PROSPECTORS & DEVELOPERS ASSOCIATION OF CANADA

September 7, 2020

Capital Markets Modernization Taskforce
Sent via email: CMM.Taskforce@ontario.ca

Re: Consultation — Modernizing Ontario's Capital Markets

Dear Chair Soliman and Capital Markets Modernization Taskforce members,

As the leading voice of Canada's mineral exploration and development community, the Prospectors & Developers Association of Canada (PDAC) represents over 7,500 individual and corporate members, including a substantial portion of the nearly 1,200 mineral industry companies listed on Canadian exchanges. It is encouraging to see active steps being taken to modernize the functionality of capital markets in Ontario and these efforts are particularly important, in light the current COVID-19 pandemic, to ensure competitiveness is maintained in this quickly-changing global landscape.

A number of the proposals contained within the CMM Taskforce Consultation Report address issues previously raised by PDAC in consultations with regulatory bodies such as the Ontario Securities Commission (OSC) and the Canadian Securities Administrators (CSA) and could provide improved access to capital for many small and medium size public companies while reducing redundant or unnecessary processes.

Notably, well over 50% of all listings on the TSX-Venture exchange are in the mineral industry and predominantly represent pre-revenue exploration and mining companies. These companies rely on access to capital via public markets to advance projects and remain viable. With this in mind, new offering products, modernized electronic resources and streamlining disclosure are just some examples of the tangible steps the CMM Taskforce proposes that can bolster the competitiveness of Ontario's capital markets without diminishing investor protections.

PDAC greatly values the opportunity to provide input to the CMM Taskforce and has given careful consideration to the extensive list of proposals being tabled. The accompanying appendix outlines recommendations developed by PDAC Committees and based on feedback from our membership, and we welcome continued engagement to provide any additional information or context that may be beneficial to the CMM Taskforce in completing this very important work.

Sincerely,

Lisa McDonald

Executive Director

Prospectors & Developers Association of Canada (PDAC)

PROSPECTORS & DEVELOPERS ASSOCIATION OF CANADA

Annex A: Detailed Response to the Capital Markets Modernization Taskforce's Consultation

This document provides feedback on 15 proposals made by the Ontario Capital Markets Modernization Taskforce ("Taskforce") that were identified as relevant to PDAC members. A number of these proposals are of particular importance and below is a brief overview of PDAC feedback on these priority areas.

- *Elimination of the 4-month hold period for AIs (proposal #5):* our members expressed various views supporting either shortening or eliminating the hold period, but also indicate a concern regarding a potential liquidity event.
- *Semi-annual reporting (proposal #6):* if the availability of such a regime would be limited only to smaller issuers, we recommend that companies without revenue from regular operation in the previous two fiscal years will be eligible to publish semi-annual reporting.
- *Alternative offering model for reporting issuers (proposal #7):* PDAC is supportive of this initiative, recommends basing it on a similar model investigated in BC, and thinks that issuers opting into semi-annual reporting (Proposal #6) should be covered under this exemption.
- *Consolidating reporting and regulatory requirements (proposal #10):* PDAC is very supportive of the proposal and identified a number of overlaps in requirements between AIF, the financial statements and the MD&A, as well as some aspects of the BAR that needs to be amended/simplified.
- *Addressing predatory short selling (Proposal #13):* The attempt to address the issue is encouraging, but we have concerns regarding the specific proposal, and suggest that before establishing new policy, a comprehensive impact analysis of the phenomenon should be initiated. In addition, the Taskforce should consider reinstating some version of the uptick rule and consider establishing more transparent disclosure standards from brokers to avoid conflict of interest.

Lastly, we would like to emphasize the significant benefits that harmonization of provincial disclosure through the Capital Markets Regulatory Authority (CMRA) will bring to small issuers. Hence, we urge the Taskforce to encourage the Ontario government to place high priority on related legislation and implementation of this initiative, which by itself would be a significant step forward in modernizing our capital markets.

2.1 Improving Regulatory Structure

Ontario Securities Commission (OSC) Governance

1. Expand the mandate of the OSC to include fostering capital formation and competition in the markets

How would incorporating capital formation and fostering competitive capital markets into the OSC's mandate help spur economic growth in Ontario?

Adding aspects such as fostering capital formation and competition in the markets to OSC's mandate would change the general staff "state of mind", priorities, and decision-making across all divisions/units of the organization, eventually improving regulation in Ontario by making it much more cost-efficient. In turn, this will increase the competitiveness of Canadian exchanges compared to global peers. Competitive markets will further enhance listing attraction in Canadian markets and provide additional work to many professionals involved in the capital markets, eventually spurring economic growth in Ontario.

