Chapter 5

Rules and Policies

5.1.1 OSC Policy 51-604 Defence for Misrepresentations in Forward-Looking Information

NOTICE OF POLICY ADOPTED UNDER SECURITIES ACT

OSC POLICY 51-604 DEFENCE FOR MISREPRESENTATIONS IN FORWARD-LOOKING INFORMATION

I. Notice of Policy

The Commission has adopted OSC Policy 51-604 – *Defence for Misrepresentations in Forward-Looking Information* (the "Policy").

The Policy relates to the defence available under the *Securities Act* in an action for damages for misrepresentation in forward-looking information contained in an issuer's disclosure. It has been adopted to address recurring questions we have received from issuers and counsel who have expressed uncertainty with respect to the requirements of the defence.

The purpose of the Policy is to outline the Commission's views on some of the policy considerations underlying the defence for misrepresentations in forward-looking information. The Policy also explains how the Commission approaches the interpretation of certain aspects of the defence, including: (i) the "proximate" requirement; (ii) the required content of applicable risk factor and assumption disclosure; (iii) the "reasonable basis" requirement; and (iv) the operation of the defence with respect to oral statements containing forward-looking information.

II. Summary of comments received on the Policy and the Commission's response

The Commission first published the Policy for comment on June 2, 2006.[1] During the comment period, which expired on August 2, 2006, the Commission received four submissions. Appendix A to this Notice contains a list of people and organizations who commented on the Policy. Copies of the comment letters may be viewed at www.osc.gov.on.ca under "Policy & Regulation\ Proposed Rules, Policies & Concept Papers".

The Commission has considered all submissions received and thanks the commenters for their contributions. Appendix B to this Notice summarizes the comments and our responses. No substantive changes have been made to the Policy as published on June 2, 2006 although the Commission has made some minor drafting changes.

Commenters were generally supportive and appreciative of the policy. Commenters did request, however, further guidance from the Commission on several issues, including most notably:

- Commission guidance as to whether or when it is permissible to incorporate by reference into a document a more lengthy discussion of material risk factors and material assumptions underlying the forward-looking information.
- A statement from the Commission that issuers may usefully look to practice in the U.S., which has had a civil liability regime in connection with secondary market disclosure for some years, for guidance in complying with the defence.
- A definition of the appropriate materiality standard that issuers should adhere to in drafting their cautionary statements.

The Commission does not believe that it is in a position to provide more specific guidance in an interpretive policy as it relates to these issues. The Commission hopes, however, that our responses to the comments will address some of the commenters' questions.

[1] (2006) 29 OSCB 4571.

III. Developments since the Policy was issued for comment

Two related developments have occurred since the Policy was issued for comment in 2006. The first was the release of the decision of the Supreme Court of Canada in *Danier Leather*[2] and the second was the rescission of National Policy 48 *Future Oriented Financial Information* and the adoption of amendments to National Instrument 51-102 *Continuous Disclosure Obligations* that deal with the disclosure of forward-looking information.

The Supreme Court of Canada in *Danier Leather* found among other things that a forecast included in the issuer's initial public offering prospectus contained, as a matter of fact, an implied representation of objective reasonableness. This finding provides the basis for determining that a forecast can constitute a misrepresentation, since a misrepresentation is defined to include "an untrue statement of a material fact".

The amendments to National Instrument 51-102 *Continuous Disclosure Obligations*, which came into effect on December 31, 2007, impose certain disclosure obligations on reporting issuers disclosing forward-looking information. These disclosure obligations, to some extent, overlap with the requirements that must be met to establish a defence under the Securities Act in an action for damages for a misrepresentation in forward-looking information. The amendments also provide that "[a] reporting issuer must not disclose forward-looking information unless the issuer has a reasonable basis for the forward-looking information."

Neither of these developments, in the Commission's view, warrants any change to the Policy.

IV. Text of Policy

The text of the Policy follows.

October 3, 2008

[2] *Kerr v. Danier Leather Inc.*, 2007 SCC 44.

