

B.6

Request for Comments

B.6.1 Proposed Amendments to OSC Rule 48-501 Trading During Distributions, Formal Bids and Share Exchange Transactions and Proposed Changes to Companion Policy 48-501 Trading During Distributions, Formal Bids and Share Exchange Transactions – Notice of Request for Comment

NOTICE OF REQUEST FOR COMMENT

PROPOSED AMENDMENTS TO
ONTARIO SECURITIES COMMISSION RULE 48-501
TRADING DURING DISTRIBUTIONS, FORMAL BIDS AND SHARE EXCHANGE TRANSACTIONS
AND
PROPOSED CHANGES TO
COMPANION POLICY 48-501
TRADING DURING DISTRIBUTIONS, FORMAL BIDS AND SHARE EXCHANGE TRANSACTIONS

June 5, 2025

The Ontario Securities Commission (**Commission**) is publishing proposed amendments (**Proposed Amendments**) to Ontario Securities Commission Rule 48-501 *Trading during Distributions, Formal Bids and Share Exchange Transactions* (**Rule 48-501**) and consequential changes (**Proposed Changes**) to the Companion Policy to Rule 48-501 (**48-501CP**) for a 90 day comment period.

The Proposed Amendments prohibit any person or company who made a short sale (described below) of a security during the period commencing five business days prior to pricing of a prospectus offering or private placement of the same class of securities sold short from buying securities in the offering unless an exemption is available. The purchase of securities in the offering is prohibited even if (i) the short seller had no prior knowledge of the offering, (ii) the offering did not constitute a “material fact” or “material change” (either, **material information**) concerning the issuer, and (iii) the short sales had no impact on the market price of the securities sold.

The Proposed Amendments and Proposed Changes are in Appendix A to this notice. Appendix B contains blacklines of Rule 48-501 and 48-501CP showing the Proposed Amendments and Proposed Changes. Other relevant information is in Appendices C and D and are described below. Appendix E contains a cost-benefit analysis.

The comment period ends on September 3, 2025.

Background

In recent years, there has been increased focus on the regulatory regime governing short selling in Canada. In 2021, the independent Capital Markets Modernization Taskforce (**Taskforce**), formed by the Ontario Minister of Finance, issued its Final Report (**Taskforce Report**), which contained a recommendation to prohibit short selling in connection with prospectus offerings and private placements. The Taskforce found that short selling in connection with prospectus offerings and private placements, and in particular bought deals pre-arranged with hedge funds who short the stock before the bought deal is announced, makes pricing and completion of offerings more difficult.

The Taskforce believed that a requirement that does not require regulators to prove intent, similar to the U.S. Securities and Exchange Commission (**SEC**)’s Rule 105 of Regulation M: *Short Selling in Connection with a Public Offering* (**Rule 105**),¹ is preferable in the circumstances of short selling in advance of an offering.

The Taskforce Report’s recommendation is attached as Appendix C to this notice.

Substance and Purpose

The Proposed Amendments would implement the Taskforce Report’s recommendation and are broadly aligned with Rule 105, however, are wider in scope in terms of the type of offering they would apply to, specifically to public offerings on a “best-efforts” basis and private placements. They also complement other initiatives to modernize short sale regulation by the Canadian Investment Regulatory Organization (**CIRO**): strengthening the obligation of CIRO dealers members entering short sell orders on

¹ 17 CFR §242.105.

a marketplace to have a reasonable expectation to settle any resulting trade at the time the order is entered,² and a proposed requirement for dealers to close out fail-to-deliver positions in the event of settlement failure at a clearing agency.³

The Proposed Amendments address two separate, but related concerns. The first is that a person or company learns of an upcoming financing by an issuer that has not been publicly announced and makes short sales in advance of the announcement intending to close out the short position by buying back securities in the financing, which will almost always be priced at a discount to the current market price, thus locking in a profit. Such short-selling activity is not driven by any fundamental views on the price of the security but rather by an opportunity to arbitrage the difference between the current market price and the offering price. The second is that the short selling itself may depress the market price, in turn lowering the price at which securities are sold in the financing.

Although there are rules, such as prohibitions on market manipulation and trading on the basis of non-public material information, that could apply to the conduct covered by the Proposed Amendments, not all conduct amounts to violations of those rules as those rules seek to address different policy concerns. For example, the financing may not be “material information” under either securities legislation or the listing exchange’s timely disclosure policies, with the issuer having no requirement to publicly disclose it. Similarly, the short selling activity may not set an artificial price for the security; it may not change the market price at all. Even if these provisions are violated, there are obstacles to enforcement. Proving a violation of trading on the basis of non-public material information⁴ requires, among other things, proving that: (i) the respondent had knowledge of the information, and (ii) the information was material.

Similarly, artificially moving the market price of a security down in order to lower the price of an offering is prohibited market manipulation,⁵ but proving a violation requires, among other things, proving (i) the creation of a misleading appearance of trading activity or an artificial price for the security; and (ii) that the respondent knew or ought to have known that would be the result.

The Proposed Amendments would prohibit buying securities in a prospectus offering or private placement in certain circumstances where the purchaser has previously made short sales of the security sold in the prospectus offering or private placement. This would introduce a conduct rule that does not require proof of knowledge, materiality or effect on market price.

The Proposed Amendments are broadly aligned with Rule 105, which is familiar to dealers with cross-border operations, but as noted above, are wider in scope in terms of the type of offering that the Proposed Amendments would apply to.

Questions:

- 1. Will the Proposed Amendments address concerns with short selling making pricing and completion of offerings more difficult?**
- 2. Will the Proposed Amendments have any unintended consequences, such as (i) making it more difficult for certain reporting issuers to raise capital or (ii) requiring a greater price discount on offerings?**

The Proposed Amendments

Short Sales

The term “short sale” is not defined in the *Securities Act* (Ontario) (**Act**), although the Act refers to “short positions,” meaning a sell order of securities the seller does not own.⁶ CRO defines “short sale” more expansively in the Universal Market Integrity Rules (**UMIR**) to mean “a sale of a security, other than a derivative instrument, which the seller does not own either directly or through an agent or trustee.”⁷ The definition goes on to list circumstances where a seller is considered either to own or not own the security to be sold.

The definition in the Proposed Amendments is more focused than either the Act or UMIR and is tailored to the activity the Proposed Amendments seek to prevent. For this reason, the definition in the Proposed Amendments is limited to Rule 48-501.

“Short sale” for the purposes of the Proposed Amendments is any sale of a security: (i) where the seller does not have title to the security sold; or (ii) that is settled or intended to be settled by the delivery of borrowed securities. This is similar to the definition in SEC Rule 200, which includes any sale settled with borrowed securities as a “short sale” even if the seller is otherwise deemed to own the securities sold.⁸ This definition will cover sales settled with borrowed securities even if the seller otherwise has a long position in the security (for example, a long holder making a sale to be settled with borrowed securities in order to create a separate short account). The focus on settlement with borrowed securities also prevents a short seller from arguing that the securities

² <https://www.ciro.ca/newsroom/publications/amendments-respecting-reasonable-expectation-settle-short-sale>.

³ <https://www.ciro.ca/rules-and-enforcement/consultations/proposed-amendments-respecting-mandatory-close-out-requirements>.

⁴ *Securities Act*, R.S.O. 1990, c. S.5 (the Act), s. 76.

⁵ Act, s. 126.1.

⁶ Act, s. 48.

⁷ UMIR s. 1.1 (definition of “short sale”).

⁸ 17 CFR §242.200. UMIR does not consider a sale settled by delivery of borrowed securities to be a short sale if the seller is otherwise deemed to own the securities sold.

lending agreement under which the seller acquired the securities transferred title, and therefore the seller has title to the securities sold.⁹

Questions:**3. Is the definition of “short sale” in the Proposed Amendments adequate for achieving the purposes of the Proposed Amendments?****Prohibited Conduct***No Restrictions on Short Selling*

The Proposed Amendments do not prohibit or create new restrictions on short selling at any time, including periods before a corporate financing. Existing rules prohibiting manipulative or deceptive trading or trading with knowledge of undisclosed material information would continue to apply to all trading activity, including short sales. UMIR rules governing short selling and manipulative trading would also continue to apply.

Prohibition on Participation in Prospectus Offerings and Private Placements

The Proposed Amendments prohibit any person or company who made a short sale of a security during the period commencing five business days prior to pricing a prospectus offering or private placement of the same class of securities sold short from participating in the offering unless an exemption is available. The purchase of securities in the offering is prohibited even if (i) the short seller had no prior knowledge of the offering, (ii) the offering did not constitute material information concerning the issuer, and (iii) the short sales had no impact on the market price of the securities sold.

