OSC Staff Notice 51-728

Corporate Finance Branch

2016-2017 Annual Report

September 21, 2017

ONTARIO SECURITIES COMMISSION

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OSC ONTARIO SECURITIES COMMISSION

Part A: Introduction

Introduction

What is our Branch mandate?

The Corporate Finance Branch (the Branch or we) of the Ontario Securities Commission (OSC) has a broad regulatory mandate which we execute in pursuing the two purposes of the *Securities Act* (Ontario) (the Act):

Investor protection	• To provide protection to investors from unfair, improper or fraudulent practices.
Efficient capital markets	• To foster fair and efficient capital markets and confidence in capital markets.

A key part of our mandate is issuer regulation. Regulation in this area is broad and takes many forms, including the following:

Issuer regulation	• Review of public distributions of securities (prospectuses). • Review of exempt market activities and related policy development. • Continuous disclosure reviews of reporting issuers. • Review and consideration of applications for relief from regulatory requirements. • Issue-related policy initiatives.

Other areas covered by our mandate include:

Insider reporting	• Review of insider reporting.
Designated rating organizations (DROs)	• Review of credit rating agencies designated as DROs.
Listed issuer regulation	• Oversight of the listed issuer function for OSC recognized exchanges. • Policy initiatives for listed issuer requirements.

In executing our functions, we consult and partner with other OSC branches in many areas, including the exempt market, listed issuer regulation and enforcement action.

What are the objectives of the report?

This report provides an overview of the Branch's operational and policy work during the fiscal year ended March 31, 2017 (fiscal 2017) and gives guidance in certain areas. The report is intended for individuals and entities we regulate, their advisors, as well as investors.

The report aims to:

- encourage compliance with regulatory obligations
- improve disclosure in regulatory filings
- provide insights on trends
- provide guidance on novel issues
- inform on key policy initiatives

Part B: Compliance

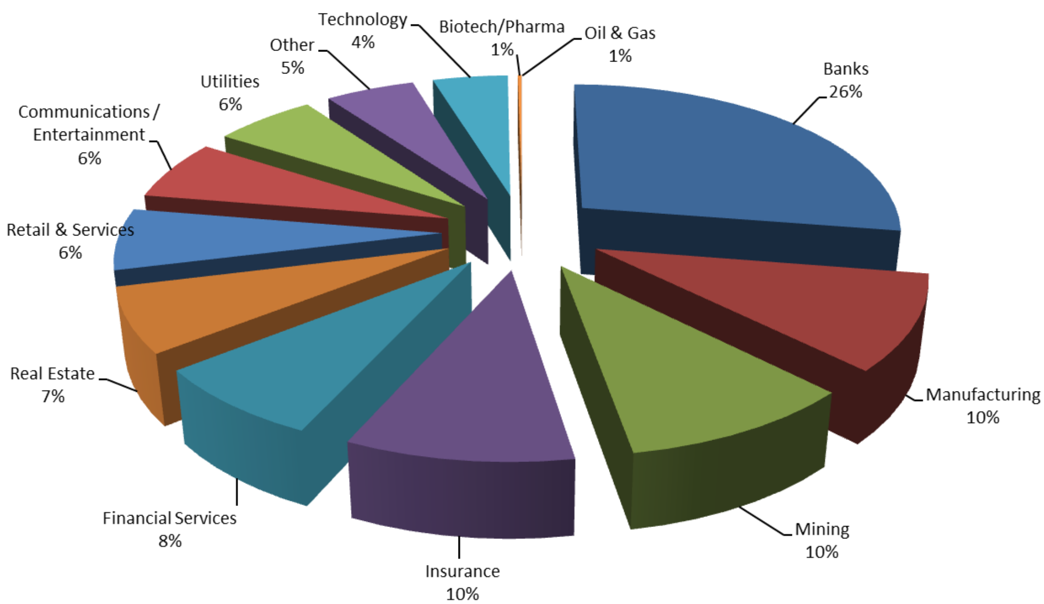
Compliance

Continuous Disclosure Review Program

Under Canadian securities laws, reporting issuers must provide timely continuous disclosure (CD) about their business and affairs. Where a reporting issuer has a head office in Ontario, or has a significant connection to Ontario, we have primary responsibility as principal regulator for reviewing that issuer's CD. Disclosure documents include periodic filings such as interim and annual financial statements, management's discussion and analysis (MD&A) as well as certifications of annual and interim filings, management information circulars and annual information forms (AIF).

The market capitalization of Ontario reporting issuers was approximately $1,239 billion as at March 31, 2017 ($1,044 billion as at March 31, 2016). The four largest industries by market capitalization were banks, manufacturing, mining, and insurance.

Market capitalization of reporting issuers, broken down by industry as at March 31, 2017



Overview of the program

Our CD review program is risk-based and outcome focused. It includes planned reviews based on risk criteria as well as ongoing issuer monitoring through news releases, media articles, complaints and other sources. We conduct the CD program through powers in section 20.1 of the Act, which is part of a harmonized CD review program conducted by the Canadian Securities Administrators (CSA). See CSA Staff Notice (Revised) 51-312 *Harmonized Continuous Disclosure Review Program*.

The CD review program has two main objectives**:**

Compliance	• To assess whether reporting issuers are complying with their disclosure obligations.
Issuer education and outreach	• To help reporting issuers better understand their disclosure obligations.

Our CD review program is critical to investor protection as we assess issuer compliance with CD requirements and review CD documents which are available to investors to make an investment decision. This function also supports the raising of new capital, as many issuers raise funds through short form prospectuses which must incorporate CD documents.

In general, we conduct either a "full" review or an "issue-oriented" review (IOR) of an issuer's CD.

Full review	• Broad in scope and generally covering an issuer's most recent annual and interim financial statements and MD&A, AIF, annual reports, information circulars, news releases, material change reports, website, social media disclosure, investors' presentation, and SEDI filings.

In planning our full reviews, we draw on our knowledge of reporting issuers and their industries and use risk-based criteria to identify issuers with a higher risk of non-compliant disclosure. The criteria are designed to identify issuers whose disclosure is likely to be materially improved or brought into compliance with securities laws or accounting standards as a result of our intervention. Our risk-based procedures incorporate both qualitative and quantitative criteria which we review regularly to stay relevant with market changes. We also monitor novel and high growth areas of financing activity when developing our review program. We may also select an issuer for review based on a complaint.

Issue-oriented review	• An in-depth review focusing on a specific accounting, legal or regulatory issue that we believe warrants regulatory scrutiny.

Issue-oriented reviews are focused on a specific issue of an individual issuer or broadly on an emerging area of risk across issuers (in some cases, industry specific). Conducting IORs broadly allows us to:

- monitor compliance with requirements and provide a basis for communicating interpretations, staff disclosure expectations and areas of concern;
- quickly address specific areas where there is heightened risk of investor harm;
- identify common deficiencies;
- provide industry specific disclosure examples to assist preparers in complying with requirements; and
- assess compliance with new accounting standards.

Outcomes for fiscal 2017

We measure outcomes of a CD review by tracking the following for each issuer:

- prospective disclosure enhancements
- refilings
- education and awareness
- other outcomes, such as enforcement referrals

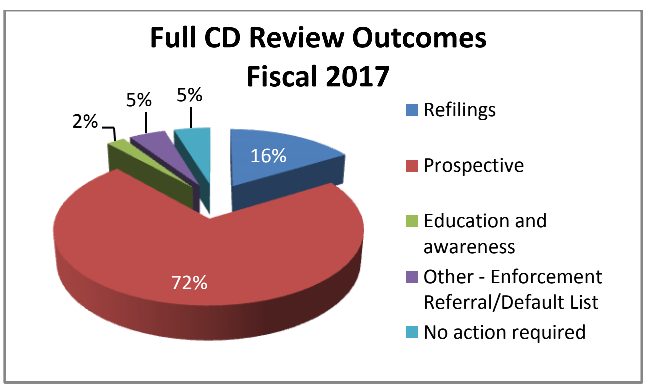
We had at least one outcome in 95% (fiscal 2016: 94%) of our full CD reviews and 94% (fiscal 2016: 73%) of our IORs.

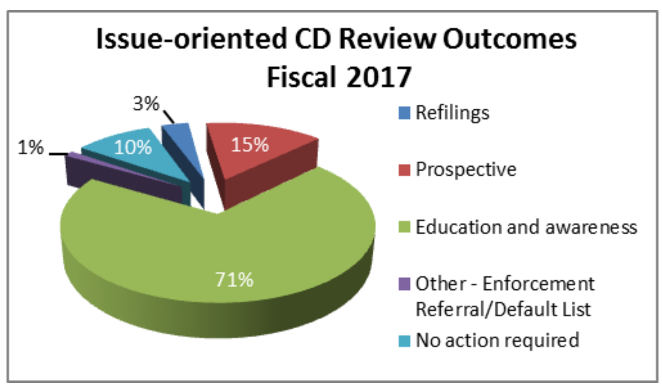
Given our risk-based criteria to identify issuers, the outcomes on a year to year basis should not be interpreted as trends since the issues and issuers reviewed each year are generally different.

Sixteen percent of full reviews and three percent of IORs resulted in an issuer refiling a document. Examples of instances where staff requested refilings include: refiling of an MD&A relating to the disclosure of potentially misleading non-GAAP financial measures, refiling of a technical report not in compliance with National Instrument 43-101 *Standards of Disclosure for Mineral Projects* (NI 43-101), or the filing of a clarifying news release when an issuer failed to update the market on material business developments.

