INVESTMENT DEALERS ASSOCIATION OF CANADA
ASSOCIATION CANADIENNE DES COURTIERS EN VALEURS MOBILIÈRES

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PRESIDENT AND CHIEF EXECUTIVE OFFICER

April 8, 2005

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Ontario Securities Commission
Saskatchewan Financial Services Commission
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Dear Mesdames/Sirs:

RE: Request for Comment on the proposed repeal and replacement of National Instrument 44-101 *Short Form Prospectus Distributions,* Form 44-101F1 *Short Form Prospectus* and Companion Policy 44-101CP *Short Form Prospectus Distributions*

A. Introduction

The Corporate Finance Committee ("we" or the "Committee") of the Investment Dealers Association of Canada (the "IDA") is pleased to respond to the Canadian Securities Administrators (the "CSA") notice and request for comment (the "Request") dated January 7, 2005 relating to the proposed amended and restated National Instrument 44-101, *Short Form Prospectus Distributions* ("Proposed NI 44-101"), amended and restated Form 44-101F1 *Short*

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Form Prospectus ("Proposed Form 1") and amended and restated Companion Policy 44-101CP *Short Form Prospectus Distributions* (collectively, the "Proposed Rule").

We commend the CSA and its staff for their efforts and strongly endorse the thrust of the proposed amendments reflected in the Proposed Rule to streamline the short form prospectus system, eliminate duplication and inconsistencies between the short form prospectus disclosure requirements and current continuous disclosure rules and expand issuer eligibility and access to the short form prospectus system. In our view, these developments would contribute to more efficient Canadian capital markets and thereby benefit Canadian investors and issuers.

B. Overview

Part I: Request for Comment on Proposed Qualification Criteria for Part 2 of Proposed NI 44-101

As discussed below, we support the proposed qualification criteria set out in Alternative B for Part 2 of Proposed NI 44-101 principally because it would afford broader access to the short form offering system in Canada than Alternative A without compromising investor protection. Since the last package of changes to the short form offering regime in 2000, there have been a number of significant regulatory and technical developments affecting the disclosure and quality of information available to the investing public, including the CSA's efforts to harmonize continuous disclosure requirements and to increase its focus and allocation of resources on continuous disclosure reviews and remedial disclosure. Accordingly, we recommend that the CSA adopt Alternative B for Proposed NI 44-101 and eliminate any seasoning requirement and quantitative (size) requirement from the issuer qualification criteria for the short form prospectus system. In the current Canadian regulatory and market environment, we do not believe that the absence of these two issuer eligibility criteria would diminish investor protection.

Part II: Request for Comment on Possible Further Changes in Prospectus Regulation

In broad terms, certain aspects of the concepts (the "Concepts") outlined in the latter portion of the Release appear to be potentially beneficial for the Canadian capital markets. Adoption of the Concepts, as set forth, however would involve a significant departure from the existing preliminary prospectus, regulatory review and receipted final prospectus process which has served the Canadian capital markets well for a considerable period of time. Accordingly, we urge the CSA in its further study and deliberations regarding the Concepts to ensure that any specific proposals resulting from the Concepts strike a practical public interest balance between market efficiency and investor protection.

In pursuing this balance, we believe it is relevant for the CSA to consider not only the indigenous needs of the Canadian capital markets but also to be aware of and sensitive to capital market developments in the United States and in other world markets. In our view, Canadian capital markets have more to gain from continuing to be a market leader embracing and reflecting

fundamental principles and market practices of well-regarded capital markets similar in operation to our Canadian capital markets, such as the capital markets in the United States.

It is our understanding that the United States Securities and Exchange Commission ("SEC") released (the " SEC Release") in November 2004 proposals embodying a major liberalization of the process for conducting registered securities offerings in the United States (*Proposed Rule: Securities Offering Reform;* Release Nos. 33-8501 and 34-506, November 17, 2004). In terms of the Concepts' outline of a final prospectus only offering process, we note that the SEC Release proposes limited "on-demand" shelf registration for a new category of very senior issuer, known as the "well-known seasoned issuer" or a "WKSI". The WKSI classification would include only those issuers that have a reporting history under the United States Exchange Act of 1934 and are widely followed in the marketplace. For "on-demand" equity shelf registration, a WKSI would have to be current for twelve months in filing periodic reports, otherwise be eligible to use Form S-3 or F-3 and have a public common equity float of $700 million (or for "on-demand" debt registration have sold $1 billion of SEC-registered debt in the past 3 years).