Scope of the Prohibition – Reporting Issuers

The Proposed Amendments only apply to distributions made by issuers who are reporting issuers in Ontario. Except as provided in section 4.1.2, there are no other criteria that limit the application of the Proposed Amendments, including with respect to the person or company that would otherwise be subject to section 4.1.1.

Questions:**4. Should the Proposed Amendments apply to distributions of securities of a broader or narrower group of issuers? If so, what criteria should be used to define this population?***Scope of the Prohibition – Securities Covered*

The Proposed Amendments apply to distributions of equity securities other than units of an exchange-traded fund (ETF) where the securities are sold for cash. The Proposed Amendments are intended to apply to distributions conducted by a reporting issuer for capital raising purposes.

The Proposed Amendments prohibit the purchase of securities under an offering where securities of the same class as the purchased security were sold short during the short sale restricted period. Accordingly, in an offering of convertible or exchangeable securities, a person or company that sells short the security for which the convertible security is exchangeable or convertible into is not prohibited from purchasing the convertible securities under the offering. The Proposed Amendments apply in this manner as the pricing of a convertible security can be influenced by factors beyond the prevailing price of the underlying security. Although certain convertible or exchangeable securities may have high price correlation with the securities to which they are convertible or exchangeable for, limiting the scope of the Proposed Amendments in this manner provides greater certainty to investors seeking to participate in an offering and provides issuers with discretion to negotiate and structure their financing arrangements without the application of the Proposed Amendments.

Furthermore, the Proposed Amendments would not apply to a distribution that is exempt from the prospectus requirement pursuant to section 2.42 of National Instrument 45-106 *Prospectus Exemptions*. For example, in a distribution of units (where a unit is comprised of a common share and a warrant exercisable for a common share at a price that is determined prior to the distribution of the unit), the Proposed Amendments would not apply to the distribution of common shares upon exercise of the warrants. Due to the potential prolonged period of time between the pricing of the underlying common share and the exercise of the warrant, and that a holder may have acquired the warrant in the secondary market as opposed to the initial offering, it may be overly burdensome for holders of warrants to ensure short sales were not conducted during the short sale restricted period. As well, the absence of an exemption could deter secondary market purchases of the warrants, thereby reducing liquidity.

The Proposed Amendments also do not apply to bona fide open-market purchases of securities sold in an at-the-market distribution as the purchaser would not have knowledge of the identity of the seller. The Proposed Changes specify that trades

⁹ A standard securities lending agreement contemplates that the securities lent may be resold by the borrower. The obligation of the borrower is to return the equivalent number of securities borrowed, not the exact securities.

between the issuer in an at-the-market offering and a purchaser that are arranged by a dealer and reported to a marketplace as a cross are not open-market transactions.

Questions:

- 5. Are the securities covered by the Proposed Amendments correctly scoped?**
- 6. Is the prohibition on buying and selling short a security “of the same class” too narrow?**
- 7. Is the exemption under section 4.1.2(b) of the Proposed Amendments appropriate?**
- 8. Are there other types of distributions or securities that should be exempted from the Proposed Amendments?**

Scope of the Prohibition – Restricted Period

The Proposed Amendments cover short sales made in the period commencing five business days prior to pricing and ending at pricing. “Pricing” is defined as the time at which the monetary consideration for the securities to be offered is determined. The Proposed Changes clarify that agreement on a formula to determine the monetary consideration at a future time (e.g., a 10 percent discount from the closing price of the security on the listing exchange on a particular day) is not “pricing”.

The restricted period ends at pricing. Therefore, a purchaser in a prospectus offering or private placement will be able to make short sales after that time and participate in the offering.

Questions:

- 9. The 5-day period is based on Rule 105 and is intended to ensure that, in a marketed offering, a short seller intending to participate in the offering would not have an opportunity to adversely affect the market price of the offering through short sales immediately before pricing of the offering, as any activity from before that period should no longer be reflected in the market price of the offered securities. Is this assumption correct?**
- 10. Should the restricted period be extended for a period of time following pricing?**
- 11. Does your answer to Question 9 depend on whether the issuer made a press release announcing the offering and when the press release was issued?**

Scope of the Prohibition – Repurchases Prior to Pricing

The Proposed Amendments do not apply if the short seller makes bona fide open-market purchases of an equivalent quantity of the entire amount of the securities sold short no later than the business day prior to pricing.

Scope of the Prohibition – Application to Underwriters and Market Makers

Although the Taskforce Report suggested consideration be given to exemptions for market makers, the Proposed Amendments do not provide exemptions for underwriters of the offering or market makers. This is consistent with Rule 105.

In the case of underwriters, short sales, if any, are typically made to purchasers of the offered securities in an over-allocation after pricing, or the conclusion of the short sale restricted period. The underwriter's short position is then closed through the exercise of the over-allotment option or open-market purchases. In the case of market makers, the Commission believes the market maker will normally have an exemption for trades made through separate accounts where decisions for each account are made separately and without coordination.

Question:

- 12. Is the assumption that the separate account exemption will be sufficient for underwriters and market makers correct? If not, please provide specific examples of how the Proposed Amendments would adversely affect their activities.**

Other Amendments

Rule 48-501 covers three separate issues concerning market activity during distributions:

- Open-market purchases by issuers, underwriters and related parties that may set an artificial price for the security being distributed in order to make a sale in a distribution, or a tender to a take-over bid or issuer bid more attractive;

- Issuance of research reports during a distribution that could be considered solicitations of purchases of the distributed security or tenders to a take-over bid or issuer bid; and
- Purchases of securities in a distribution by persons or companies who make short sales in the period immediately prior to pricing of the distribution.

Several reorganizations are made in the Proposed Amendments to make this separation of issues clearer. Purchasers by issuers and underwriters were previously covered by Parts 2 and 3 of Rule 48-501. The Proposed Amendments move former section 3.2 to Part 2 so all rules governing issuers and underwriters are found in Part 2, with Part 3 repealed. The Proposed Changes have a new Part 1.1 that explains the separate issues, and a provision formerly in Part 5 that explains that Rule 48-501 does not affect the application of anti-fraud and manipulation rules is moved to this new Part. Two exemptions for dealers involved in distributions (new sections 2.2.1 and 4.3) that were inadvertently deleted when Rule 48-501 was last amended have been restored.

Alternatives considered

No alternatives were considered.

Anticipated costs and benefits

A cost-benefit analysis is included in Appendix “E” to this Notice.

Question:

- 13. Are there any additional foreseeable costs if the Proposed Amendments are adopted? Can these costs be mitigated?**

Unpublished Materials

In developing the Proposed Amendments and Proposed Changes, the Commission did not rely on any unpublished study, report or other written materials.

Rule-Making Authority

The Proposed Amendments are made pursuant to the rule-making authority in the following provisions of the Act: (i) paragraph 11 of subsection 143(1) authorizes the Commission to make rules regulating the trading of publicly-traded securities and (ii) paragraph 13 of subsection 143(1) authorizes the Commission to regulate trading in securities to prevent trading that is fraudulent, manipulative, deceptive or unfairly detrimental to investors.

Questions

Please direct any questions with respect to this notice, the Proposed Amendments or Proposed Changes to:

Timothy Baikie
Senior Legal Counsel, Trading and Markets
Ontario Securities Commission
tbaikie@osc.gov.on.ca

Appendix A

**PROPOSED AMENDMENTS TO
ONTARIO SECURITIES COMMISSION RULE 48-501
TRADING DURING DISTRIBUTIONS, FORMAL BIDS AND SHARE EXCHANGE TRANSACTIONS**

1. **Ontario Securities Commission Rule 48-501 Trading during Distributions, Formal Bids and Share Exchange Transactions is amended by this Instrument.**

2. **Section 1.1 is amended**

(a) **by adding the following definitions:**

“at-the-market distribution” has the meaning ascribed to that term in National Instrument 44-102 *Shelf Distributions*;

“borrow” means, in respect of a security, the acquisition of the security pursuant to a securities lending arrangement and “borrow” and “borrowed” have a corresponding meaning;

“exchange-traded fund” has the meaning ascribed to that term in National Instrument 23-103 *Trading Rules*;

“pricing” means, in respect of a security, the time that the amount of monetary consideration for the issue of the security is determined, or if the security is a component of a unit, the time that the amount of monetary consideration for the issue of the unit is determined;

“securities lending arrangement” has the meaning ascribed to it in section 5.1 of National Instrument 62-104 *Take-Over Bids and Issuer Bids*;

“short sale” in this Rule means either of the following and “sold short” has a corresponding meaning:

- (a) a sale of a security where the seller does not have title to the security;
- (b) a sale of a security that is settled or is intended to be settled by delivery of a security borrowed by or for the account of the seller;

“short sale restricted period” means, in respect of a security, the period commencing five business days before pricing and ending at pricing; and

“short sale restricted security” means a security that is an equity security other than a unit of an exchange-traded fund.

