INVESTMENT DEALERS ASSOCIATION OF CANADA

JOSEPH J. OLIVER
PRESIDENT AND CHIEF EXECUTIVE OFFICER

Mr. Purdy Crawford
Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario M5X 1B8

September 5, 2002

Dear Purdy,

Attached please find the IDA response to the Five Year Review Committee Draft Report Reviewing the Securities Act (Ontario). My colleagues and I would be pleased to meet with you and the other members of the Committee, at your convenience, to elaborate on any matters contained in our submission. In the meantime, I am, of course, available to answers questions or supply more information related to our response.

Sincerely,

SUITE 1600, 121 KING STREET WEST, TORONTO, ONTARIO M5H 3T9
(416) 865-3020 FAX (416) 364-0753 joliver@ida.ca

INVESTMENT DEALERS ASSOCIATION

COMMENT

ON THE DRAFT REPORT OF

THE FIVE-YEAR REVIEW COMMITTEE

REVIEWING THE SECURITIES ACT (ONTARIO)

August 2002

INTRODUCTION

The Securities Act (Ontario) requires that the Minister of Finance establish an Advisory Committee to review the Securities Act, solicit public comment and bring forward recommendations. The Committee, chaired by Purdy Crawford, Q.C. submitted its draft Report on May 29th, 2002. The Investment Dealers Assoc. is pleased to have an opportunity to respond to the Committee's recommendations.

The Five Year Review Committee ("the Committee") Draft Report describes four themes that emerged from their deliberations and makes eighty-five recommendations grouped in six areas: (1) The Role of the Commission in Capital Markets Regulation, (2) Flexible Regulation, (3) Regulation of Market Participants, (4) The Closed System and Secondary Markets, (5) Enhancing Fundamental Shareholder Rights, and (6) Enforcement.

The IDA supports many of the recommendations, particularly as they relate to more effective regulatory structures, rules and enforcement powers. Indeed, in an earlier submission dated May 30, 2002, to the Committee the IDA has recommended legislative changes that would give SRO's greater enforcement powers to compel documents and testimony, and enforce penalties.

However, the IDA has reservations about several of the conclusions of the Committee regarding (1) self-regulation, (2) standards for materiality and (3) the fragmentation of market conduct and fiscal solvency.

We are particularly concerned about the Committees comments on self-regulation as it applies to the securities industry in Canada and abroad. We agree that there is a conflict within the concept of self-regulation. However, we believe these conflicts are, and can continue to be, effectively addressed in order to allow the obvious benefits that self-regulation brings to the regulatory process to be preserved. Moreover, the optical advantage of bifurcating the self-regulatory model into its constituent regulatory and trade components does not justify, in our opinion, its negative consequences. The underlying dynamic in such a division needs to be explored fully and understood before recommending a course of action.

As the centerpiece of its observations, the Five Year Review Committee concludes that the existing framework for securities regulation in Canada is uncompetitive, costly and increasingly unresponsive to dynamic and innovative capital markets. It is telling that the key recommendation of the Committee is to advocate a single regulator for Canadian capital markets. This should be a clarion call to federal and provincial governments to address the pressing issue of an inefficient and uncompetitive securities regulatory structure.

ROLE OF THE COMMISSION IN CAPITAL MARKETS

Limited Progress on the Harmonization/Uniformity Agenda

In globally integrated capital markets the viability of domestic markets and an effective savings and investment process depends critically on efficient and cost effective regulation. Canada is seriously handicapped by a fragmented, balkanized and anachronistic regulatory system for capital markets that has burdened issuers and investors with excessive regulatory costs and impaired capital formation in the country, particularly for small and mid-sized enterprises. The Five Year Review Committee has lent another credible voice calling for a more harmonized and efficient system for capital markets regulation in Canada, pointing notably to the deficiencies of the existing regulatory structure. What is left unsaid in the Report is that, if inertia perseveres much longer, then financial markets and the savings-investment process in Canada will be at serious risk.

The Committee has been effective not only in pointing out the good intentions of the regulators but, importantly, the serious shortcomings of their actions. For example, several years ago Canadian regulators introduced a system of mutual reliance to streamline and harmonize regulation. The Committee concludes the system has fallen short of its objective and often operates at cross-purposes, as each jurisdiction retains and exercises its statutory discretion. Further, building a system of national and multi-national instruments to create greater uniformity in regulatory policy has made little headway. Even though agreement has been reached on various national instruments, the system has proven unwieldy and inefficient by relying on consensus for implementation and change. As well, consensus has not been achieved in key areas. It is unfortunate that regulators have failed to achieve agreement on reforms for the private placement market. The recent reforms of the closed system differ significantly among the major provincial jurisdictions, adding to the inefficiencies and cost of securities issuance for small and mid-sized companies.

The IDA commends the Committee for pointing out the need for greater harmonization in securities regulation. The Committee has been particularly effective in demonstrating the difficulties in achieving positive results through the coordinated efforts of provincial regulators. There is a clear and pressing need for political leadership, at both the Federal and provincial level, to address the issue of regulatory structure and to reach a decision that can be implemented quickly. This issue has languished in part because no single policy maker has jurisdiction to effect a national solution to what is an important national issue, with significant regional implications. However, the negative consequences of not acting are becoming unacceptably high.

The Committee concludes the broadly based and complex policy agenda of the securities commissions has interfered with the mandate of the commissions for regulatory reform. In recent years, the Commission has responded with some alacrity to the ongoing regulatory needs of a growing and innovative marketplace, a task made more difficult by the need for consensus among the thirteen commissions, at least on the big issues. A

diverse and expanding agenda of regulatory initiatives has interfered with the timely completion of important initiatives, including the Integrated Disclosure System (IDS) system, debt market regulation, policy on communicating with beneficial owners of securities, and conflicts of interest. The Committee rightly calls for the better management of the regulatory agenda by commission staff, aimed at dedicating scarce resources to priority issues and ensuring these initiatives reach completion as quickly as possible.

Fragmented Market Conduct and Fiscal Solvency Regulation

It is noteworthy that while many of the Committee's recommendations have as their objective more integrated, seamless regulatory structures, the Committee recommends the fragmentation of market conduct and fiscal solvency regulation. The IDA as a national securities market conduct and fiscal solvency regulator has a unique perspective on this issue. It has been our experience that market misconduct is sometimes associated with the deteriorating financial health of the firm. The market conduct and fiscal solvency examinations are an important source of risk assessment data which is a prerequisite for preventative, forward looking regulatory intervention. In addition, it is interesting to note that the NASDR and NYSE are both a market conduct and fiscal solvency regulatory and indeed they make no organizational distinction between the two areas. It is our belief, supported by our experience that market conduct and fiscal solvency regulation are more effective if done in an integrated fashion.

