

# **CRAWFORD PANEL**

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On a Single Canadian Securities Regulator

## **ONE YEAR ON: SEEING THE WAY FORWARD**

Update Report

June 15, 2007







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On June 7, 2006, the Crawford Panel on a Single Canadian Securities Regulator issued its report proposing a blueprint for a national agency to regulate Canada's capital markets.<sup>1</sup>

A year later, Canadians might wonder whether the report will join similar studies gathering dust. The first study dates back 70 years to the Royal Commission on Price Spreads in 1935. Other studies followed in 1964, 1967, 1979, 1994 and 2002. Most argued for a federal securities regulator under the control of Ottawa.

The Crawford Panel proposes a single securities regulator under the governance of the provinces with federal participation to replace the current system where each of 13 local jurisdictions has its own set of regulations enforceable only in its own province or territory.

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<sup>1</sup> Crawford Panel on a Single Canadian Securities Regulator, *Blueprint for a Canadian Securities Commission*, June 7, 2006.



## A YEAR OF QUIET PROGRESS

The Blueprint proposed by the Crawford Panel has received wide support among capital market participants — small, medium and large corporations; institutional investors; organizations representing retail investors; investment dealers; intermediary service providers; self-regulatory organizations; and business associations. A growing number of advocates has given speeches, written newspaper and magazine articles, and communicated privately with provincial and federal political leaders. The Panel's volunteer members have maintained active contact with political and capital market leaders. Based on feedback from many sources, support for the Crawford Panel model for a single Canadian securities regulator is gaining momentum.

In October 2006, the Task Force to Modernize Securities Legislation in Canada (the Allen Task Force), sponsored by the Investment Dealers Association of Canada, published voluminous academic research. Several academics recommended a single Canadian regulator or a coordinated, unified approach to accomplish efficiencies and best practices in market regulation, the fair enforcement of investor rights, the development of principles-based securities laws, and greater Canadian economic competitiveness in the global context.

### **A matter of political cooperation**

Achieving a single securities regulator in Canada will be a matter of political cooperation. Giving impetus to the Crawford Panel proposal is publicly expressed support by the Ontario and federal governments. Private conversations by Panel members with governments suggest that political acceptance is evolving in other jurisdictions. Several have signaled that Canada must evolve to a single regulatory regime.

### **A national rather than federal agency**

A significant realization in the past year is that, due to Canada's constitutional character, a single securities regulator will have the best chance of succeeding if it is a *national* rather than *federal* agency, based upon cooperative federalism. This critical distinction opens the way forward and is a cornerstone of the Crawford Panel Blueprint.

Specifically, the Crawford Panel proposes a Council of Ministers to provide political oversight of capital market regulation on a national basis. Each participating jurisdiction, no matter how large or small, would have one vote on the Council. In this way, no one jurisdiction would dominate. The Blueprint also calls for federal participation on the Council with one vote just like British Columbia, Nova Scotia or any other jurisdiction.

This governance structure would fully protect each jurisdiction's constitutional claim to securities regulation (to regulate property and civil rights in the case of provinces, to regulate trade and commerce in the federal case). It would put to rest the fear that Ottawa would dominate a single regulator that has national scope.

## Ontario government support

Another obstacle to achieving a single securities regulator has been the perception that Ontario, which regulates more than 80 percent of Canada's listed market capitalization, would dominate such an agency. This perception has moderated in the past year as jurisdictions have come to recognize that the governance model proposed by the Crawford Panel would rebalance political oversight of the Canadian market. Jurisdictions are beginning to accept that this “pan-Canadian” solution is non-threatening and a natural evolution of the passport system.

The passport system, launched in September 2005, fosters cooperation on securities issues among participating jurisdictions to the extent that the system's national instruments are adopted on an identical basis by all participating jurisdictions. Regulatory approval in one participating jurisdiction is accepted by other participating jurisdictions, although each participating jurisdiction charges its own fees and retains the right to make its own rules. In December 2006 the Provincial/Territorial Council of Ministers of Securities Regulation stated that further regulatory reforms under the passport system “would respect individual provincial/territorial responsibilities for securities regulation.”<sup>2</sup>

Ontario is not a member of the Provincial/Territorial Council and its passport system. It has declined to join until the other jurisdictions accept that a single common regulator is the ultimate goal of the passport system. In speeches during late 2006, the Hon. Gerry Phillips, Ontario's Minister of Government Services who is responsible for the province's securities regulation, stated:

*“The passport system represents a step forward. I believe it doesn't go far enough. It can't lead to the economic and market efficiency benefits that a common securities regulator could because it still leaves us with 13 different sets of rules in 13 different jurisdictions. ... I happen to think that [the Crawford Panel Blueprint] provides Canada an opportunity to give our country a distinct competitive edge in international markets.”<sup>3</sup>*

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<sup>2</sup> Provincial/Territorial Council of Ministers of Securities Regulation, *Year End Progress Report*, December 2006.

