sifma

Invested in America

October 5, 2016

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, Ontario M5H 3S8
Fax: 416-593-2318
Email: comments@osc.gov.on.ca

VIA EMAIL

Ladies and Gentlemen:

OSC Notice and Request for Comment – Proposed OSC Rule 72-503 – Distributions Outside of Canada and CP 72-503CP to OSC Rule 72-503 Distributions Outside of Canada

The Securities Industry and Financial Markets Association, or SIFMA, appreciates the opportunity to comment on Proposed OSC Rule 72-503 *Distributions Outside of Canada* ("Rule 72-503") and Proposed Companion Policy 72-503CP (the "Companion Policy," and collectively with Rule 72-503, the "Proposed Rule"). SIFMA supports many aspects of the Proposed Rule and strongly supports the stated goal of the Ontario Securities Commission (the "Commission") of "remov[ing] uncertainty regarding the extent of the application of the prospectus and registration requirements in … cross border transactions."

SIFMA is the voice of the securities industry in the United States. One of our mandates is to advocate for effective and efficient capital markets. We represent the U.S. broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the U.S. capital markets, raising over U.S. $2.5 trillion for businesses and municipalities in the United States, serving clients with over U.S. $20 trillion in assets and managing more than U.S. $67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). Our members include the largest and most prestigious investment banks in the United States.

SIFMA respectfully submits the following comments on the Proposed Rule.

1. *SIFMA strongly supports preservation of the policy of the Interpretation Note to determine the applicability of Ontario prospectus requirements but recommends adding commentary on the policy goals of the Proposed Rule.*

The Commission states in the Companion Policy that: "…[it] does not interpret the prospectus requirement as applying to a distribution of securities outside of Canada … provided that the issuer, underwriters and other participants in the offering take reasonable steps to ensure that the securities come to rest outside of Canada and are not redistributed back into Canada." This interpretive language is a helpful statement of the jurisdictional scope of the prospectus requirement of Ontario securities legislation. Further, it preserves the principle underlying Interpretation Note 1 *Distributions of Securities Outside Ontario* (the "Interpretation Note") as a safe harbour position for issuers and underwriters that sell securities abroad but that cannot easily fit into the prospectus exemptions in the Proposed Rule. For example, SIFMA understands that this guidance may permit an Ontario incorporated issuer to conclude that a primarily U.S. 144A offering of U.S. dollar denominated debt securities may be made without putting a Canadian restrictive legend on the global note or otherwise imposing Canadian resale restrictions, on the basis that the risk of flow back into Canada is minimal. SIFMA strongly supports and appreciates that the Commission has included this guidance in the Companion Policy. SIFMA agrees that the reasonable steps outlined in Part 3 "The Operation of the Principle" in the Interpretation Note are no longer workable given changes in market practice between 1983 and 2016.

The Interpretation Note discussed connecting factors to Ontario that are relevant to determine the nature of restrictions to be put in place to ensure the securities come to rest outside of Canada. These include:

- The class and nature of the securities being distributed;
- The attractiveness to Ontario investors of such securities;
- The likelihood that, absent such restrictions or precautions, the securities would come to rest in Ontario;
- Whether a market for the class of securities being distributed or any other securities of the issuer already exists in Ontario;
- The likelihood of the development in the future of a market in Ontario for the securities being distributed;

- The way in which the distribution is proposed to be effected;

- The relationship between the capital markets of Ontario and the jurisdictions in which the securities are being distributed and the ease of access of one to the other;

- Whether or not the underwriters and other participants in the distribution are, or are affiliated with, investment dealers that conduct substantial activities in Ontario; and

- The presence of the issuer in Ontario (whether through the conduct of business in Ontario, a number of shareholders resident in Ontario, the issuer being closely followed by Ontario investors or otherwise).

