

# Securities Regulation

Doing Business in Canada

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Regulatory requirements imposed by Canadian securities authorities and stock exchanges are generally comparable to U.S. requirements. In Canada, securities regulation is within provincial jurisdiction. Currently, each of the provinces and territories has securities regulatory legislation. Although the securities regulatory regimes are generally similar within Canada, there is currently no national securities law or national securities regulator.

The Canadian uniform securities regulation system has developed “organically” over time on the basis of increased co-operation between provincial and territorial regulators. Currently, such “organic” development is evidenced by co-ordination among all provincial securities commissions (principally through an umbrella organization known as the Canadian Securities Administrators or “**CSA**”) in formulating “national instruments” and “national policies” which have been adopted by each of the provincial and territorial securities regulators. Further, with the adoption of the “principal regulator” or “passport” system by each province and territory of Canada (other than Ontario), many aspects of securities law are effectively regulated by one participating jurisdiction in addition to Ontario. In addition, the national electronic filing system (known as “**SEDAR+**”) (the Canadian equivalent to EDGAR) and the passport system encourages regulators to delegate responsibilities to one another.

Canada has a national registration database (“**NRD**”) system, which is a web-based system that permits dealers and advisers to file registration forms electronically and to deal with one principal regulator in connection with initial registration, amendments to registration and approval or review of certain sponsored individuals. Non-resident firms are not permitted to use the NRD system due to differing requirements across Canada for non-residents.

## PROSPECTUS REQUIREMENT

A “security” is broadly defined, similar to but even broader than the U.S. definition, to be any document evidencing title to or an interest in, among other things, the capital, assets, profits or property of a person or corporation. In addition, a number of different types of agreements and instruments involving monetary consideration are specifically included in the definition of “security,” including, among other things, secured and unsecured notes, stocks, treasuries, bonds, debentures, options or privileges on a security.

Provincial and territorial securities laws generally require the filing of a prospectus to qualify any

“distribution” of securities, subject to the availability of a prospectus exemption. A distribution of securities includes, among other things, a trade by an issuer in previously unissued securities and a trade in securities from a person that is a “control person” in respect of the issuer. A person (or combination of people acting jointly or in concert) is generally presumed to be a “control person” in respect of an issuer if that person (or combination of people acting jointly or in concert) holds more than 20% of the voting rights attached to the securities of the issuer. In addition, securities legislation of the various Canadian jurisdictions deems certain trades in securities that were previously acquired under an exemption from the prospectus requirements, called “first trades,” to be distributions. Securities of an issuer that is a “reporting issuer” under Canadian securities law that were acquired under an exemption from the prospectus requirements are generally freely tradable, depending on the exemption relied upon, after a four-month hold period.

Any person or corporation engaged in trading or giving advice regarding securities must be registered under the relevant provincial and territorial securities legislation unless an exemption from this requirement is available.

## PROSPECTUS DISCLOSURE

A prospectus must be prepared in accordance with applicable provincial and territorial regulations and must contain “full, true and plain” disclosure of all material facts relating to the securities being offered. In the event that a prospectus contains a misrepresentation, the issuer and each underwriter that signs it may be found liable. An issuer would not be liable if it could prove that the purchaser purchased the securities with knowledge of the misrepresentation. In addition, directors of an issuer and underwriters can also rely on a due diligence defence in order to avoid liability for a misrepresentation.

Upon filing a final prospectus and being receipted therefore, the issuer (assuming it had not already filed a prospectus) will become a “reporting issuer” in each jurisdiction in which a receipt for the prospectus was issued. As a reporting issuer, the issuer is subject to continuous disclosure rules and periodic reporting.

The regulation of trading in the “secondary market” is generally referred to as the “closed system.” In the closed system, every trade that is a “distribution” requires the filing of a prospectus or obtaining a ruling from a securities regulatory authority allowing the trade, unless a prospectus exemption is available.



