then in a special relationship with the RI if he or she knows or ought to reasonably know that the tipper is in a special relationship with the reporting issuer
  + A person who learns of a material fact or material change from a tippee is also a tippee and may also fall under this branch

#### Materiality for IT

* Two parts: materiality and disclosure

**Materiality**

* Can have knowledge of a material fact or change
* Material fact- a fact that would reasonably be expected to have a significant effect on the market price or value of the securities in question (s.1.1)
* Material change- is a change in the business, operations or capital of the issuer that would reasonably be expected to have a significant effect on the market price or value of a security of the issuer, or a decision to implement such a change - market impact test (s.1.1)
* To be determined objectively, from a reasonable investor's perspective
  + Judgment and common sense
  + "is a question of mixed fact and law that requires a contextual determination that takes into account all of the circumstances including the size and nature of the issuer and its business, the nature of the statement and the specific circumstances in which the statement was made" (*Re Biovail*, 2010)
* With material change, can look at the probability of the event happening and the magnitude of the event- whether it will be viewed by a reasonable investor as important (prob./mag test)
* Kapusta 2011 LNABASC 196 – **timing** 
  + Drilling results initially were limited information and great uncertainty, but later became material, at a critical point, with accumulation of information
  + Trades made before the critical point did not contravene IT provisions
* Re Donnini(2002 OSC) - court looked at **trading patterns** to establish knowledge of a material fact
  + Director and large shareholder of company in negotiations with company B
  + Knew that the deal was likely to be completed
  + OSC looked at his trading pattern
  + Donnini’s trades were consistent with him knowing the information was a material fact
  + Used probability magnitude test
* Re Donald*-* For the **proposing requirement** to be met “there must have been some significant level of involvement and approval of the process at the highest corporate levels of RIM”

### Disclosure

* MNPI is not public through disclosure or dissemination
* Persons in a special relationship need to make sure that the information has been generally disclosed before they purchase or sell securities of the RI
* Information must be “disseminated in a manner calculated to effectively reach the marketplace” and investors have “a reasonable amount of time to analyze the information” (NP 51-201 s.3.5(2))
* CSA advises that decision makers will consider all of the relevant facts and circumstances, including the company's traditional practices for publicly disclosing information and how broadly investors and the investment community follow the company
* Re Baffinland- generally disclosing among industry specialists is not public disclosure

#### Defences

* Onus on the respondent (trader) to prove defences

### Reasonable belief in general disclosure(s.57.4(1-2))

* Insider can try and show equality between them and the public
* Honest but unreasonable belief is not sufficient - *Re Gorrie* 2006
  + Assumed information had been disseminated at AGM

### Reasonable belief in specific disclosure (s.57.4(1-2))

* Where the special relationship person can prove a reasonable belief that the other party or the tippee, had knowledge of the material information or ought to reasonable have known of it

### No Knowledge (s.57.4(5))

* Prove that the person or company had no knowledge of material non-public information
* Can be prevented by implementing a “Chinese Wall”, however the implementation of one does not void liability, but helps, where its absence hurts

### No use of MNPI (s.57.5(4))

* I.e. was an automatic plan or made to meet contract obligations

### Tipping in the necessary course of business (s.57.2(3))

* Mixed question of law and fact that must be determined in each case and in light of the policy reasons for the tipping provisions. Tipping is prohibited so that everyone in the market has equal access to, and opportunity to act upon, material information
* Could be when issuer seeks to raise capital in private placement or in take-over bid, acquisition

Tippee unaware **that** **tipper was a special relationship person**

* Cannot be liable for illegal IT or for tipping if the original tippeee did not know and could not reasonably have known that the original tipper was a special relationship person

### Reasonable mistake of fact regarding materiality

* *R v Fingold-* expected condition of issuer to improve, did not think that fact would affect MKP
  + This defence can rarely succeed
  + If you **genuinely** and **reasonably** believe that it was not material

#### Criminal IT

* Buying or selling a security "knowingly using inside information" obtained (a) as a shareholder of the issuer (b) in the course of a business or professional relationship with the issuer or © in the course of a proposed take-over of or business combination with the issuer; (d) in the course of employment or duties with either the issuer or a person in one of (a) to (c); or (e) from someone in any of the (a) to (d) relationships
* Difference between provincial is "knowingly using" as opposed to "have knowledge of"
  + Difficult to prove

