

## Corporate Websites and Liabilities

By Isabelle Lamarre and Johanne Duchesne



For private companies, it is important not to post any document or information that could be seen as offering or soliciting trades in their securities.

Information posted on the Internet is capable of reaching both its intended recipients and anyone else in the world who has access to the Internet, but at the same time, electronic communications do not automatically reach all investors. While growing in popularity, only a minority of investors have access to the Internet. Even investors with access will be unaware that new information is available unless the company notifies them of the availability of updated information. Accordingly, disclosure by Internet alone will not meet a company's disclosure requirements under Canadian securities legislation and it is important for a public company to continue to use traditional means of dissemination.

Nowadays, companies are creating websites not only to provide information to customers and suppliers but also to provide information in a timely, cost-efficient manner to market participants and to communicate with investors. For public companies,<sup>1</sup> investor relations information should be viewed as an extension of their formal corporate disclosure record, rather than as a mere promotional tool. The inter-jurisdictional nature of the Internet also makes it important for issuers to consider how they will satisfy the registration and prospectus requirements, as well as other requirements provided in the securities laws of both local and foreign jurisdictions, when they post an offering document pertaining to the distribution of their securities.

### Annual International Surf Day

On March 28, 2000 and on April 23, 2001, the Technical Committee of the International Organization of Securities Commissions conducted its Annual International Surf Days. During the 2001 Surf Day, approximately 300 individuals from 41 participating authorities visited more than 27,000 websites. Of these sites, more than 2,400 were identified for follow-up review on the basis of possible fraud, market abuse and unauthorized financial activities. During the 2001 Surf Day, the investigators of the Quebec Securities Commission (the "QSC") visited 110 websites. Of these sites, 20 were identified for follow-ups because they appeared to

<sup>1</sup> Companies whose distribution of securities is subject to the applicable securities legislation.



solicit investors in a fraudulent manner. For example, some of these companies were not registered with the QSC or did not file a prospectus or obtain an exemption. Some of these sites have been removed following the intervention of the QSC, while others are still under investigation. Since regulatory authorities are investigating websites, it is important for companies to set up their websites in a legally acceptable manner.

Three types of illegalities under securities legislation can ensue from a company's website. First, the information provided may constitute illegal solicitation or trading. Second, the information provided on the website or by hyperlink may be considered misleading or fraudulent. Third, there can be illegal disclosure during a public offering by the Company. After explaining the rules concerning the establishment of corporate websites, we will study each of these three potential illegalities.

In Canada, National Policy 47-201 ("47-201") establishes rules with respect to the use of the Internet for trading in securities. In addition, the Toronto Stock Exchange (the "TSE") has drafted proposed guidelines with respect to electronic communications disclosure guidelines.

## Corporate Websites

The TSE strongly recommends that all listed companies maintain a corporate website to disclose investor relations information electronically.

Current securities filings of listed companies such as financial statements, Annual Information Forms, annual reports and prospectuses are maintained on the SEDAR<sup>2</sup> website which is operated by the Canadian Depository for Securities Ltd. In addition, the TSE maintains a profile page for each listed company on its website ("www.tse.com"). Furthermore, many newswire services post listed company news releases on their websites. Since these various sites are not necessarily linked to one another, it may be difficult and time consuming for an investor to search the Internet and obtain all relevant investor relations information about a particular company. By creating its own website, a company can ensure that all of its investor relations information is available in one place. It can also provide more information than would otherwise be available on-line. For example, SEDAR contains only mandatory filings, while a company's site may carry a wealth of supplemental information, such as fact sheets, fact books, slides of investor presentations and transcripts of investor relations conferences.

## Applicable Disclosure Rules for Electronic Communications

The following rules apply to all corporate disclosure through electronic communications and must be followed by each public company:

### *1. Electronic Communications cannot be Misleading*

A company is required to correct any misleading information on its website. It is not sufficient that the information has been corrected or updated elsewhere, for example, in documents filed with SEDAR. It is possible for information to become inaccurate over time and the company must regularly review and update or correct the information on its site.

Providing incomplete information or omitting a material fact is also misleading. The website must include all news releases, not just favourable ones. Documents should be posted in their entirety and, if this is impractical, excerpts can be posted but care should be taken in order to ensure that they are not misleading when read on their own.

