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CSA ADOPTS NEW INSIDER REPORTING REGIME

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Overview of Proposed National Instrument 55-104 – *Insider Reporting Requirements and Exemptions*

The Canadian Securities Administrators (the “CSA”) have adopted a new insider reporting regime set out in National Instrument 55-104 - *Insider Reporting Requirements and Exemptions* (“NI 55-104”). Provided that all necessary ministerial approvals are obtained (and, in Ontario, certain amendments to the Ontario *Securities Act* are proclaimed into force), NI 55-104 will come into force on April 30, 2010. NI 55-104 is meant to harmonize and streamline insider reporting requirements and exemptions across all Canadian jurisdictions and to focus on insiders who have the most influence over the reporting issuer and the most access to the reporting issuer’s undisclosed material information. While some provisions of NI 55-104 will not apply in Ontario, harmonization between Ontario and the other provinces and territories is expected to be achieved through concurrent amendments to the Ontario *Securities Act*. The following is an overview of NI 55-104.

Reporting Insiders – Focus on Core Group of Insiders

NI 55-104 reduces the number of people that are required to file insider reports by introducing the concept of a “reporting insider”; a person who is not a reporting insider is not subject to the insider reporting requirements. Reporting insiders include:

- The directors, chief executive officer (“CEO”), chief financial officer (“CFO”) and chief operating officer (“COO”) of the reporting issuer or of a “Major Subsidiary” of the reporting issuer. A subsidiary is considered a Major Subsidiary if it accounts for at least 30% of the assets or revenue of the reporting issuer
- A person responsible for a principal business unit, division, or function of the reporting issuer

- “Significant Shareholders” and their directors, CEOs, CFOs and COOs. A Significant Shareholder is a person who has beneficial ownership of, or control or direction over, directly or indirectly, securities of the reporting issuer carrying more than 10% of the voting rights
- “Significant Shareholders based on Post-Conversion Beneficial Ownership” and their directors, CEOs, CFOs and COOs. A Significant Shareholder based on Post-Conversion Beneficial Ownership is a person who is not a Significant Shareholder but who has the right to acquire beneficial ownership of, or control or direction over, securities of the reporting issuer within 60 days, through a convertible security or otherwise, and such person has beneficial ownership of, or control or direction over, directly or indirectly, securities of the reporting issuer carrying more than 10% of the voting rights calculated on a diluted basis
- A management company and its directors, CEO, CFO, COO and Significant Shareholders, if it is established or contracted to provide significant management or administrative services to the reporting issuer or a Major Subsidiary of the reporting issuer
- Any other insider that in the ordinary course receives or has access to material undisclosed information concerning the reporting issuer as well as significant influence over the reporting issuer.

The underlying concept of the “reporting insider”, as illustrated by the categories of persons listed above, is that only persons who have regular access to material undisclosed information and significant influence over the reporting issuer are required to file insider reports. Under the current regime, in contrast, all directors and officers of a reporting issuer or its subsidiaries are subject to the insider reporting requirements, regardless of their access to material undisclosed information or influence over the reporting issuer, unless a specific

exemption is available. In addition, the current framework brings all subsidiaries of the reporting issuer into the insider reporting regime, while NI 55-104 imposes insider filing obligations just in relation to Major Subsidiaries. Requiring insider reports from a core group of persons is intended to produce more meaningful insider disclosure without affecting the quality of the information disclosed. This streamlining is designed to promote simplicity and transparency. The overall reduction of the volume of insider reports in conjunction with the dissemination of material insider information is meant to not only be beneficial to investors but also reduce the administrative burden and costs for reporting issuers and insiders.

Reporting Insiders – Nature of Interest Reportable

Although the “reporting insider” concept reduces the number of persons who are subject to the insider reporting requirements, NI 55-104 increases the nature of the interest of the reporting insider subject to disclosure. The introduction of the concept of the “Significant Shareholder based on Post-Conversion Beneficial Ownership” is aimed at preventing persons from avoiding the insider reporting requirements by acquiring convertible securities instead of voting securities of the reporting issuer.

A reporting insider must also disclose its interest or obligations in connection with a “related financial instrument”. Related financial instruments include forward contracts, stock purchase contracts or similar contracts involving securities of the reporting issuer, and stock-based compensation such as phantom stock units, deferred share units, restricted share awards, performance share units and stock appreciation rights.

