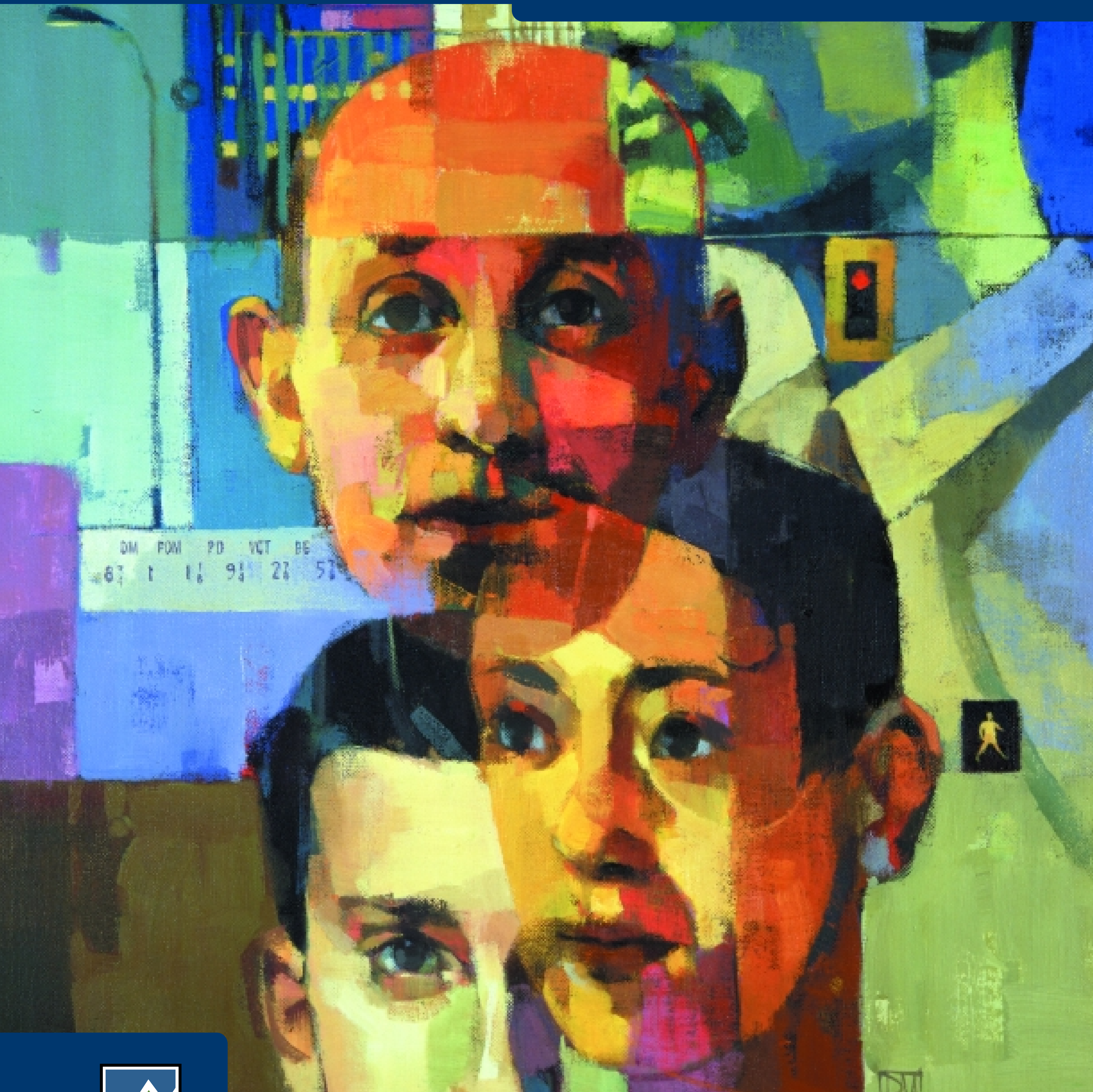
CONTINUOUS DISCLOSURE REVIEW PROGRAM

staff report | april 2000



BCSC

BRITISH COLUMBIA SECURITIES COMMISSION

TABLE OF CONTENTS

INTRODUCTION

This report provides an overview of key issues identified by staff of the British Columbia Securities Commission (the "Commission") during its review of the public disclosure provided by 48 development stage reporting issuers. The report identifies common disclosure problems and attempts to clarify the nature and extent of disclosure that is required to comply with the statutory disclosure requirements.

Directors and officers are encouraged to review the disclosure record of the reporting issuers they manage in light of the information contained in this report. Where necessary, appropriate measures should be taken to ensure that the disclosure record of those issuers complies with the regulatory requirements discussed in the report.

SUMMARY OF FINDINGS

Results of the current review suggest that a number of reporting issuers are not providing shareholders and the market with complete, accurate, timely and balanced disclosure. In particular, the quality and extent of Management Discussion and Analysis (MD&A) provided in Schedule C of Form 61 Quarterly Reports and Annual Information Forms (AIF) required under blanket order BOR#98/7 for the System for Shorter Hold Periods with an AIF (SHAIF) is generally deficient. Many of the problems associated with poor MD&A disclosure in Schedule C were previously identified by staff in NIN#96/38 published in October 1996 (see Appendix A).

In addition to the problems associated with poor MD&A disclosure, the review identified a number of other disclosure-related problems including the following:

- Several issuers completing prospectus distributions experienced a significant decline in their existing working capital subsequent to the receipt of the prospectus but prior to completion of the distribution. In some cases, the issuer faced liquidity problems sooner than might otherwise have been anticipated by investors, calling into question whether the issuer should have filed an amendment to its prospectus.

- Issuers completing public offerings frequently failed to compare actual expenditures to those budgeted in the prospectus and explain material variances between the two, and discuss the impact of those variances on the issuer's ability to achieve milestones and objectives disclosed in the issuer's prospectus.

- A number of issuers did not comply with the SHAIF AIF requirements.

- Impairments in assets were not always recognized in the financial statements (F/S) on a timely basis.

