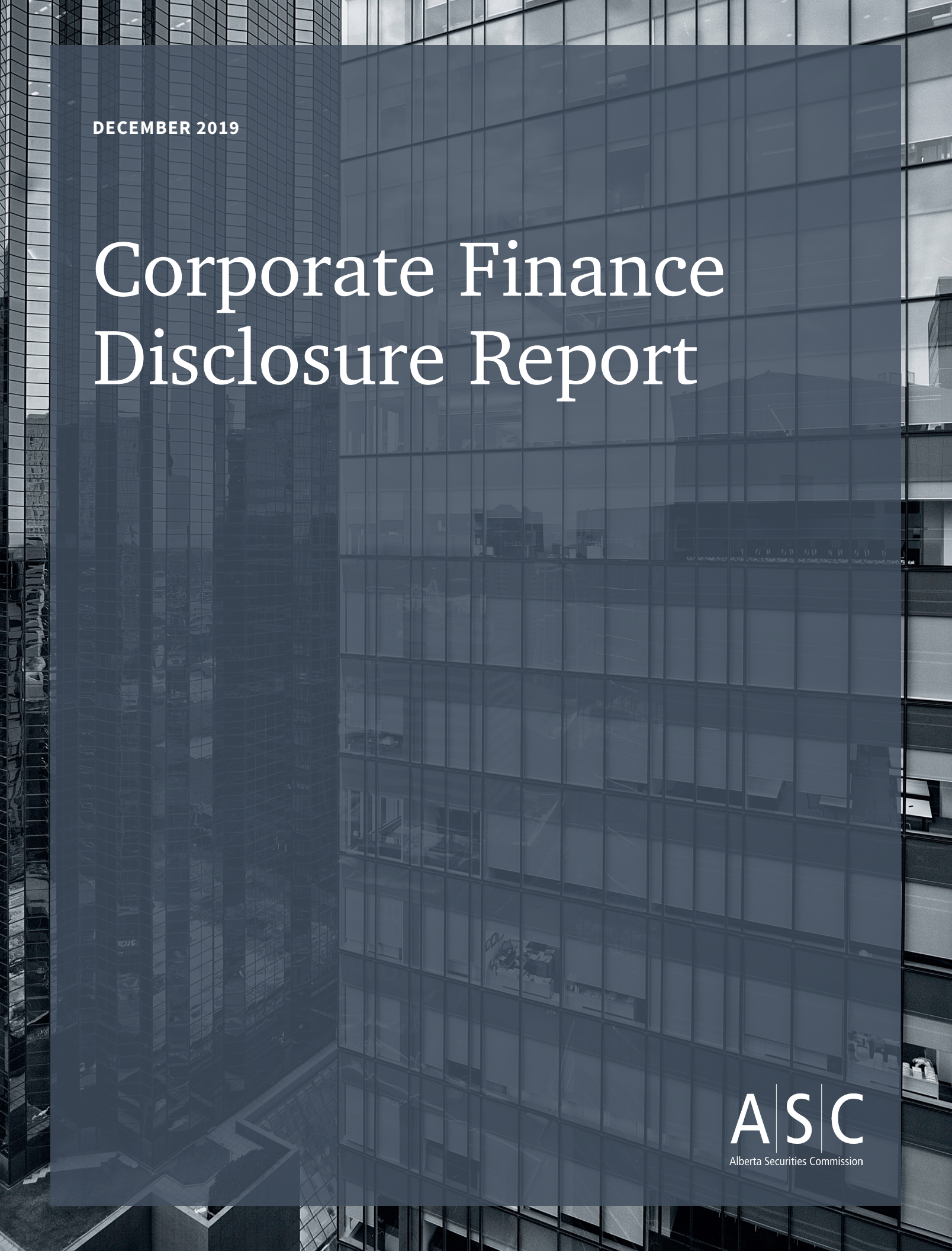

DECEMBER 2019

Corporate Finance Disclosure Report

ASC
Alberta Securities Commission

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High-quality corporate reporting promotes investor confidence.

Reliable corporate reporting is one of the critical foundations of investor confidence, without which a thriving and efficient capital market cannot exist.

In fulfilling our mandate to foster a thriving, fair and efficient capital market while protecting investors, staff of the Alberta Securities Commission's (**ASC**) Corporate Finance division review the continuous disclosure (**CD**) of Alberta reporting issuers (**RIs**) on an ongoing basis. We report our findings at the end of each year. Our goal is to highlight areas where disclosure could be improved to ensure investors receive accurate, timely and descriptive information on which to base their investment decisions.

In 2019, a number of challenges, including the continuing low price environment, contributed to an exceptionally difficult operating environment for Alberta's energy industry, which remains the largest industry constituent in the province's capital markets. These challenges have, unfortunately, sharply reduced global demand for investing in Canadian energy companies. Over the past few years, there has also been a concerted effort in Alberta to diversify our economy and we have seen RIs in new industries emerge.

Whether an established energy company or a new entrant to an emerging industry, investors require balanced disclosure. This enables them to fully understand both risks and opportunities, and reliable corporate reporting will be a critical part of the success of these new industries. We acknowledge the considerable effort made by Alberta's RIs, the majority of whom provide an appropriate level of disclosure, however there remain areas for improvement.

By their nature, ASC staff's CD reviews are generally historical-looking; however, ASC staff are also available for consultations on prospective disclosure, initial public offerings (**IPOs**), potential transactions or possible requests for relief. Such consultations may allow RIs to proactively avoid future disclosure deficiencies or reduce regulatory risk in relation to transactions. To maximize the usefulness of these consultations, we respectfully request that RIs and their advisors familiarize themselves with the applicable legal and accounting requirements and the issues raised, and provide us with as much context as possible. Our goal in all of these consultations is to come up with practical solutions. If you have issues this upcoming reporting season, we encourage you to contact us.

Please feel free to contact me or my colleagues with any feedback or questions.

Regards,

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Each year the ASC issues four reports: the annual report, the Alberta capital markets report, the oil and gas review and the corporate finance disclosure report. These reports are created to provide timely and relevant information for market participants and reporting issuers. They can be found at albertasecurities.com.

