ALBERTA SECURITIES COMMISSION
NOTICE

MULTILATERAL INSTRUMENT 55-103 AND COMPANION POLICY 55-103CP

INSIDER REPORTING FOR CERTAIN DERIVATIVE TRANSACTIONS (EQUITY MONETIZATION)

February 28, 2003

Introduction

The Alberta Securities Commission approved Multilateral Instrument 55-103 *Insider Reporting for Certain Derivative Transactions (Equity Monetization)* and Companion Policy 55-103CP for publication for a comment period of 90 days.

The proposed Multilateral Instrument and Companion Policy are initiatives of the Canadian Securities Administrators (the CSA). The CSA have developed the Multilateral Instrument and Companion Policy to respond to concerns that the existing insider reporting requirements may not cover certain derivative-based transactions, including equity monetization transactions (described below), which satisfy one or more of the fundamental policy rationale for insider reporting. We believe that timely public disclosure of such transactions is necessary in order to maintain and enhance the integrity of and public confidence in the insider reporting regime in Canada.

The Multilateral Instrument is expected to be adopted as a rule in each of Alberta, Manitoba, Ontario and Nova Scotia, a Commission regulation in Saskatchewan, and a policy in most other jurisdictions represented by the CSA. The Companion Policy is expected to be implemented as a policy in most jurisdictions represented by the CSA. The British Columbia Securities Commission has participated in developing the proposed Multilateral Instrument and Companion Policy, but has decided to implement similar requirements by seeking amendments to the British Columbia *Securities Act* instead. Consequently, British Columbia will not be adopting the Multilateral Instrument and Companion Policy.

Substance and Purpose of the Multilateral Instrument and Companion Policy

1. Purpose of the Multilateral Instrument

The Multilateral Instrument seeks to maintain the integrity of and public confidence in the insider reporting regime by:

- ensuring that insider transactions which have a similar effect in economic terms to insider trading activities are fully transparent to the market;

- ensuring that, where an insider enters into a transaction which satisfies one or more of the policy rationale for insider reporting, the insider is required to file an insider report, even though the

transaction may, for technical reasons, fall outside of the existing rules governing insider reporting; and

- reducing uncertainty relating to what arrangements and transactions are subject to an insider reporting requirement and what are not.

2. What are equity monetization transactions?

Equity monetization transactions are transactions which allow an investor to receive a cash amount similar to proceeds of disposition, and to transfer part or all of the economic risk and/or return associated with securities of an issuer, without actually transferring the legal and beneficial ownership of such securities. The term "monetization" generally refers to the conversion of an asset (such as securities) into cash.

We are concerned that, if an insider of a reporting issuer enters into a monetization transaction, and does not disclose the existence or material terms of this transaction, there is potential for harm to investors and to the integrity of the insider reporting regime because:

- an insider in possession of material undisclosed information, although prohibited from trading in securities of the issuer, may be able to profit from such information by entering into derivative-based transactions which mimic trades in securities of the reporting issuer;

- market efficiency will be impaired since the market is deprived of important information relating to the market activities of the insider; and

- requirements relating to the public reporting of such holdings (e.g., in an insider report or proxy circular) may in fact materially mislead investors, since the insider's publicly reported holdings no longer reflect the insider's true economic position in the issuer.

Although we believe that many such transactions fall within the existing rules governing insider reporting, we recognize that, in certain cases at least, there may be a genuine question whether the existing insider reporting rules apply. Accordingly, we have developed the Multilateral Instrument to address these concerns. The Multilateral Instrument reflects a principles-based approach to monetization transactions. If an insider enters into a transaction which satisfies one or more of the policy rationale for insider reporting, but for technical reasons, it may legitimately be argued that the insider falls outside of the existing insider reporting requirements, the insider will be required to file an insider report under the Multilateral Instrument. In this way, the market can make its own determination as to the significance, if any, of such arrangements.

3. When does the Multilateral Instrument apply?

If you are an "insider" of a reporting issuer, and you enter into an agreement, arrangement or understanding of any kind which

- changes your "economic exposure" to your reporting issuer, or

- changes your "economic interest in a security" of your reporting issuer,

and you are not required under any other provision of Canadian securities law to file an insider report about this agreement, arrangement or understanding, you must file an insider report under the Multilateral Instrument, unless you are covered by one of the exemptions.

