

Chapter 6

Request for Comments

6.1.1 Request for Comment - Proposed Revocation and Replacement of OSC Rule 13-502 Fees and Companion Policy 13-502CP Fees

REQUEST FOR COMMENT

PROPOSED REVOCATION AND REPLACEMENT OF OSC RULE 13-502 FEES AND COMPANION POLICY 13-502CP FEES

Request for comments

The Commission is publishing for a 90-day comment period Rule 13-502 *Fees* and Companion Policy 13-502CP *Fees*. The proposed Rule and Policy (collectively, the Proposed Materials) are intended to replace the rule and policy currently in force under the same number.

In addition to being published in this bulletin, the Proposed Materials are available on the Commission's website (www.osc.gov.on.ca).

We request comments on the Proposed Materials by November 10, 2005.

Substance and purpose of the Proposed Materials

The Proposed Materials are consistent with the current rule and policy. That is, the proposed Rule requires registrants, investment fund managers, and reporting issuers (other than most investment funds) to pay a "participation fee" each year. This fee is designed to reflect a market participant's proportionate participation in Ontario's capital markets in the upcoming year.

As with the current rule, the proposed Rule also requires the payment of "activity fees". These fees are designed to represent our direct cost where staff has undertaken certain activities for market participants (for example, reviewing a prospectus or a registration application).

While the basic principles of the current rule and policy remain, the Proposed Materials include a number of proposed changes that were made in an effort to:

- ensure consistency between the fees charged and our costs of providing services,
- improve the "readability" and "user-friendliness" of the current rule and policy by employing plain language principles and clarification where necessary,
- simplify the activity fee schedule, and
- address a number of concerns and comments raised by stakeholders.

The proposed Rule also returns the surplus collected from market participants between April 2003 and March 2006 in the form of reduced participation fees.

The most significant changes to the current rule are as follows:

1. Changes to class structure

Class 1 reporting issuer

We propose to expand the Class 1 definition to include reporting issuers whose listed or quoted securities do not include equity securities. This would mean that a reporting issuer with non-equity securities that are listed or quoted, and that is currently classified as a Class 2 reporting issuer, would be a Class 1 reporting issuer going forward. Therefore, when calculating its capitalization for the purpose of determining its participation fee, a Class 1 reporting issuer will be required to include all securities (including debt, warrants, options, etc.) that are listed or quoted, or are otherwise generally available to trade. This change will simplify the current class definitions.

Class 3 reporting issuer

In response to concerns raised by a number of stakeholders, we have revisited the definition of a Class 3 reporting issuer. We propose to replace the Class 3 reporting issuer category with three different categories for foreign reporting issuers: Class 3A, 3B and 3C. This change will better align participation fees for Class 3 reporting issuers with the benefits derived from participating in Ontario's capital markets. This will also simplify the calculation of capitalization for Class 3 reporting issuers.

Class 3A reporting issuer

The proposed definition of Class 3A reporting issuer includes foreign reporting issuers with a limited presence in the Ontario marketplace. We propose to limit the participation fee for Class 3A reporting issuers to \$600, which equals the lowest participation fee payable by a reporting issuer.

Class 3B reporting issuer

The proposed definition of Class 3B reporting issuer includes foreign reporting issuers whose trading volume on marketplaces in Canada is less than its trading volume on marketplaces outside of Canada. We propose to reduce the participation fee of Class 3B reporting issuers to the greater of \$600 and 1/3 of the participation fee prescribed under Appendix A of the proposed Rule.

Class 3C reporting issuer

The proposed definition of Class 3C reporting issuer includes foreign issuers whose trading volume on marketplaces in Canada is greater than its trading volume on marketplaces outside of Canada. The proposed Rule requires Class 3C reporting issuers to calculate their capitalization and participation fees in the same way as Class 1 reporting issuers. This will simplify the calculation of capitalization for Class 3C reporting issuers.

2. Additional exemption for subsidiary entities

The proposed Rule includes a new exemption from the requirement to pay a participation fee for a reporting issuer that is a subsidiary entity of another reporting issuer. This exemption will only be available to a subsidiary entity that is permitted to file the continuous disclosure documents of its parent in lieu of filing its own. This proposal will codify discretionary relief frequently granted under the current rule.