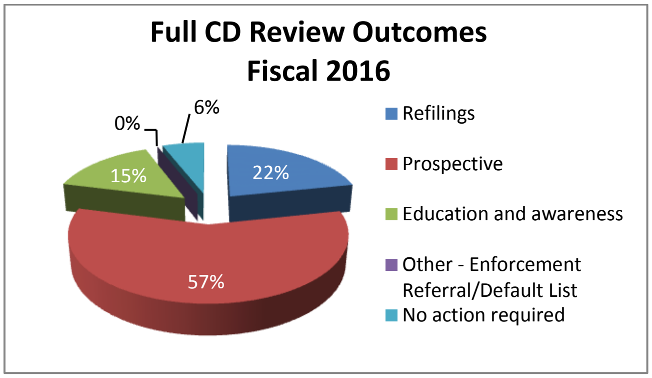
As illustrated below, 71% of IOR outcomes were in the "education and awareness" category. This was mainly due to the nature of IORs conducted in fiscal 2017. For example, we reviewed (i) social media disclosures by reporting issuers and (ii) disclosure of cyber security risks and incidents of all Ontario-based S&P/TSX Composite Index issuers. These reviews raise market awareness through the publication of staff notices discussing review findings, staff disclosure expectations and providing examples of better industry specific disclosure.

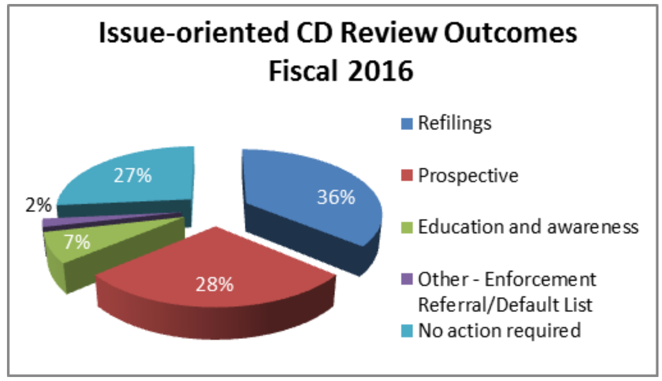
Prospective disclosure enhancements address disclosures that were either not presented or sufficiently detailed to allow an informed investment decision but did not reach a level of materiality where a refilling would be necessary.





For reference, the following were the outomes from fiscal 2016**:**





We encourage issuers to continue to review and improve their disclosure, including in those areas noted below which we frequently comment on as part of our reviews.

Trends and guidance

❖ *Management's Discussion and Analysis*

MD&A is the cornerstone of a reporting issuer's overall financial disclosure that provides an analytical and balanced discussion of the reporting issuer's results of operations and financial condition, through the eyes of management. We remind reporting issuers that disclosure must be useful and understandable. MD&A is a narrative explanation about the reporting issuer's performance during the financial period to supplement and complement the financial statements. MD&A must be transparent and clear to be informative. Reporting issuers should avoid boilerplate disclosure where the MD&A merely repeats information from the financial statements. Reporting issuers should also avoid disclosing information that users do not need or that does not provide insight into the issuer's past or future performance.

We encourage issuers to review MD&A requirements (Form 51-102F1 *Management's Discussion and Analysis*). We continue to be disappointed that many issuers struggle in providing meaningful disclosure in their MD&A, especially in the areas noted below.

Changes in accounting policies including initial adoption	• Discuss and analyze changes resulting from a change in accounting standards. Include disclosure such as the methods of adoption that the issuer expects to use, the expected effect on the issuer's financial statements, and potential effect on the issuer's business including changes in business practices. Provide increasingly detailed qualitative and quantitative information about the expected impacts of the new standards (e.g. IFRS 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers* and IFRS 16 *Leases*) as the effective dates approach.
Results of operations	• Include a detailed, analytical and quantified discussion of the various factors that affect revenues and expenses, beyond the percentage change or amount.

Risks and uncertainties	• Be specific about the material risks and uncertainties the issuer is facing, including the anticipated significance and impact those risks may have on the issuer's financial position, operations and cash flows. To make the information more meaningful, update risk disclosures when circumstances change.

Liquidity and capital resources	• Do not provide general statements such as "have adequate working capital to fund operations" or "have adequate cash resources to finance future foreseeable capacity expansions". Rather, provide insight beyond the numbers by discussing material cash requirements, explaining how liquidity obligations have been settled or will be settled and by quantifying working capital needs and how these needs relate to future business plans or milestones. Be specific about the periods to which your discussion applies.

❖ ***Non-GAAP financial measures* –** Many issuers include non-GAAP financial measures in news releases, MD&A, prospectus filings, websites and marketing materials, as these issuers believe this information provides additional insight into their overall performance. In some cases, we are quite concerned about the prominence of disclosure given to non-GAAP financial measures, the visibility and clarity of adjustments made, and the appropriateness of the adjustments themselves (e.g. excluding loan loss provisions from the calculation of net income and earnings per share (EPS) measures, defining an adjustment such as acquisition costs as "one-time" when these are recurring every year). When providing non-GAAP financial information, issuers should not mislead investors nor obscure the GAAP results.

While the volume and nature of non-GAAP financial measures vary by industry and issuer, we note below a few examples and reminders of staff's expectations:

- For mining issuers, non-GAAP financial measures are commonly used in describing production costs at producing mines and free cash flow at development projects. CSA Staff Notice 52-306 (Revised) – *Non-GAAP Financial Measures and Additional GAAP Measures* (CSA SN 52-306) applies to disclosure of the results of economic analyses and to disclosure of production results and production guidance. Specifically, we remind issuers disclosing non-GAAP financial measures on mineral projects that they should state clearly that the measure is a non-GAAP financial measure, apply that measure consistently from period to period and across documents, and provide a clear explanation of how the measure is calculated. Where non-GAAP financial measures are part of written disclosure that is not required to be filed as a CD document (for example, an investor presentation), the measures should be consistent with the non-GAAP financial measures disclosed in CD filings and clearly identified and explained.

- Non-GAAP financial measures are prevalent in the real estate industry. Recent reviews of real estate investment trusts (REITs) in Ontario have resulted in important disclosure improvements in this area, although inconsistencies remain in how these non-GAAP financial measures are presented vis-à-vis staff expectations in CSA SN 52-306.
  As distribution sustainability is of key importance to a REIT, issuers should adequately disclose the sources of cash flow for distributions in a particular period, the impact to the REIT and its ability to sustain distributions over the longer term.

One of a REIT's key ratios disclosed is the payout ratio, analyzed in terms of the REIT's distributions as a percentage of funds from operations (FFO) and adjusted funds from operations (AFFO), two of a REIT's main non-GAAP financial measures. We have noted concerns regarding the prominence of these non-GAAP financial measures, as well as unclear adjustments being made in deriving these non-GAAP financial measures. Improvements can still be made to enhance the transparency of REIT distribution disclosures when payout ratios are used.

- Other industries such as technology and biotechnology commonly present earnings before interest, taxes and depreciation (EBITDA), adjusted EBITDA and adjusted earnings per share. Our concerns in these cases are prominence of non-GAAP financial measures and the appropriateness of the adjustments being made. Non-GAAP financial measures generally should not describe adjustments as non-recurring, infrequent or unusual, when a similar loss or gain is reasonably likely to occur within the next two years or occurred during the prior two years. We remind issuers that in presenting EBITDA as a non-GAAP financial measure, it would be misleading to exclude amounts for items other than interest, taxes, depreciation and amortization.

We caution issuers that the OSC may take regulatory action if an issuer discloses information in a manner that is considered misleading or otherwise contrary to the public interest. While we have raised repeated reminders for issuers to meet staff disclosure expectations in prior fiscal Corporate Finance Branch Annual Reports and as outlined in CSA SN 52-306, we continue to see potentially misleading disclosures.

We will continue to actively review this topic in the coming fiscal year.

❖ ***Forward-looking information (FLI)*** **–** Many issuers disclose FLI in news releases, MD&A, prospectus filings, marketing materials, investor presentations or on their website. We continue to see generic factors and assumptions being disclosed. We also continue to see FLI assumptions not being quantified. Disclosure of specific and relevant material factors or assumptions including material risk factors underlying FLI is necessary for investors to understand how actual results may vary from FLI.

Some issuers disclose FLI in their prospectus or CD documents for a period beyond the issuer's next fiscal year end without providing reasonable and sufficient assumptions to support the FLI beyond the fiscal year end. Part 4B of National Instrument 51-102 *Continuous Disclosure Obligations* (NI 51-102) states that an issuer must not disclose a financial outlook unless the financial outlook is based on assumptions that are reasonable in the circumstances. It further states that the financial outlook that is based on assumptions that are reasonable in the circumstances must, without limitation, be limited to a period for which the information in the financial outlook can be reasonably estimated. In many cases, that time period will not go beyond the end of the reporting issuer's next fiscal year. We may raise comments in respect of the reasonableness of the time period of FLI presented. Where FLI is presented for multiple years and is not sufficiently supported by reasonable qualitative and quantitative assumptions, we may ask issuers to limit the disclosure of FLI to a shorter period (for example, one or two years), for which reasonable support exists. For investors to assess whether the assumptions underlying the issuer's FLI are reasonable, the issuer should disclose those assumptions in the prospectus and CD documents (as applicable), both quantitatively and qualitatively. For example, an issuer projecting aggressive growth targets without the benefit of historical experience should be able to show (i) a reasonable basis for those targets, including the key drivers behind the projected growth with reference to specific plans and objectives that support the projected growth, and (ii) why management believes that each of the targets/FLI are reasonable.