<sup>2</sup> System for Electronic Document Analysis and Retrieval.



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## *2. Electronic Communications Cannot Be Used to Provide Tips or Leak Material Information*

A company must not post a news release pertaining to a material fact on a website or disseminate it by e-mail or otherwise on the Internet before it has been disseminated by a newswire service.

## *3. Electronic Communications Must Comply with Securities Law*

A company should have special regard to the applicable securities legislation and, in particular, to registration and prospectus requirements, which may be triggered if it posts any document offering securities to the general public on its website. Documents related to a distribution of securities should only be posted on the website if they are filed with and receipted by the appropriate securities regulators.

### **TSE Guidelines**

The TSE recommends that listed companies follow its guidelines when (i) designing a website, (ii) establishing an internal e-mail policy or (iii) disseminating information over the Internet.

A company's written policy on electronic communications should include the names of those corporate officers responsible for the company's policies on electronic communications. These officers should ensure that all investor relations information made available by the company on its website or disseminated via e-mail or otherwise posted on the Internet complies with applicable securities laws and internal company policies. The TSE suggests that a company provide an e-mail link on its website for investors to communicate directly with the company's investor relations representatives. Furthermore, the company policy should specify who may respond to investor inquiries and should provide guidance as to what information should and should not be disseminated electronically. Employees should receive clear guidelines with respect to the fact that their corporate e-mail address belongs to the company and that all correspondence received and sent via such e-mail address is to be considered corporate correspondence. The Policy should prohibit employees from participating in Internet chat room or news groups and discussions relating to the company or its securities.

The TSE recommends that a company post its own investor relations information on its website rather than linking to other sites carrying that information. If a company posts and updates its own information, it has more control over the timing and the type of information that it includes on its site.

All supplemental information provided to analysts and other market observers, but not otherwise distributed publicly, should be posted on a company's website.

As a general practice, the TSE recommends that a company not post any investor relations information on its website that is authored by a third party, unless the information was prepared on behalf of the company, or is general in nature and not specific to the company. Instead of posting analysts' reports on its website, the TSE suggests that a company provide a list of all analysts who follow the company, together with their contact information, so that investors may contact the analysts' firms directly. The list should be complete and include all analysts that, to the knowledge of the company, are following its stock, regardless of their recommendations.

On websites, investment information should be clearly identified and separated from other information. In particular, promotional, sales and marketing information should not be included on the same Web page as investor relations information. A company's home page should clearly distinguish sections containing investor relations information from sections containing other information.

## Illegal Solicitation or Trading

### Canada

In accordance with National Policy 47-201, the securities regulatory authorities generally consider a person or company to be trading in securities in a local jurisdiction if that person or company posts on the Internet a document that offers or solicits trades of securities and if that document is accessible to persons or companies in that local jurisdiction. As is evident from the Annual International Surf Days, private companies which are prohibited from soliciting investment from the public may be accused of illegally soliciting funds through their websites.

The act of posting a prospectus or offering document on a website that can be accessed in a given jurisdiction constitutes an act of solicitation of a trade in that local jurisdiction and the person or company posting the prospectus or offering document must therefore, in order to comply with the registration requirements, either:

- be registered to trade in the local jurisdiction;
- have the benefit of an exemption from the registration requirements in connection with the distribution in the local jurisdiction; or
- refer all inquiries concerning the document to a registered dealer in the local jurisdiction.

In general, however, the securities regulatory authorities consider the posting of a document on the Internet that offers or solicits trades in securities not to be a trade or, if applicable, a distribution in a local jurisdiction if:

- the document contains a prominently displayed disclaimer that expressly identifies the local interested and/or foreign jurisdictions in which the offering or solicitation is qualified to be made, and the local jurisdiction is not included among those jurisdictions; and
- reasonable precautions are taken by all persons or companies offering or soliciting trades of securities through the document posted on the Internet not to sell to anyone residing in the local jurisdiction in question.

### International Rules

Canadian issuers and other market participants have to keep in mind that foreign securities regulators may take the view that documents posted on a website that is accessible by persons or companies in their jurisdiction may constitute an offering of securities in that foreign jurisdiction.