FLEXIBLE REGULATION

Tackling Financial Planning

The Committee emphasizes the dual mandate of the OSC - to protect the investing public and foster efficient and fair markets. These two objectives are often in conflict, as measures to protect the investing public impose rules and related compliance procedures on market intermediaries, and may also influence the actual execution of transactions in market practice. Regulation typically places more emphasis on investor protection as it is seen as the more immediate and tangible policy objective and accomplishment. Since most well-intentioned regulations aimed at meeting investor protection or market efficiency goals have a cost associated with them, good regulation requires an effective assessment of the net benefit to market and investors from these particular initiatives.

The Committee makes a positive contribution by emphasizing the need for vigorous cost-benefit analysis in the rulemaking exercise to achieve the right regulatory balance between protection and efficiency. Cost benefit analysis is often based upon a false premise – the need to choose between "right" and "wrong' policy. In fact the decision is nearly always the much harder decision of choosing between good and better policy. The latter premise requires rigorous cost benefit analysis based on empirical data. This means that regulators must go beyond merely articulating the advantages of cost/benefit analysis and embrace arguments based on data.

The Committee observes that the financial advice and services offered by professionals have become increasingly sophisticated and comprehensive. It is important to note, however, that current dealer registration and related professional requirements contemplate financial advice provided in the context of a securities transaction – the know your client and suitability requirements are evidence of this interrelationship. By contrast, as the Committee points out, discount dealers provide no investment advice and charge a much reduced per transaction fee to reflect that they are offering trade execution only. Therefore, a thorough review of the definitions around the registration categories of adviser and trader would need to be undertaken prior to any changes in this area.

The advisory role of the industry professional has moved across the spectrum from advising on individual securities to discretionary money management and comprehensive financial planning. This is the result of the increasing sophistication of the advisory business and the inevitable unbundling of financial services. The IDA agrees with the Committee that more stringent standards are needed for financial planners. Indeed, several years ago, the IDA approved in principle the creation of a proficiency standard for registrants who hold themselves out as financial planners. However, proposed standards for proficiency and compliance and enforcement of related business activities must be considered carefully and balance the need for investor protection against the related compliance costs to market participants. In this regard, the self-regulatory system for the securities industry and mutual fund industry should be integral to the regulatory

proposals. As well, these proposals should have buy-in from the major jurisdictions to encourage uniformity in the financial planning regime.

Abandoning Universal Registration

The IDA supports the Committee recommendation to eliminate the universal registration system in Ontario. It is noteworthy that this system, in place since the late 1980s, has not been endorsed by any other major securities jurisdiction in Canada. This is not surprising. The purpose of universal registration is to identify through registration all participants active in capital markets. However, unless the commission is prepared to monitor the market activities of these participants, which is not the case now nor contemplated in the future, universal registration serves no useful purpose and simply adds to the cost of carrying out financial business. Moreover, this objective is overwhelmed by the related costs of complying with registration requirements. Even though the requirements are relatively minimal for those not dealing with the investing public (no capital adequacy rules or reporting requirements), these minimal requirements serve no useful purpose. Universal registration should be abandoned.

THE DUAL MANDATE

The Draft Report states that "ideally" SRO and trade association functions should be carried out by two separate bodies. The justification given for this separation is the potential for conflict between the two roles.

There is a generally understood conflict between investor protection and the need to foster fair, efficient and vibrant capital markets.[1] In this respect, the OSC has the same potential conflict of interest in pursuing its dual mandate as does the IDA. The response of the Ontario government in 1998 was to create an agency more independent of government, in part to make the agency more effective in pursuing the second aspect of its mandate.

Furthermore, the Draft Report confuses (a) the conflict of interest inherent in self-regulation, which is real and has been appropriately addressed, as discussed in our initial submission and reiterated below and (b) the alleged conflict between the regulatory and advocacy roles.

The justification for the IDA's dual mandate is based on the advantages to both the investing public and our members. In addition, we believe there is no meaningful conflict, beyond the conflict inherent in self-regulation, that should concern the regulators or investors. To the extent such a conflict arises, there are mechanisms in place to deal with them constructively, in the public interest.

In our initial submission to the Committee, we analyzed the dual mandate from both the regulatory and trade association perspectives to demonstrate that neither the public interest nor the members' interests are prejudiced. We concluded then and still believe today that there is no substantive problem with the dual mandate. To our knowledge, the fire wall insulating Compliance and Enforcement from member involvement has never been breached. As a result, the dual mandate has never undermined the integrity of the Association nor resulted in a major scandal in recorded memory. It is noteworthy that the Draft Report does not allege a breach in the integrity of the Association. The Draft Report does, however, raise the concern about whether the SRO will set standards as high as an arm's length organization might and whether enforcement would be as forceful. Those concerns, which we do not believe are justifiable, could as easily arise in a separate SRO.

The Draft Report also asserts that "it is increasingly rare to find one entity carrying out the dual role." Our Exhibit I lists a sample of such organizations in Canada and elsewhere. Furthermore, we are unaware of any Association that has been required to separate its dual mandate, so clearly there is no trend in that direction. To the contrary, we understand that in Australia, a formerly pure trade association, is now in the process

[1] This is a paraphrase of the Mission of the CSA that includes all provincial and territorial securities regulators.

of acquiring SRO responsibilities. Significantly, the NYSE regulates about 600 of the largest firms who conduct well over 90% of the securities business in the US, while at the same time owning the market it regulates, arguably a more substantive conflict.

Finally, in the same section, the Draft Report refers to the elimination of self-regulation in the UK. This, of course, is a different issue. In any event, self-regulation was considerably undermined in the UK by government involvement and then racked by scandals. The IDA's track record is not comparable.

The motives underlying this decision were unique to the UK experience and cannot be attributed per se to conflict of interest concerns inherent in self-regulation. Unlike Canada and the United States, the UK has never had a history of self-regulation in the financial sector. Indeed, until the mid-1980s regulation of financial institutions (prior to the amalgamation of Jobbers and Brokers), divided (with a high degree of informality) among the Bank of England, the Treasury, the Department of Trade and Industry, and the London Stock Exchange. Following the recommendations of the Gower Commission in 1986, the United Kingdom set up a self-regulatory structure for the securities industry and managed fund industry with oversight by the Securities Investments Board (SIB) accountable to the Department of Trade and Industry. Over the ensuing ten years or so, the new regulatory structure was viewed as ineffective in the wake of a series of financial scandals, many occurring in the managed fund sector. This impression and reality was the consequence of a new and inexperienced self-regulatory construct and the lack of proper accountability to government authorities. Another important motivating factor for centralized financial regulation in the UK, under the Financial Services Authority, was the decision to overhaul the mandate of the Bank of England, removing responsibility for bank regulation from the central bank to government authorities.

For purposes of completeness, we will reiterate our analysis and follow it with a discussion of the potential consequences of separating the two functions.

