

Goodmans^{LLP} Update

Ontario's Capital Markets Modernization Taskforce Proposes Sweeping Reforms to Ontario's Capital Markets Regulatory System

Ontario's Capital Markets Modernization Taskforce (the "Taskforce") – formed in late 2019 to make recommendations to the Minister of Finance regarding the effectiveness and competitiveness of Ontario's capital markets – released its final report (the "Report") proposing wide-ranging changes to Ontario's capital markets regulatory system with the primary goal of amplifying growth and competitiveness in Ontario's capital markets. If adopted, the recommendations would have a significant impact on virtually all participants in Ontario's capital markets. The Ontario government has not yet indicated which recommendations it intends to pursue, so the timing and extent of any changes to Ontario's securities regulatory framework is uncertain.

Taskforce Recommendations

The Taskforce's overall conclusion is that Ontario's capital markets regulatory system needs an overhaul to make Ontario's capital markets more competitive and to spur economic growth. The Report identifies a number of market and industry trends that underlie its 74 specific recommendations, including:

- the long-term decline in the number of publicly listed companies in Canada,
- the corresponding increase in private market activity over the past decade,
- the emergence of new and innovative investment products and technologies, including cryptocurrencies and crowdfunding platforms,
- increasing investor focus on environmental, social and governance (ESG) and diversity issues,
- shifting industry dynamics that have created unique challenges for smaller issuers and retail investors,
- concerns that existing enforcement mechanisms may not be adequate to address financial and other misconduct in contemporary capital markets, and
- impacts of the COVID-19 pandemic.

A number of the Taskforce's recommendations involve structural reforms, including a new and modernized Ontario *Capital Markets Act* (to replace the existing Ontario *Securities Act* and *Commodities Futures Act*), governance changes to the Ontario Securities Commission (OSC) (which would be renamed the "Capital Markets Authority") and consolidation of the Investment Industry Regulatory Organization of Canada and the Mutual Fund Dealers Association of Canada into a single self-regulatory organization that would be more closely supervised by the OSC. Additionally, the Report also recommends expanding the OSC's mandate to include "fostering capital formation and competition in the markets."

The Report also includes a number of significant rule changes, including:

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- *Streamlined Public Offering Models.* The Report recommends two new avenues to allow public companies to raise capital from public investors more efficiently. The first is an alternative offering model that would allow public companies, in lieu of filing a prospectus, to raise capital (up to certain limits depending on the company's size) in reliance on their continuous disclosure record and a short offering document updating the disclosure for recent events. The second is adoption of a "well-known seasoned issuer" model (similar to the one that exists in the U.S.) that would allow certain large cap issuers to be automatically accepted for shelf registrations (i.e., without regulatory review). The Canadian Securities Administrators (CSA) previously announced they are evaluating proposals for alternative offering models that may include an offering regime based primarily on companies' continuous disclosure record and something akin to the WKSI regime in the U.S.
- *Broaden Permissible Pre-Marketing for Public Offerings.* In line with recent changes in the U.S., and to minimize the risk of failed transactions, the Report recommends expanding the ability of reporting issuers to gauge interest from institutional accredited investors for participating in a potential prospectus offering before filing a preliminary prospectus. The Report also recommends increased monitoring and compliance measures to address potential risks associated with pre-marketing public offerings.
- *Liberalize Exempt Distribution Rules.* The Report recommends the hold period for securities issued to accredited investors by eligible public companies (being those who have a minimum 12-month disclosure record) initially be reduced from four months to 30 days, and then eliminated entirely within the next two years. The Report also recommends expanding the definition of accredited investor to include individuals who meet certain proficiency requirements that demonstrate a high degree of understanding of investments and capital markets.
- *Semi-Annual Financial Reporting for Smaller Issuers.* In an effort to reduce the disproportionate burden for certain smaller companies to report financial results on a quarterly basis, the Report recommends eligible issuers (being those with annual revenue of less than \$10 million and at least a 12-month continuous disclosure record) would, with the approval of its shareholders (which must be renewed every three years), be permitted to report on a semi-annual basis. The CSA previously sought stakeholder feedback regarding the possibility of semi-annual reporting for certain Canadian public companies with mixed reviews. Since 2015, venture issuers in Canada have had the option to file, in lieu of interim management's discussion and analysis, a shorter "quarterly highlights" report, which consists of a short discussion of the material information of the venture issuer's operations, liquidity and capital resources, including known trends, risks, demands, major operating milestones, commitments, expected or unexpected events and material uncertainties.
- *Modernize Continuous Disclosure Requirements.* The Report includes a number of other recommendations that would reduce the regulatory burden associated with certain continuous disclosure requirements, including (i) combining the disclosure requirements of certain documents (such as the annual information form, financial statements and MD&A), and (ii) adopting an "access equals delivery model" for certain documents (including prospectuses, financial statements and MD&A) and electronic delivery for all other documents required to be delivered to shareholders under Ontario securities laws. As part of its ongoing burden reduction initiative, the CSA is reviewing potential overlap in continuous disclosure requirements and, in January 2020, it published a consultation paper regarding adoption of an access equals delivery model that received broad stakeholder support.
- *Share Ownership Reporting.* The Report recommends Ontario reduce the threshold for publicly reporting ownership of public companies from 10% to 5% for non-passive investors. This change would align Ontario with the general reporting thresholds in the U.S. and U.K. This change was considered by the CSA in 2013, but after receiving feedback from interested market participants, the CSA concluded the 10% threshold was more appropriate in Canada, given the unique features of Canada's capital markets, including the number of smaller issuers and liquidity levels.
- *Regulation of Short-Selling.* The Report includes a number of recommendations to address potential concerns with certain activities of short sellers, including a requirement to confirm the ability to borrow the securities required to settle a short sale, a mandatory buy-in for certain failed trades, and a prohibition on buying securities in the primary market when the investor has a short position in those securities. The Report also recommends introducing a new offense of making misleading or untrue statements about public companies, which could apply to short sellers who make false or misleading statements in support of their campaign (this proposed new offense