(b) **by deleting the word “and” after the definition of “restricted private placement”.**

3. **Part 2 is renamed “RESTRICTIONS ON BIDS AND PURCHASES BY DEALER-RESTRICTED PERSONS AND ISSUER-RESTRICTED PERSONS”.**

4. **Part 2 is amended**

(a) **by replacing “section 3.2” in Section 2.2 with “section 2.4”; and**

(b) **by adding the following sections:**

“2.2.1 Despite subsection 2.2, a dealer-restricted person that is also an issuer-restricted person may bid for or purchase a restricted security if the bid or purchase is made through the facilities of a marketplace in accordance with applicable marketplace rules.” and

“2.4 Exemptions - Issuer-restricted Persons

Section 2.2 does not apply to an issuer-restricted person in connection with any of the following:

- (a) the exercise of an option, right, warrant, or a similar contractual arrangement held or entered into by the issuer restricted person prior to the commencement of the issuer-restricted period;
- (b) a bid or purchase of a restricted security pursuant to a small securityholder selling and purchase arrangement made in accordance with National Instrument 32-101 *Small Securityholder Selling and Purchase Arrangements* or similar rules applicable to any marketplace on which the bid or purchase is entered or executed;

- (c) an issuer bid described in sections 4.6 and 4.7 of National Instrument 62-104 *Take-Over Bids and Issuer Bids* if the issuer did not solicit the sale of the securities sold under those clauses;
- (d) the solicitation of the tender of securities to a securities exchange takeover bid or issuer bid;
- (e) a subscription for or purchase of an offered security pursuant to a prospectus distribution or restricted private placement.”.

5. Part 3 is repealed.

6. The Instrument is amended by adding the following section:

“4.3 Where a dealer-restricted person is also an issuer-restricted person the exemptions in section 4.1 and 4.2 continue to be available to the dealer-restricted person.”

7. The Instrument is amended by adding the following Part:

“Part 4.1 RESTRICTION ON PARTICIPATING IN A DISTRIBUTION WHERE SHORT SALES WERE MADE BEFORE PRICING

4.1.1 Restriction on purchases of short sale restricted securities sold in a distribution where short sales were made before pricing

Except as provided in section 4.1.2, a person or company must not directly or indirectly purchase a short sale restricted security that is being sold in a distribution by a reporting issuer for cash if the person or company made a short sale of a security of the same class as the short sale restricted security during the short sale restricted period.

4.1.2 Exceptions

(1) A person or company may purchase the short sale restricted security described in section 4.1.1 in an open-market transaction on a marketplace in a distribution that is an at-the-market distribution.

(2) A person or company may purchase the short sale restricted security described in section 4.1.1 in a distribution that is exempt from the prospectus requirement pursuant to section 2.42 of National Instrument 45-106 *Prospectus Exemptions*.

(3) A person or company may purchase the short sale restricted security described in section 4.1.1 if the person or company made bona fide purchases of securities of the same class as the securities sold in the distribution and those purchases are

- (a) at least equivalent in quantity to the entire amount of the short sale restricted securities sold short by the person or company during the short sale restricted period,
- (b) made in open-market transactions on a marketplace, and
- (c) made no later than the business day prior to pricing.

(4) A person or company that sold short a short sale restricted security during the short sale restricted period may purchase a short sale restricted security described in section 4.1.1 in a separate account, if decisions regarding securities transactions for each account are made separately and without coordination of trading or cooperation among or between the accounts.”

8. This Instrument comes into force on [•].

**PROPOSED CHANGES TO
COMPANION POLICY 48-501
TRADING DURING DISTRIBUTIONS, FORMAL BIDS AND SHARE EXCHANGE TRANSACTIONS**

1. ***Companion Policy 48-501 to Ontario Securities Commission Rule 48-501 Trading during Distributions, Formal Bids and Share Exchange Transactions is changed by this Document.***

2. ***The Companion Policy is changed by adding the following Part:***

“Part 1.1 — Structure of the Rule

1.1.1 Rule 48-501 *Trading during Distributions, Formal Bids and Share Exchange Transactions* (the **Rule**) covers activities by persons and companies involved in distributions of securities. There are 3 different areas covered by the Rule:

- bids and purchases of securities of the same class as securities offered in a distribution, and solicitations of bids and purchases, other than solicitations to purchase the offered securities;
- publication of research reports by dealers involved in a distribution that cover the issuer of the offered securities; and
- restrictions on purchases of certain equity securities (other than units of exchange-traded funds) that are sold in a distribution where short sales were made in the period before pricing.

1.1.2 Fraud and Manipulation — Provisions against manipulation and fraud are found in securities legislation. Specifically, section 126.1 of the *Securities Act* (the **Act**) and Part 3 of National Instrument 23-101 *Trading Rules* (**NI 23-101**) prohibit manipulative or deceptive trading, including activities that may create misleading pricing or trading activity that is detrimental to investors and the integrity of the markets. Section 76 of the Act prohibits persons or companies in a special relationship with an issuer from trading the issuer's securities with knowledge of a material fact that has not been generally disclosed. The Rule specifically prohibits certain trading activities in circumstances where there is heightened concern over the possibility of manipulation by those with an interest in the outcome of the distribution or transaction. This rule is in addition to existing rules prohibiting market manipulation and trading on the basis of non-public material information and does not in any way interfere with those existing rules.”

3. ***Part 2 is changed by adding the following sections:***

“2.4 Pricing of a short sale restricted security described in section 4.1.1 occurs when the sale price for the short sale restricted security is determined and finalized. An offering that will be sold at an undetermined price to be established later (e.g. a certain percentage below that day's closing price on the principal market for the security) is not priced until the closing price is known.

2.5 “Open-market transactions” in this Rule are transactions made by entry of orders on a marketplace where buyers and sellers are matched by the marketplace's trading system. Trades where a dealer matches buyers and sellers or pairs orders with contra-side orders outside a marketplace and then reports the matched or paired orders to a marketplace as a cross are not open market transactions.”

4. ***Part 5 is deleted.***

5. ***The Companion Policy is changed by adding the following Part:***

“Part 7 – PARTICIPATING IN A DISTRIBUTION WHERE SHORT SALES WERE MADE BEFORE PRICING

7.1 Section 4.1.1 of the Rule restricts purchases of certain equity securities (other than units of exchange-traded funds) that are sold in a distribution where short sales of the same class of securities were made in the period before pricing. The Rule does not prohibit or restrict short selling. The definition of “short sale” is broader than the corresponding definition in the Canadian Investment Regulatory Organization's Universal Market Integrity Rules. The term covers any sale of a security that the seller does not have title to or that is settled by, or intended to be settled by, delivery of borrowed securities, even if the seller owns or is otherwise deemed to own the securities sold. Section 4.1.1 of the Rule applies even if ultimately there is no delivery obligation on the part of the dealer entering the short sell order (on its own or a client's behalf) due to netting of trades by a clearing agency. Short sales made during the short sale restricted period trigger the restrictions in the Rule even if the date for settlement of the short sales is after the date of purchases made to close the short position.

7.2 Section 4.1.1 of the Rule applies to distributions of equity securities, other than units of exchange-traded funds, sold for cash. It is intended to apply to distributions conducted by a reporting issuer for capital raising purposes, for example, where a reporting issuer raises funds through a private placement of equity securities to accredited investors.

7.3 Section 4.1.1 of the Rule restricts purchases of certain equity securities where securities of the same class as the equity securities were sold short during the short sale restricted period. Accordingly, in an offering of convertible or exchangeable securities, a person or company that sells short the security underlying the convertible or exchangeable security is not prohibited from purchasing the convertible or exchangeable security under the offering.

7.4 Section 4.1.1 of the Rule does not apply to a distribution of equity securities that is exempt from the prospectus requirement pursuant to section 2.42 of NI 45-106. For example, where a warrant is exercised to acquire equity securities for cash, the distribution of such equity securities would not be subject to section 4.1.1.

