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19 September 2002

Alberta Securities Commission
British Columbia Securities Commission
Manitoba Securities Commission
Securities Administration Branch, New Brunswick
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Department of Justice, Government of the Northwest Territories
Nova Scotia Securities Commission
Registrar of Securities, Legal Registries Division, Department of Justice, Government of Nunavut
Ontario Securities Commission
Office of the Attorney General, Prince Edward Island
Commission des valeurs mobilières du Québec
Saskatchewan Securities Commission
Registrar of Securities, Government of Yukon

Peter Brady, Chair of the Continuous Disclosure Harmonization Committee
British Columbia Securities Commission
PO Box 10142, Pacific Centre
701 West Georgia Street
Vancouver, British Columbia V7Y 1L2
and
Denise Brosseau, Secretary
Commission des valeurs mobilières du Québec
Stock Exchange Tower
800 Victoria Square
P.O. Box 246, 22nd Floor
Montréal, Québec H4Z 1G3

**Re: Proposed National Instrument 51-102 *Continuous Disclosure Obligations* (NI 51-102)
Proposed National Instrument 71-102 and Companion Policy 71-102CP *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers* (NI 71-102 and Policy)**

Dear Sirs and Mesdames:

The Canadian Advocacy Committee (CAC) of the Association for Investment Management and Research (AIMR)[1] is pleased to respond to the request for comments on the CSA's proposal for

[1] With headquarters in Charlottesville, VA, and regional offices in Hong Kong and London, the Association for Investment Management and Research® is a non-profit professional organization of over 59,700 financial analysts, portfolio managers, and other investment professionals in 107 countries of which 45,400 are holders of the Chartered Financial Analyst® (CFA®) designation. AIMR's membership also includes 117 affiliated societies and chapters in 29 countries. AIMR is internationally renowned for its rigorous CFA curriculum and examination program, which has more than 100,000 candidates from 143 nations enrolled for the June 2002 exam. Over 7,600 AIMR members live and work in Canada.

continuous disclosure obligations. The CAC represents members of AIMR and its 11 Member Societies and Chapters across Canada. The CAC membership includes portfolio managers and other investment professionals in Canada who review regulatory, legislative, and standard setting developments affecting investors, investment professionals, and the capital markets in Canada.

General Comments

The CAC supports strongly an enhanced financial reporting system that requires *evergreen*, or continuously updated, financial and nonfinancial information of all material and pertinent data and/or facts. Moreover, we commend the CSA in its approach to having a national instrument for the requirements and regulations for continuous disclosures in Canada's capital markets. The regulation in Canada's capital markets must be updated to meet the challenges of promoting efficient capital markets and maintaining adequate investor protection. Users (investors, creditors, and regulators) need timely and relevant information about a company's financial condition and performance to make well-informed and appropriate investment decisions. We believe that today's technology, e.g., online real time computer applications and the Internet, enables companies to record and report timely financial information to a wide group of users.

Disclosure Documents

We prefer a *single* evergreen document that contains current information and has links (electronic, e.g., hyperlinks) to previously filed information circulars or forms rather than a series of independent updates, which are consolidated quarterly or annually. Additionally, this single document should denote the reasons for updates, for example, the nature and timing of the event. We believe that this format will enable an investor to evaluate properly various investment options with more ease and assurance that he or she has captured all the relevant and current information about those investment options.

What is "material" in the context of disclosures?

We found the proposal to be somewhat complex and difficult to follow, regarding the various criteria and/or bright-line tests used to determine whether a reporting issuer must disclose information. The proposal uses different terms, such as: **(1)** *material change* in Part 1 – *Definitions and Interpretations* of NI 51-102; **(2)** *materiality* in Annual Information Form (51-102F1) and Management Discussion & Analysis Form (51-102F2); and **(3)** *significance* in Part 8 – *Business Acquisition Report and Disclosure of Significant Dispositions* of NI 51-102. All these definitions or thresholds determine if some event, transaction, or activity warrants public disclosure. We believe that the proposal should use one principle for determining what should be disclosed based on materiality or significance relative to the reporting issuer's current situation.

