

SME

Ontario Securities Commission

OSC SME Institute

Regulatory Overview for Directors and Audit Committees

Corporate Finance Branch

February 5, 2013

OSC

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Welcome and Introduction to the OSC SME Institute

OSC SME Institute - Objectives

Our goal is to:

- Help SMEs navigate the regulatory waters
- Demystify disclosure requirements so companies can focus on building their business
- Reduce SMEs' cost of compliance so that this money can be better spent on strategic initiatives
- Provide an opportunity for informal dialogue with OSC staff

Disclosure requirements, including those for financial reporting, are a cornerstone of investor confidence

Today's Session - Objectives

Objectives of today's session:

- Importance of gatekeeper role
- Rules to be aware of as a director or audit committee member
- Best practices to consider
- Common issues we identify

A high level of engagement by boards and audit committees in their oversight of management and responsibility for stewardship of a public company are key aspects of investor protection

Regulatory Landscape in Canada

Securities Regulatory Authorities

- In Canada, securities regulation is a provincial and territorial responsibility
- Each jurisdiction of Canada has its own Securities Act and securities regulatory authority (e.g., Ontario Securities Commission)
- The securities regulatory authorities are members of the Canadian Securities Administrators (CSA)
- CSA assists in coordinating what securities regulatory authorities do

A company deals primarily with its “principal regulator” (usually the jurisdiction in which the company’s head office is located)

Securities Regulatory Authorities

- Rules adopted by all jurisdictions are called “national instruments”
 - National instruments have forms which outline filing requirements (national instruments and forms have the force of law)
 - National instruments also have companion policies which provide guidance on how the national instrument should be interpreted (companion policies do not have the force of law)
- Guidance published to assist interpret rules are called “national policies” (national policies do not have the force of law)

Copies of national instruments, forms and companion policies that apply in Ontario are available on the OSC website at www.osc.gov.on.ca

OSC Corporate Finance Branch

- Branch of OSC that administers rules applicable to public companies and their insiders
- Oversight of capital raising in the exempt market
- Disclosure of material information that investors and other market participants need to make informed investment decisions
- Continuous disclosure filings and prospectuses
- Applications for exemptive relief from legislative requirements
- Matters relating to reports of exempt distributions, insider reports, early warning reports and take-over bids

Board of Directors' Role as Gatekeeper

The Role of Directors

“Shareholders of public companies delegate oversight of the companies they own to directors, who act as fiduciaries, overseeing the company’s business and affairs on their behalf in the best interests of the corporation.”

Canadian Coalition for Good Governance
2010 Building High Performance Boards

The Role of Directors (cont'd)

- Canadian corporate statute
 - The directors' role is to oversee the management of the business and affairs of the corporation
 - Duty to act honestly and in good faith with a view to the best interests of the corporation
 - Exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances
- Securities legislation and policies

Best Practices of High Performing Boards



*Canadian Coalition for Good Governance
2010 Building High Performance Boards*

Key Rules and Policies Relevant to Directors

Governance

Key Rules and Policies Relevant to Directors - Governance

Corporate Governance Framework:

- Board governance
 - NP 58-201 *Corporate Governance Guidelines*
 - NI 58-101 *Disclosure of Corporate Governance Practices*

- Audit committee
 - NI 52-110 *Audit Committees*

NP 58-201 *Corporate Governance Guidelines*

- Applies to all reporting issuers
- Companies are encouraged to consider guidelines in developing their own governance practices
- Main areas of focus
 - a. Independence
 - b. Board mandate
 - c. Responsibilities of board and CEO
 - d. Features of board committees

Corporate Governance Guidelines – Main areas of focus

a. Independence

- Board should have a majority of independent directors

b. Board mandate

- Board should adopt a written mandate which acknowledges its responsibility for the stewardship of the issuer
- Board mandate should set responsibility for:
 - Integrity of the CEO and other executive officers
 - Strategic plan and principal risks
 - Internal control and management of information systems
 - Approach to corporate governance
 - Succession planning
 - Communication policy

Corporate Governance Guidelines – Main areas of focus (cont'd)

c. Responsibilities of board and CEO

- Board should develop position descriptions for chair of the board and chair of each board committee
- Board and CEO should develop a position description for the CEO
- Board should develop or approve the corporate goals the CEO is responsible for achieving
- Code of business conduct and ethics

Corporate Governance Guidelines – Main areas of focus (cont'd)

d. Features of board committees

- Board committees
 - Delegate execution of responsibility to committee, however final decision-making power remains with the board
- Board assessments
 - Boards, committees and each director should be regularly assessed for effectiveness and contribution
- Director education
 - All new directors should receive a comprehensive orientation
 - Board should provide continuing education opportunities for all directors

Importance of Corporate Governance Disclosure to Investors

- Protection of shareholders
 - Strong corporate governance disclosure regime
 - Key feature of market-based monitoring of corporate conduct
 - Central to the ability of shareholders to exercise their voting rights effectively
 - Shareholders and potential investors require access to regular, reliable and comparable information in sufficient detail for them to:
 - assess the stewardship of the board and management and
 - make informed decisions about the valuation, ownership and voting of shares

NI 58-101 *Disclosure of Corporate Governance Practices*

- Purpose – requires companies to:
 - disclose their corporate governance practices
 - disclose certain information about directors and committees
 - file their code of business conduct and ethics
- Applies to all reporting issuers

NI 58-101 *Disclosure of Corporate Governance Practices (cont'd)*

- Disclosure of corporate governance practices in information circular, AIF or MD&A

