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Canadian Securities Administrators

Autorités canadiennes en valeurs mobilières

CONCEPT PROPOSAL FOR AN INTEGRATED DISCLOSURE SYSTEM

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GLOSSARY OF TERMS

The following are brief explanations of certain terms used in this Concept Proposal:

"Continuous disclosure" means all information, other than prospectuses and offering memoranda, concerning the business, operations or capital of an issuer that the issuer files with a Canadian securities regulatory authority.

An issuer's **"continuous disclosure record"** means all continuous disclosure filed by the issuer with a Canadian securities regulatory authority.

"CSA" means the Canadian Securities Administrators, comprised of the thirteen securities regulatory authorities in Canada.

"GAAP" means generally accepted accounting principles.

"GAAS" means generally accepted auditing standards.

"IDS" means the proposed integrated disclosure system.

"IDS AIF" means the annual information form prescribed for purposes of the IDS.

An issuer's **"IDS disclosure base"** means that part of the issuer's continuous disclosure record consisting of the issuer's current IDS AIF and all QIFs, and SIFs filed after the date of the current IDS AIF.

"Marketing communication" refers to any oral or written communication disseminated by or on behalf of an issuer to promote (or that can reasonably be considered to have been intended to promote) a purchase or sale of a security of the issuer or of an affiliate of the issuer.

"MD&A" means management's discussion and analysis of the financial condition and results of operations of an issuer, as prescribed by securities legislation.

"MRRS Policy" means National Policy 43-201 *Mutual Reliance Review System for Prospectuses and AIFs*.

"NI 44-101" means proposed National Instrument 44-101 *Short Form Prospectus Distributions* (republished for comment in the week ended December 17, 1999), the proposed reformulation of CSA National Policy Statement No. 47 *Prompt Offering Qualification System*.

"QIF" means the quarterly information form prescribed for purposes of the IDS.

"Reporting issuer" denotes an issuer that is obligated to file prescribed continuous disclosure; when the term is used:

- in respect of a jurisdiction that currently applies the concept, it has the meaning ascribed to the term under the securities legislation of the jurisdiction; and

- in respect of any other jurisdiction, it means an issuer that files in the jurisdiction continuous disclosure substantially equivalent to that required of a reporting issuer in a jurisdiction that currently applies the concept.

"SEDAR" means the system for electronic filing and retrieval of disclosure documents governed by National Instrument 13-101 *System for Electronic Document Analysis and Retrieval (SEDAR)*.

"SIF" means the supplementary information form prescribed for purposes of the IDS.

Many of the terms used in this Concept Proposal are defined in National Instrument 14-101 *Definitions* or in the securities legislation of individual jurisdictions.

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EXECUTIVE SUMMARY

1. Relationship to Existing Regulatory Systems

The proposed IDS would be a voluntary regime governing disclosure and distributions of securities by participating issuers. The IDS would coexist with existing alternative distribution procedures: the general long form prospectus procedures, variants such as the short form prospectus and shelf distribution procedures, and the "closed system" for prospectus-exempt distributions. The CSA will consider eliminating the short form prospectus and shelf distribution systems for IDS-eligible issuers if the pilot introduction demonstrates the IDS to be a successful substitute for these regimes. The IDS could also reduce issuers' recourse to prospectus exemptions for raising capital and the associated complexities of the closed system for resales of privately placed securities.

The CSA expect that the IDS could be implemented in most jurisdictions, without statutory amendment, by rule, regulation or policy.

2. Purposes and Focus

The IDS is intended to provide investors in both the primary and secondary markets with the same timely prospectus-quality issuer disclosure, while offering IDS issuers more timely and flexible access to primary market capital. To achieve these purposes the IDS would focus on the "IDS disclosure base" and de-emphasize the prospectus.

3. Eligibility

The CSA propose broad access to the IDS. IDS eligibility would be conditional on the issuer having reporting issuer status in all CSA jurisdictions.

The other IDS eligibility criteria set out in the Concept Proposal are intended to screen out issuers whose continuous disclosure would not be expected to provide the comprehensive information base on which the IDS is premised. For example, information concerning the operations of a special purpose issuer of derivative securities or a blind pool would

generally be of limited value and for that reason such issuers would not be eligible to offer securities under the IDS. Other criteria are modelled on the existing statutory bars to a prospectus receipt, targeting issuers whose history raises concerns about reliability.

4. IDS Disclosure Base

The IDS disclosure base would consist of publicly available continuous disclosure, upgraded to the prospectus standard of certified "full, true and plain disclosure" and in some cases provided earlier than prescribed under current requirements. Principal components would be:

- an annual information form (the "IDS AIF"), comparable to the AIF used for short form prospectus distributions but with added content;
- quarterly information forms ("QIFs") for the first three quarters of each year, consisting primarily of upgraded interim financial statements and MD&A; and
- supplementary information forms ("SIFs"), comparable to current material change reports but also triggered by additional specified events, whether or not technically "material", and containing prospectus-quality disclosure concerning events such as significant acquisitions.

5. IDS Prospectuses

The IDS would apply existing statutory requirements for a prospectus but with streamlined documents and more emphasis on the preliminary IDS prospectus, with a view to providing prospective investors with useful offering information earlier in their decision-making process. A purchase would not be enforceable against an investor who did not receive the preliminary IDS.

An IDS prospectus would contain full disclosure concerning the offering, the offered securities, risk factors and investors' statutory rights. Most disclosure concerning the issuer could be incorporated by reference from the issuer's IDS disclosure base.

6. Regulatory Role

An issuer's IDS disclosure base would be subject to a continuous disclosure review system. With the great majority of non-offering-specific disclosure required in an IDS prospectus being incorporated by reference from the IDS disclosure base, the IDS prospectus itself would undergo streamlined regulatory screening to identify cases of IDS ineligibility, issues that could prompt a detailed review or statutory grounds for receipt refusal. Few delays or refusals of IDS prospectus receipts are anticipated.

7. Marketing

Securities marketing and "pre-marketing" (before the preliminary prospectus) activities and restrictions have long been a source of concern and some confusion. With a comprehensive IDS disclosure base in place to address concerns about unequal access to information, the CSA consider that a more flexible approach to marketing restrictions would be desirable under the IDS.

The IDS would therefore give IDS issuers wide latitude in the form, content and timing of their marketing communications, exempting them from current marketing restrictions and instead imposing more responsibility on the issuer to ensure the reliability of marketing communications by requiring the incorporation by reference of written marketing communications in the IDS prospectus.

The IDS would directly prohibit any misrepresentation in furtherance of a trade, mirroring a useful provision of current British Columbia legislation.

8. Changes Outside the IDS

The CSA are considering extending IDS disclosure enhancements, affecting content, quality and timing of continuous disclosure, and IDS marketing restrictions, to all issuers.

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PART I. INTRODUCTION

This Concept Proposal describes a system of information disclosure and securities offering procedures developed by the Canadian Securities Administrators (the "CSA") to enhance the quality and timeliness of information available to investors and facilitate access to Canadian capital markets by issuers of securities. Parts IV and V of this Concept Proposal identify other initiatives under consideration by the CSA, including a proposal for disclosure enhancements of general application.

The objective of the CSA is to foster fair and efficient capital markets in a changing market environment in a way that facilitates capital formation without compromising the protection of investors. More specifically, the CSA seek to:

- facilitate prompt and flexible access by business to capital;
- enhance the ability of investors to make informed investment decisions using more useful and reliable information from securities issuers; and.
- achieve a better match of regulatory effort to existing and prospective market conditions.

The key to achieving these objectives, in the view of the CSA, lies in integrating and upgrading the quality of information made available on a continuous basis to all market participants.

The proposed "integrated disclosure system" (the "IDS") would integrate the information required to be provided by reporting issuers to investors in both the primary and secondary securities markets in a common continuous disclosure base. The foundation of the IDS would be an upgraded "IDS disclosure base" that offers the public timely access to information relating to an issuer and its business, comparable to the information currently provided in a prospectus. The IDS disclosure base, with its comprehensive and timely information available to all investors, would represent an important advance in investor protection.

With its IDS disclosure base in place, a participating issuer would be able to respond immediately to opportunities in the primary market by using an abbreviated securities offering document that incorporates by reference the issuer's IDS disclosure base and undergoes streamlined regulatory screening.

The IDS would provide an alternative to existing procedures for distributions of securities under a prospectus, including the long form prospectus procedures, the short form prospectus procedures under NI 44-101, and the shelf distribution procedures under proposed National Instrument 44-102 *Shelf Distributions*[1], and for "closed system" distributions for which an exemption from prospectus requirements is available.

The CSA propose to develop an IDS national instrument that would be implemented on a pilot basis after consideration of public comment. During the pilot period, qualifying issuers would be able to participate in the IDS and offer securities using IDS procedures or use any of the other existing prospectus exemptions or offering procedures (subject to applicable restrictions, including current marketing restrictions) for which they are eligible.