1. Review process and outcomes

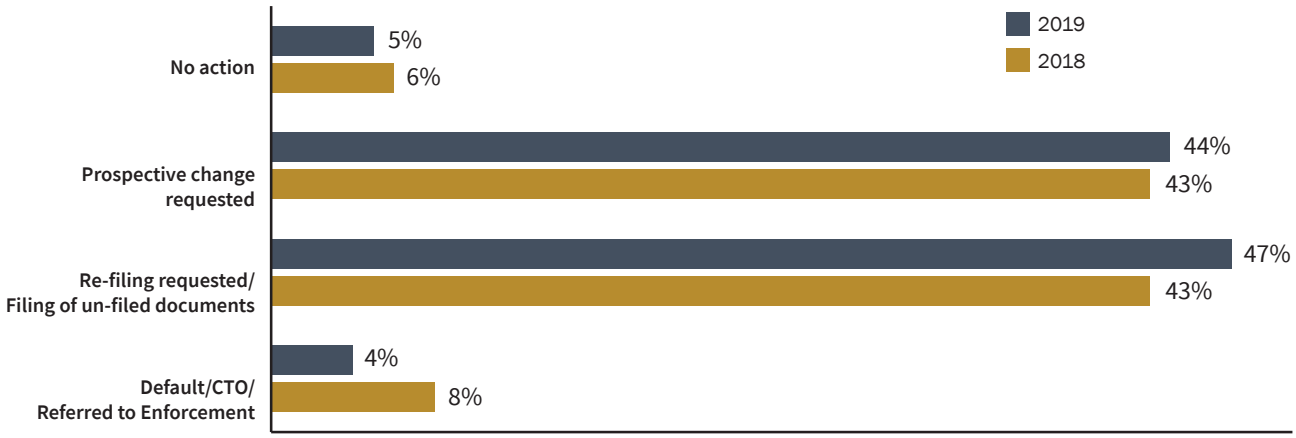
The ASC CD review program continues to be a key priority for the Corporate Finance division. We conduct CD reviews to ensure that RIs are in compliance with regulatory requirements and to provide direct feedback to RIs on how to improve their disclosure. Our program involves two types of CD reviews: full CD reviews and issue-oriented reviews (**IORs**).

The scope of our full CD reviews is comprehensive and will usually include an assessment of an RI's financial reporting and other CD filings for its most recently completed annual and interim periods. In addition to the CD an RI is required to file under securities legislation, we may also review and assess voluntary disclosures such as websites, social media platforms, webcasts and investor materials.

An IOR is a more limited review focused on particular issues, requirements or types of disclosure. IORs may be undertaken in furtherance of a CSA or ASC policy project, or to address a specific area of concern. We conduct some IORs jointly with other members of the CSA, while other IORs are limited to Alberta.

This year's IORs included specific disclosure issues in news releases, investor presentations, mining reports, MD&As and financial statements.

2019 CD Review Outcomes



In the vast majority of cases, we requested that the RI make prospective changes in its disclosure practices, file un-filed documents or re-file certain documents. In a few more serious instances, we placed the RI on the ASC's list of RIs in default of securities legislation, cease-traded the RI or referred the file to the ASC's Enforcement division for further investigation.

The less serious actions taken by us were divided between requests for prospective changes in disclosure practices, and requests for a filing of un-filed documents or re-filing of certain documents. We typically request that an RI make changes in its future disclosure in circumstances where we conclude that the deficiency identified in the RI's disclosure is not sufficiently serious or misleading to warrant a re-filing of its previously filed documents. We request the filing of un-filed documents or re-filing of certain documents when we identify un-filed documents which are required to be filed under securities legislation, or when previously filed documents contain deficiencies requiring immediate rectification. Requests to re-file documents were most frequently related to MD&As and corporate presentations. Requests to file previously un-filed documents were most frequently related to material contracts, executive compensation and other corporate governance disclosure.

This Report identifies some of the key areas where significant deficiencies were observed. It outlines our expectations for improvements and provides practical guidance, examples and practice tips to RIs.

2. Update of key disclosure issues over past five years

OVERVIEW

Since 2014, many RIs in Alberta have been significantly impacted by a sustained period of low commodity prices. In the pre-downturn period (2010 to 2013), the combination of higher commodity prices and increased domestic production has at times resulted in the oil and gas industry (including oil and gas services) accounting for over 70 per cent of the market capitalization of all Alberta-based RIs. Not surprisingly, the subsequent low commodity prices, combined with limited market access and a series of other domestic hurdles, have significantly slowed the growth of economic activity in Alberta for both RIs in the energy sector and in other industries.

In this difficult environment, many RIs have responded by implementing cost-cutting measures, trimming capital spending plans and reducing debt. We have also seen efforts made by RIs to find innovative solutions to reduce costs or increase production.

On the whole, disclosure by Alberta's RIs has been timely, balanced and responsive to the challenging market conditions. However, we continue to see opportunities for improved disclosure in areas which have been identified and discussed in previous reports over the last five years. These include liquidity and capital resources, non-GAAP financial measures (**NGMs**), forward-looking information (**FLI**) and unbalanced and promotional disclosure. We will look at issues we have encountered in these areas over the past five years, provide some examples of new disclosure trends and provide guidance regarding issues which are a frequent subject of inquiries to ASC staff.

A. Liquidity and capital resources

Disclosure of RIs' liquidity and capital resources continues to be a focus of our reviews. While we noted some improvements in the overall quality of this disclosure in 2019, we continue to regularly observe disclosure in which RIs discuss their liquidity and capital resources using boilerplate language or by simply reproducing numbers from their financial statements without helpful contextual information.

For example, we observed the following disclosure by an RI with significant liquidity risks: *"The Corporation will require additional funds to continue its investment strategy for the next twelve months. The Corporation will source funds through either debt or equity financing and such funds may not be available when needed."* While accurate, this disclosure is incomplete as it does not provide investors with sufficient information on the RI's specific cash requirements, the resources available to fund them or any associated trends, fluctuations or risks.

We remind RIs that this disclosure should be an area of focus for all entities, from established RIs to emerging RIs who are in the pre-cash flow stage and are in need of significant capital to execute their business plans. RIs can improve their disclosure by focusing on their cash requirements, funding arrangements and trends, fluctuations and risks. We examine each of these below.

CASH REQUIREMENTS

RIs are required to present an analysis of their cash requirements, in both the short and long term. This includes the expected resources necessary for both capital and operational needs as well as the repayment of obligations as they become due. We remind RIs that their capital requirement disclosure should consider both growth and sustaining capital, expenditures that are committed, and those that are uncommitted but planned.

Comprehensive disclosure in this area is particularly important for RIs who have a material uncertainty associated with their ability to continue as a going concern and those that are in the development phase and are in the process of executing on significant projects.

For instance, RIs that have negative cash flow from operations or a material risk related to their ability to continue as a

going concern might consider disclosing:

- their most current working capital amount.
- significant obligations that are maturing in the short term.
- their cash burn rate on a monthly or quarterly basis.
- the period of time that they are expected to be able to fund operations.
- how they intend to prioritize expenditures in the short term.
- their ability to meet their asset retirement obligations.

