ISSN 1180-4386

Legislative Assembly
of Ontario

First Session, 38th Parliament

Assemblée législative
de l'Ontario

Première session, 38e législature

Official Report of Debates (Hansard)

Thursday 19 August 2004

Journal des débats (Hansard)

Jeudi 19 août 2004

Standing committee on finance and economic affairs

Ontario Securities
Commission Review

Comité permanent des finances et des affaires économiques

Étude de la Commission des
valeurs mobilières de l'Ontario

Chair: Pat Hoy
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Toronto ON M7A 1A2
Telephone 416-325-7400; fax 416-325-7430
Published by the Legislative Assembly of Ontario

Service du Journal des débats et d'interprétation
Salle 500, aile ouest, Édifice du Parlement
111, rue Wellesley ouest, Queen's Park
Toronto ON M7A 1A2
Téléphone, 416-325-7400; télécopieur, 416-325-7430
Publié par l'Assemblée législative de l'Ontario

LEGISLATIVE ASSEMBLY OF ONTARIO

ASSEMBLÉE LÉGISLATIVE DE L'ONTARIO

STANDING COMMITTEE ON FINANCE AND ECONOMIC AFFAIRS

COMITÉ PERMANENT DES FINANCES ET DES AFFAIRES ÉCONOMIQUES

Thursday 19 August 2004

Jeudi 19 août 2004

The committee met at 0901 in room 151.

ONTARIO SECURITIES COMMISSION REVIEW

FIVE-YEAR REVIEW COMMITTEE

The Chair (Mr Pat Hoy): The standing committee on finance and economic affairs will come to order. Good morning, everyone.

I would call on the five-year review committee to come forward, please. You have one hour for your presentation. You may allow for questions within that one hour, if you wish. I would ask you to state your name for the purposes of our recording Hansard.

Mr Purdy Crawford: My name is Purdy Crawford. With me this morning is another member of the committee, who was, at the time the committee was formed, general counsel to the Ontario Securities Commission, Susan Jenah.

I want to refer briefly to the five-year review committee. I think I've got to make a few comments and then Susan and I will be open for discussion and questions from the members of the committee, if that's appropriate, sir.

The Chair: It is.

Mr Crawford: We're delighted to be here before this committee. It was quite an interesting process chairing this committee. It was so broad in scope, reviewing all the rules of the commission, the Securities Act and the regulations. We were probably too ambitious and tried to cover too many areas.

The other members of the committee, if I may—they can't be here this morning. It's always a bit unfortunate that these things become recognized by the name of the chair, because it was a strong committee and all the members played a very significant role in formulating the recommendations: Carol Hansell; William Riedl, who was then head of Fairvest and is now retired; Helen Sinclair, chief executive of Bankworks; David Wilson, chair and chief executive officer of Scotia Capital and vice-chair, Bank of Nova Scotia; and, as I mentioned earlier, Susan Jenah.

The committee was a volunteer committee; it was not paid. I outline in what I've called my opening remarks—I'm not going to read them but I think you are getting copies—how many meetings we had and things like that. We had no budget and very limited staff but they were very good people: Anita Anand, who is here this morning, from the faculty of law at Queen's University; Rossana De Lieto, senior legal counsel for the OSC; Krista Martin-Gorelle, senior legal counsel for the OSC; and Janet Salter of the law firm where I am counsel, Osler, Hoskin.

As I think probably the material tabled with you by David Brown yesterday indicates, quite a number of our recommendations have been enacted. I'm not going to deal with those. I want to deal with about seven major subjects.

The first one—and I'm not going to spend long on it, although in terms of its importance for Canada, I think it's fundamental—is the need for a single securities regulator. I know it's a very broad issue and it has been discussed backwards and forwards. I won't take the committee through what we said in our report or the summary of what we said in my opening statement except to say that I agree with Minister Phillips that it's a very important issue, long term, for Canada. Whatever this committee can do to further that approach of one securities regulator, from my perspective and the perspective of my committee, it would be welcome and applauded.

I was not here yesterday but I had a briefing on the telephone last night about the proceedings of yesterday. The next item I want to mention is the structure of the Ontario Securities Commission, which I gather was discussed at some length yesterday. We considered this issue as one of many issues we looked at in our report. It was fairly early on and we concluded that there was an issue as to perception, at least, as to the fact that the commission had judicial functions as well as investigation and policy-making functions.

We recognized that the structure was legal—I did have a chance to read Mr Brown's statement yesterday, or at least an earlier draft of it—under the Supreme Court of Canada decisions, but we felt there was a perception issue. The furthest we went in our report was to say that we thought it should be looked at more carefully. I believe Chairman David Brown of the commission appointed three people to look at that. I understand that their report and a couple of opinions were tabled here yesterday, and you people had an interesting discussion about it. I think it's hard for me to be definitive one way or another. I see in David's comments that he raises both

sides of the issue. We did not take a position as a committee. We just thought it should be looked at and, thanks to you people and others and this public policy forum, it is being looked at, but I'd be happy to answer questions about it at the appropriate time as we move forward.

0910

Another issue we did spend quite a bit of time on is related to the governance of mutual funds, and this is covered in my opening remarks, which you have. We made quite a number of detailed recommendations, but generally we recommended that there should be a majority of independent directors on the trust, if it was a trust, or on the board of mutual funds, if it was a company. They should have the right to appoint their own counsel and get their own independent advice.

These recommendations were formulated before the developments in the US that we've been reading about in the last year or so, in which some Canadian firms have been involved through their US operations. As I understand it, and I say in my opening remarks, I believe that some investigation is going on about mutual funds in Canada on the part of—I don't know whether it's the CSA or the OSC.

We released our draft report for public comment: So what should the function of these independent directors be? We said, obviously, if you've got to look at conflicts between the manager and the fund, the managers are there to make money. Obviously, if they can do a good job managing the fund, that helps them make money, but there's clearly a conflict of interest there.

So we thought in the draft report that probably the most important function that the independent director would have, in addition to dealing with conflicts, was reviewing the performance of the fund. After all, there are two big issues in mutual funds: the cost of the performance and the results of the performance. When we came to the final report, we backed off a little bit and didn't talk specifically about reviewing the performance of the fund.

Since then, you can argue whether there should be an independent governance structure. The SEC had an independent governance structure before and they've gone, in their recommendations or rules, to strengthening that structure, with a majority of independent directors—whether this is law yet, I don't think it is—and with the chairman of the fund being independent, in addition. We have investigations going on in Ontario, and we'll see how this unfolds.

I just think if you had a pension fund and you put money with a money manager, you normally are pretty careful in monitoring the performance. The most efficient way for most individuals to invest, because of a question of know-how, is through mutual funds. On the whole, performance of mutual funds has not been outstanding. It's an issue and something should be done about it. We said that in our report.

I want to make it clear that, first of all, I did a study once a few years ago on the independence of securities analysts and we concluded there—and I haven't done enough study here—that on the whole the integrity of our securities analysts and the integrity of our people who manage, run and promote our mutual funds is of a pretty high standard; there are always exceptions. I've certainly said it about corporate governance on more than one occasion. We have a higher standard of corporate governance in Canada, starting with the Dey report many years ago, than they have in the US, and I say this based upon a lot of US experience. I'm inclined to think it's the same with respect to mutual funds and with respect to securities analysts. So I'm not knocking our people. I just say we probably need a higher level of protection for the many individuals who invest in mutual funds.

The next item I want to refer to relates to civil liability for the secondary market disclosure. Way back in 1997, there was an Allen committee that recommended civil liability for certain types of instruments in the secondary market. As I'm sure you've been told, more than 90% of the activity and trading and dealing in securities is in the secondary market. It didn't seem to make any sense to me that there were all kinds of liabilities relating to a prospectus and IPO but no liabilities as such relating to trading in the secondary market.

In the US, through interpretation and otherwise—I think it's a phrase in some of the regulations called "manipulative and deceptive devices," sort of a fraud test—the courts developed liability in the secondary market. That has not happened in Canada to any great extent, if at all. I was the CEO of Imasco when the report came out much earlier about this—many in the Toronto Stock Exchange—and actually we were probably one of the few companies in Canada that wrote supporting the creation of liability in the secondary market. It's been around a long time. When it came to our committee looking at it, we decided we wouldn't try to reinvent the wheel. It's a complex issue and it can be done in many different ways and the devil is always in the details.

We would simply encourage the legislators, the policy-makers in Canada, you people, to get on with this and get it enacted and get it to become law across Canada. I believe the CSA has agreed that should be the approach. To me, it's a very important initiative in terms of investor protection. I know there are questions of how much liability there is. Some people will argue—probably my good friend Mr Anisman later today—that it goes too far in removing protection for the investor and others will argue it doesn't go far enough in removing protection for the investor. I say let's get on with it and turn the page and move forward.

The other item I just want to briefly touch relates to efficient regulations. We made some recommendations in the report relating to rule-making. Our recommendations were to make it conform more to the rule-making in other provinces.

Probably one of the most important recommendations we made in this respect was that if the government, the appropriate minister, decides not to approve a proposed rule, there should be a statement as to who made the submissions opposing it and some reason why they

weren't going to approve it, just to open it up to public scrutiny.

0920

There are two other items my colleague recommends that I bring to your attention. One is—we dealt with this in our report—the Uniform Securities Transfer Act. You'll be hearing about that later today. This is a piece of proposed legislation that nobody basically disagrees with. It's not controversial but it's very important in terms of mortgaging, hypothecating, pledging or transferring securities. There is a uniform system in all the states in the US. It has been worked on here. It'll make our capital markets more efficient. It will bring business to Ontario, because they're working with an old system and it's hard to give legal opinions and the transfer or the mortgage or the hypothecation is appropriate. You'll hear about this later today; I think there are one or two.

I've been a supporter of this. I hope you would recommend to the government that it proceed with finding some way to get some legislative time to get this enacted in Ontario.

Finally—this happened after our report—Gordon Thiessen is here today. He's the former head of the Bank of Canada, who heads up the Canadian Public Accountability Board. This is an organization that was established—flowing from the Sarbanes-Oxley Act—to supervise to some extent the accounting profession in Canada. It was set up as a nonprofit company. It needs statutory support. They now work with agreements between audit firms and the public accountability board. Mr Thiessen will be outlining to you later today the necessity of some statutory support. It's not a matter we dealt with, but it's a matter that—I can't speak to the details but I agree that statutory support is needed, and I'd support Mr Thiessen in that respect.

That completes my comments.

The Chair: Thank you. Did you have any comments at this time?

Ms Susan Wolburgh Jenah: Not at this time.

The Chair: OK. We have about 12 minutes per party for questioning. We'll begin with the official opposition.

Mr John O'Toole (Durham): Thank you very much, Mr Crawford. It's a pleasure to meet you and a pleasure to see you in person, presenting what you feel are the important aspects of your committee's work. Certainly it forms the basis for everything that we're doing here. That's the purpose of the review. Your suggestions, I believe, are the ones we should spend the most time commenting on.

Of anything I've heard to date—I can only speak for myself, but I do listen to others—I don't think there's any disagreement on having a national regulator—there's no question—in the climate today. There are several recommendations in here and in other reports—pretty well everyone who presents, even if they're dissenting, agrees on that issue, so I won't spend too much time on that.

I can say, in looking at the Wise Persons' Committee, that there's ample evidence there that they've stated categorically that there's a federal role in doing this under the Constitutional Act; I think it's section 93. So I'll leave that for Paul Martin to follow up on. I think the provinces can only place their voices on the table and respond to the professional input we've had here.

I think where I'm most interested myself is the issue you referred to as the public confidence issue, the perception issue, of the adjudicative functions of the securities commission. David Brown spoke yesterday, and Ms Wolburgh Jenah spoke as well, with the idea that they've considered what Coulter Osborne and others have said. You've left it sort of hanging a bit in some of your recommendations. It wasn't definitive to separate. It was more like it should be studied. That seems to be kind of an exit strategy. It doesn't mean you are definitively coming down on it. But if you're really trying to build confidence in a market and there is separation of government and the judiciary, the politics and—it's the same thing—the policy-setting role; I see the OSC doing the regulations and leading the government on the policy agenda. They do great work, I believe, at the national and international level. But that's that one piece, perception only.

Now, it's come to my attention—I'm not a lawyer, so I don't really know—that the commercial lists bench could easily do and have the knowledge to bring to the test of hearings with some knowledge. I would ask you to say that, if you were to separate it—and there may or may not be enough work. There are those that say they don't bring enough cases to trial. Is that one way we could have a transition at least for some, if not all, the cases, especially the large ones, where there's clear uncertainty? In fact, the OSC has a couple of times challenged the bench as not having the knowledge. Could you give me some sense of how you would do that transition?

Mr Crawford: I speak without a lot of knowledge of the structure of the courts. I know, as a pragmatic matter, that certainly the commercial lists bench in Ontario is very strong and has a lot of experience. I'm not sure whether it would be appropriate, feasible or constitutional for them to play the role of the adjudicative body of certain matters coming out of the Securities Act. Certainly it would be feasible for them to be an appellate tribunal from decisions of a judicial body or, for that matter, from decisions of the OSC.

It's certainly a lot better than in the US, where, although there is an independent tribunal in theory, appeals from the independent tribunal go to the active commission. So it's not really independent.

I can't give you a definitive answer, sir, except to say that I know that's a good court.

Mr O'Toole: Mr Brown saw and in fact Supreme Court Justice McLachlin was suggesting that there is a need to have the residential expertise setting regulations as well as making judgment on those regulations. That was seen as a validating reference point to keep it in-house under the OSC. That's really what I heard Mr Brown saying yesterday.

