

Problematic Promotional Activities: What SME issuers need to know

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OSC SME Institute - Objectives

- Help small and medium-sized enterprises (SMEs) navigate regulatory waters
- Explain disclosure requirements to assist with compliance so issuers can focus on building their business
- Provide an opportunity for information dialogue with staff of the Corporate Finance Branch of the Ontario Securities Commission

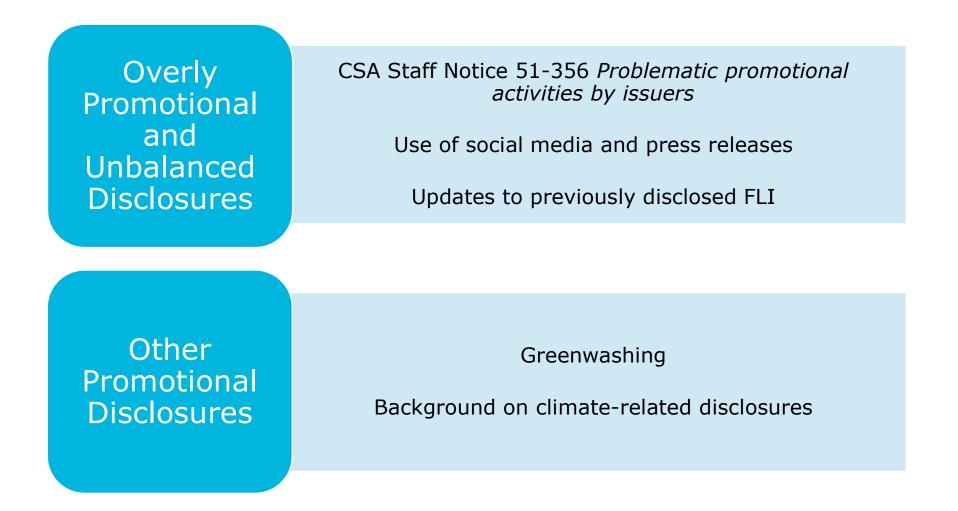
OSC SME Institute – Recent Topics

Recordings of prior SME webinars are available at

www.youtube.com/user/OntarioSecurities

- February 2023 Hot Topics in Continuous Disclosure: What small and medium issuers need to know
- March 2023 Prospectus Filings and Exemptions: What small and medium issuers need to know
- February 2024 SEDAR+: Practical Tips for Error-Free Filings

OSC SME Institute – Today's Topics



Overly Promotional and Unbalanced Disclosures: CSA Staff Notice 51-356 *Problematic promotional activities by issuers*

Problematic Promotional Activities

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- In November 2018, the CSA published CSA Staff Notice 51-356 *Problematic Promotional Activities by Issuers*, in response to observations of promotional and unbalanced disclosure by issuers
- This type of problematic disclosure is often a concern for small and medium sized issuers, such as venture issuers
- The staff notice provides numerous examples of the types of problematic promotional activities we observed
- Issuers should be mindful of these potential issues, which could result in:
 - A request to refile, amend or supplement disclosure during an OSC continuous disclosure review
 - $_{\odot}$ In egregious cases, OSC Enforcement action

Additional Policy and Staff Guidance related to Problematic Promotional Activities

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- Extracts from National Policy 51-201 *Disclosure Standards*:
 - Announcements of material changes should be factual and balanced
 - Unfavourable news must be disclosed just s promptly and completely as favourable news
 - An issuer's press release should contain enough detail to enable the media and investors to understand the substance and importance of the change it is disclosing
 - Issuers should avoid including unnecessary details, exaggerated reports or promotional commentary
- Extracts from s. 126.2 of the Securities Act (Ontario)
 - Do not make a statement that is misleading or untrue, or which does not state a fact that is necessary to make the statement not misleading and would be expected to have a significant effect on the market price of a security

Additional Policy and Staff Guidance related to Problematic Promotional Activities

• National Policy 51-201 *Disclosure Standards*

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- CSA Multilateral Staff Notice 51-336 Issuers Using Mass Advertising
- CSA Multilateral Staff Notice 51-348 *Staff's Review of Social Media Used by Reporting Issuers*
- OSC Staff Notice 51-734 Corporate Finance Branch 2022
 Annual Report
 - Refer to "Overly promotional press releases" (page 25–27)



Example #1 – A statement about revenue potential for a development stage (pre-revenue) issuer

The Company anticipates revenue of \$20 million over the next 5 years, with significant growth thereafter.