SRO Representation

The IDA is involved in two types of advocacy, one related to its SRO responsibilities and the other related to its industry association role. The bulk of the Association's activities concern the self-regulatory role, which is comparable to that performed by NASDR. It should be emphasized that roughly 85% of the IDA's budget relates to regulation (Exhibit II). The SRO focus is on rules, regulations and policies enacted by governments or securities commissions and that impact on the self-regulatory responsibilities of the Association. Since self-regulation, by definition, contains a built-in conflict of interest, that conflict must be dealt with in a variety of ways, which are discussed in Exhibit III.

There presumably can be no problem with SRO advocacy, whereby IDA staff and members use their expertise and practical experience to assist regulatory authorities and others in developing, implementing and monitoring policies designed to achieve the dual goals of investor protection and efficiency of the capital markets. To preclude the

Association from such activity would deprive the Commissions of the experience they frequently seek and would prevent the industry from participating in the public interest debate on issues affecting the industry and markets. Indeed, to preclude such activity would be tantamount to eliminating a key advantage of self-regulation. There has been no suggestion, of which we are aware, to that effect.

A reference to the Mutual fund Dealers Association (MFDA), a single mandate SRO, is instructive. The mutual fund distributors (the prospective members of the MFDA) through a variety of Committees, public meetings and extensive communication, as well as membership on the Board of Directors, participated intensively in all phases of policy development, which resulted in the by-laws that govern the member firms. No one questioned or criticized that process. To the contrary, the lack of such involvement would have been entirely inappropriate. Their participation is identical to that of the securities industry in policy development at the IDA.

Exhibit IV provides an illustrative list of IDA policy assignment indicating the personnel assigned, the reasons for the choice of personnel responsible and the origin of the policy. What the list demonstrates is that the people involved in policy development (as opposed to policy drafting and of course implementation) are those with the expertise and interest in the specific policy being developed. The result is the best that self-regulation can provide - the most senior and experienced people in the industry and IDA staff analyzing, debating and providing input into policy, so that it will be appropriate and effective.

Industry Association Representation

First, it may be helpful to indicate what such activity is not. Executive Committee visits to the Premiers, Provincial Treasurers, the Minister of Finance and the Bank of Canada do not concern, as a rule, securities regulation. Rather, they deal with fiscal and monetary policy and are generally aimed at advancing policies we perceive to be in the public interest, rather than just the interest of our members. For example, fiscal restraint and concerns about inflation may be at odds with the short and intermediate-term profitability of our member firms.

In our initial submission, we stated that the concern, if any, would seem to be directed at advocacy, not directly related to securities regulation, but designed to achieve more narrow commercial objectives on the part of our members, with less focus on the broader public interest. There are very few instances of this kind of activity, although they may occur. Unfortunately, the Draft Report quoted the first sentence in this paragraph seemingly to capture our definition of advocacy, without including the second sentence.

What people may have in mind when they raise the apparent conflict are such matters as cross-border trading or reciprocity for trading system, which relate to the level playing field for Canadian dealers, compared to foreign competitors. However, these matters, while they affect the commercial interest of our members (and almost always others as well), do not relate to our SRO functions. Therefore, no incremental conflict of interest

need result from the industry representation function and the SRO responsibilities falling under the same Association umbrella.

Functional Separation

Even though there is no practical conflict between the self-regulatory and association functions, optics dictate an organizational distinctiveness in the form of a clear organizational structure, with identifiable nomenclature and fire walls, where appropriate. To be clear, there is no involvement whatsoever by the Industry Relations and Representation Department in the decisions made by member regulation staff in the discharge of their compliance and enforcement functions. This distinction has always existed and was strengthened with the recent strategic review. Furthermore, as mentioned above, it has not, to our knowledge, ever been breached.

Consequences of Separating the Dual Mandate

It is important to examine the consequences of separating the regulatory and advocacy functions**,** thereby splitting apart an organization that has served the public interest and the securities industry with professionalism for over 86 years. This particularly so when the objection is based not on substance but rather on optics and perception.

In our opinion, there would be several negative consequences to a separation:

- Reduction of industry involvement
- Diminished regional input
- Diminished industry "buy-in" for effective compliance
- Additional economic burden
- Balkanization of advocacy and hardening of differences between bank-owned and independent firms

1. Reduced Self in Self-Regulation

The key advantage of self-regulation is the input of industry professionals who are close to markets, possess the expertise to understand the impact of proposed regulation and can recommend approaches that will most effectively meet a regulatory objective with minimum negative consequences to the efficiency and competitiveness of our capital markets. Experience in the United States suggests that NASDR (whose Board is soon to be merged back into the NASD Board) is viewed by many of its members as an arm of the SEC, perhaps in part because of the severe criticism it took for having placed its members commercial interests in the market it owned over the public interest in impartial market regulation. What is not clear is whether that more intimate tie is best serving the regulator or the public interest. In any event, we understand that it is NASDR's express desire to achieve greater member involvement to counter that perception and reality.

We are concerned that a bifurcated IDA, operating in a much smaller capital market than NASDR, would put a severe strain on the ability and willingness of the most senior market participants to contribute to the numerous committees that debate, respond to and generate regulatory policy for the Association. It is hard to believe that the head of Investment Banking or Fixed Income would sit on two committees dealing with the same subject, and if so, to what end. Having the 2IC attend in his or her place would either lessen the quality of the input or make it redundant. Furthermore, we cannot predict which Association's committees would better draw on the industry and we do not see how the volunteers' input would differ whether they were sitting on a SRO or Trade Association committee.

The Public Directors' views can be very helpful, especially in bringing a non-industry perspective (i.e. a non "self" perspective). However, were they to become dominant, with the industry's input confined to that of a suspect petitioner, it would represent a shift from self-regulation to third-party or private sector regulation, arguably a less useful model, because it is less expert.

We believe that the checks and balances currently in place, including regulatory approval of IDA by-laws, CIPF minimum standards, comprehensive oversight and Commission review of discipline decisions give the Commissions all the practical authority they need to make sure the Association places the public interest first. What is most important for the Commissions is that they continue to benefit from the advantage that self-regulation brings to their responsibilities.

2. Diminished Regional Input

Directly related to the likely dispersion of member input, could be a diminished regional input, which explains why support for the dual mandate is strongest in the West. The IDA draws on all our members across the country for our Executive Committee, Board, District Councils, Discipline Panels and numerous permanent and ad hoc committees. To the extent that market participants are farther removed from the development of regulatory policy, there would be a centralizing tendency, concentrated in Toronto. This centralization would exacerbate concerns outside Ontario that regulatory policy is insufficiently sensitive to the legitimate interests and concerns of the other provinces.

