

Modernizing Securities Regulation in Canada

Discussion Draft, June 7, 2004

PREAMBLE:

This proposal envisions provinces and territories working together to move to a new securities regulatory framework that features a common securities regulator, a common body of securities law and a single fee structure. The common regulator would be an entirely new agency with a mandate that reflects the needs of Canadian capital markets and provides appropriate protection for Canadian investors.

With agreement on these key elements, the following proposal could serve as the basis for discussions on designing a model that allows the provinces and territories to move together to a modern new securities regulatory framework within a reasonable time.

Ontario is willing to explore creative solutions that encourage the participation of all provinces and territories and that encapsulate a strong local and regional regulatory presence. There are a number of alternatives that could be acceptable to Ontario on key design elements of the proposal.

OBJECTIVE:

Modernizing the securities regulatory framework in Canada to ensure our capital market remains competitive while strengthening investor confidence and protection.

Key features of a new system will include:

- Effective and efficient delivery of regulation
- Strong investor protection
- Strong local and regional regulatory presence
- True one-window access to capital market across Canada for companies and investors
- More effective enforcement of securities laws
- A single fee structure with fees set on a cost-recovery basis
- Open and responsive regulatory policy-making
- Clear accountability to governments for the whole securities regulatory system
- Enhanced reputation abroad for Canada's securities regulatory system as competitive internationally with the best in the world

MODEL TO ACHIEVE OBJECTIVE:

A common body to deliver regulatory services to businesses and investors close to where they are located, which achieves the following benefits:

- Easier to understand for companies and investors due to a common interpretation and consistent application of regulatory requirements
- Deeper pools of capital for companies and more investment opportunities for investors as a result of seamless one-window access to Canada's capital market
- Minimal administrative duplication yielding a more cost-effective system
- Rapid, coordinated regulatory policy response to marketplace changes
- Clear accountability to governments
- A consistent voice in international forums in relation to policy development and in enforcement actions with other securities regulators
- Increased investor confidence through the effective enforcement of securities laws

A common set of securities laws which delivers the following improvements:

- No lost financing and investment opportunities caused by the delays and complexities of dealing with multiple regulators and multiple laws
- Easier for companies to raise capital and for securities businesses to operate across Canada as a result of one set of clear and consistent requirements
- A lower burden of complying with applicable laws, freeing up resources for companies and lowering the costs that are passed on to investors
- More choice for investors and companies, and more competitive capital markets, since more companies will raise capital and do business in more provinces
- Easy for investors to understand one set of clear, consistent protections

A single fee structure, with fees set on a cost-recovery basis, which provides:

- Fair treatment for market participants
- Simpler compliance which lowers regulatory costs for businesses
- More cost-effective administration when fees reflect the costs of regulation

TRANSITION TO THE NEW MODEL:

A 'passport' system requires the same initial steps as moving to a common securities regulator. For a passport to be widely accepted and seen as a step forward, it must be based on a common set of securities laws and a single fee structure and it must be part of a credible plan to move to a common securities regulator.

Ontario would consider entering into a passport with other provinces and territories as part of a clear transition to a common securities regulator, common securities laws and single fee structure, subject to the following pre-conditions:

1. Agreement to create a common securities regulator within a reasonable period of time (2 to 4 years);
2. Agreement that a common securities Act and a common set of regulations would apply in participating provinces and territories within 1 to 2 years;

3. Agreement to put a single fee structure in place in participating provinces and territories within 1 to 2 years, with fees set on a cost-recovery basis; and
4. Striking an implementation task force, that would report on a regular basis to the Ministers Council, with full-time, dedicated resources to develop the workplan and common body of securities law.

The transition passport would not take effect until the common body of securities law is in place. The transition passport would include a two-year sunset clause to ensure sufficient time to put the common regulator in place. It also would include mechanisms to ensure consistent interpretation and application of the common set of securities laws in the period before the common regulator is put in place.

DESIGN ELEMENTS:

A common regulatory agency:

- The regulatory agency would be a new entity. Ministers from participating provinces and territories would oversee the work of the task force and the development of the workplan to create the common agency.
- The agency would have a head office with strong local or regional offices. The head office would provide common overall management and direction. Local or regional offices would deliver regulatory services to businesses close to where they are located and to investors close to where they live. Staff for the new entity's local and regional offices could be drawn from the staff of the existing regulatory bodies.
- The agency would operate on a self-funding, cost-recovery basis with a single fee structure which would apply across participating provinces and territories. The provinces and territories could work to address revenue losses for any jurisdictions whose regulators do not operate on a cost-recovery basis now.
- Provinces and territories would tap the specialized expertise and best practises of existing regulators to forge a regulatory agency that is able to deliver true one-window service to investors; companies raising capital; and market participants including securities dealers, investment banks, portfolio managers and advisers.
- The provinces and territories would develop a workplan to create the new agency and to identify areas where administrative duplication and overlap could be eliminated and where resources could be freed up by eliminating the need to coordinate activities among multiple regulators. The workplan also could identify areas where resources could be re-deployed to respond to local needs or to address issues of common concern.

A strong local and regional presence:

- A strong local or regional presence would enable the agency to build on existing specialized regulatory expertise in delivering regulatory services, developing regulatory policy and conducting investigations and enforcement.
- Local offices would facilitate one-window access for capital market participants or investors seeking redress. Local offices would have real decision-making authority to maintain existing responsiveness while allowing local decisions to apply across provincial borders. Examples of areas in which local staff would make decisions include approving prospectuses, granting discretionary exemptions, accepting registrations and pursuing investigation and enforcement activities.
- Local and regional offices would play a significant role in developing regulatory policy. Lead policy roles could be assigned to local and regional offices. Examples: Alberta for issues relating to the oil and gas sector; British Columbia for the junior mining sector; and Quebec for derivatives.
- Policy development in relation to the needs of small and medium-sized enterprises (SMEs) would be assigned to a highly identifiable focused group within the agency. The SME group could be headquartered in a local or regional office.