The resale of securities sold pursuant to a prospectus exemption requires reliance on a further exemption or, if this is not available, on a prospectus – unless a set of resale restrictions is met. Those restrictions are that the issuer of securities is a “reporting issuer” for the four months prior to the trade, that the securities carry a prescribed legend, that the person proposing to sell the securities must have held them for a minimum hold period of four months and that no unusual effort is made to prepare the market for the securities being sold. The system is called “closed” because the security never becomes freely tradable unless a prospectus is filed or, if distributed under a prospectus exemption, until enough time passes to allow information about the issuer and the security to be disseminated in the marketplace.

## EXEMPTIONS FROM THE PROSPECTUS REQUIREMENT

The existing exempt offering regimes in Canada’s various jurisdictions have been consolidated in National Instrument 45-106 – Prospectus Exemptions (commonly known as “**NI 45-106**”), which is designed to generally harmonize the prospectus and registration exemptions contained in provincial statutes and instruments.

The most useful existing exemptions for an entity financing a business in Canada are the following exemptions:

(a) the “accredited investor” exemption permits certain qualified investors, including institutional investors and persons or companies that meet income or asset tests (and who, if they are an individual, have completed a prescribed Risk Acknowledgement Form) to purchase securities without a prospectus; no minimum amount must be invested and accredited investors are able to re-sell securities in any dollar amount to other accredited investors; (b) the “substantial purchase” exemption permits a person (though not an individual) to acquire securities on a prospectus and registration exempt basis where each purchaser invests no less than \$150,000 paid in cash; (c) the “asset acquisition” exemption permits a person to acquire securities on a prospectus and registration-exempt basis where the purchaser satisfies the purchase price by transferring assets with a fair market value of no less than \$150,000; and (d) the “private issuer” exemption.

In November 2022, Canadian securities regulators adopted a new prospectus exemption applicable to reporting issuers called the “listed issuer financing exemption” (commonly referred to as the LIFE exemption) pursuant to which certain reporting

issuers may distribute freely tradable equity securities without a prospectus. Subject to certain conditions, the LIFE exemption allows reporting issuers listed on a Canadian exchange to raise the greater of \$5 million or 10% of the issuer’s market capitalization to a maximum total dollar amount of \$10 million in a 12-month period by distributing securities to investors. Unlike most prospectus exemptions, securities issued under the LIFE exemption are not subject to a customary four-month hold period.

In the case of certain exempt trades, it may be necessary to file a report and pay a fee to the relevant securities regulator. To rely on certain prospectus and registration exemptions (although not the accredited investor, substantial purchase or asset acquisition exemption), the issuer is required to deliver a disclosure document to prospective investors. Where a disclosure document is provided to an investor (whether required by the exemption or voluntarily) in certain Canadian jurisdictions, including Ontario, securities legislation grants the investor a right of action for damages or rescission if the disclosure document contains a misrepresentation. In addition, a copy of the offering memorandum generally must be filed with the relevant securities regulator.

## CONTINUOUS DISCLOSURE REQUIREMENTS AND OBLIGATIONS

There are generally two kinds of reporting requirements required under Canada’s continuous disclosure regime – “periodic” and “timely.” Periodic reporting requires a reporting issuer to disclose material information by filing disclosure documents such as financial statements, annual reports, annual information forms and proxy circulars. Conversely, timely reporting requires a reporting issuer to disclose material changes as they occur, through press releases and material change reports. “Insiders” of a reporting issuer (i.e., officers, directors and shareholders of more than 10%) must also report any trade they might make in a reporting issuer’s securities within five days of the trade in question (the initial insider reports continue to be required to be filed within 10 days of the trade) and insiders that are 10% or over shareholders must file an additional “early warning report” following certain trades (see Takeover Bids below). Failure to report may result in daily monetary penalties, depending on provincial jurisdiction.

