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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

c/o 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
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c/o Denise Brosseau, Secretary
Commission des valeurs mobilières du Québec
Stock Exchange Tower
800 Victoria Square
P.O. Box 246, 22nd Floor
Montréal, Québec
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Ladies and Gentlemen:

Re: Proposed National Instrument 51-102 *Continuous Disclosure Obligations*, its related forms and companion policy (together, the CD Rule), and proposed National Instrument 71-102 *Continuous Disclosure and Other Exemptions Relating to Foreign Issuers* and its related companion policy (together, the Foreign Issuers Rule)

We have read the CD Rule and the Foreign Issuers Rule and provide you with our comments on them in this letter. Overall, we support the harmonization of continuous disclosure requirements across all Canadian jurisdictions, and agree that the harmonized requirements are in the public interest by facilitating capital-raising initiatives such as an integrated disclosure system. The first

section of this letter contains our comments on specific issues, and the second section addresses the questions you posed in your request for comments. Capitalized terms in this letter have the same meaning as those in the CD Rule and the Foreign Issuers Rule, except as otherwise indicated.

COMMENTS ON SPECIFIC ISSUES

The CD Rule

Part 4 – Financial Statements

Filing deadlines for financial statements

We generally agree with shortening the filing deadlines to the proposed time frames, as this addresses market demand for more timely disclosures. However, the change is very significant to some reporting issuers, and will likely create significant resource issues. We recommend that the changes to the filing deadlines be phased-in over a period of time, similar to the phase-in period the SEC allowed in its recently released rule of acceleration of periodic report filing dates, to allow certain issuers sufficient time to realign their resources for this purpose.

While we support differentiating the filing deadlines for large and small issuers, we object to the use of the TSE non-exempt company criterion for the differentiation. This criterion will subject many small companies to the shortened deadlines, and as these companies tend to have fewer resources, the risk of inaccuracies resulting from the tightened deadlines will likely increase. Moreover, we find it confusing to use different criteria for determining filing deadlines and AIF filing requirements.

We are in favour of using the AIF filing criterion (Small Businesses with aggregate market value of $75 million or more) to distinguish large from small issuers for filing deadline purposes. This criterion more appropriately reflects the distinction between a large and a small issuer. It is also aligned with the $75 million common equity float criterion used in the definition of accelerated filer in the recently released SEC rule.

On a related point, section 3.11 of the companion policy emphasizes the requirement for board or audit committee review before extracted financial information is published. We believe that this is a very important and useful practice that reporting issuers should follow. However, we recommend that you consider expanding this guidance. It appears inappropriate to us that reporting issuers are able to influence the marketplace with press releases regarding financial results before the audit committee, board and auditors (where applicable) have completed their work and before the reporting issuer has prepared the corresponding continuous disclosure report for the period. The processes followed to prepare and approve the continuous disclosure filing are intended to enable the reporting issuer to report information that is complete and reliable.

Press releases, which currently have more influence on the market than continuous disclosure reports, are not necessarily subject to the same processes and the quality of their information likely reflects this. Consequently we recommend not only that section 3.11 be given much greater prominence in the CD Rule but also that the publication of extracted information by press release not be permitted before the reporting issuer and its audit committee, board and auditor have substantially completed their work related to the corresponding continuous disclosure report for the period. This concept could be expressed in the form of a requirement calling for the filing of the continuous disclosure report within 48 hours of the press release.

Review of interim financial statements

Under the CD Rule, as well as current rules, the board of directors may delegate the review of interim financial statements to its audit committee. We believe interim financial statements represent an important component of a company's continuous disclosure record, and the board of directors' responsibilities for annual and interim financial statements should not differ. We recommend that the board of directors be required to review and approve interim financial statements.

In addition, we recommend that auditor review of interim financial statements be mandated. We believe auditor review of interim financial statements will significantly improve the quality of interim reporting, the overall effectiveness of the external audit function and investor confidence. Auditor reviews are currently mandatory for U.S. SEC registrants. The Canadian securities environment also supports this practice, as demonstrated in the recommendations contained in the draft report published in May 2002 by the Securities Advisory Committee, who undertook a five-year review of Ontario securities legislation.

Finally, a recently released SEC rule implementing the provisions of the Sarbanes-Oxley Act requires auditors to report on critical accounting policies to the client's audit committee on a real time basis. This rule applies also to foreign private issuers, and therefore affects Canadian SEC registrants. We expect that Canadian auditors will be obliged to perform interim reviews for Canadian SEC registrants in order to meet the reporting requirements on critical accounting policies.

Generally accepted accounting principles

The CD Rule allows only SEC Issuers to prepare financial statements in accordance with U.S. GAAP. We recommend this option be extended to all issuers, as non-SEC Issuers may also have significant U.S. stakeholders (such as a U.S. parent company) who prefer U.S. GAAP financial statements.

