

December 6, 2017

Cindy Petlock  
Chief Legal Officer  
Aequitas NEO Exchange Inc.  
155 University Avenue, Suite 400  
Toronto, ON M5H 3B7  
Sent via e-mail to: legal@neostockexchange.com

Market Regulation Branch  
Ontario Securities Commission  
20 Queen Street West, 22<sup>nd</sup> Floor  
Toronto, ON M5H 3S8  
Sent via e-mail to: marketregulation@osc.gov.on.ca

---

**RE: Aequitas NEO Exchange Listing Manual Amendments for Emerging Market Issuers (“EMIs”)**

---

FAIR Canada is pleased to offer comments on Aequitas NEO Exchange’s Consultation Paper on proposed amendments to the NEO Exchange Listing Manual for new initial listing and ongoing requirements for Emerging Market Issuers (“EMIs”) (the “**Consultation Paper**”).

FAIR Canada is a national, charitable organization dedicated to putting investors first. As a voice of Canadian investors, FAIR Canada is committed to advocating for stronger investor protections in securities regulation. Visit [www.faircanada.ca](http://www.faircanada.ca) for more information.

**1. FAIR Canada Calls for Review of Adequacy of Framework Surrounding Emerging Market Issuers Listed in Canada**

- 1.1. Aequitas NEO Exchange Inc. (“NEO”) is proposing a set of listing requirements so that it can accept listing applications from EMIs. The TSX and TSX-V and CSE also have guidance/policies for the listing of EMIs. FAIR Canada’s comments on NEO’s Consultation Paper should be viewed as equally applicable to the other Canadian exchanges.
- 1.2. There have been significant problems with certain EMIs in Canada and in the U.S. in recent years<sup>1</sup>, most notably, in Canada, the fraud at Sino-Forest Corporation in 2011. Sino-Forest, at its peak, was a company with a \$6 billion market capitalization. Enforcement proceedings in

---

<sup>1</sup> The Wall Street Journal reported that the SEC had filed about 25 enforcement cases against Chinese firms and their executives that faced accounting questions ranging from allegations of embezzlement and inflated revenues to a lack of proper disclosure to investors. See February 6, 2015, WSJ, “SEC, Big Four Accounting Firms in China Settle Dispute; Deal Over Refusal to Turn Over Audit Documents Lifts Threat of Suspension” by Michael Rapoport.

relation to Sino-Forest and certain individuals including its CEO are still ongoing (as the sanctions hearing is yet to occur) although the company and certain of its individuals have been found by the Ontario Securities Commission (“OSC”) to have engaged in deceitful or dishonest conduct related to Sino-Forest’s standing timber assets and revenue which they knew constituted fraud. In the 1990s similar problems were experienced with Chinese EMIs and with EMIs from other jurisdictions (including Semi-Tech, YBM Magnex, Noble China and South China Tire).

- 1.3. As a result of concerns about some EMIs in Canada’s capital markets, and given the increasingly globalized marketplace and corresponding need to focus on investor protection and integrity of our markets, the OSC carried out a regulatory review of EMIs in 2011. In 2012 the OSC issued OSC Staff Notice 51-719, Emerging Markets Issuer Review and OSC Staff Notice 51-720, Issuer Guide for Companies Operating in Emerging Markets. In addition, the TSX and TSX-V conducted a consultation on EMIs in 2013 and issued guidance applicable to them in July 2015.
- 1.4. FAIR Canada recommends that Canadian securities regulators conduct a follow up review of EMIs that are listed on Canadian exchanges and have significant business operations in emerging market jurisdictions to determine if the OSC’s recommendations and guidance, and the present listing standards on Canada’s exchanges have addressed the systemic issues that were identified. Is the quality and adequacy of EMI disclosure and corporate governance practices where we want it to be, and are the gatekeeper roles played by auditors, underwriters and exchanges being discharged in a manner that results in adequate investor protection and integrity of our markets?
- 1.5. FAIR Canada urges the follow-up review to include: (i) benchmarking to other jurisdictions’ approaches to addressing issues related to EMIs; (ii) conducting an empirical analysis regarding the amounts raised in Canada by EMIs and their share price and market capitalization performance over time; and (iii) an analysis of the difficulty Canadian regulators presently face in dealing with compliance and the requisite investigation of and enforcement action against EMIs, including the costs associated with regulating EMIs as well as the difficulties in pursuing criminal enforcement of fraud against EMIs.
- 1.6. The effectiveness of securities regulation is dependent on the ability of regulators to enforce compliance and to take effective enforcement action (including the use of criminal authorities) against persons and companies that breach securities laws. Canadian-based issuers and their directors and senior management are required to comply with Canadian securities laws and, if they fail to do so, regulators can investigate and take enforcement action.
- 1.7. Experience has shown that Canadian regulators are often not able to mandate compliance, conduct proper investigations, or take effective enforcement action against EMIs and their directors and senior management. Furthermore, the investigations tend to be very costly compared to domestic investigations.
- 1.8. The Sino-Forest enforcement proceeding has been one of the most lengthy hearings in the OSC’s history, the merits hearing taking almost 200 hearing days and involving over 22,000 pages of transcripts and 2,000 exhibits. It should be noted that the hearing would arguably have been longer and more complex had a no-contest settlement agreement not have been entered into with the auditors, Ernst & Young LLP. In the sanctions hearing still to come, the

OSC has the power to ban the individuals from serving as directors or officers in Canada and levy administrative monetary penalties and order payment of costs. However, given that the individuals are not resident in Canada and collection of such penalties and costs is difficult, the effectiveness of such sanctions is questionable.

