

NOVEMBER 2008

CONTINUOUS DISCLOSURE REVIEW PROGRAM:

**KEEPING THE MARKET WELL-INFORMED
IS A PRIORITY**



**AUTORITÉ
DES MARCHÉS
FINANCIERS**

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TABLE OF CONTENTS

Message from the Superintendent, Securities Markets	5
1) Introduction.....	6
2) Highlights	7
3) Results of Reviews.....	10
Companies	10
A. Financial Statements	10
Financial Instruments.....	10
Stock-Based Compensation	12
Miscellaneous GAAP Table	13
B. MD&A.....	14
C. Corporate Governance and Audit Committee	16
Compliance with Regulation 58-101	16
Compliance with Regulation 52-110	17
D. Other Matters.....	18
ABCP.....	18
Disclosure for Mineral Projects.....	19
Investment Funds	21
A. Financial Statements	21
Financial Disclosure Requirements.....	21
Notes to Financial Statements.....	22
Auditor's Report	22
B. Annual and Interim Management Reports of Fund Performance.....	23
Summary of Results of Operations.....	23
Financial Highlights.....	24
Summary of Investment Portfolio.....	24
C. ABCP.....	25
D. Compliance Reports.....	26
E. Required Warnings in Sales Communications	26
F. Other Deficiencies.....	26
4) Regulatory and Accounting Prospects	28
Regulatory Developments	28
A. Forward-Looking Information	28
B. Form 51-102F6, Statement of Executive Compensation	29
C. Regulation 52-109	29
D. Regulation 81-106.....	30
Accounting Developments.....	31
A. General Standards of Financial Statement Presentation – Going Concern.....	31
B. Inventories.....	31
C. Financial Instruments – Required Disclosure.....	31
D. International Financial Reporting Standards (IFRS)	31
5) Conclusion	34
Appendix A – Regulations and Other Texts.....	36
Appendix B – Forward-Looking Information.....	37

MESSAGE FROM THE SUPERINTENDENT, SECURITIES MARKETS

Part of the mission of the *Autorité des marchés financiers* (the “AMF”) is to monitor the securities market. The continuous disclosure review program (the “CDR Program”) was therefore established for the purpose of raising awareness among reporting issuers about the importance of continuous disclosure that is complete, complies with regulations and is delivered to investors on a timely basis.

The two fundamental objectives of the CDR Program are to foster awareness and ensure compliance. The first objective consists of helping reporting issuers better understand the nature and scope of their disclosure obligations as set forth in the Act and the regulations. The second objective consists of determining whether reporting issuers are complying with these obligations.

The reviews conducted under the CDR Program focus on an analysis of documents that are essential for investment decisions and include:

- financial statements,
- Management’s Discussion & Analysis (MD&A) or, in the case of an investment fund, management reports of fund performance,
- annual information forms,
- information circulars,
- press releases, and
- technical reports.

In this way, the CDR Program seeks to improve the quality of information available to investors and thereby bolster their confidence. Such confidence is essential for the effective operation of markets, which is at the very heart of a dynamic economy in Québec. As far as the AMF is concerned, financial sector participants must operate with the highest standards of ethical conduct, transparency and credibility.

We hope that the 2007-2008 edition of our Activity Report will help meet these standards. In addition to highlights and the results of our reviews, it sets out improvement recommendations for any agent tasked with releasing documents intended for investors.



Louis Morisset
Superintendent, Securities Markets

1

INTRODUCTION

This report presents the findings of the CDR Program¹ regarding the quality of continuous disclosure made by companies and investment funds² whose head office is in Québec.³ The first two sections set out the highlights and results of reviews carried out during the period from April 1, 2007 to March 31, 2008 and, for the first time, include the findings of reviews carried out on investment funds. They are followed by a discussion of regulatory and accounting prospects and developments.

The persons primarily responsible for communicating information to the market – senior executives, investment fund managers, directors and their advisers – can draw upon the recommendations in this AMF report when preparing continuous disclosure documents. However, under no circumstances should these recommendations be considered to be an exhaustive list as regards compliance with the Act or the regulations.⁴

- 1 Additional information on the CDR Program is available on our website at www.lautorite.qc.ca.
- 2 In this report, “companies” means those issuers contemplated in *Regulation 51-102 respecting Continuous Disclosure Obligations* and “investment funds” means those issuers contemplated in *Regulation 81-106 respecting Investment Fund Continuous Disclosure*.
- 3 The AMF follows the harmonized continuous disclosure review program of the Canadian Securities Administrators (the “CSA”). *CSA Staff Notice 51-312* provides additional information on the principal regulator in charge of continuous disclosure.
- 4 In this report, “the Act and the regulations” means the *Securities Act*, R.S.Q., c. V-1.1, as well as the regulations and other texts setting out continuous disclosure requirements. A list of the principal regulations and other texts is provided in Appendix A.

2 HIGHLIGHTS

From among the companies and investment funds covered by the CDR Program, 115 were reviewed during the 2007-2008 reporting period. This period was exceptionally marked by a liquidity crisis in the Canadian market for asset-backed commercial paper (“ABCP”) amid concerns about underlying assets linked to subprime mortgage loans in the United States. In response to the crisis, the AMF, together with the other CSA members, took immediate measures, including:

- conducting reviews of the continuous disclosures filed by companies holding substantial amounts of non-bank-sponsored ABCP;
- conducting reviews of continuous disclosure documents and simplified prospectuses of certain mutual funds holding ABCP;
- taking part in various international initiatives, in particular working committees of the International Organization of Securities Commissions with respect to rating agencies and the subprime mortgage crisis;
- monitoring developments in the reorganization of the frozen non-bank-sponsored ABCP market.