TSX-listed issuers

- Form 58-101F1 Corporate Governance Disclosure
- Must disclose corporate governance practices with reference to the guidelines

Venture issuers

- Form 58-101F2 Corporate Governance Disclosure (Venture Issuers)
- Must disclose corporate governance practices in areas addressed by the guidelines

NI 52-110 *Audit Committees*

- Summary of requirements
 - Applies to all reporting issuers

Requirements	TSX issuers	Venture issuers
Existence of audit committee	required	required
Independence - all members	required	not required
Financial literacy – all members	required	not required
Auditor directly reports to committee	required	required
Committee responsibilities	required	required
Disclosure	required	required

NI 52-110 *Audit Committees* (cont'd)

- Audit committee responsibilities
 - Written charter stating mandate and responsibilities
 - Review financial statements, MD&A and related press releases before publicly disclosed
 - Be satisfied adequate procedures are in place for review of issuer's public disclosure of financial information extracted or derived from financial statements
 - Nominate auditor, oversee work of the auditor
 - Whistle-blower procedures

Insider Reporting

Purpose of Insider Reporting

- Deterrent purpose
 - Insiders less likely to engage in improper trading if trading subject to public/regulatory scrutiny
- Signalling purpose
 - Investors provided with timely disclosure of insider transactions and, by inference, insiders' views of company's prospects
- Prevention of improper grant practices purpose
 - Timely disclosure of option grants helps minimize opportunities for improper grant practices (e.g., backdating, spring-loading, etc.)

Who must file insider reports?

- “Insider” is defined in section 1 of Ontario Securities Act
- However, only “reporting insiders” must file insider reports
- Definition of “reporting insider” in NI 55-104 attempts to capture insiders with:
 - Routine access to material undisclosed information
 - Significant influence over the company

Who is a Reporting Insider?

- CEO, CFO & COO of company, significant shareholder and major subsidiary
- Director of company, significant shareholder and major subsidiary
- Person in charge of principal business unit, division or function of company
- Significant shareholder (> 10% voting securities)
- Company itself in limited circumstances
- Any other insider that:
 - In ordinary course has access to material undisclosed information about the company, and
 - Directly or indirectly has significant power or influence over business, operations, capital or development of company

Primary Insider Reporting Requirement

- Initial report
 - Must file within 10 days of becoming a reporting insider of a company
 - Disclose the reporting insider's:
 - Beneficial ownership of, or control or direction over, securities of the company
 - Interest in, or right or obligation associated with, a related financial instrument involving a security of the company (e.g., a derivative transaction like an equity swap)

Primary Insider Reporting Requirement (cont'd)

- Subsequent report
 - Must file within 5 days of any change in their holdings (e.g., purchase or sale of securities, exercise of stock options and the acquisition of the underlying shares)
 - Disclose the change in the reporting insider's:
 - Beneficial ownership of, or control or direction over, securities of the company
 - Interest in, or right or obligation associated with, a related financial instrument involving a security of the company

M&A Transactions

Role of the OSC in M&A Transactions

- Regulate various types of M&A transactions involving reporting issuers:
 - take-over bids
 - issuer bids
 - insider bids
 - business combinations (“going private” transactions)
 - related party transactions
- Applicable requirements and standards set out in *Securities Act* (Ontario), rules, policies and Commission decisions

Role of the OSC in M&A Transactions (cont'd)

- Enforce existing regulatory regime
- Consider novel practices that may be inconsistent with the underlying policy of the regulatory regime
- Deny bid exemptions in certain circumstances
- Review appropriateness of defensive tactics by target boards
- Intervene on a public interest basis in response to abusive conduct by acquirers

Securities Regulatory Framework for M&A Transactions

- Take-over Bids and Issuer Bids
 - Ontario Securities Act and Commission rules set out specific legal requirements, including take-over bid circular and directors' circular forms
 - Policies provide Commission guidance on interpretation and application of rules as well as views on take-over bid-related issues (i.e. defensive tactics)
- Conflict of Interest Transactions
 - MI 61-101 *Protection of Minority Security Holders in Special Transactions* and related policy
 - Special requirements for transactions involving conflicts of interest (i.e. among related parties)

Conflict of Interest Transactions

- MI 61-101 regulates transactions that may raise conflict of interest concerns because they occur between the company and its related parties
 - These conflicts arise where an insider or significant shareholder could have an informational advantage over other security holders by virtue of voting power, board representation or increased access to information
- Only adopted in Ontario and Québec – However, applies to all TSX and TSXV listed companies
- Intended to level the playing field for minority shareholders

Types of Conflict of Interest Transactions

- MI 61-101 applies to four types of transaction:
 - Related Party Transactions
 - A specified type of transaction between the issuer and a significant shareholder or other related party of the issuer
 - Insider Bids
 - A take-over bid by an insider of the issuer (i.e. director, officer or 10% voting security holder)
 - Issuer Bids
 - An acquisition by the issuer of its own securities
 - Business Combinations
 - A transaction whereby an equity holder is required to sell or exchange its securities without its consent and a related party of the issuer is either the acquirer or is receiving preferential treatment under the terms of the transaction

Requirements for Conflict of Interest Transactions

- MI 61-101 sets out three main requirements for conflict of interest transactions:
 1. Enhanced disclosure
 2. Independent valuation
 3. Minority shareholder approval
- Guidance on role of directors and independent committee review is included in MI 61-101 Companion Policy