Disclosure is unbalanced. Staff are likely to view the description as insufficient disclosure.



Before the Company begins generating revenue, it will need to complete production of a prototype unit, test the prototype and remediate any defects, and submit for / obtain regulatory approval for the device. We expect this could take 2-3 years and cost between \$2 million and \$5 million depending on the extent of any issues. If regulatory approval is obtained in year 3, we anticipate that initial sales revenue could begin in mid 2024.



Disclosure is enhanced. This description provides investors with relevant information.

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Example #2 – A statement about new business opportunities

The Company is entering the crypto currency industry where it will operate a proprietary crypto trading platform.



Disclosure is unbalanced. Staff are likely to view the description as insufficient disclosure.



Example #2 – A statement about new business opportunities

The Board has approved a change of business whereby the Company will move into the crypto industry. Management has experience operating in the crypto industry and the Company is exploring development of a crypto trading platform. At this time, the Company does not have any crypto-related assets and has not expended any resources towards developing any crypto-related operations. The time/cost to develop these operations is currently unknown as a result of the early-stage nature of this initiative.



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Disclosure is enhanced. This description provides investors with relevant information.

Example #3 – Disclosure about an acquisition

The Company has signed an agreement to complete the transformational acquisition of Promo Corp, representing a \$500 million opportunity for the Company which will be immediately accretive.



Disclosure is unbalanced. Staff are likely to view the description as insufficient disclosure.



Example #3 – Disclosure about an acquisition

The Company has signed a non-binding letter of intent for the acquisition of Promo Corp. If completed, subject to the due diligence of both parties and receipt of exchange approvals, we expect the acquisition would be accretive in year 1, provided that Promo Corp is successful in opening its first store location in November. The market Promo Corp operates in has industry-wide demand of \$500 million and is growing rapidly, representing a significant opportunity for the Company.



Disclosure is enhanced. This description provides investors with relevant information.

Example #4 – Hyperbolic Disclosure

This is a COVID-cure style breakthrough which will be the play of the decade for early-stage investors.



Disclosure is unbalanced. Staff are likely to view the description as insufficient disclosure.

Example #4 – Hyperbolic Disclosure

The Company's drug will have a significant addressable market. We anticipate it will take 2-3 years and \$100 million to complete phase 2/3 drug trials and to confirm the drug is safe and effective.



Disclosure is enhanced. This description provides investors with relevant information.

Other Examples – Problematic Promotional Activities

Bad news buried at the end of a multi-topic press release with positive headlines.

Overly frequent and non-substantive press releases which make negative and potentially more substantive news harder to see.

Announcing positive initiatives (i.e. non-binding LOIs) without subsequent disclosure when the opportunity falls through.

Unfounded comparisons to more established companies.

Claims which cannot be supported.

Failing to disclose bad news, costs/barriers to success while favouring disclosure of good news.

Overly Promotional and Unbalanced Disclosures: Use of social media and press releases



Use of Social Media

- CSA Staff Notice 51-348 *Staff's Review of Social Media Used by Reporting Issuers*, was published in March 2017.
- The notice discusses the following problematic disclosure practices:
 - Selective or early disclosure when some investors receive material information through social media that other investors do not receive because it is not generally disclosed.
 - Misleading and unbalanced social media disclosure where information is not sufficient to provide a complete picture or is inconsistent with information already disclosed by issuers on SEDAR+.
 - Insufficient social media governance policies in place to support social media activity.