National Instrument 51-102 – Continuous Disclosure Obligations (commonly known as “**NI 51-102**”) was introduced to provide a harmonized set of continuous disclosure requirements for reporting

issuers across Canada (other than investment funds) and, generally speaking, sets out the obligations of reporting issuers relating to business acquisitions, annual information forms (“AIFs”), material change reporting, management discussion and analysis (“MD&A”), information circulars, proxies and other disclosure matters. The board of a reporting issuer is required to approve both interim, unless this function is delegated to the audit committee of the board, and annual financial statements prior to their release, and MD&As must include discussions of, and provide a comparative analysis of, all financial transactions, including all off-balance sheet transactions, as well as providing information about critical accounting estimates and facts that are required for a better understanding of the issuer’s affairs.

## CORPORATE GOVERNANCE PRACTICES

The CSA has adopted a uniform set of corporate governance rules and policies. These rules and policies generally require reporting issuers to disclose their corporate governance practices by way of disclosure in their information circulars or AIFs and to be filed on SEDAR+.

Other CSA policies are designed to provide “guidance” on corporate governance practices. This guidance, or best practices, constitutes recommendations relating to board independence, the role of a board in its management of board members, etcetera.

## LIABILITY FOR SECONDARY MARKET DISCLOSURE

Ontario legislation grants certain rights of action to investors who purchase or sell securities from third parties in the market (commonly known as the “secondary market”) as opposed to investors who purchase securities from an issuer (commonly referred to as the “primary market”). This legislation creates an offence for fraud, market manipulation and misleading or untrue statements. The legislation also introduces a regime for statutory civil liability by providing a cause of action in respect of a misrepresentation by or on behalf of a responsible issuer in its disclosure documents, whether oral or written, and a responsible issuer’s failure to make timely disclosure of a material change. This legislation creates a statutory right of action without regard to whether the purchaser or seller relied on any alleged misrepresentation, which is different from the common law cause of action for negligent misrepresentation which requires detrimental reliance.

## STOCK EXCHANGES IN CANADA

Canada has four main securities exchanges on which debt or equity securities can be listed for trading: Toronto Stock Exchange (“TSX”), the TSX Venture Exchange (the “TSXV”), Canadian Securities Exchange (“CSE”) and the Cboe Canada (formerly NEO Exchange) (“Cboe”). The TSX is Canada’s largest stock exchange and also oversees and administers the Montréal Exchange (primarily a derivatives exchange) and the TSXV, which is a listed exchange for more junior companies. The CSE is focused also on listing microcap and emerging companies, as it offers simplified listing processes and is generally considered to impose less onerous reporting and continued listing requirements on its issuers. Cboe is a senior stock exchange that is majority-owned by large institutional investors and in addition to listing its own securities, trades all TSX, TSXV and CSE securities.

## TAKEOVER BIDS

The regulation of takeover bids in Canada is governed by the applicable provincial and territorial securities statutes in Canada’s various provinces and territories. A takeover bid in Canada is generally defined as an offer to acquire outstanding voting securities or equity securities of an issuer that would bring the “offeror’s securities” to 20% or more of the class in question. In this context, “offeror’s securities” include securities beneficially owned or over which control or direction is exercised by the offeror or persons acting jointly and/or in concert with the offeror. A purchase resulting in a holding of less than 20% of the relevant class of securities will not constitute a takeover bid even if the bidder obtains effective control of the company.

An “early warning” notification system is imposed once 10%, but less than 20%, of the voting or equity securities of a reporting issuer is acquired. In this case, every person (or persons acting jointly or in concert) acquiring 10% or more of the voting or equity securities of a reporting issuer is required to immediately issue a press release containing certain prescribed information and to file an “early warning report” in prescribed form within two business days of the acquisition in question. A further press release and early warning report is required whenever an additional 2% of the outstanding securities is acquired or disposed of by a person holding 10% or more on a partially diluted basis.