Would such changes impact the OSC's remaining mandates (i.e., fostering fair and efficient capital markets, protecting investors and reducing systemic risk)?

Adding another mandate may create challenges that arise from conflicting aspects of the dual mandate, but a concrete process aimed at addressing these challenges will guaranty investor protection. Eventually, investors' interest is also that companies in which they invest will benefit from cost-effective regulation.

2.2 Regulation as a Competitive Advantage

Supporting Ontario's Issuers and Intermediary Market

5. Mandate that securities issued by a reporting issuer using the accredited investor prospectus exemption should be subject to only a seasoning period

PDAC supports either a reduction or progressive elimination of the current hold period for Accredited Investors (AIs).

Given the pace of and the level of disclosure within modern capital markets, a growing number of investors restrict ownership to free trading equities and this is shrinking the overall pool of potential investors and can add complexity and cost to financings under the AI prospectus exemption.

However, concerns have also been raised in regards to the initial intent behind the hold period and how its complete elimination could create downward price pressures and other unforeseen disadvantages for secondary market participants, who may not receive the same considerations as participants in an AI prospectus exempt financing (i.e. warrants, options etc.).

To balance these perspectives, the Taskforce should consider reducing (i.e. to a 2-month period) or progressive elimination (i.e. eliminate hold in batches of 33% or 50% progressively over a 4-month or shorter period).

In addition, any changes made to the hold period for AIs should be considered for any similar hold periods applied under other exemptions to ensure there is a consistent regulatory approach to exempt offerings and an even playing field for all investors.

6. Streamlining the timing of disclosure (e.g., semi-annual reporting)

- Should the option of semi-annual reporting be made available to only smaller issuers with less significant quarterly operational changes and what should the eligibility criteria for those publishing semi-annual reporting be?

In case availability of semi-annul reporting would be limited only to smaller issuers, we recommend a revenue test to determine eligibility, as follows:

"Companies in good standing and without revenue from regular operations in any of the previous two fiscal years, as reflected in consolidated financial statements for such fiscal years, will be eligible to publish semi-annual reporting."

- If semi-annual reporting is adopted, should issuers using a short form prospectus be required to supplement their financial disclosure if more than a quarter has passed since their most recent financial statements?

Yes. The requirement to supplement financial disclosure in this case is reasonable.

7. Introduce an alternative offering model for reporting issuers

- What are some of the conditions that should be imposed on issuers relying on the alternative offering model prospectus exemption?

The notion of alternative offering model exemption aimed at small financings is very encouraging, and PDAC recommends the Taskforce to consider a similar proposal already in discussions by the Canadian Securities Administrators (CSA) and the British Columbia Securities Commission (BCSC). This model defines a 12-month period in which issuers can rely on a relatively short disclosure document to raise funds up to a certain limit.

For the 12-month maximum funding, we propose a test that combines a maximum limit of at least $10M for smaller issuers, and more than that for larger issuers. Given the purpose of this offering model is reducing regulatory burden for small offerings, the mechanism of setting the limit should be proportional to issuers' market capitalization, so the exemption is not available for issuers planning to use the proceeds for a material acquisition or change of business.

- Should issuers opting into semi-annual reporting (Proposal #6) be covered under this exemption?

Yes. The rationale is that both semi-annual reporting and the alternative offering model target the same "cohort" of small issuers, asking small issuers to choose between these two options would be counterproductive.

As a safeguard, and similarly to what is suggested regarding short form prospectus under item #6, if more than a quarter has passed since the release of most recent financial statements, issuers using this new alternative offering model would be required to supplement their financial disclosure.

9. Transitioning towards an access equals delivery model of dissemination of information in the capital markets, and digitization of capital markets

- Please provide feedback regarding which of the above communication and regulatory documents (and suggestions for others) should be made available electronically rather than delivered.

All the communication and regulatory documents mentioned by the Taskforce in the discussion on this model should be included (i.e. prospectus under prospectus offerings by reporting issuers, annual and interim financial statements and related MD&A, as well as the MFRP). In addition, other continuous disclosure documents such as the AIF, management circulars, and proxy related materials should be included in the proposed model as well.

- How should shareholders be kept informed of these documents (i.e., one-time verification that shareholders will continuously monitor a company's website notifying electronic delivery of communication documents)?

