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The Cassels Conspectus* - No. 1: Financial Blackout Periods

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***con·?spec·?tus | \ k?n-?spek-t?s** - a usually brief survey or summary (as of an extensive subject) often providing an overall view.

From policies to plans, from contracts to compensation, several times each year, we will select a topic of interest to survey and analyze. The Cassels Conspectus will look at the choices that public companies make on a range of topics and issues. What is typical or atypical? Is there a conventional approach? Are you too conservative or too aggressive? What might you be missing? Let the team at Cassels help answer your questions and keep you informed of what's going on in market.

No. 1: Financial Blackout Periods

A review of variation in blackout periods surrounding earnings.

The Purpose of Blackout Periods

Securities laws in Canada prohibit insiders and others in a "special relationship" with an issuer from trading with knowledge of "material facts" or "material changes" that have not been generally disclosed to the public. Trading with the knowledge of undisclosed material information is illegal and generally known as "insider trading". Most public companies have "insider trading policies" that, while noting the prohibition against insider trading, also impose periods during which insiders and others covered by the policy cannot trade, referred to as "blackout periods". Blackout periods are not a mandated requirement imposed by law or stock exchange policies but constitute an important preventative compliance measure widely adopted by public companies. The objective of blackout periods is to help reduce regulatory investigation risks and reputational risks associated with the appearance of improper trading by prohibiting it during periods when important disclosures, such as financial statements, are being prepared and finalized for public release.

Securities regulators recommend[1] that issuers adopt insider trading policies that (a) provide for a senior officer to approve and monitor the trading activity of insiders, officers, and senior employees; (b) prohibit purchases and sales at any time by insiders and employees who are in possession of material non-public information; and (c) provide blackout periods when trading by insiders, officers and employees may typically not take place.

As part of such policies, issuers typically adopt a blackout period surrounding regularly scheduled earnings announcements, commonly known as *financial blackouts*. Regulators have not suggested any specific period for financial blackouts, but have indicated that a financial blackout period *may* mirror their recommended “quiet period”, which is a quarterly period during which no earnings guidance or comments with respect to the current quarter’s operations or expected results are provided to analysts, investors or other market professionals. The regulators recommend that this quiet period run between the end of the quarter and the release of a quarterly earnings announcement although, in practice, quiet periods vary by company.

As might be expected, financial blackout periods also vary by company, and a review of that variation is the purpose of the first issue of the *Cassels Conspectus*.

Our Review

We selected 57 reporting issuers with publicly available insider trading policies, looking for a mix of size, sector and exchange:

- *Market Capitalization*[2]: Market capitalizations ranged from $4 million to $43 billion. 24 issuers were under $100 million and 15 issuers were above $1 billion, with 18 in between.
- *Sector*[3]: The population consists of 14 cannabis issuers, 5 technology issuers, 16 mining issuers, 10 energy issuers, 3 life science issuers, 4 “clean tech” issuers, and 5 “diversified” issuers (comprised of companies in the communications services, financial services, and industrials sectors).
- *Exchange*: 27 issuers are listed on the Toronto Stock Exchange (TSX), 15 issuers are listed on the TSX Venture Exchange (TSXV) and 15 issuers are listed on the Canadian Securities Exchange (CSE). No Aequitas listed companies were selected for this specific review.

Our review examined the following:

- *Start of the Period*: We identified the reference point for start of the blackout period, the number of days before or after the financial period that the blackout period started, and whether the blackout period began before or after the financial period ended.
- *End of the Period*: In all cases, the reference point for the end of the blackout period was the earnings release date. Typically, blackout periods end after a given number of business, trading or calendar days have elapsed following the public disclosure of financial results.
- *Overall Length of the Period*: Using each issuer’s start and end dates, we calculated the theoretical maximum blackout period to compare the duration of blackout periods between issuers.
- *Correlations*: From our dataset, we drew certain preliminary correlations between the periods and

the size of the issuer, the sector of the issuer and the exchange on which the issuer is listed.

Our Findings

Start & End Dates of Blackout Periods

Start of the Blackout Period

Exchange	Financial Period End		Earnings Release Date		Earnings Review Date		No Fixed Trigger
	No.	*Avg Days Before*	*No.*	*Avg Days Before*	*No.*	*Avg Days Before*	
TSX (27 Issuers)	14	6	8	14 (13.88)	2	22	3
TSXV (15 issuers)	4	5	4	17.5	3	18	4
CSE (15 issuers)	5	14	5	12.75	2	9.5	3

Figure A: Quarterly Blackout Start Dates

Start dates for blackout periods are most often tied to the **financial period end** (23/57 issuers), followed by the **earnings release date** (17/57 issuers), and then least commonly, the **earnings review date** by the board or audit committee (7/57 issuers). The balance of periods adopt a discretionary, variable or indeterminate start date (10/57 issuers). For example, a small number of issuers initiate blackout periods during “the existence of undisclosed material information”, while others initiate blackout periods at the Chief Executive Officer’s discretion with no set timing around earnings. Figure A (above) sets out the average days before the trigger that the quarterly blackout begins, on a per-exchange basis.

