Halloween or as the Celtic say *Samhain*!

According to sources like Wikipedia and the Huffington Post, Halloween originated from the Celtic festivals. The word refers to, among other things, the *Day of the Dead*. As scary as that may sound (and October 31st is quickly approaching), there is nothing scary or unpredictable on this month's securities update. Here is AUM Law's take on recent regulatory pronouncements.

In this bulletin:

1. Proposed Changes in Québec: The Financial Sector

On October 5, 2017, Quebec's Minister of Finance introduced Bill 141 to Quebec's National Assembly which is an omnibus bill meant to modernize the framework of Quebec's financial sector. If passed into law, Bill 141 will among other things:

- replace the province's existing insurance legislation with a new *Insurers Act*;
- substantially amend the current *Act respecting financial services cooperatives* and the *Deposit Insurance Act*, the latter being renamed the *Deposit Institutions and Deposit Protection Act*;
- replace the province's existing trust and savings companies legislation with a new *Trust Companies and Savings Companies Act*;

In Brief

A Quick Update on Federal Government's Tax Proposal

Presumably as a result of over 21,000 submissions on the "*Tax Planning Using Private Corporations*" released on July 18, 2017 (the "**Consultation Paper**"), the Federal Government of Canada announced certain changes to the proposed tax reform presented in the Consultation Paper. While we do not provide advice on tax law, we wanted to ensure that you are aware of these changes.

Some of the changes to what we have previously reported on include:

1. With respect to the taxation of passive income inside a private corporation, up to $50,000 earned by a corporation in a

- amend the *Act respecting the Autorité des marchés financiers,* which will be renamed the *Act respecting the regulation of the financial sector*; and
- amend various other legislation, including the *Securities Act*, the *Derivatives Act*, the *Civil Code of Quebec,* the *Automobile Insurance Act*, the *Professional Code*, the *Real Estate Brokerage Act*, the *Act respecting the distribution of financial products and services* and the *Money-Services Businesses Act*.

If this bill is adopted, it would result in numerous changes to the operation of Quebec's financial sector including:

- restricting commission sharing received by a mutual fund broker or a scholarship plan broker;
- capturing derivatives trading platforms as regulated entities under Quebec's *Derivatives Act;*
- facilitating the distribution of certain financial products, including insurance products, via the Internet and other technological means; and
- providing additional protections for whistleblowers who disclose breaches of financial section legislation.

As part of the reorganization of Quebec's financial sector, adoption of the Bill will also result in the abolishment the province's current self-regulatory organizations, including the Chambre de la sécurité financière and the Chambre de l'assurance dommages, which will be moved under the purview of the Autorité des marchés financiers (the AMF). The transferred responsibilities include jurisdiction over the professional conduct, discipline and continuing education of licensed representatives that provide financial planning services and distribute various financial products, including insurance, mutual funds and scholarship plans.

While it is not yet certain when the Bill will be adopted into law, the current intention is for the Bill to be in force by the end of Quebec's 2018 spring parliamentary session. Interested parties who may be affected by the changes or who may wish to comment on the legislation should monitor the release of the various regulations that will be put forward by the government in support of the proposed legislative amendments.

2. Proposed OSC Rule 72-503 *Distributions Outside Canada:* Out of Sight, Out of Mind?

The OSC is currently reviewing comments on its latest draft of Proposed OSC Rule 72-503 *Distributions Outside Canada* (the "**Proposed Rule**"). The Proposed Rule is intended to clarify when prospectus requirements do not apply to a distribution of securities to investors outside of Canada. If the Ontario rules do not apply (i.e. there is no distribution or registerable activity happening in Ontario because the securities have come to rest outside of Ontario), then there is no need to rely on an exemption from the prospectus or registration requirements.

The Statement of Principle in the proposed Companion Policy indicates that in order to ensure securities come to rest outside of Canada, the issuer and other participants in the offering must take reasonable steps including obtaining representations from purchasers outside of Canada that they are purchasing with investment intent and not for the purpose of making an immediate resale. A number of other actions are suggested in the Statement of Principle.