Exemptions from Requirements for Conflict of Interest Transactions

- Certain conflict of interest transactions may be exempt from the formal valuation and/or minority approval requirements
- Exemptions in respect of related party transactions include:
 - Fair market value of subject matter of transaction not more than 25% of issuer's market capitalization
 - Issuer not listed on specified senior exchanges (valuation only)
 - Distribution of securities for cash – fair market value not more than \$2.5 million
 - Financial hardship and bankruptcy/insolvency

The application of MI 61-101 to a transaction is fact-specific. Issuers should seek legal advice to confirm compliance with MI 61-101 or the availability of an exemption from its requirements

Requirement #1 - Enhanced Disclosure

- MI 61-101 contains detailed disclosure rules to reduce the information asymmetry between insiders and minority shareholders
- Disclosure document about conflict of interest transaction typically must include:
 - description of background of bid or material terms of transaction
 - discussion of review and approval process adopted by the board of directors or special committee
 - disclosure of any bona fide prior offer received or prior valuation made within last 24 months
 - formal valuation or disclosure of exemption, if any

Requirement #2 - Independent Valuation

- Requirement to obtain formal valuation of subject matter of transaction (i.e. securities or non-cash consideration)
- Board of directors or independent committee will determine who the valuator will be and supervise the preparation of the valuation
- Valuator must be independent of all interested parties to transaction
- Valuator deemed not independent in stated circumstances, including
 - Adviser or external auditor of the issuer (unless will cease to be auditor following the transaction)
 - Success fee payable
- Specific disclosure requirements about valuation and valuator
- Prior valuations must be disclosed in certain circumstances

Requirement #3 - Minority Shareholder Approval

- Requirement to obtain minority approval (by a “majority of the minority shareholders”) for business combinations and related party transactions
- Minority shareholder class determined by excluding votes attached to shares held by the issuer, any interested party, any related party of interested parties or joint actors
- Generally, a party is not an “interested party” if it is treated identically to other shareholders and is not entitled to receive a collateral benefit

Guidance in Conflict of Interest Transactions

Role of Directors

- Commission's view on role of directors or independent special committee in conflict of interest transactions is noted in MI 61-101 Companion Policy
- Expectations for disclosure of board of director review and approval process
 - Provide sufficient information to enable security holders to make an informed decision
 - Disclosure of reasonable beliefs as to fairness of transaction
 - Including material factors considered and analysis of expert opinions
 - Assessment and discussion of formal valuation and any prior valuation
 - Make a useful recommendation
 - Non-recommendation, without reasons, generally insufficient

Guidance in Conflict of Interest Transactions Independent Special Committees

- Companion Policy to MI 61-101 recommends independent special committee for all conflict of interest transactions
 - Good practice for independent committee of disinterested directors to be involved in negotiations and/or review and report on conflict of interest transactions
 - Recommend that independent committee should select valuator and supervise preparation of valuation, when one is required
 - Independent committee provides safeguard against potential unfair advantage for an interested party as a result that party's conflict of interest or informational advantage

Guidance in Conflict of Interest Transactions Independent Special Committees (cont'd)

- “Independence” of a director is a question of fact
- Director deemed not independent in connection with a transaction if the director
 - is an interested party
 - has a material financial interest in an interested party
 - would receive a benefit not generally available to shareholders
- Members of independent committee cannot receive a payment or benefit contingent on completion of the transaction

