

2010 Oversight Review
TSX Venture Exchange Inc.

2010
Review

Alberta
Securities
Commission

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1.0 Overview

The TSX Venture Exchange Inc. (“TSXV” or “the Exchange”) is recognized as an exchange in Alberta pursuant to section 62 of the *Securities Act* (Alberta) (the “Act”). The TSXV operates under a Recognition Order, dated August 12, 2005¹ (“*Recognition Order*”). Authority for periodic oversight review is derived from section 58 of the Act.

The Lead Regulators for the TSXV are the Alberta Securities Commission (“ASC”) and the British Columbia Securities Commission (“BCSC”), acting jointly. Accordingly, the oversight review was structured by designating each Lead Regulator specific program review responsibilities as defined in the *Joint Regulatory Oversight of CDNX² by the ASC and BCSC* letter dated November 26, 1999 from the Chairs of the ASC and BCSC to the CEO of CDNX (“*Joint Oversight Letter*”). ASC staff is responsible for oversight of the Corporate Finance, Corporate Governance and Risk Management areas of TSXV’s operations. The *Joint Oversight Letter* lays out BCSC’s oversight areas as: Trading, Compliance, Systems and Clearing and Settlement. This report encompasses only the ASC’s findings. The BCSC will issue a separate report on their findings and recommendations.

The TSXV oversight review fulfills a part of the ASC’s oversight responsibilities as agreed in the *Memorandum of Understanding respecting the Oversight of Exchanges and Quotation and Trade Reporting Systems*, effective January 1, 2010.

The ASC review covered the period from January 1, 2005 to September 30, 2009.

ASC staff’s objective was to ensure that terms of the Recognition Order were met throughout the review period. As part of field work procedures, ASC conducted extensive interviews with senior management and staff, undertook an in-depth review of TSXV processes and performed detailed file testing to confirm that TSXV’s controls were operating effectively during the review period.

ASC staff did not find instances of material non-compliance with established corporate policies. Findings raised and recommendations made in this report relate to TSXV processes that in ASC’s view should be reviewed on an ongoing basis to ensure adequate control processes are in place. Certain instances where established processes were not followed or where process enhancement could be made have been raised below. Processes that ASC staff determined to be operating effectively are not discussed in this report.

¹ A Variation Order effective June 1, 2008 was signed to change the reference to “Market Regulation Services Inc” to “Investment Industry Regulatory Organization of Canada”.

² CDNX is the predecessor entity of TSXV.

Overall, ASC staff are satisfied with the processes that have been implemented at the Exchange and have not identified any material breaches of the Recognition Order. The findings raised in this report represent gaps in the control environment of the Exchange that can be addressed by process enhancement. Addressing the findings identified and implementing suggested process revisions will ensure that TSXV's control environment meets ongoing regulatory requirements as the exchange continues to grow in a rapidly changing marketplace.

2.0 Key Finding and Recommendations

2.1 Corporate Finance

2.1.1 Waivers to Corporate Finance Policies

The Executive Listings Committee ("ELC") is made up of Directors and Team Managers from the Listed Issuer Services ("LIS") offices based in Calgary, Vancouver, Montreal and Toronto and is responsible for considering whether an application for listing meets the requirements of the Corporate Finance Policies ("CFP"). LIS makes the final decision to list an issuer. An ELC memo is prepared for review by the Team Manager and /or Director of the local office by the Manager or Analyst that reviews a listing application. The ELC memo is a document that includes information on how the application meets the CFP. The ELC has established an approval process that has distinct levels of discretionary decision-making ability based on the type of policy waivers which may be required by the application and the assessed risk of the listing being applied for. Using this decision model, an application is either approved or the Manager or Analyst is requested to provide more information to allow the ELC to arrive at a decision.

In reviewing applications, TSXV staff has the ability to waive certain CFP requirements, for example, requirements for escrow arrangements, sponsorship, and disclosure requirements. The TSXV has as part of its review process established a structured approval model which outlines the discretionary authority staff at various levels (Analyst, Manager, Team Lead, Director) has to grant different types of waivers to CFP requirements. This discretionary approval model has been approved by ELC. ASC staff identified that when a waiver is judged by TSXV staff to be "non-significant," the process established by TSXV is such waivers

made in accordance with its discretionary approval model are not always brought to the attention of ELC. Significance of a waiver is determined by TSXV staff using the guidance provided in Appendix C of the Corporate Finance Oversight Framework³ and Appendix B of the CPC Operating Agreement.

Recommendations

ASC staff recommends that to ensure for completeness of file documentation, the TSXV revise its processes so that instances where TSXV staff waive CFP requirements, even where such waivers are determined to be insignificant and in accordance with the discretionary approval model, those waivers are listed in the ELC memo. Doing so will ensure that waivers granted to issuers are documented and that ELC is provided with complete details of the listing application. Implementing this recommendation will ensure that the processes will be applied consistently.

