



INVESTMENT COUNSEL ASSOCIATION OF CANADA
Association des conseillers en gestion de portefeuille du Canada

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July 30, 2003

Mr. Michael Phelps, Chair
WPC
Committee to Review the Structure of Securities Regulation in Canada
P.O. Box 10026
700 West Georgia Street
Vancouver, B.C. V7Y 1B3

Via E-mail to: wpc-cpa@farris.com

Subject: **Canada's Regulatory System**

Dear Mr. Phelps:

The Investment Counsel Association of Canada (the ICAC) is the organization representing investment counsel and portfolio management firms in Canada. Collectively, the association's seventy-three Member firms manage almost \$500 billion in assets of individual and institutional investors.

The ICAC is pleased to have this opportunity to make its views known to your Committee about the state of securities regulation in Canada. In October of last year, the ICAC issued its position paper titled "The Path to Achieving a National Regulatory System for Canada". A copy of that paper is attached as Appendix A and is posted on our web site at <http://www.investmentcounsel.org/docs/PositionPaper.pdf>. In that paper, we discuss in detail the impact on the businesses of our Member firms of the present regulatory system and propose a process for change to the system. We are very pleased that two parallel consultations have been subsequently initiated and are somewhat sanguine about the political will to address the clearly stated concerns of the ICAC and of others.

In this comment letter, we will reiterate our major issues and ask that you refer extensively to our position paper for the detail supporting our position. On the matter of the disparate rules in the thirteen jurisdictions, we attach as Appendix B, a spreadsheet outlining the rules in all jurisdictions that affect our Member firms.

Major Issues

1. Application

Because the ICAC is not self-regulatory and its Members do not participate in any self-regulatory organization, Member firms must submit to the securities regulatory authority in *each* jurisdiction in which they operate. It must be clear to anyone reading this that ICAC Member firms are subjected to the anomalies in the present system to the greatest possible extent. Firms that operate on a national basis are faced with separate registrations, different but similar rules, different interpretations of the same rule, different requirements and a host of other annoying realities outlined on page 2 of the Position Paper.

The spreadsheet, attached as Appendix B, provides a quick snapshot of many of these annoying differences. These realities will *not* be resolved through a ‘passport system’ even though the registration process may become simpler.

2. Cost

In addition to the comments about cost contained in the Position Paper, we have become aware of the recent study by the UK Financial Services Authority in which the regulatory costs in several national jurisdictions were compared. While the study examined regulatory costs for securities, banking and insurance collectively, clearly Canada is now seen to be very expensive compared to the other jurisdictions surveyed. And it is simple to attribute the level of cost to securities regulation by comparing the respective sizes of the three regulated segments examined. To Members of this association, costs are abnormally high, especially given the level of responsiveness provided by regulators.

An important point to note about cost is that little of the data available to your Committee about cost will make the point about the cost of internal compliance staff and legal and accounting counsel necessary to monitor and respond to up to thirteen securities regulators.

3. Capital Market Impact

The ICAC is much concerned about the fact that regulatory cost and complexity are serious deterrents to foreign issuers and market participants. This results in Canada playing a smaller and smaller role in global financial services. The mere fact that the majority of Canadian portfolio managers find the Canadian marketplace irrelevant, except for client mandates for Canadian portfolios, should indicate that there is a serious problem with Canada’s regulatory structure.

4. Regulatory Philosophy

In our position paper we refer to the Financial Post op-ed article of Ed Waitzer, Chair of Stikeman Elliott and former Chair of the OSC, about the agenda of regulators. The amount of policies and the industriousness of the many regulators make the monitoring of evolving regulation a daunting task. Compliance with these changing rules is extremely complex and difficult. It is the present philosophy that results in long protracted processes to introduce and to modify regulations, national policy statements and national instruments. The ICAC strongly prefers a simpler system based upon principles which, unlike rules, cannot be honoured in the breach. If all jurisdictions followed exactly the same simple rules and interpreted those rules in exactly the same way, regulation in Canada would not be attacked as it is presently.

A good discussion of a simpler approach is contained in the op-ed article which appeared on July 11, 2003 in the Financial Post and is attached as Appendix C.

Summary

In simple terms, we recommend an approach to regulation based on principles with the same standards, the same requirements and the same interpretation of the principles in all provinces where investment managers operate. We realize that this is a large task to accomplish but also believe that, if one is to fix the system, it should be done in the best way possible.

Anecdotally, I can tell you that it takes less than three weeks and very low cost for an investment counsellor to register with the SEC. Seldom, if ever, can registration be accomplished in any Canadian province in less than four months and often it takes longer. My own firm, registered in other Canadian provinces, waited for approval from one province for its registration filed six months previously. International contacts are terribly confused over the Canadian system.

We were once asked to provide our counterpart in the US all the provincial requirements for registration of US investment managers in Canada and even regulators could not provide a complete, concise document. After some pressure, we received an incomplete document that was 121 pages long. That was only for registration requirements! Finally, we attach as Appendix D, a Report on Business article about the trials of Diane Urquhart for whom investment professionals in Canada hold the highest regard. That article clearly illustrates the lack of effectiveness of Canada's regulatory system in one area. Hopefully, these few illustrations will provide insight into the magnitude of the problem you and we face.

The Member firms of the ICAC sincerely trust that this comment letter together with our position paper and the other material we have provided will be of assistance to your Committee in its deliberations.

Anything the Committee is able to recommend to simplify the present system and make regulation in any one jurisdiction the same as in any other, will be greatly appreciated.

Contacts

Representatives of your Committee may contact our Executive Director, Keith A. Douglas by mail or telephone at the address and number above. You may also contact him at kdouglas@investmentcounsel.org. All communications should be in English and can be e-mail or telephone. Mr. Douglas will be pleased to assist you in contacting specific persons about particular issues so that you may have the benefit of the most accurate and helpful information

Respectfully submitted on behalf of the Member firms of the Investment Counsel Association of Canada,

A handwritten signature in black ink, appearing to read "Timothy E. Burt".