Benefit

The report will assist issuers, primarily *development stage issuers*, their directors, officers and professional advisers in complying with the reporting requirements. The report is intended to assist issuers in achieving and maintaining a high standard of public disclosure and to help them avoid the consequences associated with filing continuous disclosure materials that are found to be materially deficient.

Common Problem

Eight out of ten issuers recently reviewed were placed on the Commission's Issuers in Default list. In addition, the disclosure of four of these issuers was considered to be so deficient that the right of those issuers to offer purchasers of their securities the shorter hold period under SHAIF was rescinded by the Executive Director until the deficiencies had been resolved.

Example

If an issuer disclosed significant revenues that were expected to be generated from a recently signed contract but failed to disclose the material costs and obligations associated with fulfilling the contract, the issuer's disclosure record would not be complete. The omission of this information would likely constitute a misrepresentation as defined in Section 1 of the *Securities Act.*

Example

Publicly announced negative exploration results combined with a prolonged period of inactivity on an issuer's resource property may indicate that an impairment has occurred in the value of the property which should be communicated to investors and the marketplace by way of a write-down of the property in the issuer's F/S.

- Significant solvency problems were not fully discussed in interim and annual MD&A, including management's plans for managing or correcting these problems.
- Expenditures, whether capitalized or expensed, were not always broken down in accordance with Rule 3(9)(b) of the *Securities Rules* in annual and interim F/S filings.
- Incorrect use of the term "deemed value" to describe the value assigned to non-monetary transactions for accounting purposes contrary to Generally Accepted Accounting Principles (GAAP).
- Inadequate note disclosure in interim F/S.
- Form 27 reports (Material Change Report) not prepared in the required form.
- Incomplete disclosure in Schedule B of Form 61 with respect to warrants and options granted during the reporting period.
- Promotional and stale-dated information in issuer websites.

THE REVIEW PROCESS

In a comprehensive review staff assess the public disclosure record of selected issuers for the purpose of determining whether such disclosure is:

Complete – All facts that are material to a particular event or transaction are fully disclosed.

Accurate – Disclosure is factual and internally consistent – an issuer's MD&A must be supported by, and be consistent with the issuer's F/S and vice versa.

Timely – Information that is material must be conveyed to investors without delay. News releases must be published as soon as practicable and Material Change Reports must be filed within ten days of a material change occurring in accordance with Section 85 of the *Securities Act.*

Balanced – Disclosure must not accentuate the "practicable" aspects of an issuer's business while ignoring the negative and should not contain information that is not factual (promotional).

The review process does not constitute an audit and it is not intended to second guess management's business decisions. However, an important part of the review process is to identify significant transactions and events in an issuer's disclosure record that may have a *material impact* on the issuer's reported financial results and, where not otherwise self-evident, request that the issuer clarify the disclosure relating to the transaction or event.

A continuous disclosure review is focused on selected components of an issuer's disclosure record including the issuer's interim and annual Form 61 report filings, Annual Reports, Material Change Reports, press releases, websites and, where applicable, SHAIF AIFs, filed or published during a pre-determined period (usually 12–24 months). Staff may also review insider trading reports.

In addition, where an issuer has recently completed a public offering, the review will include a comparison of how monies were actually spent by the issuer to how they were supposed to be spent (as disclosed in the issuer's offering document).

This part of the review is intended to determine whether or not the issuer is following the business plan disclosed in its prospectus, that it is doing so within the timeframes and budgets disclosed in the prospectus, and that it is providing an adequate explanation for any variances to its shareholders as required by the instructions to Schedule C of Form 61 and as discussed in Item 3 of NIN #96/38.

RESULTS OF CURRENT REVIEW

The following section sets out a number of the disclosure deficiencies identified during the review:

I. PROSPECTUS DISCLOSURE – MATERIAL CHANGE IN WORKING CAPITAL

Prospectus Forms 12A, 12B, 14A and 14B require issuers to disclose existing working capital on hand in the Use of Proceeds section of the prospectus. These funds are added to the funds being raised to present information to investors regarding the total funds available to the issuer on completion of the offering.

Issuers are reminded of the requirement in Section 67(1) of the *Securities Act* to amend a prospectus in the event that a *material change* occurs in the affairs of the issuer prior to the completion of a distribution. Even if the prospectus form does not require the disclosure of current working capital, a material decline in an issuer's working capital during the course of a distribution may constitute a material change requiring the filing of an amendment.

Problem

In some of the cases reviewed by staff, issuers experienced a material decline in working capital subsequent to the date of the final prospectus but prior to completion of the distribution. In one case this decline represented approximately 40% of the net funds being raised and resulted in the issuer being unable to achieve the milestones disclosed in its prospectus. In several cases the decline in working capital resulted in issuers experiencing significant liquidity problems shortly after they completed their offerings.

II. FORM 61 REVIEW

1. AUDITED ANNUAL FINANCIAL STATEMENTS

1.1 Rule 3(9)(b) of the Securities Rules – breakdown of significant expenditures

It appears some issuers may not be aware of the requirement in Rule 3(9)(b) for *development stage issuers* to include a breakdown of significant expenditures, whether capitalized or deferred, within the body of the F/S or in a supporting note or schedule to the F/S. It is important that this breakdown be included in the F/S and that at the end of the issuer's financial year the information is subject to audit. Item 6(b) of NIN #96/38 discusses the level of expenditure that is considered significant.

Recommendation

While not required by Rule 3(9)(b), junior industrial issuers are encouraged to provide an analysis of their research and development expenditures, whether capitalized or expensed, on a *major project-by-project basis* in both the annual and interim F/S to facilitate a shareholder's understanding of how funds were spent by the issuer.

Staff also recommend that research and development expenditures be presented separately from general and administration expenditures in the F/S of such issuers. This form of F/S presentation should also make it easier for issuers to provide a meaningful discussion of expenditures in the related MD&A section of their Form 61 report and SHAIF AIF.