Risk Oversight

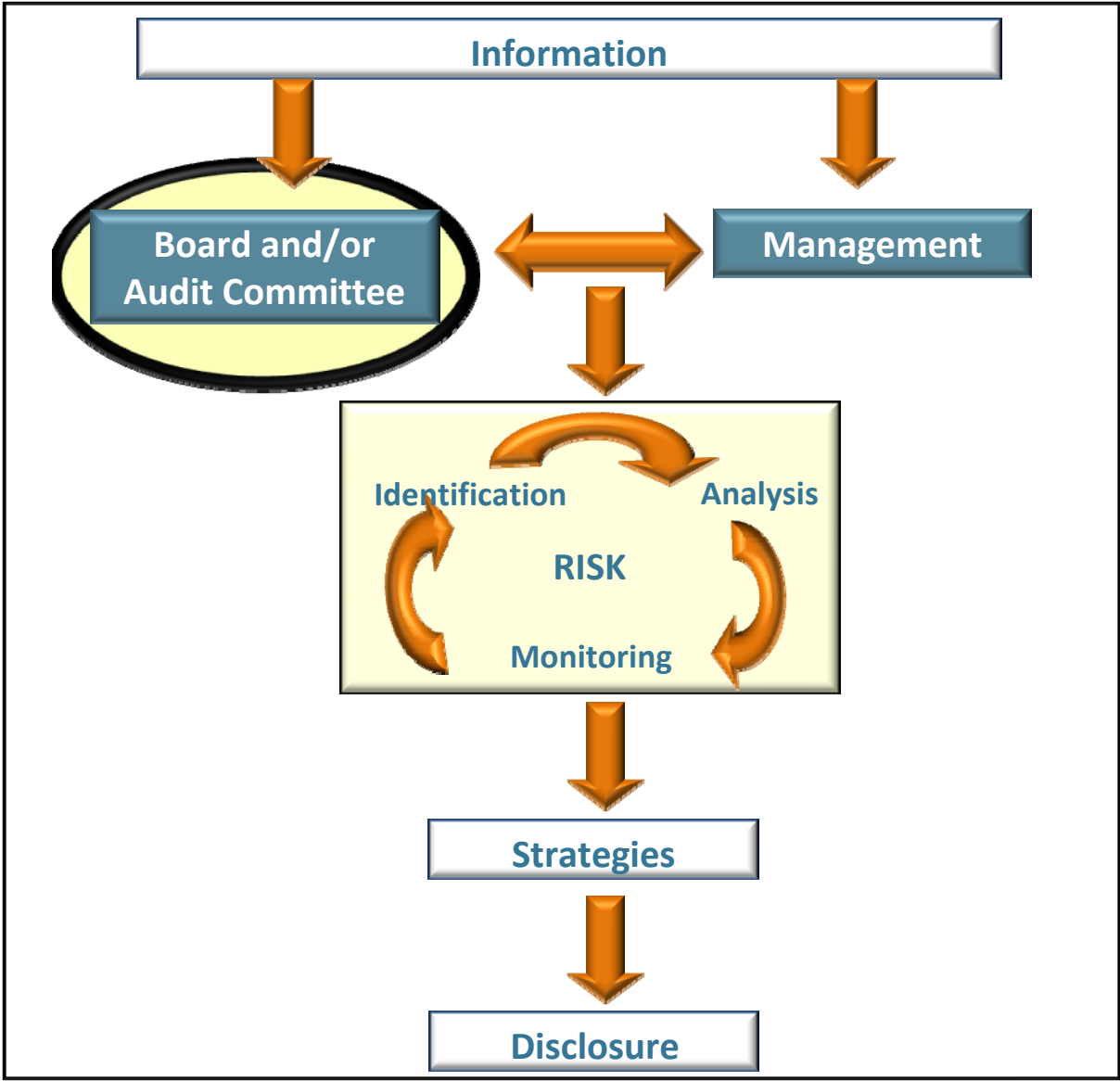
Risk Oversight

*“The risk oversight process is the **means by which the board determines that management has in place a rigorous process for identifying, prioritizing, managing and monitoring its critical risks and that this process is improved continuously as the business environment changes.***

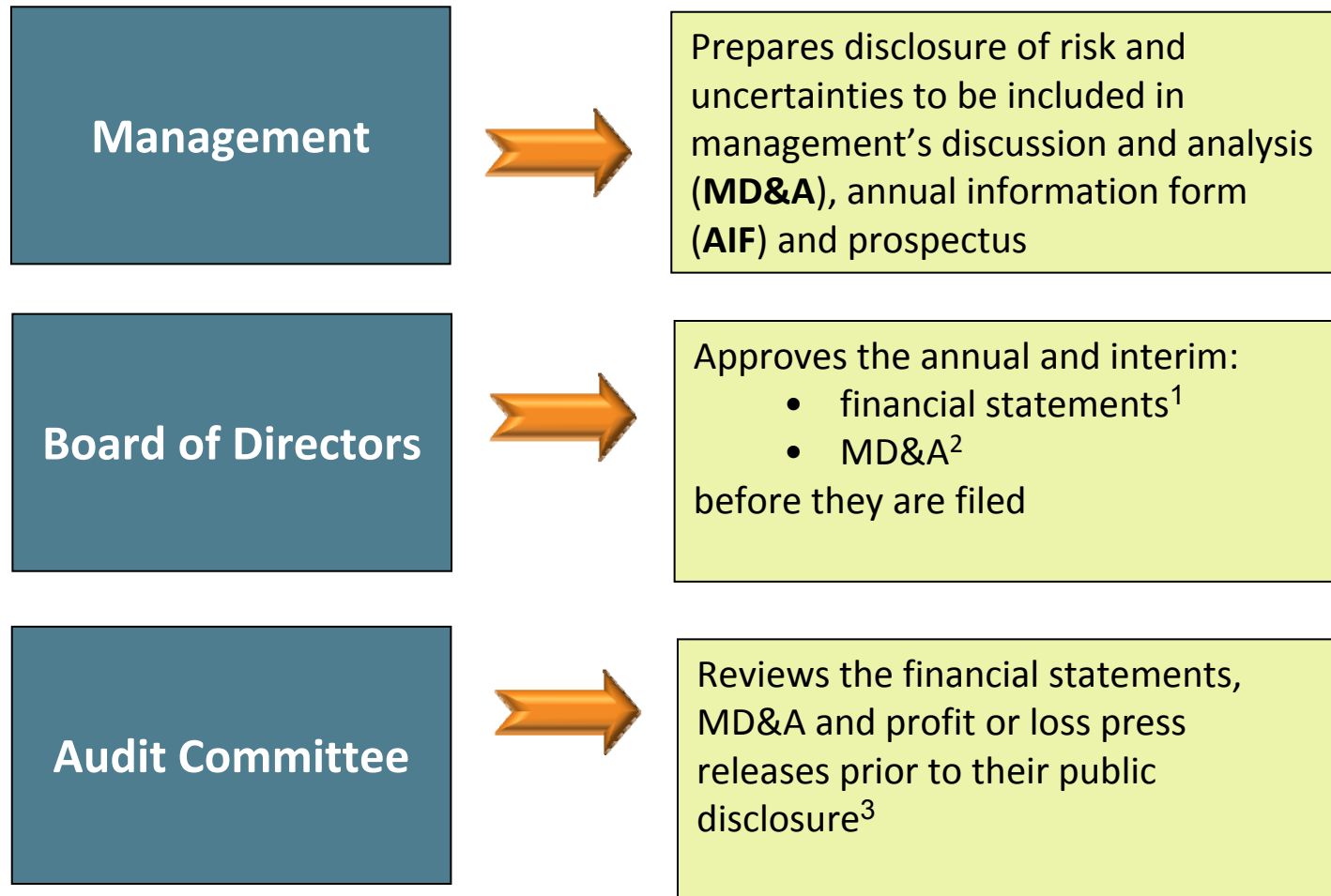
*It also involves **board understanding of the most significant risk exposures and evaluation of whether these exposures are within the enterprise’s appetite for risk-taking**”.*