If a reporting insider enters into, materially amends or terminates an agreement that has the effect of altering the reporting insider’s “economic exposure” to the reporting issuer, and the agreement involves a security of the reporting issuer or related financial instrument, the reporting insider must disclose the agreement in an insider report.

Acceleration of Reporting Deadline from 10 Days to Five Days

The deadline for a reporting insider to report any changes with respect to its interest in the securities of a reporting issuer has been reduced from 10 days to five days. The 10-day deadline for when a reporting insider must file its first insider report upon becoming a reporting insider is preserved. It is anticipated that NI 55-104 will come into force on April 30, 2010. Insider reports for transactions which occurred on or before October 31,

2010, may be filed within 10 days of the event (as opposed to five days). This transition period gives reporting insiders and reporting issuers time to become familiar with the requirements of NI 55-104.

The reduction of the filing deadline from 10 days to five days addresses some concerns with respect to the backdating and/or manipulation of stock option grants. Some commentators on NI 55-10,4 when it was at the proposal stage, suggested that the filing window should be reduced to two days (as it is in the United States), while others were of the view that a five-day filing deadline strikes a proper balance between the need for timely disclosure and the administrative burden of filing insider reports. The CSA concluded that the recent media attention with respect to sanctions have made reporting issuers and insiders aware of their obligations in regard to stock options.

Consolidation, Simplification and Consistency of Insider Reporting Requirements

The current insider reporting requirements are found in a number of different instruments. NI 55-104 clarifies and simplifies the insider reporting requirements by consolidating them into a single instrument. Upon the coming into force of NI 55-104, the following will be repealed:

- National Instrument 55-101 - *Insider Reporting Exemptions* and its Companion Policy;
- Multilateral Instrument 55-103 - *Insider Reporting for Certain Derivative Transactions (Equity Monetization)* and its Companion Policy; and
- In British Columbia, BCI 55-506 - *Exemption from Insider Reporting Requirements for certain Derivative Transactions*.

Under the current regime, stock-based compensation agreements, depending on how they are characterized, are treated differently by the instruments above. The CSA has taken the “substance over form” approach and introduces, in NI 55-104, a broad definition of “compensation arrangement”. The definition includes options, stock appreciation rights, phantom shares, restricted shares or restricted share units, deferred share units, performance units or performance shares, stock dividends, warrants, convertible securities, or similar instruments that may be received or purchased as compensation for services rendered or otherwise in connection with holding an office or employment with a reporting issuer or its subsidiary. This inclusive

definition is meant to ensure that the insider reporting requirements will be applied consistently for all stock-based compensation.

Issuer Grant Report

Reporting issuers may facilitate certain insider reporting by filing an issuer grant report on SEDI within five days of the grant of stock options or other stock-based compensation. Pursuant to NI 55-104, reporting insiders who acquire securities under a compensation arrangement established by the reporting issuer or its subsidiary are not subject to the normal insider reporting requirements, provided that the reporting issuer has disclosed the material terms of the compensation arrangement on SEDAR, the reporting issuer has filed an issuer grant report on SEDI with respect to the transaction, and the reporting insider complies with the prescribed alternative reporting requirements.

Under the alternative reporting requirements, a reporting insider must file an insider report within five days of the disposition of the securities acquired under the compensation arrangement or, in the case of securities acquired under the compensation arrangement that have not been disposed of, by March 31, in the calendar year following the year of acquisition.

Effectively, the issuer grant report provisions permit a reporting issuer to relieve its reporting insiders of the burden of the insider reporting requirements by allowing the reporting insiders to make a single annual filing with respect to stock options or other stock-based compensation.

NI 55-104 includes additional timing relief under certain circumstances for the reporting of dispositions of securities acquired under a compensation arrangement, if the disposition does not involve a discreet investment decision or is made to satisfy a tax withholding obligation and is carried out under predetermined terms.

Additional Information on NI 55-104

In connection with the adoption of NI 55-104, the CSA will also be amending CSA Staff Notice 55-308 - *Questions on Insider Reporting* and CSA Staff Notice 55-310 - *Questions and Answers on the System for*

Electronic Disclosure by Insiders (SEDI), both of which will be available on the websites of the securities commissions. These publications may be of interest to investors, insiders and issuers interested in becoming familiar with the new insider reporting regime.

CONTACT US

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