Pilot introduction of the IDS will enable regulators, issuers and investors to assess the merits of the IDS. The CSA will consider modifications to the IDS to address problems or deficiencies that come to light during the pilot period. If the IDS proves successful during its pilot introduction, the CSA will consider eliminating use of the short form prospectus and shelf distribution procedures by issuers that are eligible to use the IDS.

PART II. BACKGROUND

A. Current Securities Offering Procedures

Securities regulation in Canada has traditionally focused primarily on new offerings of securities.

Securities legislation generally prescribes the use of a long form prospectus that provides primary market investors with comprehensive information concerning the securities offered, details of the offering and the business and affairs of the issuer.

An issuer that has issued securities to the public under a prospectus, or has otherwise become a reporting issuer under securities legislation, must make both periodic (annual and quarterly) public disclosure, primarily concerning financial results, and event-triggered public disclosure of material changes in its business or affairs.

Securities legislation exempts certain private placements and other distributions of securities from prospectus requirements. Securities distributed under a prospectus

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[1] Published for comment in the week ended October 2, 1998.

exemption generally enter a closed system designed to prevent the entry of securities into a public market that lacks relevant information about the issuer.[2] Resale restrictions may condition the release of securities from the closed system on the use of a prospectus, the issuer having built up a history as a reporting issuer in compliance with continuous disclosure obligations or the expiration of a prescribed period of time.

The CSA developed the short form prospectus and shelf distribution procedures in an effort to expedite primary market access for certain issuers while maintaining the substance of long form prospectus disclosure in modified disclosure documents. Under these alternative procedures, issuers provide additional continuous disclosure by way of an annual information form (an "AIF") that contains disclosure concerning the business and affairs of the issuer but not specific to a particular offering of securities. The reliance placed by these distribution systems on the AIF represents a shift away from the prospectus as the cornerstone disclosure document. A qualifying issuer can offer securities to the public under these systems using a simplified prospectus that discloses information pertaining to the particular offering and incorporates by reference the AIF and other elements of the issuer's continuous disclosure record. Because the AIF forms part of the issuer's continuous disclosure record, these alternative primary market offering procedures also provide enhanced information to investors in the secondary market.

B. Changes in the Market Environment

While securities legislation remains focused on the primary market and the prospectus, most investment activity occurs in the secondary market, which today is overwhelmingly larger -- on the order of 25 times larger[3] -- than the primary market.

Other developments, including advances in information technology and increasing globalization of capital markets, have profoundly affected Canada's capital markets. Issuers and investors alike need to be able to respond knowledgeably and promptly to new information and market opportunities.

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[2] In some circumstances, securities legislation also requires that securities issued pursuant to certain private placement exemptions remain within the closed system for a specified period of time even if the issuer has been a reporting issuer subject to the continuous disclosure requirements in the particular jurisdiction.

[3] Comparison of Canadian primary and secondary equity market activity for 1998 by the Investment Dealers Association of Canada.

The divergence is even more pronounced in the United States. The Toronto Stock Exchange Committee on Corporate Disclosure in its March 1997 report entitled *Responsible Corporate Disclosure* (the "Allen Report") cited, at page 3, the finding of the United States Securities and Exchange Commission, noted at page 2 of its July 24, 1996 *Report of the Advisory Committee on the Capital Formation and Regulatory Processes* (the "Wallman Report"), that secondary markets had become 35 times larger than primary markets.

The CSA believe that the traditional regulatory focus on primary market prospectus disclosure is no longer sufficient. Integration of the information that issuers disclose to investors in the primary and secondary markets was advocated in the Allen Report and, before that, as part of the system of "company registration" proposed in the Wallman Report. A similar concept underlies elements of the extensive, and considerably more complex, proposal for the modernization of the United States federal regulatory system for securities offerings released by the United States Securities and Exchange Commission (the "SEC") on November 3, 1998 under the title *The Regulation of Securities Offerings,* commonly referred to as the "Aircraft Carrier Release".
The CSA took important steps toward the integration of disclosure with the adoption of the short form prospectus and shelf distribution systems. Experience with these systems has demonstrated the feasibility of heightened reliance on enhanced continuous disclosure (the AIF) to facilitate issuer access to the primary market.

Further integration of disclosure is facilitated by advances in technology that allow broad, timely and economical dissemination of information. An important example is the CSA's *System for Electronic Document Analysis and Retrieval* ("SEDAR") under which reporting issuers file information with regulators electronically. SEDAR filings are available to the public on the Internet.

PART III. THE INTEGRATED DISCLOSURE SYSTEM

A. Development of the IDS

In developing the IDS, the CSA were guided by their objective of facilitating capital formation without compromising investor protection. Their goal is a system that offers streamlined and flexible access to markets, enhances the quality, timeliness and accessibility of corporate disclosure, and aligns regulatory effort with market needs.

The IDS would shift the reporting focus from transactional offering disclosure to continuous disclosure, to provide primary and secondary markets equal access to comprehensive and timely information concerning issuers and material developments affecting their business and operations.

As part of the CSA effort to better direct regulatory resources to meet market needs, CSA staff are increasing their scrutiny of continuous disclosure. The IDS would build on this new emphasis by shifting much corporate disclosure from prospectuses to continuous disclosure. With more information provided in continuous disclosure, which will be subject to its own regulatory review systems, the IDS would also result in streamlined regulatory screening of IDS prospectuses. The result, for participating issuers, should be more efficient, flexible and predictable access to capital.

B. Eligibility to Use the IDS

1. Purposes of IDS Eligibility Criteria

The IDS would be a broadly inclusive system. Because the IDS is designed to provide a much higher quality of disclosure to secondary market investors without compromising the disclosure available to investors in the primary market, the CSA believe that the IDS should be more widely available than the short form prospectus or shelf distribution procedures.

In developing the IDS, the CSA sought to ensure that only issuers that can provide the base of high quality continuous disclosure on which the IDS is built are eligible to use the IDS. The IDS eligibility criteria are also designed to:

- avoid arbitrary exclusions not consistent with broader IDS principles or overriding concerns of investor protection; and

- provide clarity, simplicity, transparency and predictability for issuers, investors and regulators.

2. Specific IDS Eligibility Criteria

The IDS would be open to an issuer that meets all of the following five criteria:

- **Reporting issuer status.** It is a reporting issuer in all jurisdictions.

- **Continuous disclosure compliance.** It is in compliance with its continuous disclosure obligations.

- **Current base disclosure document.** Its disclosure record contains a current base disclosure document in the form of either a current IDS AIF or, for initial entry into the IDS, a long form prospectus that has not lapsed or a short form prospectus that has not lapsed accompanied by a copy of all material incorporated by reference.

- **Listing.** Equity securities of the issuer are listed on a market recognized for this purpose.

- **Not in excluded class.** It is none of the following:

  - *a special purpose issuer of derivative or asset-backed securities;*

- *an issuer that has no significant assets other than money, no business in operation and no specific business plan reasonably capable of implementation in the near future;*

- *a blind pool, a capital pool company, a keystone company, or equivalent; or*

- *a mutual fund.*

An IDS issuer will become ineligible if it ceases to satisfy any of these eligibility criteria, or if a securities regulator: (i) knows of material unresolved CSA staff comments on the issuer's disclosure filings; or (ii) is aware of circumstances that would, if an issuer filed a prospectus, obligate the regulator to refuse to issue a prospectus receipt.

3. Discussion of the IDS Eligibility Criteria

(a) Reporting Issuer Status

The issuer is a reporting issuer in all jurisdictions.

IDS eligibility would require that the issuer be a reporting issuer in all Canadian jurisdictions. No minimum period of reporting issuer status would be specified.

Under the securities legislation of most CSA jurisdictions, issuers of securities incur public disclosure and filing obligations as a consequence of becoming a reporting issuer. These obligations are consistent with the foundation of the IDS itself: a comprehensive publicly-available base of disclosure by participating issuers. As such, in the view of the CSA, reporting issuer status is an appropriate condition of IDS eligibility.

This IDS eligibility criterion also addresses a significant source of confusion and inefficiency in securities regulation in Canada: increasingly artificial trading restrictions premised on the containment of information within geographic boundaries.

The closed system best illustrates the awkwardness of the traditional premise. As noted earlier, the closed system was designed to reduce the likelihood of securities entering a public market that lacks public disclosure about the issuer. Closed system resale restrictions defer many resales of privately placed securities to the public (without a prospectus or an available prospectus exemption) until the issuer has been a reporting issuer and complied with the associated continuous disclosure requirements in the

jurisdiction(s) in which the resale takes place for a prescribed period of time. A technological environment that continually simplifies the movement of information (and of securities) requires that issuers, regulators, exchanges, transfer agents and other market participants be more vigilant in ensuring compliance with closed system restrictions.