#### Fines/Sanctions

* Four types of sanctions for Illegal IT
  + Monetary penalties, cease trade orders, denials of exemptions and prohibitions from acting as director or officer
* Civil sanctions include court orders, and court discretion over anything else
* Quasi-criminal or penal sanctions are fines or imprisonment or both
* Criminal sanctions can be as severe as 10 years’ imprisonment

#### Fines

* Minimum of "profit made or loss avoided" and max of the greater of 3M and three times the profit made or loss avoided
* Only 3M in BC
* Profit made - when a special relationship person sells securities
  + Amount the person sold for, less the securities average trading price for 20 trading days after the information was generally disclosed
* Loss avoided - when special relationship person buys securities
  + Average price over those 20 trading days, less the amount the person paid
* Tipping- any consideration the tipper received for tipping
* In BC 3 years imprisonment for tipping or illegal IT

# Takeover Bids

* TOB- is an attempt by one entity (the bidder, or offeror) to acquire control over another (the target) by bidding for some or all of the target's outstanding securities
* Where the securities bid for, together with those already owned, will be %20 or more of the outstanding securities of that class of securities at the date of the offer to acquire
  + Aimed at effective control, not legal control
* Must be securities, not assets
* "Offer" includes both direct and indirect offers (can also be joint offerors, in which case it is known as one offeror) (MI 62-104 s.1.9(1))
* Hostile TOB- where the target's management resists the TOB, as opposed to “friendly TOB”
* Regulated by **MI 62-104**
* TOB may be exempt from TOB requirements if it falls under an exemption (catch-then-exclude)

**Purpose**

* "To establish a clear and predictable framework for the conduct of bids in a manner that achieves three primary objectives- equal treatment of the target's securityholders; provision of adequate information to the target's securityholders; and an open and even-handed bid process"

#### Exemptions From TOB Regulation (pg 390)

* There are five specified situations, and the discretionary exemption by the Commission
* Catch-then-exclude- every TOB will be caught unless it falls within a specified or discretionary exemption

### Normal Course Purchase

* Offeror may acquire **up to 5%** of outstanding securities of a given class over a 12 month period
* Offeror must not pay more than market price
  + Average of closing price over past 20 days
* Class of securities must be on published market (MI 62-104 s.4.1)

### Private Agreement

* If offeror purchases securities from max five people
* If total consideration paid, including fees and commissions, is no more than 115% of the MKP of securities (MI 62-104 s.4.2)
* Cannot be made generally to all securityholders of the class
* If the premium is more than 15% it must be shared among all securityholders through a full TOB

### Non-reporting Issuer

* The target is not a RI
* No published market for the securities (MI 62-104 s.4.3)
* Maximum 50 securityholders in the class (excluding employees)
* Idea is that less protection is needed for closely held companies (smaller companies)

### Foreign Take-over Bids

* At least 90% of the offerees are resident outside Canada (MI 62-104 s.4.4)
* Offeror must reasonably believe that residents of Canada beneficially own less than 10 percent of outstanding securities of the class
* Published market on which the greatest volume of the securities was traded in the past 12 months must be outside Canada
* Canadian securityholders cannot be discriminated against, must be entitled to participate in the bid on terms "at least as favourable" to those outside of Canada

### De Minimis

* If only a minimal portion of the bid occurs in the jurisdiction
* Must be fewer than 50 securityholders of the class in the jurisdiction (MI 62-104 s.4.5)
* Must constitute, in aggregate, less than two per cent of the outstanding securities of the class
* Securityholders in the jurisdiction must be entitled to participate in the bid on terms "at least as favourable" to those outside of Canada

#### TOB Procedures

### Early warning system

* Alerts targets to potential TOBs
* Persons with 10% or more of a certain class must give “prompt” disclosure (MI 62-104 s.5.2(1)) in a news release and file a formal report with the Commission within two days
* Any increase by 2% requires another news release and report with Commission
* Person is restricted from trading securities while info is being disclosed and disseminated
  + Until one day after it is filed with Commission
* Four major exemptions
  + Do not apply to mutual funds or other eligible institutional investors (passive investors) who use an alternative monthly reporting system (NI 62-103 ss. 3.3, 4.1-4.8)
  + When a person's security holdings change due to certain issuer actions (ss.6.1 and 6.2)
  + When underwriter owns the securities as an underwriter and has made disclosure s.7.1
  + Discretion by the Commissions (s.11.1)

