

PROVINCIAL/TERRITORIAL COUNCIL OF MINISTERS OF SECURITIES REGULATION

YEAR END PROGRESS REPORT December 2006

BACKGROUND

All provinces and territories, except Ontario, have signed the 2004 *Provincial/Territorial Memorandum of Understanding Regarding Securities Regulation* (MOU). The ministers responsible for securities regulation in these jurisdictions are members of the Provincial-Territorial Council of Ministers of Securities Regulation (Council).

The MOU committed signatory jurisdictions “to move ahead with a passport system for an improved securities regulatory framework, to develop highly harmonized securities laws, simplified where appropriate, and to explore further options to consolidate and/or strengthen co-ordination and consistency of securities laws among provinces and territories, including a commitment to explore, on an ongoing basis, new opportunities to strengthen the Canadian securities regulatory framework”.

The MOU, and accompanying Action Plan, contained one key commitment for 2005: implement the “passport” system of securities regulation. The first phase of the passport system was implemented by regulators through Multilateral Instrument 11-101 *Principal Regulator System* (MI 11-101), effective September 19, 2005. Once fully implemented, the passport system will provide a single window of access to market participants and a market participant would be able to access capital markets in multiple jurisdictions simply by dealing with the regulator and the law of its principal jurisdiction (typically, the jurisdiction where its head office is located).

The initial scope of the passport system was limited by a lack of harmonized legislation in two crucial areas:

- 1) “passport tools” to enable regulatory cooperation—so that a decision by one jurisdiction can be legally effective in all participating jurisdictions; and
- 2) “targeted Act amendments” to harmonize and modernize significant portions of existing *Securities Acts* in order to support expanded use of national instruments and the passport system.

The target date for implementation of these harmonized securities laws was the end of 2006.

Under the MOU, Ministers undertook to direct a review of fees by officials and regulators, to examine the fee structure in the context of a passport system. Ministers also committed to explore options for further reform of the securities framework that would respect individual provincial/territorial responsibilities for securities regulation.

One of the principles in the MOU is that the highest standards of investor protection be effectively and consistently applied. The MOU principles focus on ensuring that the regulatory system is also efficient, cost-effective, streamlined, simplified, adaptable to evolving marketplace conditions, transparent and accountable.

A Taskforce, chaired by Alberta and made up of representatives from provincial/ territorial governments, together with members of the Canadian Securities Administrators (CSA), has been working to implement the passport system according to work plans approved by the Council.

RESULTS ACHIEVED IN 2006

2006 saw unprecedented levels of activity, cooperation and coordination among MOU jurisdictions and the CSA to harmonize, modernize and reform the securities regulatory system.

Meetings and Consultations

The Council conducted three full-day meetings with the Taskforce and CSA officials, in February, June and November. Council members also met in June with the federal Minister of Finance and other provincial/territorial finance ministers to discuss securities regulation. Securities regulation was also discussed at the Western Premiers' conference. The Council met twice with members of the Crawford Panel to receive presentations on the Panel's work regarding a single securities regulator.

The Taskforce worked extensively with regulators and Ontario. It held several extensive meetings, including one with representatives of federal and provincial prosecutors, regulatory enforcement staff and commissioners, to discuss enforcement against securities fraud. Members of the Taskforce also met with the Task Force to Modernize Securities Legislation struck by the Investment Dealers Association of Canada.

Passport System and Highly Harmonized Securities Laws

Progress during 2006 reflected an unprecedented level of cooperation and coordination among governments and regulators in Canada.

- “Passport tools” legislation was developed in consultation with the CSA. Amendments were implemented in eight jurisdictions. All other participating jurisdictions have committed to implement such legislation by the end of 2007.
- “Targeted Act amendments” to modernize and harmonize securities laws were developed in consultation with the CSA. These amendments were implemented in five jurisdictions, and introduced in two more. All other participating jurisdictions have committed to implement such amendments by the end of 2007.
- In November 2006, the Council approved a work plan and project schedule to implement Phase Two of the passport system by the end of 2007. Phase Two will rely upon the “passport tools” and harmonized securities laws, together with various national instruments implemented by the CSA. It will significantly expand the single window of access and facilitate further extension of the passport system as additional areas are harmonized. For example, the CSA has been working on comprehensive registration reform for some time, and plans to publish proposed NI 31-103 *Registration Requirements* in February 2007. It is recognized that additional legislative amendments will be necessary to accommodate the new regime, but such legislation must await the appropriate degree of consensus in consultations on NI 31-103, and all MOU jurisdictions have committed to harmonize their securities legislation at the appropriate time. Phase Two of the passport system will accommodate harmonized rules governing

prospectuses, registration, exemptive relief applications, continuous disclosure, take over bids, issuer bids and some aspects of enforcement.