This IDS eligibility criterion raises three issues:

- *Mechanical feasibility.* In the view of the CSA, attainment and maintenance of reporting issuer status in multiple jurisdictions no longer presents the mechanical impediments that might have prevailed before recent developments in information processing technology and, most important, SEDAR. With SEDAR, filings are no more mechanically difficult in 13 jurisdictions than in one.

- *Filing Cost.* Gaining and maintaining reporting issuer status in additional jurisdictions would impose costs on an issuer. The CSA are confident that the benefits of the IDS to an issuer justify some additional cost. Regulatory fees are, moreover, already under consideration by individual CSA members and by the CSA as a whole.

- *Translation*. Accessibility of disclosure is an important foundation of the IDS and securities regulation generally. Maximum accessibility might be achieved by requiring that all disclosure be provided in at least two languages. The CSA recognize, however, that translation costs can be substantial. Investor interest and market demand would, moreover, encourage issuers to accommodate the language needs of their investors voluntarily, particularly in jurisdictions in which they have a significant investor base.

  For these reasons, the IDS reflects the approach that has been applied to short form prospectus distributions in Québec.

  If an issuer files an IDS prospectus in a particular jurisdiction, that IDS prospectus and any portion of the issuer's continuous disclosure record that is incorporated by reference in the IDS prospectus must be filed in the language or languages in which a prospectus is required to be filed in that jurisdiction. The IDS would not require any change to current requirements governing the language of a prospectus filed in a jurisdiction.

  In respect of continuous disclosure, other than when incorporated by reference in an IDS prospectus, an issuer would be considered to comply with reporting issuer continuous disclosure obligations in all jurisdictions for purposes of IDS eligibility if it files its continuous disclosure in all jurisdictions in the language or languages required in the jurisdiction of the issuer's principal regulator, as determined under the MRRS Policy.

Participation in the IDS, and maintaining all-jurisdiction reporting issuer status as a condition of continued IDS eligibility, would not impose on an issuer any translation requirements beyond the requirements of its principal regulator. Additional translation requirements would be triggered only if the issuer files an IDS prospectus in a jurisdiction that requires a prospectus to be filed in a language other than that required by the issuer's principal regulator, and the translation obligation would apply only to that IDS prospectus and continuous disclosure incorporated by reference.

(b) Continuous Disclosure Compliance

The issuer is in compliance with its continuous disclosure obligations.

For initial entry into the IDS, this criterion would require that an issuer be in compliance with the continuous disclosure requirements applying to non-IDS issuers. To maintain or regain eligibility thereafter, the issuer would have to be in compliance with the IDS continuous disclosure requirements.

This criterion reflects the basic premise of the IDS that prospectus-quality information concerning participating issuers should be publicly available at all times. Any participating issuer that fails to maintain that standard would become ineligible to use the IDS.

(c) Current Base Disclosure Document

Its disclosure record contains a current base disclosure document in the form of either a current IDS AIF or, for initial entry into the IDS, a long form prospectus that has not lapsed or a short form prospectus that has not lapsed accompanied by a copy of all material incorporated by reference.

This criterion does not imply that IDS participants can substitute non-IDS disclosure documents for IDS documents. Rather, the criterion is designed to provide flexibility for entry into the IDS. Although an IDS AIF would serve as an obvious IDS entry document, the CSA see no reason to require preparation of such a document as a condition of entry into the IDS by an issuer that already has available a filed and current long form prospectus, or a short form prospectus accompanied by a copy of all material incorporated by reference, that provides information comparable in quality to an IDS AIF and addresses the subject matter of an IDS AIF. Consequently, an issuer's IPO prospectus could serve as the base disclosure document.

(d) Listing

Equity securities of the issuer are listed on a market recognized for this purpose.

The markets recognized[4] for this purpose would include the Canadian Venture Exchange, The Winnipeg Stock Exchange, The Toronto Stock Exchange, the Montreal Exchange, the New York Stock Exchange, the American Stock Exchange, the London Stock Exchange, the NASDAQ National Market and the NASDAQ SmallCap Market.

Additional regulatory supervision by recognized markets, through their assessment, monitoring or review of listed issuers, provides a useful enhancement of investor protection. Many of the proposed recognized markets, for example, review or regulate proposals to undertake related party transactions or to grant options to acquire securities, while others that undertake less transactional review impose rigorous initial listing and listing maintenance requirements.

(e) Issuer Not in Excluded Class

The issuer is none of the following:

- *an issuer organized and operating exclusively for the purpose of issuing derivative or asset-backed securities;*
- *an issuer that has:*
  - *no significant assets other than money;*
  - *no business in operation; and*
  - *no specific business plan reasonably capable of implementation in the near future, or a business plan that contemplates only a business combination with one or more other unidentified issuers;*
- *a blind pool;*
- *a capital pool company as defined in Canadian Venture Exchange Policy 2.4 Capital Pool Companies, or equivalent;*

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[4] The concept of "recognized markets" is currently used in determining eligibility to use the parallel "SHAIF" systems established under Alberta Securities Commission Rule 45-501 *System for Shorter Hold Periods for Issuers Filing an AIF* and British Columbia Securities Commission Blanket Order BOR 98/7.

- *a keystone company as defined in Manitoba Securities Commission Rule 44-501 Keystone Companies, or equivalent; or*

- *a mutual fund.*

The CSA consider the IDS to be unsuitable for issuers of the types excluded by this proposed IDS eligibility criterion. Continuous disclosure concerning these ineligible issuers would not provide the desired information base for investors, either because there is little or no information to disclose or because information concerning issuers of these types is far less important to an investor than information concerning the securities they issue or the assets or other issuers standing behind those securities. The CSA are of the view that existing offering and disclosure systems would better serve investors in securities of these excluded issuers, and the issuers themselves.

4. Eligibility Certificate

As currently required in connection with participation in the short form prospectus distribution system, IDS participants will have to file eligibility certificates on the filing of each IDS prospectus. The eligibility certificate would be executed on behalf of the issuer by one of the senior officers of the issuer and would state that the issuer satisfies the IDS eligibility criteria.

5. Rejection of Quantitative IDS Eligibility Criteria

In developing eligibility criteria, the CSA rejected quantitative measures, such as an issuer's revenues, assets or market capitalization, as a basis for IDS eligibility.

The CSA considered a number of arguments before reaching its conclusion:

- It is sometimes assumed that larger issuers will provide a higher quality of public disclosure. The CSA, however, are not persuaded that there is any significant demonstrable linkage between an issuer's size and the quality of the information it provides to investors.

- A quantitative financial eligibility criterion could produce complexity and unpredictability: an issuer might achieve and lose eligibility repeatedly as its income or market capitalization fluctuates.

- The CSA were not persuaded by the "analyst following" argument that a larger issuer is likely to command a greater following among investment analysts, whose analysis in turn is assumed to educate investors and encourage issuers to maintain and improve their disclosure.

Investors can benefit from ready access to balanced analysis from a wide variety of independent sources. The CSA, however, are not persuaded either that this outcome is essential to the functioning of the IDS, nor that ready access to varied and balanced analysis would necessarily follow from size restrictions on IDS eligibility.

Proponents of the "analyst following" view often point to the United States as a model. Differences of scale, however, must be recognized. With fewer investors, fewer investment firms willing to sustain the costs of retail analysis, and fewer trained analysts available to perform the work, Canadian investors have not typically had available to them the array of independent analysis, even for large issuers, often seen in the United States. Much of the analysis that is undertaken, moreover, is not readily available to the general public because it has been commissioned by a single institutional investor or is available only by costly subscription.

Information technology makes possible ever faster and wider dissemination and processing of investment information concerning reporting issuers of all sizes. The SEDAR website, already familiar to many Internet users[5], provides public access to disclosure filed by reporting issuers across Canada. The CSA are hopeful that this and other technological developments, coupled with increasingly knowledgeable investors, will spur more informed analysis by investors themselves. Finally, the CSA believe that the significant improvement in the information available to investors as a result of IDS disclosure requirements justifies broad IDS eligibility.

6. IDS Disqualification

An issuer that participates in the IDS will become ineligible to participate further in the IDS if it ceases to satisfy one or more of the five IDS eligibility criteria enumerated above, or if a securities regulator: (i) knows of material unresolved CSA staff comments on the issuer's disclosure filings; or (ii) is aware of circumstances that would, if an issuer filed a prospectus, obligate the regulator to refuse to issue a prospectus receipt.

Statutory prohibitions on the issuance of a prospectus receipt may apply in circumstances such as the following:

- it is not in the public interest;
- an unconscionable consideration has been paid or given, or is intended to be paid or given, for promotional purposes or for the acquisition of the property;

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[5] The SEDAR website averaged 1.5 million "hits" per week and has received up to 40 000 hits per hour and up to 1.8 million hits per week, as of February 1999.