We remind issuers that provide FLI that section 5.8 of NI 51-102 contains several important requirements (i) to update previously disclosed FLI when events or circumstances are reasonably likely to cause actual results to differ materially from the previously disclosed FLI (including expected differences), and (ii) to include a comparison of actual results to previously disclosed financial outlook.

- ***Social media disclosures* –** In addition to the required CD filings, issuers often provide stakeholders with information about their business and operations in news releases, investor presentations on their website, as well as chat rooms, blogs and third party websites such as Facebook, LinkedIn and Twitter. This information can include FLI, such as forecasts or revenue targets. Regardless of the platform for dissemination, issuers must avoid early or selective disclosure and ensure that all material information is simultaneously filed on SEDAR. Social media disclosure cannot be misleading, unbalanced or insufficient to provide a complete picture, or inconsistent with information that has been disclosed on SEDAR. Lastly, we strongly encourage issuers to adopt a social media governance policy to enhance the integrity of disclosures provided in both regulatory filings as well as on social media. Please refer to the Issue-oriented review section below for the link to the CSA Staff Notice on social media.

- ***Mining disclosure* –** Issuers that disclose a preliminary economic assessment (PEA) on an advanced property containing mineral reserves are reminded that such disclosure is only permissible when those results are disclosed in a manner consistent with the CIM definitions incorporated by reference in NI 43-101. CSA's view on the definitions is outlined in CSA Staff Notice 43-307 *Mining Technical Reports – Preliminary Economic Assessments*. We continue to see non-compliant disclosure of PEAs in technical reports which incorporate the economic analyses, production schedules, and cash flow models based on inferred mineral resources with economic studies based on mineral reserves. Issuers that make such non-compliant disclosure may be required to amend and refile their technical report. We intend to continue monitoring this area closely.

- ***Investment Entities* –** We continue to see an increase in issuers that have determined they meet the criteria to be an "investment entity" under IFRS 10 *Consolidated Financial Statements* (IFRS 10) and measure substantially all of their investments at fair value through profit and loss, including their investments in subsidiaries. Our review uncovered disappointing trends and a broad concern with issuers understanding their disclosure obligations. We observed that, in certain cases, insufficient disclosures were being provided in issuers' MD&A on the investment entity's operations, investments and risks. Some issuers omitted the required fair value disclosures in the financial statements or did not provide sufficient disclosure to understand the investment portfolio composition, performance, investment strategies and oversight and related risks. We found instances where additional investee specific financial information and operational disclosure was necessary to inform an investment decision. Given the nature of investment entities, we encourage these issuers to consider if external expertise is needed to determine the fair value of private investments. As this is an emerging area, market participants may need to look through the corporate structure and look to other securities requirements for guidance. For example, investment entities with material mining or oil and gas investments need to consider the applicability of technical disclosure requirements. Please refer to the Issue-oriented review section below for the link to the CSA Staff Notice on investment entities.

- ***Venture issuers* –** On June 30, 2015, amendments to NI 51-102 came into force creating streamlined and tailored disclosure for venture issuers. Specifically, amendments included amongst other areas (i) allowing all venture issuers to meet interim MD&A requirements by preparing a "quarterly highlights" document and (ii) permitting venture issuers to use a new tailored form of executive compensation disclosure, Form 51-102F6V *Statement of Executive Compensation – Venture Issuers* (Form 51-102F6V).

  We have observed that since the amendments came into force, only a small percentage of reporting issuers have taken advantage of using these optional forms (less than 15%) at the time of the review. We reviewed the disclosure of a sample of venture issuers that indicated that they were using "quarterly highlights" to meet the requirements for their interim MD&A; we also reviewed the disclosure of a sample of venture issuers that used Form 51-102F6V for their executive compensation disclosure.

Our review of venture issuers using the quarterly highlights indicates that the disclosure included in the quarterly highlights did not differ significantly, in most cases, from the disclosure previously provided in the interim MD&A (before the amendments came into force). Generally, venture issuers appropriately excluded from the quarterly highlights items not required under this form such as the "summary of quarterly results", but otherwise in most cases there were no significant differences from prior disclosure. For example, if the discussion of financial performance was boilerplate in the reporting issuer's prior interim MD&A, we did not see an improvement in the quality of this information in the quarterly highlights. Similarly, mining venture issuers do not need to repeat the history of a project in every MD&A (including quarterly highlights) if there are no significant differences from the previous disclosure.

In terms of the overall assessment of venture issuers' executive compensation disclosure using Form 51-102F6V, while the disclosure was generally adequate, certain areas required some improvement. Most reporting issuers included all the required disclosure in the table of "Director and named executive officer compensation, excluding compensation securities". However, a notable number of reporting issuers failed to provide a meaningful discussion of the "Oversight and description of director and named executive officer compensation". The table of "Stock options and other compensation securities" did not always include all the information required. We view executive compensation disclosure as a key aspect of the overall stewardship and governance of a company. In preparing their disclosures, reporting issuers should review the requirements of Form 51-102F6V in order to help investors understand how decisions about executive compensation are made.

We encourage venture issuers and their advisors to review and consider adopting alternatives to streamline the information provided to their investors.

Issue-oriented review staff notices published in fiscal 2017

During fiscal 2017, 86% of our reviews were issue-oriented (fiscal 2016: 87%). We published staff notices summarizing the findings from four IORs covering broad issues.

Disclosure of **cyber security risks** and **incidents**	• To the extent that it is determined that cyber security risk is a material risk, reporting issuers are reminded to provide risk disclosure that is as detailed and entity specific as possible. In considering whether and when to disclose a cyber security incident, the issuer must determine whether it is a material fact or material change that requires disclosure in accordance with securities legislation. This determination is a dynamic process throughout the detection, assessment and remediation phases of a cyber security incident, and should consider direct impacts on the business as well as regulatory and reputational matters.
Compliance of **social media** disclosures with continuous disclosure requirements	• Reporting issuers need to improve the quality of their social media disclosures to comply with NI 51-102 to prevent unbalanced, misleading or selective disclosures.

Disclosure by **Investment Entities** of fair value measurements	• Reporting issuers need to improve their disclosures under IFRS 10 as well as to provide more fulsome and entity-specific information to investors.
Disclosure about **Women on Boards** and in **Executive Officer Positions**	• Non-venture issuers need to have policies regarding the representation of women on their board and in executive officer positions or explain reasons for not having such policies in place.

See the following links for the full staff notices:

CSA Multilateral Staff Notice 51-347 *Disclosure of Cyber Security Risks and Incidents*

CSA Staff Notice 51-348 *Staff's Review of Social Media Used by Reporting Issuers*

CSA Multilateral Staff Notice 51-349 *Report on the Review of Investment Entities and Guide for Disclosure Improvements*

CSA Multilateral Staff Notice 58-308 *Staff Review of Women on Boards and in Executive Officer Positions - Compliance with NI 58-101 Disclosure of Corporate Governance Practices*

We will continue to monitor the issues identified in the IORs noted above as well as issues identified in full reviews. This includes reviewing disclosure to confirm that issuers have provided prospective disclosure enhancements as requested by staff. Where an issuer fails to make a prospective disclosure enhancement, staff will consider whether an alternative action such as a refiling is necessary.

Participation fees

We review the participation fees paid by reporting issuers under OSC Rule 13-502 *Fees* (the Fee Rule) to ensure that the correct amounts have been paid.

We remind issuers that under the Fee Rule, an issuer must include in its calculation of annual participation fees all capital market debt distributed under a prospectus or prospectus exemption, even if these debt securities are not listed or quoted on a marketplace. An issuer must include those debt securities that are held by investors who reside outside of Ontario. Debt securities issued by non-reporting subsidiaries of the issuer are also required to be included in the capitalization of the issuer. Capital market debt securities are required to be included because together with equity securities, they give a fuller and more accurate representation of the size of the issuer and its participation in Ontario's capital market.