Without guidance in the Companion Policy on which connecting factors create a risk of flowback it becomes difficult to determine in what circumstances reasonable steps should be taken and what those reasonable steps would be in light of 2016 market practice. Further, it is difficult for consistent market practice to develop in circumstances that are less clear than a primarily U.S. 144A offering of U.S. dollar debt. If the Proposed Rule does not enable clear market practice to develop, it will not have achieved its goal of greater certainty and Canadian issuers and, ultimately investors, will pay the price in increased offering costs.

Rule 72-503's new prospectus exemptions appear intentionally not to focus upon whether securities of Ontario issuers distributed abroad will flow back into Canadian markets, except where the issuer is not a Canadian reporting issuer and the securities are not being distributed in the U.S. or a "designated foreign jurisdiction." It therefore seems that the policy goal of the Interpretation Note (that is, preventing "flow back") is not the policy goal underpinning the Proposed Rule. The principle underpinning Rule 72-503's prospectus exemptions seems instead to be related to the availability of sufficient acceptable disclosure that may act as a substitute for a Canadian prospectus. That is, if an issuer is filing Canadian continuous disclosure documents or an offering document in the U.S. or a designated foreign jurisdiction, the implicit presumption appears to be that such documents will sufficiently protect any Canadian "flow back" purchasers, such that restrictions on sales back into Canada need not be imposed. SIFMA believes this principle is sound. Investors' access to issuer information in 2016 has increased substantially since 1983 when the Interpretation Note was published.

If the availability of public information about the issuer removes the concern about flowback, SIFMA submits the bolded and italicized portion of the following Companion Policy guidance should be deleted in the final version of the Proposed Rule:

> "Nothing in [Rule 72-503] prohibits or restricts the resale of the securities distributed under an exemption from the prospectus requirement in section 2.1, 2.2 or 2.3 of the [Proposed Rule]. ***Nevertheless, the Commission expects that the issuer, underwriters and other participants in the offering will have taken reasonable steps to ensure that the securities come to rest outside of Canada and are not redistributed back into Canada in a manner that constitutes an indirect distribution in Ontario.***" (Emphasis added).

The highlighted language is problematic because it suggests that Canadian resale restrictions may be required to be imposed on securities that Rule 72-503 makes freely tradeable.

Further, it creates doubt regarding what steps must be taken to permit reliance on the four prospectus exemptions introduced by the Proposed Rule, rather than alleviate the uncertainty currently inherent in the application of the Interpretation Note.

The highlighted language directly contradicts the express provisions of Rule 72-503 which provide that securities distributed abroad pursuant to section 2.1 (the "Foreign Public Offering Exemption"), section 2.2 (the "Concurrent Canadian Prospectus Exemption") or section 2.3 (the "Canadian Reporting Issuer Exemption") of the Proposed Rule are freely tradeable.

SIFMA therefore respectfully suggests that the highlighted sentence be deleted in the final version of the Companion Policy.

2. The list of "designated foreign jurisdictions" should be expanded.

Rule 72-503's list of "designated foreign jurisdictions" is drawn from National Instrument 71-102 *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers* ("NI 71-102") and is limited to Australia, France, Germany, Hong Kong, Italy, Japan, Mexico, the Netherlands, New Zealand, Singapore, South Africa, Spain, Sweden, Switzerland and the United Kingdom. Given Rule 72-503's policy rationale of accepting roughly equivalent foreign offering disclosures, the list of "designated foreign jurisdictions" appears to be underinclusive, which may be due to the fact that the list has not been updated since 2004 and was itself based on the list in Draft National Policy Statement 53 *Foreign Issuer Prospectus and Continuous Disclosure System* ("Draft NPS 53") published August 20, 1993 but never finalized. The list appears to exclude many E.U. member and other countries that one might expect would have prospectus offering disclosure regimes that are appropriately equivalent to the Canadian regime.

SIFMA recommends that the Commission consider adding to the countries that should be included in the list of "designated foreign jurisdictions." The foreign jurisdictions where the "designated exchanges" listed in the blanket orders providing exemptions from Multilateral Instrument 51-105 *Issuers Quoted in the U.S. Over-the-counter Markets* are located may be a useful starting point. At a minimum, all E.U. member countries, Switzerland, Norway and South Korea should be added to the list. Additional guidance in the Companion Policy regarding the rationale for the choice of jurisdictions that are "designated foreign jurisdictions" may also be helpful.