In some foreign jurisdictions, the local securities regulators have informed the market as to the steps that should be taken to ensure that a document posted on a website is not considered to be an offering of securities in that foreign jurisdiction. Some of these steps include the use of disclaimers in the document and/or restricting access to the document.

These rules, policies and guidelines are found in a report of the Technical Committee of the International Organization of Securities Commission (“IOSCO”) dated June 2001 entitled “Report on Securities Activity on the Internet II” which is available on the website of IOSCO at [www.IOSCO.org](http://www.IOSCO.org). Appendix I of that report lists the significant Internet-related regulations, policies and guidelines stipulated by individual jurisdictions. In particular, reference should be made to the guidelines issued by the U.S. Securities and Exchange Commission for issuers who use Internet websites to solicit offshore securities transactions and clients without registering their securities in the United States.

### Liability Pertaining to Hyperlinked Information in Communications Found on the Internet

While the Internet enables issuers to communicate more effectively with investors, it also raises concerns regarding issuers’ liability for the content of their communications. Liability is of particular concern when an issuer establishes a hyperlink to a third party’s website.

Generally, securities law imposes liability for statements to investors that contain an untrue statement of a material fact, or do not state a material fact which is necessary to prevent the disclosure from being misleading. Issuers and intermediaries are responsible for the accuracy of statements

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that they make, sponsor or endorse, regardless of the medium of communication, and that are likely to reach investors or markets. IOSCO states that, ultimately, the attribution of liability to issuers for false or misleading information to which they have hyperlinked depends on whether the issuer was involved in the preparation of the hyperlinked information or has endorsed or adopted the information. Therefore, it would seem that liability is generally a question of fact, determined on a case-by-case basis. IOSCO recommends to the regulators that the following factors be considered in order to determine whether an issuer has prepared, endorsed or adopted hyperlinked information:

- the context of the hyperlink - what is said about the hyperlink (whether there is a disclaimer regarding the hyperlink, on the one hand, or a statement endorsing the information, on the other);
- a clear or prominent indication that the reader is leaving the market participant's website;
- framing<sup>3</sup> and inlining<sup>4</sup> (inlining makes it easier to determine that the information comes from another site);
- whether the market participant has paid, or otherwise compensated, the third party for posting the information;

- whether the market participant has been paid, or otherwise compensated, by the third party for posting the information;
- whether the market participant embeds a hyperlink into a document that is required to be filed with a securities regulator or delivered to investors or others; and
- the effort of the market participant to limit the hyperlinks to which investors are directed.

## Liability for Website Communications During the Offering Process

### International Securities Laws

Securities laws are intended to ensure full and fair disclosure to investors. These disclosure requirements are designed to enable investors to make informed investment decisions. To this end, securities laws in many jurisdictions impose transactional disclosure requirements in connection with public offerings. In addition, these laws often limit certain communications during the period of an offering so as to ensure that investors are not influenced by materials outside the prospectus.

As a result, when an issuer is in the process of conducting a registered public offering, in many jurisdictions, both the issuer and intermediaries participating in the offering are subject to restrictions on communications with potential investors or, at least, are obliged to ensure that direct or indirect references to the public offering refer potential investors to the prospectus or offering document.

Because of their increasing use of websites to communicate with security holders, customers, suppliers and others, during the offering process, issuers and intermediaries should carefully consider the content available on their websites or through hyperlinks. The fact that an issuer or intermediary is engaged in a public offering may affect what information can appear on its website or can be made accessible by hyperlink.

As a general matter, IOSCO recommends that regulators allow issuers and intermediaries to maintain communications with the public during the public offering process, as long as such communications comply with the rules relating to public offerings.

<sup>3</sup> Framing involves a type of hyperlinking whereby upon clicking highlighted text, graphics or a button, information from a separate Website is imported into the Website on view and is displayed with a constant on-screen border or frame. Information from both Websites is visible at the same time. Consequently, the reader may not be aware that information has been imported from a separate Website.

<sup>4</sup> Similar to framing, except without the border.

