Securities law & corporate governance

Canada currently does not have a federal securities regulator, as other major capital markets do. Rather, each province and territory has its own securities regulatory authority and its own set of laws, regulations, rules and policies. The 13 provincial and territorial securities regulators work together to harmonize regulation across the country through rules known as "national instruments". As well, issuers can often rely on a "passport" system that allows them to deal directly with only one or two regulators.

Efforts by the federal government to establish a national securities regulatory system were complicated and delayed by a Supreme Court of Canada decision in late 2011, which determined that a then-proposed federal statute governing securities was unconstitutional. Together with the federal government, British Columbia, Ontario, Nova Scotia, New Brunswick, Saskatchewan, Prince Edward Island and the Yukon continue to pursue a co-operative capital markets regulatory system, and have published draft legislation and regulations in this regard. To date, an anticipated launch date has not been confirmed.

1. Distribution of securities
2. Listing in Canada
3. Initial public offerings
1. Distribution of securities

In Canada, unless otherwise exempt, a distribution of securities cannot be completed without the filing of a prospectus. This requirement is intended to protect investors.

A prospectus is a comprehensive disclosure document providing detailed information on the issuer's business and the securities being offered. Furthermore, if the distribution of securities is made by an entity that is engaged in the business - or holding itself out as engaging in the business - of trading in securities, the entity must be registered as a dealer. This helps to ensure that securities are sold by qualified people who have a duty to know their clients and assess the suitability of their clients' investments.

Reporting issuers (i.e., public companies) may avoid prospectus requirements by distributing securities to "accredited investors" (i.e., specified institutional investors and individual investors who meet a certain threshold of net worth or taxable income).

Private corporations in Canada may avoid prospectus requirements by relying on a "private issuer" prospectus exemption. This exemption applies in cases where the corporation has fewer than 50 shareholders, securities that are closely held by a prescribed group of non-public investors - i.e., family, close friends and business associates, and accredited investors - and a restriction on the transfer of the corporation's securities.
2. Listing in Canada

The Toronto Stock Exchange (TSX) and the TSX Venture Exchange (TSX-V) are the two major Canadian public stock exchanges. Lately, there has also been an increasing number of junior issuers listing on the Canadian Securities Exchange (CSE).

In Canada, opportunities exist for corporations to go public and access the capital markets at a much earlier stage than other markets, such as the United States. In some circumstances, the CSE and the TSX-V facilitate listing at a pre-revenue stage through a two-tiered system with different levels of listing requirements. Many non-Canadian corporations list in Canada as a first step toward listing in the U.S.

3. Initial public offerings

The process for completing an initial public offering (IPO) in Canada generally takes three to four months. An issuer must first file a preliminary prospectus with securities regulators for their review and comment, followed by a final prospectus. A prospectus must contain "full, true and plain disclosure of all material facts" related to the issuer's business and the securities being offered. It must also include three years of audited financial statements prepared in accordance with International Financial Reporting Standards (IFRS) or U.S. Generally Accepted Accounting Principles (GAAP) with a reconciliation to IFRS.

Securities regulators are required to provide their comments within 10 business days of the date that the preliminary prospectus was filed. An issuer is not permitted to file a final prospectus until all comments from regulators are settled. The prospectus rules include rules governing the pre-marketing and marketing of the public distribution of securities, including marketing materials and road shows.

An issuer planning a public offering in multiple Canadian jurisdictions will generally rely on the "passport" system. Under this system, a preliminary prospectus filed and cleared with the issuer's principal regulator is automatically accepted by the other provincial regulators.

An issuer that becomes listed in Canada upon completion of an IPO, or that otherwise becomes a reporting issuer in Canada - e.g., through acquisition of a Canadian public company by way of share exchange - will be required to comply with Canadian requirements on timely and periodic disclosure, financial reporting, and corporate governance, as well as the policies of the
4. Continuous disclosure requirements

The continuous disclosure obligations of a reporting issuer fall into two categories: periodic disclosure and timely disclosure.

Periodic disclosure occurs at regular intervals and consists of quarterly and annual financial statements, quarterly and annual management's discussion and analysis, an annual information form (for TSX issuers) and shareholder meeting materials.

In Canada, reporting issuers are required to file their continuous disclosure and timely disclosure documents on sedar.com, a free electronic database for the general public, including investors.

Canadian securities legislation also requires insiders of reporting issuers to report their security holdings, as well as any direct and indirect transactions involving those holdings.