Committee of Sponsoring Organizations of the Treadway Commission (COSO)

Risk Oversight



Key Players



Notes:

¹ – Responsibility to approve the interim financial reports and MD&A may be delegated to the audit committee

¹ – Item 4.5(1) and (2) of NI 51-102 *Continuous Disclosure Obligations (NI 51-102)*

² – Item 5.5(1) and (2) of NI 51-102

³ – Item 2.3(5) of NI 52-110 *Audit Committee Responsibilities*

Why Risk Oversight is Important

- Following the 2008 economic crisis – focus has been on companies disclosure of risks in securities filings coupled with increased scrutiny of the boards’ role in the risk oversight process
- The board plays an important role in the oversight of the risk management process and internal control system
- It is critical that companies provide meaningful, clear and entity-specific risk disclosure so that investors can:
 - understand the material risks facing the company; and
 - anticipate how these risks may affect their investment in the company (predictive value)
- Studies suggest that investors place great value on companies that provide clear and entity-specific disclosures, which ultimately benefits the company in terms of lower cost of capital

Securities Requirements – Board’s Role in Risk Oversight

- National Policy suggests that the board adopt a written mandate in which it explicitly acknowledges responsibilities for, among other things:
 - 1) adopting a strategic planning process and ***approving, on at least an annual basis, a strategic plan*** which takes into account, among other things, the opportunities and ***risks of the business***;
 - 2) the identification of the ***principal risks*** of the issuer’s business, and
 - 3) ensuring the ***implementation of appropriate systems to manage these risks***.
- Requirements to disclose the board mandate
 - Non-venture issuers must disclose or a description of the board’s roles and responsibilities absent a mandate in the Management Information Circular (**Circular**) or AIF, if a Circular is not prepared
 - Venture issuers not required to disclose

References: National Policy 58-201 – *Corporate Governance Guidelines* (**National Policy** or **NP 58-201**) and National Instrument 58-101 – *Disclosure of Corporate Governance Practices* (**NI 58-101**)

Securities Requirements – Risk Disclosure

Requirements are found in four filings:

1. Financial Statements

Disclose factors such as material uncertainties related to going concern assessment and risks associated with financial instruments¹

2. MD&A

Discuss important trends and risks that have affected the financial statements and those that are reasonably likely to affect them in the future such as a significant risk of defaults or arrears and risks associated with financial instruments²

3. AIF

Disclose risk factors relating to the company and its business that would be most likely to influence an investor's decision to purchase securities of the company³

4. Prospectus

Refer to Appendix for examples of risk disclosure

References:

¹ – IAS 1 *Presentation of Financial Statements* and IFRS 7 *Financial Instruments: Disclosures*

² – Form 51-102F1 of NI 51-102 *Continuous Disclosure Obligations (NI 51-102)*

³ – Form 51-102F2 of NI 51-102, Form 41-101F1 of NI 41-101 *General Prospectus Requirements* and Form 44-101F1 of NI 44-101 *Short Form Prospectus Distributions*

Tips for Fostering Effective Risk Oversight

The Board's Role in Risk Oversight

1. Approve the strategic plan
2. Approve the risk appetite
3. Implement a process for identifying, analyzing and monitoring risks
4. Ensure the implementation of strategies for managing the principal risks
5. Receive relevant, objective and timely information
6. Balance management compensation and risk-taking
7. Review and approve the disclosure of risks in securities filings

Tip #1 – Approve the Strategic Plan

- Approve the strategic plan prepared by management at least annually
- Understand and challenge the key underlying assumptions and potential threats in executing that plan
- Ensure that management reviews and modifies the strategic plan on a periodic basis to reflect changes in internal and external factors that may impact the company
- Receive regular progress updates from management on the execution of the strategic plan

*Acknowledge responsibility for approving the strategic plan.
Review the strategic plan of a periodic basis – it's a live document*

Tip #2 – Approve the Risk Appetite

- Approve the risk appetite so as to specify the acceptable level of risks
- Communicate the overall risk appetite and the different risk tolerances for the different types of risks on a regular basis so that management understands the acceptable levels of risk exposures
- Consider the risk appetite when evaluating new opportunities
- Maintain an open dialogue with management on the appropriateness of the risk appetite as it may vary over time

Establish a common understanding with management on the amount and types of risk that the company should take to pursue its strategy

Tip #3 – Implement a Process for Identifying, Analyzing and Monitoring Risks

- Monitor the business environment (e.g. peers and industry groups) for factors that may impact the company's risk exposures
- Agree with management on the types of risks that should be brought to your attention and how those risks should be prioritized
- Go on site visits to understand the on the ground risks facing the company
- Allocate time in each board meeting to discuss risks facing the company

Knowledge of the company's business is critical to understanding the risks facing the business and the significance of those risks

Tip #4 – Ensure the Implementation of Strategies for Managing the Principal Risks

- Be in sync with management on:
 - The risks that should be actively managed according to a plan
 - The risks that should not be actively management
- Ensure that the policies put in place by management are appropriate to the significance of the risks

Understand the impact of any internal control deficiencies on a timely basis and their potential impact on the company

Tip #5 – Receive Relevant, Objective and Timely Information

- Obtain information that provides insight into the risks facing the company on an ongoing basis
- Require that management provide regular updates to the board on the company's risk profile (e.g. updates throughout the period, not only at quarter end)
- Consider whether internal systems and processes are robust enough to provide sufficient risk related information
- Consult with peers and industry groups to remain abreast of emerging risks