EXAMPLE THAT MET OUR EXPECTATIONS

Excerpt from an RI's MD&A on their cash requirements:

"As at December 31, 2018, we were committed to pay $8.5 million of trade and other payables and $7.8 million for research and development. Furthermore, our $11.0 million loan is due on September 30, 2019 including $0.8 million related to interest and other payments payable on or before the loan's maturity. In addition, aggregate expenditures over the next 12 months under agreements with contract research organizations are estimated to total approximately $10 to 13 million. Our average monthly Cash Burn Rate, a non-GAAP measure, for the three months ended December 31, 2018 was $2.6 million. Our historical Cash Burn Rate is not indicative of our future Cash Burn Rate. Our Cash Burn Rate has increased compared to the prior period, reflecting increased research and development costs. Based on our planned business operations for the next year, we expect our Cash Burn Rate to fluctuate based on the specific activities occurring in each quarter."

FUNDING

Funding of cash requirements can be considered as two separate categories:

- **Funding currently arranged but not yet used**
  This category is typically comprised of working capital amounts and debt facilities that an RI has entered into, but that have not yet been fully drawn. When disclosing this amount, RIs should assess if there are any restrictions that would prevent a further draw on their facility. For example, we have observed RIs who disclosed funding available from a facility when they were at risk of breaching their debt covenants if a further draw on the facility was made.
- **Funding not currently arranged**
  This could include private or public debt, equity or cash flow from operations if the RI has a **reasonable basis** to assume that these sources of funding are available to them. As the mix of financing available to Alberta entities continues to change, we remind RIs of the importance of regularly re-evaluating and updating this disclosure in light of the prevailing market conditions and economic circumstances.

If an RI's current and forecasted funds are insufficient to cover their cash requirements, we remind them that disclosure must be made as to the impact of this shortfall on their operations and business plan.

TRENDS, FLUCTUATIONS AND RISKS

RIs are required to disclose any trends, fluctuations and risks that have had, or could in the future have, an impact on their cash requirements or funding. RIs are also required to describe plans to manage these issues. This disclosure is aimed at helping investors make informed investment decisions.

In the current economic climate, it is likely unsurprising that we have observed credit agreements being amended, and additional covenants and restrictions being added. For instance, some lenders have amended credit agreements to add a covenant requiring the borrower to maintain a certain liability management rating (**LMR**). Consistent with the

requirement to disclose covenants, RIs are required to disclose the LMR covenant requirement and actual ratio, along with how management monitors this ratio, if applicable.

Examples of items requiring disclosure may include, among others:

- potential dispositions and the impact on the RI's cash flows.
- risk of default on credit facilities or facilities being renewed on different terms.
- counterparty risk associated with working capital amounts.
- changes in the mix and cost of capital available to the RI.

QUESTIONS TO ASK

When reviewing the completeness of their liquidity and capital resources disclosure in the MD&A, RIs should ask:

- Have we disclosed all of our cash requirements, both growth and sustaining?
- If applicable, have we discussed our current and/or forecasted cash shortfall and what impact this will have on our business?
- Have we disclosed the trends, fluctuations and risks associated with our cash requirements and funding, as well as our plan to manage these?
- Is our discussion fair and balanced? Have we given equal prominence to both risks and opportunities?

B. Non-GAAP financial measures (NGMs)

NGMs have become more commonplace in corporate reporting over the last several years, and that trend continued in 2019. While we understand that NGMs can be useful to RIs seeking to explain their financial performance, GAAP continues to be the mandated financial reporting standard. Therefore, the use of NGMs continues to be an area of focus in our CD reviews.

It is important that investors understand the difference between GAAP and NGMs, and possible limitations of the latter. Although we have seen some improvements in this area, the presentation and use of NGMs continues to be problematic in some instances.

While the disclosure of NGMs is voluntary, we have no objection to their use provided that they are accompanied by appropriate disclosure (i.e., information necessary to understand NGMs in their proper context), do not obscure GAAP results and are not otherwise misleading.

For more detailed guidance with respect to the use of NGMs, we encourage RIs to review CSA Staff Notice 52-306 (Revised) *Non-GAAP Financial Measures* (**SN 52-306**).

In September 2018 the CSA published proposed National Instrument 52-112 *Non-GAAP and Other Financial Measures Disclosure* in an effort to formalize the guidance in SN 52-306 into a rule. Significant commentary was received on the proposed instrument and the CSA is continuing to review and incorporate this feedback into this proposed instrument. The CSA will be publishing a second request for comment on a revised version of this proposed instrument in 2020. Until then, we encourage you to contact us with any specific questions you have for the upcoming reporting season on this topic.

QUESTIONS TO ASK

The likelihood of comment from ASC staff is reduced when an RI is able to answer each of the following questions in the affirmative:

- Have our NGMs been clearly identified and have we explained that they do not have any standardized meaning under GAAP and that there are limitations on their comparability to similar measures presented by other RIs?
- Have our NGMs been named in a way that distinguishes them from disclosure items specified, defined or determined under GAAP and in a way that is not misleading? For example, in presenting EBITDA as an NGM, it would be misleading to exclude amounts for items other than interest, taxes, depreciation and amortization.
- Have we explained why the NGM provides useful information to investors and the additional purposes, if any, for which management uses the NGM? For example, do we use several NGMs without clarifying what we are trying to communicate through the use of each NGM that we cannot communicate with a GAAP measure?
- Have we presented the most directly comparable measure specified, defined or determined under the RI's GAAP with equal or greater prominence to that of the NGM?
- Have we provided a clear quantitative reconciliation from the NGM to the most directly comparable measure specified, defined or determined under the RI's GAAP and presented in its financial statements? This must include a reference to the reconciliation when the NGM first appears in the document, or in the case of content on a website, in a manner that meets this objective (for example, by providing a cross-reference to the reconciliation).
- Have we ensured that we have not described NGM adjustments as non-recurring, infrequent or unusual, when a similar loss or gain is reasonably likely to occur within the next two years or occurred during the prior two years?
- Have we presented the NGM on a consistent basis from period to period or, if the composition of the NGM has changed, have we explained the reason for the change and restated any comparative period presented?

C. Forward-looking information (FLI)

Likely as a result of investor interest, we have seen an increase in the disclosure of FLI by RIs in recent years. In addition to the increase in GAAP financial information presented on a forward-looking basis, we have also observed FLI increasingly being used in combination with NGMs. NGMs disclosed on a forward-looking basis are subject to both the guidance in SN 52-306 and the requirements of Parts 4A and 4B of NI 51-102. Many RIs fail to provide required NGM disclosure; frequent omissions include a usefulness description, an understanding of the composition of the NGM and an appropriate quantitative reconciliation (or, in the case of a corporate presentation, a cross-reference[1] to the reconciliation included in the RI's CD filings). On the FLI-side, the most common omission is the required presentation of material factors or assumptions used to develop the FLI.

