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## SUMMARY OF CANADIAN SECURITIES REGULATION

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While it is said that Canada's securities industry is overseen by the law of 13 jurisdictions, Canada's four main securities regulators (the Ontario Securities Commission (OSC), the Alberta Securities Commission (ABC), the British Columbia Securities Commission (BCSC) and the Quebec Autorité des Marchés Financiers (AMF)), together supervise roughly 95% of the market. These regulators are fully self-funded by levies imposed on market participants. They have comprehensive powers, including enforcement powers. In the case of the AMF, enforcement powers are exercised through an independent tribunal, the Bureau de Décision et de Révision en Valeurs Mobilières (BDRVM).

**Exchanges and self-regulatory organizations.** Provincial regulators rely largely on exchanges and self-regulatory organizations (SROs) for the regulation and supervision of the market and its participants. As a result of the administrative structure, Canadian SROs have similar powers and functions as US SROs. The provincial securities acts delegate the power to the provincial regulators to recognize and sub-delegate powers to approved exchanges and SROs.

Canada's main SROs include the Investment Dealers Association of Canada (IDA) which regulates Canada's 212 broker-dealers, the Mutual Fund Dealers Association of Canada (MFDA), and Market Regulation Services Inc. (RS), which has self regulatory powers over the trading in the equity exchanges. In addition, the Montréal Exchange (MX) is recognized as an SRO, and the equity exchanges (the Toronto Stock Exchange (TSX) and the TSX Venture Exchange (TSX V)) should be considered SROs, although since 2002 they have delegated market regulation functions to RS to create systemic independence. IDA and RS are now merging to consolidate member and market regulation, and will soon be the Investment Industry Regulatory Organization of Canada Inc. (IIROC).

**Interaction between provincial regulators and SROs.** Each of the provincial regulators must authorize SROs by means of a **recognition order** requiring the SRO to prove its financial and operational viability, adequate corporate governance, proper risk management, its fair treatment of its members and its appropriate standards of member conduct that promote investor protection. Ongoing, the regulator must approve an SRO's **rules**. Each SRO is subject to **periodic reporting obligations** to its regulators, including financial statements and reports on investigation and enforcement actions. Finally, the regulators have a goal of **inspecting** on-site each SRO and exchange every three years.

**Coordinating regulatory oversight of SROs.** Coordination among the provincial regulators of SRO regulation and supervision is accomplished differently for the exchanges on the one hand, and the IDA, MFDA and RS on the other hand. The exchanges are addressed by a "**lead regulator**" approach, where one regulator authorizes the exchange, any changes in the conditions of that authorization, and approves the regulations of the exchange. The other regulators then exempt the exchange from applying for recognition, though any regulators may revoke the exemption and require the exchange to become recognized in its jurisdiction. By

contrast, IDA, MFDA and RS are subject to a “**principal regulator**” approach whereby the SRO has a single point of contact with one regulator, but each regulator retains full authority over the SRO and each regulator will issue a recognition order, approve any changes in the conditions of that recognition, and approve the SRO’s regulations. The principal regulator conducts on-site inspections, but the other regulators commonly participate in the inspections.

**Current issues.** At present, the most pressing issues in Canadian regulation are related to the most immediate issue of the recent failure of ABCP issued by non-banks, and the arguments for and against a single securities regulator.

In August last year it was disclosed that certain non-bank-issued ABCP included exposure to US sub-prime mortgage-backed securities. Counterparties refused to roll the related paper, and \$33 million of the paper became frozen as a result of a standstill agreement in which the Bank of Canada and the major banks all participated. The crisis was arguably precipitated because of a regulatory peculiarity that denied the issues access to liquidity loans. The Office of the Superintendent of Financial Instruments (OSFI) established that ABCP obtain liquidity loans in case of a “general market disruption”. However, the lenders took the position that the condition precedent had not been met—there was no general market disruption. OSFI has disclaimed responsibility because the troubled ABCP was issued by non-banks. The investors agreed to a workout agreement in the third week of April. The House of Commons finance committee is intending to start hearings on the ABCP incident in early May. The committee will call upon federal and provincial regulatory authorities, including OSFI, the ISDA, the banking ombudsman and the various provincial securities commissions.

In 1998 and then again in 2006 the federal government has commissioned reviews of the fragmented securities regulation system and has received reports calling for a single national system for securities regulation. Since the ABCP incident, the Minister of Finance has pointed to the absence of a single securities regulator as one of the reasons for the failure. The call for a single regulator has been renewed after the SEC made it clear in March of this year that one of the reasons it had opened mutual recognition negotiations with Australia is because each maintains a single national system for securities regulation. The provincial regulators (except Ontario) have reached consensus that it would be preferable for issuers to have a “passport system” by which the approval of a prospectus in one jurisdiction would make it exempt from approval in the other jurisdictions. It may be that the current market shock will give new life to this discussion.