Other reporting issuers (i.e., issuers other than *development stage issuers*) required to file a Form 61 report must provide similar information in Schedule B of Form 61 if the information is not already included in the F/S. Such issuers are encouraged to include this information in their F/S.

1.2 *Presentation of costs on a property-by-property or project-by-project basis*

Several issuers failed to provide a breakdown of their total exploration costs on a *major* property-by-property basis as required by Rule 3(9)(b).

Issuers are encouraged to present property acquisition costs separately from exploration costs in the F/S on a historical basis to assist shareholders in better understanding the magnitude of each category of expenditure relative to the total expenditures on a particular property.

1.3 *Revenues reported by development-stage issuers*

Some issuers presented incidental revenues generated during the development stage as *Revenue from operations* rather than as a reduction of related deferred development or pre-operating costs in accordance with the Canadian Institute of Chartered Accountants' (CICA) Accounting Guideline #11 (Enterprises in the development stage).

1.4 *Non-monetary transactions*

Staff noted the term *deemed value* used on occasion to describe the value used for accounting purposes to record a transaction involving the issuance of shares by an issuer in exchange for an asset of indeterminate value. Section 3830.05 of the CICA Handbook states that such transactions should be recorded at the fair value of the consideration given up, that being the issuer's shares, unless the fair value of the asset acquired is more clearly determinable.

In a venture capital market the current trading price of an issuer's stock may not be indicative of the stock's fair value because the stock may not be actively traded and liquid. Similarly, the deemed value at which a stock exchange or other regulator may approve the issuance of shares in connection with a non-monetary transaction may not be representative of the fair value of those shares for accounting purposes.

Where neither the fair value of the shares given up nor the asset being acquired can be easily determined, staff suggest that the issuer should consider the vendor's net book value of the asset being acquired in estimating the fair value of the asset. In the event that this information is not available to the issuer or, alternatively, it is not considered to be representative of the fair value of the asset, staff suggest that the issuer consider whether or not the fair value of the asset being acquired is nominal.

Issuers should disclose the basis used to determine the value they have assigned to such transactions. Referring simply to a deemed value is not informative and it is likely to invite further inquiry from staff.

1.5 Financial instruments

In 1995 the CICA introduced Handbook Section 3860 (Financial Instruments), applicable to fiscal years beginning on or after January 1, 1996. While this section has been in effect for four years, several instances of non-compliance with the section were noted including the failure by issuers to disclose information regarding certain of the risk factors disclosed in Section 3860.44.

1.6 Going concern disclosure

Section 1000 of the CICA Handbook states that F/S are prepared on the assumption that an entity is a going concern, meaning it will continue operating for the foreseeable future and will be able to realize assets and discharge liabilities in the normal course of operations. Staff noted several instances where issuers failed to provide adequate cautionary note disclosure regarding the issuer's ability to conduct business as a going concern. This typically arose where the issuer did not have a source of revenue and was dependent upon ongoing equity financing, extended credit from trade creditors, and/or loans from its principals to remain in operation.

Where an enterprise may be unable to continue realizing its assets and discharging its liabilities in the normal course of business, information contained in the F/S must explicitly draw the reader's attention to this possibility.

1.7 Classification of amounts "due to" and "due from" related parties

In several instances amounts *due from* related parties with no fixed terms of repayment were classified as *current* assets and in other instances amounts *due to* related parties with no fixed terms of repayment were classified as *non-current* liabilities. Unless the terms of repayment specify that an amount *due from* a related party will be received within one year from the date of the balance sheet or within the normal operating cycle, amounts due from related parties should be presented as *non-current* assets. Conversely, unless the terms of repayment specify that an amount *due to* a related party will not be repaid within one year from the date of the balance sheet or the normal operating cycle, amounts due to related parties should be presented as *current* liabilities.

1.8 Non-trade receivables

In several cases issuers with no significant revenues had material accounts receivable balances on their balance sheets and there was no explanation of the nature of the receivables in the supporting notes to the F/S. This presentation is not in accordance with Section 3020.01 of the CICA Handbook. This section requires that accounts and notes receivable should be segregated to separately show ordinary trade accounts, amounts owing by related parties, and other unusual items of substantial amounts.

Example

In one case information regarding the fair value of a material financial asset was not presented in the notes to the issuer's F/S. Given that the amount involved was a receivable due from a related party whose ability to repay the outstanding amount may have been in question, staff believe that expanded note disclosure regarding this amount should have been provided in accordance with Section 3860.78.

Definition

Section 1510 of the CICA Handbook defines *current assets* as those assets ordinarily realizable within one year from the date of the balance sheet or within the normal operating cycle, where that is longer than a year.

Section 1510 defines *current liabilities* as amounts payable within one year from the date of the balance sheet or within the normal operating cycle, where that is longer than a year.

1.9 Analysis of investment holdings

Pursuant to Rule 3(9)(a) development stage issuers are reminded that they are required to provide a detailed analysis of their investment holdings in the *annual F/S*.

This analysis must include:

- the name of each issuer whose securities are held;
- the class or designation of each security held;
- the number of each class of shares or aggregate face value of each class of other securities held;
- the cost and market value of each class of securities held; and
- the basis of valuation, if the carrying value is other than average cost.

1.10 RTO accounting: Prior operations – supplemental information

As discussed in NIN #91/21 (Accounting for Business Combinations and Corporate Reorganizations), when a reporting issuer has been taken over by another company through a reverse takeover (RTO), supplemental information regarding the reporting issuer's operations must be incorporated into the notes of the issuer's next annual audited consolidated F/S. The supplemental information must cover the period from the reporting issuer's most recently completed financial year end to the date of the RTO.

For a reporting issuer required to file a Form 61 report, the supplemental information relating to the reporting issuer's prior financial operations must include a statement of income or deficit, a schedule of deferred costs, if any, and a statement of cash flow. As an alternative, the reporting issuer may file a separate set of audited F/S for the period from the date of the most recent audited F/S filed with the Commission to the date of the RTO.