<sup>3</sup> Hon. Gerry Phillips, Ontario Minister of Government Services, *Moving Securities Regulation Forward: Protecting Ontario's Investors and Fostering Competitive Markets*, at pp.4-5, address to Economic Club of Toronto, October 5, 2006.

In the meantime, we have learned that, while Ontario is not a participant in the passport system, the Ontario Securities Commission is actively involved with the passport jurisdictions in drafting many of its national instruments.

## Federal government support

The federal government publicly endorsed the Crawford Panel Blueprint just two weeks after the Panel issued its report. The report is an historic departure from past positions, which have favoured a federally controlled securities regulator, such as the one proposed most recently in 2002 by the Wise Persons Committee, a committee sponsored by the federal government. In June 2006, the Hon. Jim Flaherty, Minister of Finance, said:

*“This report [the Blueprint] recommends a common securities regulator for Canada and a governance model that ensures more effective participation by all jurisdictions. I believe it's a sound proposal that can contribute to reform of securities regulation in Canada.”*<sup>4</sup>

In its budget papers released in March 2007, the federal government recognized the complexity and fragmented character of Canadian capital market regulation:

*“Capital markets are an area of shared jurisdiction in Canada. The pursuit of a Canadian advantage requires the participation of all parties engaged in the regulation and business of capital markets. This includes the federal and provincial-territorial governments, their regulatory agencies and law enforcement bodies, self-regulatory organizations, standard-setting bodies and professional and industry associations, and market participants, including issuers, investors and intermediaries.”*<sup>5</sup>

The federal budget papers also state:

*“A new approach to securities regulation is proposed [in the Blueprint], one that is based more on principles and tailored to the unique makeup of Canada's capital markets, with both Canada-based global corporations and a large number of small- and medium-sized issuers. A move to proportionate, more principles-based regulation will be a significant undertaking that would be difficult to achieve under the current, fragmented structure of securities regulation. A common securities regulator will create the opportunity to*

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<sup>4</sup> Hon. Jim Flaherty, Minister of Finance, address to Halifax Chamber of Commerce, June 19, 2006, at p.7.

<sup>5</sup> Department of Finance Canada, *Creating a Canadian Advantage in Global Capital Markets*, Foreword by the Minister of Finance, Budget 2007, at pp.3-4, at [www.budget.gc.ca/2007/themes/bkcm.html](http://www.budget.gc.ca/2007/themes/bkcm.html).

*deliver this new approach. It will help improve investor protection, cut red tape, reduce costs for market participants and give an equal voice to all participating jurisdictions.”*<sup>6</sup>

## **Position of other jurisdictions**

As noted earlier, the Panel's background discussions suggest that other provinces are willing to explore the Blueprint, building on progress being made by the passport system. An issue of concern to some small jurisdictions that lack regulatory resources is the potential revenue loss from fees paid by issuers and investment dealers if there is a move to a single securities regulator.

## **Response to the Crawford Panel Blueprint**

Significantly, in the past year there has been the absence of substantive criticism of the Blueprint itself by provincial and territorial ministers. (Key components of the Blueprint are attached to this report as Appendix A). The federal government has repeatedly endorsed the core premise that all participating jurisdictions would have one vote at the Council of Ministers.

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<sup>6</sup> Budget 2007, Chapter 5, p.3.

## ADDRESSING CRITICAL ISSUES

While the specific Blueprint proposals have not attracted political criticism, premiers and ministers have raised concerns in private discussions about certain issues, including the feasibility of adopting national principles-based securities regulations; investor protection through national enforcement; the implications of a single national regulator for small- and medium-sized firms; and concerns about Canada's capital market competitiveness.

In the view of the Panel and many specialists who have studied the regulation of Canada's capital markets, these issues can only be optimally resolved if the provinces and federal government adopt a single securities regulator. The Blueprint is designed to make Canada the best place in the world in which to invest and raise capital for small and large businesses; to demonstrate leadership through innovative and cost effective responses to the needs of capital market participants; and to enforce investor rights on a consistent, tough and fair basis throughout the country.

### **The case for principles-based regulation**

Currently, 13 provinces and territories have detailed rules that tell publicly traded companies, investment dealers, investors and other market participants what they can and cannot do. It is time-consuming and demanding work to find and understand all these rules, and does not necessarily lead to a culture of compliance.

There is growing appreciation among political leaders, securities regulators, market participants and legal academics that a greater emphasis on principles-based regulation has many benefits over an excessive emphasis on rules-based regulation. The Crawford Panel recommended a single securities act containing basic principles of securities law and delegating rule-making authority to the Canadian Securities Commission. The Crawford Panel supports a principles-based approach to regulation because, among other reasons, it would improve the competitiveness of Canada's capital markets, perhaps producing a competitive edge over the United States.