Obtain information from internal and external sources regarding the risks currently facing the company including any emerging risks

Tip #6 – Balance Management Compensation and Risk-Taking

- Understand the behaviour and risks that the company's compensation policies encourage and whether such risks are appropriate
- Consider whether these policies create incentives for management to ignore or increase risk in pursuit for short-term goals
- Consider whether the incentives induce risk-taking in excess of the company's risk appetite
- Be transparent and provide clear disclosure on how executive compensation decisions are determined

For executive compensation disclosure requirements, refer to SME Institute presentation titled "Preparing Your Annual Information Circular", held on January 24, 2013

[Slides available on OSC Website]

Tip #7 – Review and Approve the Disclosure of Risks in Securities Filings

- Require that management provide draft filings well in advance of filing deadlines to allow for sufficient review time
- Critically review the draft filings, ask questions and obtain supporting and corroborating documentation
- Compare the company's disclosure of risks to that of other companies within the same industry and of comparable size

For risk disclosure best practices and examples, refer to SME Institute presentation titled "Continuous Disclosure Special Topics I: Risk and Cash Flows", held on September 18, 2012

[Slides available on OSC Website]

Dealing with the Regulator Boards' Role

Responding to OSC Comment Letters

- Set policy for management to provide comment letters to board or audit committee
- Contact staff if clarification is required
- Provide a comprehensive response to each question asked
- Include detailed analysis, if requested, which reconciles to financial statements or other filings
- Include references to authoritative accounting guidance, if appropriate

Defaults and Refilings

- Default
 - Material deficiencies in filings will result in the issuer being placed in default
 - Implications of default
 - Default status can be avoided if deficiency remedied within short time frame
- Refilings
 - Required to file press release alerting investors of refiling (refer to NI 51-102 s. 11.5)
 - Issuer remains on refilings and error list for a period of 3 years

Pre-filings

- Consult with OSC staff how securities regulation will be interpreted in particular circumstances
- Application pre-filing
 - Circumstances may deal with one or more matters
 - Listed in Ontario only – submit to OSC Applications Administrator
 - Listed in multiple jurisdictions – Passport submission (refer to NP 11-203)

Exemptive Relief Applications

- To seek relief from a securities legislative requirements
 - Applications reviewed on a case-by-case basis
 - Depends on facts and circumstances
 - Prospectus, continuous disclosure or registration
- Process depends on where relief is required
 - Ontario only – procedures outlined in OSC Policy 2.1

Latest Developments

Exempt Market Review

- Published CSA Staff Notice 45-310 *Update on Staff Consultation Note 45-401 Review of Minimum Amount and Accredited Investor Exemptions*
 - Review of the minimum amount and accredited investor prospectus exemptions
- OSC Staff Notice 45-707 *OSC Broadening Scope of Review of Prospectus Exemptions*
 - Considering the introduction of new prospectus exemptions

Proportionate Regulation for Venture Issuers

- Proposed National Instrument 51-103 *Ongoing Governance and Disclosure Requirements for Venture Issuers* was republished on September 13, 2012
- Purpose of initiative
 - To streamline and tailor venture issuer disclosure to make it more useful and user-friendly for investors
 - To make the disclosure requirements for venture issuers more suitable and more manageable for issuers at this stage of development
- The 90-day comment period ended December 12, 2012

Additional Resources

Appendices

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Appendix A

Applicable Legislation – Continuous Disclosure Obligations

Applicable Legislation – Continuous Disclosure Obligations

Ontario Securities Act

- Part 1 *Interpretation* – contains definitions; definitions are also in national instruments
- Part XVIII *Continuous Disclosure* – provisions have been varied and supplemented by National Instrument 51-102
- Part XIX *Proxies and Proxy Solicitation* - provisions have been supplemented by National Instrument 51-102

Rules

What information must be filed

- National Instrument 51-102 *Continuous Disclosure Obligations*
- National Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings*
- National Instrument 52-110 *Audit Committees*
- National Instrument 58-101 *Disclosure of Corporate Governance Practices*
- National Instrument 71-102 *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers*

How the information must be prepared

- National Instrument 52-107 *Acceptable Accounting Principles and Auditing Standards*

How the information must be filed or delivered

- National Instrument 13-101 *System for Electronic Document Analysis and Retrieval (SEDAR)*
- SEDAR Filer Manual
- National Instrument 54-101 *Communication with Beneficial Owners of Securities of a Reporting Issuer*

Applicable Legislation – Continuous Disclosure Obligations (cont'd)

Policies

- Companion Policies - Each of the above national instruments has a companion policy which provides issuers with guidance on how to interpret the legal requirements
- National Policy 51-201 *Disclosure Standards*

FAQs

- CSA Staff Notice 54-301 *Frequently Asked Questions about National Instrument 54-101 Communication with Beneficial Owners of Securities of a Reporting Issuer*

For more information, all rules, policies and notices are available on the OSC website at www.osc.gov.on.ca, except for the *SEDAR Filer Manual* which is available at www.sedar.com

Rules, Policies and Notices Related to the Consequences of Default

Late fees

- OSC Rule 13-502 *Fees*, subsection 4.3(1) and Appendix D, item A

Defaults

- OSC Policy 51-601 *Reporting Issuer Defaults*
- CSA Notice 51-322 *Reporting Issuer Defaults*

Refilings

- OSC Staff Notice 51-711 *List of Refilings and Corrections of Errors as a Result of Regulatory Reviews*

Cease trade orders

- National Policy 12-203 *Cease Trade Orders for Continuous Disclosure Defaults*
- National Policy 12-202 *Revocation of Compliance-related Cease Trade Order*