If I look at the role of the OSC and its emergence in the early 1990s and latterly as well: more and more reg-

ulations; more and more different kinds of market products; much more complex rule-making and exemptions etc; very important, absolutely critical ongoing administration of the capital market—no question. In fact, they are probably the leaders—maybe they wouldn't want to say that—in helping Canada get to the single regulator. We find out that Ontario, being the dominant player, isn't just moving all the pieces around. So that issue needs to be dealt with.

When I think of that as the validation, that says to me that none of the court principals, neither the prosecutors, the defence nor the judges themselves, have the leverage—or maybe there's not enough volume and experience. Do you understand? A retired person could do it—not retired, but someone who has been removed from the commercial list.

That, to me, is the most important part of the perception of the role of the OSC. It's huge. We aren't going to get to the single regulator immediately. It's going to be a minimum five-year deal. We could commit to it and get it done in five years, but if we don't commit, it won't be done.

Can you give me some—you are a practising lawyer, obviously, or were.

0930

Ms Wolburgh Jenah: I'd be happy to try to answer that question, Mr O'Toole, but it's really—you've raised a very, very important question and also, I think, touched on the issue that a lot of people are asking about, which is, what are the alternatives to address the perception issues? Let me just try, if I can, to give you a bit of an overview here, or a context.

There are two very different issues that we're talking about. One is the legality of the current structure, and the other is the perception, and what's the best answer for Ontario and indeed for the capital markets across the county? They are two different issues.

I think the reference to Chief Justice McLachlin's comments in the Ocean Port case really relates to the former to some extent, but also to the latter, because what she was saying in that decision was that when people challenge integrated agencies—and we're not the only agency, so this comment is not specific to us. But when people come in and challenge, and these would be people who are respondents, potentially, before an agency of this kind, what they're saying is that because of the fact that this agency, as a whole, performs all these functions—investigation, prosecution, adjudication and policy-making—there is a worry; there is an apprehension of bias. The allegation is not normally that there is actual bias. That's very rare. It's the perception; it's the apprehension. This is why Chairman Brown said that whether it's actual or apparent, if it's a perception, it concerns us, as I know it concerns you. So there is that one issue.

What she has said is that clearly where the Legislature has chosen to create a structure of this kind, that apprehension-of-bias issue cannot succeed solely on the basis of the argument that the structure is integrated, because that's exactly what the Legislature intended. So from a legal point of view, and Mr Osborne's report makes this clear as well, they agree there is no real legal issue outside of the charter question they raise and which we sought to have addressed because, as Chairman Brown said, it was a loose end.

Then you move to the perception and to the challenge of overcoming the perception issues. For all of the strengths that come with an integrated agency, you get, unfortunately, some of the side effects of it, and one of them is that perception that you have the commission as a whole performing these various functions.

In reality, when you strip this away, the commission, which is the members of the commission—it's like the board of a public company. It's not the staff. They are separate in many ways from the staff. So when people say the commission does investigation and prosecution, really, the staff of the commission are the ones who are doing the investigation and the prosecution. The commission itself, as commissioners, are not involved in that process, and where a commissioner has to sign an investigation order, they are statutorily barred from having anything to do with that matter on a go-forward basis. So the structure has been scrupulously set up to try to avoid those perceptions. But much as you try, they linger. So the real issue is the policy-making, the adjudication, versus those other functions.

One of the ways in which we try to deal with the perception issue in the context of the structure we currently have is that we have a choice at the commission. When a matter comes forward and is being investigated, it can be brought to the commission for adjudication or it can go to court under section 122. There is a third option, which is to take it to Superior Court. That's an option we don't normally use, but it is a third option under the legislation. So there are three choices.

The issue is not so simple, I think, as saying, "Should we take everything to court or should we continue to have the ability to make that choice?" Even the report by Mr Osborne is very interesting in that they attempt to delineate. I don't have the report in front of me, but at one point in the report early on, they say, "We're not suggesting that the commission not deal with any regulatory issues any more in a regulatory adjudicative tribunal context." There are some things that everyone we spoke to agreed the commission does very well. They are the regulatory matters, the takeover bid proceedings, the transaction-related matters, as they called them. So I don't think the issue is as simple as saying, "Let's just take away the adjudicative function altogether." It may be that there is an answer, a kernel of an answer, in there that that dividing line has to be more clearly articulated.

As a commission, we do struggle with that, and decisions are made all the time as to whether we'll go to court on a matter or whether we will in fact pursue it before the commission. There are many, many cases that we do take to court, as you've indicated, Mr O'Toole. So we bring a lot of proceedings to the tribunal but we equally bring a lot of proceedings to court. They tend to

be the kind of cases where there is going to be a lot of cross-examination, the consequences are going to be significant, or we're looking for jail time.

Mr O'Toole: How much time is left, Chair?

The Chair: About a minute.

Mr O'Toole: Mr Barrett, did you want to ask a quick question?

Mr Toby Barrett (Haldimand-Norfolk-Brant): Just very briefly, Mr Crawford, you make a point of examining the various models for structure, for regulation in the provinces, and you distinguish between a national regulator and a single regulator in the sense that you favour a single regulator. What distinction do you make or why do you not use the term "national" regulator, which I assume would reside in Ottawa or Montreal, perhaps?

Mr Crawford: Ideally, one securities regulator would exist in Canada, with a strong regional base. Ideally, it would be created by legislative activity in both the federal government and the provinces and territories. That's the ideal situation. I guess you'd call that national.

In today's context, you'd think that the federal government might give this leadership and move forward. It's unlikely, in my view. You do have the possibility that the provinces, acting together by delegating to one regulator, could become one, as they are nine, 10 or 11 today, and have a single regulator that could be effective. That's not as ideal. But to me it's so important to have one regulator in Canada that if it's possible to get agreement with Alberta, we should move forward with it even if we don't have agreement with all the provinces. Ultimately, if two or three provinces will come forward, the feds will get onside. But they're not going to do the leadership.

The Chair: To the NDP and Mr Prue.

Mr Michael Prue (Beaches-East York): I have two lines of questioning. I'll try to do them in six minutes each. The first one has to do with the number of prosecutions, the amount of money that is being spent by the OSC and other related bodies on prosecuting criminal and illegal wrongdoing within the system. Do you think it's adequate?

Mr Crawford: I have been of the view historically that we have not been active enough in enforcement, and I'm not just talking about Ontario; I'm talking about federally and I'm talking about all the provinces. I believe, with the establishment federally of a special unit of the RCMP to work with the provinces and with the provinces taking a more active role, that we are moving to the point where it could be adequate.

Mr Prue: So what you're saying is it hasn't been but it could be. The reason I'm asking is that a deputant yesterday gave us a lot of facts and figures—which I'm going to have researched, but let's take it for a minute that they're right—that Ontario spends about 17% of its budget on prosecutions and investigations, and states in the United States—they gave an example of 10 of them—run anywhere between 30% and 70% that they spend. We seem to spend a minute fraction. Then also, the statistics that she gave show that we actually prosecute far fewer people in this country—maybe we're more honest, but I somehow doubt it—than they do in the United States as a result. Would you comment on that?

Mr Crawford: I guess I can make two or three comments. Until the last year or two, the SEC has been dramatically underfunded and underpaid. We Canadians tend to compare where we are in the world with reference to where the United States is. I don't think we have to take a backward position or feel in any way negative or inferior in terms of our securities laws, in terms of many things in our society.

0940

No doubt the most effective prosecution, rightly or wrongly, in the US these days is coming out of the state Attorneys General, particularly in New York state.

Are we doing enough? I don't know. I think it's interesting that for the first time in a long time we have the RCMP, as a result of this new unit being set up, investigating Nortel. I think that's a very major initiative. Should we be doing more?

One of the problems, to be frank with you, with the CSA, the Canadian Securities Administrators, is that a lot of things they do require agreement. We don't have one regulator, one official body with the accountability to make a decision, therefore I get frustrated at times because it's hard to move quickly. Maybe people shouldn't move more quickly.

I wouldn't disagree with you on the whole that we could be doing more, and hopefully we're moving in that direction.

Mr Prue: The reason I asked that is that we were given statistics yesterday by Mr Brown that there is about—what did he say?—one case per day uncovered in securities in Ontario where somebody has done something illegal, wrong, shady or—I don't know what other word to use. We see the numbers of prosecutions that actually take place are far lower than that. Although it's uncovered, and maybe some of it is fairly minor, they don't seem to lead anywhere. There are huge examples: Bre-X doesn't lead anywhere; Hollinger leads nowhere. All of these cases over the years lead nowhere. Is this carte blanche in Ontario to allow people to defraud?

Mr Crawford: Gosh, it's hard for me to answer that, sir, without a lot more background. It's not something I've studied. To be frank, I was a bit disappointed that the Hollinger thing was brought to task in the United States but not in Canada some years before, but that's another matter.

Mr Prue: Perhaps we'll ask others on that later. I want to get into the other issue, which is the current structure: You made no recommendations at all. I find that kind of strange.

Mr Crawford: Don't you guys make all kinds of recommendations that are no recommendations?

Mr Prue: Well, I don't know. The Osborne report: When did you see, or have you ever seen, the Osborne report?

Mr Crawford: I have not seen it.

Mr Prue: No discussions took place among your 50 meetings about what he was saying or what he might potentially say?

Mr Crawford: Osborne?

Mr Prue: Yes.

Mr Crawford: I think the Osborne group was appointed as a result of our recommendations, where we said it should be looked at further.

Mr Prue: In his report, on pages 32 through 34, he is unequivocal, saying you cannot do anything but separate the enforcement function from the adjudicative function, and in fact, under no circumstances should it be left that way. Would you have any comment, after the fact, on his statement?

Mr Crawford: Mr Osborne is a man I have great respect for.

Mr Prue: Do you believe that the system, as it is currently operating, works efficiently, effectively and is seen as fair?

Mr Crawford: I was concerned—this was early on in our committee—the structure Susan outlined earlier was not well known, and I thought it should be made clear how the OSC operated, on its Web site and otherwise available, in terms of separating the investigation and enforcement from the judicial. It is my understanding that the commission had already started doing that and have taken further steps to do it.

Your question is, is it fair? Perception tends to be the reality. I'm not going to lose any sleep, certainly, if this committee makes a recommendation in agreement with the Osborne committee.

Mr Prue: OK, but I still want to go back to your perception. You've been there. You wrote a report. You've been around the scene for years.

Mr Crawford: My perception is gained from—a lot of lawyers have been involved in actually litigating involving the OSC. They have developed, some of them at least—and some of them are very resourceful, good lawyers—the perception or feeling that, "Well, it's supposed to be an independent group, but perception-wise, it's hard to convince my client that they are independent." I have not had that experience, but certainly among the public there's no question, as we said in our report, that there is that perception, and I think Mr Brown agreed with that.

Mr Prue: Do I still have time?

The Chair: About three minutes.

Mr Prue: Oh, my goodness, I've got lots of time.

I'd like to go back, then, to the issue about potential wrongdoing within the securities and the Ontario Securities Commission. I acknowledge that there are millions of transactions, maybe tens of millions of transactions, every day and that people are going to, if they can make a profit by scamming or—how widespread would you think fraud is? A couple are uncovered, or at least one, every day. One per trading day is usually uncovered.

Mr Crawford: I didn't hear that. Whether they were fraud or complaints, I'm not sure. You'd have to help me here.

Mr Prue: Well, there were a lot more complaints than that. We understand from one of the people that there were, in 2003, 679 SEC cases; 599 in 2002. The number of complaints—

Mr Crawford: This is in Ontario?

Mr Prue: This is in Ontario. Again, I have not verified these. This was another deputant yesterday.

Mr Crawford: I don't know, for example, how many registered reps there are in Ontario—these are salespeople acting for the securities firms—but there are a lot of them. Human nature being what it is, it would be too much—not too much, but difficult—to expect, hard to expect, that you wouldn't have some problems at times. I read the US literature a lot. We tend to just look at the big cases we see down there, but the paper is full of cases all the time of scams etc. The fact that they're not doing a good job doesn't mean that we are doing a good job. Can we do more? Sure, we can do more.

Mr Prue: So if you were to come here with a single recommendation—you made five of them. One of them is, and that's why I'm going back to page 7, "We … urge the standing committee to recommend that the government of Ontario reintroduce and proclaim in force the amendments in Bill 41 relating to fraud, market manipulation and civil liability for secondary market disclosure. Investor protection is a cornerstone of securities regulation. Introducing a regime of statutory civil liability for continuous disclosure will provide significant additional protections for investors."

From what I read, very briefly, that seems to me to be the cornerstone of what needs to be done. Would you agree?

Mr Crawford: I agree.

Mr Prue: I mean, more important than anything else.

Mr Crawford: If this committee does anything, it should support that.

Mr Prue: Thank you very much.

The Chair: Now we'll move to the government and Mr Berardinetti.

0950

Mr Lorenzo Berardinetti (Scarborough Southwest): Thank you, Mr Chairman. I'll share my time with the other members of the committee.

Thank you for coming today, Mr Crawford. I had one question, and it came up quite a bit yesterday, as well: the issue of other jurisdictions perhaps resisting or not wanting to form one united regulator. Do you have any comments on that? For example, let's say the oil people out in Alberta or perhaps the Quebec jurisdiction might not want to be part of a new system.

Mr Crawford: My first comment would be that we shouldn't expect that we're going to be able to go ahead with agreement with all the provinces. Quebec will not be there, no matter if the others are there. However, it might ultimately be there and not want to become a bit of a backwater.