That said, we believe a large number of Canadian companies will continue to prepare financial statements in accordance with Canadian GAAP. To retain comparability with these Canadian

companies, a reconciliation to Canadian GAAP is necessary. Furthermore, the notion of allowing U.S. GAAP only financial statements undermines the status of Canadian GAAP in a manner which we consider to be inappropriate at this time given that it is the standard basis of accounting used by the vast majority of Canadians. You should also consider that although attempts are being made at GAAP harmonization, many significant differences between Canadian and U.S. GAAP exist for items such as derivatives, consolidation and stock compensation. We suggest that a Canadian GAAP reconciliation be required in U.S. GAAP financial statements on an ongoing basis, and not just a two-year transition period. Since Canadian companies likely will be required to produce Canadian GAAP information for tax and regulatory purposes at least in the near term, the costs of disclosing a Canadian GAAP reconciliation should be very low.

We note that subsection (4) of section 4.7 of the CD Rule states that "…. a reporting issuer must use the same accounting principles for all periods….". We expect this statement was intended to address the nationality of GAAP being used for all periods, rather than implying that a reporting issuer is not permitted to make changes to its accounting policies. The wording of this subsection should be clarified.

Subsection 4.7(5) stipulates that in the first year after the change to U.S. GAAP, comparative information in both Canadian and U.S. GAAP must be presented on the face of the financial statements. This requirement is unnecessarily cumbersome and provides undue prominence to a basis of accounting that the report issuer has rejected in favour of U.S. GAAP. We believe the alternative presentation of Canadian GAAP comparative information in the notes to the financial statements should be available for both annual and interim financial statements.

Filing of financial statements after becoming a reporting issuer

The CD Rule requires a reporting issuer to commence filing financial statements on the first filing deadline that occurs after the date it becomes a reporting issuer. We note that under this requirement, without a corresponding amendment of the prospectus rules with respect to stale-dating of interim financial statements, there is still a gap (between 45 and 60 days after a quarter ends) in which companies that qualify as Senior Issuers may become reporting issuers without providing continuity between financial disclosure in the prospectus and that required under the CD Rule. For example, a Senior Issuer with a calendar year end need not include its September 30 interim financial statements in the prospectus if the final prospectus is receipted before November 29, but this company is also not required to file its September 30 interim financial statements under the CD Rule if the final prospectus is receipted after November 14. An amendment to the current prospectus rules would resolve this issue.

Change of auditor

The definition of "termination" in section 4.14 of the CD Rule does not include an auditor's resignation or refusal to stand re-appointment (a resignation). You should clarify whether the requirements in the CD Rule with respect to a change of auditor apply also to a resignation.

Subsection (10) requires the successor auditor to advise the reporting issuer in writing and deliver a copy of the letter to the applicable regulator if the successor auditor becomes aware that the reporting issuer has not made the required disclosure under the CD Rule. We suggest that the former auditor also be required to have a similar responsibility, so that the regulators can be promptly notified if a reporting issuer is delinquent in the filing requirements before it appoints a successor auditor.

Part 8 - Business Acquisition Report and Disclosure of Significant Dispositions

Modified significance tests for small businesses

We do not agree that the CD Rule should exempt a Small Business from the income test for the determination of significance. As an example, the modified significance test will not require a Small Business to disclose an acquisition of a non-asset based business (such as a business in the service industries) with significant losses, if the consideration paid for the acquisition is not large, even though the acquisition of a loss-making business may have material implications on the company's resources. Relief to small businesses should be given on a case-by-case basis only.

Pro-forma financial statements

Paragraph (iii) of section 8.4(3)(b) appears to restrict the method a company may use to construct a 12-month income statement to comply with the 93-day requirement. To illustrate a situation where applying this paragraph with its current wording will not achieve its objective, consider an issuer with a December 31 year end that acquires a business with an April 30 year end in October 2002. Adding the July 31, 2002 quarter to the business' April 30, 2002 annual financial statements and deducting the comparable interim period will put the period ends further apart. The wording of this paragraph should be amended to avoid this situation.

Reporting currency

We find it impracticable that both the financial statements of the business acquired and those of the reporting issuer have to use the same reporting currency, particularly in circumstances where a Canadian reporting issuer acquires a business in a foreign country. The foreign acquired business likely has prepared historical audited financial statements using a foreign currency, and the requirement to use the same reporting currency will require a restatement of the acquired

business' historical financial statements and re-issuance of the auditor's report. We believe it is sufficient to translate the acquired business' financial statements in the pro-forma financial statements only.