The terms "economic exposure" and "economic interest in a security" are defined in the Multilateral Instrument. Additional guidance is provided in the Companion Policy. The concept of "economic exposure" also appears in section 6.2 of National Policy 46-201 *Escrow for Initial Public Offerings*. The definition of "economic interest in a security" has been drafted to be generally consistent with the definition of "pecuniary interest" which appears in the U.S. insider reporting requirements.

4. Exemptions

The Multilateral Instrument contains a number of broad exemptions. These include:

- arrangements which do not involve, directly or indirectly, a security of the reporting issuer or a derivative which involves a security of the reporting issuer;

- a compensation arrangement such as a phantom stock plan, deferred share unit ("DSU") plan or stock appreciation right ("SAR") plan which would otherwise be caught by the Instrument if:

    i) the existence and material terms of the compensation arrangement are disclosed in any public document (such as the annual audited financial statements of the issuer or an annual filing made under any provision of Canadian securities legislation);

    or

    ii) the material terms of the compensation arrangement are set out in a written document, and the alteration to economic exposure or economic interest referred to in section 2.1 occurs as a result of the satisfaction of a pre-established condition or criteria described in the document, and does not involve a discrete investment decision by the insider.

- a person or company exempt from the insider reporting requirements under a provision of NI 55-101, to the same extent and on the same conditions as are applicable to such exemption;

- a person or company who has obtained exemptive relief in a jurisdiction from the insider reporting requirements of that jurisdiction, to the same extent and on the same conditions as are applicable to such exemptive relief; and

- a transfer, pledge or encumbrance of securities by a person or company for the purpose of giving collateral for a debt made in good faith so long as there is no limitation on the recourse available against the person or company for any amount payable under such debt.

5. Pre-existing arrangements which continue to have effect after the coming into force of the Multilateral Instrument

The Multilateral Instrument contemplates that, in certain circumstances, it will be necessary for insiders to disclose the existence of pre-existing monetization arrangements.

If an insider of a reporting issuer, prior to the effective date of the Multilateral Instrument,

- entered into an agreement, arrangement or understanding in respect of which the insider would have been required to file an insider report under this Instrument if the agreement, arrangement or understanding had been entered into on or after the effective date,

  and

- the agreement, arrangement or understanding remains in effect on or after the effective date of the Instrument,

then the insider will be required to file a report under the Instrument.

We believe it is necessary for the Multilateral Instrument to address pre-existing arrangements which continue in force after the effective date. If insiders are not required to disclose such pre-existing arrangements, the market will have no way of determining whether an insider's publicly reported holdings truly reflect the insider's economic position in the insider's reporting issuer.

For example, if an insider, *before* the Multilateral Instrument comes into force, enters into a monetization arrangement which has the effect of divesting the insider of substantially all of the economic risk and return associated with the insider's securities in the reporting issuer, and the insider then files an insider report *after* the Multilateral Instrument comes into force that indicates that the insider continues to have a substantial ownership position in the issuer, we believe the pre-existing arrangement will render the insider report (and all future insider reports) materially misleading. The insider report will not convey an accurate picture of the insider's true economic position in the issuer.

6. Method of Reporting

An insider will file the same form of insider report as he or she would in the case of an ordinary purchase or sale of securities of the reporting issuer in question.

A CSA staff notice containing examples of various types of monetization arrangements, together with examples of completed forms for such arrangements, will be published on or before the time the Multilateral Instrument takes effect. The staff notice will also explain how such arrangements should be reported under the System for Electronic Disclosure by Insiders (SEDI).

Authority for the Proposed Multilateral Instrument

In those jurisdictions in which the proposed Multilateral Instrument is to be adopted as a rule or regulation, the securities legislation in each of those jurisdictions provides the securities regulatory authority with rule-making or regulation-making authority in respect of the subject matter of the proposed Multilateral Instrument.