OSC POLICY 51-604 –DEFENCE FOR MISREPRESENTATIONS IN FORWARD-LOOKING INFORMATION

Part I – Introduction

1.1 Background – (1) Ontario securities law provides public issuers, directors, officers and other parties with a defence from statutory civil liability for misrepresentations in forward-looking information. The defence for misrepresentations in forward-looking information was first introduced into Ontario securities law in December 2002 and came into force on December 31, 2005 as part of the introduction of a statutory civil liability regime in favour of secondary market investors.[3] A similar defence exists in those parts of the *Securities Act* that provide a statutory right of action for damages for misrepresentations in primary market offering documents.[4] The defence contained in the *Securities Act* is based on draft legislation that the Commission, together with certain members of the Canadian Securities Administrators, proposed for public comment.

(2) Ontario securities law defines forward-looking information as disclosure about possible events, conditions or results of operations that is based on assumptions about future economic conditions and courses of action.[5] Forward-looking information includes, but is not limited to, future-oriented financial information with respect to prospective results of operations, financial position and/or cash flows that is presented as either a forecast or a projection. Earnings guidance is an example of forward-looking information. MD&A may also contain forward-looking information.

(3) Forward-looking information is, by its very nature, information that carries with it a level of uncertainty. There is a concern that attaching statutory civil liability to information that contains inherent uncertainties will discourage issuers from disclosing or providing forward-looking information. Such a "disclosure chill" would not be desirable. Understanding management's assessment of the future prospects and potential of a company is valuable to shareholders and prospective investors. Indeed, some forward-looking information, for example in the form of MD&A, is required. The policy objective behind the defence applicable to forwarding-looking information is to facilitate responsible and balanced disclosure about an issuer's anticipated future prospects.

(4) This policy statement expresses the Commission's views on some of the policy considerations underlying the defence for misrepresentations in forward-looking information and explains how the Commission approaches the interpretation of certain aspects of the defence. It is being issued under subsection 143.8(1)(b) of the *Securities Act*.

This policy statement represents the views of the Commission which do not have the force of law. These views are also not legal advice and should not be relied on as such.

We expect that disclosure practices in this area will vary among issuers and will evolve over time.

Part II – Defence for Misrepresentations in Forward-Looking Information

2.1 Legislative scheme – Written and oral forward-looking information is protected from statutory civil liability if:

(a) the document or public oral statement contains:

  (i) reasonable cautionary language identifying the forward-looking information as such (the "identifier");

  (ii) reasonable cautionary language identifying material factors that could cause actual results to differ materially from a conclusion, forecast or projection in the forward-looking information ("risk factors"); and

  (iii) a statement of the material factors or assumptions that were applied in drawing a conclusion or in making a forecast or projection set out in the forward-looking information ("assumptions");

(b) the identifier and disclosure of risk factors and assumptions appear proximate to the forward-looking information; and

(c) the person or company had a reasonable basis for drawing the conclusions or making the forecast or projection.[6]

---

3 See paragraphs (9), (9.1), (9.2) and (10) of section 138.4 of the *Securities Act*.
4 See section 132.1 of the *Securities Act*.
5 See subsection 1(1) of the *Securities Act*.
6 See subsection 138.4(9) of the *Securities Act*.

2.2 Animating Principles – The principles animating the defence for forward-looking information include:

(a) an investor who reads a disclosure document or listens to an oral statement containing forward-looking information should be able to readily:

(i) understand that forward-looking information is being provided in the document or statement;

(ii) identify the forward-looking information; and

(iii) inform himself or herself of the material assumptions underlying the forward-looking information and the material risk factors associated with a particular conclusion, forecast or projection; and

(b) effective disclosure is based on clarity of presentation and simplicity of language and style.

2.3 The "proximate" requirement – (1) Concerns have been expressed that the word "proximate" may be interpreted so as to require immediate juxtaposition of information in every instance. If this were the case, each statement of forward-looking information would need to be individually identified as such and all of the material risk factors and assumptions applicable to the statement immediately included, irrespective of the fact that these risk factors and assumptions may apply to various statements of forward-looking information in the same disclosure. The Commission does not interpret the "proximate" requirement to require immediate juxtaposition.

(2) MD&A, for example, frequently has threads of forward-looking information throughout. These threads of forward-looking information may be subject to common assumptions and risk factors. Breaking the flow of the discussion to indicate each time that a particular statement is forward-looking and to identify in a meaningful way the factors that could affect its outcome introduces complexity in presentation that could frustrate an investor's ability to readily follow the MD&A discussion and appreciate the nature of the forward-looking information. A reader may be better served by a single broader reference prefacing or following, as appropriate, the MD&A identifying and setting out the applicable assumptions and risk factors. The Commission believes that such placement should generally satisfy the "proximate" requirement of the defence.