Timothy E. Burt, CFA
President



**THE PATH TO ACHIEVING A NATIONAL SECURITIES
REGULATORY SYSTEM FOR CANADA**

A PROPOSAL OF

THE INVESTMENT COUNSEL ASSOCIATION OF CANADA

October 2002

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INTRODUCTION

The Investment Counsel Association of Canada (ICAC) is the representative Association for portfolio management firms in Canada all of which are registered as Investment Counsel/Portfolio Manager. Seventy-one firms actively support the ICAC and, collectively, are responsible for the management of over \$490 billion for high net worth and institutional investors. The hallmark of the investment services of Member firms is continuous discretionary portfolio management for which a fee based on the value of assets managed is charged.

Member firms range in size from those that manage less than \$100 million to large, integrated firms responsible for \$40 billion and more. Consequently, the impact of the regulatory system in Canada is different to many of the ICAC Members. Smaller firms face an increasing proportion of their total income being allocated to regulatory costs. Among larger firms, while the proportionate share of regulatory cost may be lower, the overall cost is extremely significant. Many of these costs are not registration and filing fees but rather compliance costs, legal fees and management time required in order to comply with the myriad of different rules in Canada's thirteen jurisdictions. Another significant cost to investment counsel firms arises from delays in arranging for regulatory approval of registrants, product offerings and requests for exemptions. One of the very basic reasons the ICAC is interested in a more efficient securities regulatory system is to achieve greater efficiency in the businesses of Member firms.

But there are other reasons such as costs of the present system that require greater attention than they have been accorded to date. Of these, perhaps the most significant is the cost to Canada's capital markets. This cost is evident in the increasing number of public offerings of Canadian corporations made in the U. S. for, among other things, a more straightforward approval process. It is also evident in the negative view that foreign investors hold of Canada's disparate market and regulatory capability.

In this Position Paper we discuss the evolution of the present system, the costs related thereto and the alternatives and make a strong and urgent plea to the responsible Ministers to immediately take the next steps to support creation of a centralized and efficient securities regulatory system for the benefit of Canadian investors and all the regulated entities that serve them. We represent that the current decentralized structure has contributed to the decline in Canada's ability to attract investment and maintain vibrant and competitive capital markets. We also set out our belief that dealing with this inefficient system has put Canada's securities market participants at a competitive disadvantage which is reaching crisis proportions.

THE PRESENT SYSTEM

Canada remains the only Western industrialized country without a centralized securities regulatory agency. The impact of this disparate system is most significant for investment counsel firms. Investment counsel firms are unique insofar as they are the only major investment industry participants that are regulated directly by securities commissions.

Canada's thirteen securities regulatory authorities each have a responsibility to enforce the securities laws of their own jurisdiction, many of which laws differ to those of other Canadian jurisdictions. In cases where an issuer is interested in selling securities in only one jurisdiction, this system works well. In cases where a management firm does business in only one jurisdiction, the present system can meet its needs. But where an issuer undertakes a national offering or a management firm offers services nationally, the present system is fraught with different rules, procedures and fees. And it has been many years since companies raised capital in a single province. While we give credit to the provincial and territorial securities commissions for forming the Canadian Securities Administrators (CSA) and addressing the needs of national issuers and registrants, much more is needed to erase the multiplicity and duplication involved in a national securities issue or in a national investment management business.

For a national investment management firm, the following are business realities:

- Conditions of registration which differ from jurisdiction to jurisdiction.
- Prospectus deficiency comments that vary from jurisdiction to jurisdiction.
- Filing and registration fees which are not uniform among jurisdictions.
- An agent for service is required in each jurisdiction.
- Differing requirements for insurance against fraud and mysterious disappearance, all of which are embarrassingly low.
- Legal counsel necessary to advise on the differing rules, and changes to those rules, applicable in each jurisdiction.
- Different application of many rules that are actually uniform.
- Differing philosophical approaches to appropriate securities regulation.
- Individual registrations differ from jurisdiction to jurisdiction.
- Policies and procedures requirements differ from jurisdiction to jurisdiction.
- Business titles allowed differ from jurisdiction to jurisdiction.
- Differing securities acts, regulations, rules and policies.
- For some mutual fund clients, notices are necessary to advise that legal action may be difficult because the manager has no office in their jurisdiction.
- Audits are conducted separately and not coordinated.
- Working capital calculations differ amongst certain jurisdictions.
- Differing registration application forms, some of which must be typed.
- Residency requirements that do not result in more effective regulation.
- Impractical dual registration restrictions.
- Extensive regulatory overlap, e.g. mutual fund dealer, IC/PM and, soon, fund manager.

The multiplicity of regulatory regimes results in each province and territory being required to maintain staff to regulate registrants and issuers seeking to deal in securities in that province. Registrants must maintain a larger internal staff complement to deal with the varying rules among jurisdictions.

The CSA has been extensively considering these very issues and are attempting to reach their own agreement on an acceptable solution. We encourage these considerations and believe that they are being carried out in good faith to achieve a goal of an efficient Canadian securities regulatory system. What concerns the ICAC is the lack of a demonstrated political will in the provinces and territories to achieve this goal. As a result, we are disturbed that regional concerns remain paramount indicating a desire to support the status quo.

HISTORICAL DEVELOPMENT OF THE PRESENT SYSTEM

The provinces in Canada have constitutional control over property rights and, therefore, control over the regulation of the distribution of securities in their jurisdictions. The main concern that the securities business has with this principle is that it fails to recognize the national and global realities. Most large securities and management businesses operate on a national basis and must cope with myriad provincial rules and practices. Increasingly, Canadian businesses are operating globally as are their foreign counterparts. Canada's regulatory system is viewed internationally as an impediment to issuers and, consequently, Canadian dealers and investors are prevented from participating in attractive opportunities.