The IDA has played a useful role for the CSA as a truly national self-regulatory organization, with intensive involvement across the country. Anything which undermines that regional sensitivity would not serve the interests of the CSA collectively or its members individually. It would not make the current system work as well nor would it help those arguing for a national commission, where concerns about concentration are at their most acute.

3. Diminished Industry "Buy-in" for Effective Compliance

A critical pre-condition to a successful regulatory and self-regulatory regime is a high degree of voluntary compliance. It is simply not practical or financially feasible to direct compliance at every firm in the industry. Therefore, it is important that there be a high degree of "buy-in" by member firms, which can be achieved through active participation in the policy development process. The Canadian model is effective for that very reason. To the extent that the self in self-regulation is diminished, that buy-in would be reduced.

4. Additional Economic Burden

The Canadian capital markets are relatively small, roughly 2% of the global market. Therefore, it is critical that the regulatory burden not undermine efficiency and competitiveness. Recently, the creation of the MFDA and RS Inc. has imposed higher fees on member firms. The bifurcation of the IDA would further increase the financial and human resource costs for market participants, already reeling under adverse market conditions and an increased regulatory and self-regulatory burden. The legitimate public policy issue is whether that additional burden can be justified by the perceived optical advantages of splitting up an 86-year old organization.

5. Potential Balkanization of Advocacy

At this stage, it is not possible to predict whether a split of the dual mandate would create one or more additional industry associations. If the investment firms see the advantage of staying together, they would still have to address the additional financial burden and time required to devote to 2 organizations, to the extent they can justify that duplicative investment of time. Alternatively, the bank-owned firms may decide they do not wish to subsidize an advocacy association that does not fully reflect their perspective and interests. And the independent firms may wish to advance a case about industry concentration and related issues. In that event, a more fractious industry will develop, which may not be healthy for Canadian capital markets, easy for policy makers or in the interests of either bank-owned or independent firms.

THE CLOSED SYSTEM AND SECONDARY MARKETS

Continuous Disclosure

The Committee follows the lead taken by the commissions that the disclosure regime for issuers needs to be overhauled to facilitate capital-raising and issuer participation in markets. The Committee rightly argues that a more efficient disclosure system strengthens investor confidence and reduces the emphasis on prospectus disclosure, thus improving the timeliness and efficiency of the capital-raising process.

The Committee notes that upgrading and placing greater emphasis on continuous disclosure has become the locus of disclosure reform. Specific reference is made to the CSA Proposal for the Integrated Disclosure System and the Continuous Market Access System proposed by the BC Securities Commission in the context of their deregulation project. The IDA has commented favourably on the IDS system but notes that limited progress has been made in turning the system into reality. The IDA agrees with the Committee that an effective disclosure system premised on efficient continuous disclosure, and placing less emphasis on offering documents will assist large and small companies raise capital on timely and cost-efficient terms. An efficient continuous disclosure regime will eventually merge much of the private market issuance into the public markets and, over time, reduce the importance of the closed system based on prospectus exemptions.

The Continuous Market Access System proposed in the BCSC Concepts Paper puts forward several innovative proposals for reforming the new issuance system. The drafting of a Uniform Securities Act that is now an ongoing exercise provides a unique opportunity for the CSA to build a new disclosure regime for secondary and primary markets that takes the best attributes of the earlier proposed IDS system and the CMA system. We encourage the CSA to give this initiative priority.

Failing to Harmonize the Closed System

The Committee makes the valid point that, despite recent reforms, the closed system is still overly intrusive, complex and inefficient. The private market remains a key marketplace for small companies to raise needed risk capital, particularly given the apparent inability for regulators to reform public market disclosure. The CSA should redouble efforts to reach a consensus on a more simplified regime for private market financing, and common standards for the different jurisdictions. The significant difference across the major jurisdictions inhibits capital-raising by mid-size companies that issue across several jurisdictions.

Problems with the Continuous Disclosure Regime

The Committee makes the key observation that reforms focused on upgrading the quality of continuous disclosure and relative influence of these documents in the disclosure process can only be effective if two conditions are met: (i) the provinces achieve much greater harmonization in the continuous disclosure model, particularly in terms of definitional matters and substantive disclosure differences, and (ii) the implementation of the statutory civil liability regime for continuous disclosure. As the Committee notes there is no harmonized approach to the continuous disclosure regime across Canada. The definition of key terms such as "material change" and "insider" differ across jurisdictions. The requirements related to insider trading and AIF requirements, for example, differ. The standards for financial statements also differ. Efforts must be made to achieve greater uniformity.

The Committee notes that the debate over civil liability has had a long and tortuous history over the past twenty years. The process culminated in the publication of draft legislative amendments in late 2000. These amendments addressed the principal objections to the statutory civil regime, notably the possible inundation of spurious claims, through procedural mechanisms to screen out unmeritorious claims, the concept of "loser pays costs" and proportionate liability provisions. The failure of provincial legislative bodies across the country to pass the CSA legislation is egregious and imposes a serious hidden cost on issuers and investors, weighing down the competitiveness of Canadian markets.

Appropriate Standards for Materiality

The standard of materiality is integral to the continuous disclosure regime as it defines what constitutes material change and material fact. Materiality under Canadian law is defined as that change of fact that has significant effect upon the price or value of a security. The US definition is somewhat different, focusing on the "reasonable investor" test, namely information that a reasonable investor would consider important in making an investment decision.

The Committee recommends that the Canadian definition be replaced with the US definition, despite investor familiarity with the Canadian concept and the long history of jurisprudence premised on the Canadian definition. The rationale taken by the Committee to propose the US definition is simply to achieve equivalence with the US definition. We believe the Committee has gone too far and should retain the "market impact" definition. There are several reasons for this position: (i) there is a familiarity and understanding of the Canadian definition that buttresses investor confidence. This familiarity is particularly important with the imminent introduction of statutory civil liability for continuous disclosure, and (ii) there is, at bottom, no meaningful difference in the definitions to justify the Committee decision since an investor will only regard as important a material change of fact that affects the market price or value of the security in

question. If however, the committee chooses to adopt an investor test we recommend adoption of a test based on importance to an investor, not mere relevance.

Selective Disclosure

The Committee takes the right approach on selective disclosure. Proposed regulations to prohibit selective disclosure in the US have been fiercely debated with the proponents arguing for fairer disclosure against those concerned about the onset of "disclosure chill". The verdict on SEC Regulation FD is still unclear. The Committee notes that, unlike the United States, Canadian laws are specific and comprehensive in respect of insider trading and the "tipping" regime. The issue for Canadian markets is that the disclosure rules are not well understood and Canadian issuers and investors sometimes fail to comply with the rules. The remedies in Canada embrace making issuers and investors aware of the rules, more effective corporate governance in respect of disclosure and vigorous enforcement of the rules. There is no need for more rules. In this regard, the Committee notes that the CSA seems to have taken the right approach.

