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THIS EXAMINATION CONSISTS OF **10 PAGES** (INCLUDING THIS PAGE)

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ALLARD SCHOOL OF LAW
UNIVERSITY OF BRITISH COLUMBIA

FINAL EXAMINATION — APRIL 25, 2019

LAW 463.002

SECURITIES REGULATION

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TOTAL MARKS: 100

TIME ALLOWED: 2 HOURS

and 15 minutes reading time

- NOTES:
1. This is an open book examination. Students are permitted to bring excerpts from the *Securities Act* (British Columbia), the Johnston, Rockwell and Ford, *Canadian Securities Regulation* textbook, and any personal notes. No other texts are permitted.
 2. THIS EXAMINATION CONSISTS OF 4 PARTS.

ANSWER ALL PARTS.
 3. Each question is given an approximate time. STUDENTS ARE CAUTIONED TO ALLOCATE THEIR TIME ACCORDINGLY.

PART ONE**(20 Questions – 1 Mark Each – 20 Marks Total)****(approximately 24 minutes)**

TRUE OR FALSE QUESTIONS: Please answer the following questions TRUE or FALSE.

Please only indicate an answer of TRUE or FALSE for each question in this Part One

1. The sale of a previously issued common share by an individual who originally purchased the common share from the issuer pursuant to the accredited investor prospectus exemption is a “distribution”.

TRUE or FALSE?
2. The secondary market disclosure civil liability provisions contained in the *Securities Act* (British Columbia) only apply to reporting issuers.

TRUE or FALSE?
3. A debenture is a security.

TRUE or FALSE?
4. An insider report, in the prescribed form, is required to be filed by every insider of a reporting issuer who has beneficial ownership of, or control or direction over, securities of the reporting issuer or a related financial instrument involving such securities.

TRUE or FALSE?
5. No area of activity governed by securities laws falls within federal constitutional jurisdiction.

TRUE or FALSE?
6. A purchase of more than 20% of the outstanding equity or voting securities of a reporting issuer by a person, or a group of persons acting jointly or in concert, will in every case require either (i) the preparation and filing of a take-over bid circular, in the prescribed form, or (ii) an exemption from the requirement to prepare and file a take-over bid circular.

TRUE or FALSE?

7. A National Instrument does not have the force of law under the *Securities Act* (British Columbia).

TRUE or FALSE?

8. National Instrument 51-102 requires a company which is a reporting issuer to hold an annual meeting of shareholders at least once every year for the purpose for electing directors and appointing auditors.

TRUE or FALSE?

9. The British Columbia Securities Commission is a self-regulatory organization.

TRUE or FALSE?

10. Insider trading is legal in Canada provided that the insider does not use material information which has not been generally disclosed and provided that the insider files an insider report, in the required form.

TRUE or FALSE?

11. A decision of the British Columbia Securities Commission may be appealed to the British Columbia Supreme Court with leave of the Justice of that Court.

TRUE or FALSE?

12. The take-over bid rules set out in National Instrument 62-104 do not apply to an acquisition of more than 20% of the equity or voting securities of a reporting issuer pursuant to an arrangement or amalgamation that requires approval in a vote of the issuer's security holders.

TRUE or FALSE?

13. The "Blue Sky Laws" are generally considered to be early examples of disclosure based regulation in the United States.

TRUE or FALSE?

14. A reporting issuer which has securities listed only on the TSX Venture Exchange is required to file its audited financial statements on SEDAR within 120 days after the end of each fiscal year.

TRUE or FALSE?

15. Advertising the sale of a common share is not a “trade”, as that term is defined in the *Securities Act* (British Columbia), where the person who engaged in the activity of advertising can demonstrate that no sale of the advertised security was ever completed.

TRUE or FALSE?

16. Management of a reporting issuer can legally solicit proxies for use at a meeting of its security holders from up to 15 security holders without an information circular.

TRUE or FALSE?

17. A company becomes a reporting issuer once a preliminary prospectus has been filed and a preliminary receipt has been issued.

TRUE or FALSE?

18. The British Columbia Securities Commission has the authority to make an order imposing sanctions in respect of conduct which does not contravene securities regulations if the making of the order is in the public interest.

TRUE or FALSE?

19. A purchaser acquired a common share of an issuer pursuant to the accredited investor exemption on January 30, 2019. The issuer completed its initial public offering of common shares and listed securities on the Toronto Stock Exchange on March 30, 2019. The investor is permitted to sell their common shares through the facilities on the Toronto Stock Exchange on the date that is four months, plus one day after January 30, 2019.