Another important factor in the evolution of the present system has been the very great increase in the staff complements of regulatory authorities and in their appetite for initiating new issues and policies. In a recent essay written for a national newspaper, former Chair of the Ontario Securities Commission, Edward J. Waitzer noted, "This 'bureaucratization' of the policy-making process could not have occurred at a worse time for Canadian capital markets. The globalization of finance is a nemesis of inefficient regulation." And he went on to state, "Not only is the traditional regulatory paradigm challenged, but so, too, are our capital markets and financial services sector as they (like so much of our country's industrial economy) struggle to identify and maintain their relevance." The ICAC could not agree more and we detail these concerns in the next section.

There have been several attempts to create a national securities authority in Canada over the last sixty years or more. More recently, in 1977, a federal proposal for a national securities law failed to capture the necessary support to go forward. Later, in the mid 1990s, negotiations between the federal government and the provinces for a national regulatory system broke down over the loss of provincial revenues arising from securities registration and filing fees. But, the breakdown in negotiations aside, this was the first time that some progress was actually made to develop a national system.

The proposal put forward by David Brown, Chair of the Ontario Securities Commission (OSC) for a pan-Canadian regulatory system (the Brown proposal) appears to the ICAC to have many elements that could lead to an appropriate compromise. It has the acknowledged support of the President of the Toronto Stock Exchange. It also has received interest and attention among the provinces. Québec remains certain that the present system, in which each province controls regulation in its jurisdiction, is the only one in which it is able to respond to the needs of the province. That position is also the basis of the concerns of some of the other provinces which, heretofore, have resisted all previous attempts to transfer regulation to a centralized authority.

In order for any progress to be made in streamlining securities regulation in Canada, these provincial positions need to be addressed and compromise achieved. Leadership, such as that demonstrated by Finance Minister John Manley, is desperately needed in the provinces.

Whatever process provokes the debate among the responsible provincial Ministers, we continue to be sanguine that the Brown proposal incorporates many useful principles through which the provincial concerns can be resolved to the satisfaction of each.

But clearly, globalization has plunged our regulatory system into an inefficient and non-competitive process unable to respond in a timely manner to the changing needs of financial market participants. Canada's inability to respond concomitantly with the U.S. to notorious governance breaches at Enron and WorldCom is a relevant example. The SEC is leading the way. Provincial Ministers should regard this as a crisis threatening the competitiveness of Canada's capital markets and they must take the necessary immediate steps to adopt a suitable and efficient national authority. It is not just about regional interests any longer.

THE COST OF THE PRESENT SYSTEM

One only needs to be aware of the structure of the present system to understand that it has the prospect of being more expensive than a national regulatory system. It is very relevant that former Finance Minister Paul Martin noted that Canada's regulatory costs are approximately double those of Australia, a comparable capital market.

To illustrate, a portfolio management firm recently registered one executive in all provinces at a direct cost of \$3,100. This kind of registration is necessary so the executive is able to travel to meet with institutional clients in any province. This cost ignores legal costs and the staff time taken to see that the registrations were effected in all the jurisdictions. But this is only the tip of the iceberg. Other costs relate to registration costs of the management firm in all necessary categories in all jurisdictions, report filings and fees, legal costs associated with compliance, deficiency letters and acting as agent for service and, lastly, staff and management time of the manager. Time delays in obtaining required regulatory approvals impose an additional significant burden and cost on investment counsel firms. Clearly, these costs would be substantially less if one authority was responsible for regulation.

But in addition to these costs to market participants, there is a significant cost to Canada's capital markets. The ICAC believes that securities regulators, among others, have a responsibility to foster strong and competitive capital markets in Canada. The 'hollowing out' of Canadian business described by Gordon Nixon, CEO of the Royal Bank is a clarion call to all Canadians to take all necessary action that will strengthen our capital markets and make them more competitive. Provincial Ministers responsible for securities regulation must seriously take cognizance of their role and responsibility in this effort to improve Canada's capital markets. We believe that the present costs to Canada's capital markets, on which securities regulation has some impact, arise in two separate ways.

1. Foreign investors have a negative view of investment in Canada for several reasons including the foreign property rule and the value of the Canadian dollar but also including the quality and cost of securities regulation.
2. Reduced choice for Canadian investors because foreign investment managers are discouraged as a result of complexities and cost. As an example, the ICAC was recently asked by its counterpart organization in Washington if there was a single document in which the conditions for registration in all provinces could be found. It does not exist and, further, no single securities commission has such information.

OPTIONS FOR A CENTRALIZED SECURITIES REGULATORY SYSTEM

Earlier we touched upon structures that could be alternatives to the present system. We have also discussed briefly the political realities of those structures. Below, we set out three possible alternatives for investment counsel firms, and the ICAC's position on each.

Harmonization

We commend the CSA for its efforts to harmonize rules for national issuers and registrants. Mutual recognition has overcome many problems yet unique local policies and practices persist. We understand that the CSA has established a deadline of December 2003 for the completion of a Uniform Securities Act with passage by the provinces expected in mid-2004. Such an accomplishment will do much to simplify the many conflicting rules. The ability of a registrant to register in only one jurisdiction and to transact business in others will be a great step forward if the application of the law and regulations is consistent among all jurisdictions. Further steps toward harmonization that are planned and are yet to be determined will all assist in simplifying the present system. But the reality of a harmonized system is a coterie of regulators and staff in each jurisdiction, all of whom must be paid by those who issue securities, manage securities or undertake securities transactions. **Harmonization is a step towards centralized regulation and would overcome the irritating differing rules, however would not eliminate the need for investment counsel firms to deal with thirteen separate jurisdictions and their unique interpretation of the rules.**

A Super SRO

As the one identifiable constituency in the investment community that is not self-regulatory, it occurs to investment counsel firms that one possible solution would be to amalgamate all the securities-related SROs into one super SRO which investment counselors might join. The ICAC believes that this might solve the one significant irritant being the need to live with disparate rules and their interpretation by supplanting the existing regulators with one. While this is one possible alternative, it is too soon to know if the self-regulatory costs would outweigh the benefits. **This is an alternative that the ICAC would, in good faith, consider pursuing further. The most significant concern of the ICAC is ensuring that a culture would exist in the super SRO that was sensitive to the business issues of investment counsel and would lead to sensible, yet effective, regulation.**

National Securities Regulator

The Brown proposal put forward November 20, 2001 is a sensible extension of the considerable work already undertaken or planned by the CSA. This proposal is the epitome of compromise and may be the key to an ultimate solution. The ICAC foresees, in this proposal, a national body that is participated in by the provinces and territories and sensitive to their specific regional issues. Carefully developed to be structured to permit regional input to policies, we believe that the pan-Canadian Commission approach has a basic underlying concept that can be the means to resolving provincial concerns and lead to a national regulatory body so badly needed. **The ICAC could support a broadly-based single regulator along the lines of the Brown proposal and urges all provincial Ministers to give due consideration to this responsible compromise solution.**

CONCLUSION

It is clear that the decades-old national debate on a goal of developing a national securities regulator has been frustrated on a number of occasions and for a variety of reasons. Most of the reasons that have prevented Canada from reaching that goal have had political roots but some have been founded in financial concerns.

