WeirFoulds LLP

SECURITIES LAW QUARTERLY

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A Newsletter Providing Concise Updates on Securities Law Developments

In this inaugural issue, we cover legal developments in three key issue areas: Offerings, Corporate Governance, and Continuous Disclosure. Our coverage is succinct and targeted to serve the needs of issuers and their advisors. For more detailed analysis, please visit us online at www.WeirFoulds.com.

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Offerings

This quarter, we have summarized two developments with regard to offerings - the Ontario Securities Commission ("**OSC**") is looking to increase its fees and the Canadian Securities Administrators ("**CSA**") is continuing its review of prospectus exemptions.

OSC to Increase Participation & Activity Fees

On August 23, 2012, the OSC published proposed amendments to OSC rules 13-502 and 13-503, which would increase the OSC's fees for the next three years. The OSC stated that it is facing a budget shortfall and is projected to run a deficit of $6.5 million in its current fiscal year (which ends March 31, 2013). While this deficit will be paid out of its surplus fund in the short-term, the OSC is looking to increase fees on both issuers and registrants to cover its costs.

On average, the total participation fees paid by issuers will increase by 15.5% per year for the next three years. This will result in issuer participation fees being 54% higher in 2015 than they are today. Registrant participation fees will see an increase of only about half that amount as their rates are set to go up 7.9% per year (approximately 25% by 2015). The OSC has indicated this difference is an attempt to bring the balance of total fees paid by issuers and registrants closer to 50/50.

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Activity fees will also be increasing in several categories such as the fee for filing a preliminary prospectus which is slated to increase from $3,250 to $3,750 and the additional fee for filing a preliminary prospectus accompanied by a technical report is proposed to increase from $2,000 to $2,500. Take-over bid circulars and issuer bid circulars will rise in cost from $4,000 to $4,500 and rights offering circulars will go from $2,000 to $3,750. If approved, the new model will be in effect for a three-year period, starting April 1, 2013. The OSC is seeking comments on the proposed changes during the comment period which closes on November 21, 2012.

OSC Provides Update on its Review of Prospectus Exemptions

On June 7, 2012, the CSA published Staff Consultation Note 45-401 – an update on the status of their review of the "minimum amount" and "accredited investor" exemptions. Back in November 2011, CSA staff put out a consultation paper and asked for feedback from market participants. This notice serves to update market participants on the status of this consultation process since the comment period closed in February 2012.

In the note, the CSA provided a high-level overview of the comments received. For the "minimum amount" exemption, depending on the results of the consultation process, the CSA may (1) retain the minimum amount exemption in its current form; (2) adjust the $150,000 threshold (up or down); (3) limit the use of the exemption to certain investors, such as institutional investors and not individuals; (4) use alternative qualification criteria; (5) impose other investment limitations, or (6) repeal the exemption. The CSA stated that from feedback reviewed so far, some commentators wanted to increase the $150,000 threshold or impose additional limitations on the use of the exemption to ensure sufficient investor protection, while others stated that the exemption should remain as is or should be broadened to increase access to capital and investment opportunities.

For the "accredited investor" exemption, the CSA is considering whether to (1) retain the exemption in its current form; (2) adjust the income and asset thresholds in the definition of accredited investor; (3) use alternative qualification criteria for individuals; (4) limit the exemption to certain investors, such as institutional investors and not individuals; and (5) impose other investment limitations. An equally diverse selection of comments were received about changing the accredited investor exemption – some in favour of loosening the standard, some preferring to tighten restrictions, and others preferring different proxies for investor sophistication based on an investor's education, work experience or investing experience.

CSA staff have indicated that they need further time to complete their review and intend on finalizing their assessment and publishing a final report later in 2012. They have not indicated what direction their final report will take, but regulators in the U.S. have recently amended their "accredited investor" exemption to exclude the value of an individual's primary residence as part of their net worth calculation.

Corporate Governance

Two court rulings were issued this quarter that touched on shareholder democracy issues - the first criticized "empty voting" and the second nullified results of an AGM because of improper proxy solicitation. The OSC also released its 2012 report on August 22, 2012, which covered shareholder democracy topics including director elections and the proxy voting system.

Court Criticizes "Empty Voting" by Hedge Fund

On September 11, 2012, the British Columbia Supreme Court released its decision in *Telus Corporation v CDS Clearing & Depository Services Inc.* in which it roundly rejected a hedge fund's practice of "empty voting". Empty voting is a practice that results in a separation (either full or partial) of the right to vote at a shareholders' meeting from beneficial ownership of the shares on the meeting date. It can result from several different circumstances from the benign (shares bought and sold between the record date and the meeting) to the potentially dangerous (hedging or borrowing techniques that permit activist investors to gain votes while avoiding market exposure).