3. Form 13-502F6 – Subsidiary entity exemption notice

The proposed Rule requires a subsidiary entity to file a Form 13-502F6 if it is relying on an exemption from the requirement to pay a participation fee. This filing will ensure that we are aware of those issuers that are relying on an exemption.

4. Filing a revised Form 13-502F4 and Form 13-502F5

The current rule provides that a registrant firm that has determined its participation fee using estimated specified Ontario revenues must file a revised Form 13-502F4 and a Form 13-502F5 after it has calculated its participation fee using its actual specified Ontario revenues. The proposed Rule provides that these filings are only necessary if the second participation fee calculated differs from the first; that is, only if the registrant over- or under-paid its participation fee.

5. Changes to Appendix A – Corporate Finance Participation Fees

The participation fees for reporting issuers will be reduced at each level of capitalization. As a percentage of the current fee, the largest reduction will be experienced by smaller issuers. (See 'Anticipated costs and benefits' below for more detail on these changes.)

6. Changes to Appendix B – Capital Markets Participation Fees

The proposed capital markets participation fees have been revised in response to concerns raised by stakeholders. A new fourth tier is proposed for registrants with specified Ontario revenue between \$3 million and under \$5 million. A new tier is also proposed for registrants whose specified Ontario revenue is \$2 billion or more. In addition, the proposed participation fees are less at the three lowest levels of specified Ontario revenue and more at every other level. (See 'Anticipated costs and benefits' below for more detail on these changes.)

7. Changes to Appendix C – Activity fees

Prospectuses

Other than for certain investment fund prospectuses, item A of Appendix C proposes a single fee (\$3,000) for prospectuses, regardless of type or size of offering.

For an investment fund prospectus prepared in accordance with Form 81-101F1 and Form 81-101F2 the proposed fee is \$400. The current fee is \$600.

Fees for prospectuses prepared in accordance with Form 15 and Form 45 have been revised such that the fees are now similar to the fees payable for prospectuses in Form 41-501F1, with some adjustments for multiple funds filing.

In each case, these proposed changes better align the fees charged with the average cost of staff time spent reviewing the prospectus.

Applications for Relief, Approval or Recognition

Some fees under item E have increased, some have decreased, and some have stayed the same. We considered the resources required to process each type of application and have revised the fee structure to generally reflect our costs of the work required.

The fee to apply for a voluntary surrender of registration has been eliminated to encourage registrants to make the application rather than allow their registration to lapse.

Initial Annual Information Form under NI 44-101

Currently, under Item H the fee for filing an initial annual information form is \$2,000. National Instrument 44-101 *Short Form Prospectus Distributions* is currently being reviewed and it is anticipated that the requirement to file an initial annual information form will be removed. If this change is accepted as proposed, this item and its corresponding fee will be removed from the proposed Rule. In lieu of filing the initial annual information form, issuers will be required to file a "Notice Declaring Intention to be Qualified under National Instrument 44-101" and no fee will be payable for the filing of this notice.

Registration-related activity

The proposed fee for reviewing an application for registration as a dealer or adviser is \$600 (item I(1)). The proposed fee for reviewing a change to a firm's registration category is also \$600 (item I(2)). The fee currently charged under each of these items is \$800. This change better aligns the fee charged with the average cost of staff time spent reviewing these applications.

The proposed fee for reviewing an individual's application for registration is \$200 (items I(3) and (4)). The fee currently charged under these items is \$400. The reason for each of the above changes is that staff require less time to review registration applications since the introduction of the National Registration Database.

The efficiencies created by the National Registration Database have also resulted in a proposed reduction of fees for reviewing firms' applications for registration and continuing the registrations of amalgamating registrants (item I(5)). The proposed fee is \$2,000; the current fee is \$6,000.

The proposed fee for an application for amending the terms and conditions of a registration is \$500 (item I(6)). The current fee for this item is \$1,500. This change better aligns the fee charged with the average cost of staff time spent reviewing these applications.

Request for certified statement under section 139 of the Act

The current fee for requesting a certified statement under section 139 is \$500 (item K). The proposed fee is \$100, which better matches the cost of providing the certificate.

Commission requests

The proposed fee for a search of Commission records (item L(2)) is \$150. The current fee is \$10. This fee increase reflects the average staff resources required to undertake these searches.