Examples – Misleading or unbalanced social media disclosure

Corporate presentations or investor decks on the issuer's website contain information which is inconsistent with or contradicted by the financial statements or other information on SEDAR+.

Non-GAAP financial measures used on social media which are not included in any regulatory filing (such as the MD&A) and where typical non-GAAP disclosures (such as but not limited to a quantitative reconciliation) were not provided.

The use of paid for analyst reports where the non-independent nature of these reports is not adequately or prominently disclosed.

Untrue, unsupported, hyperbolic or overly promotional statements.

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Best Practices for Press Releases

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Issuers should **consider the disclosure best practices** for press releases provided on page 27 of OSC Staff Notice 51-734 *Corporate Finance Branch 2022 Annual Report*

- establish appropriate written disclosure policies focused on promoting consistent disclosure practices aimed at providing informative, timely and broadly disseminated disclosure of material information to the market
- consult with advisors, as appropriate, to ensure that the information in the news release is balanced and not misleading or overly-promotional
- assess the materiality of the information being disseminated and consider whether a material change report should be filed
- ensure that disclosure in any news release is sufficiently detailed to understand its substance and importance to the Reporting Issuer's business and operations
- ensure the disclosure is consistent with disclosures previously filed by the Reporting Issuer in news releases or continuous disclosure documents
- ensure **FLI** is appropriately supported by material factors and assumptions and updated as required
- have the board of directors or audit committee review the disclosure in advance of public release, which may increase the quality, credibility and objectivity of such disclosure. Refer to 6.4(1) of NP 51-201
- ensure all material information has been included and discussed in the MD&A

Overly Promotional and Unbalanced Disclosures: Updates to previously disclosed FLI

What is forward-looking information?

Forward-looking information (FLI)

Disclosure regarding:

- possible events
- possible financial performance

Based on:

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- future economic conditions
- future courses of action
- includes other information such as:
 - key performance indicators
 - targeted efficiencies
 - metal price assumptions
 - projected production levels

Future Oriented Financial Information (FOFI)

Forward-looking financial information presented in the format of historical financial statements.

Financial Outlook

Forward-looking financial information **NOT** presented in the format of historical financial statements.

Examples include:

- projected EBITDA
- projected earnings per share (EPS)
- revenue targets
- operating ratios
- R&D spending
- projected operating costs

Forward-looking information

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National Instrument 51-102 Continuous Disclosure Obligations

- PART 4A Forward looking information
- PART 4B FOFI and financial outlooks
- PART 5.8 Disclosure relating to previously disclosed material forward-looking information

When disclosing FLI an issuer shall:

- > Identify material FLI as such and specify material risk factors
- > Have a reasonable basis upon which the FLI is derived
- > State the material factors and assumptions used in the developing the FLI
- Describe the issuer's policy for updating FLI
- Limit FOFI/financial outlook to a period in which the information forming the FLI can be reasonably estimated



Example – Historical MD&A Disclosure

Since starting operations in 2022, we have focused on growing our number of retail store locations. We have a total of 36 and 16 stores open as at December 31, 2023 and 2022 respectively. Of the 20 stores opened in 2023, 17 were opened in the last 3 months of 2023. The accelerating pace of new store openings is leading to accelerated revenue growth.



Example – Deficient FLI Disclosure

We will aggressively pursue growth opportunities and anticipate that we will increase our store count by 70 new stores in 2024, to reach 106 stores by end of fiscal 2024. We also anticipate that we will reach 256 stores by end of fiscal 2025, and 400 stores by end of fiscal 2026. By rapidly growing our store base, we expect to grow sales to \$500 million by the end of fiscal 2026.



Disclosure is deficient because there are no material factors and assumptions to support the FLI.