The fund in this case caused CDS to requisition a meeting of TELUS's shareholders. TELUS's board refused to call the meeting, in part, because it alleged that the requisition was invalid because the hedge fund is an "empty voter". While the result did not turn on empty voting, the court took the opportunity to make some strong comments on it: "the practice of empty voting presents a challenge to shareholder democracy" because "the interests of such an empty voter and the other shareholders are no longer aligned and the premise underlying the shareholder vote is subverted."

The fund has appealed the decision and it will be important to note how the B.C. Court of Appeal sees the practice. Shareholder democracy has also been top of mind for the OSC and the regulator has stated its goal of facilitating shareholder empowerment in director elections by advocating for the elimination of slate voting, the adoption of majority voting policies for director elections and enhancing disclosure of voting results for shareholder meetings.

Court Finds "TeleVote" Proxy Solicitation Improper

On August 8, 2012, the British Columbia Supreme Court released another notable decision in *International Energy and Mineral Resources Investment (Hong Kong) Company Limited v Mosquito Consolidated Gold Mines Limited*. The court overturned the results of an annual general and special meeting of shareholders ("AGM") of a public mineral exploration and development company because of improper proxy solicitation.

The AGM was contested with management and a group of dissident shareholders each proposing a different list of directors. Management retained proxy solicitation agents that utilized a "TeleVote" system (a process of collecting shareholder voting information over the phone), which the Court ruled was oppressive and unfairly prejudicial to the dissident shareholders because (i) the oral grant of authority used was inconsistent with the legislative requirements, (ii) no unique identifier was used when shareholders placed their vote (only the shareholder's postal code was noted), (iii) the proxy solicitation agent did not have a properly defined and complete record of oral grants of authority which could be readily checked for accuracy, (iv) the proxy agent faced a conflict of interest because it was soliciting proxies on behalf of management and also recording shareholders' voting instructions, and (v) the use of the "TeleVote" system was not

disclosed in management's proxy circular.

While being critical of the particular techniques used in the case before it, the Court also noted that telephone proxy solicitation was "a legitimate attempt to streamline shareholder proxy solicitations" and that if proper protocols were put in place, it could be an appropriate choice to facilitate shareholder meetings.

OSC 2012 Annual Report Highlights Corporate Governance Issues

On August 22, 2012, the OSC released its 2012 Annual Report, which details the Commission's significant activities in 2011-12. Shareholder democracy issues were highlighted in the report as the OSC is working toward increasing shareholder engagement by strengthening shareholders' rights and facilitating the effective exercise of voting rights. In particular, the OSC is considering specific policy initiatives that would support the role of shareholders with regard to uncontested director-elections, which the OSC sees as a significant governance issue. As well, the report examines concerns about the effectiveness of the proxy voting system and states that the OSC is currently investigating concerns raised by market participants about the transparency, efficiency and accountability of the proxy voting system.

The Report also mentioned the OSC's *Emerging Markets Issuer Review*, released earlier in 2012, which assessed the quality and adequacy of the disclosure and corporate governance practices of 24 emerging markets issuers, and examined the manner in which they accessed Ontario's markets. That review raised concerns about governance practices by reporting issuers that were listed on Canadian exchanges and had significant business operations in emerging markets.

Continuous Disclosure

Continuous disclosure issues are an important topic in securities regulation in the third quarter of 2012 as the CSA released the findings of their 2012 continuous disclosure review and also a staff notice on the proper use of a preliminary economic assessment ("PEA") by mining issuers.

CSA's Annual Continuous Disclosure Review Finds Deficiencies

On July 20, 2012, the CSA released CSA Staff Notice 51-337, *Continuous Disclosure Review Program Activities for the fiscal year ended March 31, 2012*. The CSA's continuous disclosure review program has dual objectives - education and compliance, which are achieved by identifying specific deficiencies and also providing notice to market participants of common issues.

The CSA conducted an IFRS issue-oriented review by reviewing the financial statements of selected issuers in addition to their MD&A. Staff noted that the most common MD&A deficiency was issuers not clearly labeling and identifying the accounting principles used when they presented a mix of financial information in accordance with pre-changeover Canadian GAAP and IFRS.