The key to all this, I think, is Alberta, to be frank with you. The other provinces are important, no question, but if Alberta and Ontario say we're going to have one commission, I think the thing will come together over time. Ontario is by far the dominant home of the capital

markets in Canada, and Alberta would be number two. British Columbia and Québec are important; I don't want to minimize them.

It's not a legal issue, as far as I'm concerned; it's a public policy issue. Have you ever heard of an administrator or a public servant or a committee member who wanted to do away with his job? It's got to be done at your level, the political public policy level. That means it's got to be done at that level, and it's got to be done by Ontario bending over backwards to accommodate the views of the other provinces, because we are the capital markets, no matter how much we do to accommodate Alberta or Québec or British Columbia, or even Nova Scotia. It's going to be here, in any event.

So we can really afford to be very committed to having local authorities and strengthening the local position and bending over backwards to make this happen. Will it happen? I hope so. Sorry I talked so long.

Mr Berardinetti: That's a very good answer. Thank you. I'll pass my time over to Ms Matthews.

Ms Deborah Matthews (London North Centre): Thank you very much. It's a pleasure to meet you. I do want to say thank you for providing this committee and the Legislature with such a strong foundation from which we can begin our deliberations. I appreciate the work you and your committee have done on that.

There are so many things I would like to pursue with you, but I'm going to focus my question on this single securities regulator. As has been said earlier, there has been very strong support for the idea that we move forward with that. My question to you is, what do you think we, as a committee, should do to further that cause?

Mr Crawford: The minimum you can do is to recommend to the government in Ontario, through the minister and the Premier and others, that they do everything feasible to move forward with a single regulator. That's the minimum.

What you can do apart from that, on your own as individuals or otherwise, depends on your contacts and everything. I don't think even the Alberta business community is opposed to one regulator, at least the major players in it. So if you can have any influence through those environments or your political friends in Alberta, or in any province, by all means, do so, if you feel that way.

Ms Matthews: I'm going to sneak in a second question. What do you see as the major drawback to the passport system?

Mr Crawford: The major drawback to the passport system is twofold, at least.

One is it doesn't deal with the formulation of policy in a hurry and the development of policy to respond to issues that are current. The CSA would continue—it's almost dysfunctional, to be frank.

The other one is enforcement. It doesn't deal with, in any way or level, how you go about enforcing these various securities laws.

And, of course, there's the international position. The international position is important because money coming to Canada for our capital markets is important to us.

But, fundamentally, it's a dysfunctional inability to move quickly to deal with changes in the environment. I mean, we don't do a bad job. You may have read in the paper yesterday or today about the SEC starting to blow the whistle on mutual funds that make special deals with brokers to distribute their products. Well, we did that here in Ontario several years ago, so we don't necessarily have to take a back seat to anybody.

But the passport system, what does it do that we're not already doing? That's what you'll find out.

The Chair: Mr Delaney?

Mr Bob Delaney (Mississauga West): Thank you very much. I'd like to follow up on some of the questions you have been asked.

Assuming Ontario agrees on the need for a single securities regulator and that the government of Ontario moves decisively on all of the areas within its jurisdiction—as you put it a few moments ago, doing "everything feasible to move forward"—where, outside the jurisdiction of the government of Ontario, in your opinion, would the next bottleneck lie on the road to implementing a single securities regulator in Canada?

Mr Crawford: Well, if I understand your question correctly, I would say Alberta and the federal government.

Mr Delaney: Could you just elaborate on that a bit?

Mr Crawford: There was a time when the people in Alberta had an inferiority complex toward Ontario. Now they don't; they have a superiority complex—maybe. They don't like us in Toronto, necessarily. That's why, when I go out there, I say I'm a poor Nova Scotian.

It takes a lot of tact and bending over backwards. With some justification, they don't like the feds, the national energy program. So they're perhaps logically suspicious of what we're up to, trying to grab all the capital markets and take them away from Alberta and other provinces too. That's why I think we really have to bend over backwards. I have said publicly in a speech I made some time ago that the first securities act for one regulator will be the Alberta act. Technical lawyers have a great problem with that, but the reality is it's no problem at all in terms of the big policy picture, things like that.

Mr Delaney: Earlier, you stated that Canada has a higher standard of corporate governance than they do in the US. The final report recommends in numerous areas that Canadian practices either be harmonized with or simply adopt US practices and procedures, be that in GAAP or other areas. Could you explain, then, how the higher standard of corporate governance you mentioned would be maintained, when more and more of our practices and procedures find their origin in the USA?

Mr Crawford: The accounting world—you were referring to GAAP, was it?

Mr Delaney: Among others.

Mr Crawford: If we could back up a bit—I guess we're running out of time, Mr Chairman. I've been a director over the years of several US companies. I'm currently a director of one major US public company. I was on an advisory board of US and Canadian rep-

resentatives, but mostly former US CEOs. I was on the Dey committee that looked at corporate governance for the Toronto Stock Exchange. It's perfectly clear to me that, historically, much more so in the US than in Canada, the CEO was the monarch. To be accountable to a board, their attitude is, "I have to be chairman, or I won't take the job of CEO." Some of the things that we were doing as a result of the Dey report or otherwise were unheard of down there.

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Now, the dramatic changes since the developments in Sarbanes-Oxley and some things—I guess Mr Rosen will tell you later today, if he's here, that we should adopt US GAAP, and we say in our report that Canadian companies that are subject to US GAAP should be able to use it in lieu of Canadian GAAP. But on the whole, the international accounting body, the Canadian accounting body and the US accounting body are working toward a uniform accounting system, which I think would be ideal.

I think that, on the whole, an accounting system based on principles is better than an accounting system based on detailed rules, which is what they have in the US. I think they've come to realize now, as a result of Enron and other cases, that maybe there's something to be said for an accounting system based on principles. We're sort of typical. We're halfway in between rules and principles. The international accounting standards body based in, I think, the UK is more principles, but we're moving together. But don't apologize for Canada.

The Chair: Thank you very much for your presentation this morning.

JOE KILLORAN

The Chair: I call on Joe Killoran. Good morning. You have 10 minutes for your presentation.

Mr Joe Killoran: I'll start my watch now.

The Chair: You may allow time for questions, if you desire.

Mr Killoran: Fine. My 10 minutes—I'll start; 600 seconds.

My name is Joe Killoran. I'm an educator and consumer/investor advocate, with an MBA from Ivey in 1979, as you'll see on page 3 of my presentation.

Full transparency and disclosure: I've known Debbie Matthews since we were kids. I used to date her older sister, Shelley, and I worked with Debbie's ex-husband in the brokerage business.

Mr Rosario Marchese (Trinity-Spadina): Too close for comfort.

Mr Killoran: Yes, but everybody from London, Ontario, is related, OK?

Interjections.

The Chair: Order.

Mr Marchese: It's too incestuous for me.

Mr Killoran: OK, my presentation. This is my wife's uncle—you all know him—Adam Zimmerman: "Who's in charge here, anyway?" That's the title. Who's in charge of consumer investor financial literacy education?

The Chair: They've asked me if you could please sit. They can't pick you up on the mike. Would you please be seated?

Mr Killoran: I'm a teacher.

The Chair: Fine. The proceedings are also televised. It helps for that as well.

Mr Killoran: Who's in charge of the education and financial literacy of consumer investors in this province? Is it the Ministry of Education? Is it the Minister of Finance? We don't have financial literacy as core education, JK to grade 12.

I'm a teacher. OK. There are nine of you now. How many of you can use a programmable business calculator to calculate present/future value, mortgage interest, lease payments? Hands up. How many of you panellists can do that? This is a poll. That is an introductory item in third-year corporate finance at Laurier and York, where I've taught.

We live in a distinct society, yes, a privileged society where people don't learn financial literacy. They are the sheeple food chain of our financial services industry. They're uneducated and unknowing, and we've got to have a revolution to change this now.

Page 2: There's the Hippocratic oath. We don't have that in our financial services industry. As Debbie knows, my esteemed father-in-law, Dr Jim Ballantyne, is an ophthalmologist. He's retired. He's 80 years of age, professor emeritus from Western med school and a past president of the College of Physicians and Surgeons of Ontario. We don't have a Hippocratic oath in our financial services industry and, Deb, I'm sure you would say he epitomizes it in medicine.

You see my CV. You also see a note from Eliot Spitzer, and I'll get to that later.

Ladies and gentlemen, I was trained by Merrill Lynch on Wall Street, March 1984. The 16th floor of the Roosevelt Hotel was my room, the safest room on Wall Street. Why? Presidential wannabe Gary Hart's suite was down the hall. The secret service were looking after him. Remember the name of the boat that Gary Hart got caught on? What's the name of it?

Ms Matthews: Monkey Business.

Mr Killoran: That's right. I guess we're here to look at the monkey business of the OSC and, are they guilty of gross malfeasance failures?

Down at the very bottom, page 3, Ed Waitzer: That was on August 28, 1997. I first met Waitzer in 1994, when he became OSC chairman. Folks, there's no democracy in capitalism. Consumer investors weren't represented.

Page 4: I was identified with learning disabilities as a child in 1958—very severe reading comprehension disability. I had to learn tricks to survive. I got an MBA with it, 1977-79, at Ivey. When I got a computer in the early 1990s and taught myself, I could communicate; I could finally do things. But I've used those tricks, as you'll see through here.

Page 5: Minimum education of our financial advisers; that's where we failed. We get the Canadian securities

course by correspondence. Your doctor has to go to med school for at least four years and an undergraduate degree. He knows the body. There's no history of investing that these guys really learn.

Page 6: The OSC is guilty of gross malfeasance in the area of perpetuating asymmetric information. When they brokered the deal for Dundee to buy Fortune Financial, the money was put in escrow that they paid for David Singh for four years. Nobody knew about it, nobody outside the province. They had Fortune offices across the country. They didn't get a registered letter saying this.

This is me: point-of-sale disclosure. It's 10 years old. I first showed it to Adam Zimmerman 10 years ago last Thursday at Georgian Bay. That was the day they closed the doors of Confederation Life that he was trying to life-save. Folks, we have to educate people: one page; point of sale. The thesis on this is interactive. Fill in the blanks between the adviser and the seller. Then you learn. If I gave you a preprinted document to buy a new car, would you really look at it? It's filled in. You just sign. You don't look at it. That's the way we educate. Adult beginning education and financial literacy: three minutes, 50 seconds.

Page 8: This is from the elder abuse. Seniors are sold deferred-sales-charge mutual funds. You see the RBC DS manual here and it says "elderly clients buying with DSC."

On page 20 you will see my demi-plus billionaire cousin Arthur Labatt say that mutual funds are sold, not purchased. We've got problems.

Reverse mortgages: 50% of them are collapsed within the first five years, as soon as the person has to be moved out to a care facility. That's after all the commissions, all the interest rates, all the penalties and all the legal set-up fees. It isn't such a good product. Maybe they shouldn't have taken it in the first place. That's elder abuse. If that were an operation that we had to reverse, all hell would break loose, and I'm sorry for swearing.

Tied advice-tied sale commissions on page 11: The trailer fee commission is the most sophisticated form of tied advice-tied sale, far more egregious than the practice of tied selling at the banks that is now banned.

Page 10: Why do we let people sell proprietary funds? The pharmacist dispenses drugs. He's got five years of university education.

OK, folks, this is the real meat and potatoes: All of our securities commissions are guilty of gross malfeasance for allowing the rebate commissions in 1999, when an adviser switches somebody to a proprietary fund.

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Assante's business plans, Loring Ward, every adviser, once they switched their book of business, got bonus shares in Assante when—40% of their client base. That's far more egregious than mutual fund free trips.

Mr Crawford, we didn't kill the practice in this country. Extra sales incentives are still going on. This is for you guys.

The founding chairman of Advocis: This is out of the courts in Saskatchewan. This is really serious stuff. This package and other things have gone to Eliot Spitzer. The Saskatchewan Securities Commission has enacted since February—Spitzer got all this yesterday. We'll see who acts quicker on this, because there's a US component.

Gentlemen, it's time to kill proprietary funds. In here, for the last 10 years of my life—and Debbie knows. Ivey has written cases about me: Joe Killoran, investor advocate.

I tried to get Trimark to live and lead by example with shareholder proposals in 1997, 1998, 1999 and 2000, an end around the OSC for its failures.

I asked for funding from the OSC so I could get independent research done on my point-of-sale document. Did Tommy Hockin tell you yesterday that he actually seeded my point-of-sale document with a $250 honorarium 10 years ago? Then, in 1995 he told me that they got exceptional focus group results on it. He never gave it and he never told anybody. He speaks like an angel but lives like a man. By the way, Tommy Hockin's parents played bridge with my father. He's another Londoner—London mafia.

Looking forward: There's my press release offering to give my stuff to the governments of Ontario and Canada—point-of-sale documents, creativity. In here you will see my communications with the Honourable Janet Ecker, as the Minister of Education, in the fall of 2001. I need help to educate adults, Janet. She became Minister of Finance.

Then a paper came out rethinking point-of-sale disclosure amongst mutual funds. There was no mention of my point-of-sale document. Janet Ecker had to practise plagiarism as Minister of Education. What do you call it? There's no mention of my thing in their 55-page document.

Folks, we have culture problems. Looking on page 20: You have to ask some tough questions. I expect this committee to go in areas and say, "Is the OSC guilty of gross malfeasance?" They are when it comes to investor education. I've been there for 10 years saying we need point-of-sale; I've been there.