Independent Governance Body for Mutual Funds

The IDA agrees with the Committee observation that independent oversight of the fund manager and management company for publicly offered mutual funds is long overdue in Canada. There have been numerous proposals for such Board oversight, including the Stromberg Report in the mid 1990s and, more recently, the CSA Concept Proposal for an independent agency to supervise the management of mutual funds. In the United States, under the Investment Companies Act, investment funds are required to have a Board of Directors including independent directors.

The Committee recommends that an independent governance body for all mutual funds be established. The Committee would give the governance body sufficient power to terminate the mutual fund manager in cases that include (i) the poor performance of a fund and (ii) evidence of self-dealing, conflicts of interest and breaches of fiduciary obligations.

The IDA supports the proposal for an independent governance body for mutual funds, but concludes that the suggested powers given to the governance body are too broad. While it is appropriate to give the governance body the right to terminate a fund manager for self-dealing and conflicts of interest, given the fiduciary responsibility to unitholders, the independent governance body should not have the power to terminate the manager solely for poor performance of the fund.

ENFORCEMENT

Overview

The IDA agrees with the Committee's recommendation for enhanced enforcement powers for the OSC. The committee's recommendations for change are consistent with the mission of the IDA and more particularly, the mandate of our Member Regulation Department.

As the committee is no doubt aware, the International Organization of Securities Commission's Objectives and Principles of Securities Regulation describe SROs as a "valuable component" of a modern regulatory system. Similarly, a committee of IOSCO released a report describing SROs as "an effective and efficient form of regulation for the complex, dynamic and ever-changing financial services industry."

The partnership of public and private regulators has served the needs of the investing public in Ontario well. The partnership takes advantage of a number of SRO strengths: 1) industry applying its unique knowledge and expertise to complex and rapidly evolving policy areas; 2) by-laws that can be more flexible and more responsive to market developments than legislated rules; 3) the public benefit by ensuring industry buy-in; 4) the cost of self-regulation being borne by the securities industry, not the taxpayers; 5) the drawing together of practitioners with a vested interest in a well regulated capital markets which foster consumer confidence; and 6) a level competitive playing field and one that encourages investor and issuer participation. The industry understands that healthy markets depend on public trust and confidence; confidence in disclosure, fair pricing, fulfillment of fiduciary obligations that put the clients first – and enforcement when things go wrong. Again, these are principles common to the Commission and the IDA.

We acknowledge that our own views on the breadth of SRO enforcement powers have changed since our original submission to the Committee two years ago. Much has changed in the intervening years. The Committee has recognized those changes and the need to respond with a credible effective enforcement capacity. Recently the IDA, the MFDA and RS Inc. made a joint recommendation to the Committee to consider providing SRO's with greater powers to compel documents and testimony in the investigation and hearing process as well as more effective tools to enforce penalties. We believe these recommendations complement the flexible approach advocated by the Committee and provides additional tools that can be tailored to the needs of a rapidly changing market place. Our proposed legislative changes would not only enhance our effectiveness and thereby, the protection of the investing public, but further strengthen the effectiveness and efficiency of the Commission. As you no doubt are aware, many enforcement matters are referred by the Commission to SROs for enforcement and therefore, our work is really an extension of the Commission's responsibilities. Full details of these submissions have been provided to the Committee in separate correspondence.

What New Powers Should the Commission Have?

The motive for many securities related offences is monetary. The Commission must have the ability to ensure wrongdoers are not unjustly enriched. This can and should include the ability to assess administrative fines and disgorge unjust enrichment. The IDA agrees that disgorgement should be a multiple of the amount of profits actually realized. By providing the multiple factor, there is likely to be a greater deterrence than would be the case of a simple disgorgement of the amounts acquired. As the Committee noted, the IDA currently has the authority to assess fines of up to $1 million dollars per offence and seek disgorgement of up to three times the financial benefit which occurred to the individual as a result of the violation.

Furthermore, the Committee is correct in its assertion that such fines should not be viewed merely as a "cost of doing business" or a licensing fee. Although the amounts suggested are reasonable by today's standards, quantifying the maximum fine within the Act itself may restrict the ability to change the amounts to reflect future reality. As indicated in the Committee's reports, it took the legislative assembly over six years to pass amendments to the Ontario Securities Act. This demonstrates the rigidity and challenge that future changes would face. We would suggest that a better option would be to have the quantum of fine be set in regulation as opposed to a specific quantum in the Act.

The ability to impose administrative fines will provide greater certainty and clarity to potential wrongdoers concerning their potential liability. This alone re-enforces the deterrence aspect of sanctions. Under the present regime, the Commission has relied upon "voluntary payments" to overcome its inability to deny unjust enrichment. Such voluntary payments have provided some deterrent effect but lack the transparency and clarity that an express sanction would have.

The use of fines and disgorgement for reimbursement of Commission costs, public education and to be held in trust pending proof of claims are reasonable. Naturally, the holding of such funds pending proof of claims has some challenges, given that the proof of claims may involve considerable time and effort. It is suggested that the Commission consider what is an appropriate time that the money be kept in trust pending proof of a claim. How such a claim is established or proven is a much thornier issue. The Committee's report is silent on the issue; however, it is entirely foreseeable that victims would be disappointed as result of regulatory action by which they were unable to get redress for their losses. Such a result would do little to encourage confidence in the Commission and the markets. Therefore, it is our submission that the Committee may wish to canvas this area in greater depth and provide greater certainty in its recommendations on how disgorgement should be treated.

Breaches of Undertaking

The recommendations made to create a new offence under section 122 of the Act, for failing to fulfill, or contravene a written undertaking is fully supported. We also support

the suggestion that a separate offence include breaches of written undertakings given to SROs.

Restitution or Compensation Order

The Committee has rightly recognized that the amount of restitution that should be paid in any particular case may be difficult to assess. The conversion of the Commission to a forum for civil redress is fraught with risks. One of those risks is the diversion of Commission resources away from its primary enforcement objective. In particular, this includes determinations and assessments more properly within the expertise of the Superior Courts. The IDA believes that the recommendation to revisit this matter in the future after considering the experience of other jurisdictions is appropriate.

Ombudsman for Banking and Investments and Alternative Dispute Resolution

The Committee recommends the establishment of a national complaint handling system. The IDA is pleased to report that in December 2001, the Investment Dealers Association and the four other major industries of Canada's financial services sector (banks, life and health insurers, property and casualty insurers, and the mutual fund industry) announced the creation of a national ombudservice, the Centre for the Financial Services OmbudsNetwork (CFSON). The new initiative is expected to be in place later this summer – the Centre's Board was announced on 31 July.