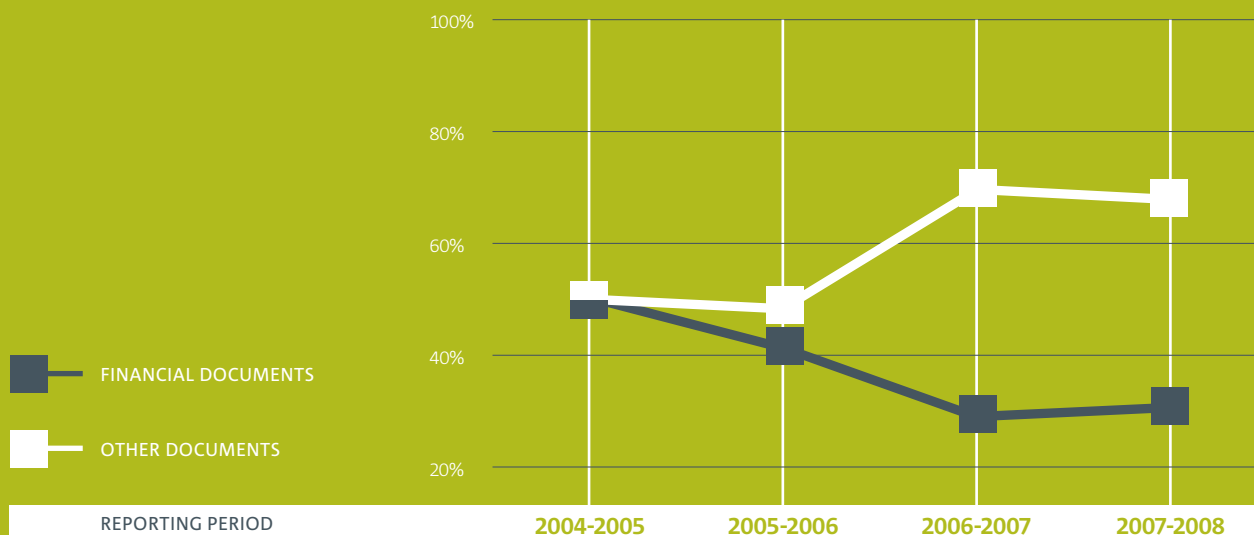
Moreover, following the reviews conducted under the CDR Program, several requests for changes were made.

The vast majority of requests for changes made to companies and investment funds pertained to the following:

- the financial statements of companies, as regards compliance with generally accepted accounting principles (“GAAP”);
- the MD&As, as regards compliance with *Form 51-102F1, Management’s Discussion & Analysis, of Regulation 51-102 respecting Continuous Disclosure Obligations* (“Form 51-102F1”);
- the annual information form or the information circular (the “circular”), as regards disclosure about corporate governance practices and the audit committee required, respectively, by *Regulation 58-101 respecting Disclosure of Corporate Governance Practices* (“Regulation 58-101”) and *Regulation 52-110 respecting Audit Committees* (“Regulation 52-110”);
- the financial statements of investment funds, as regards compliance with Parts 2 and 3 of *Regulation 81-106 respecting Investment Fund Continuous Disclosure* (“Regulation 81-106”); and
- the annual and interim management reports of fund performance, as regards compliance with *Form 81-106F1, Contents of Annual and Interim Management Report of Fund Performance* (“Form 81-106F1”).

A considerable percentage of our requests for changes still relates to regulations whose implementation dates back to 2006 for a large number of companies and investment funds. The AMF has made a sustained effort to foster awareness among companies and investment funds and expects the obligations imposed by the Act and the regulations to be understood and applied rigorously. The following graph shows the progression in the breakdown of requests for changes as related to financial statements and other continuous disclosure documents.

PROGRESSION IN THE BREAKDOWN OF REQUESTS FOR CHANGES



We remind companies and investment funds that the AMF can take the necessary measures to ensure compliance with the Act and the regulations, such as requiring amendments to previously filed documents or the filing of missing documents, or indicating defaults on the list of reporting issuers posted on the AMF website.⁵ For example, companies and investment funds are considered to be in default if they have failed to file a continuous disclosure document required under the Act or if they have provided information in a continuous disclosure document that does not comply with the terms and conditions determined by regulation or contains significant deficiencies.

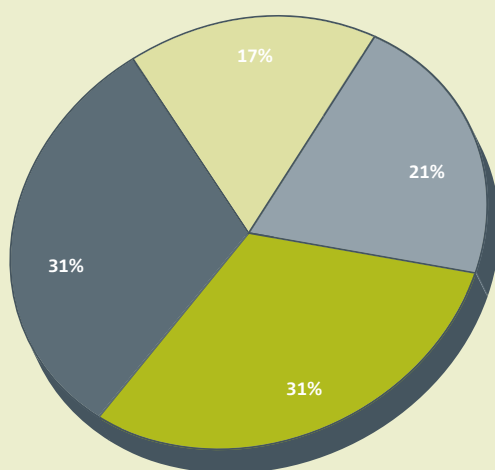
5 In this regard, see *Notice on Reporting Issuer Defaults* published by the AMF in December 2006.

3

RESULTS OF REVIEWS

COMPANIES

In this section, we discuss the deficiencies most often noted in the company records analyzed during the reporting period. They are grouped under four themes and include our observations based on ABCP-focused reviews. We also indicate the relative percentage of requests for changes related to each theme.



- A** Financial statements (31%)
- B** MD&A – Form 51-102F1 (31%)
- C** Governance and audit committee – Regulation 58-101 and Regulation 52-110 (17%)
- D** Other subjects (21%)

A FINANCIAL STATEMENTS

Financial Instruments

For several companies reviewed during the reporting period, this was the first time they were applying the new requirements set out in the *CICA Handbook* regarding financial instruments. Although, in general, these new requirements were adequately applied, we nevertheless noted certain deficiencies.

Some companies did not amend their accounting policies during the initial interim periods following the effective date of the new provisions. Others failed to determine the category into which each of the financial instruments was to be classified or did not properly classify instruments. Given that classification determines the basis for the measurement of financial instruments and impacts the presentation of gains and losses, it is essential to classify instruments properly.

We also noted deficiencies in the information provided. Disclosure regarding the following significant terms and conditions attached in particular to derivative financial instruments was omitted:

- the notional principal amount;
- the exchange rate provided for in contracts; and
- the contractual price of commodities.

Finally, disclosure required by the *CICA Handbook* in two types of circumstances was omitted:

- when the financial statements included financial instruments measured at fair value, using a measurement technique based on assumptions not supported by market prices or rates; and
- when the financial statements included financial assets or liabilities classified by the company for trading purposes.

Changes were therefore requested, because it is important for companies to provide complete disclosure that complies with the provisions of the *CICA Handbook*.