The debate has now finally reached a point where a workable proposal, that is sensitive to regional issues, is a reasonable alternative. Financial concerns of the provinces have all but been eliminated with the adoption of self-funding for the larger of the provincial commissions in Canada. The ICAC believes that these developments and the hard work being undertaken by the CSA to create both a higher level of mutual reliance and uniform legislation, form the basis of a national securities regulatory system. However, the ICAC's concern with this process is the length of time it will take to reach that objective.

The ICAC supports the initiatives of the CSA. But we also understand that its members are not able to accomplish the goal of a national regulatory system alone.

- The ICAC strongly encourages the federal Minister of Finance and provincial and territorial Ministers responsible for securities regulation in their jurisdictions to immediately begin the process to enable this vital objective to succeed. We strongly believe that the federal Minister of Finance has an important role to play in facilitating this process to the satisfaction of all as demonstrated by his appointment of Harold MacKay as Special Representative to identify the issues and recommend the appropriate process.
- The ICAC calls for an early meeting of all such Ministers at which the subject of establishing a national securities regulatory system, in as short a time frame as is possible, is the sole or major topic of discussion.
- The ICAC also calls upon those Ministers to issue a communiqué at the conclusion of such a meeting indicating what steps they are prepared to take to facilitate the establishment of a national securities regulatory system.
- The ICAC further encourages such Ministers to immediately take whatever steps are necessary to found this meeting at as early a date as is possible.

Only after Canadians are aware that federal, provincial and territorial Ministers have reached agreement on a process leading to the establishment of a national securities regulatory system, will there be any confidence that such a goal is within reach. This is truly an issue of national importance. It is one matter for the CSA to have reached general agreement on issues that could lead to this goal but quite another to actually have the means by which to accomplish it. It is for these reasons that the ICAC, whose Member firms are responsible for successfully managing almost \$1/2 trillion for Canadians, calls for urgent action to move the process the next steps towards achieving this very important goal. The ICAC is prepared to provide whatever assistance it can to facilitate a resolution.

APPENDIX “B”

**SUMMARY OF KEY REGISTRATION REQUIREMENTS
APPLICABLE TO INVESTMENT COUNSEL/
PORTFOLIO MANAGERS IN CANADA**

	Fee/ Corporate Registration	Advising Officer Fee	Copy of Procedural Manual	Financial Institution Bond/Insurance	Minimum Working Capital Requirements	Officers’ Educational/ Experience Requirements
British Columbia	\$1,500.00	\$250.00	copy required	Minimum of \$200,000 coverage	\$25,000 plus maximum amount deductible under applicant’s Financial Institution Bond.	<ul style="list-style-type: none"> - Canadian Securities Course (“CSC”) - Canadian Investment Management Program (“CIMP”) - first year of Chartered Financial Analysts Examination (“CFA”) - five years experience, three of which under the supervision of a registered advisor having control over portfolios having an aggregate value of at least \$1M
Alberta	\$1,000.00	\$250.00	copy required	Surety bond for a minimum of \$10,000	Not specified	<ul style="list-style-type: none"> - CSC - CIMP - first year of CFA - five years experience, three of which under the supervision of a registered advisor having control over portfolios having an aggregate value of at least \$1M
Saskatchewan	\$750.00	\$250.00	copy required	Surety bond of not less than \$10,000 where the advisor does not receive securities, money or other property on behalf of a client or \$200,000 if the advisor does receive securities money or other property on behalf of a client	\$5,000 or any greater amount the director considers necessary where advisor exercises control over clients funds plus maximum deductible under any required bond or insurance policy	<ul style="list-style-type: none"> - CSC - CIMP - first year of CFA

	Fee/ Corporate Registration	Advising Officer Fee	Copy of Procedural Manual	Financial Institution Bond/Insurance	Minimum Working Capital Requirements	Officers' Educational/ Experience Requirements
Manitoba	\$750.00	\$200.00	Copy required	Surety bond in minimum of \$25,000 by a bonding company authorized to do business in Manitoba and Broker's Blanket Bond/Financial Institution Bond in minimum amount of \$100,000	\$25,000 plus an aggregate of \$25,000 Shareholders Equity or such other amount as determined by the Director	<ul style="list-style-type: none"> - CSC - CIMP Parts I & II - first year of CFA - five years experience, three of which under the supervision of a registered advisor having control over portfolios having an aggregate value of at least \$5M
Ontario	\$800.00	\$400.00	copy required	\$50,000 Financial Institution Bond, or \$200,000 if client holds funds/securities	\$5,000.00 subject to increase to \$25,000.00 if client holds securities funds	<ul style="list-style-type: none"> - CIMP and first year of CFA <i>or</i> the CFA - five years experience, three of which under the supervision of a registered advisor having control over portfolios having an aggregate value of at least \$5M
Quebec	\$1,500.00	\$375.00	copy required	Bonding/insurance of a minimum of \$10,000 worth of coverage	Working capital of at least \$25,000 in additional to amount deductible under applicable insurance policy or bonding requirement	<ul style="list-style-type: none"> - five years experience in portfolio management or financial analysis - hold a university degree in a relevant discipline or have successfully completed the course leading to the designation of Certified Financial Analyst
Newfoundland	\$600.00 (Note: a fee of \$350.00 is also required in order to be exempt from having to have an office in Newfoundland)	\$250.00		3-D Insurance Policy in the amount of \$10,000 if the applicant does not handle clients' funds and a 3-D Insurance Policy in the amount of \$200,000 if the applicant handles clients' funds	Working capital of the greater of (a) \$25,000 and (b) an amount equal to the sum of 10% of the first \$2.5M of adjusted liabilities, 8% of the next \$2.5M adjusted liabilities, 6% of the next \$2.5M adjusted liabilities and 5% of adjusted liabilities in excess of \$10M	<ul style="list-style-type: none"> - CSC - Canadian Investment Finance Course - first year of CFA - five years experience, three of which under the supervision of a registered advisor having control over portfolios having an aggregate value of at least \$1M

