CSA Proposes Changes to National Instrument 45-106 Prospectus and Registration Exemptions Relating to Short-term Debt and Securitized Products

On January 23, 2014, the CSA published for a 90-day comment period proposed amendments that would modify the credit ratings required to distribute short-term debt, primarily commercial paper ("CP"). The proposed short-term debt prospectus exemption ("Short-term Debt Prospectus Exemption"), would remove the split rating condition that currently requires CP's to have a rating at or above the designated ratings thresholds, and if a second rating is obtained, it could not be below any of the same designated rating threshold. Instead, a "modified split rating" would require that CP's not have any ratings below a different set of designated rating threshold. The Short-term Debt Prospectus Exemption are intended to:

- remove the regulatory disincentive for some CP issuers to obtain an additional credit rating;
- provide consistent treatment of CP issuers with similar credit risk; and
- maintain the current credit quality of CP distributed under the Short-Term Debt Prospectus Exemption.

The CSA also proposes to modify its 2011 proposals regarding eligible securitized products investors exemptions. The 2011 proposals represented CSA's then regulatory response to the collapse of Canada's non-bank sponsored asset-backed CP ("ABCP") market triggered by the 2008 global financial crisis.

In respect of short-term securitized products, the CSA proposes to amend NI 45-106 as follows:

- The following prospectus exemptions would be unavailable for the distribution of short-term securitized products:
  - the Short-Term Debt Prospectus Exemption;
  - the private issuer prospectus exemption;
  - the family, close friends and close business associates exemptions;
  - the founder, control person and family exemption; and
  - the offering memorandum exemption.
- A new "Short-Term Securitized Products Prospectus Exemption" would be introduced.
- Issuers who distribute securities under the Short-Term Securitized Products Exemption would be subject to additional initial offering and ongoing disclosure obligations.

The CSA also proposes to make certain consequential amendments to National Instrument 25-101 *Designated Rating Organizations* (the DRO Rule), and to Companion Policy 45-106 *Prospectus and Registration Exemptions*.

The CSA arrived at their present approach after receiving mostly concerned feedback on their 2011 proposals citing, among others, that it was unfair to group ABCP's with other less risky forms of asset-backed securities. Further, the CSA came to the view that systemic risk in the Canadian financial markets, as was apparent during the 2008 financial crisis, has been mitigated for three reasons:

1. A large majority of Canadian securitized products are government guaranteed. As a result, these products are not

2. prone to investor flight or fire sales that occurred in the mortgage-back securitization sector in the U.S. during the 2008 crisis;

3. The current Canadian "private-label" securitization sector is conservative and mostly sponsored by Canadian banks with oversight by the Office of the Superintendent of Financial Institutions; and

4. The assets being securitized in the current Canadian market are traditional, cash-flow generating assets such as credit cards, as oppose to unconventional, synthetic and leveraged assets such as sub-prime mortgages, which had mostly been sponsored by non-bank entities not subject to prudent oversight. Post 2008 crisis, such complex, high-risk ABCP's are no longer being issued in Canada.

Comment period regarding the above proposals is open until April 23, 2014.

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a cautionary note

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