We would also like to point out that Form 51-102F1 respecting the MD&A requires companies to discuss the nature and extent of their use of financial instruments. Companies must describe the business purposes these instruments serve as well as the risks associated with such instruments. Disclosure in the MD&As regarding financial instruments must be improved so that the market can better understand the underlying risks associated with using them.

Stock-Based Compensation

Again this year, we noted several deficiencies regarding the application of the provisions of Section 3870 of the *CICA Handbook* respecting stock-based compensation and other stock-based payments.

The major deficiencies, which we consider to be unacceptable, pertain to the following:

- inadequate attribution of the compensation expense over the vesting period of the options; and
- failure to use a pricing model to determine the fair value of the options awarded.

Moreover, we noted several omissions as regards disclosure required by the *CICA Handbook*, in particular, the failure to specify the following:

- the conditions for the vesting of rights;
- the maximum term of options; and
- the weighted average of grant-date fair value of options.

Most of the companies that granted options with exercise prices that differed from the market price of stock on the grant date failed to disclose this in their financial statements. In this regard, we referred them to Section 3870.68 of the *CICA Handbook*.

We believe that companies must apply this section of the *CICA Handbook* more thoroughly. Some companies must ensure that they properly recognize the cost of their stock-based compensation; others must ensure that they present all of the information required.

Miscellaneous GAAP Table

In addition to the items outlined above, other deficiencies are routinely noted. A non-exhaustive list of such deficiencies is given in the accompanying table. The requirements in the *CICA Handbook* relating to these matters are clear and unambiguous. Companies must avoid these recurring deficiencies. Moreover, although our reviews often highlight the latest accounting developments, they also deal with the proper application of the entire body of GAAP.

Section in <i>CICA Handbook</i>	Description of deficiencies
1400 – General Standards of Financial Statement Presentation	■ Inconsistencies between disclosure in the financial statements and the notes ■ Use of improper terminology
1540 – Cash Flow Statements	■ Offsetting of certain transactions ■ Recognition of non-monetary transactions
1701 – Segment Disclosures	■ Incomplete information regarding profit or loss, and regarding assets ■ Failure to indicate the revenue allocation method ■ Aggregation or omission of information about major customers
1751 – Interim Financial Statements	■ Failure to provide an explanation of the seasonal or cyclical nature of operations ■ Failure to describe newly adopted accounting policies
3840 – Related Party Transactions	■ Incomplete disclosure of related party transactions ■ Failure to present the basis for measurement and classification in the financial statements

B MD&A

Nearly one third of our requests for changes related to the MD&A. This means that a number of companies do not focus sufficient efforts or resources on the preparation of this document. This is simply unacceptable. We are concerned about this finding, which has persisted over several years. Companies must familiarize themselves with the provisions of Form 51-102F1 and use the tools⁶ available to help them prepare quality MD&As.

We remind issuers that the MD&A is management's explanation of the company's performance, financial condition and future prospects. When companies prepare their MD&A, their objective must be to enhance their financial disclosure. They must also present a balanced discussion to help the market understand the financial statements as well as material information not presented in those financial statements.

Several elements are often omitted from MD&As. In an effort to foster MD&A compliance, the deficiencies most often noted over the reporting period are set out below, together with examples, our recommendations and references to Form 51-102F1.

- Failure to quantify the factors having given rise to changes in revenues.

E.g.: Our revenues were \$23.7 million compared with \$14.6 million the preceding financial year, an increase of 62%. This significant increase in revenues is due to our marketing efforts.

Companies must comment on revenues by operating business segment and analyze any changes in such amounts caused by selling prices, quantity of goods sold, or the introduction of new products. In this regard, readers should refer to paragraphs 1.4 (a) and (b) of Form 51-102F1.

- Failure to discuss gross profit.

E.g.: The cost of goods sold was \$100 million, compared with \$80 million the preceding year.

In addition to setting out the figures contained in the financial statements, companies must explain the causes of changes to their gross profit. In this regard, readers should refer to paragraph 1.4 (c) of Form 51-102F1.

6 MD&A Guidance on Preparation and Disclosure, a guide prepared by the Canadian Institute of Chartered Accountants (the "CICA").

- Failure to discuss the company's liquidity position and needs in the short term and long term.

E.g.: At year-end, the company had cash holdings of \$16.1 million and claims of \$89.8 million. Short-term assets were \$125.8 million and short-term liabilities were \$288.5 million. The company believes it has sufficient capital to meet its working capital requirements over the next 12 months.

In this example, the company has a working capital deficiency. It is therefore essential to explain how it expects to discharge its financial obligations as they come due and remedy the working capital deficiency. Companies must avoid boilerplate language and discuss their ability to generate sufficient funds to maintain their operations. In this regard, readers should refer to section 1.6 of Form 51-102F1.

- Incomplete disclosure of related party transactions.

E.g.: The company acquired \$10 million of assets and assumed the bank loan and accounts payable of A, a company under common control. The company assigned to X, a related company, its rights and obligations relating to a lease

Although a number of companies provide disclosure regarding related party transactions, most do not discuss the information sufficiently. These two examples have a point in common: the business purpose of the transactions has not been explained. The MD&A must include a discussion of the qualitative and quantitative characteristics of related party transactions that are necessary for an understanding of the business purpose and economic substance of the transactions. In this regard, readers should refer to section 1.9 of Form 51-102F1.

We reiterate the fact that the MD&A continues to be one of the best channels for companies to provide disclosure to the market with respect to their performance, financial condition and future prospects, and that they are required to do so.

This year, once again, we examined compliance with the provisions of Regulation 58-101 and Regulation 52-110. These matters are important, because over 17% of our requests for changes pertained to corporate governance and audit committee disclosure. In this regard, we urge companies to re-read these two regulations and their related policy statements.

The following paragraphs set out the principal deficiencies we identified during our reviews:

Compliance with Regulation 58-101

Part 2 of Regulation 58-101 requires companies to disclose their corporate governance practices and pertains to their obligation to file a code of conduct and ethics. The disclosure is found in Form 58-101F1 for non-venture issuers and in Form 58-102F2 for venture issuers.