(3) There may be situations where particular assumptions and risk factors apply equally to multiple instances of forward-looking information in a single document. In the Commission's view, the use of cross-referencing in a manner that supports user friendliness and the principles animating the defence is consistent with the "proximate" requirement of the defence. We recognise that practices with respect to the use and extent of cross-referencing will vary among issuers depending on the circumstances and the nature of the particular disclosure.

(4) In the Commission's view, the animating principles underlying the defence suggest that, as a general principle, the more closely-tied a particular risk factor or assumption is to a particular conclusion, forecast or projection, the more "proximate" it should be to the forward-looking information. For example, where the disclosure of risk factors and assumptions is particularly tied to a forward-looking statement but does not immediately precede or follow the forward-looking statement, it may be necessary to provide a cross-reference or footnote that ties the risk factor or assumption to the specific conclusion, forecast or projection.

2.4 Risk factor disclosure – (1) The defence for misrepresentations in forward-looking information requires the material factors that could cause actual results to differ materially from a conclusion, forecast or projection in the forward-looking information to be identified ("risk factors"). The risk factors identified in the cautionary language should be relevant to the conclusion, forecast or projection and should not be boilerplate in nature.

(2) The use of the word "material" underscores, in the Commission's view, that the cautionary statements should identify significant and reasonably foreseeable factors that could reasonably cause results to differ materially from those projected in the forward-looking statement. We do not believe that the defence should be interpreted as requiring an issuer to anticipate and discuss everything that could conceivably cause results to differ. It follows that failure to include the particular factor that ultimately causes the forward-looking statement not to materialize as predicted should not necessarily mean that the defence is not available. The defence does not, in the Commission's view, require companies to warn of every risk factor that, with the benefit of hindsight, ultimately could or might cause the forward-looking information not to come true. Similarly, the failure to include disclosure of the particular assumption that ultimately causes the forward-looking statement not to materialize as predicted should not necessarily mean that the defence is not available.

2.5 Assumption disclosure – The defence for misrepresentations in forward-looking information requires a statement to be included of the material factors or assumptions that were applied in drawing a conclusion or making a forecast or projection set out in the forward-looking information. The requirement for a statement of the material factors or assumptions that were applied requires, in the Commission's view, the factors or assumptions to be relevant to the conclusion, forecast or projection. The use of the word "material" underscores, in the Commission's view, that the defence does not require an exhaustive statement of every factor or assumption applied – a materiality standard applies.

2.6 Reasonable Basis – In order to benefit from the defence, a company must have a reasonable basis for drawing the conclusion or making the forecast or projection set out in the forward-looking information. When interpreting "reasonable basis", we believe that relevant factors would generally include the reasonableness of the assumptions applied in drawing the conclusion or making the forecast or projection; and the inquiries made and the process followed in preparing and reviewing the forward-looking information.

Part III – Defence for Misrepresentations in Oral Statements Containing Forward-Looking Information

3.1 Legislative Scheme - The *Securities Act* provides that in the case of a public oral statement containing forward-looking information, a person or company is deemed to have satisfied the requirements of the defence in paragraph 1 of subsection 138.4(9) (which are discussed in Part II of this Policy) if the person making the public oral statement states that:

a) the oral statement contains forward-looking information;

b) actual results could differ materially from a conclusion, forecast or projection in the oral forward-looking information;

c) certain material factors or assumptions were applied in drawing the conclusions or making the forecasts or projections included in the oral forward-looking information; and

d) additional information about the applicable risk factors and assumptions are contained in a "readily available" document and identifies that document.[7]

For purposes of the defence, a document filed with the Commission or otherwise generally disclosed is deemed to be "readily available".[8]

3.2 A more flexible approach – (1) The *Securities Act* recognizes that it may be unwieldy to make oral disclosures containing forward-looking information that satisfy all of the requirements of the defence contained in subsection 138.4(9). Instead, the Securities Act provides for a more flexible approach for oral statements containing forward-looking information that facilitates these types of oral communications by an issuer while still providing the information that would have been received if the forward-looking information had been contained in a written disclosure document.