1 See paragraph 5 of section III of SN 52-306.

EXAMPLE THAT MET OUR EXPECTATIONS

An RI's investor presentation included the disclosure of an NGM on a forward-looking basis for its 2019 fiscal year:

Metric	Fiscal 2019 Forecast (updated) [ASC Note 1]	Nine-months ended September 30, 2019 (historical)	Fiscal 2019 Forecast [ASC Note 2]	2018 (historical)	2017 (historical)
Production (boe/d) [a]	30,000 - 31,200	29,600	33,000 - 34,600	26,995	22,105
Revenue ($/boe)	35.10	35.75	36.89	37.20	31.45
Realized hedging gain (loss) ($/boe) [ASC Note 3]	(0.05)	(0.50)	(0.89)	(0.50)	(0.33)
Royalties ($/boe)	(2.10)	(2.05)	(2.79)	(3.01)	(2.72)
Transportation expense ($/boe)	(4.78)	(4.95)	(4.18)	(3.72)	(3.33)
Production expenses ($/boe)	(9.22)	(9.75)	(9.02)	(9.01)	(9.95)
Operating netback[1] ($/boe) [b]	18.95	18.50	20.01	20.96	15.12
Operating netback[1] ($ millions) [a x b x number of days in the period]	211.6	149.5	246.9	206.5	122.0

[1] *"Operating netback is a non-GAAP measure. See non-GAAP measure advisories section in the MD&A."*

ASC Note 1: When the RI's production and pricing assumptions were off-target in comparison with its third quarter results, the RI appropriately updated its FLI estimates in its Q3 MD&A, as required under subsection 5.8(2) of NI 51-102, and provided the following discussion of the events and circumstances supporting this change:

- "The company has experienced delays commencing production from well X as its facility has experienced start-up issues and is not fully operational as planned. As a result of the delays in starting up its well X production (approximately 3,000 BOE per day), the company has reduced its annual 2019 average production estimate to be within a range of 30,000 to 31,200 BOE per day (previously 33,000 to 34,600 BOE per day).
- WTI crude oil prices are forecasted to average US$57.00 per barrel, down 3 per cent from the average forecasted price of US$59.00 per barrel in the company's previous guidance. Forecasted NYMEX natural gas prices have been revised downwards by 4 per cent to average $2.65 per $US/mmbtu. After giving effect to the changes in commodity price assumptions and estimated expenses, operating netback for 2019 was revised down by 14 per cent to $211.6 million."

ASC Note 2: The fiscal 2019 forecast presented in this column was the RI's initial FLI estimate first disclosed in November 2018.

ASC Note 3: The revenue ($/boe) presented in the table above represented the RIs average realized commodity prices, adjusted for quality, applicable fees and deductions, pipeline tariffs and/or location differentials.

In recent years, we have seen an increased trend of RIs disclosing FLI only in voluntary disclosure, such as corporate presentations. However, the same requirements apply to FLI no matter whether it is disclosed within an RI's required filings or voluntary disclosure. When FLI is disclosed outside regulatory filings, we frequently see instances where RIs fail to discuss material differences between actual results and the previously disclosed FLI[2], or fail to provide withdrawal disclosure[3]. In a recent file, an RI disclosed an adjusted funds flow forecast of $40 million for fiscal 2018 in its corporate presentation, however the actual result of this measure for the RI's fiscal 2018 period was $5 million and the RI did not disclose or discuss this material difference in its 2018 annual MD&A. Other RIs indicated they inadvertently failed to provide a comparison to actual results or withdrawal disclosure when their corporate presentation was updated or removed from their website and the previously disclosed FLI was not tracked or kept up to date.

To reduce the risk of non-compliance with disclosure requirements in relation to previously disclosed material FLI, we recommend that an RI include in its disclosure practice a step to ensure that any material information included in voluntary disclosure is also included in the RI's regulatory filings. In our reviews, we have asked that the board and management of the RI review the information provided in voluntary filings, assess its materiality and, where material, disclose it in the RI's regulatory filings on a go-forward basis.

QUESTIONS TO ASK

Questions for an RI to consider when assessing FLI and whether sufficient and appropriate disclosure has been provided, regardless of whether the disclosure is within an RI's required NI 51-102 disclosure or voluntary disclosure:

- Do we have a reasonable basis for the FLI?
- Is our FLI appropriately identified as such?
- Were the material risk factors that could cause our actual results to differ materially from the FLI identified and disclosed?
- Has the FLI been prepared using the same accounting policies we expect to use to prepare our historical financial statements for the period covered by the FLI?
- If an NGM has been disclosed on a forward-looking basis, have the related SN 52-306 disclosures been provided?
- Has our FLI been limited to a period for which it can be reasonably estimated?
- Has our disclosure relating to previously disclosed material FLI been met for the following:
  - Update requirements in subsection 5.8(2) of NI 51-102?
  - Comparison to actual in subsection 5.8(4) of NI 51-102?
  - Withdrawal disclosure requirements in subsection 5.8(5) of NI 51-102?
- Has the materiality of information contained in any voluntary disclosure been assessed and, where material, have we disclosed it in our regulatory filings?

2 Under subsection 5.8(4) of NI 51-102, an RI must disclose and discuss in its MD&A material differences between actual results for the period and any previously disclosed FLI for this same period.

3 Withdrawal disclosure requirements are found in subsection 5.8(5) of NI 51-102 and include the requirement for the RI to disclose the decision to withdraw and discuss the events and circumstances that led the RI to the decision to withdraw the previously disclosed FLI, including a discussion of the assumptions underlying the FLI that are no longer valid.

D. Balanced disclosure

Despite the continuing market challenges, in recent years we have generally seen more balanced disclosure in RIs' regulatory filings. We have, however, observed less balance in the disclosure provided on social media platforms. In a recent review, an RI announced on its LinkedIn page that they had *"Over $50 million of contracts in the works."* Upon inquiry, although the RI confirmed that potential customers had expressed interest in the RI's products and services, these discussions were still in the "qualified leads" phase (i.e. had not yet progressed to actual contract negotiations) with no agreements, conditional agreements or letter of intents signed. It is generally our view that disclosure should be limited to those potential agreements that are reasonably likely to occur. In addition, absent any information necessary for an investor to understand the nature, timing and risks related to this social media comment, it was considered to be misleading and promotional.

We remind RIs that the requirement to provide factual and balanced disclosure extends to disclosure provided on social media platforms, even if these activities are not directly intended to communicate with investors. Further guidance is provided in CSA Staff Notice 51-348 *Staff's Review of Social Media Used by Reporting Issuers*.

We have also seen deficiencies in disclosure regarding an RI's total addressable market or market share. In a recent review an RI disclosed that it expects to have a 10 per cent share of the Canadian market for a certain industrial mineral after 2020. Given that the RI had no sales recorded to date and no sales contracts with customers, we questioned whether the RI had a reasonable basis to disclose this FLI and whether the FLI was based on assumptions reasonable in the circumstances[4]. Other common deficiencies include the presentation of market data that is not attributed to its third party source or that includes markets outside those in which the RI operates.