"Request for one's own Form 4" (Item L(3)) has been added to Appendix C. The Commission will provide a Form 4 for a fee of \$30 under the proposed Rule.

Late fees

The proposed Rule provides that the late filing of a Form 13-502F4, a Form 13-502F5 or a Form 13-502F6 is subject to a late fee.

To ease the burden on staff of tracking late fees, the proposed rule uses the calendar year, rather than the fiscal year, as the period to which the \$5,000 maximum applies for registrants. For reporting issuers, the issuer's fiscal year continues to be the period to which the \$5,000 maximum applies.

Authority for the proposed rule

Paragraph 43 of subsection 143(1) of the Act authorizes the Commission to make rules "prescribing the fees payable to the Commission, including those for filing, for applications for registration or exemptions, for trades in securities, in respect of audits made by the Commission, and in connection with the administration of Ontario securities law".

Alternatives considered

In the process of developing this Rule, the Commission did not consider any other alternatives.

Unpublished materials

In proposing the rule and policy, the Commission has not relied on any significant unpublished study, report, decision or other written materials.

Anticipated costs and benefits**1. Aggregate fees**

Under the fee regime implemented in 2003, the Commission tries to set fees at levels to meet our operating costs. We do this by setting the fees charged under Rule 13-502 and Rule 13-503 (*Commodity Futures Act*) to match our projected costs over a three-year period, less any surplus of fees accumulated during the prior three year period.

Since the introduction of the fee rules both our costs and revenues have exceeded our original estimates. For the three years ending March 2006 our costs are expected to be \$11.3 million higher than forecast primarily due to additional staffing. Key growth areas have been Enforcement and the introduction and growth of our Investment Funds branch. Given the uncertainties of our new fee schedule, when it was developed we targeted a surplus of \$12.9 million as at March 31, 2006. In late 2004, we projected a significant surplus by March 2006 due to continued high revenues arising from stronger than expected market growth. In March 2005 we rebated \$15 million to industry participants based on their contribution to our surplus.

Our current projection for March 2006 is for a surplus of \$35.9 million. As shown in the following chart, this amount has been applied to reduce the proposed participation fees. The proposed fee amounts are the average fees per annum projected for the three year period covered by the proposal. Other revenues include interest earned and late fees received. The chart also shows the aggregate fees that the Commission expects to collect under the current fee regime during fiscal 2006.

	Current Fees	Proposed fees without surplus*	% Change	Proposed fees with surplus	% Change
Activity Fees	\$ 11,566,000	\$ 10,272,841	-11.2%	\$ 10,272,841	-11.2%
Participation Fees	\$ 54,900,000	\$ 60,877,362	10.9%	\$ 48,905,572	-10.9%
Sub-Total	\$ 66,466,000	\$ 71,150,203	7.0%	\$ 59,178,413	-11.0%
Other Revenues	\$ 3,120,000	\$ 2,400,000	-23.1%	\$ 2,400,000	-23.1%
Total Revenues	\$ 69,586,000	\$ 73,550,203	5.7%	\$ 61,578,413	-11.5%

*Under the proposal, the total fees paid by market participants will be reduced by 11.0%. This decrease results from an 11.2 % decrease in activity fees and a 10.9 % decrease in participation fees. The fees paid would have increased by 7.0% had we not been able to apply the \$35.9 million surplus when setting the new fees.

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For the three years covered by the new fees, our costs are projected to increase as shown in the table below. This is due to additional staffing (17 staff across 3 years), and general inflation of operating costs, such as salaries and benefits, and occupancy costs. The additional staff are anticipated primarily in Investment Funds and Enforcement to address such issues as the continuing growth of alternative investments and other novel product offerings, harmonization of regulation, and continuing improvements in the responsiveness of Enforcement actions. Forecast Commission operating results for the next three years are as follows:

	2006/2007	2007/2008	2008/2009	3 Yr. Average
<u>Revenues</u>		(\$ thousands)		
Activity Fees	10,273	10,273	10,273	10,273
Participation Fees	46,278	48,877	51,562	48,906
Other	2,400	2,400	2,400	2,400
Total Revenues	<u>58,951</u>	<u>61,550</u>	<u>64,235</u>	<u>61,579</u>
less Expenses	<u>70,257</u>	<u>73,426</u>	<u>76,950</u>	<u>73,544</u>
Net Shortfall	(11,306)	(11,876)	(12,715)	(11,966)
Opening Surplus	35,900	24,594	12,718	11,967
Closing Surplus	<u>24,594</u>	<u>12,718</u>	<u>3</u>	<u>1</u>

For the three years ending March 2009, we project a breakeven position, after fully applying the expected March 2006 surplus of \$35.9 million to reduce fees otherwise paid by participants. Any actual surplus or deficit at the end of this three year period will be reflected in the fee setting process for the following three years.