	Fee/ Corporate Registration	Advising Officer Fee	Copy of Procedural Manual	Financial Institution Bond/Insurance	Minimum Working Capital Requirements	Officers' Educational/ Experience Requirements
New Brunswick	\$800.00	\$200.00	copy required	Surety Bond in minimum amount of \$200,000. In addition, where broker maintain its records outside of New Brunswick and does not have a branch office in New Brunswick, may be required to file an additional bond or irrevocable letter of credit in an amount up to \$50,000	Not specified	- CIMP and first year of CFA <i>or</i> the CFA - five years experience, three of which under the supervision of a registered advisor having control over portfolios having an aggregate value of at least \$5M
Nova Scotia	\$600.00	\$300.00	copy required	Insurance Policy of \$10,000 if applicant does not handle clients' funds* and a \$200,000 insurance policy if the applicant does handle clients funds (*however applicant may collect subscriptions or pre-payments)	Working capital of at least \$5,000 plus amount of deductible	- CIMP and first year of CFA <i>or</i> CFA - five years experience, three of which under the supervision of a registered advisor having control over portfolios having an aggregate value of at least \$1M
Prince Edward Island	\$600.00	\$200.00	copy required	Bonding in an amount not less than \$10,000	Minimum working capital of deductible under any clause of bonding or insurance policy plus the greater of \$25,000 and an amount equal to 10% of the first \$2,500,000 of adjusted liabilities, 7% of the next \$2,500,000 adjusted liabilities and 5% of adjusted liabilities in excess of \$10,000	- CIMP and first year of CFA - five years experience, three of which under the supervision of a registered advisor having control over portfolios having an aggregate value of at least \$1M

The debate between the OSC and the BCSC highlights the need to go beyond the nature of the regulator to the philosophy used to regulate.

Smarter regulation

By Roger Martin and Martin Guest

Securities law reform is not the usual stuff of daily media stories. However, the proverbial fur has been flying lately, as exemplified by the Ontario Securities Commission's stern response on Wednesday to the recent proposals by the British Columbia Securities Commission. Yet, we now see regular reports of politicians and regulators openly discussing the urgent need to fix what ails Canada's securities regime.

In this debate, much attention has been paid to arguments about the need for a single securities regulator in Canada. No doubt there is, at the very least, an urgent need for better co-ordination among regulators. There is, however, another debate worth having in this context. We believe it is important to focus not just on the nature of the regulator but also on the philosophy used to regulate -- a point of significant difference between the OSC and BCSC.

Regulations can be divided into two basic types: input and output. Input-oriented regulations control the details of how products and services are manufactured or sold. Output regulation focuses on end results and lets businesses figure out the best way to deliver the specified results.

Input regulation in the securities sector is exemplified by the prospectus disclosure rule for mutual funds. The existing rule sets out, in 51 pages of excruciating detail, exactly how mutual funds must provide prospectus information to investors, including mandatory word-for-word headings and subheadings, precisely stipulated disclaimers, exact date formats, mandatory rules on tables of contents and other very particular requirements.

A good recent example of output regulation can be found in the Sarbanes-Oxley Act in the United States. One of its most intensely debated elements is a simple requirement in Section 302 that the senior executives of public companies personally certify their financial statements. With this provision, the message from the U.S. Congress to executives is: "You need to ensure that your company's public disclosure is complete and correct. We don't care how you do it. Just do it. And if you don't do it, you, personally, will go to jail."

Input regulation is the dominant form of regulation, but it often produces terrible slips between the cup of prescribed inputs and the lip of desired outcomes. For example, content regulation in Canadian television was intended to result in Canadians watching lots of high-quality Canadian television drama. It indeed produced lots of Canadian television drama, but of such low quality that Canadians choose not to watch it.

Detailed input regulation of Canadian mutual funds has produced prospectuses that look more and more alike, but which even the regulators now admit investors don't read and which clearly don't meet the basic purposes for which they were intended.

Throughout the securities sector, other input-oriented rules closely control how products can be structured, managed, marketed and sold. Not only are non-standard approaches to disclosure prohibited, but novel products can be difficult or impossible to launch, and well-established investment techniques are restricted or forbidden. The unintended consequence is that innovation is strangled, and true differentiation among competitors is reduced.

This kind of "commoditization" doesn't serve the interests of investors. A one-size-fits-all approach is not appropriate for financial products. Canadian investors are increasingly dissatisfied with the crop of mutual funds available to them and they have shown this through both declining sales and growing cynicism.

In our view, what's called for in the Canadian securities industry is a switch in philosophy from input to output regulation.

Output regulation is powerful and direct. Already, U.S. executives are taking great pains to ensure they can confidently certify their financial statements under Section 302 of Sarbanes-Oxley. Their reviews are leading to an unprecedented wave of specific, candid and insightful disclosure from public companies. We note with regret that other elements of Sarbanes-Oxley, such as the Section 404 requirement regarding internal controls, are totally input-oriented and are giving rise to an orgy of bureaucratic scrutiny from auditors, involving substantial cost that may well prove disproportionate to any ultimate benefit.