- 1.9. FAIR Canada recommends that EMIs not be listed unless there are adequate arrangements between Canadian and the EMI's principal securities regulator to ensure the ability of Canadian regulators to effectively investigate and take enforcement action if necessary.
- 1.10. Fundamentally, the question should be asked as to what have been the costs and benefits of listing EMIs in Canada for Canadian investors versus what have been the costs and benefits to the EMIs, and the Canadian financial industry and the integrity of Canadian capital markets? Ultimately, is the damage to confidence in the integrity of our markets and regulatory system worth the benefits of listing EMIs and have Canadian investors, overall, benefitted in terms of attractive investment opportunities or have they experienced negative returns and/or significant losses from EMIs listed in Canada?
- 1.11. The challenges that have been identified with EMIs are significant and include the following:
  - (a) Corporate governance concerns.
  - (b) Adequacy of required disclosure.
  - (c) Effectiveness of internal controls and risk management systems.
  - (d) Risks arising from geo-political factors such as government instability or changing policies, legal and regulatory frameworks which may be less developed, ability to move or convert currency out of the foreign jurisdiction, legal title to assets, and differences in business culture and business practices.
  - (e) Complex ownership or contractual arrangements in response to laws in some jurisdictions that limit the ownership of assets by foreign entities that may result in (i) the compromising of the control over assets by the issuer if the structure requires that legal ownership of the issuer's operating assets be vested in a non-affiliated entity; (ii) limitations on the ability of shareholders to have recourse against the assets of the issuer; and (iii) inadequate public disclosure of the nature, material characteristics and risks associated with the structure.
  - (f) Reliance on individuals outside of Canada, which raises the risk of transactions benefitting those individuals.
  - (g) Lack of ability of a company or auditor to verify information or opinions about the entity's operations and performance provided by experts or professionals in overseas jurisdictions including lack of ability by the Canadian audit firm, or regulators or Canadian Public Accounting Board to review working papers or inspections of emerging market auditors; and the adequacy of disclosure when there is a change of auditor.
  - (h) Language issues impacting governance, due diligence and gatekeeper roles.

and

- (i) The adequacy of due diligence performed by underwriters and adequacy of the listing processes used by exchanges and the appropriateness of reliance upon work and due diligence performed by sponsors.<sup>2</sup>

1.12. FAIR Canada believes that in order to ensure the integrity of our markets and adequate investor protection and confidence in our markets, it is appropriate to review the steps that have been taken to address the identified issues and see the extent to which gaps still remain.

## **2. FAIR Canada’s Specific Comments on Aequitas’s Consultation Paper**

2.1. The Consultation Paper states there will be no impact on capital markets or there will only be a positive impact resulting from its listing of EMIs. FAIR Canada requests that the exchanges and the CSA examine whether providing EMIs the ability to choose to list amongst a greater number of exchanges within Canada will benefit our capital markets and foster greater market integrity and monitor the ongoing impact of listed EMIs.

2.2. FAIR Canada recommends that all listed EMIs be required to have a minimum level of comprehensive directors and officers’ insurance (provided by an insurer in Canada) so that there is financial recourse available in the event of malfeasance or other non-compliance resulting in significant financial losses to investors.

### **Definition of Emerging Market**

2.3. FAIR Canada questions whether each exchange should be able to define for itself what is an Emerging Market or whether there should be one consistent definition for all the exchanges and ideally, for all the different provincial and territorial securities regulators as well. It is confusing to investors for an issuer to be categorized as being from an Emerging Market by one exchange or regulator and not by another.

2.4. For example, the TSX-V defines an Emerging Market to mean any jurisdiction outside of Canada, the United States, Western Europe, Australia and New Zealand with the ability of the exchange, on a case-by-case basis to exclude other jurisdictions from the definition.<sup>3</sup> The OSC in Staff Notice 51-719 defined an EMI as those issuers with the following characteristics: (i) whose mind and management are largely outside of Canada and (ii) whose principal active operations are outside of Canada, in regions such as Asia, Africa, South America and Eastern Europe.<sup>4</sup>