7.5 For the purposes of Part 4.1 of the Rule, a distribution of a unit is a distribution of the securities comprising that unit. Accordingly, where securities comprising a unit are equity securities, short sales of any of those equity securities will be subject to the Rule.

7.6 For the purposes of Part 4.1 of the Rule, indirect purchasing of securities under a prospectus or private placement is also prohibited. Examples of indirect purchases include the short seller entering an agreement or arrangement with a person or company that has not sold short, pursuant to which that person or company buys securities in the distribution and transfers them to the short seller.”

6. These changes will become effective on [•].

Appendix B

Ontario Securities Commission

**Rule 48-501
Trading During Distributions,
Formal Bids and Share Exchange Transactions**

PART 1 – DEFINITIONS

1.1 Definitions

In this Rule

“at-the-market distribution” has the meaning ascribed to that term in National Instrument 44-102 *Shelf Distributions*;

“borrow” means, in respect of a security, the acquisition of the security pursuant to a securities lending arrangement and “borrow” and “borrowed” have a corresponding meaning;

“connected security” means, in respect of an offered security,

- (a) a security into which the offered security is immediately convertible, exchangeable or exercisable unless the security is a listed security or quoted security and the price at which the offered security is convertible, exchangeable or exercisable is greater than 110% of the best ask price of the security at the commencement of the restricted period,
- (b) a security of the issuer of the offered security or another issuer that, according to the terms of the offered security, may significantly determine the value of the offered security,
- (c) if the offered security is a special warrant, the security which would be issued on the exercise of the special warrant, and
- (d) if the offered security is an equity security, any other equity security of the issuer,

where the security trades on a marketplace or a market where there is mandated transparency of orders or trade information;

“dealer-restricted period” means, for a dealer-restricted person, the period,

- (a) in connection with a prospectus distribution or a restricted private placement of an offered security, commencing on the later of
 - (i) the date two trading days prior to the day the offering price of the offered security is determined, and
 - (ii) the date on which a dealer enters into an agreement or reaches an understanding to participate in the prospectus distribution or restricted private placement of securities, whether or not the terms and conditions of such participation have been agreed upon, andending on the date the selling process ends and all stabilization arrangements relating to the offered security are terminated,
- (b) in connection with a securities exchange take-over bid or issuer bid, commencing on the date of dissemination of the take-over bid circular, issuer bid circular or similar document and ending with the termination of the period during which securities may be deposited under such bid, including any extension thereof, or the withdrawal of the bid, and
- (c) in connection with an amalgamation, arrangement, capital reorganization or similar transaction, commencing on the date of dissemination of the information circular for such transaction and ending on the date of approval of the transaction by the security holders that will receive the offered security or the termination of the transaction by the issuer or issuers;

“dealer-restricted person” means, in respect of a particular offered security,

- (a) a dealer that
 - (i) is an underwriter, as defined in the Act, in a prospectus distribution or a restricted private placement,

- (ii) is participating, as agent but not as an underwriter, in a restricted private placement, and
 - (A) the number of securities to be issued under the restricted private placement would constitute more than 10% of the issued and outstanding offered securities, and
 - (B) the dealer has been allotted or is otherwise entitled to sell more than 25% of the securities to be issued under the restricted private placement,
 - (iii) has been appointed by an offeror to be the dealer-manager, manager, soliciting dealer or adviser in respect of a securities exchange take-over bid or issuer bid, or
 - (iv) has been appointed by an issuer to be the soliciting dealer or adviser in respect of obtaining security holder approval for an amalgamation, arrangement, capital reorganization or similar transaction that would result in the issuance of securities that would be a distribution exempt from prospectus requirements in accordance with applicable securities law, where, in each case, adviser means an adviser whose compensation depends on the outcome of the transaction,
- (b) a related entity of the dealer referred to in clause (a) but does not include such related entity, or any separate and distinct department or division of a dealer referred to in clause (a) where,
- (i) the dealer
 - (A) maintains and enforces written policies and procedures reasonably designed to prevent the flow of information regarding any prospectus distribution, private placement or transaction referred to in clause (a) to or from the related entity, department or division, and
 - (B) obtains an annual assessment of the operation of such policies and procedures,
 - (ii) the dealer has no officers or employees that solicit orders or recommend transactions in securities in common with the related entity, department or division, and
 - (iii) the related entity, department or division does not during the dealer-restricted period, in connection with the restricted security,
 - (A) act as a market maker (other than to meet its obligations under the rules of a recognized exchange),
 - (B) solicit orders from clients, or
 - (C) engage in proprietary trading,
- (c) a partner, director, officer, employee or a person holding a similar position or acting in a similar capacity for the dealer referred to in clause (a) or for a related entity of the dealer referred to in clause (b), or
- (d) any person or company acting jointly or in concert with a person or company described in clause (a), (b) or (c) for a particular transaction;

"exchange-traded fund" has the meaning ascribed to it in National Instrument 23-103 *Trading Rules*;

"highly-liquid security" means a listed security or quoted security that,

- (a) has traded, in total, on one or more marketplaces as reported on a consolidated market display during a 60-day period ending not earlier than 10 days prior to the commencement of the restricted period,
 - (i) an average of at least 100 times per trading day, and
 - (ii) with an average trading value of at least \$1,000,000 per trading day, or
- (b) is subject to Regulation M under the 1934 Act and is considered to be an "actively-traded security" thereunder;

"issuer-restricted period" means, for an issuer-restricted person, the period,

- (a) in connection with a prospectus distribution or a restricted private placement of an offered security, commencing on the date two trading days prior to the day the offering price of the offered security is determined, and ending on the date the selling process ends and all stabilization arrangements relating to the offered security are terminated,

- (b) in connection with a securities exchange take-over bid or issuer bid, commencing on the date of the dissemination of the take-over bid circular, issuer bid circular or similar document and ending with the termination of the period during which securities may be deposited under such bid, including any extension thereof, or the withdrawal of the bid, and
- (c) in connection with an amalgamation, arrangement, capital reorganization or other similar transaction, commencing on the date of dissemination of the information circular for such transaction and ending on the date of approval of the transaction by the security holders that will receive the offered security or the termination of the transaction by the issuer or issuers;

“issuer-restricted person” means, in respect of a particular offered security,

- (a) the issuer of the offered security,
- (b) a selling security holder of the offered security in connection with a prospectus distribution or restricted private placement,
- (c) an affiliated entity of the issuer of the offered security or a selling security holder; or
- (d) any person or company acting jointly or in concert with the person or company described in clause (a), (b) or (c) for a particular transaction;

“last independent sale price” means the last sale price of a trade on a market, other than a trade that a dealer-restricted person knows or ought reasonably to know was made by or on behalf of a person or company that is a dealer-restricted person or an issuer-restricted person;

“offered security” means all securities, that trade on a marketplace or a market where there is mandated transparency of orders or trade information, of the class of security that

- (a) is offered pursuant to a prospectus distribution or a restricted private placement,
- (b) is offered by an offeror in a securities exchange take-over bid in respect of which a take-over bid circular or similar document is required to be filed under securities legislation,
- (c) is offered by an issuer in an issuer bid in respect of which an issuer bid circular or similar document is required to be filed under securities legislation, or
- (d) would be issuable to a security holder pursuant to an amalgamation, arrangement, capital reorganization or similar transaction in relation to which proxies are being solicited from security holders that will receive the offered security in such circumstances that the issuance would be a distribution exempt from prospectus requirements in accordance with applicable securities legislation,

provided that, if the security referred to in clauses (a) to (d) is a unit comprised of more than one type or class, each security comprising the unit shall be considered an offered security;

“pricing” means, in respect of a security, the time that the amount of monetary consideration for the issue of the security is determined, or if the security is a component of a unit, the time that the amount of monetary consideration for the issue of the unit is determined;

“restricted private placement” means a distribution of offered securities made pursuant to sections 2.3 or 2.30 of National Instrument 45-106 *Prospectus and Registration Exemptions*;

“restricted security” means the offered security or any connected security; ~~and~~

“securities lending arrangement” has the meaning ascribed to it in section 5.1 of National Instrument 62-104 *Take-Over Bids and Issuer Bids*;

“short sale” in this Rule means either of the following and “sold short” has a corresponding meaning:

- (a) a sale of a security where the seller does not have title to the security;
- (b) a sale of a security that is settled or is intended to be settled by delivery of a security borrowed by or for the account of the seller;

“short sale restricted period” means, in respect of a security, the period commencing five business days before pricing and ending at pricing; and

“short sale restricted security” means a security that is an equity security other than a unit of an exchange-traded fund.