A significant increase in the number of RTO business combinations is expected as a result of the popularity of the Canadian Venture Exchange's Capital Pool Company program. Given that a large number of the *material transactions* that occur in connection with this program represent RTO business combinations, staff will be reviewing a sample of annual F/S filings to assess whether or not issuers are providing the required supplementary information.

2. QUARTERLY FINANCIAL STATEMENTS

2.1 Breakdown of expenditures

The level of non-compliance with the requirements of Rule 3(9)(b) in interim F/S filings was higher than with annual F/S filings. Issuers are reminded that this requirement applies to annual *and* interim F/S filings.

2.2 Asset impairment

In a few cases issuers were required to restate their quarterly F/S to recognize *significant* asset impairments that had occurred during the interim reporting period.

Example

In one instance, subsequent to its most recently completed quarter an issuer published a press release announcing that it no longer intended to actively explore two of its three principal resource properties as a result of disappointing exploration results. The announcement occurred before the interim F/S were filed with the Commission and should have, as a minimum, been reflected in the notes as a *subsequent event* in accordance with Section 1750.06(d) of the Handbook (Interim Reporting to Shareholders).

The issuer's announcement raised the question of why the properties had not been written down during the preceding quarter. Consequently, the F/S were retracted and reissued to recognize the impairment in the properties value that had occurred prior to the end of the interim reporting period. This resulted in the issuer writing off approximately $560,000 in deferred costs and represented 62% of the issuer's total assets.

Directors and officers should consider, on an ongoing basis, whether or not there has been an impairment in the recorded value of an issuer's assets.

2.3 Inadequate note disclosure

Section 1750.06(d) of the CICA Handbook requires issuers to provide disclosure on matters not previously reported to shareholders as part of the annual F/S. Most of the interim F/S reviewed suffered from a lack of adequate note disclosure.

2.4 Interim reporting period

Section 1750.10 of the CICA Handbook and the instructions to Schedule A of Form 61 stipulate that interim results must be reported on a year-to-date basis. Issuers frequently neglected to disclose the period being reported on in the headings of their F/S. To minimize confusion in this area, issuers should clearly disclose the period covered by the interim F/S in the headings to the income statement, cash flow statement, and supporting notes.

2.5 Cash flow statement

Section 1540 of the CICA Handbook, revised in 1998, requires the inclusion of a *Cash Flow Statement* with interim and annual F/S. Non-compliance with Section 1540 in interim F/S filed during 1999 was high.

In some cases issuers were apparently unaware of the new requirement, as they continued to prepare Statement of Changes in Financial Position. In a number of other cases, while recognizing that the name of the statement had changed, issuers continued to include non-cash items in their statement of cash flow, e.g., properties acquired through the issuance of shares.

2.6 Earnings/loss per share

Interim F/S frequently failed to provide loss per share information as required by Section 1750.06(b) of the Handbook.

2.7 Unaudited F/S

Interim F/S should be clearly marked *unaudited* in accordance with Section 1750.03 of the CICA Handbook.

2.8 RTO accounting: Prior operations – supplemental information

Issuers are reminded of the requirement found in NIN #91/21 to include supplementary information regarding the reporting issuer's prior operations in the Form 61 report filed for the first period following the date that an RTO has occurred. When filed with a Form 61 report that includes interim F/S, the supplementary information is not required to be audited.

Example

Examples of matters that must be disclosed in supporting notes to the interim F/S include material changes in accounting policies, F/S presentation, and significant changes in assets and financial commitments.

Recommendation

Earlier this year the CICA published an Exposure Draft entitled *Interim Financial Reporting*. One significant proposed change is the presentation of interim results on a year-to-date *and* a quarter-to-date basis. Issuers are encouraged to adopt this form of reporting in advance of the new Handbook section being finalized as staff believe it will enhance the quality of information provided to the market.

3. SCHEDULE B – SUPPLEMENTARY INFORMATION

Issuers generally failed to provide the level of disclosure required by the instructions to Schedule B with respect to options and warrants granted, exercised, or expired during each reporting period. In several instances information provided in Schedule B did not agree with that disclosed in the F/S.

4. SCHEDULE C – MANAGEMENT DISCUSSION

While the interim and annual F/S reviewed by staff complied with GAAP in most material respects, few issuers provided shareholders with adequate MD&A disclosure in Schedule C. The failure to provide meaningful MD&A disclosure explaining the numbers presented in the F/S resulted in limited useful information being provided to shareholders and the market. This information is critical in a venture capital market.

Many of the problems identified in Schedule C disclosure are the same as those described in NIN#96/38 (see Appendix A) and could have been avoided if issuers had followed the guidance provided in the notice.

The following section summarizes the type of disclosure deficiencies in Schedule C frequently noted during the review.

4.1 Extent of Disclosure

As noted in NIN #96/38, Schedule C is intended to provide shareholders and others with a *meaningful* discussion of an issuer's operations during the period under review *up to, and including, the date that the report is signed.* The Introduction to NIN #96/38 advises issuers that this discussion should not generally exceed *two to four pages per quarter* for an issuer that has *active ongoing operations.*

The majority of issuers reviewed by staff tended to provide one page or less of MD&A for each interim reporting period and slightly more in the annual Form 61 filing. Disclosure that was provided tended to be very general in nature and typically did not discuss significant events and transactions, including material expenditures, reflected in the issuer's F/S.

4.2 Discussion of significant expenditures

Item 6(b) of NIN#96/38 reminds issuers that they are required to discuss all significant expenditures recorded during a reporting period. These expenditures are generally the same as those required to be presented in the F/S pursuant to Rule 3(9)(b).

Example

A junior resource company may disclose total drilling costs on a particular property in the F/S. However, related disclosure in the company's MD&A, including the number of metres drilled, actual costs compared to budget, results of drill program, etc., is necessary to make the information set out in the F/S more meaningful.

Common Problem

Virtually all issuers failed to discuss, in a meaningful way, the expenditures reflected in their F/S whether they were general and administrative costs, exploration costs, or research and development costs, and whether or not such costs were expensed or capitalized.