Auditor's report

Section 8.8 of the CD Rule allows for a reservation relating to inventory in the auditor's report, only if the acquired business is a Small Business. We believe this exemption should be extended to all types of acquired businesses, since any business that has not been previously audited (for example, those of private companies or carved-out divisions) will likely have the same audit issue with respect to opening inventory. Current prospectus rules (OSC Rule 41-501 CP 3.20(4)) provide for the granting of relief to permit a reservation relating to opening inventory in appropriate circumstances, and no differentiation is made between small and other businesses. The CD Rule should not make this differentiation either.

Exemptions from disclosure requirements for significant acquisitions if more recent statements included

Section 8.11 subsection (2) provides that a reporting issuer may omit the financial statements for the earliest financial year if, among other things, the business is not seasonal. We suggest that the CD Rule describe the term "seasonal", or specify the criteria for determining whether a business is seasonal.

Definition of a business

A question we often encounter in dealing with disclosure requirements of significant acquisitions in a prospectus is what constitutes a business. Section 6.1 of the companion policy of the CD Rule provides a general interpretation of the term, which is similar to the one contained in current prospectus rules. While this is helpful in specifying that the continuity of certain aspects of the business is an important consideration, it remains unclear as to whether some, all or none of the listed characteristics need be present in order to conclude that a "business" has been acquired. We suggest the CD Rule be amended to include a more complete and thoughtful definition of a business. In considering this matter, you should ensure you are familiar with EIC-124 of the CICA Emerging Issues Committee, EITF 98-3 of the FASB's Emerging Issues Task Force and Article 11 of Regulation S-X.

Exemptions from requirement for financial statements in a business acquisition report

Section 6.10 of the companion policy provides the conditions for exemptions from the requirement to include any or all of the required financial statements in a business acquisition report (BAR). However, it does not address situations where an issuer requires an extension to the 75-day filing deadline. In some situations, such as when the acquired entity is in a foreign

country, the audit process may be particularly lengthy, and the issue a company faces is not with the requirement for audited financial statements in the BAR, but rather with the deadline for filing the BAR. Companies should be allowed in these situations to first file within the deadline a BAR with the required non-financial information, and to file the required financial information at a later date. The Commission may require a written request with valid reasons for this extension. Measures similar to those contained in OSC Policy 57-603 *Defaults by Reporting Issuers in Complying with Financial Statement Filing Requirements* should be considered.

Implications for prospectuses

The current short form prospectus rules calling for disclosures of significant acquisitions will, to a certain extent, be redundant when a reporting issuer is required to file the BAR under continuous disclosure requirements. When developing the harmonized prospectus rules, we suggest the CSA allow the BAR to be incorporated by reference.

Form 51-102 F1 *AIF*

We suggest that the term "special purpose vehicle" used in paragraph (j) of Part 1 be defined.

Form 51-102 F2 *Management Discussion & Analysis*

The wording of paragraph (j) of Part 1 seems to indicate that the MD&A should focus on a company's primary financial statements only when its primary financial statements are prepared in accordance with non-Canadian GAAP *and* a reconciliation is provided. We believe the intention is to have all MD&As focus on a company's primary financial statements, not only when a reconciliation is prepared. The wording should be amended to clarify your intentions.

The difference between the types of arrangements to be included under Item 1.4 *Liquidity* and Item 1.5 *Capital Resources* is not clear, particularly with respect to off-balance sheet financing arrangements. For example, it is not clear whether payments due under an off-balance sheet financing arrangement are contractual obligations (which would be included under section 1.4) or contractual commitments (which would be included under section 1.5). The Form should provide more explanation to clarify this matter.

Instruction (ii) under Item 1.6 *Transactions with related parties* requires disclosures regarding relationships with certain related or non-arms length parties. The form should be more specific about the type of disclosures required.

Form 51-102 F5 *Information Circular*

The disclosures required under Item 13.2 of F5 are important information for shareholders who rely on the information to cast their votes. To ensure the disclosures are comprehensive and useful, the form should be more specific regarding the nature of the disclosures required. For example, Item 13.2 refers to the inclusion of financial statements, but does not explain whether the financial statements need to be audited; it requires the inclusion of disclosures prescribed by the appropriate prospectus forms, but it is unclear as to whether the disclosures only need to include certain items in the prospectus, or should comply with the entire form. We are in favour of using prescribed forms that resemble SEC Form F-4 or S-4 to spell out the specific disclosure requirements for the restructuring transactions. Please also see our response to question 5 below.