#### The offer

* Must be extended to all holders of the securities of the class in the jurisdiction in one of two ways:
  + Can be initiated by **delivering** the bid to the offerees (MI 62-104 s.2.9(1)(b))
  + **Publishing** an advertisement containing a brief summary of the bid in a major daily newspaper
    - TOB must also be filed and delivered to the targets principal office on or before date of ad publish
    - Offeror must request a list from target of securityholders on or before date of ad publish
    - Deliver the TOB to the offerees within two business days of receiving the list (s.9(1)(a))
* Must allow offerees **at least 35 days**, and cannot purchase during this time (**MI 62-104** s.2.28)
* Offeror can accept **any consideration**, however offerees must all be given same (s.2.23(1))
  + If acquired within 90 days before launching the TOB, price offered to securityholders must be at least price acquired during window, and offeror must acquire at least same percentage (2.4(1)(b))
* Supplemental Warning System (s.5.3)
  + After TOB is launched and person acquires more than **5% then every additional 2%**
* Offeror must deliver **TOB circular** to the offerees - page 400 (s.2.10(1)(a))
* Directors' Circular delivered from directors to offerees
  + Used because of inherent conflict of interest between fiduciary duty and their jobs
  + Must establish a special committee (pg 402)
  + Delivered within 15 days of the announcement of the TOB (**MI 62-104** s.2.17)
  + Must make a recommendation why bid should occur, or give reasons for no recommendation
* Offeror cannot acquire or agree to acquire any securities of the class until TOB expires
  + Unless outside purchases after the third day
  + Intention to purchase outside was stated in the TOB circular, or news release
  + Not more than 5% total over time (s.2.2(3))
  + File a news release after outside purchase
* Offeree can vary the terms of the TOB, must issue and file a news release and send variation notice to those whose securities have not been taken up (s.2.12)
* Offerees have withdrawal rights, and rights to receive higher consideration where it is varied (pg 406) (s.2.30(2)
* Offeror must take up and pay for securities within 10 days of the TOB expiring if TOB conditions have been met, but not before 35 day TOB period is over (s.2.29)
* The take up is proportionate if more than what is offered are given (2.32)
* Offeror must file any other TOB material that “could affect control of the offeree” (s.3.2(1))

#### Defensive Tactics

### White Knight

* Different offeror, brought in to create competing TOB (
* Directors could give white knight access to confidential information
* Set up data rooms where everything is shown about the company
* Anyone who might be interested buying has to sign tight non-disclosure agreements
* Also white squire, an investor willing to invest enough to thwart the TOB, without acquiring control

### Issuer Bid

* If white knight cannot be found, directors may cause target itself to make a bid for its securityholders securities

### Sale of "Crown Jewels"

* May sell valuable assets to make it a less attractive take-over target

### Lock-Up Option

* Option granted to a party to acquire a large block of securities if a triggering even occurs
* Hopes to prevent offeror from gaining control since option holder will not tender new securities to the bid

### Break Free

* White night's TOB could contain a provision allowing target to recover a specified amount if the TOB fails
* Break fees could stifle the desired competitive environment
* Break fee goes to the white knight so that they get compensated for pulling out

### Golden Parachute

* Expensive compensation packages triggered if employment is terminated after a hostile TOB
  + Could deter offerors

### Conflicting Out

* Giving work to many law firms in hopes to prevent any from acting for a hostile bidder

### Greenmail

* Basically blackmail where offeror buys securities and then threatens target into repurchasing at a premium

### Poison Pill (Shareholder's Rights Plan)

* Entitles existing securityholders to purchase discounted shares in the case of a triggering event
* Makes it more expensive for an offeror
* Extends bid period of any TOB that is made, allowing target to explore other options or find white knight
* If securities regulators decide the SRP is inappropriate they may issue cease trade, killing SRP
* Are supposed to stay open if used as temporary measure to increase bid or look elsewhere
* "Just say no" if it is the best interests of the company to not be taken over, lasts forever due to permanent SRP - allowed in US - not allowed in Canada

## Re Royal Host

* Established that SRPs could only be temporary, and could not be used to "just say no"
* No single, inflexible rule, instead based on:
  + When the plan was adopted
  + Whether securityholder approval of rights plan was obtained
  + Securityholder support
  + Size and complexity of target company
  + Any other defensive tactics
  + Number of potential offerors
  + Steps taken to find alternative bid that would be better
  + Likelihood of finding another bid
  + Nature of the bid
  + Length of time since the bid was announced and made
  + Likelihood that the bid will not be extended if the rights plan is not terminated