The recommended approach is a one-time verification procedure suggested above, combined with an educational CSA information system that can let investors and shareholders know about the availability of various documents and facilitate easy access.

- Are there instances whereby physical delivery of such documents is more well-suited?

Following the introduction and successful implementation of the proposed model, physical delivery of paper documents should be eliminated, except for low cost streamlined paper notices sent to the addresses of registered beneficial shareholders on an annual basis. Issuers can maintain a system to send select paper documents to investors and shareholders upon request, at the expense of the investor (in accordance to "polluter pays" principle).

- Would the implementation of an access equals delivery model raise any investor protection or investor engagement concerns and what are potential solutions?

As long as the system is a "user friendly" and enable such communication channels to keep investors informed on current events and developments, the proposed model bears very little risk of undermining investor protection.

- Should this be extended to issuers in exempt markets?

Yes, from a timely disclosure, transparency and fairness perspective, all financing documents should be available electronically to all shareholders at the same time if they have elected to be part of a comprehensive financing documents notice and access system.

10. Consolidating reporting and regulatory requirements

- What are some specific reporting requirements arising from regulatory disclosures as noted above, such as the MD&A and Annual Information Form, that can be removed, consolidated and/or streamlined to reduce duplication and regulatory burden while upholding investor protection?

1) <u>Eliminating overlapping requirements between AIF, the financial statements and the MD&A:</u>

- *MD&A vs. Financial Statements:* we recommend of full consolidation of these two documents, eliminating a number of redundant form requirements related to 51-102F1 (MD&A) that are either identical or similar to financial statements' requirements under IFRS and US GAAP. These requirements include disclosure related to:
    - Financial instruments (Part 1.14)
    - Critical accounting estimates (1.12)
    - Changes to accounting policies (1.13)
    - Contractual obligations (Within 1.6)
    - Off-balance sheet disclosures (1.8)
    - Transactions Between Related Parties (1.9)
    - Liquidity risks (1.6)

  Note that in order to prevent adding burden on issuers, non-audited items should remain that way, and in order to maintain investor protection, the new document should clearly distinguish between audited and non-audited components.

- *AIF vs. FS/MD&A:* We recommend on consolidating the AIF with financial statement and MD&A.
    - However, issuers should keep the option to file a separate AIF on a later date than financial statements and MD&A, as this would afford issuers additional time to prepare and vet associated disclosures and provide the annual CEO and CFO certifications. Asking issuers to file a single annual report would make it more onerous on them to comply with reporting deadlines.
    - We also identified several overlaps between AIF and annual FS/MD&A:
        - Disclosures on legal proceeding and regulatory action (item 12 of the AIF)
        - Disclosure on risk factors faced by the issuers overlaps between the two documents
        - Some duplications with between the description of the business & general development of the business in the AIF and the overall performance & discussion of operations in the MD&A.

2) Simplifying the Business Acquisition Report (BAR):

We would also like to reinforce some of the comments we made on the BAR and small/venture issuers, in response to questions 18-20 in CSA Consultation Paper 51-404 (July 2017):

- Since the threshold for venture issuers for the asset test and the investment test is 100%, most transactions that require a venture issuer to file a BAR will also require shareholder approval, in connection with which a management information circular (MIF) is distributed. The MIF will typically provide the financial information, including pro forma financials, and a BAR containing substantially the same information which is filed up to 75 days after closing the transaction does not provide relevant or timely information. Moreover, after the transaction is completed, the issuer will then file actual financial statements showing the actual effect of the transaction on the balance sheet, which is generally more useful to investors.
- If a transaction meets the 100% significance test, a prospectus level disclosure is generally appropriate. However, where only some of the vendor's assets are acquired, the preparation of carve-out historical financial statements can be very burdensome, and does not provide very useful information for pre-revenue issuers. For acquisitions of non-revenue generating assets, a pro forma balance sheet showing the effect of the transaction should be sufficient.
- For small reporting issuers and for pre-revenue companies in particular, the profit or loss test is not appropriate since an acquisition of business with relatively small profits can trigger it.

13. Prohibit short selling in connection with prospectus offerings and private placements

PDAC has heard increasing feedback that have expressed concerns regarding the impact of predatory short selling on small mineral exploration companies and it is encouraging that the Taskforce proposal aims to address this issue. However, we have identified possible concerns regarding the specific proposal at hand and think that steps to address short selling should go beyond simply limiting this activity prior to an offering.