(2) The deeming provision in subsection 138.4 (9.1) specifically refers to the requirements of the defence being satisfied in the case of public oral statements when the person making the public oral statement makes the required cautionary statements. In the Commission's view, subsection 138.4 (9.1) should not be interpreted as exhaustive; the requirements of the defence may be satisfied in appropriate circumstances by one person making the required cautionary statements on behalf of another person who is making the forward-looking statement. The animating principles underlying the defence support a pragmatic interpretation.

Part IV – Duty to Update

4.1 We do not interpret the defence for misrepresentations in forward-looking information as imposing upon any person or company a duty to update forward-looking information beyond any duty imposed under Ontario securities law or otherwise.

[7] See subsection 138.4(9.1) of the *Securities Act*.
[8] See subsection 138.4(9.2) of the *Securities Act*.

APPENDIX A

List of Commenters

Osler, Hoskin & Harcourt LLP on behalf of Alcan Inc., BCE Inc., The Canadian Bankers' Association, EnCana Corporation, Manulife Financial, Power Corporation of Canada, Royal Bank of Canada and TransCanada Corporation (collectively the "Osler submission").

Talisman Energy Inc. ("Talisman")

Canadian Investor Relations Institute ("CIRI")

Kenmar

APPENDIX B

OSC Policy 51-604 – Summary of Comment Letters and OSC Responses

Issue and Commenter	Public Comment	OSC Response
General Comment Kenmar	The effect of the Policy will be to water down corporate and executive accountability for defective, misleading or untimely disclosure and to undermine the intent of Bill 198.	The Policy provides guidance on the Commission's interpretation of certain aspects of the statutory defence for misrepresentations in forward-looking information (FLI). The Commission believes this guidance supports the purpose of the statutory civil liability regime for secondary market disclosure. The Policy, itself, does not legally create or modify the requirements of the defence, nor does it otherwise impact the level of accountability that issuers and management face under the statutory regime.
Kenmar	The Policy should be focused on the preventative actions that issuers should take to protect against liability for defective disclosure and not on the requirements of the defence.	It is the Commission's view that the Policy will encourage issuers to approach disclosure decisions relating to FLI cautiously and thoughtfully, ultimately resulting in better quality disclosure to investors.
Kenmar	The Commission should delay articulating any guidance on a defence for misrepresentations in FLI until a judgment has been rendered by the Supreme Court of Canada in *Kerr v Danier Leather.*	The judgment of the Supreme Court of Canada in *Kerr v Danier Leather* has been rendered. After considering that judgement the Commission has concluded that no changes are necessary to the proposed policy.
Harmonization of U.S. and Ontario standards Osler submission	Harmonization between the approaches adopted in Ontario and the U.S. is of particular importance to interlisted issuers who will seek to avail themselves of the protection of the safe harbour in their corporate disclosure on both sides of the border. The Policy should include a statement to the effect that the defence for misrepresentations in forward-looking information in Ontario is intended to be consistent with the "safe harbour" available in the U.S. and that issuers may look to practice in the U.S. for guidance in complying with the defence.	The Commission acknowledges the concerns of issuers that are interlisted in the U.S. However, the the *Securities Act* creates a separate and independent defence under the civil liability for secondary market disclosure regime. The purpose of the Policy is to provide an explanation of how the Commission views certain aspects of the defence available for misrepresentations in FLI under Ontario's regime. The Policy cannot change the requirements of the *Securities Act*, nor otherwise provide that such requirements are intended to be consistent with the requirements of the safe harbour available in the U.S. While the requirements of the defence under the *Securities Act* and the U.S. "safe harbour" may be consistent in many ways and experience in the U.S. may be helpful in analyzing elements of the defence, it is incumbent upon interlisted issuers to assess the appropriateness of their disclosure practices against the requirements of both regimes and to establish and follow disclosure practices which meet the requirements of the two regimes.
Harmonization of the Policy with NP 51-201 Osler submission	The Commission should clarify the manner in which the express provisions of the *Securities Act*, together with the Policy, are intended to fit with the provisions of NP 51-201, which also deals with disclosure related to FLI. In particular, the commenter submitted that the Commission should expressly indicate that the provisions of the *Securities Act*, together with the Policy, are	CSA members have each made amendments to NP 51-201 that, among other things, expressly repeal section 5.5 (and 5.6) of NP 51-201.