4.3. Reconciliation to budgeted expenditures

The Instructions to Schedule C require issuers to compare actual expenditures to those budgeted in the issuer's offering document or other publicly disseminated document and discuss the reason for any material variation between those amounts. Issuers must also explain the impact of such variation on the issuer's ability to achieve its stated milestones. Staff noted little compliance with this requirement in the issuers they reviewed.

This issue became particularly relevant for one issuer that experienced a significant decline in its working capital during the offering period. While the decline was caused by expenditures incurred in pursuit of the issuer's business plan, the decline caused the issuer to suspend certain research projects which were intended to be funded from the proceeds of the offering. The decline in working capital, the reasons for the decline, and the impact of the decline on the issuer's business plan were not fully discussed in the issuer's interim MD&A disclosure.

The issuer spent substantially all of the money raised from the prospectus offering within 90 days of completing its offering, and it had a significant working capital deficiency at that date.

The issuer's subsequent Schedule C disclosure indicated that the issuer had commenced several research trials by the end of its third quarter in 1999. However no information was provided on the cost of the trials, or how the cost of running the trials would be funded. In addition, no information was provided on the issuer's ability to finance future commitments under various research agreements it had entered into, the consequences of not fulfilling the terms of those agreements, or management's plans to address these challenges.

The need for issuers to discuss actual expenditures compared to budgeted expenditures is described in Item 3 of NIN#96/38.

4.4 Subsequent events disclosure

Schedule C disclosure frequently failed to discuss significant subsequent events as required by the Instructions to Form 61 and as discussed in Item 2. a) of NIN #96/38.

4.5 Related party transactions

Schedule C disclosure typically did not contain a meaningful discussion of related party transactions required by the Instructions to Schedule C and as discussed in Item 4 of NIN #96/38.

Reminder

Issuers are reminded that Form 61 requires them to *compare* actual expenditures incurred subsequent to the completion of an offering of securities to expenditures that were budgeted in the offering document. This analysis can be set out in tabular form.

Issuers are required to *discuss* the reason for any significant difference between actual and budgeted expenditures, and to *explain* the impact of these differences on the issuer's ability to achieve the various milestones disclosed in the offering document.

Issuers must also discuss in Form 61 the impact these differences in expenditures may have on the time frame required to achieve these milestones.

4.6 Period under review

While not required by the instructions to Form 61, issuers are encouraged to present their Schedule C disclosure on a comprehensive, year-to-date basis by reproducing information relating to preceding quarters during the fiscal year in the current period's report.

Subsequent events disclosure (see item 4 above) would be limited to a discussion of significant events occurring subsequent to the date of the most recent F/S included with the issuer's Form 61 report.

4.7 Factual, balanced and non-promotional disclosure

As noted in Item 8 of NIN #96/38, disclosure in Schedule C should be factual, balanced and non-promotional. Where positive factors affecting an issuer's business are disclosed it is inappropriate to omit, or minimize, negative factors. *The use of superlatives should be avoided.*

4.8 Comparative periods

It is of relatively limited value for a development stage issuer to focus its MD&A discussion on current interim period results compared to those recorded in the corresponding period in the preceding year, given the rapid rate of change that such issuers typically experience as a result of their growth and the changing nature of their expenditures.

Development stage issuers are encouraged to focus their MD&A discussion on current quarter results compared to those of the preceding quarter and explain the reasons for any significant variations and the impact of such variation on the issuer's ability to achieve previously disclosed milestones.

III. SHAIF ANNUAL INFORMATION FORM

Information contained in SHAIF AIFs was often completed incorrectly or the information did not agree to the issuer's annual F/S. In one case, information that was required under National Policy 47 (NP 47) was missing and, instead, was simply bulleted in the SHAIF AIF. In another, information on outstanding share capital in the AIF did not agree with the figures presented in the F/S.

MD&A in SHAIF AIFs was particularly deficient. Issuers are required to provide a comprehensive discussion prepared in accordance with Schedule 2 of Appendix A to NP 47. Most issuers reviewed either failed to provide a meaningful discussion of significant short-term and long-term liquidity problems or they minimized the significance of these problems.

Benefit

This form of reporting will provide shareholders and the market with a comprehensive and meaningful analysis and discussion of the issuer's business affairs on a quarter-by-quarter basis (as required by the Instructions to the Form) for the entire year-to-date.

Example

One junior industrial issuer stated in its MD&A that "growth had surpassed expectations", that it had "confidently set on a path of steady expansion", and that its facility had "become a showcase of achievement". Unfortunately, the issuer neglected to provide a meaningful discussion of the significant operating loss that was reflected in the F/S accompanying the Form 61 report or the impact that this loss would have on the issuer's ability to achieve its path of steady expansion.

IV. MATERIAL CHANGE REPORTS AND PRESS RELEASES

Several problems were identified with respect to the filing of Material Change Reports and the publication of press releases. Typically, positive information was published with respect to possible agreements and letters of intent. However the ultimate outcome of such arrangements, including their collapse in some cases, was frequently not disclosed in a follow-up press release or material change report.

In several cases Material Change Reports were not prepared in accordance with the requirements of Form 27. Specifically, Item 5 of Form 27 requires that issuers provide a full description of the material change. This section requires issuers to disclose all *material terms* associated with material transactions. In many cases issuers simply attached a copy of the press release that was published at the time of announcing a new agreement but the press release failed to provide any information regarding the material terms of the agreement.

Issuers should refer to NP 40 (Timely Disclosure) for further direction regarding the nature, extent, and timing of information that is disseminated into the market.

V. WEBSITES

Several issuers created websites shortly after they completed a public offering but they frequently failed to keep the information on the website current. In addition, several issuers provided information on their websites that was not considered by staff to be factual, balanced and non-promotional (See item 7 under discussion of Schedule C above).

Given the level of interest generated through Internet-based trading activity, staff will continue to visit issuer websites as part of the continuous disclosure review process.