This approach could be refined to meet the needs of SMEs in specialized industries that are concentrated in one region (for example, small oil and gas companies). Regulatory responsibility for such sectors could be headquartered in the appropriate local office to ensure real local autonomy and maintain regulatory responsiveness.

A common body of securities law:

- The agency would administer a common Securities Act and a common set of regulations and rules. This would make it easy for companies to do business across Canada by providing one set of laws for raising capital and clear compliance standards. A common set of strong, consistent protections is easy for investors to understand and inspires confidence that investments are safe and secure
- A common body of securities law across provinces and territories could be achieved by each jurisdiction adopting the securities legislation of one province, as amended from time to time, common regulations and a common set of securities rules.

Provinces and territories would strike a task force to develop the common laws, working from regulators' Uniform Securities Law (USL) project as a starting point. The legislation could be enacted by one province and adopted by others.

- This mechanism preserves provincial legislative autonomy since each provincial

legislature would enact its own adopting legislation.

- Companies would be confident this body of law covers all requirements they would have to meet to raise capital or do business anywhere in Canada's capital market. Investors would be sure that common protections apply wherever they invest.
- Participating provinces could have scope to make limited local exemptions and/or local rules, within well-defined parameters.

Enforcement:

- The new regulator could build on the existing solid base of local investigation, enforcement and adjudication. A strong local enforcement presence could deal effectively with local violations and respond locally to investor complaints.
- Common enforcement priorities would deliver improved capacity to pursue enforcement actions on activities that span provincial borders.
- A common agency would enable more effective coordination with other law enforcement bodies, regulators and prosecutors and would facilitate more comprehensive and integrated enforcement responses.
- A strong local enforcement capability would be preserved. In addition, the common regulator offers greater flexibility to add enforcement resources and deploy them more effectively through administrative savings, more effective coordination with other bodies and greater capacity to develop more effective tools to investigate and prosecute violations that impact all jurisdictions such as illegal insider trading.
- The relationship between the securities tribunal and the regulator also could be examined. Other jurisdictions have separated the securities regulator's adjudicative role from its regulatory, policy-making and enforcement functions when moving to reorganize their securities regulatory authorities.
- The appropriate remedies and sanctions for any securities tribunal and for the courts also could be considered. Some remedies and sanctions could be reserved exclusively to the courts, as they are now, such as the ability to impose prison terms.
- There could be local hearings before the tribunal. Decisions of the agency could be appealed to the tribunal and tribunal decisions could be appealed to the local courts. Existing limits on the right to appeal would continue (e.g. no right to appeal agency decisions on discretionary exemptions).

Decision-Making Mechanism:

- More timely decision-making and more streamlined regulatory approaches by Ministers would be facilitated by an effective voting mechanism. A Ministers Council (see next section) could make timely decisions on changes to securities legislation, rules, other policy proposals and appointing the agency Board / Commission members.
- A single voting mechanism could apply to all decisions of the Ministers Council or approval thresholds could vary according to the different types of items brought before the Council for decision. For example, the required approval threshold for rules and for changes to securities legislation could differ.
- The approval threshold for votes by the Ministers Council could be negotiated.
- Identifying small business (SME) and regional interests in the policy process and in the Ministers' decision document could protect SME and regional interests. This method is often used to protect the environment and language rights.
- The ability to raise new policy ideas through an open and receptive regulatory development process could be assured through a lower approval threshold for new policy proposals. For example, a majority (or an agreed minority) of provinces could request the new agency to develop and consult on a specific rule proposal.
- Policy that is responsive to the regions that are most directly affected by it also could be ensured by allocating decision-making on an issue-by-issue basis to Sub-Councils of provinces that have regulatory expertise and significant capital market activity in specific sectors. Examples: an Oil and Gas Sub-Council of provinces could be empowered to make decisions on regulatory policy proposals in relation to that sector; similar Sub-Councils could be established for Micro-Cap Firms, Large Firm Corporate Governance, Derivatives, and other areas as warranted.
- The approval threshold for votes by the Sub-Councils could be structured as proposed for the full Ministerial Council or tailored specifically for the Sub-Councils.
- The full Ministerial Council could decide issues that are important to all provinces such as: international issues, dealings with the U.S., enforcement priorities, and proposals for changes to securities legislation.

Ministers Council:

- Clearer accountability for the regulatory framework that applies to companies and investors across Canada could be achieved by a Ministers Council overseeing the new regulator. Now, no agency or government is responsible or accountable for the

operation of the whole securities regulatory system -- securities regulators and governments are responsible only for discrete parts of the existing system.

- The Council of Ministers, comprised of provincial and territorial Ministers responsible for securities regulation, could make decisions on regulatory changes, appoint members of the common regulatory agency and oversee the agency and the securities policy development process. (See 'Decision-Making Mechanism'.) Each Minister on the Council would be accountable to their respective legislatures.

Regular meetings of this Council would ensure responsive securities regulation and timely changes when needed to respond to market developments.

The Ministers Council could appoint Commissioners / members of the regulatory agency with a view to ensuring balanced representation of jurisdictions and capital markets participants. The objective would be to achieve a strong focus on broad, relevant expertise and the common interests of the provinces and territories.

CONCLUSION:

Ontario looks forward to working with other provinces and territories to explore creative solutions in working towards an efficient and effective securities regulatory system. Together, we can achieve a modern new framework that meets the needs of investors, companies and capital markets and all provinces and territories.