We are supportive in principle and encourage further study and development by the CSA of the Concepts' outline of an offering system whereby certain eligible issuers could access public capital based solely on the filing of a final prospectus. In our view, the principal benefits of such a system include more timely and certain market access for issuers, potentially at a lower cost. However, a final prospectus only offering system would represent a significant change to our traditional means of offering securities by prospectus. Accordingly, we recommend that the development of any such offering system be carefully engineered, and by way of initial impression, we suggest that any final prospectus only or similar offering system include appropriate issuer eligibility criteria, such as a one year seasoning requirement. We believe the need for adequate information about an issuer to be available and accessible for a period of time dictates such an eligibility requirement. As well, in light of the conceptual SEC approach as reflected in the SEC Release to "on-demand" registration eligibility being limited to only certain WKSI S-3 issuers, we strongly urge that consideration be given to devising a harmonized but tailored set of Canadianized eligibility requirements (including a minimum market cap threshold) for determining those issuers able to effect these types of offerings.

We are also concerned that a final prospectus only or an "on demand" offering regime and, to a lesser extent, the specific changes to the short form prospectus regime contemplated under either Alternative A or B for issuer eligibility criteria for Part 2 of Proposed NI 44-101 represent changes which would add significantly to the pressure and strain already being placed on the role and efficacy of the underwriter and director due diligence processes in connection with prospectus offerings of securities.

The conceptual role and utility of due diligence in the statutory prospectus offering process is well-recognized and accepted by market participants, Canadian and U.S. courts and securities regulators. Due diligence is vital to the prospectus offering process and contributes significantly

to fair and efficient markets. However, we are concerned that the statutory due diligence framework may no longer accommodate the practical realities of today's capital markets, particularly in the case of accelerated offerings. Due diligence must be available not only in theory but also in practice as a complete third party defence to a civil liability claim for materially misleading prospectus disclosure. The continuation of a civil liability regime for prospectus disclosure with respect to non-issuers, in market circumstances where due diligence and reliance defences cannot practically be established by non-issuer parties, such as underwriters, would at a minimum be inappropriate.

Several recent developments in the Canadian and American capital markets have raised serious issues regarding the practical utility or role of due diligence generally in today's capital markets (e.g. investor protection and capital market implications of Yield Advantage Income Trust offering structure, December 2004) or have significantly exacerbated liability concerns for underwriters [and others] in the context of prospectus offerings. Recent regulatory and Court decisions (*In The Matter Of YBM Magnex International Inc., Griffiths McBurney & Partners, First Marathon Securities Limited et al* (Ontario Securities Commission, June 27, 2003), *Douglas Kerr et al v. Danier Leather Inc., Irving Wortzman, Jeffery Wortzman and Bryan Tatoff* (Ontario Superior Court of Justice, May 7, 2004) and *In re WorldCom, Inc. Securities Litigation* (Southern District of New York, December 14, 2004)) have raised genuine concerns. These concerns relate both to the concept of due diligence generally as it pertains to underwriters, directors and officers as well as specific concerns relating to the practical ability of an underwriter defendant subject to a civil liability securities claim pertaining to misleading disclosure in a prospectus to invoke effectively the due diligence defence and the reliance on an expert defence notionally available under the statutory framework for underwritten prospectus offerings, including short form, shelf and other accelerated offerings. Indeed, the *WorldCom* decision has been identified by one United States legal commentator as "….the most important decision in at least 10 years on….due diligence obligations of underwriters and directors." (John C. Coffee Jr., "Corporate Securities", New York Law Journal, January 20, 2005). Within 100 days of the *WorldCom* decision being rendered, all seventeen major underwriter defendants had agreed to settle this securities class action and pay more than $6 billion. As well, all the directors of WorldCom (other than Mr. Bernard Ebbers) have agreed to personally pay a total of $25.5 million to settle the same action and the former directors' insurance will pay an additional $35 million. It has been reported that *WorldCom* defendants have now agreed to settlements which represent more than one-half of the total damages sought in the class action.

Both market participants and securities regulators have a role to play in striking an appropriate balance between the statutory civil liability provisions relating to prospectus offerings, including accelerated offerings, and the practical efficacy of the statutory due diligence defence and the reliance on an expert defence. In connection with the IDA's role, a sub-committee of this Committee has been established to develop non-exclusive due diligence guidelines and best practices for purposes of attempting to satisfy in the circumstances of any given offering the statutory due diligence defence and the reliance on an expert defence available with respect to prospectus offerings in Canada. This sub-committee has prepared draft guidelines and practices

and is consulting with organizations such as The Canadian Institute of Chartered Accountants with respect to the guidelines and practices and their possible role.