Example

One issuer in a press release disclosed that its sales "were up significantly" (which was not supported by the issuer's most recently published interim F/S) but, it failed to disclose that its trade creditors had recently commenced an action to petition the issuer into bankruptcy.

Reminder

Staff intend to monitor press releases and Material Change Reports in the future. This may result in issuers being placed on the Issuers in Default list if disclosure in the Material Change Reports is materially deficient.

Recommendation

Directors and officers are strongly encouraged to review the disclosure record of the reporting issuers they manage in light of the matters identified in the report. Where necessary, the disclosure record of such issuers should be amended and restated to comply with the regulatory requirements discussed in this report.

Recommendation

Problems caused by distributing incomplete or misleading press releases could be avoided by having two senior officers or directors approve the news releases prior to distribution.

Similar consideration should be given to periodic review of the contents of issuer websites to ensure the information is kept accurate, complete and current.

CONCLUSION

This report has been prepared to assist issuers and their directors, officers, and professional advisors in preparing public disclosure documents. Many of the disclosure problems identified in the report could have been avoided if issuers had complied with the disclosure requirements set out in the *Securities Act*, the *Securities Rules*, Commission policies and related materials.

The consequences of an issuer providing public disclosure that is considered to be materially deficient are significant. In addition to the time and cost involved in resolving staff's concerns, issuers may be placed on the Commission's *Issuers in Default* list, lose access to the shortened hold period offered under SHAIF, or have their securities cease traded.

If certain directors and officers appear to be unable or unwilling to provide shareholders and the market with the level of disclosure that is required, those individuals may be subject to further review by the Commission's Compliance Division. Ultimately, such action may impact on the ability of those individuals to continue serving as directors and officers of public companies in British Columbia.

In closing, while *responsibility for the accuracy and completeness of a reporting issuer's public disclosure record rests solely with the issuer's directors and officers*, staff recommend that issuers consider retaining their professional advisors on an ongoing basis to review materials included in that record to provide a reasonable level of assurance that the materials are completed and filed properly.

(NIN#96/38)

NOTICE

Form 61 – Quarterly Report
Staff Report on Schedule C – Management Discussion

On April 20, 1995 the Executive Director issued a notice (NIN#95/19) specifying a revised Form 61 – Quarterly Report for exchange issuers. The notice included a brief discussion of reporting problems identified by staff based on their ongoing review of Form 61 – Quarterly Reports and, in particular, the inadequate level of disclosure provided in Schedule C of the Quarterly Report – Management Discussion. With the introduction of the new Securities Regulation and Rules, NIN #95/19 lapsed.

Although the quality of disclosure in Quarterly Reports filed with the Commission has improved, staff continue to have concerns about recurring deficiencies. Staff have prepared a report, attached to this notice, discussing common deficiencies in Schedule C. This report is intended to assist issuers in properly completing the management discussion section of Form 61.

Meaningful and accurate disclosure in Schedule C of Quarterly Reports is important to shareholders and the investing public. Issuers can expect to receive deficiency letters when they fail to provide the level of disclosure required. Serious disclosure deficiencies in Schedule C may result in cease trade orders under section 146 of the Act.

For example, a Quarterly Report that discloses in Schedule C only that "management has nothing to report", "no change", or "management continues to conduct its business in the manner previously disclosed" does not contain adequate disclosure and may result in a cease trade order.

Directors of exchange issuers are reminded that the board of directors is required to approve the disclosure contained in Quarterly Reports. Serious recurring deficiencies in Quarterly Report disclosure may affect an issuer's ability to obtain a receipt for a prospectus or may affect the suitability of a director under section 120(2) of the *Securities Rules*.

Staff encourage issuers who require guidance in the preparation of their Quarterly Reports to contact the Statutory Filings branch at the Commission.

DATED at Vancouver, British Columbia, on October 31, 1996.

Dean E. Holley
Executive Director

STAFF REPORT
MANAGEMENT DISCUSSION IN SCHEDULE C OF FORM 61

INTRODUCTION

The Management Discussion section (Schedule C) of the Form 61 – Quarterly Report is intended to provide shareholders and prospective investors with a meaningful descriptive summary of the issuer's operations during the period under review. Where an issuer has active ongoing operations, this discussion would generally not exceed 2–4 pages for the quarter discussed. Where an issuer has limited operations, this discussion would generally not exceed 1 page. This report discusses a number of recurring deficiencies in Schedule C and provides guidance to issuers on how to properly complete Schedule C.

COMMON DEFICIENCIES

1. Nature of Business

   Schedule C should provide a brief description of the issuer's business. Staff have noted that inactive issuers often provide little or no meaningful discussion. If an issuer is inactive and has no business, the Quarterly Report should disclose that fact together with any plans for reactivating the issuer and, if known, a brief description of the business that the issuer intends to pursue.

2. Reporting Period

   a) Schedule C requires issuers to discuss financial transactions and events during the period covered by the financial statements and "up to the date of the report". The date of the report is the date that the two directors sign the Quarterly Report on behalf of the board of directors. Staff have noted several instances where management of an issuer has limited its discussion to the period ending at the balance sheet date and has failed to discuss material events or transactions occurring after that date.

   b) The instructions to Schedule A of the Quarterly Report require issuers to prepare financial statements on a fiscal year-to-date basis. While the instructions to Schedule C of Form 61 currently require information for the quarter under review, the discussion of significant transactions should relate to the year-to-date figures reported in the financial statements in Schedule A. Therefore, the instructions to Schedule C will be amended in the near future to require issuers to discuss operations on a year-to-date basis.

3. Use of Proceeds & Milestones

   Schedule C requires issuers to reconcile intended "uses of proceeds" previously disclosed in offering documents, or other publicly disseminated documents, to the issuer's actual expenditures during subsequent reporting periods. Staff have noted instances where either no reconciliation is provided or the disclosure simply consists of the numerical differences. This discussion should explain any material variances, together with a brief description of the impact, if any, on the issuer's ability to achieve previously disclosed objectives and milestones.