EXAMPLE THAT DID NOT MEET OUR EXPECTATIONS

A sample of an RI's disclosure regarding its total addressable market.

Disclosure	Comments
"Legal cannabis spending in Canada is set to grow at a Compound Annual Growth Rate of 44.4 per cent from $569 million in 2018 to nearly $5.2 billion by 2024. The Company is well positioned to access this market".*	It was our view that without additional disclosure this statement could be viewed as promotional, considering: • the RI's licensed retail cannabis stores were mainly based in Alberta, with a very limited retail footprint outside Alberta. • the cited total market figures included spending on edible products and concentrates; products that the RI was not yet lawfully permitted to sell.
Several pages of the RI's corporate presentation referred to cannabis and hemp figures for the U.S. market, including the growth of sales of legal medical marijuana in the U.S. in 2017 to 2018 and the value of hemp imports to the U.S.	As the RI was not conducting any U.S. cannabis related activities and had no plans to do so, the discussion of the U.S. market was viewed as misleading.

** The RI obtained this information from a third-party source that they failed to reference.*

4 Section 4A.2 of NI 51-102 sets out the reasonable basis requirements and subsections 4B.2(1) to (2) of NI 51-102 sets out the reasonability of assumptions.

E. Material changes and related disclosure considerations

In response to the challenges posed by a lengthy economic slowdown, we have seen RIs reinvent themselves by changing their business, entering into new business(es) or undertaking restructuring transactions. When undertaking such a change, an RI should be mindful that additional disclosure requirements may be triggered.

RESTRUCTURINGS AND SIGNIFICANT ACQUISITIONS

We have previously reported on disclosure deficiencies relating to MCRs[5] or information circulars filed in respect of significant acquisitions or restructuring transactions. Issues associated with frequent non-compliance or in respect of which RIs have frequently asked for further guidance include:

- correctly identifying the financial statements required for the parties to the transaction (e.g. company[6], business[7], entity[8]) or for any indirect acquisition[9] completed by the parties to the transaction in the past two or three years.
- whether the financials to be presented are compliant with securities legislation (e.g. acceptable GAAP and auditing standards, the requisite number of years of financial statements, financial statement format (e.g. full financial statements, carve-out statements, operating statements, pro forma statements)).
- compliance with other disclosure requirements triggered by the transaction (e.g. MD&A, technical reports under National Instrument 43-101 *Standards of Disclosure for Mineral Projects* or oil and gas reports under National Instrument 51-101 *Standards of Disclosure For Oil and Gas Activities*).

The determination of the required financial statements and other disclosure in respect of a restructuring transaction, significant acquisition or in a long form prospectus filing can be complex, especially where the RI has recently completed a restructuring transaction or multiple acquisitions. We encourage RIs to contact us if they have questions on the requirements.

CHANGE OF BUSINESS

In last year's report we discussed disclosure considerations for going-public transactions involving RIs engaged in emerging industries or the development of new technologies. In recent years, we have seen RIs expand to operate in more than one distinct business. We remind RIs of their segment reporting obligations under GAAP and securities legislation. Disclosures about reportable segments provide critical information about an RI's business activities and the economic environment in which they operate.

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5 Under section 5.2 of Form 51-102F3, a MCR must contain the disclosure required by section 14.2 of Form 51-102F5 *Information Circular* for each entity that resulted from the restructuring transaction. As such, the MCR must include or incorporate by reference prospectus level disclosure (including financial statements) for each such entity.

6 Company means the issuer or RI.

7 Business means the business being acquired, if the matter is a significant acquisition.

8 Entity means each entity, other than the company, whose securities are being changed, exchanged, issued or distributed, if (i) the matter is a restructuring transaction, and (ii) the company's current security holders will have an interest in that entity after the restructuring transaction is completed; AND each entity that would result from the significant acquisition or restructuring transaction, if the company's security holders will have an interest in that entity after the significant acquisition or restructuring transaction is completed.

9 An indirect acquisition may constitute a scenario where an issuer or RI acquires a business that has itself recently acquired another business or related businesses.

PRACTICE TIP

Disclosure at the time of the material change:

- It is important that the RI describe the nature and substance of the material change in a timely manner. Some examples of significant facts relating to the material change may include: dates, parties, terms and conditions, description of any assets, liabilities or capital affected, purpose, financial or dollar values, reasons for the change, and a general comment on the probable impact of the change on the RI or its subsidiaries (e.g. business plan or operations, capital requirements, etc.).

Ongoing CD considerations:

- It is important to present a full picture of the RI. Key items to consider include:
  - Describing the business in an understandable way, and where an RI has more than one distinct business, describing each business separately.
  - Discussing the plans, significant milestones and timing for businesses or projects that have not yet generated revenue or that are in the early planning stages.
  - Understanding the cash requirements of each business, including where a business is generating negative cash flows from operating activities.
  - Identifying material risk factors of each business, including, if operations are located in an emerging area or market, laws or regulations associated with operations, political factors, factors that may affect the RI's title to its assets, etc.

3. Other CD issues

A. Climate change-related risk disclosure considerations

On August 1, 2019 the CSA published CSA Staff Notice 51-358 *Reporting of Climate Change-related Risks* (**SN 51-358**) in response to investors' increasing focus on climate change-related risks and concern that they are receiving insufficient disclosure of these risks. Given its potential significance to the energy industry, the ASC co-led this project. Among other things, the project involved an IOR in respect of RI's disclosure of climate change-related risk, which began in 2017.

SN 51-358 clarifies existing disclosure requirements and provides guidance regarding the application of those requirements in the context of climate change-related risks; it does not introduce any new legal requirements. SN 51-358 reinforces and expands upon the guidance provided in the earlier CSA Staff Notice 51-333 *Environmental Reporting Guidance* (**SN 51-333**) and should be read in conjunction with that notice. SN 51-333 continues to provide guidance to RIs on existing CD requirements relating to a broad range of environmental matters. RIs are encouraged to review both of these notices in preparing their annual disclosure.

SN 51-358 describes the major climate change-related risks, which are generally grouped under two categories: physical risks and transition risks. Physical risks include those risks that a change in climate itself could have on an RI's business, while transition risks are a broader set of risks associated with the consequences of the global transition to a less carbon-intensive economy.

Some Alberta RIs are leaders in this area and, during the course of our work, we observed a number of good examples of climate change-related risk disclosure. While these examples are not exhaustive and will not be applicable to all RIs, they offer investors a useful degree of specificity to the RI's business.

EXAMPLE THAT MET OUR EXPECTATIONS

Transition Risk - Regulatory and Policy

Existing and future laws and regulations may impose significant liabilities on a failure to comply with their requirements. Concerns over climate change, fossil fuel, GHG emissions, and water and land-use could lead governments to enact additional or more stringent laws and regulations applicable to the company.