Issue and Commenter	Public Comment	OSC Response
	intended to govern the defence and that NP 51-201 has now been superceded in relation to the principles applicable to the disclosure of FLI that are necessary in order to satisfy the defence. The commenter's concern focused on section 5.5 of NP 51-201 and the reference to the fact that disclosure might include a sensitivity analysis (section 5.5(3) of NP 51-201).	
Standard of Materiality applicable to the Policy Talisman	The Policy should provide a specific definition of "materiality" or clarify the applicable standard of materiality in the context of the defence for misrepresentations in FLI. In particular, the definitions of "material change" and "material fact" encompass what is commonly referred to as the "market impact" standard of materiality, whereas other pieces of securities legislation (notably Form 51-102F2 and NI 51-101 Standards of Disclosure for Oil and Gas Activities) use the "reasonable investor" standard of materiality.	The defence for misrepresentations in FLI requires issuers to disclose "material factors" and "material assumptions" in relation to their forecasts, projections and conclusions. However, unlike the terms of "material change" and "material fact", the *Securities Act* does not prescribe definitions for these concepts. While we recognize that materiality judgments can be difficult, the Commission cannot, in a policy, provide definitions of a "material factor" or "material assumption" or otherwise establish or determine the applicable standard of materiality. This request raises issues that fall outside the scope of the Policy.
Section 2.3 the "Proximate" Requirement' Osler submission	The Policy should include guidance as to whether or when it is permissible to incorporate by reference into a document a more lengthy discussion of material risk factors and assumptions. In the context of oral statements, section 138.4(9.1) of the *Securities Act* expressly permits making reference to another document containing a full discussion of risk factors and underlying factors and assumptions. The provisions relating to written disclosure are silent with respect to the ability for issuers to adopt a similar practice in the context of shorter documents such as press releases, slide presentations and interim MD&A, which, like oral statements, may not lend themselves to a full discussion of the risk factors and underlying factors and assumptions. This silence could be interpreted by the courts as deliberate. This would be contrary to current practice in Canada and the U.S. The Commission should clarify that incorporation by reference is generally an acceptable approach in shorter disclosure documents in the interests of preserving clarity and readability in corporate disclosure.	The Commission does not believe it is in a position to provide more specific guidance in the Policy on the statutory interpretation as it relates to this issue. The Commission believes, however, that as a policy matter in appropriate circumstances where material risk factors and assumptions have been identified in a document, an issuer ought to be able to incorporate by reference into a document a more lengthy discussion of material risk factors and assumptions. We also note from the memorandum of law provided by the commenter that in the U.S., the safe harbour provided under the *Private Securities Legislation Reform Act of 1995* is also silent regarding whether cautionary language may be incorporated by reference when the forward-looking statement is written rather than oral. In some cases, the U.S. courts have found that incorporation by reference in the context of written disclosure materials may be permissible, provided that the reference is clear and explicit.
Section 2.5 Assumption Disclosure CIRI	The requirement to disclose material factors or assumptions is not present in the U.S. safe harbour provisions and issuers will therefore not be able to draw upon U.S. practice for guidance. The Policy should clarify the difference between the concept	Section 2.5 of the Policy provides some explanation as to how the Commission would approach the disclosure of material factors or assumptions required under section 139.4(9)(1)(ii) of the *Securities Act*.