If the Statement of Principle is difficult to apply in the circumstances, or the issuer chooses not to do the foregoing analysis, the Proposed Rule provides a number of possible prospectus exemptions for the issuer and registration exemptions for the foreign dealer (provided the distribution is not part of a plan to avoid the prospectus requirement in Canada). One proposed prospectus exemption would be available to a non-reporting issuer for a distribution of its own security to a person outside of

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taxation year will not be subject to the increased taxes previously announced. The increase in taxation would apply to passive income over $50,000 retained in a private corporation.

2. Simplifying the new "dividend sprinkling rules" announced in the Consultation Paper. The Federal Government has not yet provided details on how such rules will be simplified. The details are expected to be included in the revised draft legislation.
3. Abandoning the proposed restrictions to the Lifetime Capital Gain Exemption as set out in the Consultation Paper.
4. Proposing to lower the small business tax rate to 10% from the current rate of 10.5% effective January 1, 2018, and to 9%, effective January 1, 2019.

If you think you might be impacted by the proposed changes, we advise you to speak with your existing tax advisor or reach out to us to help you connect with a tax specialist or otherwise assist you.

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Investment Fund Issuers Filing Annual Reports: Filing Deadline Approaching for New Form 45-106F1 *Report of Exempt Distribution*

Investment fund issuers relying on certain prospectus exemptions who are planning

Canada, as long as the issuer has materially complied with the securities law requirements of the jurisdiction outside Canada.

Issuers relying on the prospectus exemptions would have to electronically file a streamlined report of exempt distribution on or before the 10th day after the distribution date (or not later than 30 days after the end of the calendar year in which the distribution occurred for investment funds).

With respect to registration requirements, the OSC notes that registration as a dealer is generally required in Ontario if registerable activities are provided to Ontario investors or are otherwise conducted in Ontario regardless of where the investor is located. However, there may still be a question as to whether foreign dealers that participate in the distribution of securities by an Ontario issuer to purchasers outside Canada are subject to these requirements. For that reason, a dealer and underwriter registration exemption would be available to a person in connection with a distribution of securities to an outside person if a number of conditions are met. One such requirement (in the context of a distribution being made to a purchaser in the United States) is that the person must either be (i) registered as a broker-dealer with the SEC, be a member of FINRA and materially comply with all applicable conduct and other regulatory requirements of U.S. federal securities law, state securities law of the United States and FINRA rules in connection with the distribution; or (ii) exempt from registration as a broker-dealer with the SEC and materially comply with all applicable regulatory requirements of U.S. federal securities law in connection with the distribution.

While the Proposed Rule is intended to provide additional clarity to cross-border offerings, some additional questions remain. Please feel free to contact us if you have any questions on the application of the Statement of Principle or the exemptions.

3. OSC Corporate Finance Branch Report: Key Takeaways

The Corporate Finance Branch of the Ontario Securities Commission ("**OSC**") released its 2016-2017 Annual Report (OSC Staff Notice 51-728) (the "**Report**"). The objective of the Report is to encourage compliance, improve disclosure in filings, and discuss trends and key policy initiatives. We highlight below some of OSC's key findings from its compliance review of issuers and key takeaways.

By way of background, the Corporate Finance Branch of the OSC conducts two types of reviews of issuers in the context of continuous disclosure: a full review (which involves a review of financial statements, annual reports, material change reports, MD&A, etc.) and/or an issue oriented review (which targets a specific legal, regulatory or accounting issue). The OSC uses a risk-based approach when selecting an issuer for review. The majority of compliance reviews in the 2016-2017 period involved issue oriented reviews. The outcomes of the reviews included education and awareness, prospective disclosure enhancements, refiling, as well as other outcomes like enforcement action.

The Report emphasizes that many issuers struggle with providing meaningful disclosure that is both useful and understandable. The Report also reminds issuers to avoid using boilerplate disclosure and include detailed discussions about factors that affect revenues and expenses, not simply discussing changes in percentages.