Changes to environmental regulations relating to climate change could impact the demand for, formulation or quality of the company's products, or could require increased capital expenditures, operating expenses, abandonment and reclamation obligations and distribution costs, which may not be recoverable in the marketplace and which could result in current operations or growth projects becoming less profitable or uneconomic. In addition, such regulatory changes could necessitate the company to develop new technologies, requiring significant investments of capital and resources.

As part of its ongoing business planning, the company estimates future costs associated with GHG emissions in its operations and the evaluation of future projects, based on the company's outlook for carbon price under current and pending GHG regulations, using a price of $xx/tonne of CO^2 steadily increasing to $xxx/tonne of CO^2 in 2040 as a base case, against a range of policy design options. The company expects that GHG emissions regulation will continue to evolve with a carbon price signal that balances economic, environmental and energy security objectives. The company will continue to review the impact of future carbon-constrained scenarios on its business strategy.

EXAMPLE THAT MET OUR EXPECTATIONS

Transition Risk - Reputational

Maintaining a positive reputation in the eyes of its customers, regulators, communities and the general public is an important aspect of the implementation of the company's business strategy. The company's reputation may be adversely impacted by the actions and activities it undertakes, as well as the activities of its employees.

In addition, the company's reputation could be affected by the actions and activities of other companies operating in the energy industry and by general public perceptions of the energy industry, over which the company has no control. For example, negative publicity related to pipeline incidents, unpopular expansion plans or new projects, transportation of hydrocarbons by rail, as well as opposition from organizations opposed to oil and gas, oil sands or pipeline development, all have the potential to affect the perception of the company by its stakeholders. The increasing debate and focus on climate change has contributed to increasing negative public sentiment toward the hydrocarbon-based energy sector and higher levels of scrutiny with respect to emissions and overall environmental performance. If the company's reputation is diminished, it could result in: loss of customers; revenue loss; delays in obtaining regulatory approvals with respect to growth projects; increased operating, capital, financing or regulatory costs; lower shareholder confidence; or loss of public support for the company's business and operations.

B. Adoption of IFRS 16 *Leases* (IFRS 16)

Effective for financial reporting periods beginning on or after January 1, 2019, RIs that comply with IFRS adopted the new leasing standard, IFRS 16. Adoption of this new accounting standard required considerable effort and significantly altered the financial statements of many RIs.

In March 2019, we published a Financial Reporting Bulletin on IFRS 16 to provide helpful and educational information for consideration by RIs and their advisors on the impact of adoption on NGMs. RIs in the oil and gas industry are also encouraged to review this publication in preparation of their oil and gas economic evaluation of reserves and resources post-adoption. The key message in this bulletin is that the best estimates of future capital and operating costs in the oil and gas evaluation will continue to include forecasted expenditures on leased assets associated with oil and gas properties regardless of on-balance sheet classification of the right-of-use asset. Omitting these costs in the oil and gas evaluation may have broader implications in the RIs reserves report and valuation of its oil and gas properties in its financial statements.

C. MI 61-101 *Protection of Minority Security Holders in Special Transactions* (MI 61-101) and related party transactions in general

MI 61-101 imposes enhanced requirements to protect the interests of equity security holders against potential conflicts of interest that may arise when an RI participates in certain transactions. Depending on the transaction, these requirements may include additional disclosure requirements, formal independent valuations, majority of the minority security holder approval (**Minority Approval**) or consideration of the bid by an independent committee of the board. MI 61-101 applies to RIs, and the provisions respecting insider bids and issuer bids also apply to issuers that are not RIs. The types of transactions covered by MI 61-101 (and the associated enhanced requirements it imposes) include:

- insider bids, which are take-over bids made by certain parties such as a director, senior officer or 10 per cent security holder of an RI (enhanced disclosure, formal valuation, special committee).
- issuer bids, which are offers by an RI to buy back its own securities (enhanced disclosure, formal valuation).
- business combinations, which are defined to include certain transactions such as stock consolidations, amendments to the terms of equity securities, amalgamations, plans of arrangement and other transactions where the interest of an equity security holder may be cancelled without their consent, if a related party is involved and receives preferential treatment (enhanced disclosure, formal valuation and Minority Approval).
- related party transactions, which are defined to include certain transactions involving a related party, such as a sale, lease or acquisition of an asset; the release, forgiveness, assumption or amendment of a liability; the borrowing of money; or the providing of a guarantee (enhanced disclosure, formal valuation and Minority Approval).

MI 61-101 contains a number of exemptions from the valuation and Minority Approval requirements. For example, an RI engaging in a related party transaction is exempt from the formal valuation requirement where it is insolvent or in serious financial difficulty. An RI is similarly exempt if the fair market value of the asset being acquired, or the consideration paid to related parties is not more than 25 per cent of the RI's market capitalization. Valuation exemptions are also available to venture issuers[10].

We have conducted real-time reviews of transactions to assess compliance with MI 61-101 since it was adopted in Alberta in 2017. We also assess compliance through our CD review program.

10 Venture issuer, as that term is defined in section 1.1 of NI 51-102.

To date, most MI 61-101 issues have arisen in the context of private placements where a director, senior officer or insider subscribes for shares. The most common deficiencies we have noted include:

- in news releases and MCRs, failure to state the Minority Approval and valuation exemptions that were relied on and the facts supporting such reliance.
- in MCRs, the failure to include:
  - a discussion of the review and approval process adopted by the board of directors or special committee for the transaction.
  - a description of the interest in the transaction of every interested party and of the related parties and associated entities of the interested parties.

Staff have also noted issues with respect to disclosure of the background to and approval process for a transaction, including:

- inadequate disclosure of the context and background to a proposed transaction.
- failure to provide a meaningful discussion of the board's or special committee's process and their rationale for supporting a proposed transaction.
- failure to provide disclosure of dissenting views of directors in respect of a transaction.
- overly one-sided disclosure regarding a recommended transaction that does not identify potential concerns with the transaction or available alternatives to the transaction.

RELATED PARTY TRANSACTIONS GENERALLY

The application of MI 61-101 is limited to related party transactions as defined in that instrument. Although the definition of related party transaction in MI 61-101 is broad, it is not exhaustive, and as discussed above, the instrument contains certain exemptions for transactions which do fall within the definition. Even if the related party transaction is not subject to MI 61-101, transactions that involve related parties require special consideration and attention. While a related party transaction may be pursued for valid business purposes and provide significant benefits for an RI, the inherent potential for conflict of interest remains, and RIs should ensure that their disclosure alerts investors to the potential conflict and outlines any steps the RI is taking to manage conflicts of interest. Other securities legislation imposes additional requirements in this regard. For example, item 6 of Form 62-104F1 *Take-Over Bid Circular* requires the disclosure of target company securities owned by the offeror and its directors, officers and insiders and their respective associates and affiliates. Similarly, item 5 of Form 51-102F5 *Information Circular* requires the disclosure of any interest of certain persons or companies in matters to be acted upon. RIs should also ensure their financial statement and MD&A disclosure in this regard is complete.