A takeover bid must be made in compliance with the substantive and procedural requirements of the regulating statute of the applicable province or territory in the absence of an exemption from the takeover bid requirements. Generally speaking,

a takeover bid offer is to be made to all security holders of a given class on identical terms. A formal offer requires preparation of a takeover bid circular satisfying certain statutory disclosure requirements, which circular must be sent to all shareholders of the target. However, it is not necessary to make an offer for all shares and the offeror may determine the number of shares for which it wishes to bid, subject to a mandatory minimum tender requirement of more than 50% of the outstanding securities of the class that are subject to the bid, excluding those beneficially owned, or over which control or direction is exercised, by the bidder and its joint actors. On a partial bid, shares must be taken up pro-rata to those tendered to the offer. Conditions, other than financing, may be attached to the bid. For instance, it is common to make a purchase conditional upon obtaining a minimum level of acceptance, frequently two-thirds (the threshold for approval of certain fundamental corporate transactions in most jurisdictions) or 90% (the level which gives the offeror the right to acquire the balance of the shares outstanding). Subject to certain exemptions which may shorten the period, a takeover bid must remain open for a minimum deposit period of 105 days. Furthermore, after the minimum tender requirement has been achieved and all other terms and conditions of the bid have been complied with or waived, bids are required to be extended by the offeror for an additional 10 days.

There are various statutory exemptions from the takeover bid requirements and the provincial and territorial securities statutes provide securities regulatory authorities with discretion to exempt takeover bids from full bid compliance. The most commonly relied upon takeover bid exemptions under the provincial and territorial securities statutes are: (a) purchases and private agreements from not more than five persons where the consideration paid does not exceed 115% of the market price (as defined for the securities at the date of purchase); and (b) acquiring, at market prices, within any period of 12 months not more than 5% of the outstanding securities of a class measured at the commencement of the 12-month period.

In addition to the takeover bid regime, there are two other typical structures that can be used to acquire 100% of a public company, namely: (a) a plan of arrangement (which is effected under court supervision and requires the approval of two-thirds of those shareholders voting on whether to amalgamate); and (b) an amalgamation squeeze-out (which requires the approval of two-thirds of the votes of the shareholders voting on the question). In both the plan of arrangement and in an amalgamation squeeze-out, the shareholders

may, under certain circumstances and within the prescribed time, effect “dissent” rights and demand that you pay fair value if they have a concern that the amount to be paid is not fair value.

In addition, the CSA has promulgated rules regarding related party transactions, insider bids and going private transactions. The essence of these rules is that if such a transaction (which is based on the economic result and not on the form) is contemplated, then the process must be overseen by an independent committee of the board of directors, a valuation must be done by an independent valuator and there must be a vote of the approval of the “majority of the minority shareholders,” with the last two requirements subject to certain prescribed exemptions.

## CAPITAL POOL COMPANIES

The Capital Pool Company program is a unique two-stage listing process offered by the TSXV which brings together experienced participants in public capital markets with entrepreneurs seeking funding and a public listing. In stage one of the process, a new shell company (known as a “**Capital Pool Company**”) is listed on the TSXV by way of an initial public offering (the “**CPC IPO**”).

A financing, through an agent who is registered under applicable securities laws, must be completed in conjunction with the CPC IPO. The gross proceeds of the CPC IPO plus all subsequent private placements prior to the Qualifying Transaction (as hereafter defined), must not exceed \$10 million.

In stage two (the “**Qualifying Transaction**”), the Capital Pool Company identifies a suitable asset or business. In order to be accepted by the TSXV, the proposed company resulting from the Qualifying Transaction (also known as the Resulting Issuer) must be able to meet the initial listing requirements set out in the TSXV’s policies. If the acquired business can meet the minimum listing requirements of the TSX, it can be directly listed on the TSX at the closing of the Qualifying Transaction.

In many cases, taking a business or asset public in Canada through the Capital Pool Company program can be a more cost and time efficient alternative than a listing through a traditional initial public offering. Recent changes to the Capital Pool Company program effective from January 1, 2021, have provided greater flexibility and simplicity to the program by reducing the regulatory burden and relaxing certain requirements.

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