The Report also encourages issuers to adopt a social media disclosure policy. The Report indicates that disclosure on social media should be simultaneous as filings on SEDAR, and social media disclosure cannot be unbalanced, insufficient or inconsistent with information filed on SEDAR.

The Report underscores the significance of disclosure of cyber security risks. In particular, disclosure by issuers whether cyber security incidents could pose a

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to file their annual reports of exempt distribution (the "**Form 45-106F1**") in January should be thinking now about coordinating and preparing the report well in advance of the filing deadline of **January 30, 2018** (in particular those investment fund issuers that will be filing the new form of Form 45-106F1 for the first time).

To recap some of the changes, the new form requires the filer to confirm that each individual listed in Schedules 1 and 2 of the report was notified about the collection of information by the applicable local securities regulatory authority and its use, and that the individual has authorized the indirect collection of the information.

Please reach out to an AUM Lawyer and we would be pleased to assist you with your filings and any related questions.

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We can help you put in place a shareholders agreement

We noted in our September 2017 Nutshell – *A Corporate Roadmap – The Importance of Shareholders Agreements*, that it is important to have a shareholders agreement in place where a corporation has more than one shareholder, to set out expectations for management of the business and the relationship between the shareholders, and to provide for how changes in circumstances would be dealt with.

We can draft a basic unanimous shareholders agreement for a corporation for a reasonable fixed fee. Please contact our Corporate Group.

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material risk to the company. The OSC highlights the importance of cyber security disclosure in light of recent cyber attacks.

The Report discusses the OSC's review of the exempt market and identifies concerns regarding the use of the offering memorandum exemption.

Finally, the Report emphasizes the need for non-venture issues to have policies regarding women on boards and in executive officer positions, as well as it indicates that the OSC is reviewing climate change disclosure required in other jurisdictions and is considering the appropriate response for Ontario's capital markets.

We have assisted a number of clients to develop compliant social media governance policies, as well as robust cyber security policies. Please contact us for more information.

4. Issuers with U.S. Marijuana-related Activities: Disclosure

On October 16, 2017, the TMX Group and the CSA published staff notices that impact issuers with U.S. marijuana-related activities.

Canadian Securities Administrators

CSA Staff Notice 51-352 notes that there is a conflict between U.S. state and federal law related to marijuana with certain states permitting its use and sale within a regulatory framework, notwithstanding that marijuana continues to be listed as a controlled substance under U.S. federal law. As such, marijuana related practices or activities, including the cultivation, possession or distribution of marijuana, are illegal under U.S. federal law.

The CSA outlines certain disclosure expectations for issuers that currently have, or are in the process of developing, marijuana-related activities in U.S. states where such activity has been authorized within a state regulatory framework.

The disclosure expectations for issuers with U.S. marijuana related activities are that issuers should:

- describe the nature of the issuer's involvement in the U.S. marijuana industry;
- explain that marijuana remains illegal under U.S. federal law and that the approach to enforcement of U.S. federal laws against marijuana is subject to change, and discuss the risks, including the risk of adverse enforcement action;
- state whether and how the issuer's marijuana-related activities are conducted in a manner consistent with any U.S. federal enforcement priorities; and
- discuss their ability to access both public and private capital and indicate what financing options are/are not available in order to support continuing operations.

There are separate disclosure expectations for other issuers involved directly and indirectly in cultivation and distribution, and those with ancillary involvement.

TMX Group

The TMX Group Staff Notice also notes that it is illegal under U.S. federal law to cultivate, distribute or possess marijuana in the United States. Furthermore, financial transactions involving proceeds generated by, or intended to promote, marijuana-related business activities in the U.S. may form the basis for prosecution under applicable U.S. federal money laundering legislation.