1.2 Interpretation

- (1) Affiliated Entity - The term “affiliated entity” has the meaning ascribed to that term in section 1.3 of National Instrument 21-101 – *Marketplace Operation*.
- (2) [Repealed].
- (3) Equity Security - An equity security is any security of an issuer that carries a residual right to participate in the earnings of the issuer and, upon liquidation or winding up of the issuer, in its assets.
- (4) Related Entity - In respect of a dealer, a related entity is an affiliated entity of the dealer that carries on business in Canada and is registered as a dealer or adviser in accordance with applicable securities legislation.
- (5) For the purposes of the definitions of “dealer-restricted period” and “issuer-restricted period”:
 - (a) the selling process shall be considered to end,
 - (i) in the case of a prospectus distribution, if a receipt has been issued for the final prospectus, the dealer has allocated all of its portion of the securities to be distributed under the prospectus and all selling efforts have ceased, and
 - (ii) in the case of a restricted private placement, the dealer has allocated all of its portion of the securities to be distributed under the offering; and
 - (b) stabilization arrangements shall be considered to have terminated in the case of a syndicate of underwriters or agents when, in accordance with the syndication agreement, the lead underwriter or agent determines that the syndication agreement has been terminated such that any purchase or sale of a restricted security by a dealer after the time of termination is not subject to the stabilization arrangements or otherwise made jointly for the dealers that were party to the stabilization arrangements.

PART 2 – RESTRICTIONS ON BIDS AND PURCHASES BY DEALER-RESTRICTED PERSONS AND ISSUER-RESTRICTED PERSONS

2.1 [Repealed]

2.2 Issuer-restricted Person

Except as permitted under section 2.4 3.2, an issuer-restricted person shall not at any time during the issuer-restricted period,

- (a) bid for or purchase a restricted security for an account of an issuer-restricted person or an account over which the issuer-restricted person exercises direction or control; or
- (b) attempt to induce or cause any person or company to purchase any restricted security.

2.2.1 Despite subsection 2.2, a dealer-restricted person that is also an issuer restricted person may bid for or purchase a restricted security if the bid or purchase is made through the facilities of a marketplace in accordance with applicable marketplace rules.

2.3 Deemed Re-commencement of a Restricted Period

If a dealer appointed to be an underwriter in a prospectus distribution or a restricted private placement receives a notice or notices of the exercise of statutory rights of withdrawal or rights of rescission from purchasers of, in the aggregate, not less than 5% of the offered securities allotted to or acquired by the dealer in connection with the prospectus distribution or the restricted private placement then a dealer-restricted period and issuer-restricted period shall be deemed to have re-commenced upon receipt of such notice or notices and shall be deemed to have ended at the time the dealer has distributed its participation, including the securities that were the subject of the notice or notices of the exercise of statutory rights of withdrawal or rights of rescission.

2.4 Exemptions - Issuer-restricted Persons

Section 2.2 does not apply to an issuer-restricted person in connection with any of the following:

- (a) the exercise of an option, right, warrant, or a similar contractual arrangement held or entered into by the issuer restricted person prior to the commencement of the issuer-restricted period;

- (b) a bid or purchase of a restricted security pursuant to a small securityholder selling and purchase arrangement made in accordance with National Instrument 32-101 *Small Securityholder Selling and Purchase Arrangements* or similar rules applicable to any marketplace on which the bid or purchase is entered or executed;
- (c) an issuer bid described in sections 4.6 and 4.7 of National Instrument 62-104 *Take-Over Bids and Issuer Bids* if the issuer did not solicit the sale of the securities sold under those clauses;
- (d) the solicitation of the tender of securities to a securities exchange takeover bid or issuer bid;
- (e) a subscription for or purchase of an offered security pursuant to a prospectus distribution or restricted private placement.

PART 3 - PERMITTED ACTIVITIES AND EXEMPTIONS [Repealed]

3.1 [Repealed]

3.2 ~~Exemptions – Issuer-restricted Persons~~ [Repealed]

Section 2.2 does not apply to an issuer-restricted person in connection with,

~~(a) the exercise of an option, right, warrant, or a similar contractual arrangement held or entered into by the issuer-restricted person prior to the commencement of the issuer-restricted period;~~

~~(b) a bid or purchase of a restricted security pursuant to a Small Securityholder Selling and Purchase Arrangement made in accordance with National Instrument 32-101 or similar rules applicable to any marketplace on which the bid or purchase is entered or executed;~~

~~(c) an issuer bid described in sections 4.6 and 4.7 of National Instrument 62-104 *Take-Over Bids and Issuer Bids* if the issuer did not solicit the sale of the securities sold under those clauses;~~

~~(d) the solicitation of the tender of securities to a securities exchange take-over bid or issuer bid; or~~

~~(e) a subscription for or purchase of an offered security pursuant to a prospectus distribution or restricted private placement.~~

[Renumbered as section 2.4]

PART 4 - RESEARCH REPORTS

4.1 Compilations and Industry Research

Despite section 53 of the Act, during a dealer-restricted period, a dealer-restricted person may publish or disseminate any information, opinion, or recommendation relating to the issuer of a restricted security provided that such information, opinion or recommendation,

- (a) is contained in a publication which:
 - (i) is disseminated with reasonable regularity in the normal course of business of the dealer-restricted person, and
 - (ii) includes similar coverage in the form of information, opinions or recommendations with respect to a substantial number of companies in the issuer's industry or contains a comprehensive list of securities currently recommended by the dealer-restricted person; and
- (b) is given no materially greater space or prominence in such publication than that given to other securities or issuers.

4.2 Issuers of Highly-liquid Securities

Despite section 53 of the Act, during a dealer-restricted period, a dealer-restricted person may publish or disseminate any information, opinion, or recommendation relating to the issuer of a restricted security that is a highly-liquid security provided that such information, opinion, or recommendation is contained in a publication which is disseminated with reasonable regularity in the normal course of the business of the dealer-restricted person.

- 4.3 Where a dealer-restricted person is also an issuer-restricted person the exemptions in section 4.1 and 4.2 continue to be available to the dealer-restricted person.

Part 4.1 RESTRICTION ON PARTICIPATING IN A DISTRIBUTION WHERE SHORT SALES WERE MADE BEFORE PRICING

4.1.1 Restriction on purchases of short-sale restricted securities sold in a distribution where short sales were made before pricing

Except as provided in section 4.1.2, a person or company must not directly or indirectly purchase a short sale restricted security that is being sold in a distribution for cash if the person or company made a short sale of a security of the same class as the short-sale restricted security during the short sale restricted period.

4.1.2 Exceptions

- (1) A person or company may purchase the short sale restricted security described in section 4.1.1 in an open-market transaction on a marketplace in a distribution that is an at-the-market distribution.
- (2) A person or company may purchase the short sale restricted security described in section 4.1.1 in a distribution that is exempt from the prospectus requirement pursuant to section 2.42 of National Instrument 45-106 *Prospectus Exemptions*.
- (3) A person or company may purchase the short sale restricted security described in section 4.1.1 if the person or company made bona fide purchases of securities of the same class as the securities sold in the distribution and those purchases are:
 - (a) at least equivalent in quantity to the entire amount of the short-sale restricted securities sold short by the person or company during the short-sale restricted period;
 - (b) made in open-market transactions on a marketplace; and
 - (c) made no later than the business day prior to pricing.

(4) A person or company that sold short a restricted security during the short-sale restricted period may purchase a short-sale restricted security described in section 4.1.1 in a separate account, if decisions regarding securities transactions for each account are made separately and without coordination of trading or cooperation among or between the accounts.

PART 5 - EXEMPTION

5.1 Exemption

The Director may grant an exemption to this Rule, in whole or in part, subject to such conditions or restrictions as may be imposed in the exemption.

PART 6 [Lapsed]

Companion Policy 48-501 CP to Rule 48-501 Trading During Distributions, Formal Bids and Share Exchange Transactions

Part 1 — [Repealed]

Part 1.1 — Structure of the Rule

1.1.1 Rule 48-501 *Trading during Distributions, Formal Bids and Share Exchange Transactions* (the **Rule**) covers activities by persons and companies involved in distributions of securities. There are 3 different areas covered by the Rule:

- bids and purchases of securities of the same class as securities offered in a distribution, and solicitations of bids and purchases, other than solicitations to purchase the offered securities;
- publication of research reports by dealers involved in a distribution that cover the issuer of the offered securities; and
- restrictions on purchases of certain equity securities (other than units of exchange-traded funds) that are sold in a distribution where short sales were made in the period before pricing.