Where the reference point is the **financial period end**, the most common time to initiate the blackout period is within a week or less *after* the financial period end (15/23 issuers), followed by (a) a date that is *before* the financial period end and (b) more than one week *after* the financial period end (both 4/23 issuers).

Where the reference point is the earnings release date, the most common time to initiate the blackout period is 1-2 weeks prior to such date (9/17 issuers), followed by 2 weeks to a month (4/17 issuers) and a week or less (3/17 issuers).

Where the reference point is the **earnings review date**, the most common time to initiate the blackout period is within 14 days prior to board/audit committee review (4/7 issuers), followed by 30 or fewer days (2/7 issuers) and 7 or fewer days (1/7 issuers).

On TSX, nearly one-quarter of blackout period start dates (6/27 issuers) are tied to the earnings release date and are relatively late (14 or fewer days prior to the earnings release date), while nearly half of TSX issuers start blackout periods prior to the period end, or at or shortly thereafter (12/27 issuers). The presence of a notable number of early and late blackout period start dates indicate that compliance protocols and risk appetites vary considerably across TSX issuers, though the TSX contains the highest percentage of issuers with blackout periods tied to the period end. Overall, the evidence suggests that TSX issuers generally have longer blackout periods, owing to earlier and more conservative start dates. That being said, TSX issuers will generally release their financials earlier than issuers on TSXV or the CSE.

On TSXV, just over one-third of the blackout policies surveyed (6/15 issuers) contain relatively early start dates, with blackout periods beginning (a) prior to the financial period end, or at or shortly thereafter, or (b) approximately 30 days prior to the earnings release date.

CSE issuers appear to adopt more liberal approaches to blackout periods. Over one-third of blackout periods surveyed (6/15 issuers) contain relatively late start dates, with blackout periods beginning (a) 14 or fewer days prior to the earnings release date, or (b) 14 or fewer days prior to the earnings review date. Just one-fifth of the CSE policies (3/15 issuers) contain blackout periods beginning prior to the period end, or at or shortly thereafter.

End of the Blackout Period

The most common end date is 2 trading or business days after the earnings release date (27/57 issuers), with 1 trading day being fairly common also (17/57 issuers). Discretionary end date policies (i.e., where the end of the blackout period is not predetermined and is set by a decision-maker on a case-by-case basis) exist for 6 issuers.

Overall, there may be a weak correlation between the relative sophistication of the company/exchange and length of the post-public disclosure blackout. Discretionary end date policies are most commonly found among issuers listed on the CSE (3), then TSXV (2) and TSX (1).

On TSX, over half of the issuers (17/27) terminate their blackout period 2 trading or business days after the earnings release date, with 1 trading day being next most common, but not significantly so (5/27). From the companies surveyed, the TSX is the only exchange with an issuer using the longest standard (3 trading days).

On TSXV, over half of the issuers (7/15) terminate their blackout period 2 trading or business days after the earnings release date, with 1 trading day being next most common but not significantly so (4/15).

On the CSE, by contrast to the other exchanges, over half of the issuers (8/15) terminate their blackout period 1 trading or business day after the earnings release date, with 2 trading days being next most common (3/15). The evidence may suggest that CSE companies tend to, on average, adopt earlier end dates for blackout periods than companies listed on the TSX and TSXV, which have longer blackout periods generally.

Overall Length of the Blackout Period

Exchange	Total Issuers Surveyed	Mean Blackout Duration (Days)	Median Blackout Duration (Days)
TSX	27	34.75	41.5
TSXV	15	38.27	33
CSE	15	37	23

Figure B: Quarterly Blackout Duration – Mean and Median Values

Correlations

It appears that there is a slight correlation between size and complexity of issuers and the duration of blackout periods. Of the sample surveyed, a larger proportion of TSX-listed companies (which are generally larger and meet more-complex listing and disclosure requirements) have relatively long blackout periods. The CSE has a larger proportion of companies with relatively short blackout periods. The TSXV is somewhere in between: there is no significant skew towards shorter or longer blackout periods among those TSXV companies surveyed.

There does not appear to be a statistically significant correlation between exchange and use of multi-tiered blackout policies (i.e., where the blackout start date is different for various classes of persons). In other words, a less-sophisticated company on the CSE may be as likely to have a multi-tiered blackout policy as a large, sophisticated issuer on the TSX.