4. Related Party Transactions

   Schedule C requires issuers to disclose details of significant transactions with related parties, including the amount of consideration paid or received. Staff have noted that issuers have frequently disclosed the aggregate expenditures to non-arm's length persons in accordance with the instructions to Schedule B but fail to provide meaningful discussion of these transactions in Schedule C. Issuers should disclose details of significant transactions with non-arm's length persons that impact current operations or are expected to impact future operations. Both formal written contracts and informal, undocumented arrangements should be disclosed. Where a non-arm's length person provides services to an issuer, the nature of the services should be described.

5. Investor Relations Activities

Schedule C requires a brief summary of investor relation activities that have been undertaken by, or on behalf of, the issuer during the reporting period. The discussion should include, as a minimum, the names of the persons providing the service, the nature of the services provided, and the consideration paid or to be paid, including cash and/or securities. Issuers are reminded that the Vancouver Stock Exchange's Listing Policy 8 requires disclosure of the relationship between an issuer and a person providing investor relation services, including whether that person has any interest directly or indirectly in the issuer or its securities, or any right or intent to acquire such an interest. Staff recommends that this disclosure be provided in Schedule C.

6. Significant Events & Transactions

Schedule C requires issuers to discuss any significant event or transaction that occurred during the period. Quarterly Reports have often not included a discussion of significant events and transactions. Examples of significant events and transactions that issuers are required to discuss include:

(a) Acquisitions & Dispositions

Where an issuer has acquired or disposed of a material capital asset, the issuer is required to discuss the transaction. The discussion should include: the identity of the parties involved; the material terms of the agreement or arrangement; the total costs incurred; the details of any finder's fees; in the case of resource properties, the existence of any independent engineering reports, a brief description of any proposed exploration program and costs, and the source of funds to finance the programs; in the case of other material capital assets, the source of funds for the acquisition and the anticipated costs to integrate into the issuer's operations. This discussion would normally not exceed 1 or 2 paragraphs.

Where the issuer is negotiating to acquire or dispose of a material capital asset, the issuer should either have filed a confidential material change report or should discuss the proposed transaction to the extent reasonable under the circumstances.

Two examples of how disclosure should be provided are set out below. The examples assume that the transactions are material to the issuer's financial position and operating results.

Example #1 Junior Resource Issuer, Material Acquisition

By an agreement dated September 30, 1996, the issuer acquired from Company A, which had one common director, a 30% interest in the Golden mineral claims located in the Skeena Mining Division, British Columbia, for cash consideration of $50,000. The issuer can earn a further 30% interest in the property by spending $250,000 on the exploration of the property by September 30, 1997.

An independent property report prepared by Joe Bloggs, P. Eng., dated April 10, 1996, recommends that the issuer carry out a $150,000 exploration program consisting of a VLF-EM Survey, trenching and mapping. The VSE has approved the acquisition. The issuer plans to commence the exploration program in the Spring of 1997. The issuer does not currently have sufficient funds to carry out the exploration program and will be required to raise additional funds to finance the program.

Example #2 Non-Resource Issuer, Material Disposition

By an agreement dated September 5, 1996, effective September 31, 1996, the issuer disposed of its 25% interest in Company X. The issuer disposed of this investment because it required additional capital to fund its ongoing business operations described later in this report. As disclosed in note X to the financial statements this investment was sold for $500,000 and resulted in an accounting gain of $100,000. The sale was made to an arm's length party for cash proceeds of $300,000 and a note receivable of $200,000 due December 31, 1996. The VSE approved this transaction on October 2, 1996.

(b) Material Expenditures

Schedule B requires a breakdown by major category of certain expenditures. Breakdowns should be provided for those expenditures included in deferred or expensed exploration and development, deferred or expensed research and development, cost of sales, marketing expenses, general, administrative and any other material expense classification or any other material deferred classification. A category of expenditure generally would be shown separately where it represents 20% or more of the total expenditures for a material classification. All other expenditures included in a material classification may be grouped together under the heading "miscellaneous costs". Examples of major categories for exploration and development include consulting, salaries and benefits, and drilling.

The material categories of expenditures required to be disclosed to comply with the requirements of Schedule B would generally be considered to be significant transactions and should be discussed in Schedule C. Where appropriate, the discussion should address the purpose of the expenditure.

Issuers in the development stage are reminded that, pursuant to section 3(9)(b) of the *Securities Rules,* their financial statements must provide an analysis of expenditures for each of exploration, research, development and administrative costs, whether expensed or deferred. This analysis would be included in the breakdown required by Schedule B; where the analysis is included in the financial statements the issuer is not required to repeat the breakdown in Schedule B. At this time, staff take the position that an issuer is in the development stage if it has not earned significant revenues during its two most recent financial years. The Canadian Institute of Chartered Accountants has recently published a Research Report on Accounting and Reporting for Development Stage Enterprises. The research report includes a definition of development stage enterprises. Staff is currently considering the appropriateness of the study's definition of development stage enterprises for the purpose of section 3(9)(b).

(c) News Releases & Material Change Reports

Issuers should provide an update of significant events or transactions previously disseminated by news release or material change report where there are material variances. For example, if revenues and profits failed to materialize, contrary to management's earlier public announcements, Schedule C must discuss this fact and the reasons for the variance.

(d) Breaches

A breach of corporate, securities or other laws, or of an issuer's listing agreement with the Vancouver Stock Exchange may constitute a significant event that issuers are required to disclose in Schedule C. Management should describe the nature of the breach, alert investors to the potential ramifications of the breach and indicate what is being done to remedy it. In addition, financial statement disclosure may also be appropriate for a breach that represents a liability, contingency or commitment of the issuer.

(e) Regulatory Approval

Where a significant transaction required to be disclosed in the Quarterly Report is subject to regulatory approval, the Quarterly Report must disclose this fact, indicate whether the Issuer has obtained the required approval and, if not, whether it has filed an application to obtain the required approval.

(f) Working Capital

If an issuer is unable to fund its operations, or in the case of an inactive issuer, is unable to fund its general and administration costs, that inability is a significant event. Management should discuss the steps it has taken, or proposes to take, to remedy the situation.