TRUE or FALSE?

20. A majority of the directors of a company which is a reporting issuer are required to be independent, as that term is defined in National Instrument 52-110, unless the reporting issuer is controlled by another company or person.

TRUE or FALSE?

PART TWO**(15 Questions – 2 Marks Each – 30 Marks Total)****(approximately 36 minutes)**

SHORT ANSWER QUESTIONS: Please provide responses to each of the following questions.

Please briefly explain your responses and provide regulatory citations where relevant

1. What are the three regulatory objectives of securities laws? (1 mark) What are the three primary strategies that our regulators use to achieve these objectives? (1 mark)
2. Identify two ways in which a person might take control of a company which is a reporting issuer without the cooperation of the company's management.
3. In what circumstances will an omission to state a fact in a final prospectus trigger potentially liability to an issuer under the *Securities Act* (British Columbia)?
4. What is the "market impact" test and how does it differ from the "reasonable investor" test?
5. What is required for a corporation to complete a trade in its own common shares where the common shares have not been previously issued?
6. Identify two methods by which a person may legally acquire more than 20% of the outstanding equity or voting securities of a reporting issuer from security holders in Canada without preparing and filing a take-over bid circular and without obtaining approval of the acquisition of such securities in a vote of security holders of the reporting issuer.
7. A public company has two major shareholders. Shareholder A holds 46% of the voting common shares. Shareholder B holds 22% of the voting common shares. Shareholder B is in no way affiliated with or acting in concert with Shareholder A. The remainder of the voting common shares are widely held. Shareholder B decides to sell common shares through the facilities of the Toronto Stock Exchange, without providing any public notice of the sale. Is this sale a "distribution"?
8. What is "selective disclosure", why is it of concern to security regulators and what steps should a reporting issuer take to address the matter?
9. What are the six most important disclosure documents that a reporting issuer must file on SEDAR on an annual basis?
10. What are the principal defences available to a person charged with illegal insider trading in Canada?

11. What are some factors a regulator will consider in determining whether a person is in the business of trading for the purposes of the requirements of section 34 of the *Securities Act* (British Columbia)?
12. What is the objective of National Instrument 54-101 and how does the Instrument attempt to achieve this objective?
13. A prospective purchaser has entered into a binding contract to purchase common shares of a corporation that will be issued pursuant to a prospectus. The issuer has not received the prospectus. What rights does the prospective purchaser have?
14. What is the objective of National Instrument 54-101 and how does the Instrument attempt to achieve this objective?
15. An underwriter has been asked to sign the certificate to a final prospectus. What liability will the underwriter incur as a result of signing a prospectus? How can an underwriter mitigate the risk associated with this liability?

PART THREE**(25 Marks Total)****(approximately 30 minutes)**

You have been approached for advice by the two founders of company incorporated under the *Business Corporations Act* (British Columbia) under the name Homesite Trading Inc. (“**Homesite**”). The two founders each currently hold 50% of the common shares of Homesite. The two founders are also the only two directors of Homesite, and the CEO and CFO, respectively.

Homesite plans to develop an online platform for home renovation contractors and tradespeople working in Canada using state of the art blockchain technology (the “**Final Website**”). While the Final Website is only a concept at this stage, and has not been developed, the founders envision that the Final Website would work as follows:

- All services on the platform will be paid for and sold using blockchain based smart tokens called “**Home Tokens**”. (*Please note: For this question, all you will need to know is that a “Home Token” is a tradeable electronic currency. This question is NOT testing your knowledge of blockchain based businesses or cryptocurrencies! No points will be awarded for ANY commentary that is not based on the application of securities laws.*)
- Approved tradespeople would be permitted to advertise their services on the Final Website.
- If a homeowner / customer would like to contract a tradesperson using this service, he or she would select a tradesperson using the website, and purchase a sufficient number of electronic Home Tokens through the website to pay for the proposed services, which would be held in the customer’s Homesite account online.
- Upon completion of the work, tradespeople would receive payment for their services in Home Tokens debited from the customer’s online account, and credited to the tradesperson’s online account.
- Home Tokens held in an online account could be sold for cash via the website to customers wanting to purchase Home Tokens for services (the founders expect that this option would be limited at first, and would grow over time as the Final Website attracted customers). The Founders also believe that Home Tokens could be traded for other electronic currencies using third party currency trading websites, although they have not fully explored this possibility.

The founders have not begun development of the Final Website. The founders expect that it will cost approximately \$10 million to develop the Final Website.