The proposed Multilateral Instrument is being proposed for implementation in Alberta as a rule. In Alberta, the following provisions of the *Securities Act* (Alberta) (the Act) provide the Alberta Securities Commission (the Commission) with authority to adopt the proposed Multilateral Instrument as a rule:

- Paragraph 223(b) of the Act authorizes the Commission to make rules requiring any information, documents, records or other materials to be filed, furnished or delivered.

- Paragraph 223(g) of the Act authorizes the Commission to make rules governing derivatives.

- Paragraph 223(t) of the Act authorizes the Commission to make rules governing insider trading and self-dealing including rules that modify, vary or restrict any requirements under Part 15 *Insider Trading and Self-dealing.*

- Paragraph 223(v) of the Act authorizes the Commission to make rules governing the format, preparation, form, contents, execution, certification, dissemination and other use, filing, review and public inspection of all information, documents, records or other materials required under or governed by the Act.

Alternatives Considered

We have developed the Multilateral Instrument to respond to concerns that the existing insider reporting requirements in Canadian securities legislation may not in all cases cover certain derivative-based transactions, including equity monetization transactions, which satisfy one or more of the fundamental policy rationale for insider reporting. At the outset of this initiative, we considered a number of alternative approaches to address these concerns, including proceeding by way of technical amendments to the definition of "beneficial ownership" in Canadian securities legislation to address such transactions. However, in view of the fact that such transactions may be structured in a wide variety of ways, and the fact that such transactions may be expected to continue to change over time, we concluded that a principles-based approach tied to the rationale for insider reporting was preferable.

We have also considered proceeding by way of enforcement action in connection with certain types of transactions with a view to removing any ambiguity as to the application of the existing insider reporting requirements to such transactions. Although we believe that many such transactions fall within the existing rules governing insider reporting, we recognize that, in certain cases at least, there may be a genuine question whether the existing insider reporting requirements apply. Consequently, we believe that the Multilateral Instrument and Companion Policy will assist market participants by reducing uncertainty relating to what arrangements and transactions are subject to an insider reporting requirement and what are not. Adoption of the Multilateral Instrument and Companion Policy does not preclude the Commissions from taking enforcement action in appropriate circumstances based on non-compliance with existing legislative requirements.

Unpublished Materials

In proposing the Multilateral Instrument and Companion Policy, the CSA has not relied on any significant unpublished study, report, decision or other written materials.

Anticipated Costs and Benefits

We have developed the Multilateral Instrument and Companion Policy to respond to concerns that the existing insider reporting requirements may not cover certain derivative-based transactions, including equity monetization transactions, which satisfy one or more of the fundamental policy rationale for

insider reporting. We believe that timely public disclosure of such transactions is necessary in order to maintain and enhance the integrity of and public confidence in the insider reporting regime in Canada. We are concerned that, in the absence of such disclosure, the benefits associated with an insider reporting system will be substantially diminished, since there will be no assurance that an insider's publicly reported position in the insider's reporting issuer will reflect the insider's true economic position in that issuer. Consequently, we are of the view that the benefits of the proposed Multilateral Instrument outweigh the costs.

Comments

Interested parties are invited to make written submissions with respect to the proposed Multilateral Instrument. Submissions received by May 31, 2003 will be considered.

Submissions should be sent to all of the Canadian securities regulatory authorities listed below in care of the Ontario Commission, in duplicate, as indicated below:

Alberta Securities Commission
Saskatchewan Securities Commission
The Manitoba Securities Commission
Ontario Securities Commission
Office of the Administrator, New Brunswick
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Department of Government Services and Lands, Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon
Registrar of Securities, Nunavut

c/o John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 800, Box 55
Toronto, Ontario M5H 3S8

A diskette containing the submissions (in DOS or Windows format, preferably Word) should also be submitted. As securities legislation in certain provinces requires that a summary of the written comments received during the comment period be published, confidentiality of submissions received cannot be maintained.

Questions may be referred to any of:

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Text of Proposed Multilateral Instrument and Companion Policy

The text of the proposed Multilateral Instrument and Companion Policy follows, together with footnotes that are not part of the Multilateral Instrument or Companion Policy but have been included to provide background and explanation.