For more information, all rules, policies and notices are available on the OSC website at www.osc.gov.on.ca, except for the SEDAR Filer Manual which is available at www.sedar.com

Appendix B

Venture vs. Non-Venture Requirements

Venture vs. Non-Venture Requirements

Difference	Venture Issuer	Non-Venture Issuer	Disclosure Requirement
Filing Deadline for Annual Financial Statements	120 days after year end	90 days after year end	Section 4.2 NI 51-102
Filing Deadline for Interim Financial Statements	60 days after interim period end	45 after interim period end	Section 4.4 NI 51-102
MD&A Disclosure	Additional disclosure requirements if no significant revenues from operations in the last two financial years	Additional disclosure not applicable to non-venture issuers	Section 5.3 NI 51-102
Certification of Disclosure in Issuers' Annual and Interim Filings	No requirement to provide representations related to establishment and maintenance of DC&P and ICFR	Must provide representations related to establishment and maintenance of DC&P and ICFR	NI 52-109
AIF	No AIF required (unless issuer wants to file a short form prospectus)	Must file AIF	Section 6.1 NI 51-102
Determination of Significance for Filing BAR	Significance determined based on 2 tests (asset or investment test) at 40% level	Significance determined based on 3 tests (asset, investment or income test) at 20% level	Section 8.2 NI 51-102
Report of Voting Results	No requirement to report	Must report	Section 11.3 NI 51-102
Statement of Executive Compensation	No requirement to provide performance graph	Must provide performance graph	Item 2.2 Form 51-102F6
Corporate Governance Disclosure	No requirement to disclose Board mandate or position descriptions	Must disclose Board mandate and position descriptions	Form 58-101 F1/F2

Appendix C

Insider Reporting

Applicable Legislation – Insider Reporting Obligations

Ontario Securities Act

- Part 1 *Interpretation* – contains definitions; definitions are also in national instruments
- Section 107 – provision has been varied and supplemented by national instruments

Rules

- National Instrument 55-102 *System for Electronic Disclosure by Insiders (SEDI)*
- National Instrument 55-104 *Insider Reporting Requirements and Exemptions*
- National Instrument 71-102 *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers*

Late fees

- OSC Rule 13-502 *Fees*, Appendix D, item B

Policies

- Companion Policies - Each of the above national instruments has a companion policy which provides insiders and issuers with guidance on how to interpret the legal requirements

FAQs

- CSA Staff Notice 55-312 *Insider Reporting Guidelines for Certain Derivative Transactions (Equity Monetization)*
- CSA Staff Notice 55-315 *Frequently Asked Questions about National Instrument 55-104 Insider Reporting Requirements and Exemptions*
- CSA Staff Notice 55-316 *Questions and Answers on Insider Reporting and the System for Electronic Disclosure by Insiders (SEDI)*

For more information, the documents listed above have been posted on the OSC website at www.osc.gov.on.ca

What Must Be Disclosed in Insider Reports?

- When reporting an acquisition or disposition of a security, insider report must disclose:
 - Security designation (e.g., common shares)
 - Ownership type (e.g., beneficially owned directly, beneficially owned indirectly, controlled or directed)
 - Identity of holder of securities where ownership is indirect or where control or direction is exercised
 - Date of transaction
 - Nature of transaction (from list provided – e.g., acquisition or disposition in public market)
 - Number or value of securities acquired/disposed of
 - Unit price or exercise price
 - Currency paid

How Must Insider Reports Be Filed?

- Insider reports must generally be filed on SEDI so public can view them at www.sedi.ca
- Before a reporting insider files their first report on SEDI, they must file an insider profile
 - An insider profile must disclose:
 - Insider's full legal name and contact information
 - Insider's relationship to company (from list provided – e.g., director)
 - Date the insider became an insider
 - A reporting insider must keep their insider profile up-to-date

For more information, see:

- **National Instrument 55-102, sections 2.1 and 2.2**
 - **Form 55-102F1 and Form 55-102F2**

Issuer Profile Supplement

- Before reporting insiders can file insider reports on SEDI disclosing their holdings in securities of a company, the company must file an issuer profile supplement on SEDI
- Issuer profile supplement must disclose:
 - Name and contact information for insider affairs contact of company
 - Security designations of company (e.g., common shares, different series of preferred shares or debt securities)
- A company must keep their issuer profile supplement up-to-date

Issuer Event Report

- **Issuer event** – a stock dividend, stock split, consolidation, amalgamation, reorganization, merger or other similar event that affects all holdings of a class of securities of a company
- A company must file an issuer event report on SEDI within one business day of an issuer event
- Issuer event report must disclose:
 - Issuer event type (from list provided – e.g., stock split)
 - Effective date of issuer event
 - Issuer event details

Insider Reporting Exemptions

- Automatic securities purchase plan
- Issuer grants
- Normal course issuer bids
- Publicly disclosed transactions
- Issuer events

Appendix D
Applicable Legislation
– M&A Transactions

Appendix D – Applicable Legislation – M&A Transactions

Item	Reference
Ontario Securities Act	<ul style="list-style-type: none"> ▪ Part XX - Take-Over Bids and Issuer Bids
Rules	<ul style="list-style-type: none"> ▪ OSC 62-504 <i>Take-over Bids and Issuer Bids</i> ▪ MI 62-104 <i>Take-over Bids and Issuer Bids</i> <ul style="list-style-type: none"> ▪ Applicable in all Canadian jurisdictions, except Ontario ▪ Multilateral Instrument 61-101 <i>Protection of Minority Security Holders in Special Transactions</i> <ul style="list-style-type: none"> ▪ Ontario and Quebec only
Policies	<ul style="list-style-type: none"> ▪ National Policy 62-203 <i>Take-over Bids and Issuer Bids</i> ▪ National Policy 62-202 <i>Take-over Bids – Defensive Tactics</i> ▪ Companion Policy to Multilateral Instrument 61-101