Adopting a single securities act based on principles should not be difficult or time consuming as British Columbia has already done much of the needed groundwork in its earlier proposal for new securities regulation.

Doug Hyndman, Chairman of the British Columbia Securities Commission, explained in an April 2007 article in *Investment Executive* that British Columbia launched its initiative in 2001 to streamline and simplify its rulebook to reduce the burden of regulation on the capital markets while maintaining strong protection of investors and market integrity.

*“We thought then, just as we think now, that regulators should focus on delivering value to investors, who ultimately pay the costs of regulation. We owe them to make sure that the value of regulatory protection exceeds the costs it imposes.”*<sup>7</sup>

The initiative was abandoned in acquiescence to the passport system, underscoring the ineffectiveness of the current multi-jurisdictional system to move expeditiously to innovate let alone keep pace with changes in global practices.

In arguing for a principles-based approach, Mr. Hyndman stated:

*“Regulation usually works best when we set out clearly what outcome a market participant must meet and leave it to the market participant to find the best way to achieve it. That way, people have to think about what is right and wrong, not what they can or cannot get away with under the rules.”*

Mr. Hyndman concluded:

*“It's critical that we get going, to capitalize on the current momentum. We have to build confidence in this new approach, so we don't abandon it and revert to our bad old rule-making habits when we hit the next rough patch in the markets. The opportunity is here to give Canada a leading-edge system of regulation that will make our markets fair, efficient and competitive for the future. Let's seize that opportunity for the benefit of investors and all Canadians.”*

The Crawford Panel agrees. So do the academics who published reports on approaches to securities regulation under the auspices of the Task Force to Modernize Securities Legislation. However, principles-based legislation can only be effective under a single securities regulator to ensure consistent interpretation and enforcement of securities law throughout Canada. The current multi-jurisdictional regulatory structure cannot make such a guarantee. David Wilson, Chair of the Ontario Securities Commission, observed in a November 2006 speech:

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<sup>7</sup> Doug Hyndman, Chairman, British Columbia Securities Commission, *Time is ripe for principles-based regulation: Canada could have a leading-edge system that would make our markets fair, efficient, competitive*, *Investment Executive* e-magazine, April 2007.

*“Through consensus, the Canadian Securities Administrators might well be able to come up with a set of common principles for each regulatory issue. But that would still mean 13 different ways of interpreting and administering them. It would be analogous to adopting a single constitution — and leaving its interpretation to 13 separate Supreme Courts. That's why it's not enough to get the structure right or to get the approach right. The two are inextricably linked.”*<sup>8</sup>

The example of successful principles-based regulation most frequently cited is the experience of the United Kingdom, where the Financial Services Authority has enunciated eleven principles (albeit supported by a large rule book). Several recent studies, especially in the United States, claim that the principles-based approach to securities regulation is a key reason why London has gained global competitiveness in capital markets, along with an effective enforcement strategy. Another reason is that it moved to a single regulator for all financial and investment services. Last year, a study commissioned by the Allen Task Force noted that Canadian companies have listed on the UK's Alternative Investment Market in part because of its principles-based approach to securities regulation. (Other reasons include greater liquidity and easier access to global investors<sup>9</sup>).

An important feature of the UK's principles-based regulation is that it is also risk-based, meaning that regulation focuses on firms, markets or financial instruments in proportion to the perceived risk to regulatory objectives. An effective risk-focused approach also means, in the view of the U.S. Federal Reserve Board Chairman, the promotion of market discipline under which “regulators take positive steps to ensure that investors and asset managers bear the consequences of their financial decisions.”<sup>10</sup> He also argues for international collaboration on risk-focused and principles-based policies. The Crawford Panel supports this approach to principles-based regulation.

Flexible regulation based on principles could help to distinguish Canada from the U.S. in ways attractive to investors and issuers. A recent U.S. report recommends that the Securities and Exchange Commission (SEC) adopt prescriptive rules fashioned in terms of outcomes, performance and results rather than inputs and mandated processes. “Regulations and the oversight of such regulations by the regulatory authority should be risk-based and principles-based,” states the Interim Report of the Committee on Capital Markets Regulation.<sup>11</sup> A 2005 survey found that U.S. financial services professionals prefer the London regulatory environment for two reasons: first, the U.S. has too many regulatory bodies and there is lack of

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8 David Wilson, Chair, Ontario Securities Commission, *Momentum for Change: Providing the Regulation Canada Needs*, at p.3, Dialogue with the OSC, Toronto, November 10, 2006.

9 Stéphane Rousseau, *The Competitiveness of Canadian Stock Exchanges: What Can We Learn from the Experience of the Alternative Investment Market?*, in The Final Report of the Task Force to Modernize Securities Regulation in Canada, Volume 5: Maintaining a Competitive Capital Market in Canada, October 2006.

10 Ben S. Bernanke, Chairman, Federal Reserve Board, *Regulation and Financial Innovation*, address to the Federal Reserve Bank of Atlanta's 2007 Financial Markets Conference, Georgia, May 15, 2007.