Hence, we have a few recommendations to address short selling in a more holistic manner:

- Address concerns regarding the current proposal
- Initiate a research aimed at obtaining a more accurate estimate of various impacts that short selling pose on company stock price, for various company sizes
- Consider also reinstating a version of the tick rule or an alternative version of it
- Require brokers to provide better disclosure and get prior consent from clients to share loans, in order to prevent potential conflict of interests

Concerns regarding the current proposal: The taskforce's proposal, which follows amended rule 105 of regulation M in the U.S (2007), could minimize short selling prior to financing, but could also negatively affect market liquidity. In addition, it is not certain that the proposed rule will be efficient in Canada as it is in the U.S due to different pricing mechanisms of offerings. Canadian mining offerings are dominated by bought deals where price is negotiated privately between the dealer and the issuer prior to announcement, while U.S. offerings generally marketed over a period and then priced. The prohibition on short selling during a period of price discovery as it is in the US makes sense, while in Canada it is less clear that what would an arbitrary window ahead of a deal accomplish. Lastly, enforcing this rule is not easy - after-the-fact remedies/sanctions would not stop the violation, and real-time enforcement may be challenging as expressed in a risk alert on this issue, released by the SEC in 2013. In that context, it is worth mentioning that in 2007 SEC eliminated the uptick rule but in 2010 SEC reinstated an alternative version of it, arguably due to the challenges mentioned above.

Initiate thorough research: it is natural that upcoming financing will negatively affect stock prices due to dilution expectations (based on economic principles), so the assumption that short activity is the key reason for down pressure on stock price is not necessarily true. While there are anecdotal

evidence regarding the impact of short selling on small and mid-cap companies, we think that first there is need to conduct a comprehensive analysis of the impact of this phenomenon on price volatility, pricing of the deal and post trading difficulties, for each class of company size. This will provide the regulators with a better basis in developing a strategy to address predatory short selling.

Reinstate the uptick rule (or an alternative version of it): In our view, the uptick rule (or a similar version of it) is a more comprehensive solution to predatory short selling, a solution that does not have the negative consequents of harming liquidity in offering. The uptick rule was first introduced in the U.S over 80 years ago, and had remained in place until 2007, but then in 2010 was reinstated (under a slightly different version called "the alternative uptick rule"), largely in response to the "flash crash" of May 6th 2010, according to the SEC. At this time, the uptick rule was in place in Canada, but was canceled in 2012. Up until 2012, all Canadian exchanges had a tick test for short selling, but it was removed due to market data suggesting that it was not an efficient method of stopping the type of short selling it was created to mitigate. However, given technology developments since then (e.g. high frequency and algorithmic trading), there is a place for new revision of these assertions.

Address Brokers' disclosure: Another problem of short selling relates to disclosure by brokers. The concept of loaning shares from one broker to another in order to avoid notice of short selling requirement could be a conflict of interest by brokers as they are effectively lending shares held by their clients to third party brokers with a view to avoiding the short selling disclosure requirements. We think that any use in investor shares should be disclosed and consent should be given prior to loaning the shares.

14. Introduce additional Accredited Investor (AI) categories

- Would commenters recommend additional expansions to the existing AI definition? If so, which ones?

The Taskforce's proposal to expand the AI definition to those individuals based on financial education is a very positive development and PDAC has made recommendations to this effect during the OSC's Burden Reduction project in 2019. We also reinforce our prior recommendation to go beyond financial education and expand exemptions to encompass industry-related technical proficiencies such as knowledge, expertise and experience.

Since a relatively high portion of mineral sector financing is done via private placements (In 2019, ~70% in total and 90% for TSXV companies), implementing this concept would expand the pool of potential investors without having a negative impact on investor protections. In fact, these potential investors represent a cohort that contributes significantly to technical reports and project designs that underpin investment in the mineral industry (i.e. a Qualified Person), and therefore have a sufficient level of sophistication to be considered AIs.

As industry-based proficiency would require the regulator to decide what issuances be accessible to AIs under this new exemption (based on specific industry proficiency), it is recommend consulting with key stock exchanges regarding industry classifications.

15. Expediting the SEDAR+ project

- What priority should be given to the development and launch of SEDAR+?

As SEDAR+ will be especially beneficial to smaller issuers with significant disclosure costs, we are supportive in expediting the development of SEDAR+ and prioritizing the project.

