

1.1.3 CSA Staff Notice 51-320 - Options Backdating

CSA STAFF NOTICE 51-320 - OPTIONS BACKDATING

As a result of recent media attention about the apparent backdating of options in the US, Canadian market participants have expressed interest in the dating of stock options granted by reporting issuers in Canada. Staff in the jurisdictions represented by the Canadian Securities Administrators (CSA), are publishing this notice to communicate our understanding of this issue in the Canadian context.

It has been suggested that some US-based companies granted options to executives and then claimed that they issued them at an earlier date than they actually did. This enabled them to base the exercise price of the options on a lower market price for the issuer's shares. There are also broader concerns in the US that issuers may have timed the granting of stock options using their expectations of stock price movements.

There are some historically different regulatory requirements in Canada that may reduce the opportunity for Canadian companies to backdate or time option grants, for example:

- The Toronto Stock Exchange (TSX) imposes the following rules for its listed companies:
 - (i) the exercise price for options granted by listed issuers must not be less than the market price of the underlying securities when the options are granted;
 - (ii) the exercise price must not be based on market prices that do not reflect undisclosed material information; and
 - (iii) all option grants must be reported to the TSX within ten days of the end of the month in which the grant was made.
- The TSX Venture Exchange (TSX-V) imposes similar rules, though it allows an issuer to set the exercise price at a discount (ranging from 15% to 25%) from the market price, which is specified by the TSX-V.
- Securities legislation generally requires insiders of reporting issuers to file a report on SEDI within ten days of any change in their direct or indirect beneficial ownership of or control or direction over securities of the issuer, including options.

The board of directors of an issuer is responsible for ensuring that the issuer prices options appropriately and discloses them properly. The following guidance may reduce concerns about the timing of option grants and the risk of non-compliance with securities legislation:

- establish a compensation committee that follows the guidance contained in National Policy 58-201 - *Corporate Governance Guidelines*;
- consider the guidance in National Policy 51-201 – *Disclosure Standards* including adopting a corporate disclosure policy, adopting an insider trading policy, and establishing “blackout periods” around earnings announcements; and
- ensure that, following a grant of options to insiders, the issuer provides them with details of their grants so that they can comply with their legal obligation to file insider reports on SEDI within 10 days.

CSA staff recommend that all issuers assess current policies, procedures and controls for option grants and equity-based awards to ensure that they comply with relevant stock exchange rules and securities legislation. If CSA staff become aware, through disclosure reviews, tips, or otherwise, of abuses by reporting issuers, they may take enforcement action against the issuers or their directors and officers. In considering the appropriate course of action, CSA staff may take into account what steps, if any, such issuers took to ensure their policies and controls complied with regulatory requirements.

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