The following deficiencies were identified with respect to this regulation:

- Failure to file on SEDAR a written code adopted or amended by the company.
- Failure to indicate whether a written code was adopted, whether the board of directors has adopted measures to encourage and promote a culture of ethical business conduct and whether steps have been taken to ensure directors exercise independent judgement.
- Failure to disclose whether or not a majority of directors are independent. It bears reminding that a director is considered to be independent if he satisfies the conditions set out in section 1.4 of Regulation 52-110.
- Failure to disclose whether or not the independent directors hold regularly scheduled meetings at which non-independent directors and members of management are not in attendance.
- Failure to properly describe board positions or to disclose how the board of directors delineates the role and responsibilities of the CEO when there is no written position description for the CEO.
- Failure to describe what steps the board of directors takes to select new board members as well as provide orientation and continuing education for directors.
- Failure to provide specific disclosure on the compensation of directors.
- Failure to disclose whether or not the board of directors, its committees and individual directors are regularly assessed with respect to their effectiveness and contribution.

Compliance with Regulation 52-110

Barring few exceptions, the regulatory provisions pertaining to the independence of audit committee members are well understood. It bears reminding that a member of the audit committee is independent if he has no direct or indirect material relationship with the company, namely, if he has a relationship that does not interfere with the exercise of a member's independent judgment. Furthermore, the regulation specifies certain cases in which individuals are considered to have a material relationship with a company, such as an individual who, or whose immediate family member, is or has been, within the last three years, an executive officer or employee of the company.

A weakness still exists in disclosures. There is often insufficient or no description of the education and experience of each member of the audit committee; this information is relevant to the performance of their responsibilities. We also noted a number of deficiencies in the written charters of audit committees as regards compliance with the provisions of Part 2 of Regulation 52-110 related to audit committee responsibilities. The following are some of those deficiencies:

- Vague confirmation that the audit committee is directly responsible for overseeing the work of the external auditor.
- Failure to specify the pre-approval of all non-audit services.
- Failure to indicate that, in addition to being responsible for reviewing the company's annual financial statements, the audit committee is responsible for reviewing the interim financial statements, the MD&As and press releases regarding annual and interim earnings.
- Failure to indicate that the procedures for reviewing financial information disclosed to the public are adequate. To that effect, periodic assessment of these procedures is essential.
- Failure to review and approve the company's hiring policies regarding partners, employees and former partners and employees of the present and former external auditor of the company.

We expect companies to provide high quality and transparent disclosure as well as comply with the regulations respecting corporate governance and audit committees. We believe that these regulations contribute to greater investor confidence in the financial markets.

D OTHER MATTERS

ABCP

In order to ensure the accuracy of information provided to the market, the AMF, together with the other CSA members, reviewed the continuous disclosure documents of companies holding non-bank-sponsored ABCP.

As regards financial statements, we specifically focused on whether companies had done the following:

- depreciated the ABCP;
- classified the ABCP in non-current assets on the balance sheet;
- used a valid method and appropriate assumptions to measure the fair value of the ABCP;
- disclosed the method for measuring the ABCP; and
- provided information regarding the uncertainty relating to measurement of the fair value of the ABCP.

As regards MD&As, we examined whether companies had done the following:

- discussed their ability to meet their cash flow requirements;
- discussed how the ABCP affected compliance with their financial ratios; and
- discussed the uncertainty relating to measurement of the fair value of the ABCP.

By and large, our review of the financial statements indicated that companies had done the following:

- depreciated the ABCP;
- classified the ABCP as non-current assets;
- estimated the fair value of the ABCP using an adequate measuring technique; and
- provided the necessary information regarding the uncertainty relating to measurement of the fair value of the ABCP.

However, disclosure regarding the measurement technique used to estimate the fair value of the ABCP was often insufficient, primarily as regards the method used and the assumptions made.

For example, some companies indicated that they had measured the ABCP by using all public information available on the market and a discounted cash flow method. Others used factors and assumptions that a marketplace participant would have considered when measuring the fair value of the ABCP. Disclosure limited to this type of information is clearly insufficient.

Our review of the MD&As demonstrated that companies often reproduced the disclosure already provided in the financial statements, without supplementing it. Although most companies indicated that they had sufficient cash to cope with the ABCP crisis, we noted that some of them had been obliged to borrow funds to meet their obligations. Discussion regarding the impact on the company's financial condition of the future repayment of the loan, in the event of a decline in the fair value of the ABCP, was often inadequate.

Overall, although the recording and presentation of information related to non-bank-sponsored ABCP were satisfactory, companies holding this type of investment must provide high quality disclosure regarding the methods and assumptions used to measure the fair value of the ABCP, including a discussion of the impact of the ABCP on their financial condition.

Disclosure for Mineral Projects

In the continuous disclosure records of mining companies, the principal deficiencies we noted related to the following:

- compliance with the standards of disclosure for mineral projects pursuant to Regulation 43-101; and
- compliance of the MD&A with Form 51-102F1 and Regulation 52-101.

Regulation 43-101 governs how mining companies disclose scientific and technical information about their mineral projects to the public. It covers oral statements as well as written documents and websites. It requires that all disclosure be based on a technical report, or other information, prepared by a "qualified person." Furthermore, the regulation prescribes the form of the technical report and indicates situations in which such a report is required and the circumstances in which the author of the report must be independent of the company. Moreover, mining companies must disclose their reserves and resources in accordance with the definitions approved by the Canadian Institute of Mining, Metallurgy and Petroleum.

The following are the deficiencies often noted with respect to Regulation 43-101:

- Failure to file a technical report, in prescribed form, in connection with mineral projects on material properties.
- Failure to include the certificate or consent of the qualified person when filing a technical report.
- Improper classification of mineral resources or reserves.
- Failure to include required disclosure in historical estimates, such as the source and date of the estimate as well as any disclaimers.

- Use of inadequate terminology.
- Failure to indicate the name of the “qualified person” and his relationship with the mining company in press releases.

On a few occasions, we also noted that mining companies whose properties are in the development stage are providing information which leads to the premature conclusion that a mine, in the traditional sense of the term, is in production. In order to avoid any confusion with respect to the progress of their projects, we required certain companies to modify the terminology used in their continuous disclosure documents. Others were required to file press releases to re-establish the facts regarding their status.

