

# NO LONGER A "LAND OF CONFUSION" – OSC RULE 72-503 AND UPCOMING AMENDMENTS REGARDING DISTRIBUTIONS OUTSIDE CANADIAN BORDERS HELP LIFT THE FOG

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## Notice of Amendments

On March 31, 2018 Rule 72-503 – *Distributions Outside of Canada* (Rule 72-503 or the Rule) came into force following receipt of Ministerial approval. This Bulletin will examine the prospectus exemptions introduced by Rule 72-503 as well as exemptions for the resale of securities outside of Canada scheduled to come into force on June 12, 2018 as a result of amendments to National Instrument 45-102 – *Resale of Securities* (NI 45-102) and additional amendments to Rule 72-503. Together, these regulatory developments significantly clarify the rules for market participants applicable to distributions and resales of securities outside of Canada.

## Background to Amendments

On June 30, 2016, the Ontario Securities Commission (OSC) published initial proposals for OSC Rule 72-503 along with a corresponding form and companion policy. A number of comments were received prior to the end of the comment period in the fall of 2016, and on June 29, 2017, the OSC published an updated version of Rule 72-503, the corresponding form and companion policy. The final form of Rule 72-503 was published on December 21, 2017.

Rule 72-503 is intended to provide certainty to market participants in cross-border transactions. The Rule replaces OSC Interpretation Note 1 – *Distributions of Securities Outside Ontario* (Interpretation Note 1) which has been in force since 1983. Interpretation Note 1 required issuers to take the vaguely worded 'reasonable precautions' to ensure securities were distributed outside of Ontario (and thereby not trigger prospectus requirements in Ontario). Uncertainty over the application of Interpretation Note 1 made cross-border distributions increasingly difficult to administer over time.

## New Prospectus Exemptions in Rule 72-503

The Rule provides an exemption from the prospectus requirement in Ontario under the following circumstances:

- *Foreign Public Offering Document* - A distribution of securities is made to a person or company outside of Canada if:
  1. the issuer has filed a registration statement in accordance with US securities laws which is effective as of the distribution date; and/or
  2. the issuer has filed an offering document that qualifies, registers or permits the public offering of the securities in accordance with the securities laws of a 'specified foreign jurisdiction'<sup>[1]</sup> and received a receipt or acknowledgement of approval or clearance, as applicable in such jurisdiction;
- *Compliance with Foreign Disclosure Requirements and Concurrent Ontario Distribution* - A distribution to a person or company outside of Canada if:
  1. the issuer or selling securityholder, as applicable, has materially complied with the disclosure requirements applicable under the securities laws of the foreign jurisdiction, or if the distribution is exempt under such laws; and
  2. the issuer has filed with the OSC and obtained a receipt for a final prospectus qualifying a concurrent distribution of the same class or type of securities to purchasers in Ontario;
- *Reporting Issuer and Compliance with Foreign Disclosure Requirements* - A distribution to a person or company outside of Canada by a reporting issuer in a jurisdiction of Canada if the issuer has materially complied with the disclosure requirements of the foreign jurisdiction applicable to the distribution, or the distribution is exempt from such requirements<sup>[2]</sup>; and
- *Non-Reporting Issuer and Compliance with Foreign Disclosure Requirements* – A distribution to a person or company outside of Canada by an issuer that is not a reporting issuer if the issuer has materially complied with the disclosure requirements of the foreign jurisdiction applicable to the distribution, or the distribution is exempt from such requirements.

### **Availability of Prospectus Exemptions**

Each of the exemptions listed above include distributions made on or through the facilities of an exchange or market outside of Canada to a person outside of Canada as long as neither the seller nor any person acting on behalf of the seller has reason to believe that the distribution has been pre-arranged with a buyer in Canada.

Issuers that rely on the above exemptions are required to file the information set forth in Form 72-503F – *Report of Distributions Outside of Canada* electronically through the OSC's electronic filing portal within 10 days of the distribution date (or within 30 days after the end of the calendar year for issuers that are investment funds).

Securities issued pursuant to the first three exemptions above are freely tradeable, and securities issued pursuant to the fourth exemption above will be subject to a 'restricted period' under Canadian resale rules, requiring four months to have elapsed from the later of the distribution date and the date the issuer became a reporting issuer in a jurisdiction of Canada in order for the securities to be freely tradeable.

The exemptions in Rule 72-503 are not available with respect to a transaction or series of transactions that are part of a plan or scheme to avoid the prospectus requirements in connection with a distribution to a person or company in Canada.

### **Registration Exemptions**

Part 3 of Rule 72-503 provides exemptions from dealer and underwriter registration requirements in connection with distributions of securities outside of Canada if certain conditions are met. As this Bulletin is focused on prospectus exemptions, such exemptions are not summarized herein but can be found in the Rule itself:

[http://www.osc.gov.on.ca/en/SecuritiesLaw\\_rule\\_20180322\\_72-503\\_rule-distributions-outside-canada.htm](http://www.osc.gov.on.ca/en/SecuritiesLaw_rule_20180322_72-503_rule-distributions-outside-canada.htm).