- Passport Phase Two will be proposed in the form of a new National Instrument to replace MI 11-101, to be published by the CSA in March 2007. This approach is consistent with the Council's standing invitation to Ontario to join the passport system so that the benefits of the system can be available to all market participants. If Ontario does not join the passport system, the plan is to implement Phase Two on schedule as a multilateral instrument.

Although some jurisdictions have been unable to meet the timelines set in 2004 for implementing legislative amendments, such delays are normal when dealing with such large legislative packages (ie 100+ pages of amendments or, in some jurisdictions, entirely new *Securities Acts*). All MOU jurisdictions have committed to implement the required legislation in 2007. The Council's crucial achievement is obtaining agreement in all MOU jurisdictions, and with the CSA, on the substance and policy of these reforms and on the next phase of expanding the passport system.

CSA Activity

The Council and the CSA work together in coordinating the harmonization and streamlining of regulatory requirements. This is necessary to ensure that legislation and rules will continue to complement one another through the constantly evolving processes of securities regulation. In 2006, the CSA:

- implemented a uniform rule dealing with the governance of investment funds (NI 81-107 *Independent Review Committee for Investment Funds*);
- published proposed uniform rules on takeover bids and issuer bids (NI 62-104 *Take-over Bids and Issuer Bids*) and general prospectus requirements (NI 41-101 *Prospectus Disclosure Requirements*);
- released proposals on harmonized internal control requirements (CSA Notice 52-313) reflecting a more streamlined approach as compared with US rules and previous Canadian proposals;
- prepared an updated report on current investor protection and enforcement provisions in various provinces, in response to a request from the Council;
- prepared a discussion paper on improving enforcement against securities fraud, in response to a request from the Council; and
- undertook a review of administrative enforcement by the CSA to see what improvements can be made.

Enforcement and Investor Protection

- Most MOU jurisdictions have enacted, introduced or are planning legislative amendments to enhance investor protection and harmonize enforcement mechanisms, including higher maximum administrative penalties for violations of securities laws.
- Provisions supporting a harmonized civil liability regime for secondary market disclosure were developed in consultation with the CSA, based on the regime Ontario brought into force at the end of 2005. Two jurisdictions have brought these provisions into force, four have introduced or enacted them, and all other participating MOU jurisdictions have committed to implement them by the end of 2007.

- Some jurisdictions have amended legislation to provide regulators with the authority to order financial compensation for losses sustained by investors and other jurisdictions are considering such legislation.
- A Council member presented the CSA paper on improving enforcement against securities fraud to the Federal/Provincial/Territorial Ministers of Justice at their meeting in October 2006. The Ministers of Justice agreed to set up a working group involving federal and provincial justice officials, securities regulators, police and provincial officials. The working group is expected to report in fall 2007.

Fee Review

Officials developed draft principles regarding fee structures under the passport system. These included the principles that each jurisdiction has the right to set its own fees, and that only the principal jurisdiction should be involved in collecting fees paid by those using the passport system. The Council instructed officials to consult with regulators on those principles. The Council also considered that proposals for a new fee structure should await full implementation of the passport system, to enable proper assessment of resulting operational changes and efficiencies.

Securities Transfer Acts

Provinces are adopting highly harmonized securities transfer legislation, which markedly reduces cost and risk in the securities settlement system and improves the global competitiveness of Canadian capital markets.

Alberta and Ontario implemented practically uniform *Securities Transfer Acts* in 2006. Saskatchewan introduced legislation, uniform with Alberta's, in November 2006 and other provinces are expected to do the same in 2007. The *Securities Transfer Acts* were developed by the CSA and provincial officials and are a significant achievement of interprovincial cooperation in responding to the needs of Canada's capital markets.

Canadian Public Accountability Board (CPAB)

CPAB is the federally incorporated, not-for-profit corporation created to provide independent oversight of auditors of public companies in Canada. CPAB derives its authority from CSA NI 52-108 *Auditor Oversight*. CPAB expressed concern that the lack of certain statutory powers and protections impedes its ability to fulfill its mandate. In 2005, the Council agreed that Ontario would chair a working group of the Taskforce to address CPAB's requests. The Council reviewed reports from the working group at their meetings in February and June.

