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New Rules Governing Insider Reporting

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Securities regulators across Canada have introduced new rules governing insider reporting. These rules are intended to consolidate the main insider reporting requirements and exemptions in a single national instrument thereby making it easier for issuers and insiders to understand their obligations and to promote timely and effective compliance. The new rules are set forth in National Instrument 55-104 *Insider Reporting Requirements and Exemptions* (the "New Rule").[\[FN2\]](#)

Effective Date and Acceleration of Filing Deadline

The New Rule takes effect on April 30, 2010.

On October 31, 2010 the New Rule accelerates the *filing deadline for insider reports to five calendar days* from ten calendar days.

Reporting Insider

The New Rule introduces the term "reporting insider" to focus the insider reporting requirements on a core group of persons who in some cases are not "insiders" as defined in securities legislation. The definition of "reporting insider" includes:

- (a) the *CEO, CFO or COO* of the reporting issuer, of a significant shareholder of the reporting issuer or of a major subsidiary (as defined below) of the reporting issuer;
- (b) a *director* of the reporting issuer, of a significant shareholder of the reporting issuer or of a major subsidiary of the reporting issuer;
- (c) a person or company *responsible for a principal business unit*, division or function of the reporting issuer;
- (d) a *significant shareholder* of the reporting issuer;
- (e) a significant shareholder *based on post-conversion beneficial ownership* of the reporting issuer's securities and the CEO, CFO, COO and every director of the significant shareholder based on post-conversion benefi-

cial ownership;

(f) a *management company* that provides significant management or administrative services to the reporting issuer or a major subsidiary of the reporting issuer, every director of the management company, every CEO, CFO and COO of the management company, and every significant shareholder of the management company;

(g) an *individual performing similar functions* to the functions performed by any of the insiders described in paragraphs (a) to (f);

(h) the *reporting issuer* itself, if it has purchased, redeemed or otherwise acquired a security of its own issue, for so long as it continues to hold that security; or

(i) *any other insider* that:

(i) in the ordinary course receives or has access to information as to material facts or material changes concerning the reporting issuer before the material facts or material changes are generally disclosed; and

(ii) directly or indirectly, exercises, or has the ability to exercise, significant power or influence over the business, operations, capital or development of the reporting issuer.

The New Rule has increased the percentage threshold of a "major subsidiary" from 20% of consolidated assets or revenues to 30% of consolidated assets or revenues as reported on an issuer's most recent annual audited or interim financial statements. As the determination of a "major subsidiary" is based on the issuer's most recent financial statements it will generally require a backward-looking determination. Accordingly, if an issuer acquires a subsidiary or undertakes a reorganization, with the result that a subsidiary will come within the definition of major subsidiary once the issuer subsequently files its financial statements, the subsidiary will not be considered a major subsidiary for the purposes of the insider reporting requirements until such filing. Similar analysis would apply when there is a disposition of a subsidiary.

Related Financial Instruments

Historically, there has been some uncertainty as to whether, as a matter of law, certain derivative instruments involving securities are themselves securities. This uncertainty has resulted in questions as to whether a reporting obligation existed or how insiders should report a derivative instrument.

The New Rule resolves this uncertainty by including derivative instruments in the definition of "related financial instrument". Under the New Rule, it is not necessary to determine whether a particular derivative instrument is a security or a related financial instrument since the insider reporting requirements in the New Rule apply to both securities and related financial instruments. To the extent the following derivative instruments do not, as a matter of law, constitute securities, they will generally be related financial instruments and invoke the insider reporting requirements under the New Rule:

(a) a forward contract, futures contract, stock purchase contract or similar contract involving securities of the insider's reporting issuer;

(b) options issued by an issuer other than the insider's reporting issuer;

(c) stock-based compensation instruments, including phantom stock units, *deferred share units*, restricted share awards, performance share units, stock appreciation rights and similar instruments;

(d) a debt instrument or evidence of deposit issued by a bank or other financial institution for which part or all of the amount payable is determined by reference to the price, value or level of a security of the insider's reporting issuer; and

(e) most other agreements, arrangements or understandings that were previously subject to an insider reporting requirement prior to the New Rule.

Primary Reporting Requirement

A reporting insider must file an insider report within ten calendar days of becoming a reporting insider.

Thereafter, a reporting insider must file an insider report within five calendar days^[FN3] of:

(a) a change in beneficial ownership or control over securities of the reporting issuer; or

(b) a change in interest in, or right or obligation associated with, a related financial instrument (discussed above) involving securities of the reporting issuer.

Supplemental Insider Reporting Requirement for Other Arrangements

Unless addressed above, a reporting insider must file an insider report within five calendar days^[FN4] of:

(a) entering, amending or terminating an agreement having the effect of altering the reporting insider's economic exposure (as defined below) to the reporting issuer, where

(b) the agreement involves securities of the reporting issuer or a related financial instrument involving securities of the reporting issuer.

"Economic exposure" in relation to an issuer generally means the extent to which the economic or financial interests of a person or company are aligned with the trading price of securities of the issuer or the economic or financial interests of the issuer.

These supplemental insider requirements capture equity monetization transactions and other derivative-based transactions that may fall outside the scope of "related financial instruments" in the primary insider reporting requirements. These transactions, which are sometimes referred to as "equity monetization" strategies, allow an investor to receive a cash amount similar to the proceeds of disposition, and transfer part or all of the economic risk and/or return associated with the securities of an issuer, without actually transferring ownership of or control over such securities.

Stock-Based Compensation Arrangements

The definition of "compensation arrangement" makes it clear that most equity-based compensation arrangements, including options, stock appreciation rights, phantom shares, restricted share or restricted share units, *deferred share units*, performance units or performance shares, stock, stock dividends, warrants, convertible securities, or similar instruments are subject to the insider reporting regime. This includes instruments that provide for or permit a payout in cash.

