AUM LAW

March 2023 | Bulletin

March Break Edition

March Break may have just passed, but it is still important to periodically take time to relax, reflect and recharge. Not only is rest a form of nourishment, but it drives productivity. Days are getting longer, the sun is (generally) out, and spring weather is just around the corner!

We hope that all our readers were able to take some time away from work, helping with homework, or both, and are ready for the regulatory compliance updates described below.

In this bulletin:

1. Don't Stay Away too Long – Revised Guidance Published for Issuers Relying on the Offering Memorandum Prospectus Exemption

On March 8, 2023, staff of the Canadian Securities Administrators (other than Ontario), published revised Multilateral CSA Staff Notice 45-309 (the **Notice**), first published in 2012, which provides guidance for preparing and filing an offering memorandum (an **OM**) under National Instrument 45-106 – *Prospectus Exemptions* (**NI 45-106**). The Notice is relevant to issuers that rely on the offering memorandum prospectus exemption (the **OM Exemption**) and summarizes common deficiencies that have been observed in OMs prepared in accordance with Form 45-106F2. The Notice also discusses potential consequences of non-compliance with the terms of the OM Exemption.

The Notice was published in conjunction with the effective date of the amendments to NI 45-106 applicable to issuers relying on the OM Exemption that are "collective investment vehicles" and "real estate issuers" (the **Amendments**). We wrote about the Amendments in our January bulletin.

The CSA remind issuers that an OM must comply with the requirements of the OM Exemption when it is prepared, when it is delivered to prospective purchasers and when the issuer accepts an agreement to purchase the security from the purchaser. This means that the OM must be in the correct form, not contain any misrepresentations and provide sufficient information to enable a prospective purchaser to make an informed investment decision.

Staff have observed issuers making distributions under the OM Exemption using an OM that no longer meets the requirements, which is not permitted. This can occur if an issuer fails to update the OM to reflect a material change or to include more recent financial statements. If distributions under the OM Exemption are ongoing, the OM is required to be amended to include annual audited financial statements for the issuer's most recently completed financial year no later than 120 days after the issuer's financial year-end. For ongoing distributions to Ontario residents, the OM must be amended to include financial statements for the issuer's most recently completed six-month interim period no later than 60 days after the end of that period, unless the issuer qualifies for the exemption set out in the Amendments.

The CSA also remind issuers that disseminating material forward-looking information (such as expected returns) to prospective purchasers during the course of a distribution without disclosing such information in the OM is prohibited.

Other common issues with OMs discussed in the Notice include the following:

- Failing to file an OM on time;
- Failing to provide balanced disclosure;
- Inadequately disclosing available funds and use of available funds;
- Omitting key terms of material agreements;
- Omitting compensation disclosure;
- Omitting key elements of financial statements;
- Omitting required interim reports;
- Failing to obtain required audits; and
- Improperly certifying the OM.

Issuers relying on the OM Exemption should ensure that their OM complies with the requirements of NI 45-106. Now that the Amendments are in effect, any update to an OM will require a "form check" to ensure the OM complies with the Amendments. An updated OM must be filed with the regulators no later than 10 days after the first distribution under that OM. If you have any questions or would like our assistance with reviewing your OM, please contact us.

2. Watch that Spring Break Behaviour – OSFI Issues Guideline on Culture and Behaviour Risk

Building off of the Office of the Superintendent of Financial Institution's (**OSFI's**) Culture Risk Management Letter published on March 15, 2022 and the ensuing feedback, OSFI has published a draft *Culture and Behaviour Risk Guideline* (**Proposed Guideline**) for consultation on February 28, 2023. The Proposed Guideline is intended to complement OSFI's existing guidance for Corporate Governance, Operational Risk Management, and Regulatory Compliance Management. The Proposed Guideline would apply to all federally regulated financial institutions (**FRFIs**).

OSFI recognizes that organizational culture poses risks that can have a material impact on the health of a financial institution, and on the broader financial system. OSFI defines culture risk as the widespread behaviours and mindsets that can threaten sound decision making, prudent risk-taking, and effective risk management, which can lead to a weakening of an institution's financial and operational resilience. With this in mind, OSFI is enhancing their assessment of culture risks to include items beyond corporate governance for a more comprehensive assessment of the adequacy and effectiveness of FRFIs in managing organizational culture risk. The Proposed Guideline supports OSFI's mandate to contribute to public confidence in the Canadian financial system.