Québec and Ontario both passed legislation regarding CPAB in 2006. Québec passed legislation in June, amending its *Chartered Accountants Act*. In December 2006, Ontario passed Bill 151, *An Act to enact various 2006 Budget measures, amend or repeal various Acts*, which included more prescriptive provisions dealing with CPAB.

The Council was concerned with certain aspects of Ontario's Bill 151, and instructed the Taskforce to develop a harmonized model in consultation with regulators and stakeholders and to present its recommendations to the Council in 2007.

ONTARIO'S PARTICIPATION IN SECURITIES REFORM

The Ontario Minister attended most Council Meetings in 2006 and Ontario officials participated in many Taskforce meetings and conference calls. The Ontario Securities Commission actively participates in the CSA. However, Ontario has not signed the MOU and has thus far declined to support the passport system.

Ontario's Bill 151, which passed in December 2006, did not contain the "passport tools" or all the "targeted Act amendments" that would be necessary in order for Ontario to participate in the passport system. Ontario has announced that it will bring forward additional amendments to Ontario securities legislation during the spring 2007 legislative session and the Council is hopeful that those amendments will enable Ontario to participate in the passport system.

The Council has maintained an open invitation for Ontario to join the passport system—with or without signing the MOU and acknowledging that Ontario may continue to advocate a single regulator—so that Ontario market participants can share in the benefits of the system. The Council notes that the stakeholders consulted by the Crawford Panel, and the Crawford Panel's final report, strongly urged Ontario to join the passport system. Accordingly, the Council endorsed the plan for Phase Two of the passport system to be proposed as a national instrument, so that Ontario can participate if it chooses. However, if Ontario chooses not to participate, the Council's plan is for MOU jurisdictions to implement Phase Two on schedule.

GOING FORWARD—PLANS FOR 2007

Legislative Amendments

- MOU jurisdictions that have not yet introduced or implemented the "passport tools" and "targeted Act amendments" required to support the passport system have committed to doing so in 2007.
- MOU jurisdictions that have not already done so will introduce amendments to harmonize or strengthen enforcement/investor protection provisions.
- It is anticipated that additional targeted Act amendments will be required to support the CSA's ongoing reform initiatives. Particularly, the Council expects amendments required to support the CSA's registration reform project and NI 31-103, and has committed to implement such amendments at the appropriate time.

Passport Phase Two Implementation

- The Council and Taskforce will actively monitor progress on the implementation of Phase Two of the passport system. The plan is for the CSA to publish a proposed National Instrument by the end of March 2007 and for the implementation of Phase Two by the end of 2007.

Enforcement

- The Council will continue to examine alternatives to improve enforcement, in consultation with stakeholders. The Council recognizes the current widespread dissatisfaction with enforcement and considers it necessary to take a systematic approach to this complex and important problem.
- The Council will be represented on the working group established by Federal/Provincial/Territorial Ministers of Justice to consider improvements to enforcement against securities fraud. The Council recognizes that this is an area of

shared jurisdiction and will consider the working group's recommendations in consultation with other stakeholders.

- The Council will also consider what improvements can be made to enforcement of securities regulation in areas of exclusive provincial jurisdiction, in consultation with the CSA.

Benchmarks

- The Taskforce and the CSA are seeking appropriate benchmarks for measuring the performance of Canada's securities regulatory system domestically, and for international comparative purposes.
- Some comparative analyses are conducted by external bodies such as the International Organization of Securities Commissions, the Organization for Economic Cooperation and Development and the International Monetary Fund, but none provide an accurate method to measure the impact of our present reforms.
- Interim progress will be reported to the Council in 2007.

Exploring Options for Further Reform

- The Council and Taskforce will analyze the recommendations in the recent report of the IDA Task Force to Modernize Securities Legislation, and consider whether any of those recommendations should be pursued at the present time
- The Council is interested in considering any reform that will improve Canada's securities regulatory system and the competitiveness of our capital markets. Recent recommendations for reform include suggestions for principles-based regulation, the use of cost-benefit analyses in assessing proposed new rules, proportionate regulation, the use of plain language in rules and disclosure documents, promoting the financial literacy of Canadians, transferring the adjudicative functions of securities commissions to independent adjudicative tribunals, the formation of a separate capital markets court, and many others.
- The Council will consult with regulators and other stakeholders to consider which proposals should be considered priorities, and what is the most efficient and coordinated approach to such proposals. The Council's intent is to pursue reform on a timely and highly harmonized basis.

REVIEWING PROGRESS

Ministers want to keep stakeholders informed of the progress that is being achieved. In addition to annual progress reports, press releases and access to other relevant information can be obtained at www.securitiescanada.org.