2.1.2 Review Process

ASC staff reviewed the operational control environment of LIS. The goals of this review were to assess the controls that were in place during the review period, to ensure that Exchange staff were undertaking their review of applications with sufficient quality and consistency, and to confirm that the controls documentation adequately reflected the underlying filings by issuers across Canada. ASC identified the following areas where the operational control processes could be refined to ensure quality control in LIS.

(a) Filing Applications

ASC staff identified that the review process for filing applications by TSXV staff was not always consistent in approach between two TSXV offices. Specifically, this occurred in Analysts' review of stock option plan filings. While CFP requirements were adhered to by both offices, the minimum CFP requirements were requested from issuers by TSXV staff in one office and additional information

³ This is draft document that TSXV staff, the ASC and BCSC has been operating under that outlines the procedures for oversight of corporate finance activities of TSXV by the ASC and BCSC.

was required to be filed by issuers dealing with TSXV staff at another office.

In addition, ASC staff found that there appeared to be no standard internal process for reviewing filing applications, other than each Analyst's interpretation of the CFPs. There were two instances in the sample reviewed where ASC staff could not determine that a critical review process had been carried out by TSXV staff due to a lack of documented analysis in the file.

ASC staff also noted that Analysts were responsible for review and approval of filing applications, issuing bulletins and handling file completion without a secondary or quality assurance (QA) review process. Managerial input is sought at the Analyst's discretion and is not required by the review process. Managers do not review completed files, and do not, as a matter of course, review public bulletins. Based on this information, ASC staff determined that LIS may not apply a structured QA process for filing applications.

(b) Listing Applications

ASC staff identified that TSXV's listing application approval process should capture instances where TSXV staff do not receive all required listing application documentation. All missing documents, whether based on waivers granted in accordance with the discretionary approval model or through inadvertence, should be flagged in ELC memos. ASC staff understand that TSXV has created checklists for use by TSXV staff in review of listing applications and recommend that these checklists must be updated frequently to ensure they are current.

ASC staff has also identified that the ELC listing approval process is based solely on the information provided in the ELC memo. ASC staff therefore note that it is an important quality control measure that ELC verify that all information pertinent to a listing application is set out in detail in the ELC. This could be achieved by ELC performing periodic comparisons of an ELC memo to the listing file materials, or engaging in a discussion among the Team Manager/Director and the Analyst tasked with review of the listing application would ensure that no information relevant to the listing

decision contained in the documents filed by the issuer is overlooked in the ELC memo.

Recommendations:

The use of a standard approach and standard documentation system for review of listing applications should be implemented for all Managers and Analysts involved in the listing process. This control measure would provide evidence that TSXV staff has carried out a complete and consistent review of listing applications and ensures that TSXV staff fully evaluate whether the listing application meets CFP requirements. Further, compliance with this approach will provide the TSXV with information to support the denial of an application where this is appropriate.

ASC staff recommends that TSXV implement a structured QA process for its filing and listing applications. A QA process could consist of post-approval managerial review on a sample of files, independent review by TMX Group internal audit or a similar process. The results of a quality assurance process can be used to identify areas in which to improve staff training and to revise established processes to ensure consistency amongst similar application types and between TSXV offices.

2.2 Business Continuity and Risk Management

2.2.1 Local Servers

Data for LIS and Compliance and Disclosure is maintained on servers in the TSXV local offices. ASC staff requested written documentation on the process for electronic back-up and storage of this information, including if the data was assessed by TSXV or TMX Group staff as critical as well as the rationale behind the different back-up processes.

Although TMX Group and TSXV staff confirmed the data being backed-up was important historical information that is regularly accessed by LIS and Compliance and Disclosure staff, rationale for the back-up processes implemented could not be explained. These were identified as inherited legacy processes that do not appear to have been documented or recently reviewed.

Recommendations

TSXV staff should review back-up processes at least annually, consider whether there is need for consistency between local offices and document, where appropriate, the back-up process that addresses the risk of critical data being lost and the possible impairment of the functioning of the Exchange.

2.2.2 Business continuity processes and documentation

TSXV staff and TMX Group staff advised ASC staff that the business continuity process is managed at the TMX Group level. However, documented TMX Group business continuity processes require local TSXV staff to be responsible for quarterly updating of the business continuity plan for each local office. Additionally, documented TMX Group business continuity processes include an annual requirement for the most senior management team member to review and attest to the accuracy of the business continuity plan at each TSXV local office. ASC staff identified that during the review period Vancouver LIS senior management did not complete the annual attestation of the Vancouver office business continuity plan; and in Toronto and Montreal the annual business continuity plan attestation for the respective LIS departments was completed by TSXV staff rather than senior management, which is not in compliance with TMX Group policies.

ASC staff identified that information on the business continuity plan for the Vancouver office was out of date.

Recommendations

TSXV staff should ensure business continuity plan documentation is kept up to date and the processes that have been implemented by TSXV and the TMX Group for attesting to the accuracy of the business continuity plan are followed.