Output regulation is far from a new or untested concept. In the early 1970s, the U.S. Congress successfully used output regulation to improve gas mileage in the auto industry. It established Corporate Average Fuel Economy (CAFE) targets that began at 18 miles per gallon and rose to 27.5 mpg over several years. Congress left the "how" to the automakers -- through selling smaller cars, making their large cars lighter, making their engines more fuel-efficient -- whatever they found most effective. Indeed, the automakers did all of the above and met the requirements -- doubling fuel economy in the U.S. fleet. The goal of increasing fuel economy was achieved efficiently, without complicated, bureaucratic regulations.

Happily, in Canada, the British Columbia Securities Commission is promoting just this sort of output-oriented revolution in securities regulation. Its approach starts with a set of broad principles and straightforward guidance, articulated in plain language, rather than the vast and complex web of detailed regulations that currently exists. Its goal is to establish a regime with fewer but better rules, rather than just producing more rules.

For example, the BCSC would replace the existing 51-page stricture on mutual fund prospectuses with a very simple principle: A mutual fund must disclose all information relating to its business, operations or affairs that a reasonable investor would consider important in making a decision about buying or selling the fund, and the fund must keep its disclosure up to date -- period. The rule could scarcely be simpler. With the basic "output" defined, the BCSC was able to leave 50-plus pages of existing regulations on the cutting room floor. Though dramatically shorter, it is, frankly, hard to imagine anything important that would slip through B.C.'s simple principle, yet be caught by the existing 51-page version of the rule.

The B.C. model reflects the reality that most investors don't really care about the detailed "inputs" that go into securities. Having precisely mandated forms of prospectuses hasn't resulted in investors being any better informed than before. What really matters to investors is the bottom line: well-structured products that meet their needs, run by honest, competent people, fairly priced, with a view to the client's best interests.



Under output regulation, regulators give businesses the flexibility to structure, manage and market their products however they think best, provided they deliver the right sorts of bottom line results. Of course, there also needs to be meaningful penalties for any failure to achieve the mandated outcomes. But the basic approach is straightforward: The regulator simply specifies what is to be achieved and leaves it to the creativity of industry firms to determine how best to meet those objectives, while satisfying the demands of their customers.

We believe output regulation will work in the securities arena. B.C.'s new model would allow each securities firm the flexibility to determine the best way to structure itself to meet the general standards mandated. This kind of approach is very similar to the output regulation successfully used with the U.S. CAFE standards and, more recently, the Sarbanes-Oxley Section 302 certification requirement.

The OSC sees things very differently, arguing strenuously in its response to the BCSC for continued domination of input regulation. We understand the OSC's keen interest in getting the right answer for securities regulation, but we believe output regulation for securities markets is not only a viable alternative, but a preferable one. It will require a significant restructuring of the existing regulatory landscape, but it seems the environment may be receptive to such changes. Canadian investors deserve a more effective system.

Director finds no road map on route to disclosure

By KAREN HOWLETT
From Saturday's Globe and Mail

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Shortly after Diane Urquhart joined the board of Technovision Systems Inc., a small Internet service provider listed on the Canadian Venture Exchange, she expressed concerns that directors would be liable for company press releases she viewed as misleading.

Her phone call to Technovision chairman and chief executive officer Gordon Tremain back on Jan. 4, 2001, set her on a collision course with other directors. She had already requested an emergency board meeting to discuss what she later described in court documents as "serious issues" of corporate governance, including lucrative consulting fees for company executives and little progress on acquisitions.

Ms. Urquhart had every intention of being an active director. Her unsuccessful efforts to get fellow directors to address what she considered a hornet's nest of problems at the Aldergrove, B.C. company took her on an odyssey well beyond the boardroom.

She has spent the past two years writing innumerable letters, making phone calls and travelling back and forth from her home in Mississauga to British Columbia, navigating her way through the courts and Canada's patchwork securities regulatory system.

It seems that just about everyone wanted her to go away.

Ms. Urquhart, 49, is no neophyte in the investment industry. She has spent 25 years in the industry, including a decade as a top-ranked financial services analyst and head of equity research at brokerage firm Burns Fry Ltd., at one time Canada's premier research house.

She said she agreed to tell her story because directors are often accused of being asleep at the wheel. She tried to make a difference and ended up paying a big price.

Her out-of-pocket costs, including her investment in the company, total \$1.45-million.

"As a director, I believe it's important to complete the job you begin and not to be bullied out of doing it," she said in an interview.

Governance experts and securities regulators expect corporate directors to protect the interests of shareholders, she said. But when she encountered problems at Technovision, there was no road map for her to follow. When her efforts were rebuffed by other directors, she appealed to securities regulators and then to the courts, where she tried but failed to recover her losses. Ultimately, her complaints about the press releases were corroborated by regulators.

Her unrelenting pursuit of the matter has only further strained her relations with Technovision officials. Technovision alleges in court documents that she "continually harassed and obstructed" the company and its

directors. The fact that she met defeat in the courts not once but three times has given the company more ammunition to criticize her efforts.

She was not a champion for good corporate governance, Wade Simpson, the company's lawyer, said in a letter to The Globe and Mail. "Ms. Urquhart operated with regard to her personal interest first."

At a time when corporate governance issues are in the headlines, Ms. Urquhart's experience serves as a cautionary tale for directors. She confronted the worst of both worlds: regulators who talk a lot about the need to restore investor confidence but who can be reluctant to intervene; and a lack of clear securities rules that makes it difficult, if not impossible, for individuals to seek redress in the courts.

Neil Gross, a Toronto lawyer who often represents aggrieved investors, said there should be a process whereby boardroom disputes can be channeled toward a resolution without paralyzing the company.

"You'd like to think the law would recognize some avenue that [directors] should take other than just resigning and staying quiet and letting the chips fall where they may for the shareholders," he said, speaking generally.

Ontario Securities Commission chairman David Brown dismissed Ms. Urquhart's complaints to the regulator as a private dispute, and told her in a letter last February that the civil courts are the proper forum for dealing with such matters.

She fared better with B.C. regulators, however.

Former CEO Mr. Tremain, who is also Technovision's controlling shareholder, acknowledged in a settlement agreement with the B.C. Securities Commission last October that the company issued eight "incorrect and misleading" news releases in 2000 and that his trading in the shares may have resulted in an artificial price.

