



“Regulating in the New Financial Reality”

Speech by Howard Wetston

Chair, Ontario Securities Commission

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Good morning and welcome to OSC Dialogue 2011.

Dialogue is an important forum to consult with our stakeholders.

This is our first Dialogue in 4 years and it is timely given the dramatic developments in the capital markets in recent years. The pace of change continues to be rapid – indeed today’s financial landscape is quite different. We are just over 10 years into the 21st century and I believe we have experienced more change than in any previous decade.

The greater breadth and complexity of products (with disclosure that is comprehensive but not comprehensible); the growing importance of securities markets to financial stability (the total notional value of OTC Derivatives is greater than \$600 trillion U.S. worldwide); the growing interconnectness of global markets (systemic risk); securities sold with lightning speed across multiple marketplaces (IIROC now oversees an average of 200-250 million order and trade records daily); and the massive increase in the use of financial markets for retirement purposes.

All of this has combined to challenge some of the basic approaches to securities regulation. Worldwide, securities regulators are also coming to grips with this new financial reality.

The response to the G-20 requirements is bringing regulatory complexity to new heights. In the USA, for example, Dodd-Frank is over 2300 pages, may require over 240 new rules to implement and require over 60 studies.

With the background of a changing industry, regulatory reform initiatives driven at the international level, and increasing stakeholder expectations, we asked ourselves a simple question: “What does it take for the OSC to become the 21st century regulator of Ontario’s capital markets”?

In this new financial reality we must consider a more strategic approach to fulfilling our mandate of investor protection and fostering fair and efficient capital markets. While Canada weathered the crisis better than most markets, complacency is not an option. As such, we have been engaged in an extensive strategy review in recent months.

This review is also important given the upcoming Supreme Court of Canada reference with respect to the proposed Canadian Securities Act. Canada has clearly recognized the need to move swiftly to the new era of securities regulation, and whatever structure we end up with, the OSC will continue to play a pivotal role.

A great challenge facing regulators will be developing the capacity to keep up with new market developments that will surely emerge over time as a result of financial innovation or from second-order effects from the implementation of proposed rules.

In developing our strategy we consulted our staff and our stakeholders. We benchmarked ourselves against the best practices of other regulatory agencies around the world. We are preparing our Strategic Plan now. As a result, we are considering:

- Expanding the OSC's capability to conduct research and analysis by adopting a forward looking, fact-based approach in support of investor issues, market developments and rule making;

- Improving how we coordinate policy and set priorities;
- Aligning our program and operational activities with specific OSC goals;
and
- Bringing more focus to our engagement with investors.

There is an increasing recognition today that evidence-based policy making is key to better financial market regulation. Let me give you an example of what I'm talking about.

The exempt market has become increasingly important for investors and issuers. The total amount of capital raised through exempt distributions filed with the OSC in 2010 was about \$83 billion¹. Approximately \$44 billion² of that was raised in Ontario. New equity issues in 2010 across Canada were approximately \$41 billion. It is clear that there has been a significant migration from the public to the private markets. What implications does this have for policy making? Fact-based research will assist us in answering that question.

¹ Data on total amount of capital raised through exempt market distributions and amount raised in Ontario were clarified in January 2012

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Market Regulation and Derivatives

As an example of the direction we are headed in, let me talk about market regulation and derivatives.

The Canadian equity market has changed dramatically in recent years. We have moved from a single marketplace environment to multiple marketplaces, with exchanges and alternative trading systems trading the same securities. We have also seen the introduction of dark pools, which are marketplaces with no pre-trade transparency.

As the markets evolved, technology also evolved, increasing the speed, capacity and complexity of trading. These developments have had a huge impact on our market.

We have been focusing on the controls that are necessary to mitigate risks associated with electronic trading and introducing a framework to address them. Also, we have responded with a proposed regulatory framework for dark pools.

It's our view that providing some limits on their use is critical to maintaining the quality of the price discovery process.

These issues are also being considered by regulators globally. Last month, the U.K. Financial Services Authority (FSA) and the Securities and Exchange Commission (SEC) jointly hosted a roundtable with a number of regulators to discuss market structure issues including high frequency trading, market fragmentation and dark pools. It was an opportunity to share information and views on these developments.

The regulators also discussed the approaches that regulators might adopt in light of these market structure developments. It is critical that we have an appropriate framework in place for these new developments that ensures the quality of our markets going forward.

We are also in the process of reviewing Maple Group's proposed acquisition of TMX Group. This proposal raises complex and novel issues for the market. We are seeking comment on a broad range of issues, including the proposed governance structure and the definition of independent director,

potential conflicts of interest that could arise and measures to address this, and the proposed move to a vertical model integrating trading, clearing and settlement.

We have set hearing dates of December 1st and 2nd to make sure that we have an opportunity to have oral submissions from participants that have submitted comment letters.

I do want to acknowledge that Maple Group and the TMX Group announced yesterday that they have entered into a support agreement with respect to the proposed transaction. Maple also agreed to extend its offer until January 31, 2012.

We have also been extensively involved in developing new regulation in the area of OTC derivatives. These complicated financial instruments are expected to act as a hedge against risk but during the global financial crisis they exaggerated it.

Excessive leverage, interconnectness and opaqueness have created uncertainty and thus caused the G-20 to encourage the standardization, where possible, and exchange trading of these products, their clearing and settlement as well as reporting to a trade repository. While these efforts internationally may contribute to regulatory complexity, they will enhance investor protection and contribute to the reduction of systemic risk.