The Proposed Guideline sets outcomes and principles-based expectations for FRFIs to oversee their culture and assess the impact of behaviour patterns to effectively manage the associated risks. The guideline details the following outcomes and principles:

Outcome 1:	Culture and behaviour are designed and governed through clear accountabilities and oversight
Principle 1:	Desired culture and expected behaviours are designed to align with the purpose and strategy of the FRFI and governed through appropriate structures and frameworks
Outcome 2:	Desired culture and expected behaviour are proactively promoted and reinforced
Principle 2:	Leaders, at all levels, consistently promote and reinforce the desired culture and expected behaviours through their words, actions, and decisions
Principle 3:	Talent and performance management strategies and practices promote and reinforce the desired culture and expected behaviours
Principle 4:	Compensation, incentives, and rewards promote and reinforce the desired culture and expected behaviours
Outcome 3:	Risks emerging from behaviour patterns are identified and proactively managed
Principle 5:	FRFIs proactively monitor for, assess, and act to address risks related to culture and behaviour that may influence their resilience

OSFI expects FRFIs to design, govern and manage culture and behaviour in accordance with the FRFI's size, nature, scope, complexity of operations, strategy, and risk profile. Senior management will be held accountable for the design, implementation, and monitoring of FRFI culture, and robust governance structures that address and embed the desired culture across the institution. OSFI suggests that FRFIs take a 'tone from the top,' supported by middle management and an 'echo from the bottom' approach to managing cultural and behaviour risk.

At a minimum, OSFI expects FRFIs to use leadership, talent and performance management practices, and compensation and incentive plans to promote and/or reinforce their desired culture and expected behaviours. On the management side, OSFI expects FRFIs to implement strategies to monitor, identify, assess, and manage risks arising from behaviour patterns that do not align

with the desired culture and expected behaviour – such as complacency, excessive risk taking, poor communication, or lack of speaking up or raising concerns.

The consultation period runs until March 31, 2023. Industry and stakeholders can comment on the draft *Culture and Behavior Risk Guideline* by contacting culture@osfi-bsif.gc.ca. The final guideline is expected by the end of 2023, along with a self-assessment tool to help FRFIs review the design and effectiveness of their practices and support compliance with the Proposed Guideline. Additional information can also be found in BLG's article listed below.

3. Eat, Beach, Sleep, Repeat – New SRO Compliance Priorities Report Repeats Importance of Conflict Documentation

On March 20, 2023, the New Self-Regulatory Organization of Canada (**New SRO**) published its *New SRO Compliance Priorities Report for 2022/2023: Helping Firms with Compliance*. The report highlights what the New SRO believes are issues and challenges faced by the industry, and the key areas of focus of its compliance reviews in 2023.

In 2022, the New SRO's predecessor self-regulatory organizations and the Canadian Securities Administrators (**CSA**) conducted a sweep of the industry to examine compliance with the Client Focused Reforms (**CFR**) Conflict of Interest (**COI**) requirements. The results of the sweep for dealer firms were promising, in that the New SRO praised the fact that most dealers had controls in place that satisfied the requirements to identify, disclose, and address conflicts while adhering to the best interest standard. However, consistent with findings from the CSA (see our bulletin last month for more information here), the report noted gaps relating to the sale of proprietary funds, deficiencies relating to undocumented assessments of material conflicts and insufficient disclosure to clients. More specifically:

- The assessments of material conflicts, and **how** the dealer (i.e., documented process steps) would address the conflicts in accordance with the best interest standard, were not adequately documented, and
- Mandated disclosure to clients missed key components, such as:
  - the nature and extent of the COI;
  - the potential impact on and the risk the COI posed to the client; and
  - how the firm planned to address the COI, or how they had already dealt with the matter.

The report reminds readers that simply providing disclosure to clients does not in itself satisfy the requirements.

The CSA and the New SRO will publish a report later this year detailing the deficiencies found from their CFR reviews and provide further guidance for the industry. Firms are expected to review the guidance once published and review their policies and procedures, especially COI disclosures, and determine whether they may have gaps in their internal controls and remediate them accordingly.

Also later in 2023, as part of a co-ordinated review with the CSA, the New SRO will participate in "CFR-Phase II", which we expect will assess compliance with, and internal processes relating to the following requirements: Relationship Disclosure, KYC, Suitability, Know Your Product/Product Due Diligence, Misleading Communications and Outside Activities.

In addition to its reminders with respect to conflicts of interest, the New SRO included a number of other items in its report. For example, the New SRO has placed continued emphasis on adequate education and reporting surrounding cybersecurity risks. The cybersecurity self-assessment tool published by IIROC in 2022 is now available to all dealers regulated by the New SRO, to help assess preparedness and identify areas of improvement related to cybersecurity risks. While the tool is not mandatory, the New SRO does recommend using it at least once every two years.

The New SRO will continue to conduct examinations on investment dealers to evaluate how dealers are demonstrating their compliance with the cybersecurity incident reporting requirements (**CIRR**) and how cybersecurity risks are being managed. The New SRO continues to find insufficient evidence from dealers to demonstrate their compliance with the CIRRs.