The principal requirement for timely disclosure is that a reporting issuer must issue and file a press release "forthwith" when a material change in its affairs occurs, or when material information relating to its affairs becomes known to management. A "material change" is a change in the business, operations or capital of the reporting issuer that would reasonably be expected to have a significant effect on the market price or value of any of its securities. This includes situations where a decision to implement one of the changes referred to above is made by the board of directors (or other persons acting in a similar capacity), or by the reporting issuer's senior management if it believes that confirmation of the decision by the board of directors (or people acting in a similar capacity) is probable.

5. Civil liability

Breach of timely and continuous disclosure requirements - including a misrepresentation in publicly disclosed communications - can result in civil and administrative proceedings against a reporting issuer. Possible consequences include being placed on a list of defaulting reporting issuers maintained by most securities regulatory authorities, the issuance of a temporary or permanent cease-trade order by the securities regulatory authorities, or delisting by the TSX or the TSX-V.

Reporting issuers in all Canadian jurisdictions have liability to investors under Canadian securities legislation for damages for misrepresentations in a publicly disclosed communication - such as an information circular or public oral statement - or failure to make timely disclosure.
Plaintiffs are deemed to have relied on either the misrepresentation or on the reporting issuer having complied with its disclosure obligations. However, provincial securities laws do set limits on liability and provide for defences. Leave of the court is required for an action to proceed. Court approval is also required for settlements, and costs are awarded to the prevailing party as determined by the court.

In addition to the reporting issuer, its directors and officers - and other persons who knowingly influence the release of a misrepresentation - also have liability to investors under Canadian securities legislation. Generally, a defendant will not be liable for a misrepresentation in a publicly disclosed communication if the defendant proves that:

- Before the release of the information containing the misrepresentation, the defendant conducted or caused to be conducted a reasonable due-diligence investigation.
- At the time of the release, the defendant had no reasonable grounds to believe the document or statement contained the misrepresentation.

Similarly, a defendant will not be liable for breaches of timely disclosure obligations if it shows that, before the failure to make timely disclosure first occurred, it conducted or caused to be conducted a reasonable due-diligence investigation, and that it had no reasonable grounds to believe that the failure to make timely disclosure would occur.

6. Financial reporting requirements

An issuer listed on the TSX must file audited annual comparative financial statements, accompanied by an auditor’s report, with securities regulators within 90 days of its financial year-end. For an issuer listed on the TSX-V or CSE, the time period is 120 days. The board of directors must approve these financial statements before they are filed.

Interim comparative financial statements are required on a quarterly basis and must be filed with securities regulators within 45 days of the end of the financial period for TSX-listed issuers, and within 60 days for issuers listed on the TSX-V or CSE. These statements are generally reviewed by auditors but are not required to be audited.

A reporting issuer is required to deliver annual or interim financial statements to security holders only upon request - provided the reporting issuer annually sends a request form to each security holder.

7. Shareholder meetings
A meeting of shareholders of a corporate issuer must be held each year, generally not later than six months following its fiscal year-end.

Typically, a corporate issuer must mail a notice of meeting to all registered shareholders entitled to vote, to the corporation's directors and to the auditors at least 21 days prior to the meeting. Along with the notice, reporting issuers are also required to send to shareholders a management information circular describing the matters to be voted on at the meeting, and providing other corporate disclosure and proxy voting instructions. The notice and all documentation related to the meeting must be mailed concurrently to all holders of non-voting equity securities.

In lieu of mailing these materials to shareholders, a "notice and access" regime permits these materials to be made available and accessible to shareholders through the Internet - so long as certain conditions are satisfied and notice is provided to shareholders. The requirements of applicable corporate statutes must also be considered.

8. Expedited public financings and private placements

A reporting issuer that has established a minimum 12-month continuous disclosure record in Canada, and has filed an annual information form (AIF), is generally eligible to complete a public offering on an expedited basis by filing a short-form prospectus. An AIF is a disclosure document filed within 90 days of an issuer's financial year-end that contains the corporate and non-offering disclosure found in a long-form prospectus. Only TSX-listed issuers are required to file an AIF.

A short-form prospectus describes the securities being offered, and incorporates by reference certain documents previously prepared and filed by the issuer - such as the most recent AIF, management information circular, annual and interim financial statements, and any material change reports. The short-form prospectus is usually cleared by securities regulators across Canada within one week.

9. Prospectus-exempt distributions

Certain exemptions permit issuers to distribute securities without filing a prospectus. Most notably, these exemptions include distributions to accredited investors and employees, and distributions of securities (other than to individuals) with an acquisition cost to the purchaser of not less than $150,000 in cash.
Examples of accredited investors include:

- Registered investment advisers and dealers, financial institutions, governments and government agencies, insurance companies, pension funds, and certain investment funds
- Individuals and corporations that meet certain income or financial asset thresholds

Prospectus exemptions are also available for certain non-financing distributions, such as securities exchange take-over bids and distributions made in connection with a business combination or a reorganization transaction.