The Commission's revenues are subject to operating risk, such as market fluctuations or mergers of participants, which could materially reduce revenues. Also, due to the timing of the receipt of revenues (generally, approximately 70% of Commission revenues are received in the January to March period), the Commission is subject to cash flow fluctuations each year, which could be exacerbated by a sudden decline in revenues. If this occurs, the Commission has a reserve of \$20 million available to offset deficits or cash flow needs. The Commission could also borrow as necessary to address such issues on a short term basis.

2. Allocation of Fees within and between Groups

Our analysis of costs and revenues has confirmed that since the introduction of the new fee regime in 2003, issuers have been paying a disproportionate amount of our costs. In calculating the relative shares of the surplus to be returned to issuers and registrants we relied on the amount generated by each group. We calculated that 84% of the surplus was generated by reporting issuers and 16% was generated by registrants.

As a result, although total participation fees (after applying the surplus) are projected to decline by 10.9%, the impact will be different for registrants and issuers. Participation fees are projected to decrease by 40.5% for issuers and increase by 22.4% for registrants. The table below sets out the required participation fee changes with and without the benefit of the surplus.

	Current Participation Fees	Proposed fees without surplus	% Change	Proposed fees with surplus	% Change
Corporate Finance Fees	\$ 29,100,000	\$ 27,382,506	-5.9%	\$ 17,316,814	-40.5%
Capital Markets Fees	\$ 25,800,000	\$ 33,494,856	29.8%	\$ 31,588,758	22.4%
Total	<u>\$ 54,900,000</u>	<u>\$ 60,877,362</u>	10.9%	<u>\$ 48,905,572</u>	-10.9%

(The appendix to the proposed Companion Policy shows how the Commission has applied the surplus to each level of participation fee.)

The participation fee paid by an issuer will decline in the range of 40% to 57% depending on the issuer's fee tier. The most significant decreases will affect issuers in the lowest four tiers. This group, which represents 77% of issuers, will have an average decrease of 45%.

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In an effort to improve fairness to smaller registrants, the changes in fees for the various tiers were adjusted to reduce differences that existed in fees as a percentage of registrant revenue levels. Participation fees for registrants with revenues below \$3 million will decrease in the range of 10% to 38%. Participation fees for registrants with revenues between \$3 and \$5 million will increase by 32%. This group was underpaying under the previous fee structure. Participation fees for registrants with revenues of \$5 million or more will increase in the range of 9% to 13%. The percentage changes in fees are lower than the required overall increase in participation fee revenues for registrants due to projected movement of registrants through the tiers.

The overall effect of the changes to both sets of participation fees is that they will be more equitable in two respects. First, the proportion of capitalization or revenue paid in participation fees will be more similar across the fee levels. In addition, the proposed participation fees better reflect the actual regulatory costs associated with each group. That is, where issuers were bearing over 50% of these costs, under the proposed participation fees (before the surplus reduction) they will now cover 45%.

Comments

Interested parties are encouraged to make comments on the Proposed Materials. Submissions received by November 10, 2005 will be considered. Submissions received after that date may be considered, depending on the status of the initiative at that time.

Deliver your comments to the following address:

c/o John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 800, Box 55
Toronto, Ontario
M5H 3S8
jstevenson@osc.gov.on.ca

A diskette containing the submissions (in DOS or Windows format, preferably Word) should also be submitted.

The Commission will publish written comments received unless the Commission approves a commenter's request for confidentiality or the commenter withdraws its comment before the comment's publication.

Questions

Please refer your questions to any of:

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Text of the Proposed Materials

The text of the Proposed Materials follows.

August 12, 2005