As part of the settlement, he resigned from Technovision, was banned from acting as a director or officer of a public company for three years and ordered to pay \$30,000.

Ms. Urquhart could not sue Technovision over the misleading press releases — under current Canadian securities rules, companies are only liable for what they say in a prospectus.

At the same time, Technovision was able to sue her because Canada has no rules to protect corporate whistle blowers. Technovision has accused Ms. Urquhart, her husband, Hugh, and seven others in the Internet sector of waging a "campaign of slander" against the company and making "unfounded" complaints about its management and directors.

"I'm pretty badly beaten up here," she said. "From my perspective, a director should not be sued for doing their job."

The Technovision board The story, which is contained in court documents and regulatory filings, begins in early 2000 when Ms. Urquhart and six business associates launched an Internet service provider (ISP) called iTCANADA.com Inc. She invested \$1.2-million in the company for a 33-per-cent, fully diluted interest.

In March, 2000, iTCANADA paid \$860,000 for options to purchase up to 28 other ISPs as part of a plan to quickly consolidate industry players as consumers made the transition from dial-up to high-speed providers.

"We saw it as a once-in-a-lifetime transition opportunity," she said in the interview.

Mr. Tremain entered the picture in August, when iTCANADA was unable to raise the \$35-million needed to exercise all 28 options. It ended up negotiating an agreement with Technovision, whereby Ms. Urquhart and her business associates exchanged their shares in iTCANADA for 0.1 million shares of Technovision, which

were to be held in escrow under stock exchange rules. She received 2.9 million shares; the shares would be cancelled if Technovision failed to acquire a set number of Internet subscribers.

The two companies struck a definitive agreement in October, 2000. The options on the 28 ISPs were not yet exercised; doing so would have made Technovision the sixth-largest ISP in Canada with 240,000 customers and annual revenue of \$50-million.

As of April that year, Technovision had 35,000 subscribers.

Ms. Urquhart joined Technovision's seven-member board on Dec. 6, 2000, as a non-management director. Shortly after, she became concerned about delays closing the deals to acquire the 28 ISPs. On Jan. 2, 2001, she wrote to other Technovision directors, requesting an emergency board meeting.

She took an active role in the hopes of persuading management directors to "fulfill their commitment" to acquire the ISPs, she said in a chambers brief filed in the Supreme Court of British Columbia.

The ISP owners who had signed the letters of intent were backing out because of delays closing the deals, her letter said. As of Jan. 2, only two of them had signed binding agreements.

At the same time, Technovision was boasting on its Web site that it had an "aggressive acquisition strategy," yet she saw no evidence of this, her court brief said.

Stephen Winters, the company's corporate counsel and a director, said in a lengthy memo to all directors on Jan. 5 that it is not "helpful or appropriate" for the board to attempt to manage operations, but it should be available to provide "constructive input on a periodic basis."

Her relations with Mr. Tremain and Mr. Winters became more difficult in the following weeks, to the point where she was denied information she was entitled to have about the company, Mr. Justice Peter Lowry of B.C. Supreme Court said in a decision. "Ultimately, her opportunity to speak at board meetings was rudely curtailed."

Things went from bad to worse for Ms. Urquhart. In March, 2001, Technovision bought out five of her six associates in iTCANADA. The group returned a total of 5.2 million shares to the company for cancellation in exchange for \$610,000 to be paid over time. Bernard Borgmann, a member of the group, resigned as an officer and director of Technovision. In September, Ross Jepson, another member of the group, was paid \$100,000 over time for reaching a similar agreement and resigned as an officer.

Ms. Urquhart was also offered \$500,000 to cancel her agreement with the company, but declined. The 2.9 million Technovision shares she was to receive had a market value of \$3.2-million at the time the deal between the company and iTCANADA was struck, she said.

"The effect of those agreements was to isolate Ms. Urquhart as the only remaining member of the Borgmann group in either management or on the board of Technovision," Judge Lowry's decision said.

She also ran into a brick wall when she asked for a copy of a report on Technovision's executive compensation prepared by KPMG LLC, the company's auditors. KPMG did the report in response to questions raised by the Venture Exchange about the company's related-party deals.

The exchange asked for the name of the director who owned a numbered company that received \$734,626 in consulting fees in the fiscal year ended May 31, 2000, and \$606,297 for the six months ended Nov. 30, 2000, and for a copy of the non-management directors' resolution approving the payments.

Ms. Urquhart says in court documents she never saw copies of the consulting agreements, let alone approved them. Technovision posted revenue of \$6.4-million and profit of \$583,000 in fiscal 2000.

After management directors refused to give the compensation report to her, she asked KPMG for a copy. Don Matthew, a partner at the firm, responded in an e-mail on June 27, 2001, that it discusses requests from board members with management. "This is the way we communicate with our clients."

A KPMG spokeswoman declined to comment, citing client confidentiality.

Ms. Urquhart did not get a copy of the report until December, 2001, a few days before she went to court in British Columbia, seeking to recover the value of her shares.

The KPMG report revealed that Mr. Tremain was the sole shareholder of the numbered company and that he was to receive an annual salary of \$495,000 under a consulting agreement. Denise Page, Mr. Tremain's common-law spouse and a director and executive vice-president of Technovision, was to be paid \$300,000.

Gordon Tremain's stock trades Ms. Urquhart also learned in March, 2001, that officials at the Venture Exchange had been investigating Mr. Tremain's trading of the company's shares for the past nine months.

On July 3, 2001, a surveillance official at the exchange said in a letter to Technovision board members that its review did not substantiate any violation of exchange policies and it considered the case closed. But the exchange then as a matter of routine practice referred the case to the B.C. Securities Commission, which opened its own file.

Initially, staff at the BCSC were not prepared to do much. On Oct. 22, 2001, an investigator wrote to Ms. Urquhart, who had also alerted the commission about Mr. Tremain's trading, informing her that its staff had determined there was insufficient evidence to conclude whether he did any illegal insider trading.