Issue and Commenter	Public Comment	OSC Response
Osler submission Talisman	of a "material factor" and a "material assumption" and provide guidance on the requirement to disclose "material factors or assumptions" underlying the forecast, projection or conclusion.	The Commission believes that issuers should make reasonable judgements with respect to these matters in the context of the particular circumstances.
CIRI	The Commission should clarify whether cautionary language in news releases and MD&A should be expanded in all instances to include material factors and assumptions and a reference that the issuer believes the assumptions to be reasonable. For the safe harbour defence in the U.S., risks but not material factors or assumptions, related to FLI are required in the cautionary language. Different safe harbour defence requirements in Canada would appear to require expanded cautionary language.	The provisions of the *Securities Act* specifically provide that this defence for a misrepresentation in FLI in written materials is only available if, among other things, the document contains "a statement of material factors or assumptions that were applied in drawing a conclusion or making a forecast or projection set out in the forward-looking information". We do not believe it is necessary to clarify that in order to meet the requirements of the defence under the Securities Act, additional disclosure may, in some instances, be required in Ontario compared to the U.S. There is no requirement that cautionary language include a statement that the issuer believes the assumptions are reasonable. Section 138.4(9)(2) of the *Securities Act* simply requires the issuer to have a reasonable basis for drawing the conclusions or making the forecasts and projections set out in the FLI. In the absences of such a requirement, the Commission does not believe issuers must make such a statement.
CIRI	The Commission should clarify that the statements "We do not believe that the defence should be interpreted as requiring an issuer to anticipate and discuss everything that could conceivably cause results to differ. It follows that failure to include the particular factor that ultimately causes the forward looking statement not to materialize as predicted should not necessarily mean that the disclosure is not protected by the defence" pertain to assumptions as well as to risk factors.	Subsection 2.5 of the Policy provides that "the use of the word 'material' underscores, in the Commission's view, that the defence does not require an exhaustive statement of every factor or assumption applied – a materiality standard applies." We believe that this statement, with its emphasis on materiality, makes it clear that the Commission is of the view that a failure to include every assumption or factor applied in drawing a conclusion or making a forecast or projection will not necessarily mean that the defence is not available. To address the commenter's comment, however, we have clarified the Policy.
CIRI	The Policy should provide that the factors or assumptions required to be disclosed should not only be relevant and material to the conclusion, forecast or projection, but should also be qualified as "reasonably foreseeable and probable".	Section 138.4(9)(1)(ii) of the *Securities Act* requires disclosure of "material factors or assumptions that were *applied* in drawing a conclusion or making a forecast or projection set out in the forward-looking information". The Commission is of the view that a qualification that factors and assumptions be "reasonably foreseeable and probable" is too narrow. Rather, an issuer must disclose the assumptions or factors it *applies* which are, *relevant* and *material* to the conclusion, forecast or projection. If the assumptions or factors were not reasonable, an issuer would arguably fail to establish "a reasonable basis for drawing the conclusions or making the forecasts and projections set out in the forward-looking information."

Issue and Commenter	Public Comment	OSC Response
Talisman	The Policy should provide more specific guidance on disclosure of material assumptions and, in particular: • Whether material assumptions should be qualitative or quantitative in nature (or both); • What level of detail is expected in the material assumptions; and • For quantitative assumptions, how should an issuer balance disclosure requirements with the need to protect competitive information.	The Commission does not believe it is in a position to provide more specific guidance. Determining what assumptions to apply in forming a conclusion, forecast or projection is a matter of judgment and a fact-specific exercise. In some circumstances greater detail about a material assumption will be required than in others. The Commission is of the view that "material assumptions" may be qualitative or quantitative in nature and that clarification in the Policy is not necessary.
Section 2.6 Reasonable Basis CIRI	Issuers must follow appropriate processes and procedures in preparing and reviewing FLI. Issuers should be able to rely on implementation of their disclosure controls and procedures as a defence to misrepresentations in FLI.	As described in section 2.6 of the Policy, the Commission believes that the process followed by an issuer in preparing and reviewing forward-looking information, including the implementation of disclosure controls and procedures, may be relevant to establishing a "reasonable basis" for forward-looking information. However, process alone may not be sufficient to establish a "reasonable basis" for forward-looking information. Other considerations, such as inquiries made and assumptions applied, may be relevant.
Section 3.2 A More Flexible Approach CIRI	In the context of oral statements, the Policy should clarify the type of occasions, if any, when an FLI spokesperson would need to reiterate any cautionary statements.	In the case of public oral statements, subsection 138.4(9.1) of the *Securities Act* provides that the requirements of the defence for misrepresentations in forward-looking information will be deemed to be satisfied when the person making the public oral statement makes the required cautionary statements. In Section 3.2(2) of the Policy, the Commission expresses the view that the requirements of the defence may be satisfied *in appropriate circumstances* by one person making the required cautionary statements on behalf of another person who is making the forward-looking information. Issuers must exercise their own judgment in determining when a spokesperson may need to reiterate the required cautionary statements. The Commission does not believe it is in a position to provide more specific guidance.