The report also advised that where the cybersecurity functions of a group of entities were centralized, policies did not address the specific requirement to conduct a separate assessment of materiality, substantial harm, significance, and other thresholds on an individual basis.

Following amendments to National Instrument 33-109, outside activities will also remain an area of focus during New SRO examinations. Dealers should be familiar with the new framework brought about by these amendments, particularly as it relates to the reporting of outside activities and the codification of new rules surrounding the definition and handling of positions of influence. The New SRO pointed to a significant increase in deficient filings uncovered as part of its ongoing reviews, particularly with respect to reportable activities.

Another item covered in the report included digital engagement practices. Given the increasing sophistication of digital engagement strategies, the New SRO will be closely monitoring potential instances of improper advertising and sales communication practices. This includes gamification strategies which may oversimplify complex products, encourage reckless behaviour, and imbue investors with a false sense of confidence.

Improper delegation was also noted; while delegation of supervisory controls/tasks is permitted under the Universal Market Integrity Rules, the New SRO continues to find instances where delegated responsibilities have not been formally documented in detail. Ambiguity around who is responsible for supervisory controls can have obvious negative consequences for investors and the market. As such, any such delegation must be clearly demarcated and well documented.

4. Refreshed and Refocused: Rules Introduced to Support SEDAR+

With SEDAR+ set to replace SEDAR on June 13, 2023, the Canadian Securities Administrators (**CSA**) published two advance notices for the adoption of certain rules which will serve to support the transition. The first notice pertains to the CSA's repeal and replacement of Multilateral Instrument 13-102 *System Fees for SEDAR and NRD* (**MI 13-102**) with the new instrument: Multilateral Instrument 13-102 *System Fees*. The second notice pertains to the CSA's adoption of National Instrument 13-103 *System for Electronic Data Analysis and Retrieval + (SEDAR+)* (**NI 13-103**) and accompanying companion policy (collectively, the **Amendments**).

The repeal and replacement of MI 13-102 is based on the CSA's commitment of making SEDAR+ a more cost-effective filing system, and as such the revised MI 13-102 and the methodology of calculating system fees is established on a projected cost-recovery basis (i.e., the cost to operate SEDAR+) and to support future developments and enhancements. As part of this, a key change includes the introduction of a flat fee based on filing type to replace the previous method where

the majority of system fees were calculated based on the number of jurisdictions where documents were filed. Currently, depending on type of filing, there may be a system fee payable to the principal regulator as well as a separate fee payable to any applicable non-principal regulator.

Other system fees associated with certain filings have also been eliminated, including system fees related to filings for the registration of an individual in an additional jurisdiction (for a future phase when registration related materials are filed through SEDAR+) and related party transactions. Regulatory filing fees will still be payable where applicable. There will also be new system fees (once registrant activities are included in SEDAR +) to file applications for exemptions from a registration requirement.

Additionally, SEDAR+ will not have a separate charge for creating a profile, as compared to SEDAR where users currently pay a one-time charge. As a result of all of these changes, the CSA projects that the total system fees they collect will decline. A full list of filing types with associated system fees can be found in the CSA's notice of repeal and replacement of MI 13-102.

NI 13-103 introduces specifics of which documents are to be transmitted through SEDAR+ (versus the documents that may be transmitted outside of SEDAR+). Generally, all documents required to be filed or delivered to a securities regulator are to be filed or delivered through SEDAR+, subject to certain limited exceptions, such as documents required to be delivered in connection with a compliance review. A full list of the exceptions can be found in the CSA's notice of NI 13-103. It is important to note that SEDAR+ will have a phased implementation, and as such, certain documents which are not to be filed through SEDAR+ at this time are expected to be brought into SEDAR+ in a future phase. For example, an insider filing an insider report under National Instrument 55-102 *System for Electronic Disclosure by Insiders (**SEDI**)*, will continue to do so for now through SEDI. A list of the documents expected to be brought under SEDAR+ can be found in Column A of the Appendix to NI 13-103. As part of Phase 1, the filing of Form 45-106F1 *Report of Exempt Distribution* for all jurisdictions will now be through SEDAR+, the filing of which will be subject to a system fee. As such, the use of the British Columbia Securities Commission and Ontario Securities Commission's separate electronic filing portals for this purpose will be discontinued. Coinciding with the introduction of NI 13-103, the former instrument National Instrument 13-101 *System for Electronic Document Analysis and Retrieval (**SEDAR**)*, including the SEDAR Filer Manual, will be repealed.

The Amendments will come into force on June 9, 2023. If you require assistance in navigating the transition to SEDAR+ or have any questions regarding the Amendments, please contact us. For further information, you can also consult BLG's article listed below.