In regards to the second item on materiality, the proposal refers to the definition provided in the Canadian Institute of Chartered Accountants' Handbook. The Handbook states in the General Accounting Financial Statement Concepts Standard 1000.17 -

> *" Users are interested in information that may affect their decision making. Materiality is the term used to describe the significance of financial statement information to decision makers. An item of information, or aggregate of items, is material if it is probable that its omission or misstatement would influence or change a decision. Materiality is a matter of professional judgment in the particular circumstances."*

We agree with the above statement, but believe more guidance should be issued for determining materiality. Frequently, companies use only quantitative thresholds as a rule of thumb in determining materiality to the exclusion of qualitative elements, such as risks, uncertainties, terms and conditions of business arrangements. These qualitative elements could potentially have a material impact on a company's operating performance and financial condition. Therefore, we believe that materiality assessments based solely on quantitative thresholds or bright-lines are inadequate and incomplete. Corporate management, auditors, and regulators need to consider *all* relevant circumstances, including both quantitative and qualitative factors, in assessing materiality of a business event, transaction, or activity.

Reconciliation of Financial Information

Under the proposal, Canadian reporting issuers will be permitted to file financial statements prepared in accordance with U.S. GAAP[2]. Those issuers who choose to use U.S. GAAP will have to prepare a reconciliation of the net income, showing the material differences between U.S. GAAP and Canadian GAAP, for only two years from when U.S. GAAP is first adopted. Certain foreign filers will not have to provide any reconciliation between their jurisdiction's required accounting standards and Canadian GAAP.

We are aware that Canada's capital markets represent a relatively small share of the total global capital markets and as such, the CSA has concluded that its members cannot impose certain requirements on foreign filers without impeding the growth of Canada's capital markets. Nonetheless, an overarching principle for Canada's capital markets should be investor protection, including the transparent and complete disclosure of relevant market information that enables users to compare reporting issuers' (both domestic and foreign) financial information. Such comparison, we believe, is necessary to make well-informed investment decisions. Also, we are concerned that exemptions from certain disclosures requirements will create market conditions that may attract reporting issuers that are undesirable and unscrupulous because the reporting requirements are viewed as being lax compared to other capital markets.

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[2] Generally accepted accounting standards.

We believe that reconciliations should be provided if more than one set of accounting principles are permitted or accepted for filing financial statements and related disclosures in Canada's capital markets. Therefore, we disagree with the CSA's proposal for certain foreign filers, i.e., such filers do not have to prepare a reconciliation to Canadian GAAP. Additionally, we question the two-year requirement for domestic filers using U.S. GAAP. This proposal presumes that the differences between U.S. GAAP and Canadian GAAP will be consistent and/or minimal for a company over time, thus, enabling investors to become familiar with the differences during this two-year period. Consequently, users of financial statements will not need a reconciliation to explain the differences. We disagree with this presumption.

We believe that the results of a 2001 AIMR survey[3] of professional users of financial statements support our views on this issue. The survey asked questions pertaining to the use of multiple sets of accounting standards for preparing financial statements in Canada's capital markets and whether reconciliation between other accounting standards and Canadian GAAP was sufficient. The following are the survey results to these pertinent questions:

- ***Would your ability to understand and analyze financial statements be impaired if different GAAP standards are adopted in lieu of Canadian GAAP for financial reporting in Canada's capital markets? (Respondents = 226)***

Multiple sets of standards are adopted for financial standards:

Greatly impaired	*31%*
Somewhat impaired	*47%*
Not impaired	*14%*
Not sure	*8%*

IAS is adopted for financial reporting:

Greatly impaired	*9%*
Somewhat impaired	*36%*
Not impaired	*29%*
Not sure	*26%*

U.S. GAAP is adopted for financial reporting:

Greatly impaired	*1%*
Somewhat impaired	*18%*
Not impaired	*75%*
Not sure	*6%*

The responses to the above questions have strong correlation between the responses to the survey question that asked respondents about the accounting standards used by the companies that they followed and analyzed. [4] Additionally, 80% of 228 respondents

[3] The survey was conducted to have a broad representation of Canadian users of financial statements. The survey responses were used to formulate the AIMR response to the Canadian Securities Administrators' (CSA) discussion paper - "Financial Reporting in Canada Capital Markets". The Accounting Subcommittee of the AIMR Canadian Advocacy Committee (formerly Council) issued a comment letter to the CSA, addressing the discussion paper and outlining the results of the survey, on 29 June 2001. This comment letter is available at www.aimr.org/advocacy.

[4] The survey results showed that 92% and 85% of the 223 respondents follow and analyze companies that use Canadian GAAP and U.S. GAAP, respectively, indicating a strong familiarity with these bases of financial reporting. However, a much smaller

indicated that only one set of accounting standards should be used on a global basis to prepare financial statements for cross-border or cross-jurisdiction offerings of securities.