would also apply to positive misleading statements). The CSA recently published a consultation paper seeking feedback about potential regulatory changes to address potential concerns with activist short selling.

- *Regulation of Proxy Advisory Firms.* The Report recommends introducing a new regulatory framework for proxy advisory firms that would include (i) providing issuers with a right to “rebut” proxy advisor reports (which rebuttal would be included in the proxy advisor report), and (ii) restrict proxy advisors from providing consulting services to issuers in respect of which the proxy advisor also provides clients with voting recommendations. In 2015, the CSA published policy guidance for proxy advisory firms that was intended to ensure transparency about the process leading to vote recommendations and potential conflicts of interest.
- *Board Diversity and Renewal.* The Report recommends public companies be required to set targets for board and executive management diversity, as well as implementation timelines (targets of 50% for women over a five-year period and 30% for other diversity groups within seven years is recommended). To provide greater opportunities for board renewal, the Report also recommends setting 12-year maximum term limits (subject to limited exceptions) for directors of public companies.
- *Enhanced ESG Disclosure.* The Report recommends mandating disclosure of ESG factors, including climate change-related disclosure that complies with the international Financial Stability Board’s Taskforce on Climate-Related Financial Disclosures recommendations for issuers through regulatory filing requirements of the OSC.
- *Mandatory “Say on Pay”.* The Report recommends all public companies have an annual non-binding advisory shareholders vote on the board’s approach to executive compensation.
- *Universal Proxy Ballots.* The Report proposes that so-called universal proxy ballots (which permit shareholders to vote for any combination of management’s and a dissident’s nominees) be required for all contested meetings, and that both sides in a proxy contest have equal access to voting results on an ongoing basis (currently, parties only have access to voting results for their own forms of proxy). The Report acknowledges that further consideration and consultation are required to facilitate the use of universal proxies.

Next Steps

The Ontario government, in consultation with the OSC, will review the Report and consider which recommendations to pursue.

Many of the recommendations are the same as or similar to the recommendations that were included in the Taskforce’s Consultation Report published in July of 2020. Stakeholder feedback in response to the Consultation Report was mixed. Some of the concerns raised include disharmony between new regulatory requirements in Ontario and those in other Canadian jurisdictions (and in some cases the U.S.), the potential for some overly prescriptive regulations that may increase regulatory burden for some market participants, and a desire for further analysis of the relative costs and benefits of recommendations for novel proposals.

Ontario – along with British Columbia, Saskatchewan, New Brunswick, Newfoundland and Labrador, Nova Scotia, Prince Edward Island and Yukon – continue to pursue implementation of the Cooperative Capital Markets Regulatory System (CCMR), which would establish a harmonized capital markets regulatory system and single regulatory authority across all of the participating jurisdictions. If that initiative proceeds, the support of the other participating jurisdictions would be required for the Taskforce’s recommendation to be incorporated into the CCMR.

To discuss the Report or any of its recommendations and how they impact your company, please contact any member of our [Corporate Finance and Securities Group](#).

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