A number of mining companies are providing incomplete disclosure in their MD&As regarding their mineral projects and their means of financing. Mining companies must, among other matters, provide the following disclosure:

- A summary of the exploration work undertaken during the reporting period and the results of such work.
- A description of each mineral project together with the plan for each project (status of the project, expenditures made and anticipated costs).
- A discussion of decisions made by management for each property, particularly regarding the abandonment or complete or partial sale of a property.
- A discussion of the manner in which the company intends to finance its exploration work.
- A breakdown of the material components of capitalized or expensed exploration costs.
- An analysis of capitalized or expensed exploration costs on a property-by-property basis.

Finally, we remind mining companies that technical information is reviewed as part of our CDR Program.

INVESTMENT FUNDS

In this section of the report, we discuss the deficiencies most often noted in the investment fund records analyzed during the reporting period, grouped by relevant subject and accompanied by our recommendations.

The CDR Program relating to investment funds encompasses the entire continuous disclosure record of an investment fund, including all documents filed pursuant to Regulation 81-106 and all disclosures or publications intended for investors, such as a fund's website. The majority of the 262 investment funds governed by the Act and for which the AMF is the principal regulator – including some 221 mutual funds – are covered by the CDR Program respecting investment funds. The AMF may review the continuous disclosure records of investment funds by way of a full review or an issue-oriented review.

The AMF reviews focused primarily on conventional mutual funds, because they are an investment vehicle of choice for most investors. However, our recommendations can apply to the continuous disclosure documents filed by other types of investment funds, such as non-redeemable investment funds and exchange-traded funds.

A FINANCIAL STATEMENTS

Financial Disclosure Requirements

As regards disclosure to be made in the statement of net assets, the statement of operations and the statement of changes in net assets, certain investment funds did not disclose all of the information required by sections 3.1, 3.2 and 3.3 of Regulation 81-106 under separate line items. We noted, among other things, that investment funds presented, in a single line item in the statement of operations, expenses which should have been presented separately. For example, some investment funds combined the trustee's fees with the custodial fees or they presented securityholder reporting costs under "other expenses."

We remind readers that these regulatory provisions are necessary in order to help investors to compare and understand the financial information presented to them. The only exceptions to these presentation requirements are set forth in section 3.7 of Regulation 81-106 regarding inapplicable line items. We invite readers to consult this section.

Notes to Financial Statements

The notes to the financial statements of certain investment funds do not include all the information regarding the basis for determining the current value and the cost of portfolio assets. In this regard, the principal deficiencies noted relate to the accounting policies adopted by investment funds for valuing their portfolio securities.

For example, we noted that certain funds that invest part of their portfolio in securities of closed companies had not presented the accounting policy regarding the method used to determine the fair value of the securities of those companies.

We remind readers that the presentation of this information is required pursuant to subparagraph 3.6(1)(1) of Regulation 81-106 and also complies with section 1505.04 of the *CICA Handbook*.

Given that the basis for determining the current value and the cost of portfolio assets has a material impact on the financial statements of investment funds, we wish to ensure that the notes to their financial statements contain as complete as possible a summary of the significant accounting policies adopted by the funds.

Auditor's Report

Certain provisions of Part 2 of Regulation 81-106, relating to the auditor's report that accompanies the annual financial statements, and certain provisions of *Regulation 52-108 respecting Auditor Oversight* ("Regulation 52-108") were not respected. In particular:

- certain auditor's reports did not indicate that the auditor had issued an auditor's report on the comparative financial statements;
- certain auditor's reports were not signed; and
- one auditor's report had not been prepared by a "participating audit firm", as defined in Regulation 52-108.

We remind readers that annual financial statements of an investment fund that are filed and accompanied by an auditor's report that is not signed or was not prepared by a "participating audit firm" do not comply with the regulatory provisions and will require the filing of amended annual financial statements accompanied by a compliant auditor's report.

Summary of Results of Operations

Management's discussion of fund performance is intended to supplement and accompany the financial statements. In accordance with section 2.3 of Part B of Form 81-106F1, this discussion must in particular allow investors to make a connection between the performance of the investment fund and its results of operations. Certain management summaries of the results of operations did not meet this objective, because the discussion of the significant factors that affected the performance of the investment fund was incomplete or superficial.

In one instance, the performance of securities in a given industry segment, in which the fund had increased its investment percentage, had a very significant impact on the fund's unrealized gains and, incidentally, on its performance. Management did not provide any disclosure on this important aspect of the fund's results, despite the fact that this was a situation in which a change in the composition of the investment portfolio had had an impact on the fund's results of operations.

In another case, management presented identical summaries of the results of operations for two investment funds in the same family of funds, although the funds did not have the same investment objectives or strategies and their portfolio mixes were different. Management of these two investment funds included a discussion of economic and market changes in their reports, but failed to make a connection between these changes and the results of operations of the two funds.

We pay particular attention to management's discussion of fund performance, because it is intended to give investors the ability to look at the investment fund through the eyes of management by providing both a historical and prospective analysis of the investment activities and operations of the investment fund. We invite readers to consult Item 2 of Part A of Form 81-106F1.

To managers who present the performance of broad-based securities market indices in the summary of the results of operations, we also recommend that they make concrete links between the performance of the indices presented and the performance of the investment fund. The objective is to show investors that the investment fund's performance is related to the performance of industry or market sectors in which the fund makes investments.

Similarly, it is important to remember that management's report must present the information in plain language and avoid excessive use of financial jargon and technical terms.

Financial Highlights

In certain management reports, a number of notes accompanying the tables provided for under Item 3.1(1) of Part B of Form 81-106F1 were missing or incomplete. Furthermore, we noted that certain terms being used were not those provided for under this item.

The notes accompanying the tables are important, because they provide information needed to understand the financial data provided in the tables. Similarly, given that differences in the manner in which financial information is presented make it difficult for investors to understand and compare such information, the terms used must be the same for all investment funds.

Summary of Investment Portfolio

We noted that the breakdown of the investment portfolio does not always properly reflect the nature of the investment fund.

For example, a money market fund with a portfolio invested in various Canadian money market instruments, such as treasury bills, bankers' acceptances and ABCP, presented a summary of its portfolio broken down into the following categories: 90% in money market instruments and 10% in cash. In such a case, the breakdown of the portfolio is too broad and does not provide readers with a relevant representation of the fund's portfolio on the given date. Given the nature of the fund, a breakdown of its portfolio according to the type of money market instrument would have been more meaningful.