- ***If different accounting standards are permitted, is a numerical reconciliation of material differences between the two set of standards sufficient information for making a comparison? (Respondents = 222)***

  YES – *78%*
  NO – *22%*

  Several respondents, who indicated ***NO*** to the above question, provided comments explaining why numerical reconciliations are not sufficient. The most frequently stated reason is that narrative explanations to the numerical reconciliation should be provided to explain the differences between the GAAP used to prepare the financial statements and Canadian GAAP.

Management Discussion and Analysis (MD&A)

We agree strongly and commend the CSA on its proposal to *require* reporting issuers to prepare and file a management discussion and analysis (or MD&A) report along with its annual and quarterly financial statements. The MD&A report, when prepared properly, provides users of financial statements with additional information and data, explaining the company's results of operations and financial condition for those periods being reported. Management's discussion should be candid and open, and free of boilerplate messages. AIMR, through other committees[5], has expressed views, in responding to the SEC, that the MD&A should not be audited so as to allow for such candid and open discussions.

In December 2000, several investment professionals from AIMR's Canadian membership participated on a CICA focus group to discuss the current quality of MD&A and how to improve it. During this discussion, several areas of improvement to the MD&A were identified – (1) MD&A reporting should be required rather than discretionary disclosure; (2) the format should be similar to that required by the SEC in regards to the type of information provided; (3) it should provide more discussion and analysis about forward-looking information and risks and uncertainties that the company manages; and (4) the MD&A report should supplement the financial statements and notes by providing substantive and detailed discussion/analyses from management's perspective and rather than boilerplate or canned disclosures updated from period to period by changing dates, amounts and/or percentages already provided in the financial statements and/or accompanying notes.

Later in December 2001, the CICA issued its review draft – *MANAGEMENT'S DISCUSSION AND ANALYSIS: Guidance on Preparation and Disclosure*. This review draft proposed a principles-based approach to preparing the MD&A report. The fundamental and primary principle of the

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number of respondents – 17%, 15%, and 4% - tracked companies that used IAS, U.K. GAAP and other accounting standards, respectively.

[5] Financial Accounting Policy Committee (FAPC) and U.S. Advocacy Committee (USAC).

guidance is that the MD&A report should enable readers to view the past results and future prospects of an issuer "through the eyes of management". This first principle underlies these six principles for preparing the MD&A report:

(1) Complement as well as supplement financial statements;
(2) Have a forward-looking orientation;
(3) Focus on long-term value creation:
(4) Integrate long- and short-term perspectives;
(5) Present information that is material to the decision-making needs of users; and
(6) Embody the qualities of reliability, comparability, consistency, relevance, and understandability.

We agree strongly with the above objectives and principles, as well as the guidance provided in the CICA's review draft.

Comments on Specific Issues

Criteria for Determining Financial Statement Filing Deadlines

The Rule uses TSE non-exempt company criteria to identify issuers subject to shortened filing deadlines for annual and interim financial statements and MD&A. Those criteria include having net tangible assets of at least $7.5 million, or in the case of oil and gas companies, proved developed reserves of at least $7.5 million. These criteria mean that the more stringent 90 and 45 day filing deadlines will apply to Canada's most senior issuers, many of which are currently subject to the same filing deadlines in the United States. They are different from the market value threshold that is proposed to trigger the AIF filing requirement in the Rule, in recognition of the fact that an issuer's market value is not always an appropriate way to assess its ability to prepare financial disclosure within shorter times.

Generally, we are opposed to having different treatment or requirements, based on size or other bright-line criteria, for public companies that have access to capital on Canada's financial markets. All public companies should report financial information in a timely and transparent manner regardless of their size, such as the proposed net tangible assets or reserves of at least $7.5 million. Investors need to have relevant and timely information from those public companies, whether small or large, seasoned or unseasoned, which are being evaluated and analyzed as potential investments, as well as those currently held as investments.

Additionally, we believe that Canada should have similar filing deadline requirements as the U.S. because many Canadian-based companies are listed on securities exchanges in Canada and U.S., essentially, integrating these financial markets through dual listings. The U.S. SEC recently approved a rule, requiring registered companies to file their annual reports (or Form 10-K) and quarterly reports (10-Q) within 60 days and 30 days, respectively by 2004. There will be a transition period for these deadlines – 75 days for annual reports and 45 days for quarterly reports for fiscal years ending after December 15, 2003 and reports for years ending after December 15, 2004 would have to be filed by the recently approved deadlines of 60 and 30 days.