The CSA also conducted a review of issuers engaged in oil and gas activities to assess compliance with requirements set out in National Instrument 51-101, *Standards of Disclosure for Oil and Gas Activities (NI 51-101)*. Noted deficiencies included: (i) lack of disclosure on significant factors and uncertainties; (ii) improper use of the terminology set out in the Canadian Oil and Gas Evaluation Handbook (COGEH); (iii) not including all required signatures on Form 51-101F3, *Report of Management and Directors on Oil and Gas Disclosure*; (iv) non-compliance with NI 51-101 and Revised CSA Staff Notice 51-327, *Guidance on Oil and Gas Disclosure*, concerning the disclosure of resources other than reserves; (v) no provision of appropriate cautionary language concerning the 6:1 boe conversion ratio of natural gas to oil so as to clearly discern between the energy equivalency and the market price equivalency; (vi) and lack of consistency and accuracy in the use of units of measurement and disclosure of reserves within and between disclosure documents.

CSA Concerned About Disclosure in Mining Technical Reports

On August 16, 2012, the CSA released *CSA Staff Notice 43-307 Mining Technical Reports - Preliminary Economic Assessments*. The notice addresses certain concerns of CSA staff regarding the use and disclosure of a preliminary economic assessment ("PEA") by a mining issuer.

CSA staff stated that amendments to National Instrument *43-101 Standards of Disclosure for Mineral Projects* (NI 43-101) that took place in 2011 are being misinterpreted by some issuers. The amendments in 2011, included a change in definition of a PEA so that they are no longer restricted to early-stage projects. This resulted, according to CSA staff, in issuers inappropriately using PEAs in several different ways: (i) using a PEA as a Proxy for a pre-feasibility study, (ii) preparing a PEA using inferred mineral resources, concurrently with or as an add-on or update to their Pre-Feasibility Study or Feasibility Study, (iii) disclosing results of potential economic outcomes for their material mineral properties that are not supported by a technical report; (iv) appearing to use "overly optimistic or highly aggressive assumptions" or methodologies that diverge significantly from industry best practices in the PEA; (v) disclosing the results of a PEA that includes projected cash flows for by-product commodities that are not included in the mineral resource estimate; and (vi) releasing PEAs where individuals are taking responsibility (full or partial) for technical reports that support the results of a PEA, while not possessing relevant experience. The notice provides guidance on avoiding these situations.

OSC Panel Provides Analysis on Insider Trading Provisions in OSA

On August 1, 2012, the OSC released a decision in an insider trading case, which contained analysis of the phrase "person or company in a special relationship with a reporting issuer" from section 76(5) of the Securities Act (Ontario). Section 76(5) prohibits a person from trading in the securities of an issuer with which the person is in a "special relationship" on the basis of material facts or material changes that have not been generally disclosed.

At an August 2008 golf tournament, Paul Donald, a former Research in Motion ("**RIM**") executive, heard from another RIM executive that RIM was interested in acquiring Certicom. He promptly purchased $305,000 worth of Certicom shares and later made $295,000 when RIM completed its plan of arrangement in March 2009.

The OSC hearing panel decided that Donald's actions did not constitute insider trading because RIM was not yet "proposing" any acquisition of Certicom in August 2008. Approval of RIM's senior management had not occurred when Donald received the information. According to the panel, without a final decision, RIM could not be said to be "proposing" any action. Despite this finding, Donald's actions were still found to be contrary to the public interest and a hearing (for which a decision has not yet been released) was scheduled for September 13, 2012, to determine the appropriate penalties for Donald. The OSC has the authority to levy fines or ban an individual from becoming an officer or director of a public company.

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Securities Practice

Our extensive experience enables us to advise on the operation and regulation of markets, both in Canada and abroad. We represent local and national issuers, securities dealers and advisors, underwriting syndicates, financial institutions, boards of directors, special committees and lenders, investors and venture capitalists as well as foreign issuers and investors in the Canadian and US financial markets.

We provide legal advisory services to public and private companies as well as governmental organizations throughout Canada to assist in entering and resolving capital market, restructuring, and merger and acquisition related matters. In addition, with the assistance of our litigation lawyers, we provide expert litigation support for a wide range of matters related to securities regulation. We advise securities dealers on the underwriting of offerings, registration of Canadian and foreign investment dealers, limited market dealers, portfolio managers and advisers, representation at broker-dealer disciplinary hearings and Ontario Securities Commission compliance.

If you would like more information, please contact Michael Dolphin, Kim Lawton or another member of the securities group.

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