- the issuer's proceeds from an offering of securities currently in the course of distribution will be insufficient to enable the issuer to accomplish its stated business purposes;

- having regard to the financial condition of the issuer, or of an officer, director, promoter or control person of the issuer, the issuer cannot reasonably be expected to be financially responsible in the conduct of its business;

- the past conduct of the issuer, or of an officer, director, promoter or control person of the issuer, affords reasonable grounds to believe that the business of the issuer will not be conducted with integrity and in the best interests of its securityholders; or

- a person or company that prepared or certified any part of the issuer's IDS disclosure base is not acceptable to the regulator.

A disqualified issuer will remain ineligible until such time, if any, as the issuer resolves the reason for disqualification. For example, if an IDS issuer does not comply with its IDS continuous disclosure requirements, it will be unable to file an IDS prospectus until the required continuous disclosure has been filed.

An issuer would not be able to use the offering procedures under the IDS to offer securities at a time when the issuer is ineligible to use the IDS. However, an issuer's ineligibility to participate in the IDS, whether or not the issuer had previously participated or been eligible to participate in the IDS, would not preclude the issuer from:

- preparing, filing or maintaining an IDS disclosure base; or

- subsequently achieving or regaining eligibility to use the IDS.

C. IDS Continuous Disclosure

The IDS would entail significant changes in information disclosure by issuers, all intended to enhance the quality and timeliness of information available to investors. Core disclosure documents, some unique to the IDS and others modified from disclosure documents in use under existing disclosure systems, that together would comprise an issuer's IDS disclosure base are described immediately below under the heading "IDS Continuous Disclosure Documents". Other changes in disclosure standards and content that would be implemented as part of the IDS are described later under the heading "IDS Continuous Disclosure Enhancements".

1. IDS Continuous Disclosure Documents

The IDS disclosure base of a participating issuer would consist of an annual base disclosure document containing comprehensive prospectus-quality information about the issuer and its business, updated by both periodic (quarterly) disclosure and event-triggered disclosure of significant changes affecting the issuer or the value of its securities.

A more detailed description of the IDS disclosure documents follows.

(a) The IDS Disclosure Base

(i) IDS Annual Information Form

The cornerstone of the IDS disclosure base is the IDS annual information form (the "IDS AIF"), an annual consolidation of information about the business and affairs of an IDS issuer.

The form and content of the IDS AIF would be similar to those of the AIF already in use by participants in the short form prospectus distribution system. The IDS AIF would require certain additional disclosure not currently required in an AIF, including full financial statements with comparatives, information concerning legal proceedings affecting the issuer, material contracts to which the issuer is a party, escrow affecting securities of the issuer, risk factors relating to the issuer and its business and not specific to a particular offering of securities, a statement of the issuer's consolidated capitalization and identification of the issuer's auditors and transfer agents.

The IDS AIF would be prepared and filed annually. To the extent that information contained in other required disclosure filed during the immediately preceding fiscal year of the issuer continues to apply, that information would be restated and included in the IDS AIF.

The standard of disclosure required in the IDS AIF would be full, true and plain disclosure, as is currently the case with disclosure in a prospectus.

(ii) Quarterly Information Form

The IDS AIF would be supplemented by a quarterly information form (a "QIF") filed for each of the issuer's first, second and third financial quarters.

A QIF would include the issuer's interim financial statements for the relevant year-to-date period and management's discussion and analysis ("MD&A") similar to that required under NI 44-101. A QIF would also list each SIF (see below) filed by the issuer since the date of its current IDS AIF, to the extent that the information contained in an SIF has not been superseded. In each case, the QIF would provide the date of filing and a brief description of the subject matter of the SIF.

(iii) Supplementary Information Form

If a triggering event occurs during the year, the IDS would require an issuer to file an SIF disclosing the triggering event. A supplementary information form (an "SIF") would be very similar to, and for IDS issuers would take the place of, the material change report currently required to be filed under the securities legislation of many CSA jurisdictions.

SIFs would be required to contain full, true and plain (that is, prospectus-quality) disclosure of the event and would form part of the issuer's IDS disclosure base. As is now the case with material change reports, confidential filing of the SIF would be permitted when, in the opinion of the reporting issuer, the required disclosure would be unduly detrimental to the interests of the reporting issuer or when the material change consists of a decision to implement a change made by senior management of the issuer who believe that confirmation of the decision by the board of directors is probable and senior management has no reason to believe that persons with knowledge of the material change have made use of such knowledge in purchasing or selling securities of the issuer. However, an issuer could not file a prospectus while a confidential SIF is pending.

As is currently the case in most CSA jurisdictions in respect of material changes, including those jurisdictions that do not prescribe material change reports, the events that trigger the obligation to file SIFs would also obligate the issuer to announce the event, forthwith after the occurrence, by issuing a news release. News releases would form part of the issuer's continuous disclosure record but would not form part of the IDS disclosure base.

The obligation to issue a news release and file an SIF would be triggered not only by the occurrence of a material change, but also by the occurrence of any of the following events, whether or not it constitutes a material change:

- a change in the issuer's name;
- a change of the issuer's auditor;

- a change of the issuer's chairperson, chief executive officer, chief financial officer, chief operating officer, president or any equivalent position;

- a change in dividend policy or practice;

- the occurrence of an event concerning the financial condition of the issuer that, if a distribution were in progress at the time, would render the issuer a "specified party" as the term is defined in proposed Multi-Jurisdictional Instrument 33-105 *Underwriting Conflicts*[6], except to the extent that, in the case of a breach of a financial covenant, there is a reasonable likelihood of the breach being waived or cured;

- the issuer forming, or becoming aware that a selling securityholder has formed, a reasonable expectation that a prospectus distribution of equity securities of the issuer by the issuer or the selling securityholder, respectively, will proceed;

- the completion of a private placement transaction or other private financing transaction, or, upon the issuance of a press release, a proposed private placement or private financing, the SIF to disclose the nature of the securities offered, the offering size (where offering completed) or estimated size (for proposed offerings which have been announced by way of press release), and names of selling securityholders (if applicable);

- the completion of any prospectus distribution, the SIF to disclose the aggregate number or value of securities distributed and the net proceeds to the issuer;

- the abandonment of any prospectus distribution, or of a proposed private placement transaction or other proposed private financing transaction in connection with which a SIF was required;

- in respect of a significant business combination, including a "significant acquisition" of a business or of assets that amount to a business, or a significant acquisition of significant influence (applying the definitions and significance tests in NI 44-101), three SIFs as follows:

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6 Published for comment in the week ended February 6, 1998. The definition of "specified party" in proposed Multi-Jurisdictional Instrument 33-105 *Underwriting Conflicts* identifies a number of situations that would indicate that the issuer has been, or may be, experiencing financial difficulty, including defaults in the payment of principal or interest due on loan obligations, certain downgradings of debt or preferred shares and bankruptcy or receivership.

- upon a proposed business combination becoming “probable” (applying concepts from NI 44-101), an SIF disclosing that fact and known material terms, conditions and contingencies and reasons for the proposal; and

- upon completion or abandonment of the proposed business combination:

    - an SIF disclosing that fact and, in the case of completion, material terms and conditions; and

    - a further SIF, to be filed within 75 days after completion of the business combination, containing financial and other disclosure concerning the business combination that conforms to short form prospectus disclosure requirements for significant business combinations under NI 44-101 (the corresponding news release need announce only the filing of the SIF with a brief description of its subject matter);

- in respect of a disposition of an asset or a business material to the issuer, two SIFs as follows:

    - upon the proposed disposition becoming "probable" (applying NI 44-101 concepts), the SIF to disclose that fact and known material terms, conditions and contingencies, proceeds to the issuer and reasons for the proposal; and

    - upon completion or abandonment of the proposed disposition, the SIF to disclose that fact and, in the case of completion, material terms and conditions and proceeds to the issuer and a narrative description of the anticipated effect on the issuer;

- the imposition on the issuer or, if known to the issuer, on a director, officer, promoter or significant shareholder of the issuer, of a penalty or sanction relating to Canadian securities legislation by a court or Canadian securities regulatory authority, or the execution by any of these parties, if known to the issuer, of a settlement agreement with a Canadian securities regulatory authority (whether or not the penalty or sanction is or may be the subject of an appeal); and

- the imposition on the issuer or, if known to the issuer, on a director, officer, promoter or significant shareholder of the issuer, of any other penalties or sanctions imposed by a court or regulatory body that would likely be considered important to a reasonable investor in making an investment decision.

To the extent that any of this disclosure is contained in another element of the issuer's IDS disclosure base or in an IDS prospectus that has not lapsed, the issuer would not be required to file an SIF.