## Re Pulse Data

* ASC denied cease-trade for SRP
* Directors adopted SRP to look for other bidders, couldn't find any
* Held vote, 78 percent voted to maintain SRP
* Court held that it was therefore in the interest of the company to maintain SRP

## Lions Gate

* Affirmed *Royal Host*, position that SRP is temporary

## Re Baffinland

* When another bidder has been found the SRP needs to go, it has fulfilled its purpose

#### Empty Voting Rights

* When people who have voting rights to not have economic interest in the company
  + I.e. Return Swap (where A owns shares, agrees to pay B if increase, B agrees to pay A if decrease –A gets voting rights, B is affected financially) – **Empty voting**
* **Negative voting** – where an investor has voting rights and *negative* net economic exposure, an interest in the share price decreasing to over-hedging
* **Hidden ownership** –economic exposure but no voting interest (like B, above), avoids disclosure obligations
* Early warning reporting systems are designed to avoid empty voting rights/hidden ownership problems
* TELUS Corp– Mason’s strategy had nothing to do with the well-being of TELUS and its shareholders

# Statutory Civil Liability (SCL)

* Getting sued in the courts, generally by investors
* Applies across the country in five contexts:
  + Prospectus misrepresentation (SCL broader than CL)
  + OM misrepresentation
  + Circular misrepresentation
  + Trading and tipping while in possession of material non-public info
  + Misrepresentation about continuous disclosure docs
* Can get into trouble on two different standards:
  + Regulatory standard - where BoP
  + Criminal - BRD
* Primary market is part 16
* Secondary market is part 16.1

Standing to bring an action- page 436

* Purchaser has standing against prospectus and OM misrep. (*BCSA* s.132(1))
* Any securityholder who receives circular has standing for circular misrep (132(1))
* Person on the other side of a trade from inside trader or tippee has standing against both (136(1)-(3))
* Commission has standing if person is not pursuing it within 60 days of request
* Standing to bring action for **secondary market:**
* When there is a "release" of a "document" containing a misrepresentation, and that release is made by a "responsible issuer", an "influential person", or a "person with actual, implied or apparent authority" to act on behalf of the responsible issuer or the influential person
* When a "public oral statement" relating to the business or affairs of a "responsible issuer" and containing a misrepresentation is made by a "person with actual, implied or apparent authority" to speak on behalf of the responsible issuer
* When a "public oral statement" relating to a "responsible issuer" and containing a misrepresentation is made by an "influential person" or a "person with actual, implied or apparent authority" to speak on behalf of that influential person
* When a "responsible issuer" fails to make timely disclosure

#### Class Action Certification

* Requires an identifiable class of plaintiffs
* Court must **certify** a class action before it can proceed
  + Must establish to Court of Appeal a reasonable likelihood of success
* **Do not need to prove reliance**
* Class:
  + Bre-X - look at who has shares at the time of public disclosure of fraud, as those who had sold lost value because of the sale
  + Ragoonanan- Court denied certification because no evidence was presented as to how many claimants there would be –no identical requirement of each plaintiff – no reliance
  + Green v CIBC- Contrasted *Bre-X*, said reliance is necessary since otherwise secondary market liability provisions would become redundant as they temper the advantage of presumed reliance with safeguards such as a liability cap -
* Settlements must also be approved by the court
* In BC, costs are not awarded unless frivolous conduct arose, in Ontario, loser pays
* Jurisdiction is generally determined by the residency of the investor (for prospectus it is jurisdiction where distribution occurred)

Limitation Periods - section 140 *BCSA*

* For rescission - 180 days from the date of the transaction
* For damages, it is the earlier of: 1) three years from the date of the transaction; and 2) six months after the issuance of a news release disclosing that the plaintiffs have obtained leave to commence a secondary market SCL action
* For secondary market SCL, it is is the earlier of 1) 3 years from the date the impugned conduct occurred; and 3) 6 months after the issuance of a news release disclosing that the plaintiffs have obtained leave to commence a secondary market SCL action

Primary Market SCL -Prospectus, Offering Memorandum and Circular Misrepresentations- section 131