In Brief

SEDAR+ is Not a Stress Free Zone - Foreign Issuers and Reports of Exempt Distributions

As mentioned above, the Phase 1 rollout of the new SEDAR+ filing system will be launching on June 13, 2023. This phase of the rollout requires numerous filings to be submitted on SEDAR+ after June 13, including by foreign issuers who are required to file a Form 45-106F1 (Report of Exempt Distribution). As of this date, foreign issuers/funds, including those who currently file their F1s through the portals offered by the Ontario Securities Commission and the British Columbia Securities Commission, will be required to make their filings through SEDAR+. These forms will be available for viewing by the public.

The Canadian Securities Administrators (**CSA**) have made it clear that any issuers who have filing obligations must be onboarded or registered with the SEDAR+ platform in the future. This requires, among other things, the filing of an Electronic Filer Agreement (**EFA**). For foreign issuers/funds who rely on a related entity or other filing agent to make their filings on their behalf, this will also require the submission of a Filing Agent Authorization Form (**FAAF**). The CSA has strongly suggested that onboarding occur prior to April 14, 2023.

We expect that additional guidance will be forthcoming from the CSA to assist foreign issuers with respect to onboarding to the SEDAR+ platform.

Break's Over – New OSC Service Commitments

The Ontario Securities Commission (**OSC**) published its 2023 Annual Service Commitment Review on March 21, 2023. The OSC has updated its service standards and returned to pre-extension 2021 service timelines and targets for reviewing prospectus filings and applications for exemptive relief (excluding exemptions from recognition applications for market infrastructure entities). All service standard changes are effective April 1, 2023, except changes to prospectus-related standards which came into effect earlier on January 9, 2023.

Many of the 2023 updates detail changes to timelines relating to prospectus filings, where the working day standards have generally been reduced (along with certain review percentage targets). With respect to registrants, it is notable that no changes have been made to the extended timelines for new registration submissions for entities or individuals. With respect to acknowledgements for a filed Notice of End of Individual Registration or Permitted Individual Status, the OSC aims to respond within 24 hours of receipt, for routine filings. For registered firms selected for a compliance review, findings are intended to be communicated within 14 weeks of the initial meeting (80% of the time, excluding sweeps), which is an increase from the previous 12 week service standard. The OSC's performance results against these standards can be found on its website.

It is noted in the statement that staff time spent on a review depends on the quality and effectiveness of a firm's compliance program, as well as the availability of key personnel and prompt responses to staff requests for information. It is further noted that staff will provide regular touchpoints to advise of progress at a minimum of every two weeks. If you require any assistance getting ready for a compliance review, please contact your usual lawyer at AUM Law.

Title Protection Frameworks Ramp Up – No Time for a Breather

As summarized way back in our August, 2021 bulletin, the Financial and Consumer Services Commission of New Brunswick (**FCNB**) has previously consulted on a framework for the protection of titles used by financial professionals in that province. That consultation ended in October of 2021, but the government of New Brunswick has now taken the next step and introduced a bill entitled the Financial Advisors and Financial Planners Title Protection Act. As currently formulated, a person who is not a financial advisor or financial planner with an approved credential from a credentialling body will not be permitted to use the title "financial advisor" (conseiller financier) or "financial planner" (planificateur financier), a title prohibited by regulation, a variation or abbreviation of any of those titles or an equivalent in another language or a title that implies a person is entitled to use any such titles.

The government would need to further consult on rules based on the final version of the legislation enacted.

Meanwhile, in Ontario, where the title protection framework has been in place since March, 2022, the Financial Services Regulatory Authority of Ontario (**FSRA**) and the New Self-Regulatory Organization of Canada (**New SRO**) are continuing to look at how the New SRO can become a credentialing body for financial advisors. Approved credentialing bodies must oversee conduct of their credential holders and enforce compliance with minimum requirements. FSRA, the Ontario Securities Commission (**OSC**) and the New SRO are trying to ensure there is no regulatory duplication, and that the New SRO's fees would be reduced to recognize the fact that the OSC already oversees its activities.

FSRA will continue to maintain a list of existing approved credentialing bodies and credentials on its website and monitors the market for changes in title usage.

BLG's Resource Corner

Our colleagues at BLG have provided the following insights we thought might interest our readers:

- A New Year and a New SRO: Two months in
- Emphasizing risk culture in financial institutions: OSFI releases draft Culture and Behaviour Risk Guideline
- CSA publishes rules for new SEDAR+
- Corporate transparency in Québec: New disclosure obligations coming into force on March 31, 2023
- Less is more - Data minimization and privacy/cyber risk management

For more information, please visit the BLG website.