---

<sup>2</sup> OSC Staff Notice 51-719, “Emerging Markets Issuer Review”; and Australian Securities & Investments Commission (“ASIC”), August 2013, REP 368, “Emerging market issuers”, available online <http://download.asic.gov.au/media/1344404/rep368-published-3-September-2013.pdf>, ASIC, April 2017, Report 521, “Further review of emerging market issuers”, <http://download.asic.gov.au/media/4211645/rep521-published-6-april-2017.pdf>, TSX Staff Notice to Emerging Market Issuers, July 13, 2015, available online at [http://tmx.complinet.com/en/display/display\\_viewall.html?rbid=2072&element\\_id=918&record\\_id=1117&filtered\\_tag](http://tmx.complinet.com/en/display/display_viewall.html?rbid=2072&element_id=918&record_id=1117&filtered_tag) and

<sup>3</sup> TSX-V Policy 2.10, Listing of Emerging Market Issuers at section 2.1, available online: <https://www.tsx.com/resource/en/1159>.

<sup>4</sup> OSC Staff Notice 51-719, at p. 3.

Australia’s securities regulator defines an Emerging Market to include Eastern Europe, Asia and the Pacific (excluding Singapore, Hong Kong, Japan and New Zealand), Africa, South America, Mexico, Central America, the Caribbean or the Middle East.<sup>5</sup>

- 2.5. NEO’s definition of Emerging Markets provides a list of countries or geo-political regions that are not Emerging Markets and, therefore, a country is an Emerging Market if it is not found on the list. NEO’s definition appears to result in a definition of Emerging Markets that is narrow and excludes such countries as Mexico, the Republic of Korea, Taiwan and South Africa from the definition. The definition also gives NEO the discretion to exclude other jurisdictions from the definition and adjust the list based on very broad factors such as participation in international organizations such as APEC and the G20. This could result in several countries generally accepted as being Emerging Markets being excluded from the definition, for example Argentina and China. FAIR Canada believes a broad definition of what constitutes an Emerging Market fosters better investor protection and integrity of our markets and should be adopted pending a harmonized definition being determined.

#### **Qualifications of Management and Corporate Governance**

- 2.6. FAIR Canada observes that the TSX requirements for an EMI include each of the CEO and CFO and, when taken as a whole, the board of directors, having adequate knowledge and experience with Canadian public company requirements whereas NEO, in section 2.10(5)(a)(i), simply requires that an EMI’s senior management and board of directors, when taken as a whole, have such knowledge and experience. FAIR Canada suggests that both the CEO and CFO should each individually possess such knowledge and experience and that NEO revise its requirements set out therein to at least the same level of that of the TSX.
- 2.7. FAIR Canada recommends that consistent with OSC Staff Notice 51-720, section 2.10(5) should require that the board of an EMI have sufficient understanding of and experience with the cultural and business practices of the emerging market jurisdiction (rather than simply identify such experience) and FAIR Canada recommends that there be at least two independent members of the board with such understanding and experience (rather than one director who could be non-independent).
- 2.8. In addition, exchanges should require that EMIs have robust policies, procedures and processes designed to ensure that EMIs senior management and board of directors have adequate knowledge of cultural and business practices and have mechanisms to ensure that they do not place full reliance on local management or local board members and rather obtain input from other (independent) sources.

#### **Books and Records and Material Agreements**

- 2.9. FAIR Canada recommends that in addition to having a certified English translation of all documents that an EMI is required to file with the exchange, that it also be required that all

---

<sup>5</sup> ASIC, April 2017, Report 521, “Further review of emerging market issuers”, at p. 5.

material agreements be translated into English or French (depending on primary language of the board) so that books and records of the issuer can easily be reviewed and understood.

### **Corporate Governance**

- 2.10. FAIR Canada recommends that there be at least two independent directors with public company experience and significant experience in the EMI's principal business jurisdiction rather than one independent director with experience in one or more Emerging Market jurisdictions generally. Such knowledge and experience should include that of the business operations of the EMI in the principal business jurisdiction along with the culture, laws, financial regulation, local business practices and political landscape of that jurisdiction.
- 2.11. FAIR Canada also recommends that independent directors of an EMI be required to carry out regular site visits, meet with the EMI's local management and advisors, including *in camera* sessions with local auditors.

### **Corporate and Capital Structure**

- 2.12. FAIR Canada recommends that an EMI's public disclosure should, in addition to describing any proposed non-traditional corporate or share capital structure and providing an explanation of why it is necessary, also provide full, true and plain disclosure of the associated risks of the structure and the evaluation of those risks by the company and the controls in place to address those risks.

We thank you for the opportunity to provide our comments and views in this submission. We welcome its public posting and would be pleased to discuss this letter with you at your convenience. Feel free to contact Frank Allen ([frank.allen@faircanada.ca/416-214-3443](mailto:frank.allen@faircanada.ca/416-214-3443)) or Marian Passmore ([marian.passmore@faircanada.ca/416-341-3441](mailto:marian.passmore@faircanada.ca/416-341-3441)).

Sincerely,



Canadian Foundation for Advancement of Investor Rights

cc: Louis Morisset, Chair of the CSA