Appendix E

Risk Requirements and Risk Disclosure Examples

Appendix E – Risk Requirements

Disclosure Requirement	Reference
The board's role in risk oversight	<ul style="list-style-type: none"> ▪ NI 58-101 <i>Disclosure of Corporate Governance Practices</i>, Item 2 of Form 58-101F1 (non-venture issuers) ▪ NP 58-201 <i>Corporate Governance Guidelines</i>, Item 3.4
MD&A risk disclosure	<ul style="list-style-type: none"> ▪ Form 51-102F1 of NI 51-102 <i>Continuous Disclosure Obligations</i> <ul style="list-style-type: none"> • Part 1 (a) General Provisions • Item 1.2 Overall Performance • Item 1.4 Results of Operations • Item 1.6 Liquidity • Item 1.8 Off-Balance Sheet Arrangements • Item 1.12 Critical Accounting Estimates • Item 1.14 Financial Instruments and Other Instruments
AIF risk disclosure	<ul style="list-style-type: none"> ▪ Form 51-102F2 of NI 51-102 <i>Continuous Disclosure Obligations</i> <ul style="list-style-type: none"> • Part 1 (a) General Provisions • Items 5.2 Risk Factors • Item 7.3 Ratings

Reference: <http://www.osc.gov.on.ca/en/6439.htm>

Appendix E – Risk Requirements (cont'd)

Disclosure Requirement	Reference
Prospectus offering documents	<ul style="list-style-type: none"> ▪ Form 41-101F1 of NI 41-101 General Prospectus Requirements <ul style="list-style-type: none"> • Item 1.10 Risk factors • Item 3.1(1)(d) Summary of Prospectus - General • Item 10.3(1)(14) Description of Securities Distributed – Asset-backed securities • Item 10.4(g) Description of Securities Distributed – Derivatives • Item 10.9 Ratings • Item 21.1 Risk factors ▪ Form 44-101F1 of NI 44-101 <i>Short Form Prospectus Distributions</i> <ul style="list-style-type: none"> • Item 7.3(9) Description of Securities Distributed – Asset-backed securities • Item 7.4(g) Description of Securities Distributed – Derivatives • Item 7.9(e) Ratings • Item 17.1 Risk factors

Reference: <http://www.osc.gov.on.ca/en/6434.htm>

IOR of Risk Disclosures – Examples (cont'd)

Market for new products/market participation – non-compliant disclosure

In order to remain competitive, we plan to introduce several news products in the coming years. As communicated in our most recent filings, we plan to launch products that meet the needs of customers and produce these products in the most cost effective way. In order to determine the needs of customers, our external consultants conduct surveys on a frequent basis to determine the styles and colours that meet their needs. Based on the results of these surveys, we develop techniques and processes that can produce the desired products in the most cost effective way. When a new product is introduced, there is no certainty that it will be accepted by our customers. This may adversely impact our business.

IOR of Risk Disclosures – Examples (cont'd)

Market for new products/market participation: compliant disclosure

When a new product is introduced, there is no certainty that it will be accepted by our customers. We believe that product Star, expected to be launched in early 2012, has attributes that consumers will find attractive relative to its competition. These attributes include longer shelf life, more efficient processing capabilities and cheaper per unit price. However, there is no guarantee that these positive attributes will result in product Star displacing competitive products that are currently on the market. While we expect the launch of product Star to result in 20% increase in our overall sales, there is no guarantee that this will occur. A failure to successfully launch product Star may result in a failure to achieve the sales targets and pressure on our financial position, which is more fully discussed elsewhere in this document. A product launch failure may also negatively impact the value of our brand in the marketplace. These potentially adverse consequences could place downward pressure on our common share price.

Entity specific

Potential impact

IOR of Risk Disclosures – Examples (cont'd)

Risks unique to operations in Country ABC – non-compliant disclosure

If the Company's operations in Canada needs additional resources to undertake new projects, the Company may face delays repatriating funds held in Country ABC. Our business and operations could be materially and adversely affected.

IOR of Risk Disclosures – Examples (cont'd)

Risks unique to operations in Country ABC – compliant disclosure

Entity specific

One of the Company's material subsidiaries, Subsidiary A, earns all of its revenues in Country ABC which operates with currency A. Under current Country ABC regulation, the transfer of after-tax profits is limited to x% of subsidiary revenues in currency A on an annual basis. While the regulatory body Luzonzo is relaxing restrictions on the transfer of funds to countries outside of Country ABC, there is no certainty that future after-tax profits from Subsidiary A can be repatriated back to Canada.

Potential impact

If the Company's operations in Canada needs additional resources to undertake new projects, the Company may face delays repatriating funds held in Country ABC. Our business and operations could be materially and adversely affected. There can be no guarantee that these repatriation limits will not be changed so as to require the prior approval of the regulatory body Luzonzo to repatriate profits back to Canada. Any failure to obtain the prior approval from the regulatory body Luzonzo may affect our ability to expand operations and achieve our objectives. To mitigate this risk, the Company and its board of directors proactively monitor and engage experts to understand the developments of regulatory body Luzonzo and to assess how any changes or proposed changes may impact the Company's business.

Strategies to mitigate the risks

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Questions?