"However," the letter continued, "we did find that Tremain's trading appears to have had an undue influence on the market for the company's shares and may have been contrary to the principles of fair trading. As a result, the staff has issued a strong caution letter to Tremain regarding his trading activities."

The caution letter did little to satisfy Ms. Urquhart. At her prodding, staff at the BCSC eventually launched an investigation into Mr. Tremain's trading, which ultimately led to the settlement agreement in October, 2002.

"Diane was adamant," Sasha Angus, head of enforcement at the BCSC, said in an interview. "She provided us with further information, and that was of assistance to us. In all these matters, it's a matter of resource allocation, trying to figure out what we're going to pursue and what we're not. Mr. Tremain's behaviour was such that he required further investigation."

On eight occasions in August and September, 2001, Technovision announced that it had exercised specific option agreements with ISPs, whereas only letters of intent had been signed, the settlement said. Mr. Tremain acknowledges that the news releases were "incorrect and misleading," it said.

He bought 408,900 shares from Aug. 15 to Dec. 28, 2000, at prices ranging between \$1.10 and \$1.52. Some of the purchases were "high closes," meaning he bought just before one of the misleading news releases, the settlement says.

When Mr. Tremain resigned from the company last October as part of the settlement, Ms. Page, his spouse, went back on the board but resigned as executive vice-president. (She had stepped down from the board in May, 2002.) The courts Ms. Urquhart took her fight with Technovision to court in July, 2001, when it became obvious to her that the company was not going to exercise its options to acquire the remaining 26 ISPs with which it had signed letters of intent. At that point, it had struck deals with two of them.

She filed an oppression suit in B.C. Supreme Court, alleging that the situation was both oppressive and unfairly prejudicial to her because most, if not all, of the 29 million Technovision shares she was to receive

in exchange for her stake in iTCANADA would be cancelled if the options were not exercised, and she would lose her investment.

In September, Technovision fired back with its own lawsuit against Ms. Urquhart, her husband and seven others in the ISP industry. In documents filed in the B.C. courts, it accuses Ms. Urquhart of damaging the company's reputation by secretly contacting stock market regulators and initiating "unfounded complaints" about management and other directors and of sabotaging its bank funding by contacting the bank.

Ms. Urquhart counters in an affidavit that the actions of management directors caused the loss of the financing. Her affidavit also said her complaints to the regulators were reasonable and made to the appropriate entities.

Technovision also accuses her of "self-dealing" in her attempts to allegedly take over the company. She says her attempts to raise money in mid-2001 to buy the remaining ISPs were conditional on her not resolving matters with Technovision and the company not acquiring the ISPs.

On Dec. 17, 2001, the first day of her oppression hearing, Ms. Urquhart learned that she had been voted off Technovision's board three days earlier, she said in the interview.

This was not the only surprising news. She also learned in court that only three of the 28 ISPs met financial tests that Technovision had set as conditions for proceeding with an acquisition. This information was contained in a due diligence report prepared in the fall of 2000. But Judge Lowry said in his decision it appeared the iTCANADA associates were never informed of the report, nor was it discussed at any Technovision board meeting.

Ms. Urquhart lost the suit. Judge Lowry said the oppression remedy is limited to instances where an individual is affected in his or her capacity as a shareholder, not a director. He also said the ISPs were not acquired for a variety of reasons, including the withdrawal of bank funding, all of which were within the reasonable expectations of the parties involved at the time they entered into the share agreement with Technovision.

She appealed but lost again. Representing herself, she attempted to provide the court with what she characterized as new evidence not submitted in the oppression hearing. Some of it was not available during her original court hearing.

In a unanimous ruling on Jan. 23, three judges in the Court of Appeal for British Columbia said it appeared Technovision's management was "lacking in talent and honesty," but said she should have outlined her entire case at the beginning.

Ms. Urquhart fared no better in the Ontario Superior Court where, once again representing herself, she argued that the buyout agreements between Technovision and her former associates amounted to an illegal issuer bid under the Ontario Securities Act.

Her former partners argued in court that her loss of the oppression suit in the B.C. courts was a final decision on that matter.

They argued in a factum filed in court that her action was an abuse of process because it was her third legal proceeding based on "virtually identical" facts.

Mr. Justice Romain Pitt agreed. In his February decision, he dismissed the "unorthodox nature" of her complaint as "frivolous and vexatious."

Last month, Ms. Urquhart failed to persuade a B.C. judge to dismiss the company's lawsuit against her.

As things stand, there is also a dispute before an arbitrator over how many Technovision shares Ms.

Urquhart owns.

Technovision, meanwhile, announced this month that it has signed a letter of intent to merge with another Internet service provider, PCNet, a Victoria-based company listed on the TSX Venture Exchange. It said the new nine-member board will include five independent directors.

The OSC Ms. Urquhart was also forced to deal with regulators in two provinces. B.C. regulators were responsible for probing Mr. Tremain's trading because Technovision is based in the province. Ontario regulators handled her complaint about the buyout agreements Technovision struck with her former business associates because the individuals involved all live in the province.

Ms. Urquhart has alleged that the buyout was an illegal issuer bid because the same offer was not made to other shareholders.

While OSC staff noted in a letter to her that components of the settlement agreements "appear to have constituted an issuer bid," they said a breach of the securities act was "largely technical in nature" and that there is no evidence that investors suffered any harm from not having an opportunity to participate.

The fact that regulators in another province had already dealt with the company was also a factor. "Enforcement resources are very thinly spread, and we are loath to expend resources on the same matter as another regulator," OSC enforcement director Michael Watson said in an e-mail to her.

OSC officials declined to comment for this story. Mr. Borgmann also declined to comment. His lawyer, Cynthia Amsterdam, said there is no judicial finding anywhere that her client was involved in any impropriety.

"She has been trying every possible means to do something because the courts do not agree that she's been wronged. That's the bottom line," she said.

As for Ms. Urquhart, she now knows that it would have been much easier had she just turned a blind eye as a director and walked away.

"It's not a job anyone can do with how we're structured," she said. "What backing do you get?"