Most issues we have identified in relation to related party transactions have arisen in relation to smaller RIs, which are more likely to have control persons or other large shareholders which are potential "related parties" in the context of a transaction involving an RI. We encourage RIs contemplating transactions directly or indirectly involving a potential related party to seek advice regarding the requirements of corporate and securities legislation in this regard, and to reach out to us with specific inquiries.

PRACTICE TIPS

- RIs should implement a comprehensive process for identifying and dealing with related party transactions and conflicts of interest, including conflicts of the type regulated by MI 61-101, and disclose details of that process.
- Although MI 61-101 only requires the active involvement of a committee of independent directors in evaluating a transaction and potential alternatives in the context of insider bids, RIs frequently establish an independent committee to consider other types of business combinations or strategic transactions, and we believe that such committees facilitate good corporate governance and a full consideration of available strategic alternatives.
- The independent committee should retain and supervise a financial advisor to provide a valuation or fairness opinion and ensure that the RI provides meaningful disclosure of that valuation or fairness opinion.
- Even if a related party transaction is not subject to MI 61-101, disclosure of related party transactions should be reviewed.

D. Early warning reporting requirements

The early warning reporting system is intended to inform the marketplace of actions taken by security holders who have beneficial ownership of, or control or direction over, 10 per cent or more of any class of securities[11] of an RI. When a security holder's actions (acquisition or disposition of securities) trigger reporting requirements they are required to inform the marketplace by:

- issuing and filing a news release no later than the opening of trading on the business day following the event; and
- filing Form 62-103F1 *Required Disclosure under the Early Warning Requirements* (**Form 62-103F1**), no later than two business days following the event.

We have encountered a number of instances where security holders did not fulfill their reporting obligations, and we have also received a number of inquiries from security holders on their reporting requirements. The questions below represent the most common areas requiring clarification:

1. **When are my filing obligations triggered?**[12]
   - **10 per cent ownership**: An acquisition of securities that increases your ownership to 10 per cent or more of the outstanding securities of that class.
   - **Change of +/- 2 per cent or more in ownership**: An acquisition or disposition of securities that results in a 2 per cent or greater increase or decrease in the ownership percentage reflected in your most recent report; for example, a change in your ownership percentage from 13.2 per cent to 11.2 per cent or less, or 15.2 per cent or more.
   - **Change in a material fact**: There is a change in a material fact in your most recently filed Form 62-103F1.

2. **When do my filing obligations end?**

   A security holder's early warning reporting obligation ends when its ownership percentage falls below the 10 per cent reporting threshold and to announce this, a news release and early warning report is filed under subsection 5.2(3) of National Instrument 62-104 *Take-Over Bids and Issuer Bids* (**NI 62-104**). In such circumstances, you are not required to report any further changes unless you regain at least 10 per cent ownership.

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11 In determining their ownership interest, security holders must consider securities that they have beneficial ownership of, or control or direction over and securities convertible into voting or equity securities of that same class.

12 Note that the reporting requirements differ for eligible institutional investors who choose to report under the alternative monthly reporting system. Refer to Part 4 of National Instrument 62-103 *The Early Warning System and Related Take-Over Bid and Insider Reporting Issues* for additional information.

3. **My ownership percentage decreased because the RI issued additional securities. Are my filing requirements triggered?**

   No. Filing requirements are only triggered by actions taken by the security holder, not the RI.[13] However, the next time you make an acquisition or disposition of securities you will need to consider any changes to the overall number of the RI's outstanding securities in your ownership percentage calculation to determine if any filing requirements have been triggered.

4. **I am contemplating an acquisition of outstanding voting or equity securities of an RI that will increase my proportionate ownership of such securities to 20 per cent or more; what now?**

   We recommend that you consult with legal counsel before offering to purchase such securities as your offer will subject you to the take-over bid regime governed by National Instrument 62-103 *The Early Warning System and Related Take-Over Bid and Insider Reporting Issues* and NI 62-104.

5. **I still have questions! What resources are available?**

   Additional questions on how to file these reports can be directed towards our SEDAR/SEDI hotline at: 403-297-2489 or sedar.sedi@asc.ca. Any questions on the early warning report filing requirements can be directed to our inquiries line at: 403-355-4151 or inquiries@asc.ca.

PRACTICE TIP

Reporting insiders are required to report any changes in their beneficial ownership/interest/control/direction over securities in SEDI within five days following the transaction.

4. Offering documents

A. New listings — capital structure

The decision to file a prospectus for an IPO and become an RI is a significant step and, wherever possible, we want to add certainty to the process.

Issuers seeking to become RIs and their advisors are encouraged to review CSA Staff Notice 41-305 *Share Structure Issues – Initial Public Offerings*.

We understand that the evolution of an early-stage business typically involves the founders and early investors of an issuer investing at lower prices and increasing the value of the issuer's shares as the business develops. This is generally not an issue. However, an IPO by a issuer that has an unusually large number of shares outstanding, issued for nominal cash consideration (or for assets or business development where the value is not readily supportable) may raise public interest concerns related to the issuer's capital structure. These concerns are heightened when the business has a limited history of operations or development for which there are no other clear proxies for valuation and the IPO financing is relatively small. We are concerned with these structures because the large number of nominally priced shares can create a platform for future market manipulation, and the dilution of invested capital caused by existing shares issued for nominal amounts means that IPO investors receive an unconscionably low percentage of ownership compared to the amount of capital they are investing.

Although some Canadian stock exchanges have published guidelines to address at least some of these issues, we still

13 Part 6 of NI 62-103.

encounter them from time to time and accordingly, issuers should note that we may raise comments or object to an issuer's share structure.

We would be pleased to discuss the proposed capital structure of a prospective issuer in advance of a prospectus offering.

B. Restricted securities

Restricted securities are equity securities that carry restricted voting rights or a lower number of votes per share, or that are entitled to more limited participation in the earnings or assets of an issuer than another class of equity securities. Securities legislation imposes additional disclosure requirements in relation to such securities, to ensure that security holders are aware of these limitations. An issuer with restricted securities outstanding, proposed to be offered under a prospectus, or securities that may be converted into or exchanged or exercised for restricted securities, should include a detailed description of:

- the voting rights attached to the restricted securities and the voting rights, if any, attached to the securities of any other class of securities of the issuer that are the same as or greater than, on a per security basis, those attached to the restricted securities.
- any significant provisions under applicable corporate and securities law that do not apply to the holders of the restricted securities, but do apply to the holders of another class of equity securities, and the extent of any rights provided in the constating documents (typically, the issuer's articles of incorporation and bylaws, declaration of trust, or similar organizing document) or otherwise for the protection of holders of the restricted securities.
- any rights under applicable corporate law, in the constating documents or otherwise, of holders of restricted securities to attend, in person or by proxy, meetings of holders of equity securities of the issuer and to speak at the meetings to the same extent that holders of equity securities are entitled.
- how the issuer complied with, or the basis upon which it was exempt from, the requirements of Part 12 of National Instrument 41-101 *General Prospectus Requirements*, including:
  - the use of an appropriate restricted security term, such as not including the word "common", "preference" or "preferred", unless certain conditions are met.
  - not filing a prospectus under which restricted securities, subject securities[14] or securities that are, directly or indirectly, convertible into, or exercisable or exchangeable for, restricted securities or subject securities, are distributed, unless certain exemptions apply.