1.1.2 Fraud and Manipulation — Provisions against manipulation and fraud are found in securities legislation. Specifically, section 126.1 of the *Securities Act* (the **Act**) and Part 3 of National Instrument 23-101 *Trading Rules* (**NI 23-101**) prohibit manipulative or deceptive trading, including activities that may create misleading pricing or trading activity that is detrimental to investors and the integrity of the markets. Section 76 of the Act prohibits persons or companies in a special relationship with an issuer from trading the issuer's securities with knowledge of a material fact that has not been generally

disclosed. The Rule specifically prohibits certain trading activities in circumstances where there is heightened concern over the possibility of manipulation by those with an interest in the outcome of the distribution or transaction. This rule is in addition to existing rules prohibiting market manipulation and trading on the basis of non-public material information and does not in any way interfere with those existing rules.

Part 2 — Definitions and Interpretations

- 2.1** "connected security" — The definition of "connected security" in section 1.1 of the Rule includes, among other things, a security of the issuer of the offered security or another issuer that, according to the terms of the offered security, may *significantly determine* the value of the offered security. The Commission takes the view that, absent other mitigating factors, a connected security "significantly determines" the value of the offered security, if, in whole or in part, it accounts for more than 25% of the value of the offered security.
- 2.2** [Repealed]
- 2.3** End of "dealer-restricted period" and "issuer-restricted period" — distribution of securities and exercise of over-allotment option — The definitions of "dealer-restricted period" and "issuer-restricted period", with respect to a prospectus distribution and a "restricted private placement", refer to the end of the period as the date that the selling process ends and all stabilization arrangements relating to the offered security are terminated. Paragraph (a) of subsection 1.2(5) provides interpretation as to when the selling process is considered to end. As further clarification, the selling process is considered to end for a prospectus distribution when the receipt for the prospectus has been issued, the dealer has distributed all securities allocated to it and is no longer stabilizing, all selling efforts have ceased and the syndicate is broken. Selling efforts have ceased when the dealer is no longer making efforts to sell, and there is no intention to exercise an over-allotment option other than to cover the syndicate's short position. If the dealer or syndicate subsequently exercises an over-allotment option in an amount that exceeds the syndicate short position, the selling efforts would not be considered to have ceased. Securities allocated to a dealer that are held and transferred to their inventory account at the end of the distribution are considered distributed. Subsequent sales of such securities are secondary market transactions and should occur on a marketplace subject to any applicable exemptions (unless the subsequent sale transaction is a distribution by prospectus). To provide certainty around when the distribution has ended, appropriate steps should be taken to move the securities from the syndication account to the dealer's inventory account.
- 2.4** Pricing of a short sale restricted security described in section 4.1.1 occurs when the sale price for the short sale restricted security is determined and finalized. An offering that will be sold at an undetermined price to be established later (e.g. a certain percentage below that day's closing price on the principal market for the security) is not priced until the closing price is known.
- 2.5** "Open-market transactions" in this Rule are transactions made by entry of orders on a marketplace where buyers and sellers are matched by the marketplace's trading system. Trades where a dealer matches buyers and sellers or pairs orders with contra-side orders outside a marketplace and then reports the matched or paired orders to a marketplace as a cross are not open market transactions.

Part 3 — Restricted Persons

- 3.1** Meaning of "acting jointly or in concert" — The definitions of "dealer — restricted person" and "issuer-restricted person" in section 1.1 of the Rule include a person or company acting jointly or in concert with a person or company that is also a dealer-restricted person or an issuer-restricted person for a particular transaction. For the purposes of the Rule, "acting jointly or in concert" has a similar meaning to that phrase as defined in section 1.9 of National Instrument 62-104 *Take-Over Bids and Issuer Bids*, with necessary modifications. In the context of this Rule only, it is a question of fact whether a person or company is acting jointly or in concert with a dealer- or issuer-restricted person and, without limiting the generality of the foregoing, every person or company who, as a result of an agreement, commitment or understanding, whether formal or informal, with a dealer-restricted person or an issuer-restricted person, bids for or purchases a restricted security will be presumed to be acting jointly or in concert with such dealer-restricted person or issuer-restricted person.
- 3.2** Exclusion of "related party" — The definition of "dealer-restricted person" in clause 1.1(b) excludes a related entity where certain conditions are met. Subclause (i)(B) requires the dealer to obtain an annual assessment of the operation of the policies and procedures referred to in subclause (i)(A). In the Commission's view, this assessment may be conducted as part of the annual policy and procedure review of the supervision system as required by Policy 7.1 of the Universal Market Integrity Rules.

Part 4 — [Repealed]

Part 5 — Exemptions [Repealed]

~~5.1 — Fraud and Manipulation — Provisions against manipulation and fraud are found in securities legislation, specifically, Part 3 of National Instrument 23-101 — *Trading Rules* (NI 23-101) and section 126.1 of the *Securities Act* (Ontario) (when that provision comes into force). NI 23-101 prohibits manipulative or deceptive trading, including activities that may create misleading pricing or trading activity that is detrimental to investors and the integrity of the markets. The Rule specifically prohibits certain trading activities in circumstances where there is heightened concern over the possibility of manipulation by those with an interest in the outcome of the distribution or transaction. The Rule also provides certain exemptions to permit purchases and bids in situations where there is no, or a very low, possibility of manipulation. However, the Commission is of the view that notwithstanding that certain trading activities are permitted under the Rule these activities continue to be subject to the general provisions relating to manipulation and fraud found in securities legislation such that any activities carried out in accordance with the Rule must still meet the spirit of the general anti-manipulation and anti-fraud provisions.~~

5.2 [Repealed]

5.2.1 [Repealed]

5.3 [Repealed]

Part 6 — Research

6.1 Section 53 of the Act — Part 4 of the Rule provides exemptions from section 53 of the Act which prohibits providing research that in the Commission's view constitutes an act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of a trade prior to the filing and receipt of the preliminary prospectus and prospectus. The Commission is of the view that although sections 4.1 and 4.2 do permit dealer-restricted persons to disseminate research reports, this dissemination continues to be subject to the usual restrictions applicable to dealer-restricted persons when they are in possession of material inside information regarding the issuer.

6.2 Meaning of "reasonable regularity" — Sections 4.1 and 4.2 of the Rule provides circumstances where a dealer-restricted person may publish or disseminate information, an opinion, or a recommendation relating to the issuer of a restricted security. Clause 4.1(a) and section 4.2 require that the information, opinion or recommendation is contained in a publication which is disseminated with reasonable regularity in the normal course of business of the dealer-restricted person. The Commission considers that it is a question of fact whether a publication was disseminated "with reasonable regularity" and whether it was in the "normal course of business". A research publication would not likely be considered to have been published with reasonable regularity if it had not been published within the previous twelve month period or there had been no coverage of the issuer within the previous twelve month period. The nature and extent of the published information should also be consistent with prior publications and the dealer should not undertake new initiatives in the context of the distribution. For example, the inclusion of projections of issuers' earnings and revenues would likely only be permitted if they had previously been included on a regular basis. In considering whether it was "in the normal course of business", the Commission may consider the distribution channels. The research should be distributed through the dealer-restricted person's usual research distribution channels and should not be targeted or distributed specifically to prospective investors in the distribution as part of a marketing effort. However, the research may be distributed to a prospective investor if that investor was previously on the mailing list for the research publication.

6.3 Meaning of "similar coverage" and of "substantial number of companies" — Clause 4.1(b) of the Rule requires that the information, opinion or recommendation includes similar coverage in the form of information, opinions or recommendations with respect to a substantial number of issuers in the issuer's industry. This should not be interpreted as requiring that the opinions and recommendations relating to the issuer and other issuers in the issuer's industry must be similar or the same. In this context, in determining what is a "substantial number of issuers", reference should be made to the relevant industry. Generally, the Commission would consider a minimum of six issuers to be a sufficient number. However, where there are less than six issuers in an industry, then all issuers should be included in the research report. In any event the number of issuers should not be less than three.