* Liability is triggered when the document is sent to securityholders
  + Investor doesn't have to prove receipt, comprehension or reliance
* Can argue that the prospectus is a contract, but that would not get you too far
* Misrepresentations are defined to mean:
  + An untrue statement of material fact, or
  + An omission to state a material fact that is required to be stated or that is necessary to make a statement not misleading in the light of the circumstances in which it was made
* **There is deemed reliance, receipt, and comprehension**
* Different directors can be held to different standards
* 131(1)(a) - reliance is found **where there was a misrepresentation at time of purchase**
* CL Tort claims *Queen v Cognos* - negligent misrepresentation - tricky to prove
  + Have to demonstrate that there is a relationship between the buyer and seller so that the seller had a DOC at common law
  + Have to prove that there was a misrepresentation
  + Have to prove negligence
  + Have to prove that you relied
  + Have to demonstrate damages
* **Prospectus** investor has a **right of action** against: (s.131(b))
  + The issuer or selling securityholder (recission or damages)
  + Any underwriter who signed the prospectus certificate (rescission or damages)
  + Any director of the issuer when the prospectus was filed (damages only)
  + Any person who consented to any part of the prospectus (damages only - for their part)
  + Any other person who signed the prospectus (damages only)
* **OM** investor has a right of rescission or damages against the issuer and selling securityholder - section 132.1
* **TOB** document investor has a right of rescission or damages against the offeror, and a right of damages only against:
  + Any director of the offeror when the TOB document was signed
  + Any person who consented to any part of the TOB document (as to their part)
  + Any other person who signed the TOB document

#### Defences

* **Only defences available** for an issuer or a selling securityholder are that it was **not a material fact** or **knowledge of misrepresentation**
* Onus is on the party claiming the defence

### Knowledge of misrepresentation:

* Complete defense
* Investor knew of the misrepresentation at the time of purchase

### Impugned party had no knowledge

* If the impugned party proves that the prospectus or OM was filed, or the TOB send, without that person's knowledge or consent
* Person must also have given "reasonable general notice" of this lack of knowledge or consent upon becoming aware of the situation

### Withdrawal of Consent

* Liability is defeated if the person withdrew consent to a prospectus or TOB document, or OM, wher ethe person became aware of a misrepresentation after it was filed or sent, and gave "reasonable general notice" of the withdrawal and the reason

### Reliance on an Expert

* No defence for issuer or a selling securityholder
* If the misrepresentation relates to an expert's contribution to the prospectus or TOB document
  + The impugned party did not believe there was a misrepresentation and had no reasonable grounds to believe it

### Due diligence

* No defence for issuer or a selling securityholder
* If you did your due diligence, you conducted reasonable investigation as to provide reasonable grounds for believing there was no misrepresentation
  + **The standard for determining "reasonable investigation" and "reasonable grounds" is that of "a prudent person in the circumstances" - *Danier Leather***
  + The investigation is called due diligence
  + Directors can be held at different standards
  + Have to do due diligence of every single thing

#### Damages

* Damages are limited to the amount the security depreciated as a result of the misrepresentation
* Onus is on defendant to prove damages do not represent the security's depreciation
* Generally joint and several
* Later material facts do not have impact on a prospectus, only material changes - *Kerr v Danier Leather*

Trading or Tipping With MNPI- s. 136

* Insider traders and tippers are jointly and severally liable for damages to the party on the other side of the trade
* Inside trader or tipper is liable to both the purchaser and the RI (increases accountability)
* Only defence is a reasonable belief that the MNPI was generally disclosed (due diligence, have to do reasonable investigation)

Secondary Market SCL - CDL misrepresentations - s. 140.3

* For documents pg 463
  + When a "responsible issuer" or a "person [or company] with actual, implied or apperent authority to act on" the responsible issuer's behalf "releases" a "document" containing a misrepresentation, the investor has a right of action against: the responsible issuer; each director of the responsible issuer at the time of the relase; each officer of the responsible issuer who "authorized, permitted or acquiesced" in the release; each "influential person" (and its directors and officers) who "knowingly influenced" the responsible issuer (or the person or company with authority) to release the document (or knowingly influenced a director or officer of the responsible issuer to release the document); and each "expert", where misrepresentations from the expert's report, statement or opinion are used in the document with the expert's consent
* For "public oral statement" pg 464:
  + Relating to the business or affairs of the responsible issuer, made by "a person with actual, implied or apparent authority to speak on" the responsible issuer's behalf, the action lies against: the responsible issuer; the person who made the public oral statement; the responsible issuer's directors and officers who authorized, permitted or acquiesced in the public oral statement being made; each influential person (and its directors and officers) who knowingly influenced the person making the public oral statement (or knowingly influenced a director or officer of the responsible issuer in authorizing, permitting or acquiescing in the making of the public oral statement); and each expert, where misrepresentation from the expert's report, statement or opinion are used in the public oral statement with the expert's consent.