Item 5(2)(a) of Form 81-106F1 requires the summary of investment portfolio to break down the entire portfolio of an investment fund into the most appropriate subgroups or categories. We believe that a breakdown of the portfolio into the most appropriate categories is important, because the summary of investment portfolio draws the attention of investors to the risks and probabilities associated with the types of investments, geographical locations and industry sectors. It also allows investors to determine to what extent an investment fund meets their investment objectives and strategies at a given moment. We invite readers to consult the instructions relating to Item 5 of Form 81-106F1.

We carried out an issue-oriented review of ABCP holdings by mutual funds that are investment funds in Québec. The AMF, together with the other CSA members, sent a letter on August 20, 2007 to the managers of these mutual funds to collect data on the ABCP held in their portfolios.

Our findings indicated that five families of mutual funds held bank-sponsored ABCP and non-bank-sponsored ABCP, five families of mutual funds held only bank-sponsored ABCP and 10 families of mutual funds did not hold any ABCP. On October 31, 2007, given the amount of non-bank-sponsored ABCP held in their portfolios, four families of mutual funds sold all these holdings, at cost plus the accrued interest, to their manager or to a related entity, pursuant to exemptive reliefs granted by the AMF.

Beginning in September 2007, again in co-operation with the other CSA members, we carried out a review that focused on the continuous disclosure documents and simplified prospectuses of certain mutual funds holding ABCP. The review, which was carried out within the scope of simplified prospectus renewals, revealed the following:

- Disclosure in simplified prospectuses of the risks associated with holdings of asset-backed securities, be they ABCP or other asset-backed securities, is not always accurate or complete, particularly as regards the rollover risk associated with ABCP holdings. When relevant, we asked mutual funds that invest in asset-backed securities to update the disclosure in their prospectuses regarding the various risks associated with holdings of asset-backed securities, such as the credit risk, the rollover risk, the risk of fluctuations in value and the risk related to interest rates.
- The investment objectives and strategies described in Part B of the simplified prospectuses of mutual funds are not always accurate as regards mutual fund investments in ABCP or other asset-backed securities. When a mutual fund had a significant portion of its net assets invested in ABCP or other asset-backed securities, we ensured that the investment objectives and strategies contained complete and clear disclosure regarding these investments.
- The classification of ABCP and other asset-backed securities in the investment portfolio is not always appropriate, given the nature of these securities. For example, we noted that certain mutual funds classify ABCP with other money market instruments, without making any distinction, or they classify asset-backed securities with other fixed income securities. This type of classification does not allow readers to properly assess the percentage of net assets of a fund invested in asset-backed securities.

D COMPLIANCE REPORTS

During the period, 29 mutual funds failed to file their compliance reports within the time limit stipulated in section 12.1 of *Regulation 81-102 respecting Mutual Funds* ("Regulation 81-102"). We remind readers that compliance reports are important, because they certify compliance with the provisions of Parts 9, 10 and 11 of Regulation 81-102 regarding sales and redemptions of mutual fund securities and the commingling of funds. Furthermore, a failure to file these reports could result, among other things, in the default being recorded on the list of reporting issuers published on the website of the AMF.

E REQUIRED WARNINGS IN SALES COMMUNICATIONS

A number of mutual funds post information on their websites regarding their performance. We noted that the information regarding performance data was not always accompanied by the warnings required by section 15.4 of Regulation 81-102. We asked these mutual funds to add or supplement the required warnings in their sales communications.

Disclosure regarding performance data constitutes a sales communication within the meaning of section 1.1 of Regulation 81-102 and, as such, must comply with the various applicable provisions of Part 15 of Regulation 81-102 regarding sales communications and prohibited representations. These warnings are essential in order to prevent a misinterpretation of performance data by investors.

F OTHER DEFICIENCIES

The following is a non-exhaustive list of other significant deficiencies noted in the continuous disclosure documents of investment funds. Although these deficiencies occurred less frequently than those discussed above, we believe investment funds and their managers should take them into account in order to improve the quality of the financial information they publish.

- Certain annual financial statements and annual management reports were not posted on the website of the fund in accordance with section 5.5 of Regulation 81-106.
- Certain interim financial statements for the period ended June 30, 2007 did not comply with Section 3855, *Financial Instruments – Recognition and Measurement*, of the *CICA Handbook*. Listed portfolio securities were valued at their closing market price rather than at their last bid price and transaction costs were not recognized in net income.

- One investment fund that held securities of several underlying funds used an incorrect net asset value per unit to value the securities of one of these funds as at the last business day of the year.
- Certain annual and interim financial statements contained a significant number of typographical errors that could affect investors' understanding of the financial information.
- Discussion of related party transactions in the management report of certain funds did not comply with Item 2.5 of Part B of Form 81-106F1 or had been omitted.
- In 2007, index provider PC-Bond renamed all Scotia Capital indices as DEX indices. Certain management reports did not reflect this change.
- The quarterly portfolio disclosure of certain funds was not posted on the website of the fund within the time period stipulated in subsection 6.2(2) of Regulation 81-106.
- Certain proxy voting records were not prepared and posted on the website of the fund in accordance with subsection 10.4(1) of Regulation 81-106.

4

REGULATORY AND ACCOUNTING PROSPECTS

One of the two fundamental objectives of the CDR Program is to foster awareness among companies about their continuous disclosure obligations. Consequently, this section discusses certain regulatory and accounting prospects and developments that will be subject to review over the next few years.

REGULATORY DEVELOPMENTS

A FORWARD-LOOKING INFORMATION

28

The CSA amended the provisions relating to forward-looking information. The amendments, which have been in force since December 31, 2007, harmonize and clarify the obligations relating to the preparation and communication of forward-looking information. Moreover, the same provisions for updating, comparison to actual results and withdrawal apply to future-oriented financial information and to financial outlooks.

Regulation 51-102⁷ groups together these new provisions which apply to all material forward-looking information required to be communicated to the public,⁸ namely:

- information filed with the CSA;
- information contained in press releases published by a company;
- information posted on a company's website; and
- information published in promotional or similar documents disseminated to the public.