A similar observation applies to discretionary policies (i.e., where a blackout period's start and end date are not enumerated in the policy, instead relying on an enumerated decision-maker to determine the start and end dates on a case-by-case basis).

Figure B (above) sets out the mean and median quarterly blackout durations on a per-exchange basis.

Sector-Specific Analysis

There are observable differences between blackout policy duration and complexity by sector as well. Below are some sector-specific insights pertaining to issuers and their blackout policies:

Cannabis (14 Issuers)

Of the 57 issuers surveyed, only those in the cannabis sector have any blackout policies that begin prior to period end. Over half of the issuers adopt relatively early start dates, with blackout periods beginning either prior to financial period end (3 issuers) or at or within 7 days of financial period end (5 issuers). The balance of the issuers have start dates beginning 14 days prior to the earnings release date (3 issuers), at or within 14 days of financial period end (2 issuers), or 14 or fewer days prior to the review date (1 issuer).

Blackout period end dates for cannabis issuers are slightly earlier than the general trend: where the most common end date across all issuers is 2 trading or business days following the earnings release date, it is 1 trading or business day for cannabis issuers (7/14 issuers), followed by 2 trading or business days (6/14 issuers).

Mining (16 Issuers)

Notably, a quarter of mining issuers surveyed implement discretionary blackout policies: that is, where the imposition of a blackout period (and/or their durations) are decided on a case-by-case basis (4/16 issuers). Generally, this subset of blackout policies demonstrates an even distribution between relatively early and relatively late start dates (5/16 issuers each). Accordingly, there are just as many trading policies that are conducive to longer blackout periods (e.g., those beginning at or within 7 days of period end) as shorter ones (e.g., those beginning within 7 days prior to the earnings release date).

In terms of end date, there is a significant skew in favour of the 2 trading or business day standard. Half of the mining companies surveyed adopt this standard (8/16 issuers), while a quarter adopted discretionary end dates (4/16 issuers). Notably, one mining issuer adopted a multi-tiered approach to end date, which varies depending on whether earnings are released prior to or during the trading day.

Energy (10 Issuers)

Energy issuers appear to favour later blackout period start dates relative to those in other sectors: only one issuer adopts a start date at or within 7 days of financial period end. Notably, a significant number of issuers in this subset tie the start date to the earnings review date by the board/audit committee (3/10 issuers). This is in contrast with the cannabis and mining issuers surveyed, with each of those subsets containing just one such policy (2/30 issuers).

Similar to cannabis issuers, blackout period end dates for energy issuers reverse the general trend. The most common end date among such issuers is 1 trading day following the earnings release date (5/10 issuers), with 2 trading days being next most common (3/10 issuers). Notably, the latest end date among all 57 companies surveyed belongs to an energy issuer, at 3 trading days after the earnings release date.

Discretionary Exemptions During Blackout Period

Of the 57 issuers surveyed, 26 have policies which expressly incorporate an exemption regime that allows for persons to engage in trading activity (including the exercise of stock options) during the blackout period. This contrasts with policies with general trading controls that do not expressly set out an exemption regime. Such an issuer may instead rely on a general trading pre-clearance protocol that is perpetually in effect, during and outside of blackout periods. Whether that approach is adopted in practice cannot be determined.

Who Can Approve an Exemption?

Of the 26 policies containing an exemption regime, the most common approving officer(s) of such exemptions (noting that more than one person may be empowered to do so) were the issuer's Chief Executive Officer (10 policies), Chief Financial Officer (8 policies), and Chief Legal Officer or General Counsel (5 policies).

In contrast to policies that vest approval authority in an executive officer(s), 8 policies vested such power in a board or person specially appointed to review trading activity, such as an Audit Committee or Information/Trading Officer.

Reasons Permitting an Exemption

A large majority of policies with an exemption regime (20/26 issuers) required the person seeking the exemption to demonstrate "exceptional" or "extenuating" circumstances (and in all cases, this was a non-exhaustive standard). Among such policies, frequent examples of "exceptional" circumstances include: (a) financial hardship/pressing financial commitments (6/20 issuers) and (b) where the timing of the trade is critical for tax planning (6/20 issuers).

The remaining policies with an exemption regime (6/26 issuers) do not enumerate specific criteria by which a person's request for an exemption is assessed.

The Cassels Conspectus *is brought to you by our Securities Group and is edited by Greg Hogan. This issue features contributions from André Boivin, Alex Pizale, and articling students Timon Li and Mohammad Ameli.*

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[1] See section 6.11 of *National Policy 51-201 Disclosure Standards*.

[2] As at May 31st, 2022.

[3] Using sectors used by TMX Group, and adding another grouping for cannabis issuers. CSE listed companies were assigned to appropriate sectors.

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