Part 7 – PARTICIPATING IN A DISTRIBUTION WHERE SHORT SALES WERE MADE BEFORE PRICING

7.1 Section 4.1.1 of the Rule restricts purchases of certain equity securities (other than units of exchange-traded funds) that are sold in a distribution where short sales of the same class of securities were made in the period before pricing. The Rule does not prohibit or restrict short selling. The definition of "short sale" is broader than the corresponding definition in the Canadian Investment Regulatory Organization's Universal Market Integrity Rules. The term covers any sale of a security that the seller does not have title to or that is settled by, or intended to be settled by, delivery of borrowed securities, even if the seller owns or is otherwise deemed to own the securities sold. Section 4.1.1 of the Rule applies even if ultimately there is no delivery obligation on the part of the dealer entering the short sell order (on its own or a client's behalf) due to netting of trades by a clearing agency. Short sales made during the short sale restricted period trigger the restrictions in the Rule even if the date for settlement of the short sales is after the date of purchases made to close the short position.

- 7.2** Section 4.1.1 of the Rule applies to distributions of equity securities, other than units of exchange-traded funds, sold for cash. It is intended to apply to distributions conducted by a reporting issuer for capital raising purposes, for example, where a reporting issuer raises funds through a private placement of equity securities to accredited investors.
- 7.3** Section 4.1.1 of the Rule restricts purchases of certain equity securities where securities of the same class as the equity securities were sold short during the short sale restricted period. Accordingly, in an offering of convertible or exchangeable securities, a person or company that sells short the security underlying the convertible or exchangeable security is not prohibited from purchasing the convertible or exchangeable security under the offering.
- 7.4** Section 4.1.1 of the Rule does not apply to a distribution of equity securities that is exempt from the prospectus requirement pursuant to section 2.42 of NI 45-106. For example, where a warrant is exercised to acquire equity securities for cash, the distribution of such equity securities would not be subject to section 4.1.1.
- 7.5** For the purposes of Part 4.1 of the Rule, a distribution of a unit is a distribution of the securities comprising that unit. Accordingly, where securities comprising a unit are equity securities, short sales of any of those equity securities will be subject to the Rule.
- 7.6** For the purposes of Part 4.1 of the Rule, indirect purchasing of securities under a prospectus or private placement is also prohibited. Examples of indirect purchases include the short seller entering an agreement or arrangement with a person or company that has not sold short, pursuant to which that person or company buys securities in the distribution and transfers them to the short seller.

Appendix C**Excerpt from the Ontario Capital Markets Modernization Task Force Report¹⁰****26. Prohibit short selling in connection with prospectus offerings and private placements**

The existing prospectus system is generally working effectively for Canadian issuers. However, multiple stakeholders advised that short selling in connection with prospectus offerings and private placements is making pricing and execution of prospectus offerings more difficult. Since prospectus offerings and private placements are generally priced at a discount to the market price, market participants and investors who expect to purchase under the offering may seek to profit through aggressive short selling prior to the offering to depress the price of the offering...

In the U.S., the Securities and Exchange Commission has addressed some of these concerns through the prohibition in Rule 105 of Regulation M: Short Selling in Connection with a Public Offering... Stakeholders noted to the Taskforce that bought deals pre-arranged with hedge funds who are shorting the stock before the bought deal is announced ... harms the company, its shareholders and the uninformed investors trading against the short sellers.

Recommendation:

The Taskforce recommends that the OSC adopt a rule prohibiting market participants and investors who have previously sold short securities of the same type as offered under a prospectus or private placement, from acquiring securities under the prospectus or private placements.

There are current requirements that could potentially apply to short selling in advance of a prospectus offering or private placements, such as:

- Market participants and investors who have access to material undisclosed information concerning the offering would be precluded from short selling by the insider trading prohibition;
- The underwriter registration requirement may apply to market participants and investors who sell short in advance of an offering and fill their short position through the offering, since this is a form of indirect distribution;
- Insiders of the issuer who enter into securities lending arrangements in connection with short sales prior to an offering would be subject to reporting requirements; such transactions may also be limited by the insider trading prohibition and applicable blackout periods; and
- The prohibition on market manipulation may apply to conduct that artificially depresses the price of the securities.

These requirements, however, would require detailed and contextual analysis.

A simple requirement that does not require regulators to prove intent is preferable. This would prohibit market participants and investors who have a short position arising from a short sale in a security of the same type as offered under a prospectus or through a private placement (or fungible with such securities, such as a warrant, option or convertible or exchangeable security) from acquiring securities in an offering. It would create greater clarity for all market participants and be less complicated from both a conduct and compliance perspective. This recommendation should not apply to trading in exchange-traded funds. Exemptions for activities such as market-making by registered dealers should be considered.

¹⁰ <https://www.ontario.ca/document/capital-markets-modernization-taskforce-final-report-january-2021/22-regulation-competitive-advantage>

Appendix D

The Short Selling Regulatory Regime

Currently, the bulk of short selling rules are in CISO's UMIR. The Act does not define "short sale," however the Act references "short positions," requiring a short seller placing a sell order with an agent that is a registered dealer to inform the agent that the seller does not own the security.¹¹ The bulk of short selling rules were in the rulebooks of the listing exchanges, and later moved to CISO's UMIR, where they remain.¹² Over time, restrictions on the price at which a short sale could be made¹³ have been removed, although general anti-manipulation rules (both in UMIR and the Act) remain in place. CISO rules include requirements that short sell orders be marked as such, that CISO dealer members report trades that have not settled within 10 days following the date contemplated for settlement and that the dealers provide semi-monthly reports of short positions in each Canadian listed security. CISO also has the ability to designate individual securities as ineligible for short sales or subject to a requirement that arrangements be made to borrow securities prior to entry of a short sell order. As noted above, CISO has recently adopted a rule strengthening the obligation of CISO dealer members entering short sell orders on a marketplace to have a reasonable expectation to settle any resulting trade at the time the order is entered,¹⁴ and has proposed a requirement for dealers to close out fail-to-deliver positions in the event of settlement failure at a clearing agency.¹⁵

In addition, CISO's Investment Dealer and Partially Consolidated Rules establish margin and capital requirements for short positions.

In contrast, the bulk of short sale regulation in the United States is in SEC rules.

Recent Short Selling Initiatives

In 2019, a working group of the Canadian Securities Administrators (**CSA**) began to undertake research and analysis on activist short selling. This was done in the wake of an increased number of campaigns targeting Canadian issuers and concerns raised about the potential impact of activist short selling on Canadian markets. The research considered three specific areas: (i) the nature and extent of activist short selling activity in Canada, (ii) the Canadian and international regulatory framework; and (iii) issues related to enforcement and other remedial actions. The research found that there was not a disproportionate amount of activist short selling campaigns in Canada compared to the number of public companies, and that there was little evidence of activist short sellers having a negative impact on the markets.

In 2020, the CSA issued a Consultation Paper (**Consultation Paper**) describing its research and conclusions and listed a number of questions concerning activist short selling, and asking for examples of problematic conduct and what empirical data sources the CSA should consider.¹⁶ The CSA received a number of comments in response. None provided specific evidence of problematic activist short selling, but many expressed concerns about short selling in general and various aspects of short selling.¹⁷

In 2022, to address the concerns expressed in the comments on the Consultation Paper, the CSA and CISO issued a staff notice to provide an overview of the existing regulatory landscape surrounding short selling, give an update on current related initiatives and request feedback on areas for regulatory consideration.¹⁸ The following areas were discussed in the comment letters as possible matters for further study and analysis:

- Adopting pre-borrow or locate rules requiring dealers making or facilitating a short sale to have made arrangements to borrow the securities or to have a reasonable belief that the securities can be borrowed prior to the time of settlement;
- Shortening the timeline for reporting extended failed trades but not until the industry adjusts to T+1 settlement;
- Increasing transparency of short selling and short positions; and
- Introducing mandatory close-outs/buy-ins of short positions.

Coincident with these initiatives, the Taskforce Report was issued.

¹¹ Act, s. 48.

¹² UMIR was originally developed by CISO's predecessors, Market Regulation Services Inc. and the Investment Industry Regulatory Organization of Canada. For simplicity, this notice uses the term "CISO" to refer to CISO or its predecessor organization at the relevant time.

¹³ The so-called "tick test" requiring short sales to be executed at or above the last sale price of the security.

¹⁴ <https://www.ciso.ca/newsroom/publications/amendments-respecting-reasonable-expectation-settle-short-sale>.

¹⁵ <https://www.ciso.ca/rules-and-enforcement/consultations/proposed-amendments-respecting-mandatory-close-out-requirements>.