Like existing material change reports, SIFs would be required to be filed within a specified period after the occurrence of the triggering event. An issuer could use the text of the corresponding news release as the basis of an SIF provided that (i) its content and quality satisfy the SIF requirements; (ii) it is accompanied by a cover page or introduction that identifies it as an SIF, and (iii) it is certified (see "Certification", below). A news release must be issued promptly after the triggering event, but the SIF filing period balances needs for quality and timeliness by allowing the issuer time to ensure that the SIF meets the higher prospectus-level quality of the IDS disclosure base. With the exception of the 75 day filing period for a post-acquisition SIF noted above, the filing period for an SIF would be ten days after the triggering event.

In a further effort to ensure that a full IDS disclosure base is in place to support an IDS offering, as discussed below in connection with IDS offering procedures, IDS offering procedures could not be used if an SIF-triggering event has occurred until the required SIF has been filed.

2. IDS Continuous Disclosure Enhancements

Securities regulation in Canada has, as noted above, focused primarily on offering disclosure rather than on continuous disclosure. The integration of primary and secondary market information would provide investors in both markets with the same high-quality information. The IDS disclosure documents described above are designed to ensure that significant elements of traditional prospectus disclosure are available earlier and continuously in the IDS disclosure base.

In the course of developing the IDS disclosure documents, the CSA have identified a number of changes in general disclosure content and timing necessary to ensure the desired quality of IDS disclosure and to address calls for general disclosure enhancements by, among others, the *Report of The Toronto Stock Exchange Committee on Corporate Governance in Canada*[7], the Wallman Report, Allen Report and the Aircraft Carrier Release. Some of the proposed disclosure enhancements bridge the gap between current continuous disclosure and prospectus disclosure standards, while others go beyond current disclosure standards.

A number of the proposed IDS continuous disclosure enhancements are consistent with existing requirements of certain CSA members. Further, concurrently with the publication of this Concept Proposal certain CSA members will be publishing for

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[7] December 1994; sometimes referred to as the "Dey Report" after the Committee Chair.

comment separate policy initiatives which will propose to implement many of these continuous disclosure enhancements regardless of whether an IDS is implemented.

(a) Annual Disclosure

(i) Financial Statements

Current requirements governing annual financial statements would be amended, in their application to the IDS, to require:

- filing within 90 days, rather than the current 140 days, after the issuer's financial year end;

- that financial statements prepared in accordance with foreign GAAP include in notes a reconciliation of the financial statement disclosure to Canadian GAAP and other disclosure consistent with Canadian GAAP;

- that, if financial statements are accompanied by a foreign auditor's report, the auditor's report be accompanied by a statement by the auditor (i) disclosing any material differences in the form and content of the foreign auditor's report, and (ii) confirming, in the case of foreign GAAS other than United States GAAS, that the auditing standards applied are substantially equivalent to Canadian GAAS;

- that financial statements prepared in accordance with foreign GAAP or accompanied by a foreign auditor's report be accompanied by a letter from the auditor that discusses the auditor's expertise (i) to audit the reconciliation of foreign GAAP to Canadian GAAP, and (ii) in the case of foreign GAAS other than United States GAAS, to make the determination that auditing standards applied are substantially equivalent to Canadian GAAS;

- review by the issuer's audit committee (if the issuer has or is required to have an audit committee) and approval by the issuer's board of directors or equivalent.

(ii) IDS AIF

Standards for annual disclosure would be upgraded, for purposes of the IDS, to render the IDS AIF more informative than the standard form of AIF currently in use. The standard of IDS AIF disclosure would be elevated to the full, true and plain disclosure standard required in a prospectus. The deadline for filing an IDS AIF would be 90 days after the issuer's year end, as compared to the current 140 day filing deadline for non-IDS AIFs.

IDS AIF content requirements would include:

- the content contemplated in NI 44-101 for a non-IDS AIF;
- MD&A that includes discussion of fourth-quarter financial results;
- disclosure of the issuer's corporate governance policies and practices as recommended in the Dey Report[8];
- disclosure, comparable to that mandated by the SEC[9], concerning the policies applied by the issuer to account for derivatives, including quantitative and qualitative disclosure and sensitivity analyses, and concerning material exposure to risks relating to market interest rates, foreign currency values, commodity prices, equity security prices and other market risks; and
- to the extent not already disclosed as a result of the above, all other disclosure required to meet current and proposed non-offering-specific content requirements for a long form prospectus, including full financial statements with comparatives, information concerning legal proceedings affecting the issuer, material contracts to which the issuer is a party, escrow affecting securities of the issuer, risk factors relating to the issuer and its business and not specific to a particular offering of securities, a statement of the issuer's consolidated capitalization and identification of the issuer's auditors and transfer agents.

(b) Quarterly Disclosure

The deadline for filing an IDS QIF would be 45 days after the relevant interim period, as compared to the current 60 day filing deadline for interim financial statements.

(i) Interim Financial Statements

Current requirements governing interim financial statements would be amended to require:

- inclusion of a balance sheet as of the last day of the interim financial period;

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[8] Op. cit., footnote 7.

[9] See the SEC's Securities Act Release No. 7386 (January 28, 1997) *Disclosure of Accounting Policies for Derivative Financial Instruments and Derivative Commodity Instruments and Disclosure of Quantitative and Qualitative Information about Market Risk Inherent in Derivative Financial Instruments, Other Financial Instruments, and Derivative Commodity Instruments*.

- inclusion of notes to the interim financial statements sufficient to ensure that the financial statement presentation is not misleading;

- for interim financial statements prepared in accordance with foreign GAAP, inclusion of a reconciliation to Canadian GAAP; and

- review by the issuer's audit committee (if the issuer has or is required to have an audit committee) and approval by the issuer's board of directors or equivalent.

(ii) Interim MD&A

Interim financial statements would be supplemented or accompanied by MD&A for the same interim financial period of the issuer.

(c) Certification

Fundamental to the IDS is the availability, to all investors (not only recipients of a prospectus), of the prospectus-quality IDS disclosure base. To ensure that the necessary standard of disclosure is met, the IDS would require that each IDS AIF, QIF and SIF be accompanied by certificates of senior management and directors of the issuer attesting that the document contains full, true and plain disclosure of the information presented or required to be presented in the document.

D. IDS Offerings

1. Principles

The enhancement of continuous disclosure under the IDS would give both primary market and secondary market investors access to comprehensive, timely and high-quality information concerning participating issuers. With this integrated disclosure base in place, the IDS would enable eligible issuers to offer securities in the primary market more quickly and with greater certainty than under existing offering procedures.

The securities offering procedures under the IDS would also reflect the following principles:

- A prospective investor should be provided with information, concerning both the issuer and a specific offering of securities, necessary to make an informed investment decision in advance of making (and being bound by) that decision.

- To the extent consistent with the other principles underlying the IDS and securities legislation generally:

    - issuers will be allowed wide flexibility in determining the form and content of information that they provide to prospective investors in connection with an offering of securities; and

    - regulatory procedures should facilitate efficiency and timeliness in IDS offerings of securities.

2. The IDS Prospectus

The comprehensive information about an issuer and its business contained in its IDS disclosure base would allow primary market offerings of securities under the IDS using an abbreviated offering document.

(a) IDS Prospectus Content

The IDS prospectus would be required to be certified by the issuer and underwriters and to contain full, true and plain disclosure of all material (or otherwise required) information relating to the issuer and the offering. The text of the IDS prospectus could be brief, largely focusing on disclosure concerning the offering and the offered securities, with prescribed content as follows:

- identification of the issuer;

- a detailed description of the securities offered;

- intended use of proceeds of the offering;

- plan of the distribution;

- market and trading history for the offered securities;

- earnings coverage;

- risk factors -- full disclosure of risk factors particular to the offered securities and a summary description of risk factors relating to the issuer and its business as set out in the issuer's IDS AIF;

- income tax considerations relevant to the offering;
- the relationship between the issuer and the underwriters of the offering; and
- investors' statutory rights of withdrawal, damages and rescission.

The IDS prospectus would also be required to incorporate by reference:

- the documents in the issuer's IDS disclosure base, except that, to the extent that more than one QIF has been filed since the last IDS AIF, only the most recently filed QIF need be incorporated by reference; and
- all written marketing communications (see "IDS Marketing Regime", below) pertaining to the offering or the securities offered under the IDS prospectus and disseminated by or on behalf of the issuer while the securities are in the course of distribution.

In addition, the IDS prospectus must guide readers to each document incorporated by reference, either by (i) explaining how they can obtain or retrieve electronically, without charge, a copy of the incorporated document, or (ii) attaching to the IDS prospectus a copy of the incorporated document.

Issuers would be free to include in an IDS prospectus, at their option, a full restatement or a summary of information incorporated by reference, provided that the presentation is fair and balanced and the reader is also directed to the source document.