Accordingly, the TSX is of the view that issuers with ongoing business activities that violate U.S. federal law regarding marijuana are not complying with certain sections of the TSX Company Manual. Such business activities may include: (i) direct or indirect ownership of, or investment in, marijuana-related businesses; (ii) commercial interests or arrangements with marijuana-related businesses that are similar in substance to ownership of, or investment in, marijuana-related businesses; (iii) providing services or products that are specifically designed for, or targeted at, marijuana-related businesses; or (iv) commercial interests or arrangements with entities engaging in the business activities described in (iii). In light of its

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2017 Capital Market Participation Fees

The OSC has sent out a notice to all registered firms in Ontario that the 2017 participation fee calculations are updated and available on the OSC website. The OSC reminds market participants that the deadline to file the annual participation fee calculation is **December 1,** and the deadline to *pay* the annual participation fees is **December 31.**

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OSC Tweets Crypto Currency Policy

The OSC recently used Twitter to elaborate on its views regarding cryptocurrency. In particular, the OSC made clear that it is keen to support innovation in the area including initial coin offerings.

However, the OSC indicated that it must balance these new ways of raising capital with the need to protect investors from fraudulent activities.

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position, the TSX will be conducting a review of affected listed issuers. Be Mindful of Local Exemptions and Requirements

5. Be Mindful of Local Exemptions and Requirements

Although National Instrument 45-106 Prospectus Exemptions ("**NI 45-106**") and National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations ("**NI 31-103**") consolidate and harmonize most of the prospectus and registration exemptions available under Canadian securities laws, there continues to be several distinctive local prospectus and registration exemptions as well as some unique requirements that apply in particular Canadian jurisdictions.

By way of example, in Alberta, ASC Rule 45-511 Local Prospectus Exemptions and Related Requirements ("**ASC 45-511**") imposes additional requirements on issuers that deliver an offering memorandum to a purchaser in respect of a distribution made in reliance on the $150,000 "minimum amount investment" prospectus exemption in section 2.10 of NI 45-106. In particular, the offering memorandum must either be prepared in accordance with the form requirements generally applicable to an issuer that relies on the "offering memorandum exemption" or include a form of certificate, executed by the requisite individuals, which states that the offering memorandum does not contain a misrepresentation. In addition, the offering memorandum must include a statement describing the particular rights of action available to the purchaser in Alberta as a result of relying on the exemption.

Local rules such as ASC 45-511 are generally triggered when securities of an issuer (including an Ontario-based issuer) are sold to an investor who resides in the local jurisdiction.

Although there is a relatively high degree of harmonization in Canadian securities regulation, if you are involved in the distribution of securities to investors who reside outside of Ontario, it is important to be aware of local requirements. We would be pleased to help you navigate them.

6. Heads up Portfolio Advisers: Potential new DRO coming to Canada

The CSA is currently considering comments received on its proposal to amend provisions of National Instrument 25-101 Designated Rating Organizations ("**NI 25-101**") and related instruments. The proposal put forward is in response in part to an application by Kroll Bond Rating Agency ("**Kroll**") to be recognized as a DRO for certain purposes. The regulators can make a designation for the purposes of allowing a credit rating organization to satisfy either (i) a requirement in securities law that a credit rating be given by a DRO, or (ii) a condition for an exemption under securities law that a credit rating be given by a DRO. Currently, these credit rating provisions refer to the required credit rating of the four existing DROs, namely, S&P, Moody's, Fitch and DBRS. The CSA is now proposing to recognize the credit ratings of Kroll, but only for the limited purpose of meeting certain eligibility requirements to file a short form or shelf prospectus for issuers of asset-backed securities.

A number of investment policy statements and restrictions require holding securities of a certain rating. If Kroll is recognized as a DRO, among other things, asset-backed securities rated by Kroll may become a permissible investment under such policies, and additional competition among DROs may result.

In addition to the proposed changes relating to Kroll's application, other proposed amendments to NI 25-101 would deal with new requirements in the European Union for credit rating organizations. The changes are required for the EU to recognize the Canadian DRO regime as an "equivalent" regime and thus for the credit ratings of a Canadian office of a DRO to be used for regulatory purposes in the EU. Other changes being proposed reflect amendments to the IOSCO Code of Conduct Fundamentals for Credit Rating Agencies. Some proposed amendments include adding policies to mitigate conflicts and to ensure independence of credit ratings.