The CFSON is an industry-based, integrated consumer assistance service that builds on existing industry consumer redress mechanisms, including the IDA's arbitration program, by providing a single point of entry for the consumer. By calling the CFSON's 1-800 number, clients with complaints about their financial services provider will be referred to the appropriate dispute resolution service. Depending on the individual facts of the case, the client will be referred to the financial institution, the industry's ombudsman, or to a further level of dispute resolution, where it is available.

Additionally, the participating industry groups will sponsor independent ombudsman services that will assess individual complaints, work fairly and impartially with both the consumer and the firm, and produce a report that includes recommendations. The services, which will be cost-free to clients, will operate independently of the industry association and will have their own Board, with a majority of independent directors.

The IDA, the Mutual Fund Dealers Association and the Investment Funds Institute of Canada have agreed to create a single ombudsman service for their member firms. As a group, the IDA, MFDA and IFIC decided to appoint the current Canadian Banking Ombudsman as the ombudservice for the securities industry, called the Ombudsman for Banking and Investments.

The OBI and the Centre will complement the existing arbitration system and provide the clients of IDA member firms with access to one of the most robust and comprehensive consumer redress systems in the world. The proposed By-Law to mandate the Association's Member firms participate in OBI and the CFSON was submitted to the Ontario Securities Commission in June 2002.

The IDA Arbitration Program is meant to provide a quick, low cost alternative dispute resolution forum for claims of $100,000 or less. It is the only SRO-sponsored program of its kind in Canada, provided at no cost to the taxpayer. The Committee, while generally supportive of the arbitration program, cites two disadvantages: i) cost and ii) the fact that there may be an imbalance of power.

The relative strengths of the contending parties in a dispute will always vary and has no necessary connection to the process the parties chose to resolve that dispute. These imbalances exist in the government-sponsored civil justice system as well, and it seems unfair in our view, to highlight this issue as a criticism of the arbitration program. The parties are who they are, and arbitrators act judicially to reduce any imbalance that exists.

As to cost, while the IDA has provided a forum for dispute resolution that is inexpensive compared to the civil justice system, it is not free. It should be remembered that there would be no need for an industry-sponsored arbitration program if the government-sponsored civil justice system was not so inefficient and expensive. In very rare cases the arbitrators do assess costs against the client, however, it has been our experience that this occurs only in cases where the result is justified on the facts. In the majority of cases, had these cases been taken to court the litigating clients would have been assessed the costs of the member's representation. Therefore, it is our belief that the arbitration system as established, is in fact cost effective, timely and attempts to level any imbalance in power that can be reasonably done.

The report also suggests that there is a lack of transparency in the arbitration program. The Committee recommended that member firms notify potential clients that there is an arbitration process at the commencement of their relationship or whenever a dispute arises. The IDA is pleased to report that By-law 37.2 requires that all IDA members provide the IDA alternative dispute brochure to all new clients or whenever a written complaint has been received from a client. This policy has been in place since April 2000.

The Committee also recommended that the IDA make available statistics relating to the use of the arbitration program. The IDA agrees with this recommendation and will develop a reporting format that does not create a disincentive to clients to seek arbitration, and complies with all federal, provincial and territorial privacy laws.

Finally, we believe the IDA arbitration program contrasts favourably with the arbitration program administered by the NASD in the U.S. In the United States, the arbitration process is more akin to true litigation than an arbitration process. The NASD model restricts both clients and member firms from litigating their claims in the courts. The

result is that the NASD arbitration process operates as a substitute litigation court and not as an alternative dispute resolution mechanism. This includes reliance on a body of precedence, discovery, and the full range of court type of litigation. Therefore, it is our submission that the parallels between the two systems are so remote than no reliance can be placed upon the U.S. experience. On the contrary, the U.S. experience has demonstrated that arbitration can become as time consuming, complex, and costly as the civil justice system.

Broadening of Existing Commission Powers

The IDA agrees with the recommendations broadening of the powers of the Commission. In fact, we are encouraged by the Committee's recommendation that the Commission be given broader powers to order compliance with the direction, decision, order or ruling of recognized self-regulatory organizations or exchanges. This would be very helpful to the IDA in certain circumstances and could be used to enforce self-regulatory powers such as the collection of fines.

Confidentiality under Section 16 of the Act

Again, the IDA is supportive of the recommendation that the Commission issue a policy statement providing interpretative guidance on the scope of confidentiality provisions in section 16 of the act and the process for making an application for disclosure under section 17 of the Act.

Need for an Anti-Fraud and Market Manipulation Provision

The need for the Act to expressly prohibit market manipulation and fraudulent activity is self-evident. Similarly, including a provision prohibiting a person or company from making a statement, written or oral, that the person or company knows or ought reasonably to know is a misrepresentation are logical. The present process of relying upon the broad enforcement powers in the public interest lends supports to the critics of enforcement actions that do not contain an identifiable violation of the Act. Providing specific offences of fraud, market manipulation and misrepresentation will add credibility to the enforcement process. Given the recent well-publicized allegations of fraud and misrepresentation in the public markets, it is the IDA's view that such amendments should be completed as quickly as possible to restore Ontario public confidence in the capital markets. For the same reason, the IDA supports the recommendation that the Commission consider pursuing alternative enforcement mechanisms as a regulatory response to illegal insider trading.

Conclusion on Enforcement

The Committee's report on the Commission's Enforcement role has been well thought out and well reasoned. As indicated, we would ask the Committee to consider our request for Securities Act amendments that will augment our ability to carry out our regulatory mandate more efficiently and to ensure that our investigations and hearings support the Commission as much as possible.

Exhibit I

REGULATORS THAT HAVE EXPRESS DUAL MANDATES

INTERNATIONAL

1. International Securities Market Association

The International Securities Market Association (ISMA) is the self-regulatory organization and trade association for the international securities market. ISMA has performed a central role by providing a global framework of industry-driven rules and recommendations which regulate and guide trading and settlement in this market. The Association also provides its member firms with a range of other services, products and support.

ISMA oversees the efficient functioning of the international securities market through the implementation and enforcement of a self-regulatory code covering trading, settlement and good market practice.

2. Korean Securities Dealers Association

The Korea Securities Dealers Association ("KSDA") was established under the Securities and Exchange Act and its principle function is to promote self-regulation in Korea's securities industry. The KSDA enforces self-regulatory rules to maintain fairness and raise public and institutional confidence in the securities market. The KSDA maintains ongoing communication with the government to provide comments or suggestions regarding policy issues or other matter that may improve rules and regulations related to the securities market.

CANADIAN

1. The Canadian Institute of Chartered Accountants

The CICA has a dual mandate for regulation and trade association type activities.

The CICA, together with the provincial and territorial institutes of chartered accountants, represents CAs and students. The CICA conducts research into current business issues and sets accounting and auditing standards for business, not-for-profit organizations and government. It issues guidance on control and governance, publishes professional literature, develops education programs and represents the CA profession nationally and internationally.