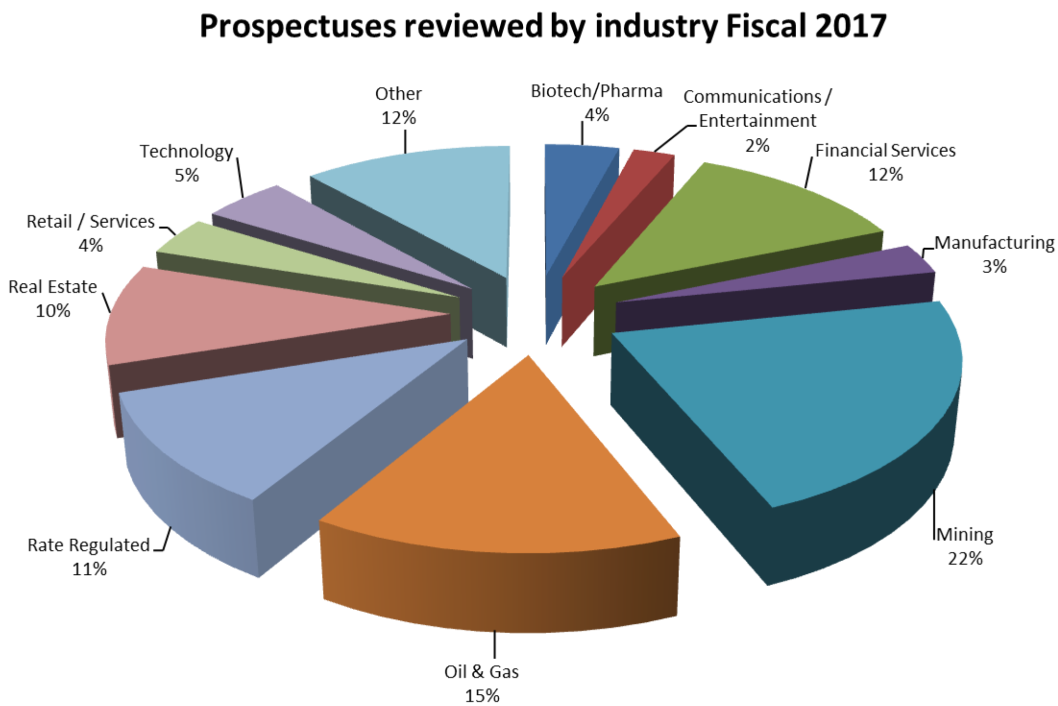
Issuer education and outreach

Issuer education and outreach from the program happens at both a micro level through direct communication with an issuer, as well as at a macro level through broad communications, such as staff notices. We also share the observations and findings of our review program through the Branch's outreach program for small and medium enterprises (SMEs) called The OSC SME Institute. Through the institute, we offer SMEs a series of free educational seminars to help them and their advisors understand the securities regulatory requirements for being or becoming a public company in Ontario, and participating in the exempt market. For further details see Information for Small and Medium Enterprises on the OSC's website. Finally, staff of the Branch give presentations from time to time at industry conferences, professional advisory firms' offices and provide staff views and commentary through various media mediums.

Offerings – Public

Statistics

Another key component of our compliance work is the review of offering documents. In fiscal 2017, we receipted approximately 400 prospectuses (fiscal 2016: over 300). These filings covered a wide range of industries with mining, oil and gas and financial services being the most active sectors based on the number of offerings.



Trends and guidance

In fiscal 2017, the number of prospectuses we reviewed where Ontario was the principal regulator was higher than the prior fiscal year. The resource and financial services industries continued to be active over fiscal 2017. We also continued to see offerings in a relatively new industry to the Canadian capital markets, medical marijuana. This emerging industry often requires enhanced disclosure due to regulatory uncertainty, differences in legal and regulatory frameworks across jurisdictions and other novel considerations that should be disclosed to investors. In light of the recent announcement by the Canadian Federal government on the proposed legalization of recreational marijuana, we expect to continue to see increased activity in the marijuana industry.

Key takeaways from our work reviewing offering documents in fiscal 2017 are set out below. Many of the matters highlighted could benefit from pre-file discussions between issuers and staff to avoid delays at the time of the prospectus filing. This process is outlined in National Policy 11-202 *Process for Prospectus Reviews in Multiple Jurisdictions*. For any relief sought in connection with an offering where the relief will be evidenced by receipt, issuers should provide written submissions explaining why relief is required and pay the appropriate application fee. For more information on the procedural steps the issuer should follow, please see OSC Staff Notice 41-703 *Corporate Finance Prospectus Practice Directive #2 – Exemption from Certain Prospectus Requirements to be Evidenced by a Receipt*.

The guidance below also applies to prospectus-level disclosure included in an information circular in connection with a proposed significant acquisition or a restructuring transaction as required by Item 14.2 of Form 51-102F5 *Information Circular*.

- ***Disclosure improvements –*** Disclosure outcomes, where we required material disclosure changes to a prospectus, remained our most consistent outcome. Highlighted below are areas where we frequently find deficiencies.

    - *Description of business and regulatory environment* – This section of a prospectus needs to be clear and comprehensive as issues may arise in circumstances where an issuer:

        - appears to have no business or the offering is a blind pool,
        - has a complex corporate structure,
        - has a significant change in business/operations,
        - is in the medical marijuana industry and lacks disclosure about its specific regulatory environment, or
        - has recently completed a significant acquisition or capital restructuring where a securities regulatory review has not been carried out.

    - *Risk factors relating to the business and/or offering* – Be specific. Avoid boiler plate language and tailor the disclosure to the issuer's situation (e.g. assess political/regulatory risk, discuss factors that may affect the issuer's title to its assets). Discuss any steps the issuer has taken to mitigate the risk.

    - *MD&A disclosure in a long form prospectus* – Include relevant information and provide sufficient detail, especially regarding those items highlighted in this report under the heading "Compliance – Continuous Disclosure Review Program – Trends and Guidance". MD&A in a long form prospectus should be just as comprehensive as a stand-alone MD&A.

    - *Use of proceeds* – Provide sufficient detail and be comprehensive. For example, generic phrases such as "for general corporate purposes" are insufficient disclosure. Provide an itemized description of how the proceeds will be used. In those rare instances where an allocation is not appropriate, explain management's reasons for not allocating the funds and the purpose of the offering.

- ***Asset vs. business acquisitions –*** When an issuer makes an acquisition, there are instances where judgement is involved to determine whether the acquisition is an asset acquisition or a business acquisition. An acquisition could meet the definition of an asset acquisition under International Financial Reporting Standards, while the same acquisition could be considered a business acquisition for securities law purposes. The term "business" should be evaluated in light of the specific facts and circumstances. We generally consider the acquisition of a separate entity, a subsidiary or a division to be an acquisition of a business, and in certain circumstances, the acquisition of a smaller component of a company may also be considered an acquisition of a business, irrespective of whether or not financial statements were previously prepared for the business. We also generally view the acquisition of licenses, patents, royalties and intellectual property as "business" acquisitions for securities law purposes, as the revenue producing activity or potential revenue producing activity remains the same.

    Part 8 of Companion Policy 51-102CP provides guidance in determining whether an acquisition constitutes the acquisition of a business. Specifically, in making that determination, an issuer should consider the continuity of business operations, including the following factors:

    (a) whether the nature of the revenue producing activity or potential revenue producing activity will remain generally the same after the acquisition; and

(b) whether any of the physical facilities, employees, marketing systems, sales forces, customers, operating rights, production techniques or trade names are acquired by the issuer instead of remaining with the vendor after the acquisition.

If an existing reporting issuer completes an acquisition of a business that is considered significant, the BAR requirements under Part 8 of NI 51-102 would apply.

We encourage issuers and their advisors to consult with staff on a pre-file basis if there is uncertainty as to whether the acquisition is an asset acquisition or a business acquisition for securities law purposes.

- ***Financial statement disclosure for certain significant acquisitions* –** Where an issuer is raising proceeds to fund an acquisition that makes up a material portion of its business, or that is larger than the issuer's existing business, the issuer should consider whether the prescribed disclosure that is normally required for a significant acquisition (as that term is used in Form 41-101F1 and Form 44-101F1) is sufficient for the prospectus to contain full, true and plain disclosure. Reporting issuers with an existing AIF should consider if their AIF needs to be supplemented with additional disclosure in the prospectus in light of the acquisition, and whether inclusion of additional audited financial statements is necessary. Venture issuers should consider whether additional disclosure is necessary for the prospectus to contain full, true and plain disclosure even if an acquisition does not meet the applicable asset or investment significance tests. We encourage issuers and their advisors to consult with staff on a pre-file basis on these issues to determine the appropriate level of disclosure.

- ***Primary business in an initial public offering (IPO)* –** An issuer filing an IPO prospectus must include in its prospectus a three-year financial history (two years for an IPO venture issuer) of the business that investors are investing in, even if this financial history spans across multiple legal entities over the three-year period. This includes the financial history for those businesses acquired or that will likely be acquired if those businesses are in the same primary business of the issuer. This provides investors with information on the issuer's entire business, which is the subject of their investment.

  In instances where there are multiple acquisitions in the same primary business of the issuer, we encourage issuers and their advisors to consult with staff on a pre-file basis to consider what financial statements of smaller immaterial acquisitions can be excluded from the prospectus. Results from applying the significance tests is not the only consideration when determining whether disclosure, including financial statements disclosure is necessary for the prospectus to contain full, true and plain disclosure. However, if the result from applying any of the significance tests is over 100% (i.e. the business represents more than half of the reporting issuer), it is important for investors to have the financial history of this business even though it is not in the same business as that of the primary business of the issuer.

- ***Sufficiency of proceeds and financial condition of an issuer* –** Securities legislation sets out specific circumstances under which a receipt for a prospectus shall not be issued. One example is where the aggregate proceeds being raised by an issuer through the prospectus (together with other resources) are insufficient to accomplish the purpose of the offering as stated in the issuer's prospectus.

  As such, a critical part of every prospectus review is considering the issuer's financial condition and intended use of proceeds. A prospectus must contain clear disclosure of how the issuer intends to use the proceeds raised in the offering as well as disclosure of the issuer's financial condition, including any liquidity concerns. In some instances, an issuer's representations about its ability to continue as a going concern and the period during which it expects to be able to continue operations may be inconsistent with the issuer's historical statements of cash flows (in particular, its cash flows from operating activities). In these cases, we may request that the issuer provide a cash flow forecast or financial outlook-type disclosure to support its expected period of liquidity (i.e., ability to continue operations). However, disclosure on its own may not be sufficient to satisfy our receipt refusal concerns in certain circumstances.

For issuers filing a base shelf prospectus, we may take the view that the structure of a base shelf prospectus is not appropriate given the issuer's financial condition and uncertainty of financing. Typically, receipt refusal concerns on financial condition arise if the issuer does not appear to have sufficient cash resources to continue operations for the next 12 months or to meet concrete developmental milestones expected to be completed in the next 12 months. In these cases, to address our concern that incremental drawdowns may be insufficient to satisfy the issuer's short term liquidity requirements, we may request that the issuers:

- withdraw the base shelf and file a short form prospectus with a minimum subscription amount,
- withdraw the base shelf and file a short form prospectus with a fully underwritten commitment, or
- arrange for additional committed sources of financing.