We discuss the "designated foreign jurisdiction" concept as used in the context of the new dealer registration exemption in section 3.1 of the Proposed Rule in item 5, below.

3. *The Companion Policy guidance that suggests that foreign purchasers may be entitled to statutory withdrawal and other rights under Ontario law in certain circumstances should be deleted.*

The Companion Policy contains the following guidance:

"If an issuer or selling securityholder files a prospectus to qualify a concurrent distribution to a person or company in Ontario, the issuer may choose to file a prospectus in Ontario to qualify the distribution of securities to an investor outside of Canada. ***Any prospectus filed in such circumstances should therefore clearly state whether or not it also qualifies the distribution of securities to an investor outside of Canada, recognizing that purchasers of Ontario prospectus-qualified securities may be entitled to certain rights and investor protections under the Act even if the investor is outside of Canada***."

The highlighted phrase seems to say that statutory withdrawal rights under Section 71 of the *Securities Act* (Ontario) (the "Act") and the statutory cause of action for a misrepresentation in a prospectus under Section 130 of the Act may be extended to foreign investors simply by, perhaps inadvertently, including the securities to be offered in the foreign jurisdiction in the number of securities qualified by the Ontario prospectus.

This position would have significant implications. The guidance could be taken to mean that including the securities to be offered in the United States in the number of securities qualified by a Canadian "southbound" MJDS prospectus for a cross-border offering has the legal effect of extending Ontario's statutory two-day withdrawal right to investors in the U.S. public offering. This result would be unworkable from a practical perspective, is out of sync with both U.S. disclosure requirements under the MJDS and the U.S. markets' settled understanding that Canadian statutory rights are not available to U.S.

purchasers, and could cause significant disruption to the manner in which (and whether) MJDS cross-border offerings are undertaken.

Part I, Item 1 of the SEC's Form F-10, which is the primary SEC form used by Canadian issuers for southbound MJDS offerings, provides that the "prospectus used in the United States need not contain any disclosure applicable solely to Canadian offerees or purchasers that would not be material to offerees or purchasers in the United States, ***including, without limitation … any description of offerees' or purchasers' statutory rights under applicable Canadian, provincial or territorial securities legislation (except to the extent such rights are available to the U.S. offerees or purchasers) …***"(emphasis added). The disclosure regarding statutory rights available under applicable Canadian law is routinely and intentionally deleted in the version of the prospectus that is filed with the SEC and delivered to U.S. purchasers. This is a clear and unambiguous indication that Canadian issuers and U.S. market participants do not believe and do not intend that Canadian statutory rights are available to U.S. purchasers in MJDS offerings, even if the Canadian prospectus qualifies the distribution of the securities sold in the United States.

Therefore, extending statutory rights under Ontario law to U.S. purchasers of securities cannot be the correct result. If U.S. investors were entitled to all of the statutory rights afforded to Ontario purchasers under the Ontario prospectus, the U.S. dealer selling the Ontario prospectus qualified securities in the United States would be subject to an obligation to deliver the Ontario prospectus to each U.S. purchaser together with the U.S. prospectus so each U.S. purchaser would effectively purchase the securities under two prospectuses. If no Ontario prospectus were delivered to the U.S. investor, the 2-day withdrawal right would be perpetual since the right of withdrawal commences upon delivery of the final prospectus. This position would run contrary to decades of market practice and wreak havoc among Canadian issuers and dealers who would now face the risk of ongoing contingent exposure to the exercise of Canadian withdrawal rights by U.S. investors who participated in past offerings.