11 *Committee on Capital Markets Regulation Interim Report*, November 20, 2006, at p.8 at [www.capmktreg.org](http://www.capmktreg.org).

consistency among them; second, the UK's more flexible, principles-based regulatory philosophy is preferable to the SEC's prescriptive, rules-based approach.<sup>12</sup>

The obstacle to Canada seizing a principles-based competitive advantage is the current regulatory structure. Canada is the only advanced economy in the world that does not have a single securities regulator. When an issue like principles-based regulation emerges, Canada has to debate among 13 jurisdictions whether a change in regulatory approach makes sense. The B.C. experience illustrates the difficulty.

Even if it were possible to achieve consensus among the 13 regulators to adopt a principles-based, risk-based approach to regulation, there would still be 13 different regulators bringing to the marketplace their interpretation as to whether a particular course of conduct complied with applicable principles. Markets, and market participants, desire certainty. A plethora of different regulators interpreting broad principles instead of specific rules does not produce that certainty. One regulator consistently interpreting principles can provide the consistency and certainty that the market needs.

A principles-based regulatory approach also offers regulatory flexibility, which is especially important to small- and medium-sized companies competing for investment capital. As Janice Sarra, Associate Dean and Professor of Law at the University of British Columbia, and Director of its National Centre for Business Law, noted:

*“The British Columbia draft legislation reflects the profile of the province's capital market, with its heavy preponderance of small- and medium-sized enterprises (SMEs). It can be adapted to accommodate the similar needs of SMEs in other provinces. ... A principles-based approach can readily accommodate the regional interests of Canada to the extent they are distinctly different. This would fit well with the blueprint proposed by the Crawford Panel on a Single Canadian Securities Regulator that includes effective regional centres or local offices in every jurisdiction.”<sup>13</sup>*

Finally, the federal government announced in March 2007 that it will work with the provinces and territories to establish targets and timelines for adopting a new approach to securities regulation based on clearly enunciated and sound principles.

In favourably citing the UK experience, the federal government stated:

*“Canada can pursue an advantage through a less complicated and more flexible system of securities regulation, founded on sound principles and supplemented by clear and effective rules that are proportionate to the different needs and capacities of small and large firms.”<sup>14</sup>*

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12 Oxera Consulting Ltd., United Kingdom, November 2005, pp.21-22.

13 Unpublished article.

14 Department of Finance Canada, *Creating a Canadian Advantage in Global Capital Markets*, at p.9.

In the Panel's view, the broadening support for a principles-based approach to securities regulation will intensify pressure for a single securities regulator.

## National enforcement of investor rights

The consistent and fair enforcement of investor rights on a national basis are persuasive reasons supporting the need for a single securities regulator. We are confident that other jurisdictions will come to the same view. As the Ontario Securities Commission succinctly stated: “Effective enforcement is our biggest challenge.”<sup>15</sup>

Many organizations have expressed dissatisfaction with the current system. For instance, speaking on behalf of the National Pensioners and Senior Citizens Federation, Diane Urquhart, a former managing director of equity research and equity strategist for Scotia Capital Markets, said earlier this year with respect to enforcement: “The present state of securities regulation in Canada goes beyond incompetence. It is a national disgrace.”<sup>16</sup>

In October 2006, the federal, provincial and territorial ministers responsible for justice agreed to establish the Working Group on Securities Fraud Enforcement to review ways to improve enforcement against securities fraud and other commercial crimes. The working group consists of representatives from police, securities regulators, Crown prosecutors and criminal law policy officials. Co-chaired by Louis Dionne, director of criminal and penal prosecutions for the Quebec Department of Justice and David Wilson, Chair of the Ontario Securities Commission, the working group has been asked to present its final report to the justice ministers by the fall of 2007. No doubt the working group will hear about and discuss the benefits of achieving their mandate by placing enforcement under a single securities regulator.

At the moment, however, enforcement responsibility is dispersed among 10 provinces, three territories and the federal government. All have a constitutional interest in keeping a watchful eye on issuers, investment dealers, investors and other market participants. Each province has its own approach to enforcement. Some jurisdictions lack sufficient expertise to investigate and prosecute complex cases. Self-regulatory organizations, federal, provincial and municipal police, and the federal and provincial judiciary also have enforcement interests. Police departments have their own priorities and capacities. Some judges wonder if they have sufficient knowledge to handle complicated cases.

Former Supreme Court of Canada Justice Peter Cory and former Dean of Osgoode Hall Law School Marilyn Pilkington recently completed a study of critical issues in enforcement for the Allen Task Force.<sup>17</sup> The study found that many high profile cases have not been prosecuted, insider trading is undeterred, some prosecutions are unfair, regulators delay in acting to prevent investor losses, investigations are not managed effectively, and securities commissions as both regulator and adjudicator have the appearance of

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<sup>15</sup> Wilson, *Momentum for Change*, at p.5.