2.3 Ensuring a Level Playing Field

Promoting Competition

18. Introduce a retail investment fund structure to pursue investment objectives and strategies that involve investments in early stage businesses

Notionally, we endorse the concept of investment fund supporting early stage business. Early stage mineral exploration and development companies typically generate no revenue, and rely almost exclusively on capital markets to obtain financing and advance projects. However, lack of revenue generation can significantly limit financing options and as a result, most equity capital for mineral exploration is raised via private placements from AIs.

A potential solution for this challenging reality is the involvement of the provincial governments and their agencies in the market. Therefore, irrespective of whether such a fund would be structured as an interval fund or as some other type of 'long-term view' investment fund, PDAC supports the Taskforce proposal. We recommend research of other semi-governmental concepts such as SIDEX in Quebec would benefit the Taskforce and welcome further consultation on this concept with the Taskforce.

19. Improve corporate board diversity

- Please provide feedback on the proposal above and identify any challenges or concerns that may arise.

Board diversity is an important competitive advantage for a company, therefore we welcome the proposal of the Taskforce to require TSX-listed companies to set targets, and annually provide data in relation to the representation of women, black people, indigenous people, and people of colour (BIPOC), on boards and in executive officer positions.

In that context, PDAC is developing feedback regarding potential amendments of sections 11-15 in form 58-101F2 of National Instruments 58-101 (Disclosure of Corporate Governance Practices), so the term "BIPOC" (or similar) would be added to any place where the term "Women" is mentioned.

2.4 Proxy System, Corporate Governance and Mergers and Acquisitions (M&A)

Proxy Advisory Firms

20. Introduce a regulatory framework for proxy advisory firms (PAFs) to: (a) provide issuers with a right to "rebut" PAF reports, and (b) restrict PAFs from providing consulting services to issuers in respect of which PAFs also provide clients with voting recommendations

- Please provide feedback on the proposal above and identify any challenges or concerns that may arise.

We support the proposal to introduce a regulatory framework for PAFs. Currently, small issuers often do not have the ability to dispute incorrect statements of a PAF due to lack of institutional contacts or other resources needed for a rebuttal to PAFs comments, particularly where their recommendations go against management.

One challenge arises from the short timelines for rebuttal, since issuers send out AGM materials only 33 days before the date of the meeting. The information and rebuttal right should be supplied on a timely manner to those affected parties. A proposed solution for this would be a double staged mechanism, under which the PAF will have only several days (e.g. 5 days) to publish an intent to

comment on the material sent by the issuers, and only several additional days to publish the comments, leaving enough time for the issuer to respond.

- Does the proposal to restrict PAFs to either providing consulting services or making voting recommendations in respect of an issuer appropriately address conflicts of interest?

While it is prudent that PAFs be under very few restrictions as to the recommendations, it is also necessary that there be provisions to avoid conflict of interest. One approach to it is to require PAFs to set up separate divisions much in the same manner as accounting firms do when potential conflict of interest arise between activities.