Elimination of Requirement to Deliver Financial Statements

The Rule will eliminate mandatory delivery of financial statements and management discussion and analysis, MD&A, to all securityholders. Issuers will only be obligated to deliver copies of these documents to securityholders that request them. Issuers will have to disclose annually in their AIFs and information circulars that the financial statements and MD&A are available without charge and how to obtain them. Do you agree with this approach? Why or why not? What approach would you suggest?

We have mixed views about the proposed approach for delivering financial statements and MD&A. Under this approach, there are presumptions made that *all* securityholders have access to the Internet and/or prefer an electronic version of corporate and financial information; or that perhaps they do not read these financial reports. Thus, the reporting issuer should not have to incur the cost to print and deliver, via postal mail, the financial statements to the securityholders.

We realize that a reporting issuer can incur significant costs in the production of its financial reports, and related analyses, especially if glossy colored photographs and other charts or graphs are included. However, production costs cannot be eliminated completely, and are costs of raising capital that are needed to provide transparent and timely information for the capital markets. However, these costs can, and should, be effectively reduced so that an investor's ability to access this essential information is not impaired. We believe that most securityholders would rather have a presentation without all the high-gloss "bells and whistles" where only substantive and meaningful corporate and financial information is reported. This format would reduce, perhaps significantly, the cost to produce and distribute these documents.

Therefore, we believe that reporting issuers should ***ask*** securityholders how they want to receive, at a minimum, the financial statements and MD&A. A securityholder should ***not*** have to request (either by phone call, email, or other form of communication) that he or she receives this information sent by postal mail. Certainly over sometime, this method of delivery will be used less as more and more investors become familiar with, and have the means to access, electronic versions of the financial statements and MD&A posted on SEDAR and/or the reporting issuer's web site.

SEC Developments

In the proposal, the CSA identifies SEC Releases that propose changes to corporate disclosure requirements for SEC registrants. Should the CSA change the Rule to reflect the proposed SEC requirement?

Yes. As indicated in our previous comment to filing deadlines, the financial markets in Canada and U.S. are integrated to a large extent. Similar requirements would facilitate cross-border listings for companies that want to have access to capital in Canada and the U.S., as well as improve comparability between companies publicly traded in these two markets.

Combination of Financial Statement and MD&A Filings

The CSA is considering amending the Rule so that financial statements and MD&A would have to be filed at the same time, as one filing. MD&A contains important discussion of financial statement disclosure, and is already subject to the same filing deadlines as financial statements. Should the financial statements and MD&A be combined for filing requirements?

As mentioned previously, we support strongly this proposal to combine the filing of the financial statements and MD&A. The MD&A supplements the financial statements in that it (1) explains and elaborates on the company's financial performance and condition and (2) provides forward looking information about the company's operations and strategic plans to achieve certain operating targets. This information contained in the MD&A enables users of financial statements to predict future earnings and/or cash flows with more accuracy, and improve their ability to make well-informed investment decisions. (Please refer to our commentary under **General Comments – *Management's Discussion and Analysis (MD&A)*.**)

Significant Acquisitions Disclosure

The proposed significance tests for business acquisitions in the Rule were the subject of extensive comments when the prospectus rules were being reformulated. The CSA analyzed the comments and finalized the tests in the prospectus rules. Several commenters said that significant acquisition disclosure should be required in CD, not just in prospectuses. Many commenters expressed the view that Canadian acquisition disclosure rules should parallel the SEC Rules. The significance tests proposed in the Rule are very similar to the SEC Rules and are consistent with the significance tests in the prospectus rules.

The proposed Rule requires one, two, or three years of financial statements depending on whether an acquisition is significant at a 20%, 40% or 50% threshold. Would it be better or worse to have only one threshold for determining significance with a requirement for two years of financial statements when the threshold is met? If you support this approach, what would you suggest as an appropriate threshold and why?

We believe that financial and nonfinancial information about business acquisitions, which have a material effect on the acquirer's financial condition and future performance, including earnings or cash flows, must be disclosed and made available in a timely manner to market participants. Although the proposal is aligned with current SEC rules, which would facilitate cross-border listings in Canada and the U.S., we are generally opposed to quantitative thresholds because they can be gamed more easily than principles that stipulate what should be disclosed, similar to those principles expressed in the CICA's draft guidance for preparing a MD&A report.