We strongly urge the CSA to examine and consider formally the current reality regarding the statutory due diligence defence and the reliance on an expert defence in the context of prospectus offerings, particularly accelerated offerings, in today's Canadian capital markets so as to ensure there is, not only in theory but also in substance, an appropriate balancing of gatekeeper responsibilities and potential civil liability. For instance, in today's markets what constitutes a "reasonable investigation" or "reasonable grounds" for a belief about the information in a prospectus for purposes of the affirmative due diligence defence and the reliance on an expert defence for a short form or shelf offering are exceedingly difficult questions to answer due, in part, to these developments. In the past, the SEC has periodically attempted to provide assistance on this issue (e.g. SEC Release No. 6335: *Circumstances Affecting the Determination of What Constitutes Reasonable Investigation and Reasonable Grounds for Belief Under Section 11 of the Securities Act,* August 6, 1981 and SEC's adoption of "safe-harbour" Rule 176 under the Securities Act of 1933). We understand similar "due diligence" consideration is being undertaken by certain U.S. capital market participants (See, "Scared Straight: Wall Street May Do More Due Diligence", The Wall Street Journal, April 7, 2005, page C1). We strongly believe that due diligence guidelines, best practices or safe-harbour provisions can and should be developed in a manner which both serves the public interest and the Canadian capital markets and enhances the current as well as future accelerated securities offering processes in Canada. In our respectful submission, it is incumbent upon market participants and regulators to act responsibly and address the current need for such due diligence guidelines, practices or provisions.

C. Discussion Regarding Certain Questions

Part I: Proposed Qualification Criteria – Alternative A or Alternative B for Part 2 of Proposed NI 44-101?

1. The changes reflected in Alternative A for Part 2 of Proposed NI 44-101 are necessary to update and harmonize Current NI 44-101 with the CD Rules and other regulatory developments. Alternative B, however, represents a significant broadening of access to the short form prospectus system.

(a) Do you believe this broadening of access is appropriate?

We believe the broadening of access contemplated by Alternative B for Part 2 of Proposed NI 44-101 is appropriate. Our belief is based on our assessment of the efficacy of the current disclosure regime applicable to Canadian reporting issuers. We believe that the timeliness and quality of

information provided by Canadian reporting issuers has improved generally over the past five years and provides a reasonable foundation for broadening issuer access to the short form offering regime without compromising investor protection.

(b) What are your views on the proposed qualification criteria set out as Alternative B?

We support and recommend the adoption of the qualification criteria set out as Alternative B for Part 2 of Proposed NI 44-101. For the reasons set forth above, we submit that neither a seasoning requirement nor a quantitative (size) requirement is necessary in the public interest in terms of qualification criteria for access to the short form prospectus system. We do note explicitly that our level of comfort with Alternative B is significantly influenced by the maintenance of a Canadian listing requirement for issuer eligibility for the short form prospectus system and our understanding based on your comments in the Request that the adoption of either Alternative A or B would not adversely affect the ability of Canadian issuers to continue to access and use the multi-jurisdictional disclosure system ("MJDS") with the SEC. We believe that it is imperative that the Proposed Rule not adversely affect the ability of Canadian reporting issuers to access and use the MJDS.

Other Aspects of the Proposed Rule

2. (a) Is the requirement to deliver an undertaking of the issuer to file the periodic and timely disclosure of applicable credit supporters under paragraph 4.3(b)2 of Proposed NI 44-101 an appropriate response to our concern about the lack of adequate credit supporter disclosure in the secondary market?

We support in principle the objective of making available periodic and timely disclosure of the credit supporter in the subject circumstances. However, consideration might be given to the following possible modifications: (i) could the undertaking come from either the issuer or the credit supporter? and (ii) could the undertaking be limited to periodic and timely disclosure required by applicable home jurisdiction corporate/securities laws?

4. (a) Does Item 15 of Proposed Form 1 accomplish its objective, which is to ensure disclosure of any ownership interests that would be perceived as creating a potential conflict of interest on the part of an expert?

Item 15 of Proposed Form 1 contains a detailed set of requirements with significant exceptions nestled deep in the wording of subsections 15.2(4) and (5). While the principle underlying Item 15 may be meritorious, we are concerned that the prolixity of Item 15 may compromise the objective.

(b) If not, what changes should be made to the parameters?

We would suggest consideration be given to including as a line item requirement of Proposed Form 1 affirmative issuer disclosure confirming, or explaining otherwise, that each person or company described in paragraphs 15.1(a) and (b) has been determined by the board of directors, or similar body, of the issuer to be independent of the issuer and its management. The concept of "independence" underlying this requirement would include consideration of any registered or beneficial interests, direct or indirect, in any securities or other property of the issuer, its associate and affiliates.

Part II: Request for Comment on Possible Further Changes in Prospectus Regulation

5. (a) Do you believe that issuers, investors or other market participants would benefit from the elimination of preliminary prospectuses and prospectus review?