In other words, information that is allowed to be posted on the website should be limited to ordinary-course business and financial information. This type of information may include the following:

- advertisements concerning the issuer's products and services;
- periodic reports filed with regulatory authorities;
- proxy statements, annual reports to security holders and dividend notices;
- routine press releases concerning business and financial developments;
- answers to unsolicited inquiries concerning business matters from securities analysts, financial analysts, security holders and participants in the field of communications who have a legitimate interest in the issuer's affairs; and
- security holders' meetings and responses to related security holder inquiries.

Thus, an issuer that is preparing for its first registered public offering while concurrently establishing a website should proceed with extra caution when determining its website content. A new issuer likely does not have considerable experience in ordinary-course business communications with the marketplace. Consequently, its website content may condition the market for the offering and, due to the unfamiliarity of the marketplace with the issuer or its business, investors may be unable to view the issuer's communications in an appropriate context or to distinguish offers to sell securities from product or service promotional activities or other business or financial information.

## Prospectuses and Roadshows in Canada

In the case of a distribution by way of a preliminary prospectus filed with Canadian securities regulatory authorities, in order to comply with securities legislation, a person or company conducting the distribution should record the names and addresses of all parties who receive a copy of the preliminary prospectus, including those recipients who only view the preliminary prospectus by electronic means.

Persons or companies should also be aware that the posting of new information on their websites during a period of distribution may be construed as advertising, which is subject to restrictions in Canada. For example, the securities regulatory authorities do not object in principle to an issuer or underwriter holding a roadshow<sup>5</sup> over the Internet during the waiting period<sup>6</sup> in connection with a distribution of securities. However, care should be taken to ensure that the transmission of a roadshow over the Internet complies with the waiting period requirements and securities legislation generally. In such a case, the following guidelines should be followed:

- a copy of the preliminary prospectus must be made available to each viewer before each roadshow transmission. Each transmission should contain statements

emphasizing that the roadshow does not contain all of the information found in the preliminary prospectus, and that the actual preliminary prospectus should be reviewed for complete information. A copy of the preliminary prospectus may be sent electronically to potential investors in accordance with the guidelines contained in National Policy 11-201;

- electronic access to the transmission of a roadshow over the Internet should be controlled by the issuer or underwriter conducting the roadshow, using such means as password protection, in order to ensure that all viewers are identified and have been offered a preliminary prospectus. Any persons or companies that are considered "prospective purchasers" under securities legislation relating to roadshows may be invited to view the roadshow;
- an issuer or underwriter should not transmit a roadshow to a person or company unless that person or company has agreed not to copy or further distribute the transmissions. An issuer or underwriter should take reasonable steps to prevent copying or further distribution of transmissions.

<sup>5</sup> A roadshow is a presentation made by a dealer to a prospective purchaser of securities in a jurisdiction during the "waiting period" in compliance with securities legislation requirements.

<sup>6</sup> The waiting period is the time between the issuance of a receipt for the preliminary prospectus pertaining to the distribution and the issuance of a receipt for the final prospectus.

## Sanctions

In case of illegal solicitation or trading (distribution without a prospectus), every person who has subscribed may apply to have the transaction rescinded or the price revised, at his option, without prejudice to his claim for damages. Furthermore, the plaintiff may claim damages from the issuer or the holder, as the case may be, whose securities were distributed without a prospectus, from the promoter of the venture, from senior executives of the issuer, or from the dealer responsible for the distribution.

Fines can be also be imposed by the securities regulatory authorities on persons or companies who act in contravention of the laws, rules and regulations. The fines vary in accordance with the profit realized and the number of contraventions and, in the Province of Quebec, can reach as high as \$1,000,000.

The securities regulatory authorities may also order an investigation to inspect websites or electronic communications. In the event that a securities regulatory authority discovers an illegality within a website, it can order the website to be closed and prohibit the officers responsible for the website from trading in the securities of the corporation.

## Legal Issues

As discussed above, corporate websites and electronic communications may give rise to many legal issues. It is in the best interest of a company to consult its legal advisors in order to determine its potential liability with respect to its website and electronic communications, as well as to ensure that the appropriate policies are adopted and that the required legal disclaimers about the accuracy, timeliness, and completeness of the information posted on its website are included.

For any questions with respect to the foregoing, please communicate with Isabelle Lamarre at (514) 877-2995 or Johanne Duchesne at (514) 877-3045.

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