In the notice accompanying the proposed changes, the CSA notes that investors could benefit from additional safeguards in NI 25-101, including changes to increase protection of the integrity of the rating process.

7. Cybersecurity Regulatory Guidance

Canadian regulators have been pretty consistent over the last couple of years that registrants need to implement a cybersecurity program as part of its system of controls and risk management obligations. On October 19, 2017, the Canadian Securities Administrators ("**CSA**") released Staff Notice 33-321 *Cybersecurity and Social Media* ("**Staff Notice**") which provides results of a cybersecurity survey that was posed to registrants in October 2016, and provides some guidance on the regulator's expectation regarding what a registrant's cybersecurity and social media program should look like.

1) Policies and Procedures:

There is a clear expectation that registrants have polices for their cybersecurity program and that registrants train employees regarding cybersecurity. Cyber policies should cover a number of areas including:

- electronic communications
- firm issued or firm connected devices
- software update and maintenance
- oversight of third party vendors that have access to technology infrastructure
- incident response plan to a cybersecurity incident
- employee training on topics including password strength, handling confidential information, suspicious emails and escalating cyber security incidents.

2) Risk Assessments:

A firm should do an inventory (at least annually) on the areas of operation most vulnerable to cyber threats and what assets (such as client information) would be exposed if those operations were to be compromised. If exposed, a registrant should have an incident response plan to control the damage. This incident response plan should be tested annually.

3) Third Party Vendors:

A registrant should be conducting due diligence on the vendors that have access to the firm's technology systems. Furthermore, registrants should be adding cybersecurity and privacy information in their service provider contracts including an obligation on the service provider to inform the registrant if it has been part of a cybersecurity incident.

We recommend that you speak to us to ensure you are addressing cybersecurity considerations in your service provider contracts.

4) Data Protection:

Registrants should be encrypting/securing their data by ensuring passwords are required for access to sensitive information and that data is backed up and preserved at an offsite location.

5) Cyber Insurance:

The Staff Notice notes that 59% of registrants currently do not have cybersecurity insurance.

6) Small and Medium Sized Firms:

The Staff Notice indicates that many respondents to the survey believed their cybersecurity risk to be low due to the size of their firm. The Staff Notice makes it clear that the financial industry is a known target of cyber-attacks. Accordingly, regardless of size, registrants should ensure they have a strong cybersecurity program.

7) Social Media:

Registrants must have policies and procedures in place to monitor employees for unauthorized use with respect to social media.

If you require further information or you are looking to build up your cybersecurity program, please reach out to us.

News & Events

AUM Law Team Member Announcement

We are very pleased to announce that **Janet Holmes** has joined the firm as Director, Knowledge Management and Communications and as Special Counsel.

Janet was a Senior Vice President in the Government and Public Affairs team at Moody's Corporation, where she was deeply involved in helping the rating agency transition to a highly regulated environment across the globe. Before joining Moody's in 2007, she worked as a Senior Corporate Governance Specialist at the Organization for Economic Cooperation and Development. Before that, she spent nearly six years at the Ontario Securities Commission, first as Senior Legal Counsel for its Takeover Bid Team and later as Manager of International Affairs. She also was seconded to the UK Financial Services Authority for a year, where she worked on the implementation of new laws for insider trading and market abuse. Before joining the OSC in 1998, she worked for law firms in New York and Toronto, including as a partner in the Research Group at Davies, Ward & Beck.

Please join us in welcoming Janet to the team!

TDSI Alternative Fund Summit

Our very own **Jeff Scanlon** spoke at the recent TDSI Alternative Fund Summit on October 17th, 2017. Jeff discussed the important topics of heightened KYC and suitability expectations, heightened liability and best interest, and targeted reforms. AUM Law continues to be active in the community and at the forefront of regulatory change.