An IDS prospectus would not be considered complete unless it identifies, and incorporates by reference, disclosure of each event that triggered an obligation on the part of the issuer to file an SIF if the event occurred subsequent to the date of the issuer's current IDS AIF or a more recent QIF, and prior to the date of the final IDS prospectus. See also the discussion below concerning IDS prospectus amendments.

(b) Preliminary and Final IDS Prospectuses

The objective of the CSA in developing securities offering procedures is to ensure that prospective investors have access to reliable and complete information before they make an investment decision. In common with existing statutory and alternative securities offering procedures, the IDS would require both a preliminary and a final form of IDS prospectus. The IDS, however, would place greater emphasis than current distribution systems on the *preliminary* version of the prospectus. The most important functions of

the final IDS prospectus would be to (i) update and complete[10] the disclosure in the preliminary IDS prospectus and (ii) serve as the basis of investors' statutory rights of withdrawal and rights of action for damages or rescission on grounds of misrepresentation.

The greater importance attached by the IDS to the preliminary IDS prospectus is primarily reflected in provisions relating to delivery, discussed below under the heading "IDS Prospectus Delivery". In general, the regulator would issue a receipt for a preliminary IDS prospectus on filing. Once receipted, the preliminary IDS prospectus would be delivered to prospective investors.

The CSA also considered the extent to which the preliminary and final IDS prospectuses should be distinguished by their content. Two approaches were considered.

The traditional form of a final prospectus, if applied to the IDS, would repeat most of the text of the preliminary IDS prospectus.

The CSA are not persuaded that the traditional approach to the form of a final prospectus is necessary under the IDS. Acknowledging incorporation by reference as an accepted principle of the IDS, and assuming early delivery of the preliminary IDS prospectus (with the content summarized above under the heading "IDS Prospectus Content"), the IDS contemplates a very streamlined final IDS prospectus that would serve largely as an information checklist.

The final IDS prospectus would (i) identify the issuer, (ii) identify and incorporate by reference each document in the issuer's IDS disclosure base and the preliminary IDS prospectus, and (iii) include prospectus certificates. The issuer would not be required to restate in the final IDS prospectus any of the incorporated disclosure with the exception of statements of investors' statutory rights and directions for obtaining copies of the incorporated disclosure. An IDS issuer could, however, at its option adopt a more traditional form of final IDS prospectus.

The final IDS prospectus would set out in full any material information (for example, pricing) concerning the offered securities that was not disclosed in the preliminary IDS prospectus, and it would not only incorporate by reference but also summarize (or, at the issuer's option, repeat or attach) any SIF filed after the date of the preliminary IDS prospectus.

The abbreviated text of the checklist form of IDS prospectus would not diminish the issuer's responsibility for ensuring that the document, together with all incorporated

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[10] Some offering information -- pricing, for example -- may be provided only in the final prospectus because it is not known to the issuer until after the preliminary prospectus has been filed.

documents, provides full, true and plain disclosure of all required information, nor would it alter the role of the documents as the basis of investors' statutory rights concerning misrepresentations and withdrawal.

The CSA consider that the brevity of the final IDS prospectus would be advantageous to investors. The convenient list of incorporated disclosure documents would give readers a second opportunity to consider and, if desired, consult incorporated documents (including the preliminary IDS prospectus) of interest to them before they finalize their investment decision. New information, which should be the focus of attention for investors who had already given careful consideration to the preliminary IDS prospectus, would stand out more prominently in the shorter document than in a restated version of the preliminary IDS prospectus, as might the statements of investors' statutory rights.

The checklist approach to the final IDS prospectus could be seen as a culmination of the concept of incorporation by reference and an embodiment of IDS principles of streamlined documents and procedures centring on the IDS disclosure base.

3. IDS Prospectus Amendment

Amendment of an IDS prospectus would be governed by current provisions of securities legislation. An IDS prospectus must provide full, true and plain disclosure, verbatim or through incorporation by reference and summary, of all required information relating to the issuer and the offering, and contain certificates to that effect. Any amendment to an IDS prospectus would similarly be required to contain (i) full, true and plain disclosure and (ii) prospectus certificates, and to be clearly identified as an amendment to a specific IDS prospectus.

As under existing offering procedures, an IDS prospectus could be amended either by a full restatement of the IDS prospectus being amended or by a briefer document limited to additional or substituted information. Under the IDS, an issuer choosing the latter alternative could make use of an SIF modified for this purpose by the addition of (i) an introduction or a cover page identifying it as an IDS prospectus amendment and (ii) prospectus certificates.

A discussion of differing procedures applicable to amendments to preliminary and final IDS prospectuses follows.

(a) Amendment of a Preliminary IDS Prospectus

Securities legislation requires the amendment of a preliminary prospectus, and delivery of the amendment to each recipient of the preliminary prospectus, in the event that an adverse material change occurs between the issuance of receipts for the preliminary and

final prospectus. In most jurisdictions, the adverse material change would also trigger separate material change reporting requirements.

Similar requirements would apply under the IDS. Whether or not a preliminary IDS prospectus has been filed, an adverse material change would trigger the obligation to file an SIF. That SIF could, at the issuer's option, also be used to amend a preliminary IDS prospectus, provided that when used for that purpose it is clearly identified as an amendment and bears prospectus certificates. An issuer that does not wish to modify an SIF for this purpose would be able, as at present, to amend a preliminary IDS prospectus using either a fully restated preliminary IDS prospectus or a briefer amending supplement, in either case identified as an amendment and bearing prospectus certificates.

An event other than an adverse material change would not require amendment of an outstanding preliminary IDS prospectus, although the issuer would be free at its option to file and deliver an amendment in any of the three alternative forms described immediately above. If the issuer filed an SIF in respect of the event but no amendment of the preliminary IDS prospectus was required, that SIF would be incorporated by reference and summarized in (or repeated in or attached to) the final IDS prospectus.

(b) Amendment of a Final IDS Prospectus

If an SIF-triggering event occurs after the date of a final IDS prospectus receipt and before completion of the IDS offering or the lapse of the final IDS prospectus, a prospectus amendment would be required. Amendment in other circumstances would not be required but would be permitted at the issuer's option.

Delivery of the amendment would complete delivery of the final IDS prospectus. As at present, an investor's statutory right of withdrawal would run from receipt of the amendment, thus ensuring that investors have an opportunity to assess the effect of the information disclosed in the amendment before being bound by their investment decision.

An amendment to a final IDS prospectus must (i) be clearly identified as an amendment to the specific final IDS prospectus, (ii) restate investors' statutory rights, making clear that delivery of the amendment begins a new period in which the right of withdrawal can be exercised, and (iii) include prospectus certificates. As in the case of amendments to a preliminary IDS prospectus, the amendment could take the form of a modified version of the relevant SIF, a distinct supplement to the final IDS prospectus being amended or a full restatement of the final IDS prospectus being amended.

Current securities legislation would apply to require delivery of the amendment to each purchaser of a security under the distribution whose statutory right of withdrawal had not expired before the occurrence of the event (if any) that prompted the amendment. As at

present, issuers might choose to deliver the amendment to other purchasers, the consequence in all cases being the recommencement of the statutory withdrawal period.

4. IDS Prospectus Delivery

(a) Delivery of the Preliminary IDS Prospectus

As noted above, a key objective of the CSA in developing the IDS is to provide prospective investors with comprehensive information before they make an investment decision.

The CSA are of the view that traditional securities regulatory practice overemphasizes the value of the final prospectus in the investor's decision-making process. The problem is one of timing, as aptly described in the Aircraft Carrier Release:

> "In firm commitment underwritten offerings, the final prospectus invariably arrives after the investor has made its investment decision. While delivery of final prospectuses . . . may be useful to investors who are considering litigation or resale, it does little to fulfill the prophylactic goals of the Securities Act.
>
> The cost of delivery of a final prospectus, where it is otherwise readily available to the public, may exceed any marginal benefit to investors. To provide investors with the maximum benefit from the prospectus, our proposals would re-focus prospectus delivery requirements on a point in time before investors have made their investment decisions."[11]

The IDS would place greater emphasis on the preliminary IDS prospectus. An agreement to purchase a security in an IDS offering would not be enforceable against the purchaser unless the purchaser had first received a copy of the preliminary IDS prospectus and any amendment. A prominent statement to this effect would be required in both the preliminary and final IDS prospectus, in any IDS subscription agreement and in any confirmation of purchase.

The CSA considered whether the IDS should specify the timing of delivery of the preliminary IDS prospectus, to ensure that a prescribed minimum period of time is available to an investor before an investment decision becomes binding. This approach was rejected as both impractical and unnecessary. Identifying the moment in time at which an offering has commenced, is about to commence or has, after commencement, reached a particular stage, and identifying the time at which an investment decision is made, all involve complex and case-specific considerations. Specific timing

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[11] Op. cit., pages 174-5.

requirements would almost certainly give rise to difficult issues of interpretation and diminish the predictability of the IDS procedures.

