



THE MANITOBA
SECURITIES
COMMISSION

December 5, 2000

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Securities Commission
Nova Scotia Securities Commission

Mr. John Stevenson, Secretary
Ontario Securities Commission
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c/o Dean Murrison, Committee Chair
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**Re: Comment on Multilateral Instrument 72-101 –
Distributions outside of a local jurisdiction**

The Manitoba Securities Commission (the "Commission") welcomes the opportunity to comment on Multilateral Instrument 72-101 *Distributions Outside of the Local Jurisdiction* ("MI 72-101") and the Companion Policy to Multilateral Instrument 72-101 *Distributions Outside of the Local Jurisdiction* ("72-101CP"). The Commission believes that continued dialogic between securities regulators throughout Canada is an effective means of developing policy as well as providing the public with a better understanding of the numerous considerations which lead to the development of regulatory policy. The continuing dialogue between regulators is also indicative of the continuing cooperation between Canadian securities regulatory authorities.

The Commission offers no comments on Multilateral Instrument 72-101 *Distributions Outside of the Local Jurisdiction* ("MI 72-101"). In the Commission's view, MI 72-101 is clear and provides a useful exemption for very specific circumstances.

The Commission does have comments on 72-101CP which were prepared after consultation with the Securities Advisory Committee to the Commission. These comments reflect the views of the Commission and of the Securities Advisory Committee to the Commission.

Summary of Comments

72-101CP, part 2 deals with the characterization of a distribution, purportedly to make it clearer to issuers and their advisors as to how they may establish which jurisdiction is a local jurisdiction for the purposes of MI 72-101.

The Notice accompanying publication of MI 72-101 and 72-101CP requested comment on the connecting factors set out in section 2.2 as well as a proposed connecting factor being "a substantial market for the securities being distributed exists in the local jurisdiction".

In the view of the Commission, part 2 of 72-101CP does not assist a reader in any significant fashion and may in fact create confusion because of the overly expansive view asserted as to what may constitute connecting factors to a local jurisdiction. Further, the proposed connecting factor on which comment is invited is even less clear with the emergence of national markets in Canada.

The Commission is of the view that:

1. The connecting factors enumerated are not the most relevant factors for determining whether a distribution in the local jurisdiction has occurred;
2. The connecting factor that "A significant percentage of the outstanding securities of the class of securities being distributed are directly or indirectly held of record by residents of the local jurisdiction" is overly expansive and not generally accepted to be a determinative connecting factor at law;
3. The proposed connecting factor that "a substantial market for the securities being distributed exists in the local jurisdiction" is overly expansive and not generally accepted as a determinative connecting factor at law; and
4. The connecting factors enumerated create confusion and suggest that multiple local jurisdictions exist when as a matter of law that would not and should not be the case.

The Commission believes that as the connecting factors do not reflect the unanimous view of the securities regulatory authorities that may be adopting the instrument, any reference to them should be removed from 72-101CP.

Connecting Factors

The stated purpose of including the connecting factors in 72-101 CP is to provide guidance to issuers, however the list is prefaced by the statement "if one or more connecting factors to the local jurisdiction exist, such as the following:". This provides no real guidance. This suggests that any one factor might be enough to support jurisdiction. The list is also noted as not being determinative in all instances. Further, the listed connecting factors are not consistently applied amongst all jurisdictions. All that this list accomplishes is to make matters more uncertain.

The Commission agrees that items 1¹ and 4² listed in 2.2(1) are generally accepted by courts as being relevant connecting factors in most if not all cases for determining a real and substantial connection to a jurisdiction. The same does not apply to the factors noted below.

A significant percentage of the outstanding securities of the class of securities being distributed are directly or indirectly held of record by residents of the local jurisdiction

The assertion of jurisdiction where there are a substantial number of securities held in a jurisdiction has not been generally accepted at law. The Commission is concerned that the inclusion of this factor as stated does not accurately portray the law. The factor is included as a general statement as to when a connection exists. However, the exercise of jurisdiction on this basis will rarely support an extra-territorial exercise of powers by a securities regulatory authority unless there is likely to be harm to the public interest within their own province or territory in the particular circumstances. The Ontario Securities Commission, as an example, has in the past required there to be a transactional connection to Ontario to exercise its jurisdiction; even where there was a substantial number of security holders resident in Ontario, this was not sufficient to establish a transactional nexus³.

The general rule is of course that provincial legislation cannot operate outside of the province. The exception is where the pith and substance of the legislation is the protection of a right or interest within a province. Courts have accepted that a securities regulatory authority can exercise extraterritorial jurisdiction where the public interest is at stake. Where there is likely future harm to investors in the province or to the capital markets in the province or territory, the number of shareholders in the province can be considered in assessing what the harm might be. While there may be instances where such a factor might be considered by a Commission in exercising its public interest jurisdiction, it is hard to conceive why it would be a relevant factor in all but the most rare circumstances. Obviously, it cannot be said to be generally accepted as a connecting factor in all cases as the phrasing in 72-101CP suggests.