Issuers, including those filing a base shelf or non-offering prospectus, should review CSA Staff Notice 41-307 *Corporate Finance Prospectus Guidance - Concerns regarding an issuer's financial condition and the sufficiency of proceeds from a prospectus offering*.

- ***Audit Committees in IPOs*** - Where an issuer files an IPO prospectus, it must have an audit committee in place that meets the composition requirements prescribed in National Instrument 52-110 *Audit Committees* (NI 52-110) no later than the date of the receipt for the final prospectus.

  This means that a non-venture issuer, subject to exemptions that are set out in NI 52-110 must have an audit committee in place that is composed of at least three members, all of whom are independent and financially literate as defined in NI 52-110. A venture issuer must have an audit committee in place that is composed of at least three members, a majority of whom are not executive officers, employees or control persons of the issuer or of an affiliate of the issuer.

- ***Material contracts –*** We encourage issuers to review all contracts entered into within the last financial year, or before the last financial year if the contract is still in effect, to determine whether the contract is a "material contract" that must be filed on SEDAR. While material contracts entered into in the ordinary course of business are generally exempt, we remind issuers that any material contract on which the issuer's business is substantially dependent must be filed.

- ***Medical marijuana –*** We expect that the growth of the marijuana industry will continue given the Canadian Federal government's introduction of legislation to legalize the recreational use of marijuana. Canadian licensed medical marijuana producers have conducted significant public equity financing over the last year and are investing heavily in production capacity expansion projects, the scale of which would likely only be utilized in the event of a legalized recreational marijuana market. If issuers publicly state that they are funding construction projects to expand their current production growth facilities in anticipation of the legalization of recreational marijuana in Canada, such disclosure should be qualified, as appropriate, by specific risk factor disclosure.

As issuers in the medical marijuana industry operate in a complex legal and regulatory framework, these issuers should consider filing on SEDAR their Health Canada licenses, and leases for facilities associated with those licenses, on which their business is substantially dependent.

- ***Blank cheque preferred shares where restricted shares are issued and outstanding –*** Where an issuer has a class of restricted shares issued and outstanding and its authorized share capital includes "blank cheque" preferred shares (i.e. preferred shares issuable in series, having such rights, restrictions and conditions as may be determined by the issuer's board prior to the issuance) there is a concern that a future issuance of preferred shares may further restrict the rights of the existing class of restricted shares. In these circumstances, we will ask the issuer for an undertaking to provide staff with reasonable prior notice in the event that the issuer intends to issue a series of preferred shares with greater voting rights than those of the existing class of restricted shares. This will provide staff with sufficient time to consider what, if any, additional disclosure should be made to the future offering document.

- ***Prospectus filings generally –*** We remind issuers that a preliminary prospectus, together with all accompanying materials in acceptable form, should be filed before 12:00 p.m. on the day that the receipt is required. If materials are filed after 12:00 p.m., the receipt will normally be issued before 12:00 p.m. on the next business day and dated as of that day.

  For those issuers filing a short form preliminary prospectus for a bought deal, issuers should advise the prospectus review officer by email at prospectusreviewofficer@osc.gov.on.ca before 12:00 p.m. that the preliminary prospectus will be filed by 3:00 p.m. on that day.

  If issuers anticipate filing a preliminary prospectus within a reasonable period of time after 12:00 p.m. (or 3:00 p.m. for a bought deal prospectus) and need a receipt issued that day, they should advise the prospectus review officer and explain in the email the reason for not filing before the applicable deadline. We will attempt to accommodate these requests, but there is no assurance that a receipt will be issued on the same day.

  Where an issuer plans to conduct an overnight marketed deal, the issuer should (a) advise the prospectus review officer by email no later than the morning of the day on which the receipt is required (but prior to filing the materials), and (b) file all materials in acceptable form before 12:00 p.m. that day. In such cases, we will make reasonable efforts to issue a receipt for the preliminary prospectus at or just after 4:00 p.m. on the day of the filing.

  See OSC Staff Notice 41-702 *Prospectus Practice Directive #1 - Personal Information Forms and Other Procedural Matters Regarding Preliminary Prospectus Filings*.

Update on Special Purpose Acquisition Corporations

In fiscal 2015, we received the first IPO prospectus filed by a special purpose acquisition corporation (SPAC) pursuant to *Part X Special Purpose Acquisition Corporations* of the Toronto Stock Exchange (TSX) Company Manual (SPAC Rules). The SPAC Rules, which were adopted in 2008, provide the framework for the IPO and listing of an issuer that has no operating business.

We have receipted eight SPAC IPO prospectuses to date, including one from a sponsor that created its second SPAC. While generally following the same structure, including placing 100% of the IPO proceeds into escrow, certain SPACs have differed in terms of the deadline for completing a qualifying acquisition, the targeted industry for its qualifying acquisition, the number of warrants issued and the potential for top-up payments payable to the escrow fund. The second generation SPAC has also adopted several changes based on terms found in U.S. SPAC IPOs.

To date, four issuers have completed a qualifying transaction, two issuers have redeemed their securities due to not being able to meet their acquisition deadline and two SPACs are seeking a qualifying acquisition. We note that IPO purchasers do not have statutory liability rights for a misrepresentation about the acquired business (as that information is only disclosed in a non-offering prospectus at the time of the qualifying acquisition). To address this concern, we have required SPACs at the time of filing a non-offering prospectus to provide a contractual right of action for rescission or damages to all IPO purchasers for misrepresentation in the non-offering prospectus.

Offerings – Exempt Market

Recent changes to increase access to the exempt market have expanded investment opportunities for all investors, including retail investors. The OSC recognizes the need to be vigilant in its oversight of these markets as they evolve under the new regulatory framework. Our program for overseeing distributions in the exempt market, including those under the new prospectus exemptions, has three main elements:

Assessing compliance	• To assess whether issuers are complying with their disclosure obligations.
Enhancing awareness	• To help issuers better understand their disclosure obligations.
Gathering data regarding the use of the prospectus exemptions	• To be able to analyze and report on the use of prospectus exemptions.

Our Branch and the Compliance and Registrant Regulation Branch of the OSC have primary responsibility for oversight of compliance in the exempt market. Both branches are working to coordinate and conduct the compliance reviews of issuers and registrants.

Assessing compliance

As part of the compliance and oversight program, the OSC oversees issuers and registrants that distribute securities under prospectus exemptions to confirm whether they are complying with their respective obligations.

We use a risk-based approach to select issuers for review. As part of our reviews, we look at offering materials that are distributed to investors. In reviewing the offering materials, we will look to identify misuse of the exemptions and conduct that may be contrary to the public interest. Where warranted, we will take appropriate compliance and cross-branch referral action, including recommendations regarding enforcement action.

Oversight activities for the 2017 fiscal year focused primarily on the use of the offering memorandum exemption (OM Exemption) under s. 2.9 of National Instrument 45-106 *Prospectus Exemptions* (NI 45-106), which came into force on January 13, 2016.

Enhancing awareness

We issued comment letters to issuers in connection with reviews primarily for the following reasons:

- failure to comply with the disclosure requirements of the OM Exemption, including financial statement requirements;
- failure to file marketing materials;
- insufficient disclosure regarding the business of the issuer, such as operating history and information regarding the issuer's mortgage portfolio (if applicable); and
- out of date disclosure.

❖ *Disclosure requirements*

Of those reviews that have been concluded, a primary outcome was enhanced issuer awareness of the requirements and issuers undertaking to make prospective disclosure enhancements. These enhancements aim to improve disclosure so that a potential investor could make an informed investment decision and understand the risks of the investment.

❖ *Marketing materials*

Any marketing materials used in connection with a distribution under the OM Exemption must be incorporated into the prescribed form of offering memorandum and filed with the OSC (either as an attachment to a report of exempt distribution or through the OSC electronic filing portal) within 10 days of the first use of the materials. This requirement is subject to a limited exception that allows the use of an OM standard term sheet. We found in several instances that issuers have delivered or made available materials to prospective investors without filing those materials.

We also remind issuers that use exemptions other than the OM Exemption, such as the accredited investor exemption, family, friends and business associates (FFBA) exemption, private issuer exemption or minimum amount exemption, to consider the requirements of OSC Rule 45-501 *Ontario Prospectus and Registration Exemptions* (OSC Rule 45-501) regarding disclosure provided in connection with the distribution of securities. Material purporting to describe the business and affairs of an issuer that are prepared primarily for prospective investors will generally fall within the definition of "offering memorandum" in section 1(1) of the Act. While the use of such documents is voluntary and not subject to specific form requirements, Part 5 of OSC Rule 45-501 provides that statutory rights of action in favour of a purchaser of securities will apply if the material contains a misrepresentation. Furthermore, an issuer is required to include a description of these statutory rights and deliver the material to the OSC within 10 days. These requirements may apply to materials such as investor presentations, letters or brochures.

❖ *Ongoing disclosure requirements*

Issuers are required to make their annual audited financial statements reasonably available to each purchaser of securities distributed under the OM Exemption and to deliver the financial statements to the OSC. These financials statements must be accompanied by a notice detailing the use of funds raised under the exemption in accordance with Form 45-106F16 *Notice of Use of Proceeds.*

As indicated in Appendix D of the Fee Rule, we remind issuers that a fee for the late delivery of annual financial statements to the OSC will be levied.