To raise funds to construct the Final Website, the founders are considering selling \$10 million worth of Homesite common shares to raise funds. Unfortunately selling common shares to

investors will result in them losing much of the voting control of their business, which they would like to avoid if possible.

As an alternative, the founders would like to know if can raise funds by selling \$10 million worth of Home Tokens to purchasers online (“**Founding Purchasers**”). The founders have developed an initial website (the “**Initial Offering Website**”) where Founding Purchasers could set up an online account and purchase Home Tokens. As planned, Founding Purchasers would purchase each Home Token for \$0.10, resulting in the sale of 100 million Home Tokens. Founding Purchasers would be able to purchase Home Tokens directly from Homesite using the Initial Offering Website. The founders expect that there would be millions of Founding Purchasers.

Founding Purchasers would be able to use the Home Tokens as follows:

- Founding Purchasers could use Home Tokens to purchase services on the Final Website, once the Final Website is built and operating.
- Founding Purchasers would also be able to sell their Home Tokens to customers of the website via the Final Website, once the Final Website is operating, although as noted above, the founders expect that this option would be limited at first, and would grow over time as the Final Website attracted customers.
- Finally, as noted above, the founders believe that Founding Purchasers would also be able to trade their Home Tokens for other electronic currencies online using third party online trading websites, but they have not fully explored this possibility (they have seen these types of sites internationally, but they are not sure if they have seen any operating in Canada). Initially the Home Tokens would have no value on third party trading sites, but the founders expect that the Home Tokens would rise in value once the web platform is developed, and once there was a demand for Home Tokens from customers wanting to purchase Home Tokens in order to pay for services on the web site.

The founders have a few questions for you in connection with their plans above. Please address the following:

1. Are Home Tokens “securities”? The founders believe that the Home Tokens are just an electronic currency, similar to a retail gift card, and not a “security” – but they would like your advice. Please explain your reasoning. Please note, there are arguments for and against. Please consider both sides, come to a conclusion, and provide your reasoning. *(Please note: We are more interested in your reasoning, rather than in whether you come to the “right” conclusion).* **(8 marks)**

2. The founders have asked you to explain the consequences to their plan to sell \$10 million in Home Tokens if the Home Tokens are found to be “securities”. Please explain these consequences and your reasoning. **(5 marks)**
3. The founders have asked you to explain whether there will be any restrictions on the resale of Home Tokens by Founding Purchasers once purchased, if the Home Tokens are found to be “securities”. If there may be restrictions, please explain. **(5 marks)**
4. The founders would like to include the following statement on the Initial Offering Website to help promote the sale of Home Tokens to Founding Purchasers:

Homesite fully expects the Final Website to be operational within one year of completing the sale of 100 million Home Tokens to the Founding Purchasers.

The founders would like to understand if there is any potential risk to them if they include this statement? **(5 marks)**

5. If the founders instead decide to raise funds by issuing common shares of Homesite, what issues should they be aware of? **(2 marks)**

PART FOUR**(25 Marks Total)****(approximately 30 minutes)**

You have recently started your articles and a senior partner has come into your office and asked you to prepare a memo outlining the ways in which a new client of the firm, Shining Light Holdings Inc., can acquire control of a British Columbia company, Red Ridge Resources Ltd. Unfortunately, the partner was leaving to catch a flight when he gave you this assignment, and didn't have time to provide many details, other than to inform you that (i) the client is a private equity fund based in Singapore, (ii) Red Ridge is an underperforming junior resource company with a promising cobalt property somewhere in Africa, (iii) the shares of Red Ridge are listed on the TSX Venture Exchange, (iv) it is not known whether or not the deal will be friendly, and (v) more information about Red Ridge is accessible on a securities commission website called "Cedar" or something similar.

The partner requires your memo on his return to the office in two days, when he will be meeting with the General Counsel of Shining Light to discuss the matter. You seek help from one of the associates in your firm, who advises that your memo should:

- (i) discuss alternative transaction structures, including take-over bids, arrangements and proxy contests, and the principal advantages and disadvantages of each;
- (ii) recommend the use of a take-over bid, and explain the reasons for this recommendation;
- (iii) provide an overview of the regulatory regime for take-over bids;
- (iv) address the principal steps, actions and documents involved in making a take-over bid;
- (v) explain Red Ridge's possible responses to an unsolicited take-over bid;
- (vi) advise how the client can maximize the likelihood of success; and
- (vi) provide advice with respect to trading of Red Ridge shares prior to the completion of a transaction.

Please prepare the requested memo, following the advice received from your associate.

— END OF EXAMINATION —