<sup>16</sup> Quoted in David Clarke, *Canadian seniors group calls for enforcement reform*, Investment News at [www.investmentnews.com](http://www.investmentnews.com), March 12, 2007.

<sup>17</sup> Hon. Peter de C. Cory and Marilyn L. Pilkington, *Critical Issues in Enforcement*, in The Final Report of the Task Force to Modernize Securities Regulation in Canada, Volume 6: Strengthening Market Credibility and Integrity, pp.172-248, October 2006.

bias. To make matters worse, police, prosecutorial services and courts lack sufficient specialized knowledge of capital markets, there are delays in court proceedings, and penalties are inadequate and inappropriate. Investors are unhappy about being unable to obtain compensation for losses caused by wrongdoing.

Canada's multi-jurisdictional approach to securities regulation is a good part of the problem. The study found divided jurisdiction over enforcement dilutes resources, encourages competition among jurisdictions, confuses accountability, increases costs, creates unnecessary delays, and generally impedes effectiveness.

*“It can result in unfairness to an individual or entity seeking to resolve a matter in more than one jurisdiction. If this situation is continued it will eventually have a serious detrimental effect on the operation of Canadian capital markets.”*<sup>18</sup>

The study recommended that enforcement be coordinated nationally to ensure the effective use of resources and the development and deployment of expert skill and knowledge across the country; and a nationally coordinated program be implemented for the prosecution of capital markets cases. Additional judicial appointments must also be made to provincial courts and additional facilities must be established to ensure the capacity to prosecute and try capital markets offences.

The Crawford Panel urges political leaders to commit to a single securities regulator with the expertise, the will and the muscle to make enforcement a priority.

Not all disputes should end up in court. The Crawford Panel has proposed a Canadian Securities Tribunal independent of the Canadian Securities Commission to decide conflicts between the regulator and those charged. The Cory/Pilkington study also recommended that the adjudicative functions of securities commissions be transferred to an independent tribunal.

The Panel is pleased that the federal government has decided to take a leadership role by committing to a single securities regulator to strengthen capital market enforcement and by accepting our proposal for a separate securities tribunal to adjudicate disputes. The federal government has also committed to supplement substantially the resources of Integrated Market Enforcement Teams, led by the Royal Canadian Mounted Police, to achieve more effective and timely investigations.

The attention now being paid to enforcement from a national perspective should give further impetus to acceptance of a single securities regulator, paralleling the pressure building from support for a principles-based approach to securities laws.

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<sup>18</sup> Ibid., p.247.

## Implications for small- and medium-sized firms

Supporters of the current Canadian regulatory system argue that it is the best system for small- and medium-sized firms as it allows governments to protect the interests of these firms within their jurisdiction. They question whether a single regulator would similarly be able to protect the interests of these firms. This resistance is based on the false belief that the interests of companies seeking capital in the public markets differ markedly from province to province. It also incorrectly assumes that businesses seeking \$1 million to \$10 million from public investors lack either the competency or inclination to go outside their home province in search of equity capital.

Governments quite properly worry about helping small- and medium-sized enterprises (SMEs) to grow and prosper. They represent 99 per cent of all firms in Canada and employ two-thirds of private sector workers. Compared with the United States, Canada has a much heavier concentration of firms at the small end of the scale and relatively few firms at the upper end. For the Canadian economy to prosper, growth-oriented SMEs need ease of access to competitively priced equity capital. In this respect, the interests of SMEs are identical, irrespective of their home province. Unfortunately for them, the current system with 13 regulators is unduly costly and inhibiting.

In early 2007, the Canadian Bankers Association published a breakthrough study that challenged assumptions underpinning some current thinking about SMEs.<sup>19</sup> The study examined the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval (SEDAR) database to understand the nature of Canadian capital markets and SME issuers. The SEDAR data suggest that issuers headquartered in the four largest provinces are primarily small firms involved in the resource, industrial, finance, insurance and real estate sectors. CBA looked at how much capital these firms are trying to raise, where they are raising it and what it costs them to do so.

The prospectuses of 298 SMEs that raised capital between 2002 and 2006 were examined. The median offering size was \$6 million and nearly two-thirds were for less than \$10 million. The sample has a concentration of smaller firms. Despite the small size of the offerings, only seven firms raised capital in their home province alone, discounting the claim that SMEs primarily raise capital locally. At the other extreme, one-quarter of the sample (primarily larger issuers) raised capital in 10 or more jurisdictions.

The vast majority of issuers, therefore, raised small amounts of capital in more than one jurisdiction but restricted themselves to a few provinces and territories. This underscores the fact that these firms do not reach investors across Canada. What limits their reach? One important factor is the additional regulation-related costs of filing in multiple jurisdictions. In examining the SEDAR information, including expense data, issuer size and number of jurisdictions, the research highlights:

- Firms limit the number of jurisdictions in which they raise capital. Most raise capital in two to four jurisdictions.