Determining an appropriate period for the investment decision process is, moreover, problematic. The CSA seek to ensure that appropriate information is available to investors, not to direct investors in the use of that information. Each offering and each investment decision involves different considerations and information requirements. No prescribed preliminary IDS prospectus delivery period would be likely to suit all investors and all situations.

The CSA are of the view that the existing framework of securities legislation, that mandates use of both a preliminary and a final version of a prospectus, and provides investors with a statutory right to withdraw from a primary market purchase of securities within two business days after receiving a final prospectus, will ensure that investors have a period of time after receiving an IDS prospectus in which to consider their investment decision. The IDS would build on these minimum requirements with the contractual condition requiring delivery of the preliminary IDS prospectus, which the CSA are confident would result in earlier and more widespread delivery of this important document than prevails under existing distribution systems. Finally, the IDS focus on the IDS disclosure base would give prospective investors access to comprehensive, high-quality information about IDS issuers well in advance of any investment decision.

(b) Delivery of the Final IDS Prospectus

Securities legislation requires an issuer to file, and deliver to the investor, the final prospectus. As noted above, investors' statutory withdrawal rights run from final prospectus delivery.

For many offerings of securities, where all material terms of the offering and the securities offered were known early in the offering process and disclosed in the preliminary IDS prospectus, and where no SIF reporting requirement was triggered during the course of the offering, the final IDS prospectus could be a very brief document that reminds investors of the identity and business of the issuer, sets out key terms of the offering, directs the investor to the issuer-centred and offering-centred information previously disclosed and incorporated by reference, advises investors of their statutory rights and bears the required certificates.

The IDS would require delivery of the final IDS prospectus to the investor not later than delivery of the confirmation of purchase. The final IDS prospectus could accompany the confirmation of purchase. In any case, the period in which an investor could exercise the statutory right of withdrawal would commence with delivery of the final IDS prospectus.

5. Role of the Underwriter and Other Advisors

Underwriters would retain an important role under the IDS, notwithstanding the accelerated IDS offering procedures.

Due diligence by underwriters provides an extra level of review that can enhance the quality and reliability of the issuer's disclosure. The IDS's shift in emphasis from the prospectus to the underlying continuous disclosure base would not diminish the benefit, to investors, of underwriter due diligence. Acceleration of the offering process, which to some extent is already evident under the short form prospectus and shelf distribution systems, should not preclude an underwriter from serving this useful investor protection function.

For these reasons, the IDS retains the existing requirement for underwriter certification of the IDS prospectus. The CSA are hopeful that the faster offering process made possible by the IDS would lead underwriters, as well as auditors and lawyers and other advisors, to increase their involvement in issuers' continuous disclosure in order to satisfy themselves as to the quality of the disclosure relied on by prospective investors.

6. Marketing Practices

(a) Existing Marketing Restrictions

Securities legislation currently:

- prohibits any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of a distribution of securities unless a preliminary prospectus and a (final) prospectus for the securities have been filed and receipted; and

- limits other marketing or promotional activities after the issuance of a final prospectus receipt.

These existing marketing restrictions were designed to prevent issuers from conditioning the market or stimulating interest in a proposed offering of securities before a prospectus is available, and to discourage high pressure securities sales practices.

(b) IDS Marketing Regime

(i) Objectives

To a large extent the existing marketing restrictions are a consequence of the traditional regulatory focus. With the prospectus as the basic source of information, the regulatory obligation to protect investors dictated measures to insulate them from marketing efforts not accompanied or preceded by at least a preliminary prospectus.

The IDS, with its emphasis on ensuring that securities markets are continuously informed by timely, prospectus-quality continuous disclosure whether or not an offering of securities is pending, would alleviate many of the concerns underlying the existing marketing restrictions. The CSA are of the view that marketing restrictions more clearly directed at deterring the dissemination of misleading information would be more beneficial to investors.

Accordingly, the CSA have developed new marketing restrictions and requirements, more consistent with the principles underlying the IDS. The proposed restrictions represent a move away from traditional efforts at limiting investor contact with securities-related information prior to or during the course of an offering, in favour of more issuer responsibility for marketing information coupled with deterrents to misleading and improper securities marketing and promotional tactics.

The CSA are of the view that the proposed marketing restrictions, together with IDS disclosure enhancements, would amply address investor protection needs. Accordingly, an offering of securities conducted by an eligible issuer using the IDS offering procedures would be subject to the *new* IDS marketing restrictions and requirements but would be exempt from the *existing* marketing restrictions.

(ii) IDS Marketing Restrictions

For the purposes of the IDS marketing restrictions, the term "marketing communication" refers to any oral or written communication disseminated by or on behalf of an issuer to promote (or that can reasonably be considered to have been intended to promote) a purchase or sale of a security of the issuer or of an affiliate of the issuer. Marketing communications would not ordinarily include either (i) business communications disseminated by an issuer in the ordinary course of its business to promote the sale of a product or service (other than a security) or to enhance the reputation or public awareness of the issuer, or (ii) a document available to investors only by virtue of having been filed with a public agency pursuant to a requirement unrelated to securities laws. A research report or media interview discussing an issuer's securities would not generally constitute a marketing communication unless it is disseminated by or on behalf of the issuer.

An IDS issuer, and any person or company with actual, implied or apparent authority to act on behalf of the issuer, would be prohibited from disseminating, directly or indirectly, a marketing communication that:

- contains an untrue or misleading statement;
- discloses a material fact that has not previously been disclosed in the issuer's IDS disclosure base;
- is inconsistent with information in the issuer's IDS disclosure base;
- distorts, by selective presentation or otherwise, information contained in the issuer's IDS disclosure base;
- includes a forecast, projection or other forward-looking information not contained in the issuer's IDS disclosure base[12];
- could reasonably be regarded as sensational or that forms part of conduct that could reasonably be regarded as high pressure[13]; or
- does not contain a prominent legend advising investors to read, before making an investment decision, the issuer's IDS disclosure base and the relevant IDS prospectus (if filed and not lapsed), and advising investors as to how they can view and obtain copies of such disclosure without charge.

The IDS would also incorporate (where not already provided in securities legislation) a prohibition of any statement made with a view to effecting a trade in a security if the maker of the statement knows, or ought reasonably to know, that the statement contains a misrepresentation. This prohibition is derived from existing paragraph 50(1)(d) of the *Securities Act* (British Columbia) and would enhance the ability of regulators to halt or sanction misleading communications that jeopardizes the investing public.

(iii) Incorporation by Reference

An IDS prospectus would be required to identify and incorporate by reference all written marketing communications that pertains to the offering or the securities offered under the IDS prospectus and that is disseminated by or on behalf of the issuer while the securities are in the course of distribution. Documents incorporated by reference in a prospectus must be filed and be available to investors.

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12 Forecasts and projections in the IDS disclosure base would, of course, be subject to the requirements of proposed National Instrument 52-101 *Future Oriented Financial Information*.

13 A companion policy to be adopted in connection with implementation of the IDS can be expected to provide guidance on the meaning and interpretation of these terms.

This requirement would allow IDS issuers flexibility in the design and use of securities marketing material while ensuring that:

- all investors have access to the same information; and
- the information in the marketing material is of sufficient quality that the issuer and others will certify and bear responsibility for it as part of the IDS prospectus.

(iv) Intended Effect of IDS Marketing Regime

The exemption of IDS issuers from existing marketing restrictions and the substitution of the new IDS marketing prohibitions, coupled with incorporation by reference of written marketing communications in the IDS prospectus, are intended to offer IDS issuers much greater flexibility in obtaining new financing than is currently available. An IDS issuer could "test the waters" and solicit expressions of interest in a contemplated offering without fear of inadvertently contravening existing marketing restrictions and without incurring significant expense in commencing prospectus preparation. The issuer would also have wide discretion in tailoring marketing material for prospective investors, provided that investors are not misled and the issuer assumes responsibility for its marketing communications.

This flexibility can be offered to issuers without jeopardizing investor protection because the issuer's activities would take place against the backdrop of its comprehensive IDS disclosure base.

E. Electronic Delivery

To facilitate efficient and reliable dissemination of information, the IDS would permit the delivery of all IDS disclosure documents by electronic as well as traditional paper means, in accordance with the principles set out in National Policy 11-201 *Delivery of Documents by Electronic Means*[14].

F. Regulatory Review of IDS Disclosure

The IDS would shift much of the regulatory focus from the prospectus to continuous disclosure and so facilitate a streamlined regulatory role in the IDS offering process.