We teach Jack Welch in our business schools: boundaryless behaviour for ideas; speed; stretch; continuous improvements; six sigma. We're not practising that on behalf of consumer investors.

Ask the question, if they're guilty of gross malfeasance: We didn't let the Koebel brothers fix the Walkerton water system. Whom are we going to allow to fix the problems in this country?

Look at every committee the OSC has set up. You won't see democracy and capitalism or consumer investor representation. You will not see it. All of my work—point-of-sale-tied selling—is up for a prestigious international award in economics. It will be recognized outside of Canada before it's recognized inside Canada. The Honourable Jim Peterson knows that's going to hurt us on a global scale. I've tried; I've genuinely and sincerely tried. The OSC is guilty of gross malfeasance.

The Chair: Thank you for your presentation.

Mr Killoran: I'm going to give these documents to you to photocopy for people if they want them, but I would like these back.

The Chair: All committee members will get a copy and we will return the originals.

Mr Killoran: I would thank you for that. I have one final comment. In there you have something—read this book, Somebodies and Nobodies: Overcoming the Abuse of Rank. People want dignity. Your constituents want dignity. The people of this province want dignity. They want to be able to fund their longer life expectancy themselves.

The Chair: Thank you.

GLORIA HUTTON

The Chair: I would call on Gloria Hutton. Good morning. You have 10 minutes for your presentation. You may allow time within that 10 minutes for questioning, if you desire. I would ask you both to identify yourselves for the purposes of Hansard.

Ms Gloria Hutton: My name is Gloria Hutton.

Mr Kevin Hutton: I'm Kevin Hutton, her son.

Ms Hutton: I would like to thank the committee for the opportunity to appear here today. As I told you, my name is Gloria Hutton. I am an Ontario investor who has lost faith in our investment industry and its regulatory authorities overseen by the Ontario Securities Commission. These authorities include the Investment Dealers Association of Canada, IDA, and the Canadian Investor Protection Fund, CIPF.

More than four years ago my husband, Ron, and I saw our life savings disappear in a multi-million dollar fraud perpetrated by a licensed investment broker whom we thought to be a family friend. He was subsequently convicted of fraud and jailed. Our loss included a $500,000 locked-in pension, which vanished from an account held in trust by the Toronto-Dominion Bank. It was removed without proper authorization or documentation and deposited into a worthless company operated by the licensed broker. The broker, we later learned, had an administration arrangement and regular dealings with the bank.

In its investigation, the IDA found the bank procedures wanting but lacked authority to act, other than to lift the broker's licence and to levy a substantial fine. We believe the fine remains unpaid.

An early review of our case was misrepresented by the IDA, and an initial claim of loss by Ron and me was arbitrarily rejected by the CIPF. That authority and certain board members dismissed us as victims of our own stupidity.

After seeking legal support, we were eventually reimbursed by the CIPF for the base value of the pension, more than two years after it was lost. But we were required to waive any right to legal action against the IDA, the CIPF or the bank. Reimbursement by the CIPF was written on a cheque from the TD Bank.

Lacking any savings to secure our future in retirement, we found it necessary to sign away our legal rights, under duress. Meanwhile, the CIPF asserted that it had been unnecessary for us to hire a lawyer to win our claim.

I will not burden you with the ordeal of additional painful dealings with the Law Society of Upper Canada and the association of chartered accountants of Canada. Those matters are for another day. But I think you can appreciate that we were sadly coming to the conclusion that rather than protecting the investor, Ontario's investment industry seemed to have a greater interest in protecting itself.

We wanted answers. Specifically, how was our pension, held in trust by the TD Bank, removed without proper authorization and documentation? We posed that question to the Ontario banking Ombudsman, later the Canadian Ombudsman for Banking Services and Investment. Following initial inquiries in which the bank claimed itself to be a victim of the broker's fraud, the Ombudsman said he could not pursue the matter. He cited our agreement with the CIPF not to hold the bank legally accountable. We said we were simply seeking an answer to our question, but he would not move further. Subsequent appeals to the Ontario Securities Commission, the office of the superintendent of financial institutions and the Financial Consumer Agency of Canada were rejected as being beyond their mandates.

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In the early days of our ordeal, we learned that the OSC had conducted an audit of the IDA operations in 1999 and found a number of its practices wanting. Curious to know whether flawed oversight by the IDA might have contributed to our investment losses, we sought a copy of the audit. We were told by the OSC that we could not have it because it was a confidential document. We went to Ontario's commissioner of freedom of information and personal privacy. A number of times the commissioner's office has ruled that the OSC must release the audit to us, only to be stonewalled at the last minute. More recently, the OSC won a stay of the commissioner's ruling, pending a judicial review, which has yet to be heard. Meanwhile, the time for potential legal action, already a debatable recourse, is running out.

The OSC, which claims to have investors' interests at the top of its priorities, insists that release of the document would jeopardize its ability to draw candid responses to questions from staff of the IDA and civil servants. We dismiss this as a weak attempt by the OSC to shield the IDA and itself from public scrutiny. We argue that staff and civil servants have a professional obligation to deal forthrightly with matters adversely affecting investors' interests and confidence.

As the OSC pleads the need for secrecy, a similar audit of the IDA in British Columbia has been made public, which raises the question, if the OSC morphs into a national securities agency, will the interests of Canadian investors be submerged by other financial concerns, or will transparency in the Canadian investment industry become a new way of doing business?

I greatly appreciate the time you have allotted to me to make our experience known to you. No words, however, can adequately describe the enormous trauma all of this

has caused our family. The last four years have been hell, not made more easy by regulatory agencies supposedly committed to our protection.

I have brought with me today a file on the experience of my husband and me over the past four and a half years. I will leave it with you for detailed study and reflection by you and your research staff. We would be pleased to co-operate with your staff, should additional information be required. Perhaps, with your powers, you can help Ron and me find out how, and under what circumstances, our pension vanished from the TD Bank.

I would ask that you consider whether this is the way you want Ontario's investment industry to work and whether the OSC cares sufficiently about individual investors to act more rigorously and openly on their behalf. If the OSC was indeed discharging its claimed commitment to protect investors, I wouldn't be here today. Therefore I would ask you to establish investor protection as a fundamental priority within Ontario's investment industry, which is certainly not the case at present; direct the OSC to released the IDA audit to us; investigate whether administrative arrangements between banks and investment brokers place investors at risk; and if Ontario is to participate in a national regulatory program, require that investor protection receive the attention it deserves.

On the basis of our experience, an independent organization with the authority of law is needed to monitor the industry and order financial redress where investors are defrauded or victimized by corporate negligence. In other words, I would ask you to initiate changes to ensure that regulators fulfill their stated objective of protecting the interests of investors in this province.

Thank you for your time.

The Chair: Thank you. Any material you would leave, we would photocopy and ensure every committee member has that.

Ms Hutton: I would appreciate that.

The Chair: Your time has expired. We don't have time for questioning. Thank you for appearing before the committee.

DEMOCRACY WATCH

The Chair: Committee members, now we have a teleconference with Democracy Watch. Good morning.

Mr Duff Conacher: Good morning.

The Chair: Is this Mr Duff Cochrane?

Mr Conacher: It's Conacher.

The Chair: Conacher. Oh, I'm sorry. You have 20 minutes for your presentation.

Mr Conacher: Thank you very much for the invitation to appear before the standing committee on finance and economic affairs and for facilitating my presentation by teleconference. I wanted to check, first, whether every committee member has received the submission I forwarded to the clerk, as what I will be doing is simply taking you through that submission briefly and then opening it up for questions. Has that been received?

The Chair: Yes, they have it.

Mr Conacher: It has. Thank you very much.

The proposal that Democracy Watch is placing before the committee today is for the creation of an individual investor association using the method that has been used successfully in the US to create citizen groups that will watch over various industry sectors.

The proposal is supported by a coalition entitled the Corporate Responsibility Coalition, which is made up of more than 30 organizations, representing more than three million Canadians in the total membership of the groups from across Canada in the coalition.

The creation of such a group would be based on using the method, as I mentioned, that has been used in the US to create citizen watchdog groups. The groups that have been created in the US are called citizen utility boards, and they are created to advocate for fair telephone, electric, gas and water rates and sensible policies before regulators, the government and the courts on behalf of their members, who are individual ratepayers.

How do the ratepayers join? This is the key to the method of creating such watchdog groups. The government requires the utilities to enclose a one-page pamphlet periodically in the utility companies' billing envelopes. The pamphlet informs customers about the organization and invites them to join, for an annual membership fee.

By requiring the utilities to enclose the pamphlet, allowing the pamphlet to piggyback on the envelopes the utilities are already sending out each month to their customers, the government gives the customers a very low-cost and effective method of everyone being reached and everyone having an easily accessible opportunity to band together into a watchdog group that is funded only by individual ratepayers, is directed only by individual ratepayers, and serves only the interests of individual ratepayers.

Of course, more than utilities send out mass mailings to customers. So this method can be used to form watchdog groups over many different industry sectors wherever the businesses mass mail the customers or have some other mass point of contact with customers.

This method can be used in the investment industry because both publicly traded companies and mutual fund companies are required to send out mailings to their investors. So those mailings could include a one-page pamphlet that would invite these individual shareholders across Canada to join watchdog groups that, again, would be funded only by them, directed only by them and serve only their interests.

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It's important to note that this group can be created at no cost to the Ontario government or any other government in Canada and no cost to the investment industry at all, because the government can loan the group the funds to print the first pamphlet, and there are no extra costs for businesses to insert the pamphlet and no extra postage costs either. So for absolutely no cost to government or the investment industry, investors can be given an opportunity to band together into a broad-based, well-resourced group that can represent their interests.

The reasons for establishing such an organization are many. First of all, the investment marketplace favours sellers in many ways, mainly because consumers are not organized to protect their interests. The cost of individual consumers protecting their interests is prohibitive in many cases, so businesses in the sector are easily able to take advantage of their market power in terms of their treatment of customers. As well, enforcement agencies, as has been revealed yesterday, either have inadequate powers and/or resources and/or penalties are too low, or the enforcement agencies have dual roles that create conflicts of interest and hamper enforcement.

Compounding these ongoing problems and barriers to individual investors holding the investment industry accountable and ensuring fair service is that the customers pay all of the costs of the investment industry's lobbying efforts, all of their lawyers' costs, and all of their advertisements. In other words, customers pay for all the costs of the investment industry forwarding its own agenda—not the customers' agenda but the industry's agenda. The industry has an enormous ability to advocate its interests and protect its interests while customers are left on their own with nowhere to call and very high barriers to banding together into organizations that can represent their interests. That is why, as a result of these barriers and despite widespread, ongoing problems with the investment industry, there are only very small, very resource-limited groups, some of which you heard from yesterday, some of which you're going to hear from today, that have been created and are dedicated to representing and advocating for individual investors.

If such a group was created using the US method, it would give investors an easy way to band their resources together to establish a broad-based, well-resourced group that would represent their interests and balance the marketplace. This group could play a great role in educating investors, a role that sellers in the industry and governments cannot play simply because there is deep consumer skepticism about educational materials created by sellers and by governments. This deep consumer skepticism exists for logical reasons because consumers know that sellers have a great incentive to not give them full information about a product or service in order to try and close a sale. As well, they know that governments are greatly influenced by industry lobbyists and, as many polls show, there is not a great trust of governments across Canada now because of past behaviour by politicians and other public officials. So this group would be able to provide the role of educating investors, with investors knowing that the group was only serving their interests, was only funded by them and was only directed by them, and so would be giving them the straight goods on the various products and services and helping them shop around and protect themselves.

As well, governments cannot make decisions in the public interest when consumers are not effectively represented in policy-making processes. Again, because there are only very small groups that exist that are dedicated to representing investors, the government is not hearing the full picture from the consumer side and instead is getting a skewed picture based on the overwhelming resources that the industry lobbyists have.

Another reason to create such an organization is that Canadians want such an association created, using the method of the pamphlets being sent out. I won't go through all the results of the survey that was conducted by Environics Research Group, a survey of 2,000 individual Canadians using personal interviews, but the findings show overwhelmingly that Canadians want this group and that the banking and financial services area is the number one area in which Canadians, and also Ontarians, in terms of the segment of Ontarians who were surveyed for this survey—both the national results and the Ontario results show that financial services is the number one area in which consumers want such a group created. As well, a survey of citizen groups that was undertaken by Democracy Watch resulted in, again, overwhelming support for this method being used to create a citizen watchdog group that would represent individual investors.

What are the next steps to creating such an association? The next steps are that the government, using a model law that Democracy Watch has, which is based on US experience, would draft a bill, introduce it and pass it in Ontario. The law would set out the structure and operations bylaw of the association and would give the association the right to have the pamphlet enclosed one to two times each year in the mailings of publicly traded companies and mutual fund companies, with the mailings only going to individual investors, not to institutional investors, because institutional investors, given that they are large companies, already have the resources they need to protect their interests in the marketplace.

Then the government would provide either a loan or a grant to the group to pay the cost of printing the first pamphlet and appoint an interim board to direct the group. The way this has worked in the US is that once a threshold has been crossed, in terms of the number of members joining the group, the interim board then conducts the nomination and election process for the first board of directors. Then the group repays the government loan for printing the first pamphlet, if the government has made that loan. The government could also provide a grant, if it wanted to further facilitate setting up the group. Then the group goes on as a broad-based, well-resourced, self-sustaining organization into the future, paying for all of its operations.