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<sup>19</sup> Canadian Bankers Association, *The impact of multiple regulators on the cost of raising capital for small- and medium-sized businesses*, CBA Paper, February 2007, at [www.cba.ca](http://www.cba.ca).

- For any particular offering size, for example \$3 million, expenses increase as the number of jurisdictions in which the offering is made goes up.
- The proportion of capital raised that is consumed by regulation-related expenses is four times higher for small offerings (\$1 million) than it is for larger offerings (\$10 million).
- Should a firm conduct an offering in 13 jurisdictions rather than only one, its regulation-related expenses would likely double. A firm raising \$1 million in all 13 jurisdictions would see expenses consume over 15 percent of the amount of capital raised.

The CBA study concluded that:

*“The current regulatory system drives up the cost of acquiring capital, particularly for SMEs. The Canadian economy is more dependent upon SMEs than are other nations, especially the United States. SMEs in both countries have traditionally lagged larger firms with respect to productivity growth, but American SMEs have performed substantially better than Canadian SMEs in this regard. Productivity enhancing investments have proven to be best financed by equity capital, but we have a structure for securities regulation that fragments the market and makes it particularly expensive for SMEs to raise equity capital.”*

A 2006 study by the Certified General Accountants Association of Canada found that 60 percent of small- and medium-sized firms consider securities regulation the most unreasonable regulatory burden they face (followed by 22 percent considering tax regulation the most unreasonable). These views were strongest among SMEs in British Columbia and Alberta.<sup>20</sup>

A single securities regulator would reduce the cost of raising capital for SMEs and give Canadians in all parts of Canada equal access to investment opportunities. Another challenge facing these firms in Canada is the current “one size fits all” approach of most securities rules. Bank of Canada Governor David Dodge has argued repeatedly for uniform principles that also take into account the size and complexity of the issuer, most recently in December, 2006:

*“The principles of Canada's regulatory framework must apply to all firms, and must be as good as, or better than, those of any country. But the application of the rules can and should be tailored appropriately to take into account the size and complexity of the company. ... Canada should try to develop a comparative advantage in securities regulation for these smaller firms if it is to remain a market of choice for companies, both Canadian and foreign.”*<sup>21</sup>

<sup>20</sup> Certified General Accountants Association of Canada, *Tackling Compliance: Small Business and Regulation in Canada*, October 31, 2006 at [www.cga-online.org](http://www.cga-online.org).

<sup>21</sup> David Dodge, Governor of the Bank of Canada, *Improving Financial System Efficiency: The Need for Action*, p.4, address to the Economic Club of Toronto, December 11, 2006 at [www.bankofcanada.ca](http://www.bankofcanada.ca), at p.4.

After reviewing the situation in the UK and U.S., he added:

*“[We] in Canada increasingly look as if we are stuck in the middle of the 20th century and are not positioning ourselves well to compete in the 21st century. For the sake of efficiency, we need a single, uniform framework for securities regulation. Rules need to be applied in a uniform way across the country, and tailored to be appropriate for firms of all sizes, while providing appropriate protection for investors.”*<sup>22</sup>

The federal government made the case for “proportionate or tiered” regulation in the 2007 budget, commenting:

*“Regulation tailored by size or market capitalization would give issuers the opportunity to innovate, grow and develop in their chosen markets, without being stifled by overly complex rules. This would be particularly beneficial to such issuers as high-technology start-ups and junior oil and gas and mining companies.”*<sup>23</sup>

It is now clearer than it was a year ago that moving to a single securities regulator will lower the cost of capital for SMEs, reduce their fees for complying with so much regulation, improve their nation-wide access to investors, and it would also permit the regulator to adopt tiered regulation to their benefit.

## Canada's capital market competitiveness

From the global perspective, capital markets are becoming more competitive. The London Stock Exchange, the Deutsche Börse and Euronext are aggressively wooing companies, large and small, to list with them rather than in North America. London's Alternative Investment Market is emerging as an exchange of choice for small firms throughout the world. Asian exchanges, from Hong Kong to Bombay, and in nations such as Australia, are taking a competitive stance in response to a shrinking technology-based world. In North America, U.S. exchanges are seeking global alliances to maintain competitive leadership. Barriers to free trade in securities are diminishing, a trend that is expected to gain momentum.

Canada must pay greater attention to its capital market competitiveness and review its regulatory regime in a global context. Companies at home and abroad dislike regulatory complexity. Having to deal with 13 regulators in such a tiny capital market in the global scheme of things is not helpful to positive perceptions of Canada's attractiveness. This outdated regulatory model undoubtedly encourages issuers and investors to go elsewhere. Technology and globalization make that very easy to do.