Example – Enhanced FLI Disclosure

We will aggressively pursue growth opportunities and anticipate that we will increase our store count by 70 new stores in 2024, to reach 106 stores by end of fiscal 2024, which corresponds to expected sales of \$50 to 80 million for fiscal 2024. We are focused on expanding the number of stores in a responsible manner and using a reasoned growth strategy, targeting major urban centres which meet pre-defined population and income criteria. Management believes this growth target is achievable based on the following assumptions:

- We have agreements, leases and planned launch dates in place for 40 of the 70 new store openings planned for 2024;
- We have substantially negotiated the terms for 15 of the 70 new store openings planned for 2024, but launch dates and locations are still being finalized;
- We are in active discussions with major retail partners for 15 of the 70 new store openings planned for 2022;
- We assume stores are opened evenly throughout the year and generate on average approximately \$0.7- \$1.1 million in sales, depending on location.



Disclosure is enhanced. This description provides investors with relevant information.

Updating Previously Disclosed FLI

Previously Disclosed FLI (Provided in the December 2023 Annual MD&A)	Update for Current Results to Date (Provided in the March 2024 Interim MD&A)
We have agreements, leases and planned launch dates in place for 40 of the 70 new store openings planned for 2024;	We have launched 15 of the 70 planned new store openings for 2024 and are on track to meet the previously disclosed target of 70 store openings in 2024. For the remaining 55 stores to be launched in 2024, we now have agreements/leases in place for 45 of them.
We have substantially negotiated the terms for 15 of the 70 new store openings planned for 2024, but launch dates and locations are still being finalized;	We have now substantially negotiated terms for a total of 30 stores, with 15 of them having been launched in the YTD, and launch dates planned for a further 10 of them.
We are in active discussions with major retail partners for 15 of the 70 new store openings planned for 2024;	We have completed successful negotiations with 15 retail partners and have initiated negotiations with a further 10 retail partners, in relation to planned 2024 store openings.
We assume stores are opened evenly throughout the year and generate on average approximately \$0.7- \$1.1 million in sales, depending on location. As a result, we expect total sales of \$50 to 80 million for fiscal 2024.	Due to shift in retail consumer trends away from physical retail stores and towards digital platforms, we have revised our assumptions for average store sales to approximately \$0.5 million - \$0.8 million, for expected total sales of \$35M to \$56M for fiscal 2024.

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Withdrawing Previously Disclosed FLI

- XYZ Company discloses projected annual revenue for 2024 to be \$3M
- As at Q2 2024, XYZ Company has reported \$800K in total sales
- The business does not experience seasonality

Example disclosure

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During the second quarter ended June 30, 2024, the Company became aware of certain government restrictions on sales of product B, which have rendered our assumptions relating to revenue projections unrealistic, and as such, the Company is withdrawing our previously issued fiscal 2024 revenue projections. In addition, the estimated opening of 3 more locations originally planned for fiscal 2024 will not be completed until next year in order to address new government regulation, as well as continued supply chain issues.

Regulatory Responses to Problematic Promotional Activities

Problematic promotional activities may result in **enforcement action or other regulatory responses** such as requiring an issuer to:

• Issue a clarifying news release

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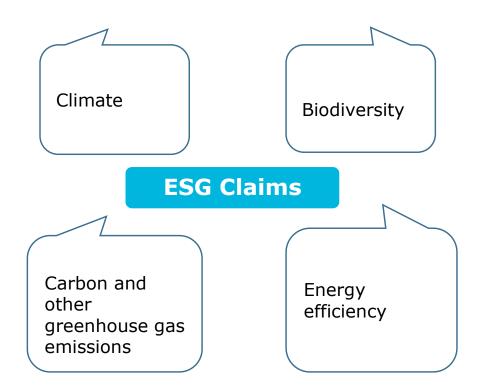
- Retract or remove overly promotional language from disclosure record (including website and/or social media)
- Re-file continuous disclosure documents

Other Promotional Disclosures: Greenwashing

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What is greenwashing?

Misleading, unsubstantiated or otherwise incomplete claims about business operations or the sustainability of a product or service being offered, conveying a false impression.