Democracy Watch's projection is that the group would likely have 400,000 members and, at $30 each member, a $12-million budget, which would provide, finally, adequate resources to counter the power of the industry lobby, to help people if they have a problem and need to go to court or are dealing with the regulators, and to help them comparative shop and shop around to make sure that they are asking all the questions they need to ask of financial advisers, brokers and others in the industry to ensure their interests are being protected and they are being treated fairly.

Again, Democracy Watch and the Corporate Responsibility Coalition is appealing to the Ontario government to balance the marketplace. At no cost to the government and no cost to the industry, give consumers the resources they need to protect themselves and to band together through this method in an organization that can balance the marketplace and represent individual investors and give them some market power to counter the market power that the investment industry and all the sellers now have.

I will leave it at that. I welcome any questions from any members of the committee.

The Chair: Thank you for your presentation. We have about two minutes per party for questioning. We'll begin this round with the NDP.

Mr Prue: This is an American example you've given. In how many states is this taking place?

Mr Conacher: This has taken place in four states in the US.

Mr Prue: Which four are they?

Mr Conacher: Illinois, Wisconsin, Oregon and California.

Mr Prue: All of them have passed a law and all of them give the money for the first pamphlet—they all do the same thing?

Mr Conacher: In terms of what the government has done?

Mr Prue: Yes.

Mr Conacher: It has differed in different states, whether it's been a grant or a loan or whether the group has obtained a loan from a financial institution in order to print the first pamphlet.

Mr Prue: For how many years has this been going on?

Mr Conacher: Since 1979.

Mr Prue: So there must be quite a body of evidence by this point as to the effectiveness of the organizations.

Mr Conacher: Yes, very much so, and they have proven to be very effective. For example, the group in Illinois has successfully challenged unjustifiable proposed rate hikes by the utilities in the state of Illinois and has, as a result, saved the customers more than $6 billion that would have essentially been straight gouging by the utilities in Illinois if their rate hikes had gone through, but the rate hikes were turned back by the energy boards based on the advocacy of the citizen utility board.

1040

Mr Prue: Obviously you're not here, so you wouldn't have seen it, but we have had a number of people and organizations that have come forward talking about illegal activities, criminal wrongdoing, that kind of stuff, within the stock exchange in Ontario. They've been talking about the need for more enforcement. Would you generally agree with that, and how would your proposal help to better regulate and enforce the existing laws?

Mr Conacher: Definitely, more enforcement is needed, and the Osborne report shows that the dual roles of the commission raise questions about enforcement ability. The creation of such a broad-based, well-resourced individual investor association would very much help enforcement, because it would be an umbrella group where complaints about the industry would be compiled in one place and within a group that is there representing consumers, and that group would then be able to place those complaints before regulators and also before the government in terms of systemic policy changes needed. As well, the group being in existence would facilitate the development of class action lawsuits.

But generally, as well, any seller will act differently when consumers are organized, as compared to when consumers are on their own, with no place to call and very few resources to go to court or even file complaints. When you create such a group that will likely, again, have 400,000 members and a $12-million budget, you will see sellers change their behaviour, because they'll know that any customer can call that group and that they will be getting a call from that group's lawyer, as opposed to just from a customer who is own their own, who has had all their money taken from them and has no resources to fight back. So it will balance the marketplace and change the behaviour of sellers systemically, and that's why it's needed the most and that's the greatest benefit it will have.

The Chair: Now we'll move to the government and Ms Matthews.

Ms Matthews: Thank you very much for this, Duff. I think it's a really innovative idea and one that deserves a lot more investigation by the members of this committee. I know I speak not just for the people on our side but for all the members of the committee when I say that the protection of investors, especially individual investors, is clearly a core priority for us. The question is, how do we achieve that? It seems to me that this is an idea that can play an important role in that.

My question to you is, who else have you spoken to about this? Is this an idea that's gaining some interest? We've had delegations here from organizations like CARP. Have you spoken to those kinds of organizations, and what's the reaction?

Mr Conacher: I have not spoken directly with that organization. I have spoken with some of the others that are testifying in these couple of days of hearings. As I mentioned already, there are 30 organizations, part of the Corporate Responsibility Coalition, that support this proposal. As well, as is in the brief that I've submitted today, there is Canadian support for using this method. They actually want it done, and so do the members of the Corporate Responsibility Coalition, for every industry sector.

That is the support that is out there, and I would urge the Ontario government to consider using this method to create a utility watchdog group, to create an insurance watchdog group, and as well to create a health care patients' watchdog group in Ontario. Wherever there is mass mailing by business, a pamphlet can be piggy-backed in those same envelopes and can be a way of allowing the citizens to band together their resources as easily as businesses are able to band together their resources.

Again, when you have such an unlevel playing field where customers are paying for all of the advocacy that business does, you have to do something to give customers a way of banding together their own resources. This is the best method that has been developed in the world, as far as I'm concerned, from the studies that we've done.

The Chair: Now we'll move to the official opposition and Mr Barrett.

Mr Barrett: Mr Conacher, I hear what you're saying on legislation and organizational development. Consumer information is very important. I do question, in your brief, to what extent people read the annual reports or even open them up. It's one way of distributing information. Much of the mutual fund industry has their literature on shelves in banks, for example, and I wonder if the salesman, the dealer, should be encouraged to put your brochure in people's hands as they're making decisions to purchase or renew some of their—I'm using mutual funds, for example. Especially in the case of fees, people do not know what fees they're paying.

I have a brochure here from the industry, a mutual fund brochure. I picked it up in a bank. The small print on the back, and I do have difficulty reading this: "Commissions, trailing commissions," or trading commissions, "management fees and expenses all may be associated with mutual fund investments. Please"—and I can't read the rest of this. It's basically, "Please take a look at the prospectus before investing."

In your view, how many people follow that advice?

Mr Conacher: The Canadian Bankers Association did a survey about six years ago on what financial consumers were looking for, both in terms of just retail banking questions but also investment questions. They showed the highest level of concern and level of awareness by consumers that they knew they had to know more, but they didn't know who to ask. They didn't trust the sellers and they didn't quite know how to protect themselves. They had misconceptions about deposit insurance and what kinds of things it protected when you were dealing with a bank and through a bank branch. It showed very high levels of concern and awareness that people needed to know more but they didn't know how to figure it out, and they were just relying on friends.

Based on those kinds of surveys, I would say that most people are feeling quite lost. This is not something that is taught in high schools: how to invest properly, what questions to ask; it's not even taught if you get up into post-secondary education. So people are dealing with something very essential to themselves—their money—but really we educate people very poorly on how to do this.

This is the role that the group could play. You mentioned the small print in the pamphlet. What this investors' association would be able to do for all investors—again, because the pamphlet is going out to all potential investors who may want to join—is magnify that small print. Right now the seller puts the key information in small print because they want to downplay that key information. The organization would magnify the small print because it is the key information that consumers need to know, and be a place where any consumer could call. Even if they didn't join the organization, they'd at least be aware of it because they'd receive it in the mail-outs that the industry is sending, and the group would be able to magnify that small print, help people shop around and protect themselves, but also participate in policy-making and also help people complain and even go to court—again, all at no cost to the government and no cost to the industry.

The Chair: Mr Conacher, your time has expired. We appreciate your presentation this morning.

Mr Conacher: Thank you very much. If people have any further questions, they can contact me at Democracy Watch. We have several materials on our Web site under our citizen association page about this idea and how it's working in the US and how we think it should be working here in Canada. Thank you again.

The Chair: Thank you.

For the benefit of the committee, the 10:40 presentation has cancelled.

1050

DAVID YUDELMAN

The Chair: I ask that David Yudelman come forward, please. Good morning. You have 10 minutes for your presentation. You may leave time within that 10 minutes for questions, if you so desire. I would ask you to identify yourself for the purposes of our recording Hansard.

Dr David Yudelman: My name is David Yudelman. I'll mention a couple of things about myself for your benefit. I have worked for banks and financial institutions in Canada both as a staff member and as a consultant and writer. I've written speeches for various bank chairmen, such as Matt Barrett and Bill Mulholland, and for various Ontario ministers. I've worked as a consultant on the Toronto Stock Exchange. I've also written a fairly lengthy report for the federal government, giving a consumer view of Canadian financial services and suggesting ways to transform these services. My written submission, copies of which I think may already have been passed on to you, was drawn from this report, which was made public under the name The Scorpion and the Frog.

I mention my background to make two things clear. First, I'm not a specialist on the securities industry as such, although I have worked in the industry. My presentation will not focus on the fine details of securities regulation but rather on the overall relationship between consumers and financial services generally.

Secondly, I'm not here as a partisan to criticize the financial services industry on behalf of the consumer. I've worked in and for the financial services industry and I believe it provides consumer services at least as good as anywhere else in the world, and perhaps better.

I recognize the narrow boundaries of the committee mandate but I want to say at the outset that the consumer

does not distinguish between regulatory regimes. The consumer does not care whether something is under the jurisdiction of the provincial or federal government. The consumer wants solutions to problems, not jurisdictional excuses.

Those of us who know the complexity of Canada's regulatory regime may think the consumers' demands in this regard are unrealistic, but the desire for one-stop regulation is deep, and I would argue it's fundamentally a sensible argument. In the long run, it's an issue that Canadian governments in general must deal with. Therefore my aim today is to try to give you a bird's-eye view of the overall needs of the consumer in an age of increasing financial complexity.

In spite of the strength and efficiency of Canada's financial institutions, the consumer increasingly needs help. I've only been here for half an hour and I've already heard the appeals and concerns. Apparently simple decisions taken by consumers, compounded over time, can and do make an enormous difference to the financial future of Canadians. The difference between a secure, independent retirement and dependence on welfare can be very small. Compounding can work against the consumer; it doesn't always work for the consumer.

The flexibility and creativity of Canadian financial institutions mean that they can offer to the consumer a vast range of alternatives. Paradoxically, this bewildering range of options can make the consumer more vulnerable and more in need of protection than in other countries where the options are few.

Essentially I want to ask one question here today: Who protects the consumer in Ontario and in Canada?

Markets depend for their success on the belief of those participating in them. We have to believe that markets are fundamentally fair. If we free them up enough to allow widespread dishonesty and unfairness, people will go elsewhere and the markets themselves will falter.

One of the questions we asked consumers and industry respondents for The Scorpion and the Frog study was whether they believed financial institutions give consumers advice that primarily meets the needs of consumers, or whether the advice primarily meets the needs of the industry. The results were really revealing. If we exclude the neutral replies, the majority of consumers thought that the industry's advice was slanted toward the needs of the industry. But the split was only 39% to 26% in favour of cynics: 26% of consumers thought that industry advice was primarily geared to their benefit; the industry thought the reverse. It thought that its advice was primarily altruistic and focused on the needs of the consumer. But the split here was even smaller, with 41% of the industry saying the advice was altruistic and 36% saying that in fact the advice the industry gave was geared to the needs of the industry. There's nothing really surprising in that except perhaps for the fairly even balance between the views of the cynics and the optimists on both sides.

Then we asked the same question to a group of government regulators, as well as public servants working within government financial services departments. Here the results were astonishingly different. No less than 60% of the regulator group thought the financial institutions give consumers advice that primarily fits the needs of the financial institutions—60%. Only 14% thought the financial institutions offered disinterested advice to the consumer. Clearly, the regulators and the public servants know something about the vulnerability of consumers that consumers themselves do not know. Also clearly, the industry either does not know this or is reluctant to admit it.

Given that you, as a committee, and the regulators whose work you are reviewing know only too well by now how vulnerable consumers are, what can be done about it? A number of solutions have been proposed, including—and I refer to Duff Conacher's presentation immediately preceding this—the encouragement of consumer associations.

In theory, I think this is an excellent suggestion; in practice, my research of consumer organizations worldwide and my experience with Canadian consumer associations show that they are weak, they're underfinanced and they're largely staffed by volunteers. Some of these volunteers are knowledgeable and dedicated, but they are the exception. Worst of all, Canadian consumer associations tend to be co-opted by the very bodies they are meant to oppose and actively seek out donations and sponsorship money from the industry. There's a price to be paid for these donations and for this sponsorship money.

I'm not trying to suggest that consumer associations have no role. With large and consistent arm's-length financial backing from governments—and Duff Conacher's suggestion is one way that this can be done; it's been tried for some time in the United States, with mixed results—some consumer associations have managed to do good work. Most notably, recently this has happened in the UK.

I would suggest that you note that consumer associations have never been consistently effective over time in protecting the interests of consumers, even in the United States, where the associations are the strongest, unless they have protracted government support. That brings the regulators back into the picture and it brings you as a committee back into the picture.

Another solution suggested to help the consumer of financial services is education. The major provider of this education in Canada to date has been the industry itself, which has offered consumers education programs as a public relations service. The Canadian financial services industry has in fact spent a great deal of money on consumer education programs. As you know, some of this money is contributed involuntarily as a result of fines imposed by regulators for a variety of misdeeds against the consumer.

1100

The Chair: I want to remind you that you have about a minute left in your presentation.

Dr Yudelman: To be fair, however, the industry has also contributed a great deal of time and money volun-

tarily and has done a good job of educating consumers about a wide variety of issues. But when it comes down to a clash of interests between the industry and the consumer, it is totally unrealistic to expect the industry to give advice against its particular interests. The industry's nature is to maximize its return on capital just as a scorpion's nature is to sting frogs. It is not only unrealistic, it is also unfair to expect the industry or the scorpion to act against its nature. Hence the title of the study I referred to earlier, The Scorpion and the Frog.