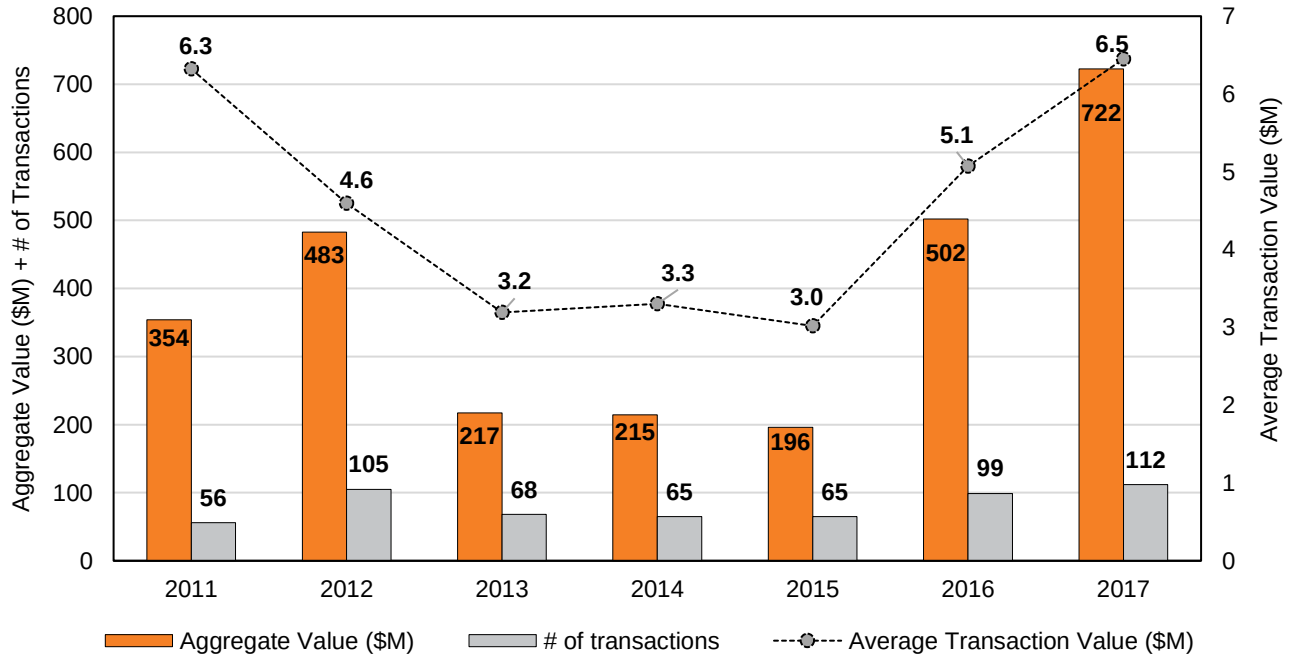
Ownership Transparency

21. Decrease the ownership threshold for early warning reporting disclosure from 10 to 5 per cent

- Are there reasons to exclude certain issuers from the scope of the proposal, such as venture issuers or those below a specified market capitalization?

Venture issuers should be excluded from the scope of the proposal, because it may cause key "passive" investors to reduce their ownership level. Research conducted by PDAC in 2018 revealed an increasing trend of sector reinvestment by major mining companies into junior mineral exploration companies. Figure 1 below shows the aggregate and average transaction value, as well as the number of transactions completed by major mining companies investing in juniors, and shows how from 2013 to 2017 the aggregate equity value raised by junior companies from major mining producers increased by more than 500%. The increased reinvestment has been critical in offsetting outflow of public funds from junior mineral explorers during the same period, and therefore, constitutes a crucial part in the ability of small mineral issuers to access capital. Major mining companies (as well as other passive investors) often prefer to stay below the 10% ownership threshold in order to avoid exposure. Hence, there is a significant risk that reducing the threshold to 5% will push many of these companies to reduce ownership level below 5%, resulted in a loss of financing source for the small issuers.

Figure 1: Majors' Investment in Junior Mineral Exploration Companies



Proxy Voting System

30. Eliminate the non-objecting beneficial owner (NOBO) and objecting beneficial owner (OBO) status, allow issuers to access the list of all owners of beneficial securities, regardless of where security holders reside, and facilitate the electronic delivery of proxy-related materials to security holders.

- Should reporting issuers be entitled to know who their beneficial owners are?

Yes. The OBO/NOBO statuses were created at times that digitalization of financial disclosure was in its infancy. Today, especially given the consideration of the access equal delivery model (i.e. proposal #9) this status has become obsolete and only diminishes the efficiency of communicating with key investors, without adding investor protections.

- And if so, should beneficial owners be allowed to opt out of being solicited for voting instructions directly by a reporting issuer?

Yes. With inclusion in the system as default option, opt out rate should be minimal. It is very likely that many OBO shareholders chose to define themselves as such mostly to avoid receiving unnecessary mail. An up to date equal access delivery system (as mentioned in OSC proposal #9) will eliminate the rationale initially employed to choose the OBO status, therefore minimizing opting out rate.

2.6 Modernizing Enforcement and Enhancing Investor Protection

Modernizing Enforcement

35. Improve the OSC's collection of monetary sanctions

We generally take the view that relief of regulatory burden should be accompanied by provision of better tools to enforce compliance and sanctions on bad actors, which makes regulation to the general market more efficient and effective. As mentioned in the discussion of the Taskforce, new legislation in British Columbia in that area seems to have been successful, and therefore we support the initiative to enact similar legislation in Ontario.

Additional Commentary

Prioritization of the Capital Markets Regulatory Authority (CMRA)

When operational, the CMRA has potential for a significant reduction of issuers' disclosure burden through regulatory jurisdictional harmonization. Therefore, this initiative by itself would be a significant step forward in modernizing capital markets in Ontario and across Canada. We suggest that in its final report, the Taskforce recommend that the Ontario government place high priority on implementing the CMRA; furthermore, the provincial government should work with the other participating jurisdictions to complete and pass legislation that will establish timelines for the new authority to become operational.