¹⁶ CSA Consultation Paper 25-403 Activist Short Selling (December 3, 2020).

¹⁷ CSA Staff Notice 25-206 Activist Short Selling Update (December 8, 2022).

¹⁸ Joint CSA and IIROC Staff Notice 23-329 Short Selling Canada (December 8, 2022)

Appendix E

Cost-Benefit Analysis

I. Current regulatory framework and rationale for intervention

As outlined in Joint CSA and IIROC – Staff Notice 23-329 *Short Selling in Canada*,¹⁹ short selling is subject to a well-developed framework comprising Canadian securities legislation and CIRO requirements. The current regulatory framework does not explicitly address the issue of closing short positions with securities issued from treasury, either in a prospectus offering or a private placement.

The Proposed Amendments are intended to address issues that have arisen in the specific context of short sales made immediately prior to pricing of a prospectus offering or private placement by persons or companies intending to purchase securities in the offering.

II. Proposed Amendments

The Proposed Amendments would prohibit anyone who sells short the same class of securities that will be issued in an offering, during the period commencing five days prior to the pricing of the offering and ending on pricing, from purchasing new issue securities in the offering, regardless of knowledge of the offering or intent with respect to the effect of the short sales on the market price of the securities. The rule is substantively similar to Rule 105 of the U.S. Securities and Exchange Commission (SEC).

The Proposed Amendments apply to distributions of equity securities for cash by reporting issuers in Ontario.

III. Stakeholders affected by the proposed Instrument/Rule

- (a) *Issuers* may have fewer potential buyers of securities in a financing as some potential buyers (short sellers) will be excluded or may choose not to participate in the financing. However, the Proposed Amendments will prohibit activity that may indirectly affect the price of an offering by a listed company by lowering the market price on which the price of the offering is based. If the market price is not so lowered, the distribution may be done at a higher price which would allow the issuer to raise more capital from the offering.
- (b) *Certain market participants involved in short selling* will not be able to participate in financings if they have sold short securities of the same class as those being distributed within five days of pricing, even if they were not aware of the financing at the time of the short sales, unless an exemption is available. The Proposed Amendments may make it more difficult to close short positions as there may not be sufficient stock available in the market at an acceptable price.
- (c) *Other Investors.* The Proposed Amendments will prohibit activity that may indirectly affect the price of an offering by a listed company by lowering the market price on which the price of the offering is based. If the market price is not so lowered, the distribution may be done at a higher price, resulting in less dilution for existing shareholders and higher capital obtained by the issuer, but at a higher cost for investors participating in the offering.
- (d) *Dealers* involved in offerings may have additional costs in monitoring participation by short sellers in offerings. Given that the rule is modeled on SEC Rule 105, the costs should be minimal for dealers that already have policies and procedures for compliance with that rule.

IV. Impact of the proposed amendments on each of the OSC mandate components

The OSC considers the impact of proposed rulemaking on the OSC's mandate to:

- provide protection to investors from unfair, improper or fraudulent practices,
- foster fair, efficient and competitive capital markets and confidence in the capital markets,
- foster capital formation, and
- contribute to the stability of the financial system and the reduction of systemic risk.

The Proposed Amendments may impact the competitive capital markets, efficiency and capital formation components of the OSC's mandate.

¹⁹ https://www.osc.ca/sites/default/files/2022-12/csa-iroc_20221208_23-329_short-selling.pdf

Unfair, improper or fraudulent practices – Short selling securities and purchasing securities in a public offering allows a short seller to avoid market risk and virtually guarantees profits. The proposed rule reduces the impact of short selling on the price of an equity security during a period when an issuer intends to raise capital through a prospectus offering or a private placement.

Investor protection – Short selling may affect the market price which could affect the pricing of a private placement or prospectus offering. The Proposed Amendments protect investors by reducing dilution costs that may result from low issuance prices for new equity securities due to activities by certain short sellers. They also eliminate the information asymmetries reflected in short sellers trading with knowledge of a financing that the issuer is not required to disclose and enable retail investors to manage their investment portfolios more efficiently.

The Proposed Amendments do not depend on knowledge of a financing or subjective or objective knowledge of the effects of the short sales.

Fair, efficient and competitive capital markets – Although short selling can play a role in the price discovery process which may promote market efficiency, short selling around the time of a new issue of equity securities (prospectus offering or private placement) with the intent of closing the short position with the new issue could have an effect on the price of an equity security and consequently of the financing. This rule amendment ensures that security prices are determined by the interplay of other market forces thereby promoting market efficiency.

The rule will ensure that offerings are priced based on market prices that have not been influenced by certain types of short selling, enhancing investor confidence.

Contribute to the stability of the financial system and the reduction of systemic risk– Significant levels of short selling prior to an offering can have significant impact on the market price of securities and in some instances cause offerings to be postponed temporarily, abandoned or made at significantly lower prices which do not reflect the market value of securities.²⁰ The proposed rule reduces the volatility in securities and increases investor confidence in the market.

V. *Anticipated costs and benefits*

a. Benefits to stakeholders

i. *Issuers*

Issuers may receive a higher issue price if the price is calculated by reference to the market price and there is no short selling in the five days before pricing by short sellers who wish to participate in an offering of the same class of securities sold short (i.e., activity that could affect the market price of the securities that will be the subject of an offering).

ii. *Certain market participants involved in short selling*

The Proposed Amendments provide short sellers with regulatory certainty by clarifying the OSC's expectations concerning the practice of closing short positions with securities acquired in a distribution.

iii. *Investors*

The Proposed Amendments will prohibit activity that may indirectly affect the price of an offering by a listed company by lowering the market price on which the price of the offering is based. If the market price is not so lowered, the distribution may be done at a higher price, resulting in less economic dilution for existing shareholders, although investors participating in the distribution may pay a higher price. Also, uninformed investors in the market will not trade against short sellers who intend to close their short positions with new issue equity securities thereby promoting fairness and a level playing field for investors.

iv. *Dealers*

The proposed rule provides dealers with regulatory certainty by clarifying the OSC's expectations concerning the practice of closing short positions with securities acquired in a distribution. This clarity will help dealers better meet their compliance obligations.

b. Costs to stakeholders

i. *Issuers*

Issuers may have fewer potential buyers of securities in a financing as some potential buyers (namely short sellers) will be excluded or may choose not to participate in the financing.

²⁰ [Proposed Rule: Short Selling in Connection With A Public Offering; Release No. 34-54888](#)

ii. Certain Market Participants Involved in Short Selling

Market participants making short sales during the relevant period will not be able to participate in financings, even if they were not aware of them, unless they close their short position that was opened within five days of pricing in advance of the financing as set out in the rule amendments or another exemption applies. The Proposed Amendments may make it more difficult to close short positions in the market at an acceptable price.

iii. Investors

- *Institutional investors and other traders* that engage in short selling will also need to have policies and procedures to ensure compliance with the Proposed Amendments.
- *Other investors* may experience a mixed impact. To the extent that certain short selling negatively affects the market price of the issuer's security, purchasers in an offering will pay a higher price, but existing shareholders will experience less economic dilution.

iv. Dealers

Dealers involved in offerings may have additional costs in monitoring participation by short sellers in offerings. We anticipate that these costs will not be significant. Given that the rule is modeled on SEC Rule 105, the costs should be minimal for dealers that already have policies and procedures for compliance with that rule.

VI. Summary comparison of costs and benefits

It is not possible to quantify the costs and benefits of the proposed amendments as there is not sufficient publicly available data or other data available to the Commission on participation by short sellers in distributions, also there is no requirement to keep records of this activity. In its release announcing the adoption of Rule 105 as a final rule, the SEC stated among other things, that they anticipated that Rule 105 would impose compliance costs in the form of increased surveillance for broker-dealers, but will provide a protective measure against abusive conduct that hampers the capital raising process and harms issuers.²¹ The SEC found that the major costs would be borne by traders and firms that derive significant revenue from closing pre-pricing short sales with securities sold in an offering.²² As such, staff expect that compliance costs will not be significant other than for firms engaging in the conduct prohibited by the Proposed Amendments to a significant degree.

VII. Description of alternatives considered

Staff considered maintaining the status quo. The Taskforce found that bought deals pre-arranged with short sellers who short before the bought deal is announced are problematic in Canadian markets, particularly within capital-intensive industries. This activity harms issuers, shareholders, and uninformed investors trading against short sellers. The status quo was not the preferred option.

²¹ SEC Release 34-50103 (July 28, 2004).

²² Ibid.