A well-developed and appropriately staffed system of continuous disclosure review is necessary to ensure that enhanced disclosure standards are met. CSA members are devoting increased staff resources to monitoring and reviewing continuous disclosure filings. This trend would intensify with implementation of the IDS. At the same time, the CSA are developing procedures for more effective and efficient disclosure review,

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[14] Published in the week ended December 17, 1999.

through selective and targeted review, coordinated among jurisdictions. Increased resources are also being devoted to enforcement measures.

With these measures in place to supplement the IDS requirements, a high-quality information base would underlie an IDS offering. The IDS prospectus itself, incorporating by reference the issuer's IDS disclosure base, can be a very simple document. Disclosure pertaining to the issuer would already be contained in the issuer's IDS disclosure base, which would have been subject to a system of periodic, selective or targeted regulatory review. Together, these factors would permit an effective yet very efficient regulatory role in an IDS offering. In addition, the filing and review procedures under the MRRS Policy would be available for multi-jurisdiction IDS offerings.

Filed IDS prospectuses would undergo regulatory screening but not, generally, detailed review. IDS prospectus screening would serve primarily to give regulators an opportunity to assess whether:

- there is a basis for believing that the issuer is ineligible to use the IDS;
- the offering presents issues that could prompt the regulator to conduct a detailed review; or
- the regulator is obliged under existing statutory provisions to decline to issue a prospectus receipt.

This screening process could also bring to light matters that would be brought to the attention of regulatory staff responsible for continuous disclosure review, who might intensify or revisit their review of the issuer's IDS disclosure base.

The CSA anticipate few instances of delay or refusal in the receipting of IDS prospectuses, and no unacceptable degree of uncertainty in the IDS offering process attributable to IDS prospectus screening. IDS eligibility would be within the knowledge of the issuer, and issues that could prompt a full prospectus review or denial of a receipt (under provisions that already apply to prospectuses filings) would generally be of a nature and magnitude known to the issuer. Finally, IDS issuers would retain their rights under securities legislation to be heard and, if dissatisfied with a resulting decision, to appeal.

G. Implementing the IDS

The IDS is expected to be capable of implementation by regulators in most jurisdictions without statutory amendment.

The CSA intend to develop a national instrument, taking into account comment on this Concept Proposal, that would implement the IDS. In accordance with past practice, the national instrument would itself be published and subject to revision in light of public comment, following which it could be adopted as a rule, regulation or policy in each CSA jurisdiction.

As noted in the Introduction, the CSA propose to implement the IDS on a pilot basis. During a pilot period of at least two years, regulators, issuers and investors will be able to assess the merits of the IDS. The CSA will consider modifications to the IDS to address problems or deficiencies that come to light during the pilot period.

The IDS would coexist during the pilot period with alternative offering procedures such as the short form prospectus and shelf distribution procedures. Qualifying issuers would be able to participate in the IDS and offer securities using IDS procedures, or use any existing prospectus exemption or alternative offering procedure (subject to applicable restrictions, including current marketing restrictions) for which they are eligible. The CSA are hopeful that many issuers will opt to use the IDS during the pilot period.

The CSA will consider eliminating use of the short form prospectus and shelf distribution procedures for IDS-eligible issuers in the event that experience with the IDS during its pilot introduction demonstrates that it is an adequate substitute for these regimes.

PART IV. CHANGES OUTSIDE THE IDS

In developing the proposed IDS, the CSA have undertaken a fundamental review and reassessment of securities regulatory objectives, principles and practices and the requirements of securities legislation.

Many issues addressed in the IDS are relevant to issuers and investors in general. In the view of the CSA, elements of the IDS could, if applied generally, enhance investor protection and the efficiency of capital markets. Unless and until the disclosure enhancements and marketing restrictions described below are extended to issuers generally, IDS participants would have to meet higher standards than non-IDS participants, an inconsistency that could serve as a significant disincentive to issuer participation in the IDS.

A. Non-IDS Disclosure Enhancements

The CSA are considering extending to all issuers many of the continuous disclosure enhancements incorporated in the proposed IDS as described in Part III under the heading "IDS Continuous Disclosure Enhancements". A number of the continuous disclosure

enhancements proposed in the IDS are consistent with existing requirements of certain CSA members. In addition, certain CSA members will soon publish for comment separate instruments which propose to adopt many of these changes regardless of whether an IDS is implemented.

Disclosure enhancements currently under consideration for general application include:

- applying to non-IDS material change reporting the triggers and the content and quality requirements applicable to SIFs under the IDS (as well as the extended 75 day period for the filing of a report containing financial information for a completed significant acquisition);

- shortening the period for the filing of annual and interim financial statements to 90 and 45 days, respectively, after the end of the reporting period;

- requiring the reconciliation to Canadian GAAP of annual and interim financial statements prepared in accordance with foreign GAAP;

- requiring that, if financial statements are accompanied by a foreign auditor's report, the auditor's report be accompanied by a statement by the auditor (i) disclosing any material differences in the form and content of the foreign auditor's report, and (ii) confirming, in the case of foreign GAAS other than United States GAAS, that the auditing standards applied are substantially equivalent to Canadian GAAS;

- requiring that financial statements prepared in accordance with foreign GAAP or accompanied by a foreign auditor's report be accompanied by a letter from the auditor that discusses the auditor's expertise (i) to audit the reconciliation of foreign GAAP to Canadian GAAP, and (ii) in the case of foreign GAAS other than United States GAAS, to make the determination that auditing standards applied are substantially equivalent to Canadian GAAS;

- requiring audit committee review of annual and interim financial statements (for issuers that have or are required to have an audit committee) and directors' approval of annual and interim financial statements;

- requiring a discussion of fourth quarter results in annual MD&A;

- requiring annual disclosure of the issuer's corporate governance policies and practices;

- requiring annual disclosure, comparable to that mandated by the SEC, of market risks and of the policies applied by the issuer to account for derivatives;

- requiring quarterly filings of:

    - interim financial statements that include (i) a balance sheet, and (ii) notes sufficient to ensure that the financial statement presentation is not misleading; and

    - MD&A;

- requiring that each material change report, quarterly filing and AIF be accompanied by certificates of senior management and directors of the issuer attesting that the document contains full, true and plain disclosure of the information presented or required to be presented in the document, the certificate serving both to encourage a prospectus standard of disclosure and to make clear the signatories' direct responsibility for the integrity of the disclosure.

B. Marketing Activities

CSA members are considering a general prohibition of misleading statements comparable to existing paragraph 50(1)(d) of the *Securities Act* (British Columbia) discussed in Part III in connection with the IDS under the heading "IDS Marketing Restrictions":

> "A person [or company], ... with the intention of effecting a trade in a security, must not ... make a statement that the person [or company] knows, or ought reasonable to know, is a misrepresentation".

As noted above in connection with a similar proposal under the IDS, this provision (contravention of which would constitute an offence) would enhance the ability of regulators to halt or sanction communications that can mislead the investing public.

The CSA are also considering supplementing existing marketing restrictions applicable to non-IDS offerings by new marketing restrictions parallel to the IDS marketing restrictions.

PART V. OTHER CSA INITIATIVES

Development of the IDS has not occurred in isolation. It represents one element of an array of initiatives undertaken by the CSA to protect investors and foster confidence in capital markets by providing effective and efficient securities regulation in a rapidly evolving environment.

Other CSA initiatives also respond to what CSA members consider an unwarranted disequilibrium in the regulation of the primary and secondary markets. Enhanced "public enforcement" -- regulatory review and enforcement -- of continuous disclosure requirements has begun and will continue. As noted in Part III, the CSA are also developing a system for the coordinated review of continuous disclosure.

CSA members have also developed and published, on May 29, 1998, a *Proposal for a Statutory Civil Remedy for Investors in the Secondary Market* that would extend to secondary market investors a statutory civil right of action, comparable to that already in place for prospectus investors, in respect of losses attributable to misrepresentation in continuous disclosure. CSA staff are currently analyzing extensive public comment received on this proposal. The CSA believe that the proposed civil remedy and the IDS would complement one another, but at this time the implementation of neither proposal is contingent on implementation of the other.

PART VI. REQUEST FOR COMMENT

The CSA have developed the IDS to refocus securities regulation in Canada in a manner that more effectively and efficiently satisfies the dual regulatory objectives of protecting investors and fostering sound capital markets. Specific objectives of the CSA were to develop a system that offers streamlined and flexible access to markets, enhances the quality, timeliness and accessibility of corporate disclosure, and aligns regulatory effort with market needs.

The CSA believe that the IDS described in this Concept Proposal reflects an optimal balance of protection for investors and flexibility, predictability for issuers that would go far to achieving these objectives.

The CSA invite comment on the all aspects of the proposed IDS, and on the possible extension, to all issuers and offerings, of the disclosure enhancements and marketing restrictions discussed in Part IV. Details concerning the submission of comments will be found in Notices published by CSA member jurisdictions and may also be obtained by contacting your securities regulatory authority.