While we believe that issuers, investors and other market participants could in certain circumstances benefit from the elimination of preliminary prospectuses and prospectus review, we are concerned that the elimination of preliminary prospectuses and prospectus review could undermine the integrity of the public securities offering system in Canada and create additional strain on a statutory due diligence scheme which we are concerned may no longer be aligned with market reality in the context of accelerated offerings.

(b) What are the principal benefits of such a system?

The principal benefit of such a system would be expedited access to the capital markets.

(c) Are there any potential drawbacks?

This approach would require additional formal reliance on the existing disclosure profile of eligible issuer. Additionally, we are concerned that it may forfeit some of the long-standing market integrity created by the preliminary and final prospectus receipt regime which has served Canadian capital markets well for decades. See also (d) and (e) below.

(d) Are you concerned about a lack of regulatory review in the context of a prospectus offering?

From a marketplace perspective, we are concerned about a lack of regulatory review in the context of a prospectus offering. The existing and predecessor Canadian prospectus offering regimes have created a significant degree of market integrity and afforded market participants efficient and fair markets and the opportunity generally to perform their obligations and discharge their legal responsibilities. However, recent developments suggest that certain aspects of the current prospectus offering regime, such as the practical availability of certain underwriter and director defences, may no longer be in alignment with the theoretical statutory model and, accordingly, we strongly recommend that any final prospectus only or "on-demand" registration system be made available only to seasoned adequately-capitalized reporting issuers. For instance, we would strongly recommend that the CSA study carefully the SEC Release's WKSI concept and, at a minimum, develop a "made in Canada" equivalent equity float test for any such super-accelerated prospectus offering regime.

(e) Are you concerned that expediting the prospectus filing would put undue pressure on the due diligence process?

As discussed above, we are concerned that expediting the prospectus filing process would exacerbate the significant existing market pressure on the due diligence process.

6. (a) If we eliminate the preliminary prospectus and prospectus review as contemplated above, do you think we should impose more onerous restrictions on this offering system, given the lack of regulatory review at the time of the offering?

Yes.

Such restrictions could include additional qualification criteria and restrictions, such as the following:

(i) a one year seasoning requirement to ensure eligible issuers have filed required CD for a minimum period and to allow for regulators to review such CD.

Yes.

Such restrictions could include additional qualification criteria and restrictions, such as the following:

(ii) a prohibition from offering securities if the regulator has identified significant unresolved issues relating to the issuer's CD.

We agree only if the identified significant unresolved issues would currently result in the issuance of a cease trade order under applicable securities legislation. Otherwise, we believe disclosure is a preferable alternative to regulatory prohibition.

Such restrictions could include additional qualification criteria and restrictions, such as the following:

(iii) a restriction on types of eligible securities to disallow securities which may not be supported by the issuer's CD.

We agree that issuer eligibility should be aligned generally with different types of securities. For example, eligibility to issue debt should not necessarily qualify an issuer to issue equity.

7. Do you believe that a marketing regime triggered on the issuance of a press release or other public notice announcing a proposed offering is workable and would be utilized by issuers and dealers? If so, should the press release or public notice be required on "the issuer forming reasonable expectation that an offering will proceed" or on some other event?

A marketing regime involving a public notification of a forthcoming offering through a media release or term sheet, in tandem with reliance on the continuous disclosure regime, still leaves potential for abuse in the offering process. The decision of the issuer to offer treasury shares is typically material undisclosed information as market prices will likely be affected significantly by an announcement to proceed with an offering of new equity securities.

The issuance of a press release announcing a forthcoming securities offering once the issuer forms "a reasonable expectation" to proceed with an offering is a necessary requirement, but is not sufficient to prevent potential abuse in the marketplace. At a minimum, regulators should remind investors and dealers that upon receipt of material undisclosed information, such as information about a forthcoming offering, the dealer and investor become "a person or company in a special relationship with the reporting issuer", and as such is ineligible to purchase or sell securities of the reporting issuer as long as the material fact or material change has not been generally disclosed.

Despite statutory restrictions on trading based on material non-public information, the IDA has imposed specific pre-marketing restrictions in bought deal offerings to provide an added safeguard to prevent trading abuse in secondary markets. Whether or not these pre-marketing restrictions remain necessary, the CSA could in any event permit the elimination of the requirement for underwriters to provide written certification for compliance with the pre-marketing rules that have been in place since the early 1990's.

The Committee respectfully requests CSA staff to consider carefully the foregoing comments outlined in this letter. Representatives of the Committee would be pleased to discuss our comments in greater detail with CSA staff. Please do not hesitate to contact Ian Russell, Senior Vice-President, Industry Relations & Representation, at (416) 364-6133.

Yours sincerely,

Joseph J. Oliver