With respect to foreign private placements that are made concurrently with a Canadian prospectus offering, SIFMA believes that the prevailing practice is to qualify under the Canadian prospectus the securities that may be sold via a foreign private placement (for example, in the U.S. as a Rule 144A tranche to "qualified institutional buyers"). This practice developed because the final prospectus must be filed prior to the time actual sales can be confirmed (since no actual trades can take place until after the final prospectus has been receipted). It is impossible to determine with certainty prior to launching a deal what proportion of demand will be generated from Canadian purchasers versus foreign purchasers. The guidance above therefore casts considerable uncertainty over the legal effect of structuring foreign private placements (and, as described above, U.S. public offerings under the MJDS) in the manner that they are currently structured, and we respectfully submit it ought to be deleted.

Moreover, foreign purchasers located in foreign jurisdictions with comparable disclosure requirements do not require the protection of Ontario securities law in addition to those of their home country. Further, it is not clear that the Ontario legislature has the constitutional authority to extend such protection to purchasers outside Ontario. Section 1.1 of the Act states the purposes of the Act are: (a) to provide protection to investors from unfair, improper or fraudulent practices and (b) to foster efficient capital markets and confidence in capital markets. Absent exceptional circumstances, the jurisdictional scope of this provision must be protection of Ontario investors and confidence in Ontario markets, not U.S. or other foreign markets. The Companion Policy expressly recognizes this by stating: "The Commission takes the view that an investor outside of Canada will ordinarily expect to rely on the prospectus, registration statement or similar protections of the securities laws of the foreign jurisdiction in which the investor is located. The Commission recognizes that compliance with the prospectus requirement or conditions of a prospectus exemption may be unnecessarily duplicative of these protections and will generally not be necessary to fulfill the purposes of the Act." In the United States, for example, a purchaser in a private placement under Rule 144A would have remedies under the anti-fraud provisions of the U.S. federal securities laws including under Rule 10b-5 under the Securities Exchange Act of 1934, as amended. Further, the Companion Policy provides that the Commission's goal is to ensure that the securities come to rest outside of Canada and are not redistributed back into Canada. This is an acknowledgement that the Commission's mandate is the protection of Ontario investors not foreign investors.

4. *The Restricted Resale Exemption should explicitly permit sales over exchanges or markets outside of Canada*

Section 2.4(1) of the Proposed Rule provides that "[t]he prospectus requirement does not apply to a distribution of securities to a person or company outside of Canada if, in connection with the distribution, the issuer of those securities or the selling securityholder has complied with the securities law requirements of the jurisdiction outside of Canada." Section 2.4(2) of the Proposed Rule provides that "[t]he first trade of securities distributed under the exemption in subsection (1) is a distribution unless (a) the trade is to a person or company outside of Canada; or … [t]he issuer of the securities is and has been a reporting issuer in a jurisdiction of Canada for the four months immediately preceding the trade [and] [a]t least four months have elapsed from the distribution date."

SIFMA respectfully submits that Section 2.4(2)(a) should be revised to provide that the first trade of securities distributed under 2.4(1) will not be a deemed a distribution if made to a person or company outside of Canada ***or through an exchange or a market located outside of Canada***.

This modification would (i) reflect the reality that most purchasers on foreign exchanges may be presumed to be outside of Canada and (ii) align the wording of section 2.4 of the Proposed Rule with the exemption in section 2.14 of National Instrument 45-102 *Resale of Securities* ("NI 45-102").

It is interesting to note that the Restricted Resale Exemption is conditioned on the issuer or selling securityholder complying with the laws of the foreign jurisdiction. There is no such qualification on the resale exemption in Section 2.14 of NI 45-102. SIFMA respectfully submits that foreign securities regulators should regulate foreign markets and the condition in section 2.4(1) of the Proposed Rule creates the unnecessary duplication of regulation (by requiring compliance with foreign law as a condition of compliance with Ontario law) that the Companion Policy states the Proposed Rule seeks to avoid. This comment applies equally to the Concurrent Canadian Prospectus Exemption and the Canadian Reporting Issuer Exemption, each of which is also conditioned on compliance with foreign law.