Shareholders expect their companies to maximize returns, not to primarily look out for consumers. That's somebody else's job. But whose job is it to look after consumers if they can't do it themselves? I suggest this question comes back to the job this committee has before it. At the very least, it's obvious that governments have a central role to play, but I would go even further and suggest that governments, and specifically regulators, have the most important job of all in protecting consumers.

This committee has an historic opportunity to make a major difference. Everybody knows the difficulties. They know about the tortuous regime of divided and conflicting jurisdictions, but the Australians had similar problems and they overcame them with political will and determination. We can do the same thing in Canada.

We need a single regulator for securities in Canada, without a doubt, and I think that's within our immediate reach. But beyond that, the provinces and the federal government need to create a single regulator for all financial services. If you like, do not think of the job ahead of you as looking out for the consumer of financial services; think of it as cleaning up ineffective and inefficient markets by making them fairer and more transparent.

One last point: Since regulation without effective enforcement is worse than no regulation at all, I would appeal to you to make sure that in future the regulators regulate and the enforcers enforce, and that those who attempt to distort the markets for their own personal gain be punished with more than a slap on the wrist. Thank you.

The Chair: Thank you for your presentation this morning.

ROBERT KYLE

The Chair: I would call on Robert Kyle. Good morning. You have 10 minutes for your presentation. You may allow time within that 10 minutes for questioning, if you wish. I would ask you to identify yourself for the purposes of Hansard.

Mr Robert Kyle: Good morning. My name is Robert Kyle. I'm an investor advocate. I appreciate the opportunity to come to you and speak on this issue of securities regulation in Ontario as it pertains to the five-year review of the Ontario Securities Act.

As was mentioned in the last couple of days, there has been quite an upheaval within the US markets, an undertaking by Mr Eliot Spitzer to uncover fraud, misrepresentation and forgery and just general malfeasance within the US securities system.

I'm basically going to read to you from my slides. I have provided for the gallery in the back copies of all the slides so they can follow along if they like. I noticed the screens aren't really accessible to them.

I'm going to give you a lot of quotes so you'll have other people's feelings on the system as it exists today.

Mr Spitzer, in an article, "On the Warpath," January 25, 2004:

"The major failure has been at the SRO (self-regulatory organization) level.

"Whether you are talking about research or mutual funds or specialists, there has been a failure to properly question behaviour that they know about before anyone else."

On the next slide: "Self-regulation has been an abysmal failure—an absolute, abject, complete zero.

"It has done nothing to protect investors."

"Self-regulatory organizations (SROs) have scant incentives to monitor quality and expose fraud because fraud exposure is often interpreted by consumers as a bad signal of SRO quality."

In Canada, in Ontario in particular, the Ontario Securities Commission has recognized the IDA as a self-regulatory organization. When a government empowers a private association to perform a government function, they do so with guidelines in place. These guidelines are there to protect the public. They're there to prevent abusive use of that power.

I have provided you on this slide with one of the conditions of recognition in this province: "The guidelines for investigations of supervisory practices," dated May 1992, "are to be followed and updated." I received a letter when requesting those guidelines from the IDA. The IDA's response was that the guidelines document "is not current, nor has it been applied to our knowledge by staff of the ... IDA ... in any investigation...." That speaks volumes.

The OSC and the IDA, when they were requested through the Information and Privacy Commissioner, basically advised the Information and Privacy Commissioner that "the guidelines advise as to when and how the IDA will conduct investigations of member firm supervisory functions." Well, they've never used them, but they were able to keep them secret.

Oversight of the IDA is a failure. I quote from Jeff MacIntosh, law professor, director of Capital Markets Institute, University of Toronto:

"Nor is there effective oversight from other quarters. Politicians know little about securities regulation and care less." That may change today. "The Ministry of Finance struggles valiantly, but has neither the personnel nor the expertise to function as an effective cop. And the courts have given the regulators near carte blanche to make decisions that are perceived to be within their area of expertise."

No accountability to the public: Earlier today, Gloria Hutton was here and described to you her situation and

how she has applied for the OSC's audit of the IDA. Within that audit, two senior officials at the IDA were fired. Why were they fired? The papers report they were fired because they were changing fines and penalties—not one or two, but extensively. We can't see that report. The Information and Privacy Commissioner has ordered its release. They are contesting it, looking for judicial review in the Superior Court.

Conflicts of commitment and conflicts of interest at the IDA: The Ontario Court of Appeal, on June 25, 2003, in Morgis v. Thomson Kernaghan, stated—ruled—that the IDA has no duty of care to the individual investor.

The guidance posted for investors on the OSC Web site states the following: "Where the registered firm is a member of a self-regulatory organization ... either the IDA or the MFDA, you should direct your complaint to the enforcement division of the appropriate SRO."

The SROs have contracts with their members. They do not have contracts with the public. It's almost like having one lawyer represent both the bandit and the victim, while promising to act in the best interests of both. How is that possible?

IDA selective prosecution and fraud: Here's a recent case in which a broker admitted misappropriation of funds and forgery. They came to an agreement with the IDA that if he agreed to leave the industry, they wouldn't pursue it. What happens to the investors? How big is his bank account compared to their bank accounts?

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IDA—industry regulator, registered lobbyist and industry representative: "There is a well-documented propensity for specialized bodies such as agencies or regulatory commissions to develop very close relations with regulated entities. Specific mechanisms to assist the public interest and community-based interveners in policy-making and regulatory processes are needed to counteract this tendency."

On December 1, 2001, in the United Kingdom, the Financial Services Authority became the single regulator of financial services, banking and insurance. It assumed responsibility for supervising firms formerly regulated by SROs. There is no reliance upon SROs under the UK act: "One of the reasons for abandoning self-regulation is that SROs were viewed as associations that represented their members' interests over those of the investing public." That was in the draft of the Purdy Crawford five-year review of the Ontario Securities Act. But after speaking with the IDA and the Nova Scotia Securities Commission, that did not make it to the final draft of the separation of the roles of the IDA.

Sitting on the fence: "The IDA is Canada's only national entity with delegated responsibility"—delegated responsibility—"for securities regulation and investor protection." This is evidence given by Mr Joe Oliver, president of the IDA, to the Senate standing committee on banking, trade and commerce. But in a courtroom, in their factum, when they were opposing an investor who tried to include the IDA in a lawsuit, the IDA stated that it is "merely an unincorporated voluntary association of securities dealers governed by a constitution, bylaws and regulations which deal with the conduct, management and control of the association's affairs.

"Although the IDA is not a statutory body, it does operate within a statutory regime." That's in their factum.

The IDA had their annual conference this summer. These are a couple of pictures from their pamphlet. I don't know if you can read it in the picture. It says, "Survey the field, weigh all options, bide my time... but when should I make my move?" What does this fox remind you of? Perhaps a fox guarding a henhouse? Below, it says, "Cunning and clever, successful in outsmarting adversaries to achieve goals." It's written in the margin. Who are their adversaries?

A consumers' nightmare: Mr David Yudelman was speaking a few moments ago. From within that report, the Scorpion and the Frog, I make this extraction: "The regulation of financial services in Canada, according to Dr Yudelman, 'remains a consumer's nightmare, a tangled, confused structure divided by type of government, type of financial service, government regulation versus self-regulation and by prudential and market regulation.'" He's saying it's a mess. The consequence of any inaction may well force a greater dependency on the social safety nets provided by government.

No transparency: Yesterday, Mr Brown delivered his Coulter Osborne report. How many months late was it—six, seven? What did he need the extra time for? I think we got that yesterday from Ms Deb Matthews, who made it quite clear that he went and shopped around to get the legal opinion he required. This is a quote from Mr Brown, the chair of the Ontario Securities Commission:

"Somebody said to me, 'Boy, if we have a scandal in Canada, we are going to have to be as transparent as the United States.'

"And I said, 'Well, if we are, we could just destroy our markets.'"—David Brown, OSC chairman. Is this what we deserve?

The Chair: I remind you that you have about a minute left in your presentation.

Mr Kyle: I hope everybody has the slide presentation in front of them, because I'm never going to finish. I'm going to skip to the very last one.

The Wealth of Nations, 1776: "The interests of the dealers, however, in any particular branch of trade or manufactures, is always in some respects different from, and even opposite to, that of the public.

"The proposal of any new law or regulation of commerce which comes from this order ought always to be listened to with great precaution, and ought never to be adopted till after having been long and carefully examined, not only with the most scrupulous, but with the most suspicious attention.

"It comes from an order of men whose interest is never exactly the same with that of the public, who have generally an interest to deceive and even to oppress the public, and who accordingly have upon many occasions, both deceived and oppressed it."

The OSC's measure of success, as stated by Ms Rebecca Cowdery: "If the industry won, so did

investors," speaking to the NI 81-107 new mutual fund governance rules.

I leave it to you to decide whether Adam Smith or Rebecca Cowdery has a better grasp on the criteria that you as a committee should use to gauge the success of the current regulatory regime vis-à-vis ensuring the public interest. Again I'll go back to her comment: "If the industry won, so did investors." Please weigh that.

Investors deserve better. We need an independent tribunal charged with a clear mandate of investor protection, empowered by legislation to decide issues of law and to order financial redress for abused investors whenever appropriate. Fix the system.

Based on what you've seen here today, I've given you more than just my impression. You've seen many different accredited individuals speaking out on securities regulation. We're not that much different from the US.

In my view, if Mr Brown is trying to preserve the capital integrity of these markets—you do not do so by hiding what is happening within this industry. That is not preserving the integrity. You may preserve the level of the TSE, but it's a false economy.

The Chair: Members of the committee do have a hard copy of your presentation. Thank you.

CONSUMERS COUNCIL OF CANADA

The Chair: I would call on the Consumers Council of Canada, please. Good morning. You have 20 minutes for your presentation and you may allow time within that time for questions, if you wish. I would ask you to identify yourselves for the purposes of our recording Hansard.

Ms Whipple Steinkrauss: I'm Whipple Steinkrauss, the vice-president of the Consumers Council of Canada. To my right is Michael Lio, our executive director.

The Consumers Council of Canada is an independent, not-for-profit federally incorporated consumer organization which works in partnership with business and government, helping to manage today's consumer issues. It's arguably the most active consumer group in Canada. Our goal, as I say, is to work collaboratively to advance the voice of consumers.

Our members acknowledge and support the eight international consumer rights. They're listed here in the attachment we have given you. We believe it's good business to manage consumer issues effectively and we encourage organizations to work with us to do that.

Today we're here to speak to a number of issues related to overall governance, information and disclosure, representation, redress and consumer education. Studies by the Financial Consumer Agency of Canada, consumer organizations in Quebec, the Cartier Group and our own council all indicate a shockingly low level of financial literacy in Canada, despite the fact that virtually all Canadians are involved with the financial sector and increasingly with the securities industry. Not surprisingly, given their complexities, the insurance and securities industries are the least well understood. As was indicated earlier, the primary source of information about savings and investment vehicles is the industry itself. One third of the people studied in these studies that we've mentioned earlier find the information provided to them difficult to understand. Those most satisfied with the current system are well-educated men between the ages of 45 and 65. Those most in need of assistance and most vulnerable are the young, the less well educated and women, especially those over 65. We present this information against the backdrop of a changing environment.

There are five things that we think have made a big difference in this industry:

(1) Low interest rates are driving small investors, especially seniors relying on capital returns for most of their livelihood, into higher-risk investment vehicles such as equities simply to survive.

(2) The decline in defined benefit pension plans has brought many new players into the equity markets, either as overseers or direct managers of what will be their pension investments.

(3) The sales culture in the investment industry has become increasingly aggressive. What you need to look at here are the compensation practices of these firms. For example, in many companies the people who sell the most get a higher commission on the overall sales than do those who sell less. There's a tremendous incentive to sell. The people who have the smallest book at the end of the day get dumped. As a result, there's a lot more churning and so on because of these kinds of practices.

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(4) There's a host of relatively new, quite complex investment vehicles now being aggressively marketed to the small investor and to people who have neither the skills nor the expertise to understand them and hence to assess their appropriateness for their own portfolios.

(5) Unsophisticated investors tend to rely on the professionalism of the industry for their financial health, just as they would on a doctor for their physical health, because they lack the knowledge and skills to assess the advice given.

(6) Contracts covering arrangements such as wrap accounts are designed to make the industry as bullet-proof as possible. I've gone over some of these contracts with two or three people and they are literally a power of attorney for the firm. It's one of the reasons redress is so difficult.

While the majority of people in this industry, like all others, are decent individuals striving to produce reasonable results for their clients, there are a number who profiteer at the expense of the guileless and the less informed. It is the council's view that the current regulatory regime is failing this group, and this is our primary concern.

With overall governance, as was mentioned earlier, self-regulatory organizations do not necessarily have an incentive to monitor quality and expose fraud, because of the way it makes them look. The council supports the proposition that in all corporations, be they public or private, whistle-blower protection should be afforded to those who expose illegality and wrongdoing.

We would go further. We would suggest that, where those people who are aware of it do not do so, they can be held accountable and liable for aiding and abetting that dishonesty. I think that piece would make a huge difference in terms of what happens. We've seen so much now, in crown corporations and private companies, where people have been intimidated into not saying anything, and we need to do something about that.

There are interesting examples of self-interest in this industry. For example, the IDA has long been seeking statutory immunity enjoyed by governments despite the fact, as was mentioned earlier, that it has no legal mandate to act in the public interest or to protect the consumer, and a recent court case found it had no duty of care to the individual investor. Further, it can impose fines and drive people out of the market but it has no authority to collect the fines once they've left, and that does little to help the investor who may have lost his entire life savings.