Prescribed notice of a prospectus-exempt distribution of securities must be filed with the applicable securities regulators in certain circumstances, together with the payment of a prescribed filing fee. If an offering memorandum is delivered to a Canadian investor in respect of such prospectus-exempt distribution, certain provincial securities regulators require it to be filed as well.

**10. Early warning reporting**

A person who acquires 10 per cent of the voting or equity securities of a reporting issuer - including convertible securities and rights to acquire voting or equity securities - is required to comply with the "early warning" provisions of Canadian securities law. These provisions include the obligation to issue a press release and to file an early warning report.

The purpose of the early warning report is to disclose to the market that a particular investor holds a significant ownership stake in the reporting issuer, and to provide information on the investor's intentions with respect to the investment.

A further report and press release are required for each increase and decrease in ownership of at least two per cent, as well for each change in a material fact contained in the most recent report required to be filed. Relaxed early warning reporting requirements are available to certain eligible institutional investors who declare no intention to acquire over 20 per cent of an issuer's securities.

Subject to certain exemptions, a person is prohibited from acquiring greater than 20 per cent of the voting securities of a reporting issuer unless that person first complies with the take-over bid rules of Canadian securities law, which require that an offer to acquire securities be made to all shareholders.

**11. Take-over bids**
A take-over bid is an offer made by a person (or group of persons acting in concert) to acquire from securities holders - i.e., not from treasury - voting or equity securities of any class of an issuer that, together with outstanding securities of the class already owned, exceeds 20 per cent of the outstanding voting or equity securities of such class.

Generally, a take-over bid is made by mailing a take-over bid circular to all shareholders and filing it with the applicable securities regulators. The take-over bid circular describes the terms and conditions pursuant to which the offeror will purchase the issuer's securities from shareholders and, where the consideration includes securities, also contains disclosure relating to the offeror and the securities being offered. As a result of recent amendments (discussed in more detail below), a take-over bid must be open for a minimum deposit period of 105 days subject to certain exceptions.

A take-over bid must be open for a minimum deposit period of 105 days, unless the target board states in a news release that a shorter deposit period (not less than 35 days) is acceptable - in which case, all concurrent bids must remain open for at least the stated shorter deposit period - or the target issues a news release that it intends to enter into a specified alternative transaction - in which case all concurrent bids must remain open for a deposit period of at least 35 days.

A minimum threshold for shareholder acceptance is a typical condition of a take-over bid. A minimum tender condition of more than 50 per cent of the outstanding securities of the class that are subject to the bid is required by law, however, 66 2/3 per cent and 90 per cent minimum tender conditions are the most common thresholds. An acceptance level of 66 2/3 per cent generally permits the offeror to eliminate the remaining shareholders who have not tendered their shares under the take-over bid pursuant to a second-stage transaction, such as an amalgamation. If an offeror acquires 90 per cent of the shares of a class not owned by it, the acquirer is permitted by most Canadian corporate statutes to compulsorily acquire the remaining shares.

Take-over bids must be extended for at least an additional 10 days after the minimum tender requirement is met.

There are very few exemptions from the take-over bid rules. The most useful exemption requires that securities be purchased by private agreement from no more than five sellers in respect of an offer to acquire that is not made generally to shareholders at a price not exceeding 115 per cent of the market price of the securities. Generally, the market price is equal to the average closing price of the securities on the stock exchange during the 20 trading days preceding the date of the agreement. Another exemption permits the purchase of no more than five per cent of a class of securities during any 12-month period at prices not exceeding
the market price of the securities.

12. Insider reporting

Directors, chief executive officers, chief financial officers and chief operating officers of a reporting issuer, of a significant shareholder (those holding more than 10 per cent of the voting shares) of a reporting issuer, or of a major subsidiary of a reporting issuer - as well as the significant shareholders themselves - are generally considered to be "reporting insiders" and are required to file insider reports under Canadian securities laws. Other employees of a reporting issuer, by virtue of their responsibilities or their access to information and their ability to exercise power or influence, may also be considered "reporting insiders."

Insider reports are intended to provide the marketplace and regulators with disclosure relating to a reporting insider's direct or indirect beneficial ownership, control or direction over the reporting issuer's securities. A reporting person must file publicly available reports within 10 days of becoming a reporting insider, and within five days of subsequent changes in security ownership.