### Burden of proof:

* For "core documents" (prospectus, TOB circular, MD&A, AIF, annual financial statements, interim financial reports), plaintiff need only prove the misrepresentation (s.140)
* Non-core documents, P must also prove the defendant (except an expert), knew of the misrepresentation, deliberately avoided discovering that there was a misrepresentation, or was guilty of gross misconduct

#### Defences

* Onus on defendant (s.140.4)
* Investor knew of the misrepresentation
* Due diligence (see above)
* Justified confidential disclosure of material change
* Misrepresentation was reasonably disclosed, with appropriate cautionary language
* Defendant relied on an expert

#### Damages (Secondary Market)

* Investors are unlikely to receive full compensation (s.140.5)
* Focus is to deter, not to compensate
* Damages for **acquisition** **after** **the misrepresentation**/failure to make disclosure:
  + Disposed on/before 10 days after: average price paid and price received on disposition
  + After 10th trading day: damages are the lesser of the difference between average price paid and price received on disposition, OR, the difference between average price paid and the average price over the 10 trading days after public correction or disclosure
  + Where securities are not disposed: damages are difference between average price paid and average trading price over 10 days after public correction
* Defendant may decrease damages by proving that some portion of the price difference was attributable to factors other than the misrepresentation or failure to make timely disclosure
* Liability is proportionate, not joint and several
* There is a liability cap, but it is not awarded if D had knowledge of the misrep or failed to make timely disclosure
  + For a responsible issuer or non-individual influential person: greater of $1M or 5%
  + Director, officer, or person who made misleading public oral statement: greater of $25k or half compensation received over 12 months

# Investment Funds

* Vehicles for retail investors to invest in the markets with professional help, at a relatively cheap rate
* Can have trust, corporations, LLPs
* It is a growing market segment in Canada
* Investment fund is defined as "mutual fund or non-redeemable investment fund (NRIF)"
* Different definition of material change for mutual fund, to be more suited to the situation
  + Change in "business, operations, or affairs of the issuer that would reasonably be expected to have a significant effect on the market price or value of the security of the issuer"
* Standard of care for an investment fund manager
  + Obligations is to act in fiduciary manner towards the fund
  + Reasonably prudent person in the circumstances
* Civil liability for failure to deliver documents
  + Otherwise secondary market applies
* Mutual funds have to file simplified prospectus, AIF, fund facts, but only send the fund facts to the investor
  + Fund facts have to be written to a grade six level
  + NRIFs do not have to
* Continuous disclosure - 81-106 - applies to NRIFs as well
  + Management Reports, financial statements, quarterly reports, AIF
  + Calculation of Management Expense Ratio - Section 15.1, 15.2
* NI 81-102
  + Talks about how you can run an investment fund
  + Restrictions on concentration on particular assets etc.
  + Part II limits what investment funds can do
    - Can't purchase property, mortgages
    - Can't purchase commodity
    - Can't purchase commodity derivatives
  + NRIF can't buy property, but can buy many more commodities and can leverage themselves better using derivatives
    - Can offer better returns
* Concern is that people are not understanding the risks about NRIFs
* MER is a tail-end commission rate based on operating fees and management fees
  + If you want to make a profit, you have to do better than the commission rate
  + It is not correlated to success
* Mutual Funds:
  + Can cash out any time, redeemable
  + Language of mutual funds is falling out of Nis
* NRIF
  + Can sell them but have to sell them on the market somewhere
  + Can't sell them back to the fund itself
  + People are increasingly buying into them
  + More speculative, have to have more money, commit to money being used over longer period of time
  + Concern that mom and pop were buying into these
  + Proposals that the rules of mutual funds are going to be expanded to NRIFs

* Three main actors:
  + Wholesaler/manufacturer
    - Financial institutions that establish in the fund or trust and build the financial instruments that people can buy
    - Mainly banks and independent fund manufacturers
    - Big mutual fund manufacturers
  + Fund Managers
  + Distributors/dealers/advisors
    - Try and sell you the instruments
    - If you are an investment dealer, you can sell anything
    - If you are a mutual fund, you can only sell mutual funds
* Regulators are trying to reform this industry
  + 31-103 has made distributors and fund managers registrants

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* *Richard Bruce Moore (Settlement)*

* *Walton* increased the circumstantial evidence requirement
  + - The tipper needs to know or intend that it is likely that the recipient will act on that info in some way

* *In the Matter of Jowdat Waheed and Bruce Walter ("Baffinland")*
  + Generally disclosing among industry specialists is not public disclosure