The New Rule allows an *issuer* to file, within five calendar days of the applicable grant, a single report of a grant

under a compensation arrangement in a prescribed form that provides the market with timely information about the existence and material terms of the grants. If this is done and the material terms of the relevant plan have been disclosed in a document filed on SEDAR, the directors or officers receiving grants must (unless otherwise disclosed by the reporting insider) disclose, on a transaction-by-transaction basis or in acceptable summary form, each acquisition and specified disposition of a security under a compensation arrangement on or before the earlier of: (i) March 31 of the next calendar year and (ii) five calendar days of disposition of securities (other than certain specified dispositions) acquired under the compensation arrangement.

Note that there is, however, no obligation for an issuer to file an issuer grant report and if the issuer does not do so the director or officer must meet the filing deadlines under the primary reporting obligations in respect of each grant made to the reporting insider.

Note also that this exemption is limited to directors and officers. Employees and consultants are not included.

Automatic Securities Purchase Plans

The New Rule provides directors and officers of a reporting issuer and of a major subsidiary an exemption from the reporting requirements for both acquisitions and specified dispositions (as defined below) of securities and related financial instruments under an automatic securities purchase plan or ASPP.

"ASPP" means a dividend or interest reinvestment plan, a stock dividend plan, or any other plan established by an issuer or by a subsidiary of an issuer to facilitate the acquisition of securities of the issuer if the timing of acquisitions of securities, the number of securities which may be acquired under the plan by a director or officer of the issuer or of the subsidiary of the issuer, and the price payable for the securities are established in advance by a formula or criteria set out in the plan and not subject to a subsequent exercise of discretion.

"Specified dispositions" are those which are incidental to the ASPP and do not involve a discreet investment decision of the reporting insider or which are made to satisfy a tax withholding obligation. The purchase of a security as a result of the application of a pre-determined, mechanical formula does not generally represent a discrete investment decision. Accordingly, this exemption does not apply to securities acquired under a cash payment option of a dividend or interest reinvestment plan or a lump-sum provision of a share purchase plan or to an acquisition of options or similar securities granted to a director or officer.

Unless otherwise reported by the reporting insider, directors or officers must disclose, on a transaction-by-transaction basis or in acceptable summary form, each acquisition and specified disposition of securities acquired under an ASPP during a calendar year on or before the earlier of (i) March 31 of the next calendar year and (ii) five calendar days of disposition (other than by a specified disposition) of securities acquired under the ASPP.

Note that, again, this exemption is limited to directors and officers.

Normal Course Issuer Bids and Publicly Disclosed Transactions

Under a normal course issuer bid, the issuer must disclose each acquisition of securities by it within ten calendar days of the end of the month in which the acquisition occurred.

Similarly, an issuer is not required to report transactions, other than a normal course issuer bid, involving securities of its own issue if the material terms of the transaction are disclosed in a public filing made on SEDAR.

Issuer Events

"Issuer Event" means a stock dividend, split, consolidation, amalgamation, reorganization, merger or other similar event that affects all outstanding securities of a class of an issuer in the same manner.

Unless otherwise reported by the reporting insider, a reporting insider must report issuer events when next the reporting insider files a report in respect of the affected securities.

Contravention of the Insider Reporting Requirements

It is an offence to fail to file an insider report in accordance with the filing deadlines prescribed by the New Rule or to submit an insider report that is misleading or untrue. An offence of this nature may result in one or more of the following:

- (a) the imposition of a late filing fee;
- (b) identification as a late filer on a public database of late filers;
- (c) the issuance of a cease trade order that prohibits the reporting insider from trading in or acquiring securities or related financial instruments of any reporting issuer until the failure to file is corrected or a specified period of time has elapsed; or
- (d) in appropriate circumstances, enforcement proceedings.

The securities regulators also warn that they may consider information relating to wilful or repeated non-compliance of the insider reporting requirements in the context of a prospectus review or continuous disclosure review, since this may raise questions regarding the integrity of the insiders and the adequacy of the issuer's policies and procedures relating to insider reporting and insider trading.

Summary Only

The foregoing is a summary only of the provisions of the New Rule. Reference is made to the text of the New Rule for full details of the changes to the insider reporting requirements.

[FN1.](#) JEFFREY A. READ practices corporate and securities law at the Vancouver office of Fraser Milner Casgrain LLP, focusing on advising public companies, investment dealers and international clients with investments in British Columbia. Jeff has written several articles on topics including private placements, shareholders' meetings and disclosure obligations and has taught courses on those and other subjects for groups including the Continuing Legal Education Society of British Columbia, the Law Society's Professional Legal Training Course and Simon Fraser University. He is co-editor of the annual Carswell publication *British Columbia Securities Act and Rules Annotated* and is the past Chairman of the Securities Section of the British Columbia Branch of the Canadian Bar Association.

[FN2.](#) The New Rule replaces National Instrument 55-101 *Insider Reporting Exemptions* and Multilateral Instrument 55-103 *Insider Reporting for Certain Derivative Transactions (Equity Monetization)* ("MI 55-103"). In Ontario, the main insider reporting requirements will remain in the *Securities Act* (Ontario). Despite this difference, the substance of the requirements for insider reporting will be the same across Canada.

[FN3.](#) A reporting insider may file an insider report within 10 days of a change described in this section if the change relates to a transaction that occurred on or before October 31, 2010.

[FN4](#). A reporting insider may file an insider report within 10 days of an event described in this section if the event relates to a transaction that occurred on or before October 31, 2010.

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