5. *The new dealer registration exemption raises a concern of extraterritorial regulation of foreign dealers selling securities of Ontario issuers abroad. Its interaction with section 8.18(2)(a) of* National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations should be clarified.*

The Commission's rationale for the new dealer and underwriter exemption in section 3.1 of the Proposed Rule is that it will provide "greater certainty to market participants" and will "help address the challenges that foreign dealers and underwriters may face in determining whether the dealer and underwriter registration requirement applies to their activities." SIFMA's view, however, is that these are not challenges that foreign dealers face with any regularity, if at all. In short, this is not a problem that needs to be solved and the new dealer registration exemption is, if anything, *harmful* to market certainty, in that it calls into question, whether a foreign dealer distributing securities of an Ontario issuer in a foreign jurisdiction to foreign investors *may be engaged in the business of trading in securities in Ontario, or acting as an underwriter in Ontario*. We believe that is clearly not the case.

SIFMA recommends the exemption in Section 3.1 of the Proposed Rule be deleted as unnecessary. If the Commission determines to include the new dealer registration exemption in the final version of the Proposed Rule, we believe some changes should be made.

The Proposed Rule's new dealer registration exemption should extend to dealers that are registered in any foreign country, not just in the United States or in a "designated foreign jurisdiction", just as the international dealer exemption in Section 8.18 of National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("NI 31-103") is not limited to dealers in any specified countries.

The Proposed Rule's new dealer registration exemption would only apply to dealers that, among other things, are (i) registered in the U.S. or a "designated foreign jurisdiction," and (ii) in compliance with "all applicable dealer registration requirements and other broker-dealer regulatory requirements" of the foreign jurisdiction applicable in connection with the distribution. There are at least three issues with these requirements. First, as discussed above in the context of the offshore offering exemptions, the list of "designated foreign jurisdictions" is problematic. A Brazilian dealer (for example) offering securities of an Ontario incorporated issuer to investors in Brazil would not be able to avail itself of the exemption, because Brazil is not included in the list of "designated foreign jurisdictions." But it is not clear why this should be so. As previously discussed, the list of "designated foreign jurisdictions" was developed for Draft NPS 53 and NI 71-102 and identifies countries that (in 2004) had continuous disclosure regimes that the Canadian Securities Administrators deemed sufficiently equivalent to Canada's continuous disclosure regime such that an issuer's foreign reports could be filed to satisfy its Canadian continuous disclosure obligations. It is not clear that, because the Commission viewed those countries' continuous disclosure regimes as adequate for Canadian purposes in 1993 or 2004, such countries' *securities dealer regulations* are roughly equivalent to Canadian dealer regulations in 2016 (or that excluded countries' securities dealer regulations are somehow lacking). This contrasts with the international dealer exemption in section 8.18 of NI 31-103, where a dealer registered in any foreign jurisdiction is considered eligible to trade foreign securities (of issuers from any other country) with permitted clients in Ontario. Moreover, it is not clear why the Commission ought to care about any notion of equivalence in this context, since the new dealer registration exemption only applies to activities outside of Ontario involving non-Ontario investors. Therefore, we believe that the Proposed Rule's new dealer registration exemption should extend to dealers that are registered in any foreign country, not just in the U.S. or in a "designated foreign jurisdiction", just as the international dealer exemption in Section 8.18 of NI 31-103 is not limited to specified countries.

The second issue is that the exemption is conditioned on compliance with "***all*** applicable dealer … requirements." For example, a U.S. registered broker-dealer offering securities of an Ontario incorporated issuer to investors in the United States would not be permitted to rely on the exemption unless it is in compliance with "***all*** applicable conduct and other regulatory requirements of U.S. federal and state securities law and FINRA rules in connection with the distribution." This means that any minor "foot fault" with respect to, for example, state level "blue sky" requirements or FINRA regulations even so minor as a late filing, would mean that the exemption would not be available to the U.S. broker-dealer, which could by implication result in a contravention of the requirement to be registered in Ontario as a dealer. A dealer that is sufficiently in compliance with the requirements of its foreign jurisdiction, such that the regulator of the foreign jurisdiction permits the dealer to continue to carry on business, should not be prohibited from doing underwriting business in the foreign jurisdiction for Ontario issuers.