2. Real Estate Council of Ontario

The Real Estate Council of Ontario was established to administer the Real Estate and Business Brokers Act (REBBA) on behalf of the Ontario Ministry of Consumer and Business Services.

RECO's Board has established task forces to address issues affecting consumers and/or members. The role of each task force is to identify, research, consult, and make recommendations for improvements and potential legislative or regulatory change. Task forces members include consumer, industry and government representatives, as well as experts on specific areas of concern (e.g. regulatory law).

3. Ontario College of Pharmacists

The Ontario College of Pharmacists is the registering and regulating body for pharmacy in Ontario. All persons within Ontario who wish to dispense prescriptions and sell products defined as drugs to the public, must register as pharmacists with the College.

Beyond the statutory requirements, Council brings pharmacists' views to a central coordinating body. Here, members discuss policies and make recommendations to governments regarding legislation. Council provides direction to the Registrar for administration of that legislation. It also provides leadership and guidance for the profession in providing pharmaceutical services to the public.

SROS THAT MAY HAVE DUAL MANDATES IN PRACTICE

CANADIAN

1. The Law Society of Upper Canada

The Law Society of Upper Canada exists to govern the legal profession in the public interest. The Law Society regulates Ontario's legal profession to ensure a competent and ethical bar. The LSUC stresses the mandate of public interest and does not address an advocacy role on behalf of members in their mandate, mission or value statements. However, in practice the LSUC undertakes what can be characterized as advocacy on behalf of the members. This is evidenced by their lobbying activities and intervenor status in certain legal cases. In particular, the LSUC's role in promoting fair compensation for lawyers pertaining to legal aid reforms, the establishment of the task force related to paralegal issues, and the development of Title Plus all indicate an advocacy role on behalf of the membership.

2. The Association of Professional Engineers of Ontario

Professional Engineers Ontario licenses Ontario's professional engineers, and sets standards for and regulates engineering practice in the province. It has a statutory mandate under the Professional Engineers Act to protect the public interest.

It is also expected that PEO Council will bring proposals to the Ontario government that will ensure that public interest remains protected as the practice of engineering changes. The proposals are characterized as being in the public interest as opposed to for the benefit of members. The types of proposals made would have to be analysed to determine whether infact the proposals could be seen to be for the benefit of the members themselves.

REGULATORS THAT DO NOT HAVE DUAL MANDATES

INTERNATIONAL

1. UK - Financial Services Authority

The FSA is the single regulator of financial services, banking and insurance in the UK. It assumed responsibility for supervising firms formerly regulated by SROs. There is no reliance upon SROs under the new U.K. Act.

2. NASD - National Association of Securities Dealers

There is a clear distinction between the SRO, the NASD, and the lobby organization, the Securities Industry Association.

3. Australia - The Australian Securities and Investments Commission & The Securities Registrars Association of Australia Inc.

The Australian Securities and Investments Commission (ASIC) is an independent Commonwealth government body established by the Australian Securities and Investments Commission Act 1989. It began on 1 January 1991 as the Australian Securities Commission, to administer the Corporations Law. It replaced the National Companies and Securities Commission (NCSC) and the Corporate Affairs offices of the States and Territories.

The Australian Securities and Investments Commission enforces and administers Corporations Law and consumer protection law for investments, life and general insurance, superannuation and banking (except lending) throughout Australia. The ASIC has the function of monitoring and promoting market integrity and consumer protection in relation to the Australian financial system, the provision of financial services, and the payment system. It regulates and informs the public about Australian companies, financial markets, financial services organisations and professionals who deal and advise in investments, superannuation, insurance, deposit taking and credit.

The Securities Registrars Association of Australia Inc. provides a forum where members comprising registrars, stockbrokers and other securities industry participants discuss issues related to the industry. The SRA assists in the direction of the securities industry in Australia by making submissions to statutory authorities such as the Australian Stock Exchange and the Australian Securities Investment Commission.

CANADIAN

1. Royal College of Dental Surgeons of Ontario

The Ontario Dental Association performs "trade association" functions while the RCDSO is the regulator.

2. College of Occupational Therapists of Ontario

COTO is a regulator with a public interest mandate.

3. Ontario College of Teachers

The College sets and regulates teaching qualifications and standards of conduct, registers members, and investigates and disciplines members charged with professional misconduct. The Ontario Teachers Foundation, a separation body, is the official liaison between the teachers of the province and the Minister of Education.

4. College of Nurses of Ontario

The College of Nurses of Ontario's mission is to protect the public's right to quality nursing services by providing leadership to the nursing profession in self-regulation.

5. College of Physicians and Surgeons of Ontario

The College of Physicians and Surgeons of Ontario (CPSO) is the self-regulating body for the province's medical profession. The College regulates the practice of medicine to protect and serve the public interest.

The Canadian Medical Association, The Ontario College of Family Physicians and other such organizations act as the "trade associations" for the medical profession.

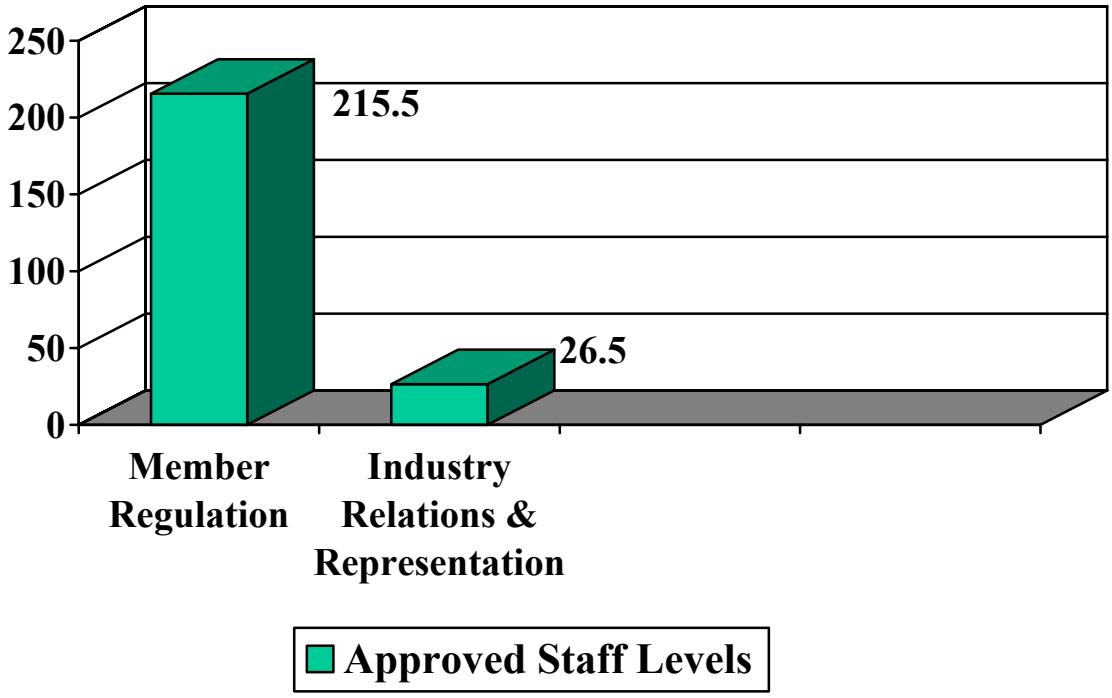
6. The College of Physiotherapists of Ontario

First and foremost, the College exists to protect the public interest. Unlike a professional association that acts to promote the interests of its members, the College acts to protect the public interest by regulating and continually improving the practice of physiotherapists.