PRACTICE TIP

To determine if the restricted security disclosure requirements apply to you, consider if any of the following apply:

- Another class of securities appears to carry a greater number of votes per security relative to the equity security.
- Conditions attached to the class of equity securities, the conditions attached to another class of securities of the issuer, or the issuer's constating documents have provisions that nullify or appear to significantly restrict the voting rights of the equity securities.
- Another class of equity securities that appears to entitle the owners of securities of that other class to participate in the earnings or assets of the issuer to a greater extent, on a per security basis, than the owners of the first class of equity securities.

14 Subject security means a security that results, or would result if and when issued, in an existing class of securities being considered restricted securities.

5. Important staff notices and initiatives

NOTICE	DESCRIPTION	DATE OF PUBLICATION
CSA Notice and Request for Comment - Proposed Amendments to National Instrument 52-108 *Auditor Oversight* and Proposed Changes to Companion Policy 52-108 *Auditor Oversight*	Request for public comment on proposed amendments in response to challenges the Canadian Public Accountability Board has had in obtaining access to inspect audit work performed by an audit firm in a foreign jurisdiction that forms part of the audit evidence supporting an auditors' report issued by a participating audit firm. The comment period expires January 2, 2020.	October 3, 2019
CSA Multilateral Staff Notice 58-311 *Report on Fifth Staff Review of Disclosure Regarding Women on Boards and in Executive Officer Positions*	Outlines key trends and observations from reviews of disclosure regarding women on boards and in executive officer positions.	October 2, 2019
CSA Notice and Request for Comment - Proposed Amendments to National Instrument 51-102 *Continuous Disclosure Obligations* and Changes to Certain Policies Related to the Business Acquisition Report Requirements	Request for public comment on proposed BAR amendments. Key proposed amendments include: • Altering the determination of significance for Non-Venture RIs such that an acquisition of a business or related businesses is a significant acquisition only if at least two of the three existing significance tests are triggered. • Increasing the significance test threshold for Non-Venture RIs from 20 per cent to 30 per cent. The comment period expired on December 4, 2019.	September 5, 2019
CSA Staff Notice 51-358 *Reporting of Climate Change-related Risks*	Reinforces and expands upon the guidance provided in SN 51-333 *Environmental Reporting Guidance*, which continues to provide guidance to RIs on existing CD requirements relating to a broad range of environmental matters, including climate change.	August 1, 2019
Office of the Chief Accountant Financial Reporting Bulletin: *Adoption of IFRS 16: Non-GAAP Financial Measures and Reserves Reporting Considerations*	Brings attention to two matters that have arisen on adoption of IFRS 16 *Leases*: • How to report changes in NGMs. • Cost estimates in oil and gas evaluations.	March 2019

6. Resources Available

Listed below are some commonly used regulations to assist RIs in understanding the requirements and where to find them. In the online version of this report, this list provides links directly to our website.

To keep up-to-date on recent and upcoming changes, please subscribe to our updates[15] or follow us on Twitter @ASCUpdates.

Continuous Disclosure Rules	NI 51-102
Financial Statements	Part 4
Forward-Looking Information	Part 4A & 4B
MD&A	Part 5
Business Acquisitions	Part 8
Material Contracts	Part 12
Continuous Disclosure Forms	
MD&A	Form 51-102F1
AIF	Form 51-102F2
BAR	Form 51-102F4
Executive Compensation Non-Venture Issuers	Form 51-102F6
Executive Compensation Venture Issuers	Form 51-102F6V
Interpretation and Guidance	
Understanding Interpretations of the NI 51-102 Rules	51-102CP
Disclosure Standards	NP 51-201
Non-GAAP Financial Measures	SN 52-306 (Revised)
Environmental Reporting Guidance	SN 51-333
Report on Climate Change-Related Disclosure Project	SN 51-354
Corporate Governance Guidelines	NP 58-201
Corporate Governance	
Audit Committee Rules	NI 52-110
Non-Venture Issuers	Form 52-110F1
Venture Issuers	Form 52-110F2
Corporate Governance Disclosure	NI 58-101
Non-Venture Issuers	Form 58-101F1
Venture Issuers	Form 58-101F2
Certification of Disclosure	NI 52-109

15 https://www.albertasecurities.com/news-and-publications/weekly-updates-web-page

7. Contact personnel and other information

FEEDBACK ON THE REPORT AND OTHER CORPORATE FINANCE MATTERS

We welcome comments on this Report, consultations or pre-filings and other Corporate Finance matters. Comments may be directed to any of the individuals listed below:

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GLOSSARY OF TERMS

The following terms have the meanings set forth below unless otherwise indicated. Words importing the singular number include the plural, and vice versa.

"**AIF**" means Annual Information Form, specifically, a completed Form 51-102F2 *Annual Information Form* (**Form 51-102F2**).

"**BAR**" means Business Acquisition Report; specifically, a completed Form 51-102F4 *Business Acquisition Report* (**Form 51-102F4**).

"**CD**" means continuous disclosure.

"**CSA**" means the Canadian Securities Administrators.

"**FLI**" means Forward-looking Information, as that term is defined in National Instrument 51-102 *Continuous Disclosure Obligations* (**NI 51-102**).

"**GAAP**" means generally accepted accounting principles.

"**IPO**" means an initial public offering.

"**Issuer**" - Sections 1(cc) and 1(ccc) of the *Securities Act* (Alberta) provide the definition of issuer and reporting issuer (**RI**) respectively. Although most of this report is directed towards Alberta RIs, certain securities legislation addressed in this report applies to all issuers including RIs, in these instances "issuer" has a specific meaning in application and reference. The report refers to RI unless use of the term issuer is necessary to make the distinction.

"**MCR**" means Material Change Report, specifically, a completed Form 51-102F3 *Material Change Report* (**Form 51-102F3**).

"**MD&A**" means Management's Discussion and Analysis, specifically, a completed Form 51-102F1 *Management's Discussion & Analysis* (**Form 51-102F1**).

"**SEDAR**" has the same meaning as in National Instrument 13-101 *System for Electronic Document Analysis and Retrieval*.

"**SEDI**" means System for Electronic Disclosure by Insiders.

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