### **Companion Policy and Statement of Principle**

The prospectus exemptions in Rule 72-503 are largely based on the assumption that the distribution is taking place in accordance with the laws of the foreign jurisdiction and therefore, the prospectus requirements in Ontario will be duplicative and not necessary. The companion policy to Rule 72-503 (CP) reiterates this in its statement of principle that the Ontario prospectus requirement does not apply to a distribution of securities outside of Canada that is made in compliance with the securities laws of the foreign jurisdiction in which the investor is located.

Notwithstanding the foregoing and the repeal of Interpretation Note 1, the OSC still expects an issuer, selling security holder, underwriter and other participants in the distribution to take sufficient measures in the circumstances of the distribution (similar to the 'reasonable precautions' referenced in Interpretation Note 1) to make it reasonable to conclude that the offered securities come to rest outside of Canada:

- a restriction in the dealer agreement that prohibits the sale of securities to any person or company in Canada, except pursuant to a Canadian prospectus or in reliance on an available prospectus exemption;
- clear statements in the offering document that the securities: (i) have not been qualified for distribution by prospectus in Canada, and (ii) may not be offered or sold in Canada during the course of their distribution except pursuant to a Canadian prospectus or in reliance on an available prospectus exemption;
- the distribution is conducted as a broad-based public offering in one or more foreign jurisdictions and, if

there is no existing trading market outside of Canada, it is reasonable to expect that a trading market for the offered securities will develop outside Canada; and

- purchasers outside Canada provide representations and warranties, or are given notice that their purchase of the securities will be deemed to constitute a representation and warranty, that they are purchasing the securities with investment intent and not with a view to distribution.

The CP further states that the OSC will not view reliance on an exemption available under the Rule itself as determinative that the Ontario prospectus requirement would not otherwise apply to a distribution outside of Canada or to activities related to the distribution.

### **Additional Exemptions for Resales Outside Canada to Come into Force in Summer, 2018**

There have always been significant concerns amongst market participants regarding the limitations on the ability to resell securities of issuers that have a minimal connection to Canada. In its original form, Rule 72-503 proposed amendments that were broader (with respect to resale among other things) than what exists in the final Rule 72-503, however, notwithstanding this, the OSC has confirmed that the final amendments to come into force in the summer of 2018 (which will amend NI 45-102 and Rule 72-503) should be sufficient to address these concerns.<sup>[3]</sup>

NI 45-102 will be amended to provide a prospectus exemption in connection with the resale of securities acquired in a distribution in Canada by a 'foreign issuer' where such resale occurs on an exchange or market outside of Canada or to a person or company located outside of Canada. For this purpose, the concept of 'foreign issuer' represents a new way to evaluate an issuer's connection to Canada. The term is defined to mean an issuer that is not incorporated or organized under the laws of Canada unless one of the following applies: (i) the issuer has a head office in Canada; or (ii) the majority of its directors or executive officers ordinarily reside in Canada. The amendment to NI 45-102 is expected to come into force on June 12, 2018.

The existing exemption for the resale of securities of non-reporting issuers set out in Section 2.14 in NI 45-102 created practical difficulties for some foreign issuers in meeting the minimum ownership restrictions (requiring that residents of Canada not to hold more than 10% of the outstanding securities of the issuer) in order to be eligible for use of the exemption.

In Ontario, the OSC is amending Rule 72-503 to reflect both the existing resale exemption in NI 45-102 as well as the new exemption expected to come into force on June 12, 2018.

The recent adoption of Rule 72-503 and the announced resale exemption amendments to bring it into line with the amendments to NI 45-102 point to the OSC's desire to be responsive to concerns of market participants and also reflects a continuing effort to harmonize regulatory requirements across jurisdictions. On

an overall basis, the Canadian Securities Administrators are attempting to increase the access of Canadian issuers and investors to the global marketplace and promoting foreign issuer activity in Canada.

Please contact a member of McMillan's Capital Markets and M&A Group if you have any questions with respect to these changes or the reporting obligations discussed above.

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[1] 'specified foreign jurisdictions' include, among others, Australia, Hong Kong, Japan, Mexico, South Africa, the U.K. and members of the European Union.

[2] An issuer will have 'materially complied with the disclosure requirements applicable to the distribution under the securities law of the jurisdiction' if the issuer has taken reasonable steps to ensure the distribution is effected in accordance with securities laws of the foreign jurisdiction. It is unclear whether this means obtaining a legal opinion by foreign counsel but once market practice develops, compliance will become easier.

[3] In Alberta, the prospectus exemption for resales outside Canada will be found in Alberta Securities Commission Blanket Order 45-519 *Prospectus Exemptions for Resale Outside Canada* (ASC Blanket Order 45-519)

### **A Cautionary Note**

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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