External auditors must not issue a report on forward-looking information. Furthermore, the new requirements are consistent with the provisions of Section 4250 of the *CICA Handbook, Future-oriented financial information*. A summary of these requirements is set forth in Appendix B.

⁷ See Parts 4A and 4B as well as section 5.8.

⁸ It should be noted that the requirements respecting forward-looking information do not apply to disclosure contained in an oral statement or to disclosure provided for in *Regulation 51-101 respecting Standards of Disclosure for Oil and Gas Activities* or *Regulation 43-101 respecting Standards of Disclosure for Mineral Projects*.

It is important to remember that companies must be vigilant so as to identify all forward-looking information communicated to the public that gives rise to the regulatory requirements, because the AMF and the other CSA members intend to pay particular attention to compliance with these new provisions.

B FORM 51-102F6, STATEMENT OF EXECUTIVE COMPENSATION

On September 19, 2008, the CSA published the final version of *Form 51-102F6, Statement of Executive Compensation, of Regulation 51-102 respecting Continuous Disclosure Obligations* ("Form 51-102F6"), which will come into force on December 31, 2008.

This new form will help the market understand the manner in which compensation decisions are made. The significant additions relate, among other things, to the following items:

- the discussion of compensation;
- the summary compensation table (which henceforth will include a column showing total compensation); and
- the summary compensation table for share awards and option awards at their fair value on the award date.

C REGULATION 52-109

On August 15, 2008, the CSA published the final version of the *Regulation to repeal and replace Regulation 52-109 respecting Certification of Disclosure in Issuers' Annual and Interim Filings* ("Regulation 52-109"). The regulation will apply to annual and interim documents for accounting periods ending on or after December 15, 2008.

Significant additions have been made to the regulation. Henceforth, the certifying officers of non-venture issuers will have to certify:

- that they have evaluated the effectiveness of the internal control over financial reporting (ICFR);
- that they have disclosed in their annual MD&A their conclusions about the effectiveness of ICFR; and
- that they have disclosed the material weaknesses related to ICFR design and operation.

Moreover, the certifying officers of venture issuers will no longer be required to provide certification regarding the design and effectiveness of disclosure controls and procedures or the design of ICFR.

D REGULATION 81-106

The *Regulation to amend Regulation 81-106 respecting Investment Fund Continuous Disclosure* came into force on September 8, 2008. There were essentially two objectives to the amendments made to Regulation 81-106:

- modify the requirements regarding the calculation of the net asset value following the introduction of Section 3855, *Financial Instruments – Recognition and Measurement*, of the *CICA Handbook*; and
- clarify and correct certain regulatory provisions.

Amendments to Part 14 of Regulation 81-106 now allow investment funds to calculate their net asset value according to the fair value of their assets and liabilities instead of complying with Canadian GAAP. Thus, henceforth, all references to “net assets” or “net assets per unit” are considered to be net assets determined in accordance with Canadian GAAP as presented in the financial statements of the investment fund, while all references to “net asset value” or “net asset value per unit” are considered to be net asset value determined in accordance with Part 14 of Regulation 81-106.

Furthermore, *Policy Statement to Regulation 81-106 respecting Investment Fund Continuous Disclosure* contains various instructions regarding the definition and determination of fair value, including for securities not listed on an active market.

Moreover, we would like to draw attention to certain changes that clarify or correct certain regulatory provisions:

- section 3.2 of Regulation 81-106 now requires transaction costs to be presented as a separate line item in the statement of operations;
- section 15.2 of Regulation 81-106 now requires transaction costs to be excluded when calculating the management expense ratio; and
- Item 3.1 of Part B of Form 81-106F1 was amended in order to introduce new provisions for the calculation of the trading expense ratio for a fund of funds.

We will pay particular attention to the application of the above-mentioned amendments in our subsequent reviews.

ACCOUNTING DEVELOPMENTS

A

GENERAL STANDARDS OF FINANCIAL STATEMENT PRESENTATION – GOING CONCERN

Under the new provisions of Section 1400 of the *CICA Handbook*, companies are required to disclose material uncertainties related to events or conditions that may cast significant doubt upon their ability to continue as a going concern.

B

INVENTORIES

Section 3031 of the *CICA Handbook* reduces the number of methods permitted for determining the cost of inventories and provides more detailed guidance on the determination of such cost. Furthermore, it increases disclosure requirements.

C

FINANCIAL INSTRUMENTS – REQUIRED DISCLOSURE

Under Section 3862 of the *CICA Handbook*, companies must provide greater disclosure about their exposure to the risks arising from financial instruments and about the manner in which they manage those risks.

D

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

The Accounting Standards Board of Canada confirmed January 1, 2011 as the date for the adoption of IFRS as GAAP in Canada (the “changeover to IFRS”) for publicly-listed companies.⁹ Consequently, all reporting issuers are targeted and must prepare for the changeover to IFRS. In addition to educating themselves and acquiring in-depth knowledge of IFRS, companies will have to take the following steps:

2008

Establish an IFRS changeover plan.

Analyze the expected impact on reporting.



⁹ In order to allow for their early adoption, the CSA may grant exemptive relief, on a case by case basis, from the obligation to adopt IFRS on January 1, 2011.

2009

Update the IFRS changeover plan.

Quantify more precisely the impact of the changeover to IFRS.



2010

Collect data for purposes of preparing IFRS-based comparative financial statements in 2011.

Companies must provide information regarding the changeover to IFRS principally in their MD&As. Pursuant to Item 1.13 of Form 51-102F1, they must discuss and analyze any changes in their accounting policies they expect to adopt due to a change in accounting standards. More specifically, companies must do the following in their annual and interim MD&As:

- describe the new accounting standard;
- disclose the permitted methods of adoption and the method they expect to use;
- discuss the expected effects on their financial statements; and
- discuss the potential effects on their business.

Until the changeover to IFRS, companies should adopt the following approach:

2008

Describe in their interim MD&A the key elements and timing of their IFRS changeover plan. Provide the description no later than in the annual MD&A.

If, at the time of preparing its MD&As, the company is well advanced in its IFRS changeover plan, it should discuss the impact of the IFRS changeover on its financial reporting.



2009

Provide an update of progress on its IFRS changeover plan in its interim MD&As.

Update information previously provided.