One of Canada's biggest challenges is being able to respond quickly to emerging issues. An objective of the Crawford Panel Blueprint is to demonstrate leadership through innovative and cost effective responses

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<sup>22</sup> Ibid., p.5.

<sup>23</sup> Department of Finance Canada, *Creating a Canadian Advantage in Global Capital Markets*, p.10.

to the needs of capital market participants. The context is global. The current regulatory system is simply too laborious and bureaucratically fragmented to demonstrate the nimble competitiveness that issuers and investors have come to expect. Risk capital, a driving force of economic innovation and national prosperity, is indifferent to political boundaries. New pools of capital, controlled by private equity firms, hedge funds and public sector pension funds, have changed the dynamics of investing.

Studies published by the Allen Task Force emphasize the competitiveness challenge. For example, Mark Gillen, law professor at the University of Victoria, states that improving Canada's capital market competitiveness can improve the allocation of savings to investment, lower the cost of capital and increase the country's level of production. If our capital market was more competitive than other jurisdictions, "then it can attract foreign issuers and investors and become a more significant provider of services associated with capital markets."<sup>24</sup> Christopher Nicholls, law professor at the University of Western Ontario, observes that: "As a heavily-regulated small market, there is some risk that Canada will not be attractive as an alternative either to the similarly regulated but deeper U.S. market, or to the more flexibly regulated U.K. market."<sup>25</sup> Anita Anand, law professor at the University of Toronto, characterizes Canadian securities regulation as voluminous given the size of capital markets at two to three percent of world capital markets, the number of issuers that access them, and the amount of capital raised. "It is imperative that securities regulation encourage domestic and foreign issuers to choose Canada as a market where they will raise capital."<sup>26</sup> She adds that: "The structure of Canada's regulatory regime, consisting of thirteen separate securities regulators, surely adds to the difficulty in attaining a competitive position globally."<sup>27</sup>

Industry specialists generally recognize how the issues discussed in this report can only be handled effectively by Canada moving to a single securities regulator. Their position was succinctly summarized by the Investment Industry Association of Canada, which officially declared its support for a common regulator on June 12, 2007:

*"A common regulator would provide the flexibility and cost-effectiveness to respond to fast-moving and innovative global markets. A common regulator that is responsive to the needs of regional and small businesses would also provide the catalyst to move to a more principles-based regulation. ... It is unrealistic to expect that the operation of multiple regulators within the CSA can match the efficiency that a common securities regulator would provide."*<sup>28</sup>

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24 Mark Gillen, *The Role of Securities Regulation in Promoting A Competitive Capital Market*, in Task Force to Modernize Securities Regulation in Canada, Volume 4: Maintaining a Competitive Capital Market in Canada, October 2006 at p.12.

25 Christopher Nicholls, *The Characteristics of Canada's Capital Markets and the Illustrative Case of Canada's Legislative Regulatory Response to Sarbanes-Oxley*, *ibid.*, at p.138.

26 Anita Anand, *Towards Effective Balance Between Investors and Issuers in Securities Regulation*, in The Final Report of the Task Force to Modernize Securities Regulation in Canada, Volume 3: Evolving Investor Protection, October 2006 at p.18.

27 *Ibid.*, p.68.

28 Bill Hatanaka, Chairman and CEO, TD Waterhouse Canada Inc., and outgoing Chair of the Investment Industry Association of Canada, quoted in news release *Investment Industry Association comes out in favour of common regulator at its annual conference in La Malbaie*, June 12, 2007 at [www.iiqc.ca](http://www.iiqc.ca).

## THE WAY FORWARD

The challenge today is finding a way to move the Blueprint forward so that it satisfies political concerns and builds on the specialized knowledge and professionalism that resides among Canada's multiplicity of securities regulators.

The Crawford Panel recommends that:

1. Provincial/territorial ministers responsible for securities regulation, as well as the federal minister of finance, create a small task force of professional specialists to draft the first Canadian Securities Act.

We suggest that the task force consist of five to seven professionals, including one or two closely involved in drafting the United Kingdom's Financial Services and Markets Act 2000. The UK experience required a seismic shift in thinking about a totally different approach to securities regulation. Canada must make a similar significant mindset shift by including on the task force knowledgeable professionals who understand how market participants will carry on business in a principles-based regulatory environment. Leveraging experience and expertise in Canada and the UK should prove invaluable in ensuring the draft legislation preserves a Canada-centric character and demonstrates global leadership.

The draft statute should be based as much as possible on the proposed principles-based legislation drafted previously by the British Columbia Securities Commission.

The national instruments currently adopted by the CSA should form the underlying rules. The task force should identify other rules that need to be adopted on a national basis by the Canadian Securities Commission.

The task force should be asked to complete its work within one year.

2. The securities ministers should establish a second task force to settle a memorandum of understanding (MOU) on the structure and governance of the Canadian Securities Commission. The MOU should take into consideration, and be based upon, the structure set out in the Crawford Panel Blueprint.