Emerging Market Issuers Review

The OSC's Emerging Market Issuers Review is an important example of oversight in the context of this new financial reality.

Staff from across the OSC are reviewing 24 reporting issuers from different industries in various emerging markets. We are trying to determine whether these emerging market issuers, as well as those involved in bringing the issuers to market and auditing their financial statements, provided the required disclosure and conducted the required due diligence.

Our preliminary findings have revealed important messages about the role of gatekeepers and boards. We have noted to date:

- Governance challenges when the issuer's management and bulk of operations are located in a foreign jurisdiction.
- Audit procedures that may be impacted by business practices in overseas jurisdictions.
- The inability of Canadian regulators to access audit working papers when the auditor resides in a foreign jurisdiction.
- And, the impact of local business practices on internal controls and risks.

I would like to touch on two things in light of these observations.

First, it is critical that advisors have adequate knowledge of the emerging market issuer, its business practices and the risks of operating in foreign markets.

Understanding the cultural norms and relationships that are needed for the emerging market issuer to operate in that environment are essential.

Second, examination and due-diligence procedures that would normally be considered appropriate in a North American environment may not address the business and cultural practices in an emerging market context.

We want our capital markets to remain attractive to issuers from other countries. Fostering markets that are fair and efficient will attract both domestic and foreign issuers, but in order to ensure investor protection it may be necessary for gatekeepers and boards to step up and carry out their duties with a greater degree of vigilance and oversight.

Strengthening Enforcement

While the OSC has in the past had to investigate cases that were international in scope, recent investigations demonstrate the investigative and jurisdictional challenges that some international cases pose for our Enforcement staff. Challenges related to geography, language and culture. Challenges in accessing records and interviewing individuals. My question is: Can we effectively enforce the Ontario Securities Act internationally?

The mind, management, assets, operations are overseas and often in emerging markets. Despite the challenge, we have a duty to our markets and investors to do whatever is reasonable and practical to investigate and take appropriate enforcement action.

Responding to the challenges posed by international enforcement files is an example of how we have intensified our enforcement over the past year. Our enforcement momentum is producing results, but we know that there's more to do. That's why staff recently proposed new policy initiatives to enhance the regime for the greater benefit of investors and the capital markets.

1. A program for explicit "no-enforcement action agreements".
2. The introduction of no-contest settlements.
3. A clarified process of self-reporting under the current credit for cooperation program.
4. Enhanced public disclosure of the credit granted for cooperation with the OSC.

These proposals are expected to improve the quality, quantity and timeliness of the information that comes into the OSC.

These tools will also allow our Enforcement staff to take decisive action to protect the interests of investors and the capital markets. Staff have invited comment on these proposals for 60 days.

Our policy proposals quickly generated an interesting public debate about the OSC's enforcement regime, which I am certain will be discussed in the plenary session later this morning.

Today's agenda also includes a plenary discussion and a breakout session on investor issues. Investor protection is a core part of the OSC's mandate and today's dialogue needed to reflect the importance of investor protection as an OSC priority.

Investor Protection

Our strategic review has identified the need for a clearly identifiable point of responsibility for investor interests, including greater analysis of the needs of

retail investors. We recognize that there is a perception that the OSC could be more focused on investors. We have a lot to do – but we are doing a lot.

Effective January 1, 2011, we introduced Fund Facts – stage one for mutual fund companies. Stage two of fund facts was published for comment on August 11, 2011.

In stage three, the CSA will publish for comment proposed requirements that would implement point of sale delivery for mutual funds.

Effective June 22, 2011, the CSA published proposals for enhanced disclosure about costs of investing and an account performance reporting requirement. If adopted, it would apply to both IIROC and MFDA dealers. The proposed document was tested with investors and registrants.

The Investor Advisory Panel is providing a broad range of investor feedback on proposed rules and policies. Two of the Panel members are participating in our conference today.

And lastly, the OSC and its Investor Education Fund supported efforts by the Ontario government to introduce a financial literacy program for students in Grades 4 to 12, which started in September.

Meanwhile, we have become involved in discussions about the future of dispute-resolution processes in Canada. The CSA strongly supports the existence of a single system of informal dispute-resolution to which investors can have recourse as an alternative to litigation or binding arbitration. From our perspective, a principal benefit of such a system is that it permits quicker resolution of complaints in a cost-effective manner. It also contributes to investor protection and confidence in the regulatory system.

There will be more discussion about complaint-handling systems in this morning's investor plenary session moderated by Vice-Chair Mary Condon.

Regulating in the context of a new financial reality requires not only a commitment to our priorities but also excellence in execution. I recognize

that change is difficult and I realize we are regulating in a period of the most dramatic change in decades.

We are examining internal procedures and finding ways to do even better.

Using information and technology more effectively.

Looking closely at our processes to make sure they are effective and efficient.

Ensuring the OSC is a good place to work and that we recruit the best people and keep them. In the end, our success depends on our people.

Today, we have outstanding people who are dedicated to fulfilling our mandate and have embraced the opportunity for change.

Against the background of changing markets and a changing industry, regulatory reform initiatives driven at the international level and by other major markets and increasing stakeholder expectations, we asked ourselves a

question “What does it take for the OSC to become the 21st century regulator of Ontario’s capital markets”?

The answer for us is to understand the new financial reality, to take a more strategic approach to fulfilling our mandate and to develop the capacity to keep up with market developments.

That’s what we have to do and that’s what we are going to do.

Thank you.