



Current Developments: Canadian Securities and Auditing Matters

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Canadian Securities and Auditing Matters

This edition provides a summary of newly effective and forthcoming regulatory and auditing matters in Canada from January 1, 2018 to March 31, 2018.



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Canadian Securities: New guidance

Issuers with U.S. Marijuana-Related Activities

In February 2018, the Canadian Securities Administrators (CSA) issued Staff Notice (SN) 51-352 (Revised) *Issuers with U.S. Marijuana-Related Activities* to highlight disclosure expectations for such issuers.

The notice sets out disclosure expectations, premised on the assumption that marijuana-related activities are conducted in compliance with current laws and regulations of a U.S. state where such activities are legal. The CSA expects in a prospectus bold boxed cover page disclosure about the illegal nature of marijuana under U.S. federal law and the potential risks associated with this circumstance. Issuers who enter the Canadian capital markets through a reverse take-over or spin-off transaction should include these disclosures in their listing statement.

The SN lists specific disclosures necessary to fairly present all material facts, risk and uncertainties for all issuers with U.S. marijuana-related activities and additional disclosures required for (i) issuers with direct involvement in the cultivation or distribution of marijuana in accordance with a U.S. state license (ii) issuers with indirect involvement in the cultivation or distribution of marijuana in accordance with a U.S. state license and (iii) issuers with a material ancillary involvement.

The CSA reminded issuers that they expect disclosures will be monitored on an ongoing basis and supplemented, amended and communicated in the event of government policy changes or the introduction of new or amended guidance, laws or regulations regarding marijuana regulation.



Canadian Securities: Proposed guidance

Future Initiatives Related to Reducing Regulatory Burden

In March 2018, the CSA issued CSA SN 51-353 *Update on Consultation Paper 51-404 Considerations for Reducing Regulatory Burden for Non-Investment Fund Reporting Issuers*. In the notice, the CSA highlights planned policy initiatives as a result of the consultation paper.

The policy initiatives identified include:

- investigating changing prospectus requirements including (i) considering an alternative prospectus model (ii) changing requirements connected with at-the-market offerings to facilitate more use and (iii) revisiting the primary business requirements which outline the historical financial statements required to be included in an IPO prospectus;
- investigating changing continuous disclosure requirements including (i) removing or modifying the criteria to file a business acquisition report (ii) eliminating duplicative disclosure amongst financial statements, management's discussion and analysis (MD&A) and other forms (iii) consolidating two or more of the financial statements, MD&A and annual information form into one document and (iv) examining where the volume of information in annual and interim filings can be reduced; and
- investigating switching the current default to electronic delivery of documents provided that investors retain the option to receive paper documents.

Mortgages

In March 2018, the CSA issued a request for comments related to Proposed Amendments to National Instrument (NI) 45-106 *Prospectus Exemptions* and NI 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* relating to syndicated mortgages. The proposed amendments include changes to the mortgage exemptions, the offering memorandum exemption and the private issuer exemption.

Comments are requested on or before June 6, 2018.

Changes to the Mortgage Exemptions: The proposed amendments, together with related legislative amendments in Ontario, would remove the Mortgage Exemptions for syndicated mortgages in Newfoundland and Labrador, the Northwest Territories, Nova Scotia, Nunavut, Ontario, Prince Edward Island and Yukon (the "Impacted Provinces"). Other provinces currently do not have such an exemption. Alternative prospectus exemptions would be required for the distribution of syndicated mortgages in all CSA jurisdictions. In those jurisdictions where the Mortgage Exemptions currently apply to syndicated mortgages, market participants that are in the business of trading syndicated mortgages would be required to consider whether the registration requirement applies to them. Since entities involved in financing real estate developments tend to engage in repeated financing activities, the CSA expects that some of these firms will be required to become registered as a dealer or to rely on a registration exemption. In the Impacted Provinces an amendment to the registration exemption will be made effective one year later than the change to the prospectus exemption to allow time for market participants to register