The existing arbitration process is based on a court model. It's expensive and simply not affordable for many small investors, the major cost being that they need to engage relatively sophisticated legal advice in order to present their case. Add to this the limits on compensation, the time it takes to get a remedy and the forfeiture of the right to sue and you can understand why consumers conclude they are badly served by the system.

Other jurisdictions, as mentioned earlier, have recognized the limitations of SROs. Britain has done away with them entirely. Others have given outside bodies the authority to undertake operational reviews of them. We have neither here to the same extent.

While the council does not purport to be an expert on what might be the best model of governance to achieve the dual role of investor protection and fostering fair and equitable capital markets, the conflicts of interest in this existing system are simply unacceptable. There is clearly a need to improve investor protection by rebalancing the interests of the investor and the industry. The consumer protection role should be completely removed from industry control, and part of the fees paid by registrants should be allocated to an independent consumer protection authority that has no other role.

With respect to information, it is difficult for a small investor to get the information needed to make wise purchasing decisions. Often, it is verbal and limited to facts that sell the product. For example, rarely are individuals told that sellers get much higher levels of compensation for rear-end loads than front-end loads or no-load funds. They are simply told, in order to sell it, that there's no charge for this transaction. This makes them very attractive to those with the fewest resources and the most vulnerable, like the young, the elderly and so on. Most investors have no idea how salespersons earn their income, unlike, for example, a real estate person, where you know exactly what that person earns from that transaction.

Know-your-client forms are a key component, it is said, in this effort to assess consumers and provide appropriate information, yet, these are only used to encourage appropriate investments. The forms are not standardized. The terms used are not defined. Many do not require the signature of the investor. The investor often is not given a copy and, finally, there is no requirement that they be reviewed at regular intervals.

So what happens on the ground? We'll just give you three quick examples. We've been told of aging seniors with 80% of their portfolios in high-risk equities—and these are solicited trades. This is not someone who's wanting to make a quick buck who says, "I want so many shares of whatever." These were solicited trades. We've been told of people, within a year and a half of the necessary RRSP rollover to a RIF, having their entire portfolio, or most of it, converted to rear-end load equity funds. Suddenly they're 69 years old, they have to take out their first 5% or 6%, and the portfolio lists 1%, so they have to sell. Guess who makes the money? You could never call that a conscionable transaction. You could never call that, under any circumstances, reasonable advice, and it happens to people. These are the kinds of things that are happening. There are also other kinds of cases we could go on at length about, but we don't have time today.

Regardless of what percentage of transactions in the industry are like this, the council believes their numbers are going to increase. The reason they're going to increase is because more and more people with lower levels of literacy are coming into the markets. We're going to see a problem, I think, if we don't deal with this.

When written information is provided—for example, when one opens an account—it can be overwhelming to the average investor, both by volume and it is not well understood. A separate consumer protection authority could mandate standardized, plain-language documents and the process to be used when informing new investors.

Another major concern of our council is the practice of putting confidentiality clauses in settlements between the industry and an individual investor who has been the victim of malfeasance and, indeed, in some cases, outright criminality. As a result, a prudent investor has no way of finding out that a particular trader has a bad track record. And if there are no criminal charges pursued, that person gets back in the industry, sometimes simply by moving to Manitoba, or if he's in Manitoba, moving to Ontario. The culture of the industry is to keep all these matters quiet, so as not to undermine confidence. From our perspective, the only cases that ever get referred to law enforcement are those where the industry loses a lot of money; very rarely when something can be covered up.

The council recommends the law require the industry to report all illegal activity to the law enforcement community and that charges be laid where appropriate. There are a lot of very serious crimes being committed that are covered up by a deal and a confidentiality agreement, and this should not be occurring.

Finally, on redress: Arbitration between parties with widely different levels of resources at their disposal is not

a suitable mechanism for resolving disputes. In the case of the securities industry, it has significant resources to defend itself. The most significant cost to the individual, of course, is the cost of legal services. The court process can be very long and drawn out. I'm told that arbitration in Ontario can cost upwards of $15,000. When you add to this the cap of compensation at $100,000, that the decision is binding and therefore no further legal action be undertaken, you can understand why a lot of people do not pursue redress. They don't know whether they're going to succeed; it's just another cost added to it. Frankly, you have better consumer protection in Ontario if you're buying a travel package or a used car, because you've got a comp fund you can go to at no cost, than when you get cheated by the securities industry.

What should a redress mechanism for the small investor be characterized by?

Minimal, if any, cost, with frivolous claims pre-screened;

An industry code of conduct developed by industry and consumers;

The availability of expertise to assist the investor to address the imbalance of power and resources;

Timelines around resolution; and

An unbiased panel to rule on the matter, with equal consumer and industry representation and an independent chair, whatever form that takes, be it a tribunal, a committee, whatever. That's the kind of format we think would be appropriate.

The council is aware of investors who have won significant settlements in court, but in one case it was drawn out over 10 years. If you're an older person, you're probably going to die, either of a broken heart or some other ailment, before you ever get the settlement. It just goes on and on and on. There are appeals and so on. This is not helpful.

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For consumer education: As we indicated at the outset, the level of financial literacy among Canadians is shockingly low. There are three or four studies available that I'm sure you may already have in hand, but we could provide them, if necessary. One of the most striking findings for the council was that people actually overrate their financial literacy. They know less than they think they know, and they don't get answers because they don't know any of the questions. This adds significantly to their vulnerability.

The council believes this is a serious problem, and one which governments, even in their own self-interest, should address immediately. If significant numbers of less financially literate citizens are left to navigate the complex financial services industry without help, many are going to reach their retirement years with little, if any, income because of unwise decisions made with their pension assets. The same fate may befall some of our less sophisticated seniors.

A consumer education program is needed. Ideally, it should be part of an industry-independent redress authority. Industry fees could resource consumer education. The authority should produce up-to-date, plain-language materials, available as needed, in a variety of formats, and a telephone hotline service for those seeking independent advice. We're not talking about recommendations on specific products but information on how to assess them.

We trust our perspective will be helpful in your decision-making and thank you for your attention.

The Chair: Thank you for your presentation. We have slightly less than six minutes for questions. That's two minutes per party. We'll begin with the government side.

Mr Berardinetti: I want to thank you for coming here today and for your presentation. Can you just briefly provide a bit more information about the organization that you represent? I know it's contained in the material, but I just wanted to know a little bit more. Is it basically a seniors' group?

Ms Steinkrauss: No, no. It's a multi-issue consumers association. It's been in existence about 10 years. It's federally incorporated. We exist to provide a consumer voice. We work particularly on public policy issues and corporate policy issues. We've been involved with both the corporate community and government committees of various sorts in trying to change practices, law and so on to enhance the voice of consumers. We receive our funding from a variety of sources: individual memberships, corporate memberships, government projects and so on. We have a policy that no more than 30% can come from any source so that we can remain independent.

Mr Berardinetti: Thank you.

The Chair: We'll move to the official opposition.

Mr O'Toole: Thank you very much for your presentation. It's good to see the consumer protection—or whatever your mandate is. It would appear that you say on page 4 that, "The council's primary concern is the protection of the small investor, recognizing many of whom are not investors by choice."

Do you have any specific advice with respect to the two challenges here: the national securities regulator and the issue of separation in governance of the judiciary from the regulation-making authority, the OSC? Do you think they should be separated? If so, how?

Ms Steinkrauss: We definitely think the adjudicative function should be separated from the overall regulatory function. We think that it needs to be an independent body. Now, we're talking about the small investor here. There may be a different set of rules for pension funds, institutional investors and so on, and we don't have any difficulty with that. You've got very highly paid people who can take on some of those types of cases. We can't speak with expertise to those issues. What we can say is that for the ordinary citizen who has a difficulty, there is simply not a vehicle that is affordable, that's timely, that has some of those characteristics I mentioned. So definitely—

Mr O'Toole: Would you do that by claim level or entitlement? A small loss would have one process; a large institutional loss, like pensions funds, would have another one?

Ms Steinkrauss: I would tend to do it by individual versus corporate. Think of someone who's got $1 million. It seems like a whole lot of money. But this is a person who's been at a small business all of their lives, and they don't have any other pension. So if they get 5% on that, they get $50,000 a year. This does not make them a wealthy person. As a pensioner, that person also has to reinvest some of that money to generate money going down the road.

So there are people like this who are coming to our attention, who are losing $200,000 and $300,000. There was a case that I read not too long ago of a woman who had a little over $1 million. In three years, she went through $300,000 in trades from churns.

You see, once you've agreed to it, it's hard to win this in court. They don't want to go to court because—someone has phoned them up and said this is a great idea, and they're not too sophisticated. Also, in a wrap account, sometimes they've literally signed away their rights. You should see some of these contracts. It would be important for this committee to read some of the wrap contracts. I had two or three different people read them. One was an accountant who was a vice-treasurer of an oil company and another was a person who had worked in the securities industry. All of them said, "Over my dead body would I sign a document like this."

The Chair: We'll move to the NDP and Mr Prue.

Mr Prue: We've heard for the last two days from a number of individuals who feel like they're getting ripped off by the system. We heard today that there is very little money being spent in actual enforcement by the OSC. In comparison to the American counterparts, it's half, a third or a quarter and the number of prosecutions is surprisingly low.

Would you think that the enforcement of the act and beefing up the enforcement in a proper adjudication system is the major issue facing consumers?

Ms Steinkrauss: It is. The other one is simply the cost and timeliness of redress where there is a problem. In any industry, you're going to have malfeasance. There's a certain percentage of people, it doesn't matter what they do—

Mr Prue: It seems like this one has a little bit more than its share.

Ms Steinkrauss: That's right. The incentives for malfeasance are high. As I say, another one is compensation practices. They're very interesting.

Actually, we've been contacted by brokers in the industry who've said, "If you could fix this, we'd love it."

The Chair: Thank you for your presentation this morning.

CANADIAN PUBLIC ACCOUNTABILITY BOARD

The Chair: I call on the Canadian Public Accountability Board. Good morning. You have 20 minutes for your presentation. You may leave time within that 20 minutes for questions, if you wish. I would ask you to identify yourselves for the purposes of our recording Hansard.

Mr Gordon Thiessen: Thank you, Mr Chairman and members of the committee. My name is Gordon Thiessen. I am the chair of the board of directors of the Canadian Public Accountability Board. With me is David Scott, who is the CEO of the board.

The job of the Canadian Public Accountability Board, or CPAB as we call it, is audit oversight: overseeing the auditors of public companies and other reporting issuers.

We appreciate the chance to talk to you. We have provided the clerk with copies of a letter to you that sets out in more detail the matters I want to talk about today.

Essentially we're here to ask the Parliament of Ontario to consider some amendments to the Securities Act, amendments that would enhance the effectiveness of our oversight role. Our request has the support of the chair of the Ontario Securities Commission, David Brown, who is also the chair of the council of governors of CPAB.

CPAB is a not-for-profit organization. It was created in April 2003. This was after the date of the final report of the five-year review committee, as Purdy Crawford mentioned to you this morning, so that committee did not specifically discuss a role, but in its report did stress the importance of investors being able to rely on audited financial statements. That's where we come in.

Our purpose is to encourage high-quality external audits of public companies and other reporting issuers by enforcing quality standards for audit firms subject to our oversight, by inspecting the work of those firms and, where necessary, imposing requirements, restrictions and sanctions. In addition to our own direct remedies, we will refer any appropriate matters to provincial securities regulators and to provincial accounting bodies, where needed.

A council of governors, which is chaired by David Brown, appoints the directors of CPAB. The board consists of 11 individuals who cover a broad spectrum of experience and perspective and who come from across Canada. Eight of the 11 directors, including the chair and vice-chair, are independent of the accounting profession. Five of the directors on the board are resident here in Ontario.

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Canada's securities commissions now require public accounting firms to become participants in our oversight program if they wish to audit the financial statements of reporting issuers, and so far, over 200 audit firms have registered with us. The participating audit firms enter into an agreement with us whereby they agree, among other things, to abide by a set of rules that govern our relationship with them. Our inspection activity commenced in April this year and it began with the four largest accounting firms. These firms collectively audit over 70% of the reporting issuers in Canada by number, and if you look at them by market capitalization, these four firms audit essentially 90% of reporting issuers. By the end of this month, we intend to issue a public report on the broad conclusions coming out of our inspections so far.

So CPAB is an important element in the Canadian securities regulators' investor confidence initiatives. We are comparable in function to the Public Company Accounting Oversight Board, PCAOB, or "peekaboo," as some people call it, that was created under the Sarbanes-Oxley Act in the United States. It, of course, was part of a response to the high-profile corporate failures: Enron, Worldcom etc. We strongly believe that there is a need for legislation in Canada that would give CPAB statutory powers and protections similar to those that the PCAOB has under Sarbanes-Oxley.

In the short term, we are relying on a network of agreements with participating audit firms and with provincial accounting bodies. These arrangements have allowed us to commence our inspection work, but they cannot adequately duplicate what could be accomplished by legislation. It is apparent to us that our efforts in audit oversight will be constrained if we cannot obtain a sound statutory footing.

All of our requirements could be accomplished by means of amendments to provincial securities legislation. We have in our letter to you, Mr Chairman, provided illustrative wording that we believe could be added to the Securities Act.

Let me quickly tell you about the issues that face us here. First is the issue of statutory immunity. CPAB, including its governors, directors and staff, is exposed to the risk of litigation now that we have begun our inspection activity. Sooner or later our inspections are going to uncover circumstances that may lead us to impose serious restrictions or sanctions on a public accounting firm, and that could lead to some retaliatory litigation. This is of particular concern to the members of our board of directors. Without statutory immunity, there is a significant risk that in the future we are not going to be able to attract high-calibre board members or, indeed, professional staff, and they are essential for an effective, independent auditor oversight program.