- CSA Staff Notice 51-364 Continuous Disclosure Review Program Activities for the fiscal years ended March 31, 2022 and March 31, 2021
- OSC Staff Notice 51-735 Corporate Finance Branch 2023 Annual Report

Existing Requirements and Guidance

Overly promotional disclosure

- CSA Staff Notice 51-356 Problematic promotional activities by issuers
 - Discusses concerns with disclosure and promotional campaigns that provide unbalanced/unsubstantiated material claims about the issuer's business

Misleading statements

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- National Policy 51-201 Disclosure Standards
 - General prohibitions against false or misleading statements that would be expected to have a significant effect on the price or value of an issuer's securities

Forward-looking information (FLI)

- Parts 4A & 4B and section 5.8 of National Instrument 51-102 *Continuous Disclosure Obligations*
 - Disclosure of material factors and assumptions; updates to previously issued FLI



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Example of Greenwashing: Net Zero

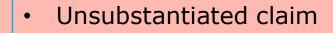
- Disclosure of target to transition to net zero
- Misleading if no credible plan to achieve target is provided
- Include: Disclosure that is factual and balanced

All public disclosures, whether voluntary or required should be factual and balanced



Example of Greenwashing: Carbon Neutral CSA Staff Notice 51-364

"The Company plans to be carbon neutral by 2023."



• Statement may be FLI



Example of Greenwashing: Emissions Reduction CSA Staff Notice 51-364

"Strategic relationship with high-quality partners attentive to environmental stewardship and performance enhance our long-term value. Our key partner exemplifies this by setting aggressive emissions reduction targets and investing in multiple environmental/economic-enhancing technologies."



- Promotional language
- No accompanying disclosures



Example of Greenwashing: "Global Leader" CSA Staff Notice 51-364

"The Company is a global leader in environmental solutions."



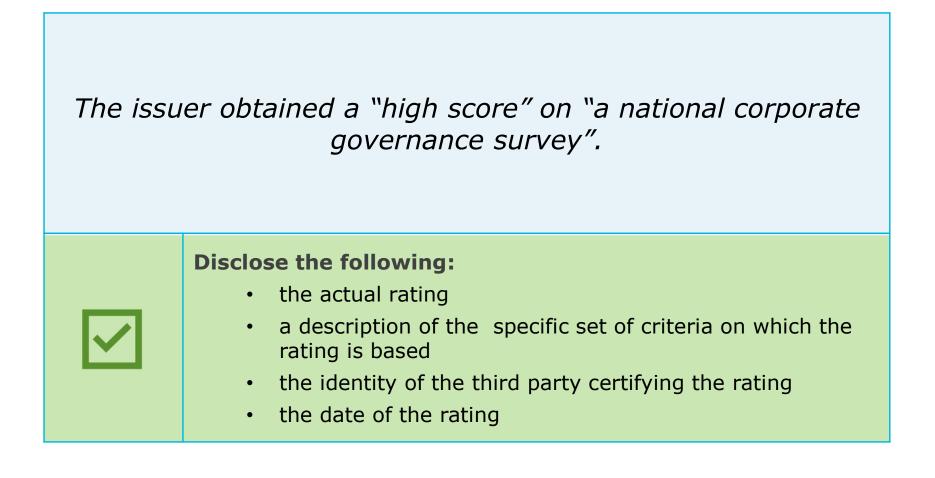
- Promotional language
- Nominal revenue from operating activities

Forward-Looking Information

Reminder Regarding Forward-Looking Statements

Where an Issuer discloses future plans to improve its operational performance in the context of ESG standards, such as to reduce greenhouse gas emissions or to obtain a carbon neutral position, the Issuer is reminded that this type of statement will typically constitute FLI. An Issuer must have a reasonable basis for FLI, identify the material risks factors that could cause actual results to differ materially, state the material factors or assumptions used to develop the FLI and describe its policies for updating the information. COMMISSION

Example of Greenwashing: ESG Ratings 2023 Corporate Finance Branch Report



Background on climate-related disclosures



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- Generally, materiality is the determining factor of any assessment of whether information is required to be disclosed in an issuer's continuous disclosure.
- For purposes of continuous disclosure documents, information is likely material if a reasonable investor's decision whether to buy, sell or hold securities in an issuer would likely be influenced or changed if the information in question was omitted or misstated.
- See Form 51-102F1 (MD&A), Part 1(f) and Form 51-102F2 (AIF), Part 1(e).