We also remind issuers that when filing audited annual financial statements, issuers should do so on the OSC's electronic filing portal by selecting "Annual financial statements required to be delivered pursuant to s. 2.9 (17.5) of NI 45-106 *Prospectus Exemptions*." Alternatively, the audited annual financial statements can be attached to the issuer's latest OM if an updated OM is being filed concurrently.

Gathering data regarding the use of the prospectus exemptions

A detailed report regarding the use of prospectus exemptions in Ontario during 2015 and 2016 is available at OSC Staff Notice 45-715 2017 *Ontario Exempt Market Report*.

We remind issuers and investors that new prospectus exemptions were recently introduced including the following:

- Existing security holder exemption – February 11, 2015
- Family, friends and business associates exemption – May 5, 2015

- Offering memorandum exemption – January 13, 2016
- Crowdfunding exemption – January 25, 2016

Investments through the exempt market have increased substantially in the last few years. In 2016, Ontario residents invested approximately $72 billion in over 2,500 non-investment fund issuers through prospectus-exempt offerings. A large number (approximately 57% of Canadian issuers) of small issuers participated in Ontario's exempt market. Small issuers are defined as issuers raising less than $1 million annually.

There was a notable increase in both the number of small Canadian issuers and the gross proceeds raised by these issuers from 2015 to 2016. The increased activity was concentrated among small Canadian issuers in three main industries: natural resources, consumer goods and services and real estate and mortgage finance. Collectively, the new prospectus exemptions have gained traction among a sizeable proportion (25%) of Canadian issuers in the short period that they have been introduced.

Real estate and mortgage investment issuers represented a significant majority of the issuers using the new prospectus exemptions and raised most of the funds under the exemptions. In particular, mortgage investment entities (MIEs) were amongst the most active users of the OM and FFBA exemptions. As a result, most of the issuers we reviewed were real estate issuers or MIEs. We will continue to monitor the use of exemptions to improve compliance and inform future policy-making.

❖ *Priorities*

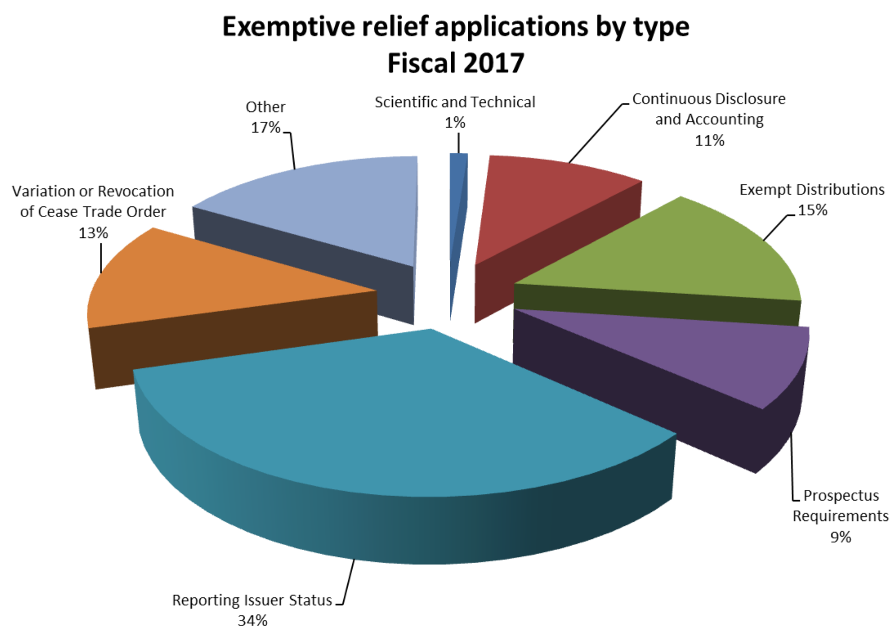
We expect to continue to focus on the distributions under the OM Exemption in the next fiscal year. In addition, we will prioritize reviews of distributions in the real estate and mortgage sector as we consider issues related to the transition of syndicated mortgage investments to the securities regulatory regime. Please refer to "Part C - Responsive Regulation - Syndicated Mortgages" in this report for more details regarding the transfer of regulatory oversight of syndicated mortgage investments.

Exemptive Relief Applications

Staff reviews and makes recommendations to appropriate decision makers on applications for exemptive relief. The review standard for granting relief varies, but it generally requires a decision maker to determine that granting the requested relief would not be prejudicial to the public interest.

Statistics

In fiscal 2017, we reviewed over 170 applications for exemptive relief from various securities law requirements (fiscal 2016: over 160).



Trends and guidance

The number of applications received in fiscal 2017 was moderately higher than fiscal 2016, although the proportion of the various types of applications was generally consistent. Applications for relief in connection with reporting issuer status remained the predominant type of application, followed by exempt distributions and partial or full revocations of cease trade orders.

On June 23, 2016, amendments to Multilateral Instrument 11-102 *Passport System* (MI 11-102) came into force in CSA jurisdictions other than Ontario expanding the passport system to cover applications to cease to be a reporting issuer and Multilateral Instrument 11-103 *Failure-To-File Cease Trade Orders in Multiple Jurisdictions* (MI 11-103) was implemented. See CSA Notice of Publication of Multilateral Instrument 11-102 *Passport System* and Multilateral Instrument 11-103 *Failure-to-File Cease Trade Orders in Multiple Jurisdictions* for further information.

Although Ontario has not adopted MI 11-102 and MI 11-103, two new policies were developed to provide an interface between Ontario and the other CSA jurisdictions to make the securities regulatory system as efficient and effective as possible for all reporting issuers in Ontario and the other CSA jurisdictions:

- National Policy 11-206 *Process for Cease to be a Reporting Issuer Applications* (NP 11-206)

- National Policy 11-207 *Failure-to-File Cease Trade Orders and Revocations in Multiple Jurisdictions* (NP 11-207)

The amendments and implementation of new rules and policies introduced a more efficient process for the filing and review of applications to cease to be a reporting issuer and revocations of failure-to-file cease trade orders. The changes also coordinated the process for jurisdictions to reciprocate failure-to-file cease trade orders, where applicable.

We will continue to monitor the types of applications we receive and the exemptive relief granted to determine whether we should consider changes to our rules or policies.

Key takeaways from our exemptive relief work in fiscal 2017 are set out below.

❖ ***Revocation of a cease trade order that has been breached –*** If an issuer has breached the terms of a cease trade order, it can still seek a revocation. However, we will ask for disclosure of the circumstances surrounding the breach in the draft decision document which staff will consider in making a recommendation in connection with the issuer's application. In some cases, staff will not recommend granting a revocation order in the face of one or more breaches of the cease trade order. Staff may also consider whether breaches of a cease trade order warrant enforcement action.

  We remind issuers and their advisors that "trade" is defined broadly in the Act and includes acts in furtherance of a trade such as advertising or soliciting investors, directly or indirectly, to promote a trade.

❖ ***Revocation of a long standing cease trade order –*** Where an issuer with a long standing cease trade order seeks a revocation, the review process may take longer than usual as staff will review the issuer's updated CD record to consider whether it is sufficient for investors to make an informed decision. In some cases, we may require an issuer to provide a written undertaking that it will not execute a reverse takeover of, a restructuring transaction involving, or a significant acquisition of a business outside of Canada unless the issuer files with the OSC and obtains a receipt for a final prospectus containing the disclosure required for the transaction.

❖ ***Revocation of failure-to-file cease trade orders –*** Under MI 11-103 and local statutory provisions adopted by certain CSA jurisdictions: (i) a failure-to-file cease trade order will generally result in the same prohibition or restriction in other participating jurisdictions; and (ii) a reporting issuer will generally deal only with the regulator that issued the failure-to-file cease trade order if it is seeking a revocation or variation of this order that has the same result in multiple jurisdictions.

  NP 11-207 outlines the interface process for Ontario to opt into decisions to issue and revoke failure-to-file cease trade orders made by other CSA regulators. We remind issuers that in Ontario, as a result of amendments to the Act and the Fee Rule, the OSC can treat the filing of the CD document referred to in a failure-to-file cease trade order that has been in effect for 90 days or less as an application for the revocation of the cease trader order. An application and related fee is not required in this circumstance.

❖ ***Applications for a decision that an issuer is not a reporting issuer –*** We receive a significant number of these applications each fiscal year and our process for reviewing them is currently set out in NP 11-206. The process for Ontario-only applications for such a decision is set out in OSC Staff Notice 12-703 *Applications for a Decision that an Issuer is not a Reporting Issuer*, which was revised on June 16, 2016.

  Foreign issuers who seek a decision that they are no longer a reporting issuer should review the "modified procedure" to consider details that help support such an application. Staff will generally ask issuers to describe the due diligence that was conducted in order to make the representations that residents of Canada do not own more than 2% of each class of outstanding securities and do not comprise more than 2% of the total number of securityholders. We also remind issuers that there should be sufficient time between the required news release announcing the application and the issuance of the order to provide securityholders with the opportunity to object to the order.

- ***Business acquisition report (BAR) relief –*** Relief from the BAR requirements continues to represent a significant number of applications reviewed by the Branch. We remind reporting issuers that the cost or time involved in preparing and auditing the financial statements required to be included in the BAR are not generally viewed by staff as relevant factors when considering whether to recommend relief. Reporting issuers should file their BAR relief applications early to avoid going into default.