7. Update and Comparison of FOFI

   Part 7 of National Policy #48 requires issuers to update previously released future oriented financial information when a change occurs in the events or assumptions used to prepare the FOFI that has a material effect on the previously issued FOFI. The need to update FOFI is a significant event and should be discussed in Schedule C. Updated FOFI must be included in the Quarterly Report filed immediately following the change in events or assumptions used to prepare the FOFI that triggers the need for update. If management considers that there are no changes in the events or in the assumptions used to prepare FOFI that have a material effect on FOFI, management should communicate its conclusion in the Quarterly Report immediately following the end of the FOFI period in accordance with Part 7 of National Policy #48. National Policy #48 also requires a comparison of actual results to previously issued FOFI. The Quarterly Report immediately following the end of the FOFI period must disclose material differences identified by this comparison.

8. Factual, balanced and non-promotional discussion

   Disclosure contained in the Quarterly Report must be factual, balanced and non-promotional. The Quarterly Report should avoid the use of superlatives. The Quarterly Report must disclose all material facts where they are necessary to prevent statements made in the Quarterly Report from being misleading. For example, it would be misleading to disclose the potential value to the issuer of a sales contract and not also disclose the material terms of the contract that may impact on its value to the issuer, as well as the estimated associated costs. The issuer should also disclose whether the issuer has the resources, as of the date the Quarterly Report is signed, to meet its obligations under the contract.

CONCLUSION

Staff's ongoing review of Quarterly Reports indicates that the quality of disclosure in Schedule C has improved, however, staff continue to have concerns about the quality of information in Schedule C. Staff will continue to monitor the quality of disclosure issuers provide in Schedule C. Serious disclosure deficiencies may result in cease trade orders under section 146 of the Act. Issuers who have questions about their disclosure obligations are encouraged to contact staff.

EXAMPLES OF RULE 3(9)(B) DISCLOSURE

Example 1
High-Tech Inc.
– a development stage junior industrial issuer

Example 2
High-Hope Resources Ltd.
– a development stage junior mining company

HIGH-TECH INC.

Statement of Operations and Deficit
(Unaudited – Prepared by Management)
Nine month period ended September 30

	1999	1998
RESEARCH AND DEVELOPMENT EXPENSES		
Amortization	$ 39,743	$ 69,571
Computer rental	–	10,743
Consulting fees	97,628	177,741
Grants	(30,752)	(20,500)
Rent	13,607	18,938
Royalties	17,405	–
Salaries and benefits	110,838	180,071
Telephone and internet	5,250	16,523
Travel	1,000	9,172
	254,719	462,259
GENERAL AND ADMINISTRATIVE EXPENSES		
Accounting and legal	$ 22,442	$ 39,749
Advertising and promotion	18,025	24,334
Amortization	16,932	11,000
Automobile	12,386	14,026
Management fees	75,000	29,798
Insurance	–	4,959
Interest and bank charges	14,505	692
Office	12,430	35,009
Regulatory and transfer fees	6,630	12,969
Rent	25,280	20,678
Salaries and benefits	110,298	60,682
Shareholder communication	–	93,552
Telephone	14,056	10,608
Travel	–	9,565
	327,984	367,621
LOSS BEFORE OTHER ITEM	(582,703)	(829,880)
OTHER ITEM – Interest income	336	–
LOSS FOR THE PERIOD	(582,367)	(829,880)
DEFICIT, BEGINNING OF PERIOD	(2,301,014)	(6,730,106)
DEFICIT, END OF PERIOD	**$ (2,883,381)**	**$ (7,559,986)**

HIGH-HOPE RESOURCES LTD.

Schedule of Deferred Exploration Costs
For the years ended December 31, 1999 and 1998

	Dry Lake Claims	Sand River Claims	Other	1999	1998[2]
Balance, beginning of year	$5,191,855	$3,772,062	$310,989	$9,274,906	$5,654,243
Airborne survey	15,847	398,174	–	414,021	456,826
Drilling	2,725,030	568,320	–	3,293,350	2,974,639
Engineering	2,154,911	–	–	2,154,911	–
Geology	124,107	–	–	124,107	–
Geological consulting	2,780	–	–	2,780	12,500
Geophysics and geochem	313,500	100,278	–	413,778	84,000
Lab	67,837	–	–	67,837	–
Miscellaneous	14,393	2,914	1,200	18,507	11,299
Permitting	87,139	2,819	636	90,594	39,455
Report preparation	28,745	4,759	321	33,825	20,862
Sample processing	913,427	–	–	913,427	183,698
Technical studies	141,327	–	–	141,327	23,419
Current expenditures	6,589,043	1,077,264	2,157	7,668,464	3,806,698
Costs written-off	–	–	(234,675)[1]	(234,675)	(186,035)[1]
Balance, end of year	$11,780,898	$4,849,326	$78,471	$16,708,695	$9,274,906

Note:

1 *A supporting note to the schedule of deferred exploration costs should provide details of property costs written off during the period.*

2. *The detailed analysis of 1999 exploration costs presented above should also be presented for the 1998 comparative figures on a property-by-property basis in the schedule.*

3. *Aquisition costs are presented separately in the company's balance sheet and in the supporting notes to the F/S.*

Sources of Additional Information

1. The BC Securities Commission website is a useful source of information for issuers and their directors, officers, and professional advisors. The website address is: www.bcsc.bc.ca

2. CARSWELL publishes an annotated version of the British Columbia *Securities Act and Rules* on an annual basis. This publication also includes Commission Policy Statements, Blanket Orders and Rulings, and Notices and Interpretation Notes. Carswell's customer relations telephone number is 1(800) 387-5164.

3. Simon Fraser University's downtown campus offers a program designed primarily for directors and officers of reporting issuers and their employees. The program is taught by legal, accounting, and regulatory professionals. The program consists of two three-day courses, one entitled "Going Public" and the other "Continuous Disclosure".

Notes