13. Insider trading and tipping

Insider trading involves buying or selling a reporting issuer's securities with knowledge of material information about the reporting issuer that has not been publicly disclosed. Tipping involves providing material undisclosed information to a person other than in the necessary course of business.

Insider trading and tipping are serious offences. Conviction in Ontario, for instance, can result in a fine of up to $5 million, imprisonment for up to five years less a day and/or banishment from trading in securities. Defendants have a defence to an insider-trading or tipping allegation if they prove that they reasonably believed that such material information had been generally disclosed.

14. Corporate governance

In response to the U.S. Sarbanes-Oxley Act of 2002, Canada's securities regulatory authorities promulgated a series of corporate governance-related instruments.

For example, TSX-listed issuers are required to have an audit committee composed of at least three directors, all of whom must be both "independent" and "financially literate." Issuers listed
on the TSX-V are required to have an audit committee composed of at least three directors, the majority of whom cannot be officers, employees or control persons of the issuer, or any of its associates or affiliates. The CSE provides greater flexibility on audit committee composition.

In addition, these instruments set out a list of non-binding corporate governance guidelines that reporting issuers are encouraged to consider in developing their own practices. While compliance with the guidelines is voluntary, mandatory disclosure is imposed on reporting issuers with respect to whether or not their corporate governance practices comply. Other corporate governance recommendations include:

- A board consisting of a majority of independent directors with an independent chair or lead director, and with the independent directors holding regularly scheduled meetings at which non-independent directors and members of management are not in attendance
- Written board and board-committee mandates that outline the functions and responsibilities of the board and its committees
- Clear position descriptions for the chair of the board, the chair of each board committee and the chief executive officer
- A written code of business conduct and ethics
- Nominating and compensation committees composed entirely of independent directors
- Orientation for new directors and continuing education opportunities for all directors
- Regular board, board committee and individual director assessments regarding effectiveness and contributions

There are also annual corporate governance disclosure requirements for TSX-listed issuers relating to the representation of women on boards and in senior management, and director term limits. These requirements use a "comply or explain" model and were developed with a view to increasing transparency regarding the representation of women on boards and in senior management, and to promote board renewal and opportunities for women board candidates.

Under the Canada Business Corporations Act (CBCA), a "distributing corporation" will also need to comply with new disclosure requirements relating to diversity as of January 1, 2020. While similar to the above-noted disclosure requirements under securities laws, the CBCA requirements cover "designated groups" not just women. The term "designated groups" means women, Aboriginal peoples, persons with disabilities and members of visible minorities.

15. Québec

Documents of a contractual nature, such as prospectuses and take-over bid circulars (tender offer materials), must be translated and sent to Québec residents in French.
16. Dealer, adviser and investment fund manager registration requirements and exemptions

Any person or company that engages in (or holds itself out as engaging in) the business of trading in securities in Canada - including acting in furtherance of a trade, such as the marketing of securities - must be registered as a dealer in each province or territory where such business activities are undertaken.

A person or company registered as a broker or dealer in a jurisdiction outside of Canada may rely on an "international dealer" exemption, which, subject to certain pre-notification filings (and the payment of an annual fee if trading in certain provinces), generally permits a dealer to trade in non-Canadian securities to Canadian institutional investors and ultra-high-net-worth individuals.

Portfolio managers with Canadian clients must be registered as advisers in the Canadian jurisdictions where the clients reside. Portfolio managers that are registered, or those that are exempt from registrations in their home jurisdictions, may rely on an "international adviser" exemption, which, subject to certain pre-notification filings (and the payment of an annual fee if advising clients in certain provinces), generally permits them to act for institutional investors and ultra-high-net-worth individuals - as long as less than 10 per cent of their revenue is derived from Canadian clients.

The administrative fund managers of Canadian and certain non-Canadian investment funds (including private hedge funds) responsible for directing the business, operations or affairs of an investment fund - which may or may not be the same entity as the fund's investment adviser/portfolio manager - must be registered as investment fund managers, and must meet certain minimum risk-free capital, insurance and other compliance requirements. Again, subject to certain pre-notification requirements, non-Canadian investment fund managers that manage investment funds that admit Canadian investors may rely on an available non-resident investment fund manager registration exemption.

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Doing business in Canada - a checklist
Is Canadian business in your organization's future? Our checklist offers a high-level summary of the legal issues organizations should consider before entering the lucrative Canadian market.

Doing Business in Canada: Top ten things that may surprise you
Although Canada's legal system may be familiar to many foreign investors and companies, it has a number of unique aspects that may surprise you.
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