Bright-line tests, or quantitative thresholds, are not sufficient for determining whether something is material enough to warrant disclosure of a business transaction and/or activity, such as a business acquisition. Other factors that are qualitative in nature should also be considered, such as the effect on the acquirer's overall operations caused by increased risks from geographic locations, business activities, currency exchange, and financial risks, including the level of exposure to these risks as a result of the acquisition. Both quantitative and qualitative factors should be considered in determining whether an acquisition is significant or not. (Please refer to our commentary under **General Comments** – ***What is "material" in the context of disclosures?***.)

Requirement to File Material Documents

The Rule requires issuers to file constating documents and other instruments that materially affect the rights of securityholders or create a security. Would an acceptable alternative to filing be to require issuers to describe these documents in their AIFs or information circulars, rather than file them?

We do not support the alternative, which is to provide a description of constating documents in a reporting issuer's AIF or information circulars rather than filing the complete documents, e.g., corporate bylaws and corporate agreements dealing with debt issuance and other obligations. These are documents that must be prepared in the course of doing business and therefore, should also be filed electronically for public access and review.

Criteria for Identifying Small Issuers

The proposed Rule distinguishes small issuers in different ways, for different purposes, as follows:

- *Issuers that are not "senior issuers" (that are TSE non-exempt) have more time to file their financial statements, MD&A and AIFs than senior issuers (see Criteria for Determining Financial Statement Filing Deadlines for more details);*
- *Issuers that are "small businesses", based on a similar definition to that in the prospectus rules (less than $10 million for each of assets and revenue) are exempt from certain significant acquisition disclosure requirements;*
- *Issuers that are small businesses (less than $10 million for each of assets and revenue) and have a market value not exceeding $75 million are not required to file an AIF;*
- *For the purpose of Form 51-102F6 Statement of Executive Compensation, an "exempt issuer" must have revenue and a market value of less than $25 million.*
- *Are these ways of identifying small issuers appropriate? Is there one definition that would be appropriate for all purposes? Why or why not?*

Again, we generally do no support different requirements for public traded companies based on size, or other similar criteria, for reasons mentioned in earlier comments, which can be summarized as follows:

- Investor protection should be the primary concern in assessing the need for financial reporting requirements and other security regulations;

- Full and fair disclosure of all relevant and pertinent facts and information should be provided to investors and made available to prospective investors; and

- Materiality, the basis for disclosing information, should be determined from assessing the qualitative, as well as quantitative, elements of the business transaction, activity, relationship, etc.

Cost-Benefit Analysis

The CSA believes that the costs and other restrictions on the activities of reporting issuers that will result from the Rule are proportionate to the goal of timely, accurate and efficient disclosure of information about reporting issuers. The CSA is interested in hearing the views of various market participants on any aspect of the costs and benefits of the Rule and we invite your comments specifically on this matter.

The following statements are paraphrased from the 1993 AIMR Report, *Financial Reporting in the 1990s and Beyond*, regarding cost/benefit analysis from the user viewpoint -

> *"The benefits of producing financial statement information should exceed the cost of producing it. We support strongly this percept. However, we object to the way it is portrayed to others.*
>
> *Investors both reap the benefits as well as bear the costs of improvements in accounting and disclosure standards. The financial managers of business firms act simply as agents of the owners. In that regard, it is the current and potential shareholders and their financial advisors who should best be able to advise standard setting and regulatory bodies as to the proper balance of costs and benefits associated with their proposals."*

We recommend that the CSA consider thoroughly the following items and weigh them appropriately in its assessment of the costs and benefits associated with the implementation of these proposals (NI 51-102 and NI 71-102):

- Often direct benefits derived from implementing a new regulation are not easily identified or quantified, while most incremental costs are.

- Benefits are not always immediate, and thus, often discounted or not considered in the overall analysis.

- The hidden costs (or inverse benefits) associated with **not** providing certain corporate and/or financial information that is needed for sufficient transparency. Such an omission can have negative effects, which could be exponential in nature or a rippling effect on the market. Insufficient disclosure of off-balance sheet activities or pertinent business activities, such as special purpose entities that were not consolidated, resulted in great financial harm to investors, creditors, and other stakeholders in the company affected.

Closing Remarks

We appreciate the opportunity to comment on these CSA proposals to improve continuous disclosure of publicly traded companies' financial statements and other supplemental information, such as the MD&A. If you have any questions or seek elaboration of our views, please do not hesitate to contact Georgene Palacky at 1.434.951.5334 or gbp@aimr.org.

Sincerely,

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