What are the specific considerations for determining materiality in the context of climate change-related risk?

- We have encouraged issuers to undertake analysis of climate-change related risks, including adjusting their approach to:
 - 1.<u>Time horizon</u>: materiality assessments should not be limited to the short term.

2. <u>Measurement</u>: issuers should not only consider existence of climatechange related risks, but also (where practicable), quantify and disclose the potential financial impact.

Existing Requirements

Material commitments, events, risks or uncertainties that management reasonably believes will materially affect the company's future performance	Material risk factors	Environmental policies that are fundamental to operations, including the steps taken to implement them
MD&A 51-102F1 Item 1.4(g)	AIF 51-102F2 Item 5.2	AIF 51-102F1 Item 5.1(1)(k) Item 5.1(4)
	Forward Looking Information 51-102 (4A, 4B, 5.8)	

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CSA Guidance

Environmental	CSA Staff Notice 51-333 <i>Environmental</i>
(general)	<i>Reporting Guidance</i> (October 2010)
Climate- related (specific)	CSA Staff Notice 51-354 <i>Report on Climate</i> <i>Change-related Disclosures Project</i> (April 2018) CSA Staff Notice 51-358 <i>Reporting of Climate</i> <i>Change-related risks</i> (August 2019)

Guidance on climate-related risks

1. Examples

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 Sets out examples of climate change-related risks that may affect companies and the related financial impacts

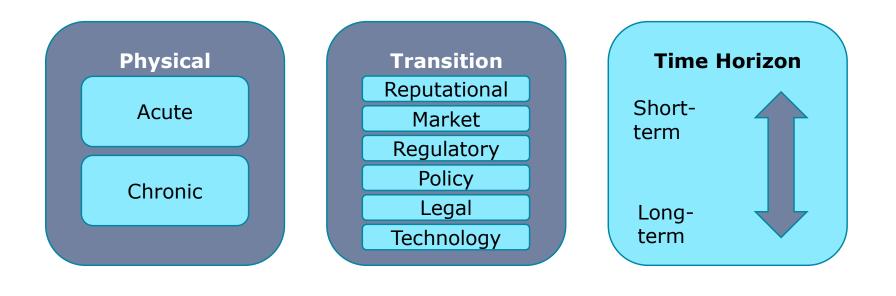
2. Practical support to boards and management

 Provides select questions to help inform their consideration of material climate change-related risks and making appropriate disclosure

3. Materiality guidance

 Provides both general principles and specific considerations for determining materiality in the context of climate change-related risks

Climate-Related Risks



CSA Staff Notice 51-358

Damage to assets	Supply chain and operational disruptions	Availability and quality of water	Availability of insurance and financing
Increased costs in a variety of areas, including GHG emissions	Restrictions on licenses	Increased regulation and litigation	Shifts in customer perceptions and preferences
	Stigmatization of the issuer's market sector or industry	Increased shareholder concern or negative shareholder feedback	

CSA Staff Notice 51-358



Balance sheet – assets

valuation/impairment stranded assets



Balance sheet liabilities

contingent liabilities legal claims regulatory sanctions or penalties reclamation liabilities



Income statement

Decreased revenue due to decreased demand, regulatory restrictions, supply chain and operational interruptions

Increased expenses due to higher costs (water, energy, insurance, cost of capital, capital expenditures), legal claims, penalties, regulatory costs (carbon tax) ONTARIO

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Recent developments

International

- International Sustainability Standards Board
- Securities and Exchange Commission

Domestic

- Canadian Sustainability Standards Board
- Canadian Securities Administrators

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