A third issue with the new dealer registration exemption is that is casts uncertainty over the operation of the international dealer exemption. Section 8.18(2)(a) of NI 31-103 provides that an international dealer relying on the exemption in such section may participate in "any activity, other than a sale of a security, that is reasonably necessary to facilitate a distribution of securities that are offered primarily in a foreign jurisdiction."

Rather than include the new dealer registration exemption in the final version of the Proposed Rules, a better approach would be for the Commission to clearly state in published guidance that Ontario's dealer and underwriter registration requirements do not apply to distributions of securities by foreign dealers to investors located in foreign jurisdictions. To the extent a foreign dealer is engaged in conduct in a foreign jurisdiction that may have deleterious consequences for the Ontario capital markets (e.g., selling securities abroad of a fraudulent Ontario incorporated issuer) the Commission may invoke its public interest jurisdiction.

6. *SIFMA is concerned about the new reporting obligations to be imposed by the Proposed Rule.*

Where an issuer with connections to Ontario publicly offers securities abroad (usually in the United States) and concurrently sells the securities into Ontario in a private placement, market practice has been to list only the Ontario purchasers – and not list the foreign public purchasers, which would as a practical matter be impossible – on the exempt distribution report filed on Form 45-106F1 *Report of Exempt Distribution*. This position is premised on the conclusion that, unlike the case in certain other provinces, no Ontario distribution takes place with respect to the foreign sale, so there is no need to report foreign purchasers acquiring securities under a prospectus exemption. The Proposed Rule will provide important certainty on this point, because none of the new prospectus exemptions are to be included on the list of prospectus exemptions that trigger a filing on Form 45-106F1.

The Proposed Rule does, however, require filing a report on Form 72-503F *Report of Distributions Outside of Canada*. Although foreign purchasers need not be listed in the report, this new filing obligation imposes a regulatory burden on Ontario issuers that does not currently exist under the Interpretation Note regime. As most Ontario prospectus offerings and private placements now include a foreign sales component, the reporting requirement is likely to have real and substantial cost implications for Ontario issuers, without any evident offsetting regulatory purpose.

If the Commission determines to include reporting on Form 72-503F in the final version of the Proposed Rule, the reporting obligation should be an obligation of the issuer, and no reporting obligations should be placed on the foreign dealer. Moreover, under no circumstances should Form 72-503F require disclosure of purchaser information. The inclusion of information with respect to investors outside of Canada would result in the loss by Ontario issuers of access to the global capital markets. We are aware that the Proposed Rule does not contemplate either a reporting obligation being placed on foreign dealers or the disclosure of purchaser information. However, given the outcome of the process that resulted in the new version of Form 45-106F1, SIFMA's members have developed a heightened sensitivity regarding the scope of Canadian reporting obligations, and wish to emphasize the negative impact of these kinds of requirements.

7. *Include Guidance Regarding Operation of the Foreign Public Offering Exemption in the Companion Policy.*

The second prong of the Foreign Public Offering Exemption could be interpreted as being conditioned on the offering document that is filed in the foreign jurisdiction being "similar to a[n] [Ontario] final prospectus." SIFMA does not believe that the Commission intends for issuers and underwriters to undertake an analysis regarding whether foreign public offering disclosure requirements are similar enough to Ontario's public offering disclosure requirements to permit reliance on the exemption. Such a requirement would be unworkable in practice. SIFMA therefore suggests that the Commission clarify in the Companion Policy guidance that (i) the phrase "similar to a final prospectus" does not mean *substantively* similar to a final prospectus, but instead means a "public offering document" (as opposed to a private placement memorandum) and (ii) so long as "a receipt or similar acknowledgement of approval has been obtained" from the foreign jurisdiction for a public offering document, the exemption is available and the foreign offering document is presumed to be "similar to a final prospectus."

*****

Should you wish to discuss the contents of this letter with us, or obtain more information about the concerns we have raised, please contact the undersigned at (212) 313-1118.

Sincerely,

Sean Davy, Managing Director, Capital Markets Division
Securities Industry and Financial Markets Association