  We acknowledge that significance test calculations may, in rare circumstances, result in anomalous results. In these cases, issuers should still be able to demonstrate that an acquisition is not significant. To that effect, staff may consider on a case-by-case basis alternative metrics in support of a determination that an acquisition is not significant from a practical, commercial or financial perspective. In recommending relief, staff will consider the relevance and breadth of alternative metrics presented.

- ***Applications for prospectus and registration relief in connection with employee share offerings by a foreign issuer –*** We have received a number of applications for forward looking (5 years) prospectus and dealer registration relief in connection with global employee share offerings by foreign public companies which typically involve a special purpose investment vehicle (SPIV). We have generally recommended that the requested relief be granted provided that certain representations remain true and correct for any subsequent employee offering and subject to certain customary conditions relating to first trade in securities.

  Under these types of offerings, employees are sometimes provided with an opportunity to participate in a "leveraged plan" under which the SPIV will enter into a swap (a type of derivative) with a financial institution and use the funding to purchase an additional number of shares (e.g., 10 additional shares) on behalf of the employee. We have generally recommended, as a condition of exemptive relief in respect of leveraged plans, that distributions of units of a SPIV to employees in Ontario be made through an investment dealer. Accordingly, if an issuer intends to apply for exemptive relief for an SPIV involving a leveraged plan but without the involvement of an investment dealer, we recommend that the issuer make a pre-filing sufficiently in advance of when the relief is required to allow staff a reasonable period of time to consider the matter. Please see OSC Staff Notice 33-748 *Annual Summary Report for Dealers, Advisers and Investment Fund Managers* for a detailed discussion on this matter.

- ***Applications for prospectus relief generally –*** Issuers and their advisors should carefully consider whether the OSC has previously granted the requested relief with facts and circumstances similar to those of the issuer. Where relief is novel, staff's review will take longer and this process often involves consulting with the CSA. Issuers and their advisors may wish to consider whether a pre-file is appropriate for such novel applications. See National Policy 11-203 *Process for Exemptive Relief Applications in Multiple Jurisdictions*.

Insider Reporting

We review compliance of reporting insiders and issuers with insider reporting requirements through a risk-based compliance program. We actively and regularly assist filers and their agents by providing guidance on filing matters.

The objective of our insider reporting oversight work is two-fold:

- compliance
- education and outreach

Insider reporting serves a number of functions, including deterring improper insider trading based on material undisclosed information and increasing market efficiency by providing investors with information concerning the trading activities of insiders, and, by inference, the insiders' views of the respective issuer's future prospects. Non-compliance affects the integrity, reliability and effectiveness of the insider reporting regime, which in turn has a negative impact on market efficiency. Where we identify non-compliance, we reach out to filers and request remedial filings. Filers should make remedial filings as soon as they become aware of an error to accurately inform investors of their activities and to avoid any further late filing fees.

We educate filers through our compliance reviews and we also reach out to new reporting issuers directly to inform them of insider reporting obligations. We encourage issuers to implement insider trading policies and monitor insider trading to meet best practice standards in National Policy 51-201 *Disclosure Standards*. Issuers and insiders should also review guidance provided in OSC Staff Notice 51-726 *Report on Staff's Review of Insider Reporting and User Guides for Insiders and Issuers*.

Guidance and filing tips

We remind issuers and their insiders that the definition of "reporting insider" can be found in National Instrument 55-104 *Insider Reporting Requirements and Exemptions* (NI 55-104). Issuers and insiders should also refer to the definition of "significant shareholder" and the interpretation of "control" in NI 55-104 as well as the interpretation of "beneficial ownership" in the Act when determining who is required to file on SEDI. Understanding these definitions and interpretations will help filers identify and comply with their obligations.

We also encourage issuers and insiders to refer to the filing tips provided below to avoid some of the common errors we observed during the most recent fiscal year.

❖ ***Tips for issuers***

- Check your issuer profile supplement to ensure your insider affairs contact is up to date.
- Ensure that your issuer profile supplement shows all your security designations.
- If you have engaged in a normal course issuer bid recently, set up an insider profile on SEDI to report acquisitions.
- The exemption in Part 5 of NI 55-104 does not apply to the acquisition of options or similar securities or related financial instruments (e.g. deferred share units, restricted share awards or stock appreciation rights) granted to a director or an officer. Rather, you must comply with Part 6 of NI 55-104 and file an issuer grant report within 5 days of the grant date if you want

insiders to have the benefit of the delayed reporting exemption available for these transactions.

- In filing an issuer grant report, disclose all of the details required by NI 55-104. If you have not, your reporting insiders cannot rely on the exemption in Part 6 of NI 55-104 and may be subject to late filing fees.

- Create deferred share units, restricted share awards and other similar securities under the security category of "issuer derivative" on SEDI. Creating these under the category of "equity" is incorrect.

❖ ***Tips for insiders***

- Check your insider profile to ensure the contact information is correct.

- File an amended insider profile within 10 days of any change in your name, your relationship to an issuer or if you have ceased to be a reporting insider of an issuer.

- File insider reports on SEDI to reflect all of your securities holdings and related transactions for an issuer. For example, if you have recently received a grant of stock options or other form of compensation under a reporting issuer's compensation plan, you are required to file an insider report disclosing those holdings.

- For securities exchangeable, exercisable or convertible into other securities of the issuer, disclose all of the details required by 55-102F2 *Insider Report*, including the exercise price and expiry date.

- File reports on transactions in securities over which you have control or direction or beneficial ownership.

- Consider whether you can rely on any of the exemptions in Part 9 of NI 55-104. For example, the "corporate group" reporting exemption in section 9.5 of NI 55-104 is not available where securities representing 10% or more of voting rights in a reporting issuer are held for an individual through a holding corporation which the individual controls. In such cases, both the individual and the corporation must file insider reports.

- Review CD filings of the reporting issuer (e.g., management information circulars) that include your securities holdings for accuracy and completeness. Report any discrepancies to the reporting issuer.

Designated Rating Organizations

In April 2012, the CSA implemented a regulatory oversight regime for credit rating agencies (CRAs) through National Instrument 25-101 *Designated Rating Organizations* (NI 25-101). The regime recognizes and responds to the role of CRAs in our credit markets, and the role of CRA-issued ratings which are referred to in securities rules and policies. Under the regime, the OSC has the authority to designate a CRA as a DRO, to impose terms and conditions on a DRO, and to revoke a designation order, or change its terms and conditions, where the OSC considers it in the public interest to do so.

There are currently four CRAs that have been designated as DROs in Canada under NI 25-101: DBRS Limited, Fitch Ratings, Inc., Moody's Canada Inc., and S&P Global Ratings Canada. In Canada, the OSC is the principal regulator of these DROs.

We conduct reviews of DROs using a risk-based approach. Our reviews focus on credit rating activities of the CRAs in Canada or in respect of Canadian issuers.

When we identify a concern, or an area of material non-compliance, we may take various actions depending on the nature of the observation and the perceived or potential harm to the marketplace. This may include, but is not limited to, recommending changes to the DRO's policies, procedures or information and documents on the DRO's website, or requiring training or specified oversight of DRO staff in areas where we have seen non-compliance with the DRO's policies or procedures.

Proposed rule amendments and policy changes

On July 6, 2017, the CSA published for comment proposed rule amendments and policy changes related to DROs and credit ratings of DROs.

The CSA is proposing to amend NI 25-101 to reflect new European Union (EU) requirements for credit rating organizations, to ensure the EU continues to recognize the Canadian regime as "equivalent" for regulatory purposes after these new requirements go into effect on June 1, 2018. The proposed amendments would allow credit ratings of a Canadian office of a DRO to continue to be used for regulatory purposes in the EU.

To ensure that NI 25-101 continues to reflect the International Organization of Securities Commissions (IOSCO) Code of Conduct Fundamentals for Credit Rating Agencies (the Code), the proposed amendments also reflect new provisions in the March 2015 version of the Code.

CSA staff are also proposing to amend National Instrument 44-101 *Short Form Prospectus Distributions* and National Instrument 44-102 *Shelf Distributions* to recognize the credit ratings of Kroll Bond Rating Agency, Inc. (Kroll), but only for the purposes of the alternative eligibility criteria for issuers of asset-backed securities to file a short form prospectus or shelf prospectus, respectively. Kroll would only be designated as a DRO if the proposed rule amendments are enacted as final rule amendments and come into effect following any necessary Ministerial approvals. At this time, CSA staff do not anticipate proposing that Kroll be designated as a DRO for purposes of other credit rating provisions in securities rules and policies.

Stakeholders are invited to submit their comments in writing by October 4, 2017.

Part C:
Responsive Regulation

Responsive Regulation

Overview

The OSC continues to play a leading role in several significant policy initiatives with other securities regulators in the CSA in addition to policy initiatives that are applicable only in Ontario. This section reports on the status of certain of these initiatives:

- exempt distribution reporting
- distributions of securities outside of Ontario
- syndicated mortgages
- climate change related disclosures
- reducing regulatory burden for non-investment fund reporting issuers

Exempt Distribution Reporting

In June 2016, the CSA introduced a new harmonized report of exempt distribution which replaced two existing forms. This harmonized report will:

- reduce the compliance burden for issuers and underwriters by having a harmonized report of exempt distribution, and
- provide securities regulators with the necessary information to facilitate more effective regulatory oversight of the exempt market and improve analysis for policy development purposes.

See CSA Notice of Amendments to National Instrument 45-106 *Prospectus Exemptions* Relating to Reports of Exempt Distribution for further information on the new report.