¹ The issuer's mind and management is primarily located in the local jurisdiction as evidenced by the head office of the issuer and by the residence of the directors and senior officers of the issuer.

² The operations of the issuer are principally conducted in the local jurisdiction.

³ *Re Asbestos* (1994) 4 C.C.L.S. 233 (OSC)

Where the connection is not substantial and a securities regulatory authority attempts to exert jurisdiction over an issuer outside of its province, the result is an unconstitutional exercise of jurisdiction.

As an example, a Manitoba issuer, X Corp is a reporting issuer equivalent in Manitoba only, has shares listed on the NASDAQ National Market and is otherwise a qualified issuer. X Corp has its head office in Manitoba and all of its operations within Manitoba. A pension plan with an Ontario situs has a 20% holding in X Corp. X Corp has no other connection to Ontario other than the one shareholder. X Corp. decides to make a distribution into the United States of the same class of securities as are held by the pension plan. According to 72-101CP, there would be 2 local jurisdictions: Manitoba and Ontario. There is no nexus with Ontario, however 72-101 CP suggests otherwise. This provides no certainty.

A substantial market for the securities being distributed exists in the local jurisdiction

The situation becomes even more confused with the proposed connecting factor "a substantial market for the securities being distributed exists in the local jurisdiction". Market is not a defined term. A market exists where there are buyers and sellers. One interpretation could thus be that where there are a substantial number of security holders there is a substantial market. The problems with this approach have been detailed above.

One method of bringing together people in a market is through an exchange. On what basis can the situs of an exchange constitute a connecting factor? In the Commission's view, the same factors described above apply in this instance as well. The exercise of jurisdiction on this basis should only occur where there is likely to be harm to the integrity of the capital market within the securities regulatory authority's own province or territory in the particular circumstances. As already noted, the Ontario Securities Commission has in the past required there to be a transactional connection to Ontario to exercise its jurisdiction; even where there was a substantial number of security holders resident in Ontario and a substantial market for the securities being distributed existed in the local jurisdiction (as the securities were listed on the TSE), this was not sufficient to establish a transactional nexus⁴.

The Montreal Exchange and Toronto Stock Exchange can both have issuers listed who have head offices and operations in provinces other than those where the exchange offices are located. It is not generally accepted that the location of the computers which effect trades will create a transactional nexus for an offering of securities outside of that province or territory.

Matters become even more confusing when the Canadian Venture Exchange ("CDNX") is considered. Where is the market? Currently CDNX is recognized as an exchange by the Alberta Securities Commission and the British Columbia Securities Commission. Orders exempting CDNX from recognition on specific conditions have been granted by the Ontario Securities Commission and the Commission. CDNX is also seeking a similar order from the Commission des valeurs mobilières du Québec. CDNX has a connection to each of these jurisdictions. Does the fact that CDNX has such a connection with these jurisdictions imply an issuer listed on CDNX offering securities will also have this connection regardless of where the securities may be offered? The Commission would suggest not, absent circumstances where a proposed offering will threaten the integrity of the capital markets within their jurisdiction.

Resolution

Ultimately the purpose behind a companion policy is to provide guidance and clarification where ambiguity exists in a rule. Likewise, a companion policy to a multilateral instrument should speak for all the parties adopting the multilateral instrument. It is the view of the Commission that the connecting factors as described and proposed fail to accomplish either of these purposes.

The Commission does not believe that NI 72-101 is ambiguous. The reference to a local jurisdiction, when interpreted using plain language, suggests that the usual connecting factors concerning location of head

⁴ *Re Asbestos* (1994) 4 C.C.L.S. 233 (OSC)

office, directing mind and control, or substantial operations in a province would apply. However, the connecting factors described in 72-101 CP create an ambiguity where none really exists.

Also of great concern is that the connecting factors are over expansive and suggests that the jurisdictions which are publishing NI 72-101 and 72-101CP support "long-arm regulation" when this is in fact not the case⁵. As detailed above, we do not believe the list of connecting factors accurately reflect the view of the courts. This over broad statement as to when jurisdiction may be taken will create confusion for filers and will impose filing obligations in jurisdictions where there is no real connection.

It should be remembered that NI72-101 is a relatively singular exemption which can only be relied upon in very specific circumstances. 72-101CP is meant to provide guidance on the operation of NI72-101. 72-101CP should not be used as a means of disseminating general views as to when jurisdiction might be supported, especially when the views of all jurisdictions are not the same and do not appear to be accepted generally at law. If the CSA believes it to be appropriate to develop a consistent position as to when jurisdiction might be founded, this is not the place for it.

The Commission does not support "long-arm regulation" and would not want to be seen as acquiescing to such a position. Failing the removal of the connecting factors from 72-101 CP, the Commission will not be publishing 72-101 CP in its current form.

Yours truly,



Don Murray
Chairman

DGM/kl

cc CSA Chairs

⁵ *Re Asbestos* (1999) CarswellOnt 454 (Ont. C.A.)