The Foreign Issuer Rule

As indicated in our comments on U.S. GAAP financial statements, we believe a reconciliation of U.S. or other foreign GAAP financial statements to Canadian GAAP is essential for comparability among Canadian issuers. The fact that a Designated Foreign Issuer is subject to the disclosure requirements of a designated foreign jurisdiction provides some comfort over the quality of the issuer's disclosures, but does not provide comparability of the issuer's financial statements with those of Canadian issuers. We suggest that all issuers, including Designated Foreign Issuers, be required to provide reconciliation to Canadian GAAP if their financial statements are prepared in accordance with some other basis of accounting.

RESPONSES TO QUESTIONS LISTED IN REQUEST FOR COMMENT

The numbers for the responses below correspond to the numbers of the questions in the request for comment with respect to the CD Rule.

1. *Criteria for Determining Financial Statement Filing Deadlines*

   See our comments above in relation to filing deadlines for financial statements.

2. *Elimination of Requirement to Deliver Financial Statements*

   We agree with the proposed approach.

3. *SEC Developments*

   Filing deadlines – The final SEC rule for acceleration of periodic report filing dates applies only to U.S. domestic reporting companies, and Canadian SEC registrants are therefore excluded. The CD Rule will result in consistency between the reporting time frame of Canadian SEC and non-SEC issuers, and, accordingly, no further reduction of Canadian

reporting time frames is necessary.

Current report requirements – No comment.

Critical accounting policies disclosures – We support the proposal in the CD Rule to require additional disclosures in the MD&A, particularly the additional disclosures relating to critical accounting policies. These disclosures allow the investors to assess the degree of judgment made in, and hence the risk associated with, management's choice or use of accounting policies. We believe the proposed SEC changes to further require disclosures about critical accounting estimates and the initial adoption of accounting policies that have material impact follow the same principles of enhancing risk assessment. We therefore support a change to the CD Rule to reflect the proposed SEC changes.

4. *Combination of Financial Statement and MD&A Filings*

   No comment.

5. *Disclosure of Restructuring Transactions in Information Circulars*

   (a) We consider that the definition of "restructuring transaction" in item 13.2 includes the appropriate classes of transactions.

   (b) We believe no expansion of Item 13.2 to include significant acquisitions is necessary.

   (c) We think Item 13.2 is clear about the entities to be included in the disclosures.

   (d) We do not believe that Item 13.2 is clear about the prospectus disclosures required for restructuring transactions, even when the qualifying words "to the extent necessary to allow a reasonable securityholder to form a reasoned investment decision" are added. We suggest the use of a prescribed form for disclosures of these transactions. See our responses to (e) and (f) below.

   (e) and (f) We are in favour of the use of a prescribed form, similar to SEC Form F-4 or S-4.

6. *Significant Acquisitions Disclosure*

   We believe the significance tests should be consistent between continuous disclosure requirements and prospectus requirements. We agree with the tests in the CD Rule currently proposed, as they are consistent with current prospectus requirements. We presume there are no plans to revise the prospectus requirements with respect to significant acquisitions in the near term.

7. *Requirement to File Material Documents*

   No comment.

8. *Criteria for Identifying Small Issuers*

   Our general comment on this question is that the use of different criteria for determining different continuous disclosure filing requirements is unnecessarily complex and potentially confusing. Unless there is a strong reason to differentiate the filing criteria, only one approach should be used throughout the CD Rule.

   As mentioned in the comments above on filing deadlines for financial statements, we are in favour of using the definition of Small Businesses, supplemented by the criterion of aggregate market value of $75 million or more, as the threshold for determining financial statement filing deadlines. The use of the definition of Small Businesses without the market value criterion for determining exemptions from significant acquisition disclosure requirements is appropriate, as acquired businesses may or may not have a market value. The $25 million criterion for determining whether an issuer is an "exempt issuer" for the purpose of Form 51-102 F6 *Statement of Executive Compensation* appears arbitrary, and we do not see the reason for imposing a different criterion for this Form.

9. *Approach to Regulation of Small Issuers* and
10. *Cost Benefit Analysis*

    We agree that the cost-benefit analysis is different for issuers of different sizes. We therefore agree with the use of a two-tier reporting structure for certain continuous disclosure requirements.

    We generally agree with the cost benefit analysis included in the Notice, except for those matters addressed above.

11. *Credit Supporters and Exchangeable Shares*

    (a) and (b) – No comment.

    (c) We support the basic concept of requiring the credit supporter or the parent company of the exchangeable share issuer to comply with continuous disclosure obligations. The issue of whether only certain types of continuous disclosure documents should be provided rather than complying with all continuous disclosure obligations should depend on the extent to which securities of the underlying reporting issuer are in substance securities of the credit supporter or the parent. If a security effectively represents an investment in a credit supporter

or parent, those entities should comply with all continuous disclosure obligations.

Should you have any questions or comments on this letter, we would be pleased to hear from you.

Yours sincerely,

Ernst & Young LLP

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