On July 7, 2016, the CSA published a staff notice addressing the granting of an exemption for certain foreign issuers from the requirement in Schedule 1 of the new report to identify whether a purchaser is a registrant or an insider of the issuer. The OSC made as a rule an amendment instrument providing for this exemption in Ontario. The amendment instrument came into force on July 29, 2016.

For more information, see:

- CSA Staff Notice 45-320 *Exemptions for Certain Foreign Issuers from the Requirement to Identify Purchasers as Registrants or Insiders in Reports of Exempt Distribution*
- Ontario Amendment Instrument Amending National Instrument 45-106 *Prospectus Exemptions*
- CSA Staff Notice 45-308 (Revised) *Guidance for Preparing and Filing Reports of Exempt Distribution*

On September 29, 2016, the CSA published revised guidance that included:

- clarification regarding the certification of the report,
- guidance on the reasonable steps the underwriter filing the report should undertake to obtain and confirm the required information regarding the issuer,
- guidance on the procedures that an issuer or underwriter could implement in order to reasonably confirm that a purchaser meets the conditions for a particular exemption,
- guidance on the increased flexibility for completing Schedule 1 for purchasers in certain circumstances who may qualify under more than one paragraph of the definition of "accredited investor", and

- guidance on disclosure of an issuer's North American Industry Classification Standard code that corresponds to the issuer's primary business activity where there is ambiguity on the appropriate code.

On June 8, 2017, the CSA, other than British Columbia Securities Commission, published for a 90-day comment period proposed amendments to the report. The British Columbia Securities Commission anticipates that, subject to receiving the necessary approvals, it will, in the near future, publish for comment amendments that are consistent with those published by the rest of the CSA.

The proposed amendments:

- provide greater clarity and flexibility regarding the certification requirement of the report while still supporting the regulatory objectives of filed reports being true and complete, and
- streamline certain information requirements to assist filers in completing the report while still providing us with the information necessary for oversight and policy development.

Proposed Foreign Issuer Resale Exemption

On June 29, 2017, the OSC, along with the CSA, published for comment proposed amendments to National Instrument 45-102 *Resale of Securities* (NI 45-102). These proposed amendments represent the first phase of a broader CSA policy project to review and modernize the Canadian resale regime for prospectus-exempt securities of both reporting and non-reporting domestic and foreign issuers.

If approved, these amendments to NI 45-102 would introduce a new prospectus exemption for the resale of securities of non-reporting foreign issuers (the Proposed Foreign Issuer Resale Exemption). The Proposed Foreign Issuer Resale Exemption is intended to address feedback we have received that the maximum ownership conditions in the existing resale exemption in section 2.14 of NI 45-102 have become an impediment to participation by certain market participants in prospectus-exempt offerings by foreign issuers.

A key feature of the Proposed Foreign Issuer Resale Exemption is the replacement of the maximum ownership conditions with a new "foreign issuer" test. If adopted, the Proposed Foreign Issuer Resale Exemption would exempt the resale of securities where the issuer is not a reporting issuer in any jurisdiction of Canada if:

- the resale is made on an exchange or a market outside of Canada, or is made to a person or company outside of Canada, and
- the issuer is a "foreign issuer".

The comment period for these proposed amendments to NI 45-102 ends on September 27, 2017. See CSA Notice and Request for Comment on Proposed Amendments to National Instrument 45-102 Resale of Securities, Proposed Changes to Companion Policy 45-102CP to National Instrument 45-102 Resale of Securities, Proposed Consequential Amendments to National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations, and Proposed Consequential Changes to National Policy 11-206 Process for Cease to be a Reporting Issuer Applications.

Distributions of Securities Outside of Ontario

Concurrently with the publication of the CSA's Proposed Foreign Issuer Resale Exemption on June 29, 2017, the OSC republished for comment a revised OSC Rule 72-503 Distributions Outside of Canada (Proposed OSC Rule 72-503) and related materials (the OSC Distributions Out Proposal). See Notice and Request for Comment on Proposed OSC Rule 72-503 Distributions Outside of Canada and Companion Policy 72-503CP to OSC Rule 72-503 Distributions Outside of Canada.

The key change from the OSC's initial publication of proposed OSC Rule 72-503 last summer (2016) was to remove resale provisions from the rule in order to facilitate the harmonization of resale treatment under NI 45-102 and, in particular, under the proposed Foreign Issuer Resale Exemption.

If approved, the OSC Distributions Out Proposal would modernize and replace Interpretation Note 1 Distributions of Securities outside Ontario, bringing greater certainty to cross-border activities in Ontario by providing explicit exemptions from prospectus and registration requirements.

The comment period for the 2017 OSC Distributions Out Proposal ends on September 27, 2017.

Syndicated Mortgages

Subsections 35(4) and 73.2(3) of the Act provide that mortgages sold by persons registered or exempt from registration under mortgage brokerage legislation are exempt from the registration and prospectus requirements in Ontario. These exemptions currently include syndicated mortgages, which are defined as mortgages in which two or more persons participate, directly or indirectly, as the mortgagee. As such, syndicated mortgage investments are primarily regulated by the Financial Services Commission of Ontario (FSCO).

As detailed in the 2017 Ontario Budget, the government plans to transfer regulatory oversight of syndicated mortgage investments from FSCO to the OSC. This is consistent with the manner in which these products are regulated in most other provinces.

Going forward, the government will work with both FSCO and the OSC to plan an orderly transfer of the oversight of these products.

Climate Change Related Disclosures

The disclosure practices of issuers in relation to climate-related risks and financial impacts have attracted significant international attention in recent years. Many investors who are concerned about business risks and financial impacts associated with climate change are requesting improved disclosure of such risks and impacts, and the actions being taken to address them. In addition, the demand for improved disclosure has resulted in the proposal of a number of voluntary frameworks for disclosure of climate-related risks and impacts, culminating in the publication in June 2017 of a set of recommendations by the Financial Stability Board's Task Force on Climate-related Financial Disclosures.

As a result, on March 21, 2017, the CSA announced a project to review the disclosure by Canadian reporting issuers of risks and financial impacts associated with climate change.

Pursuant to this project, we will:

- Review climate-related disclosure requirements in the securities laws of certain international jurisdictions, such as Australia, the United Kingdom and the United States, as well as recommendations contained in voluntary disclosure frameworks for climate-related disclosure, including those published by the International Integrated Reporting Council, the

Global Reporting Initiative, the Sustainability Accounting Standards Board and the Financial Stability Board's Task Force on Climate-Related Financial Disclosures.
- Review public disclosure by Canadian reporting issuers in both their mandatory CD filings and voluntary sustainability disclosure, to assess the extent to which these filings currently include disclosure concerning material climate-related risks and financial impacts, and the governance processes related to them.
- Gather feedback from TSX-listed reporting issuers through an anonymous online survey about climate-related disclosure and associated costs.
- Conduct focused consultations with investors, reporting issuers and other stakeholders.

Following our review, we will publish a progress report outlining the findings of our review. We will also determine whether a further regulatory response is required to enhance climate-change related disclosure.

Reducing Regulatory Burden for Non-Investment Fund Reporting Issuers

The OSC 2016-2017 Statement of Priorities noted that the OSC would continue to try to identify opportunities to avoid or reduce undue burdens and seek opportunities to streamline regulatory measures that balance improving the fairness, efficiency and competitiveness of Ontario's capital markets while maintaining appropriate safeguards for investors. Additionally, the current CSA Business Plan identifies a review of the regulatory burden on reporting issuers as one of the CSA's key initiatives for 2016-2019.

Changes brought on by shifts in market conditions, investor demographics, technological innovation and globalization all have a real impact on reporting issuers. As capital markets evolve, the OSC's approach to regulation needs to reflect the realities of business for Canadian reporting issuers to remain competitive.

In collaboration with the CSA, the OSC published CSA Consultation Paper 51-404 *Considerations for Reducing Regulatory Burden for Non-Investment Fund Reporting Issuers* (the Consultation Paper) on April 6, 2017. The purpose of the Consultation Paper is to identify and consider areas of securities legislation applicable to non-investment fund reporting issuers that could benefit from a reduction of undue regulatory burden, without compromising investor protection or the efficiency of the capital market.

Potential areas identified in the Consultation Paper to reduce regulatory burden in the public markets include:

- Expanding the application of streamlined rules for smaller reporting issuers

- Simplifying prospectus rules and process requirements, which could include:
    - reducing the audited financial statement requirement in an IPO prospectus
    - streamlining other prospectus requirements
    - consideration of an alternative prospectus model
    - facilitating at-the-market offerings
    - facilitating cross-border offerings
    - further liberalizing the pre-marketing and marketing regime

- Reducing ongoing disclosure requirements, which could include:
    - removing or modifying the criteria to file a business acquisition report
    - reducing disclosure requirements in annual and interim filings
    - permitting semi-annual reporting

- Eliminating overlap in regulatory requirements, which could include:
  - eliminating overlap between the disclosure requirements of IFRS and Form 51-102F1
  - eliminating overlap between the various National Instrument 51-102 forms
  - consolidating the requirements of the MD&A, AIF and financial statements into one document

- Identifying ways to enhance electronic delivery of documents

The OSC continues to work with securities regulators in the other CSA jurisdictions to consider all comments received on the Consultation Paper and assess the scope and timing of any further work to reduce regulatory burden for non-investment fund reporting issuers. In collaboration with the CSA, the OSC intends to publish an update on next steps when this assessment has been completed. For more information, see CSA Consultation Paper 51-404 *Considerations for Reducing Regulatory Burden for Non-Investment Fund Reporting Issuers.*

The OSC Inquiries & Contact Centre operates from
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