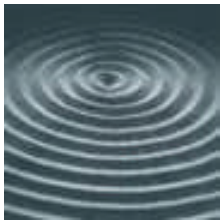
2500, 20 Queen St. West
Toronto, ON
Canada
M5H 3S1
Tel. 416.595.8500
Fax 416.595.8695
www.millerthomson.com



M I L L E R T H O M S O N L L P

Barristers & Solicitors, Patent & Trade-Mark Agents

TORONTO VANCOUVER CALGARY EDMONTON WATERLOO-WELLINGTON MARKHAM WHITEHORSE WASHINGTON, D.C.

Bill C-13 aimed at restoring investor confidence after spate of corporate crimes

Eli Laius

May 28, 2004

CRIMINAL LAW

Bill C-13 aimed at restoring investor confidence after spate of corporate crimes

By Eli Laius

With corporate governance a hot topic on the political agenda, the federal government has introduced Bill C-13, which aims to strengthen the ability of the police and the Crown to investigate and prosecute capital markets fraud by expanding the fraud and evidence-gathering provisions of the *Criminal Code*.

The proposed legislation is part of a larger federal strategy to help restore investor confidence in the capital markets in the wake of the various corporate governance scandals. The bill was given Royal Assent on March 29 and, when brought into force, will:

- increase the maximum prison sentences for the existing fraud offences, including an increase from 10 to 14 years for fraud and fraud affecting the public market under section 380 of the *Code*;
- provide a list of aggravating factors for sentencing purposes, including whether the perpetrator took advantage of his or her elevated status in the community in committing the offence;
- allow the court to issue production orders to obtain information and documents from persons not under investigation;
- establish concurrent federal jurisdiction to prosecute certain capital market fraud cases;
- provide "whistleblower" protection to employees who report unlawful conduct; and
- create a new criminal offence of insider trading.

The latter is particularly significant in light of the high-profile insider trading cases (Martha Stewart, for instance) that have contributed to the current wave of investor cynicism.

"Insider trading" involves trading in the securities of a company while in the possession of undisclosed, material information regarding the company.

Insider trading in the securities of a publicly-traded company is currently prohibited under provincial securities legislation.

For example, under the subsection 76(1) of the *Securities Act* (Ontario) (the "Securities Act") a person who is in a special relationship with a public company is prohibited from purchasing or selling the company's securities with knowledge of a material fact or material change that has not been generally disclosed to the public, and from disclosing such information to others (or "tipping").

Those in a "special relationship" to a company include not only traditional "insiders", such as directors and senior management, but also employees and professional advisers of the company, among others.

Subsection 122(1) of the Securities Act provides for a maximum term of imprisonment of 5 years and/or a fine of up to $5 million for the contravention of Ontario securities law.

Under subsection 122(4), however, a person convicted of insider trading can be subject to a fine equal to a maximum of triple the amount of profit made or loss avoided by the person by reason of the contravention. Pursuant to subsection 122(5), the general $5 million fine applies if the profit made or loss avoided cannot be determined.

Like the securities law offence, the new criminal prohibition will apply to a broad range of people beyond traditional insiders, including those who possess inside information by virtue of being shareholders or professional advisers of the company.

The new offence will impose liability where such persons knowingly use inside information in the purchase or sale of securities or disclose such information to others. Insider trading will constitute an indictable offence and carry a maximum sentence of 10 years imprisonment, while tipping may be treated as either a summary or indictable offence and carry a maximum sentence of 5 years imprisonment.

Significantly, the new offence requires the Crown to establish that the accused knowingly made use of the inside information in the purchase or sale of the security, whereas the *Securities Act* offence is based on mere knowledge of undisclosed material information.

Eli Laius

Previous incarnations of the offence under the Securities Act contained a similar "makes use of" requirement, which was shifted from an element of the offence to a statutory exception with the 1978 amendments to the Securities Act.

The defence itself was removed in the 1987 amendments to the Securities Act after being critiqued by both commentators and government studies of securities legislation as an unnecessary impediment to successful prosecutions.

Indeed, the authors of *Proposals for a Securities Market Law for Canada* (1979), Canada, concluded that the "availability of the 'make use of' defence may not unreasonably be said to have led to an incorrect result in every case in which it has been considered."

Accordingly, the use requirement under the criminal offence may serve to hamstring prosecutions.

The removal of the "make use of" defence from the Securities Act survived constitutional scrutiny under s. 7 of the *Charter* in *R. v. Woods* [1994] 88 C.C.C. (3d) 287.

The federal government has also announced the creation of Integrated Market Enforcement Teams (IMETs) which will bring together RCMP officers, federal lawyers and other investigators with provincial securities regulators and local police forces to investigate capital markets fraud.

The IMETs will be located in Toronto, Montreal, Vancouver and Calgary and are expected to become operational over the next two years.

Eli Laius is an associate in Miller Thomon's Securities and Corporate Finance Group.