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Changes to the Offering Memorandum (“OM”) Exemption: The OM Exemption is available for the distribution of syndicated mortgages. The OM Exemption allows for the distribution of securities to retail investors and is premised on adequate disclosure being provided to prospective purchasers. Projected values of the completed development and the fact that the syndicated mortgage is secured against real property are often emphasized in connection with the marketing of these investments. The proposed amendments require issuers to deliver an appraisal of the current fair market value of the property subject to the syndicated mortgage to prospective purchasers under the OM Exemption. The appraisal would be prepared by a qualified appraiser who is independent of the issuer. Any other value of the property disclosed by the issuer would be required to have a reasonable basis and the issuer would be required to disclose the material factors and assumptions underlying that value and whether it was prepared by a qualified appraiser who is independent of the issuer. Consistent with the current approach in British Columbia, the Proposed Amendments also include supplemental disclosure requirements that are tailored to syndicated mortgages, including disclosure of development risks, prior obligations secured against the real property and the price paid by the developer to acquire the real property. Issuers of syndicated mortgages would be required to meet the requirements of Form 45-106F2 *Offering Memorandum for Non- Qualifying Issuers*, as supplemented by proposed Form 45-106F18 *Supplemental Offering Memorandum Disclosure for Syndicated Mortgages*. The new disclosure requirements include information regarding the business and financial position of the borrower under the syndicated mortgage. The CSA expects that the issuer of the syndicated mortgage and the borrower will generally be the same entity. However, in circumstances where the issuer of the syndicated mortgage is not the borrower, its ability to rely on the OM Exemption will be dependent on its ability to provide the required information regarding the borrower and to certify that it does not contain a misrepresentation. Any mortgage broker involved in the distribution of a syndicated mortgage under the OM Exemption would also be required to provide a certificate

that the offering memorandum does not contain a misrepresentation with respect to matters within its knowledge and that the mortgage broker has made best efforts to ensure that matters that are not within its knowledge do not contain a misrepresentation. The certificate requirement for mortgage brokers is modelled on the current requirements that apply in British Columbia.

Changes to the Private Issuer Exemption: The proposed amendments would make the Private Issuer Exemption unavailable for the distribution of syndicated mortgages.



Auditing Matters

Auditor Reporting Model

More insight and transparency

The International Auditing and Assurance Standards Board (IAASB), has issued new requirements on auditor reporting.

Without changing the scope of an independent audit, these requirements open the door for the auditor to give users more insight into the audit and improve transparency.

In April 2017, the Auditing and Assurance Standards Board (AASB) in Canada approved the new and revised auditor reporting standards as Canadian Auditing Standards (CASs) effective for periods ending on or after December 15, 2018.

Highlights of the new auditors' report in Canada include:

- re-ordering the contents of the auditors' report (opinion first);
- expanded descriptions of responsibilities of management, those charged with governance and the auditors;
- separate section on "Other Information" (e.g. MD&A);
- disclosure of engagement partner's name (listed entities); and
- description of key audit matters (KAMs) (applicable only when required by law or regulation or when the auditor is engaged to do so).

U.S. developments

In June 2017, the Public Company Accounting Oversight Board (PCAOB) adopted their enhanced auditor reporting standards which includes, among other requirements, discussion of critical audit matters (CAMs) (similar to KAMs) and tenure of the auditor.

Highlights and effective dates of the new U.S. standards are:

- New auditors' report format, tenure and other information: audits for fiscal years ending on or after December 15, 2017;
- Communication of CAMs for audits of large accelerated filers: audits for fiscal years ending on or after June 30, 2019; and
- Communication of CAMs for audits of all other companies: audits for fiscal years ending on or after December 15, 2020.

Impact to Foreign Private Issuers in Canada

Auditors of foreign private issuers ("FPIs") are trying to address whether they can still issue a "combined" report (which many FPIs in Canada issue today) that meets both the CAS and enhanced PCAOB standards for 2018 year-end engagements.

At this time, it is increasingly unlikely the SEC and PCAOB will approve a combined report. If the SEC and PCAOB determine that a combined report is not possible, auditors of FPIs may need to consider whether issuing only a report under PCAOB standards is appropriate for their needs or whether they will need to issue two reports; one referring to the CASs and one referring to the standards of the PCAOB.

Auditing Accounting Estimates and Related Disclosures

The IAASB has issued an exposure draft on ISA 540 (Revised). Significant changes in how auditors evaluate accounting estimates and related disclosures have been proposed.

This proposed standard:

- enhances requirements for risk assessment procedures to include specific factors related to accounting estimates, namely complexity, judgment, and estimation uncertainty;
- sets a more detailed expectation for the auditor's response to identified risks related to accounting estimates, including augmenting the auditors' application of professional skepticism; and
- is scalable regardless of the size or sector of the business or audit firm.

Numerous stakeholders have submitted comment letters in regards to the exposure draft to the IAASB expressing concerns over how to operationalize this new standard. The IAASB is in progress of addressing the concerns and a final draft of the proposed standard is scheduled to be presented to the IAASB for approval in June 2018.



The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.