Describe the major differences between its current accounting policies and those it is required to apply under IFRS.



2010

Provide an update of progress on its IFRS changeover plan in its interim MD&As.

Update information previously provided.

Discuss in more detail the key decisions and changes it has made, or will have to make, relating to the changeover to IFRS.

Discuss decisions about available accounting policy choices.¹⁰

Present available quantified information about the impact of IFRS on the key line items in its financial statements.

Work to identify potential amendments to securities regulations as a result of the changeover to IFRS is ongoing. For more information on this subject, we invite readers to consult the following documents released in 2008:

- *CSA Staff Notice 52-320, Disclosure of Expected Changes in Accounting Policies Relating to Changeover to International Financial Reporting Standards;*
- *CSA Staff Notice 52-321, Early Adoption of International Financial Reporting Standards, use of US GAAP and reference to IFRS-IASB;*
- *CSA Concept Paper 52-402, Possible changes to securities regulations relating to International Financial Reporting Standards.*

Finally, we invite companies and their advisers to consult the regulations as well as the *CICA Handbook* for the conditions of application and effective dates relating to the subjects referred to in the preceding sections. Again, the foregoing is not an exhaustive list of the new regulatory provisions or accounting standards.

¹⁰ Choices offered under the IFRS 1, *First-time Adoption of International Financial Reporting Standards*, and other individual IFRS standards that are relevant to the company.

5

CONCLUSION

Although a number of continuous disclosure documents reviewed under the CDR Program require improvements, the majority of companies and investment funds do comply with the Act and the regulations. We recognize that the rapid pace of changes in accounting standards and regulatory provisions has had a significant impact on companies and investment funds this past decade or so. Notwithstanding these changes, we strongly urge them to pursue a level of excellence in fulfilling their continuous disclosure requirements; it is our hope that our exchanges contribute to this success.

The findings of our reviews under the CDR Program indicate that certain investment funds and companies must further strive to improve the quality of the following documents:

- the financial statements, as regards compliance with GAAP, particularly with respect to disclosure of the methods used and assumptions applied in determining the fair value of ABCP and other financial instruments;
- the MD&A, as regards compliance with Form 51-102F1, including the presentation of a balanced discussion of the company's results of operations;
- the annual information form or circular, as regards disclosure of governance practices required by Regulation 58-101, disclosure of the audit committee's responsibilities regarding a written charter as prescribed by Regulation 52-110 and disclosure of technical information as required by Regulation 43-101; and
- the annual and interim management reports of fund performance, as regards compliance with Form 81-106F1, including the presentation of a complete and meaningful discussion of the results of operations and the presentation of an overview of the portfolio broken down into the most appropriate subgroups or categories.

We reiterate the importance of monitoring regulatory prospects and developments and draw readers' attention to the new requirements related to forward-looking information as well as to the amendments made to Regulation 52-109, Form 51-102F6 and Regulation 81-106. As regards accounting developments, we confirm that our reviews will cover the new standards set out in the *CICA Handbook*, including the standards applicable to inventories and financial instruments. Moreover, we must emphasize the importance of preparations for the changeover to IFRS, a task that will present a major challenge in the next few years.

Finally, we are counting on you – senior executives, investment fund managers, directors and advisers – to provide the market with high quality information. For its part, the AMF helps ensure that issuers and investment funds furnish securityholders and the market with documents that comply with the Act and the regulations, thereby furthering its mission of monitoring the securities market. At the AMF, keeping the market well-informed is a priority!

A

APPENDIX

REGULATIONS¹¹ AND OTHER TEXTS

The following regulations and other texts contain the principal provisions of the continuous disclosure system applicable to companies and the continuous disclosure system applicable to investment funds. Other obligations may apply. All of the regulations and other texts can be consulted in the “Regulation” section¹² of the AMF’s website.

- *Regulation 43-101 respecting Standards of Disclosure for Mineral Projects;*
- *Policy Statement 41-201 respecting Income Trusts and Other Indirect Offerings;*
- *Regulation 51-102 respecting Continuous Disclosure Obligations;*
- *National Policy 51-201, Disclosure Standards;*
- *Regulation 52-109 respecting Certification of Disclosure in Issuers’ Annual and Interim Filings;*
- *Regulation 52-110 respecting Audit Committees;*
- *Regulation 58-101 respecting Disclosure of Corporate Governance Practices;*
- *Notice 52-306 (revised) – Non-GAAP Financial Measures;*
- *Regulation 81-101 respecting Mutual Fund Prospectus Disclosure;*
- *Regulation 81-102 respecting Mutual Funds;*
- *Regulation 81-104 respecting Commodity Pools;*
- *Regulation 81-105 respecting Mutual Fund Sales Practices;*
- *Regulation 81-106 respecting Investment Fund Continuous Disclosure;*
- *Regulation 81-107 respecting Independent Review Committee for Investment Funds.*

¹¹ Also refer to notices, policy statements and forms relating to regulations.

¹² www.lautorite.qc.ca

B

APPENDIX

FORWARD-LOOKING INFORMATION

		NFFLI ¹³	FOFI & FO ¹⁴
Establishment	Reasonable basis	■	■
	Reasonable assumptions		■
Disclosure	Identification: forward-looking information	■	■
	Warning: actual results may vary	■	■
	Material risk factors	■	■
	Material assumptions used to develop the forward-looking information	■	■
	Policy for updating forward-looking information	■	■
	Date of management approval		■
	Purpose of the FOFI or financial outlook and caution to readers that the information may not be appropriate for other purposes		■
Updates	Discussion of events and circumstances that occurred and may cause actual results to differ materially from previously disclosed forward-looking information	■	■
	Discussion of all expected material differences	■	■
Comparison	Discussion of all material differences between actual results and previously disclosed FOFI or financial outlooks		■
Withdrawal	Confirmation of the decision to withdraw	■	■
	Discussion of the events and circumstances that led to the decision, including the assumptions that are no longer valid	■	■
■ applicable requirement			

¹³ Non-financial forward-looking information.

¹⁴ Future-oriented financial information and financial outlooks.

We welcome comments on the CDR Program from companies, investment funds, their advisers and investors. Such comments contribute to the ongoing improvement of our review process so that it can effectively address the concerns of the market.

For more information or to provide us with your comments, please contact:

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