7. The College of Respiratory Therapists of Ontario

The role of the College of Respiratory Therapists of Ontario is to regulate the profession of respiratory care in the public interest.

Exhibit II


250
200
150
100
50
0
215.5
26.5
Member Regulation
Industry Relations & Representation
Approved Staff Levels

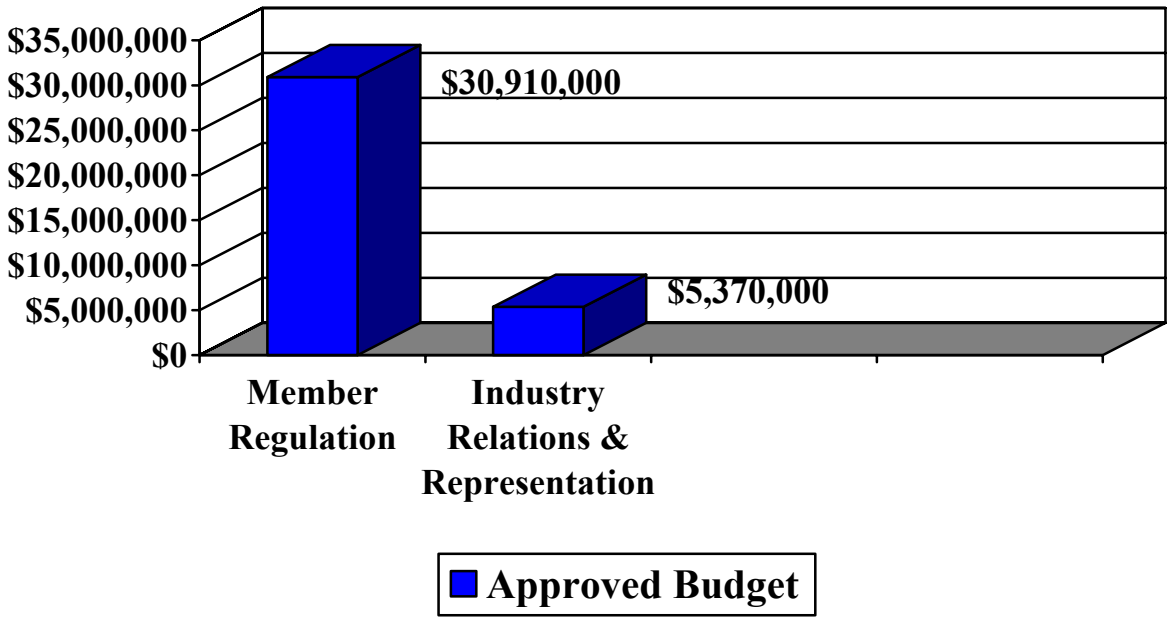

$35,000,000
$30,000,000
$25,000,000
$20,000,000
$15,000,000
$10,000,000
$5,000,000
$0
$30,910,000
$5,370,000
Member Regulation
Industry Relations & Representation
Approved Budget

Exhibit III

RESOLVING THE CONFLICT IN SELF-REGULATION

The nature of self-regulation implies a potential conflict, which must be addressed in a wide variety of ways, each of which contributes in some measure and all of which, when combined, make for an ethical, objective and effective self-regulatory organization.

(a) Goals, objectives, strategies and action plans are developed, implemented and supervised, consistent with a self-regulatory regime that is designed to be objective, professional, rigorous, open, and monitored.

(b) An appropriate number of Public Directors are elected to the Board and to the Executive Committee as well as the Audit, Compensation, Member Regulation Oversight, Human Resources and Pension Committees.

(c) Transparency is maintained in respect to by-law adoption, adjudicative procedures, governance structure and the committee system, as well as public submissions to regulatory authorities and the government.

(d) The Securities Commissions monitor the Association in accordance with the conditions of its recognition.

(e) There is accountability to the public, regulators and our members, directly and through the Executive Committee and the Board of Directors.

(f) The Member Regulation Oversight Committee of the Board oversees the Association's regulatory responsibilities.

(g) Attracting and retaining high caliber and ethical professionals is a high priority.

Compensation policy insulates compliance and investigative staff from membership evaluation.

Exhibit IV

ILLUSTRATIVE IDA POLICY DEVELOPMENT ASSIGNMENTS

REGULATORY POLICY	PERSONNEL ASSIGNED	REASON FOR CHOICE OF PERSONNEL RESPONSIBLE	ORIGINATION OF POLICY
Regulation of Debt Markets	IRR, then Member Regulation	Expertise	OSC
Capital Rules	Member Regulation Policy Dept./FAS	Expertise & Representation	FAS, Reg. Staff or CSA
Ombudsman	President/IRR	CSA request	Joint Forum of Securities and Insurance Regulators
Analyst Policy 11	IRR, then Member Regulation	IRR staff supported Crawford Committee – continuity	Crawford Committee
Proficiency Rules	IRR & Sales Compliance	Retail Sales Expertise	Retail Sales Committee, CSA, CSI
Enforcement Rules	Enforcement	Expertise	Member Regulation, Chambers Report, CSA
Request for enhanced enforcement powers	Enforcement	Expertise	Member Reg., MFDA, RS Inc.
Hagg Conflict Rules	IRR, then Member Reg.	IRR staff supported Hagg Committee – continuity	Hagg Committee/Corporate Finance Committee
Equity Markets/ATS	IRR/Member Regulation	Expertise, IRR staff supported Committee	OSC, Equity Markets Committee
BCSC Concept Paper	Pacific District Council, Member Regulation & IRR	Expertise and regional representation	Corporate Finance & Retail Sales Committees
Financial Planning	President, then IRR	Request of OSC	OSC, Retail Sales Committee
Québec Bill 107	Québec District Council, President	Regional representation	Québec legislature
National Registration Database	Member Regulation	Expertise	CSA
T+1	Member Regulation, President	Expertise, on Board of CCMA	CSA, Canadian Capital Markets Association
Risk Assessment	Member Reg., FAS	Expertise	Member Reg.