This task force should report to the securities ministers in six months.

Once its work is completed, the recommended structure and governance of the Canadian Securities Commission should be reflected in the Canadian Securities Act being drafted by the first task force.

## APPENDIX A

### Key Components of the Crawford Panel Blueprint

1. A Council of Ministers to provide political oversight of capital markets on a national rather than local basis. The Council would approve the originating legislation as well as rule changes once the Canadian Securities Commission is operational. It would appoint a nominating committee for the Commission's own board of directors.
2. An independent board of directors for the proposed Canadian Securities Commission. With a non-executive chair, its members would have competencies relevant to capital market regulation and competitiveness. The directors would act in the best interests of issuers, investors, intermediaries and the public. They would not represent the interests of a specific government, although the board would be accountable to the Council of Ministers, much as a corporate board is accountable to its shareholders.
3. An arm's-length mechanism for selecting and electing directors identical to that used by federal and provincial finance ministers to appoint directors at the Canada Pension Plan Investment Board. Each jurisdiction would appoint a public or private sector representative to the nominating committee. The committee would find, screen and recommend candidates. The ministers would elect directors only from the list submitted by the committee and would not substitute their own nominees. This process defuses the risk of political domination by any jurisdiction.
4. A Canadian Securities Commission managed by a team led by a Chief Commissioner, who would report to the Board. Appointment of a strong first Chief Commissioner (as well as a strong first non-executive Board Chair) will set the tone of success for the entire organization. The Chief Commissioner would recommend the appointment of vice commissioners to the Board. The requisite talent already exists among leading provincial regulatory agencies.
5. A Canadian Securities Tribunal separate from the Canadian Securities Commission to adjudicate disputes. It would have its own offices, staff and budget. Panels of adjudicators would conduct hearings throughout Canada, consistent with rules of procedure approved by the Council of Ministers.

6. A securities act focused on the powers, responsibilities and duties of the Commission, Council of Ministers, Board of Directors and Nominating Committee, and including basic principles of securities law. To achieve a single act, one province would enact the appropriate legislation for others to adopt by reference. The constitutional authority of the provinces and federal government to incorporate legislation by reference has been upheld by the Supreme Court of Canada.
7. A common body of rules with rulemaking and the ability to grant exemptions delegated to the Canadian Securities Commission. Commission staff would recommend rules to the Board. If approved in principle, the proposed rules would be published for public comment. Final rules, including changes arising from public consultation, would then be formally approved by the Board, which would notify the Council of Ministers of its decisions. The rules would become effective on a date determined by the Board unless two-thirds of Ministers vetoed the proposed rule within 45 days of it being referred to the Council. This approach removes uncertainties about the interpretation of rules in different jurisdictions at different times under different political regimes.
8. A single fee structure premised on the Canadian Securities Commission being self-financing.

## THE PANEL

This Update Report is the work of a national Panel charged with recommending a model for a common securities regulator for Canada. The Panel's original terms of reference were to recommend a securities regulatory framework that features a common securities regulator, a common body of securities law and a single fee structure.

In May 2005, the Hon. Gerry Phillips, Ontario's Minister of Government Services, who is also responsible for securities regulation in the province, asked Purdy Crawford to chair the Panel. Panel members are drawn from all regions of Canada and a diversity of relevant backgrounds. The Panel members are:

<b>Purdy Crawford</b>	Counsel, Osler, Hoskin & Harcourt LLP (Panel Chair)
<b>Brian A. Canfield</b>	Chair, TELUS Corporation
<b>Claude Lamoureux</b>	President and Chief Executive Officer, Ontario Teachers' Pension Plan
<b>John A. MacNaughton</b>	Corporate director and former President and Chief Executive Officer, Canada Pension Plan Investment Board
<b>L. Jacques Ménard</b>	Chairman, BMO Nesbitt Burns and President, BMO Financial Group, Québec
<b>John Watson</b>	Corporate director and recently retired Executive Vice-President and Chief Financial Officer, EnCana Corporation
<b>Dawn Russell</b>	Associate Professor and former Dean, Dalhousie Law School

The Panel acknowledges the contribution of previous Panel member Gwyn Morgan, Corporate director and retired founding CEO of EnCana Corporation, and Janet Salter, lawyer, Osler, Hoskin and Harcourt LLP, who serves as the Panel's Chief of Staff.

The Panel published a discussion paper, *A Blueprint for a New Model*, on December 8, 2005. Based on consultations with market participants at a series of regional roundtables and discussions with provincial ministers responsible for securities regulation, the chairs of most securities regulatory authorities across the country, and various federal and provincial public servants and members of the private sector, the Panel produced its final report, *Blueprint for a Canadian Securities Commission* on June 7, 2006.

Notwithstanding the fact that Minister Phillips appointed this Panel, the opinions in this paper are solely those of the Panel and are not made on behalf of the Province of Ontario.





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