Persons acting on behalf of the securities commissions, provincial accounting bodies, and the PCAOB in the United States all enjoy statutory immunity for good faith conduct. We don't see any strong argument against the provision of comparable statutory immunity for those of us, acting on behalf of CPAB, exercising auditor oversight powers in good faith. Indeed, we believe that the lack of statutory protection may compromise our ability to carry out our role with the vigour that it should have.

We also believe it is advisable to make CPAB and its inspectors immune from subpoenas in unrelated matters. Exposure to subpoenas undermines our ability to protect the privacy, confidentiality and privilege of information that we gather as part of our auditor oversight process.

This leads me to my next point. We need statutory access to confidential, private and privileged information to carry out our work properly. Our inspection and investigation activity requires us to collect and retain confidential and possibly privileged information about the accounting firms and their clients, as well as personal information about the individual partners and the staff. However, accountants' professional obligations to protect their clients' confidential information limit our ready access to, and use of, such information. Moreover, accounting firms, not surprisingly, are concerned that disclosure of certain information to us may constitute a waiver of solicitor-client privilege. This is a complex area which we can't really explore fully with you today, but it is covered in more detail in our letter to you, Mr Chairman.

Just let me provide you with one example. We need access to personnel files to understand the basis under which individual audit partners and staff and firms are rewarded and promoted. We need to know about their attendance and training courses to make sure they keep up to date and we need to know about their professional qualifications.

Currently, our access to that information is achieved by requiring every single professional in every audit firm to sign an agreement and consent. There are thousands of people affected. It's a substantial burden for the firms to secure all these consents, and there's a risk that we won't get all the documents and that consents may not be enforceable in particular cases. So the extensive burden and management risks and legal risks could be alleviated if securities legislation in each province and territory were amended to authorize our collection and use of personal information.

We're a national organization, but our oversight of auditors' publicly traded companies relates to provincial responsibility for securities legislation. The legislative change that we seek needs to be implemented in every province. We're currently concentrating our efforts on the four large provinces that are home to the large majority of reporting issuers and their auditors. Provincial securities regulators in all these provinces support the necessary changes we are asking for with respect to securities legislation.

In the case of Alberta, we now have a letter from the minister indicating that the Alberta government is prepared to act on our request. We've encountered a positive reception in BC, Alberta and Quebec. But it is in Ontario, the home of the TSX, the centre of Canadian capital markets, where legislation is really crucial if the Canadian Public Accountability Board is going to play its role effectively in investor protection.

We appreciate the opportunity of bringing our concerns to your attention. We're happy to answer any questions and provide any information you may require either now or later. Thank you, Mr Chairman.

The Chair: Thank you. We have about three minutes per party and we'll begin with the official opposition.

Mr O'Toole: Thank you very much, Mr Thiessen, for your presentation. I appreciate that. It's a pleasure to take the time.

Just a general observation: It seems everything I pick up, David Brown is either chair or involved directly; it's interesting. I'm not sure if there's any conflict there. I don't say that in any derogatory fashion. He must be

eminently respected in terms of his understanding of not just the market but all of the various players.

I was interested today—I don't want to appear as totally an advocacy type. We've had a lot of those presentations today, so I get on the wavelength there a bit. One of the recommendations by Mr Kyle today, on page 32, which I thought was a fairly innocuous little recommendation, is that the Provincial Auditor should undertake an audit of the OSC and IDA and the MFDA, some of the organizations. When the auditor, Mr Peters, was there, I had the greatest respect. We've always said that crown corporations, school boards and hospitals should all have oversight. Since the OSC is sort of seen to be a branch of government, would you have a problem with that, an oversight audit of those self-regulatory organizations and the OSC?

Mr Thiessen: That the OSC does the audit of these organizations; is that what you mean?

Mr O'Toole: Yes. The public auditor would audit this OSC, the IDA and the MFDA.

Mr Thiessen: Not on the face of it, but I must confess this is not an area that I'm particularly familiar with, so it would not be an informed opinion. I don't know, David, if you've got a view about that.

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Mr David Scott: I actually know Erik Peters very well. He does do some audit work at the OSC; I know that. I don't see any problem in his doing an operational audit of the OSC and of some of the SROs. We should be clear that we are not an SRO under this structure.

Mr O'Toole: I understand that. I appreciate your input.

The Chair: Thank you. We'll move to the NDP.

Mr Prue: I'm still trying to understand, if you're not an SRO, who set you up. I don't understand. We've got this whole thing. Who set you up? You're not a government agency and you're not an SRO, so who set you up?

Mr Thiessen: We were set up by the various securities regulators. The council of governors that essentially set us up is made up of the chair of the Canadian Securities Administrators, the chair of the Ontario Securities Commission, the chair of the Quebec securities commission, the federal superintendent of financial institutions and the president of the Canadian Institute of Chartered Accountants. That's the group that set us up. That's the group that appointed the board of directors.

Mr Prue: Who pays the bills? That will tell me more than anything else.

Mr Thiessen: The audit firms pay the bills. We essentially impose on them fees to cover the cost of us doing our inspection services.

Mr Prue: They are required by law, under what statute, to give you the money?

Mr Thiessen: They are required under a securities regulation that was passed by the Canadian Securities Administrators that says that any public company or reporting issuer in Canada has to be audited by an audit firm that is subject to the oversight of the Canadian Public Accountability Board. So if you're an auditor and you want to audit public companies, you have got to register with us and submit to our oversight. That is what gives us the clout we need.

Mr Prue: And you have that clout without any legislation at all?

Mr Thiessen: That's right. But one of the reasons we're here is that we do feel we need some legislative base. Right now we're essentially operating with the benefit of this regulation plus a series of contracts the participating audit firms have signed with us. But this is not as strong a base as you'd like to have if you're going to engage in oversight.

The Chair: Thank you. Now we'll move to the government side.

Mr Delaney: Do CICA or any of the provincial institutes have within their powers the ability, through regular practice inspection, to do any part of the oversight of the accounting firms that you've described?

Mr Thiessen: Absolutely. We are in the process of setting up arrangements with each of those provincial accounting bodies across the country. While it is our intention to inspect the very large firms, the Big Four, we're then going to also inspect the next, middle-sized ones. We're also going to inspect any audit firm that audits a public company that is registered in the US, because the American PCAOB wants that comfort from us. But for the smaller auditors that remain, we are essentially going to sign memorandums of understanding with each provincial accounting body to continue to do that work. We will work together with them. Hopefully it will be done to our standards and subject to our oversight.

Mr Delaney: That's pretty thorough and comprehensive, and in my experience the provincial institutes have some teeth. So over and above the 95 recommendations in the five-year committee final report, what major amendments need to be made to securities acts across Canada?

Mr Thiessen: The major amendment, from our point of view, is that we want to give CPAB some legislative standing, some statutory standing, in every province, standing that would give us statutory immunity from suit, legislation that would give us access to confidential, private and privileged information and legislation that would protect us from subpoenas in unrelated areas. We're in a situation now where there's some concern about providing us with information for fear that you lose your privilege the moment you give it to us. If you were involved in a court case, all of a sudden that privilege could be waived. That's what we're looking for.

Mr Delaney: Thanks. That answers the question.

The Chair: Thank you for your presentation this morning.

SANDRA GIBSON

The Chair: Our next presenter is Sandra Gibson. Good morning. You have 10 minutes for your presentation. You may allow for questions within that 10 min-

utes, if you so desire. I would ask you to state your name for the purposes of Hansard.

Ms Sandra Gibson: My name is Sandra Gibson. I am currently engaged in a lawsuit against TD Bank and a broker who did work for them. Having heard other speakers this morning, I recognize that there are those who are far more educated and articulate than I to discuss the problems of accountability and transparency. So I would like, if I may, to tell you about my direct experiences with the OSC and the IDA, in the hope that it might help you to recognize the problems as they currently exist in the system and what appears to me to be a very convoluted, if not incestuous, relationship between the IDA and the OSC, all to the disadvantage of abused investors.

My first experience with these regulatory bodies was when I contacted the OSC in April 2003. That was the time at which my problems with TD Bank crystallized. Because TD Bank did not offer any help to me whatsoever, even though my investments at that time were in a most precarious position, I had to go elsewhere to seek help. I was fortunate to have been recommended by a friend to a small private investment firm that recognized the urgency of my situation and the problem of having to act quickly to protect me from further losses.

The principal of the small firm advised me to contact the OSC and the IDA and to write a letter to TD Bank, with copies to Ed Clark and on down. I followed all three of his suggestions. My first contact was to call the OSC and describe my problem to them. I do not recall the exact wording of the conversation, because it was well more than a year ago, but it was made very clear to me that I should be speaking to the IDA, that my problem was inappropriate for the OSC to be dealing with.

Because I couldn't recall the conversation, I decided, as an exercise, to call the OSC this week. I spoke with a Mr Kamal Khanna and briefly described my problem with TD Bank. Mr Khanna stated to me quite emphatically that all problems concerning members of the IDA had to be referred directly to the IDA for arbitration. I told Mr Khanna that I was aware of the lack of power of the IDA, in terms of the fact that they cannot grant restitution. Mr Khanna spoke, again most emphatically, and said that the OSC cannot order financial restitution.

Well, I don't know if you're familiar with the section of the Securities Act that states very clearly that the OSC can require the court to order restitution to a company or individual. So I would like to ask all of you when Mr Brown or his predecessor made the decision that they wouldn't bother dealing with individuals, and on whose authority did the head of the OSC make that decision? As I'm aware, there has been no amendment to the Securities Act, has there? Can someone answer that question?

The Chair: We're here to hear your deputation. I must admit that I'm not aware of a recent change, but that doesn't mean one couldn't have happened. The committee is not prepared to answer questions on behalf of other groups.

Mr O'Toole: We could leave that with the committee as an open question.

The Chair: Yes. The committee will take that as an open question and seek an answer to it.

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Ms Gibson: Thank you. As it happens, I did have an experience with the OSC at the corporate level. It was, in fact, by accident, but I would like to relate that experience to you as well.

During June of this year, I attended and witnessed a shareholders' meeting of a corporation held here in Toronto. I had been told the OSC was investigating the company, but I had no way of knowing whether that was true or not.

After the meeting, quite by accident, I was introduced, along with several other people, to a man who stated he was an OSC investigator and that he had been looking into the particular company for over a year. He was wearing a T-shirt. During the course of the ensuing conversation, the investigator volunteered the information that he had "only a grade 12 education." He also wondered aloud, in the presence of a number of shareholders, whether perhaps the particular company should not be referred to the police for investigation.

Because I was in some doubt as to the status of this individual, I did call the OSC a few days later—I had his card—and inquire whether, in fact, he was employed there. He is.

I wish you had been present to witness the expressions on the faces of a number of American shareholders who were present at the meeting, because the company I'm referring to is closely affiliated with another corporation which is publicly traded in New York.

You say that I cannot ask questions, Mr Hoy, but perhaps you would consider how it would be possible for someone with a grade 12 education to investigate companies of the complexity I've referred to. So much for the OSC.

I also wrote a formal letter of complaint to the IDA in April 2003. I did receive a response from Mr Popovic. He included the standard brochure from the IDA; I don't know whether you're familiar with it. In my case, he might have saved his paper, because there is nothing offered here that would have helped me in my situation. I think you would have to agree that perhaps the IDA, in terms of settlements or restitution, is a little out of step, a little behind the times. For example, the process of arbitration is available to individuals who have lost $100,000 or less. If you've had a look, I think you'd discover that many, many individuals have lost a great deal more than that, including myself.

The other option, of course, is to go to OBSI, the provincial ombudsman. Again, that did not suit my purposes. So it was very clear to me very early on that the only option available to me was to initiate civil action. I'm sure you're now aware, having heard other speakers, that this option is available, really, to what must be a small minority of abused investors, because the costs are enormous. One law firm I interviewed informed me that if I settled out of court, the legal costs would be $50,000; if I proceeded to court, the costs would be between

$125,000 and $150,000. I think it's pretty clear, isn't it, that there aren't many of us who are in the position to follow that route.

The other thing I would like to refer to—and to me it's an outstanding situation—is gag orders or confidentiality agreements. The lady from the consumer council has already mentioned it, but I wonder if you would stop and think about the fact that if I bought a new car and the car was defective and the manufacturer replaced the car, would they ask me to sign a gag order? If I bought a new house and it proved to be structurally defective and I sued the builder, would he ask me to sign a gag order? Why is it that the industry gets away with this? The only reason, obviously, is they don't wish the public to be apprised of the extent to which there are misdemeanours occurring within the industry. Yet we consider this the norm, the common practice.

The other item I would like to mention is that it has repeatedly been made clear to me by various members of the legal profession and the investment industry that when I proceed with my lawsuit and either discuss settlement or, I guess, go to court, certainly in the settlement process I will be deemed very lucky if I am offered 50 cents on the dollar. Why should that be? Why would I not be permitted to recoup all the money I have lost?

I really feel that's about all I have to say. If you'd like to ask me questions, I'd be pleased to answer.

The Chair: Regrettably, our time has expired. I will have the researcher go over your question with you before you leave, if you wouldn't mind taking a minute for that. The committee thanks you for your presentation this morning.

The committee is recessed until 1 pm.

The committee recessed from 1205 to 1303.

ADVOCIS

The Chair: The standing committee on finance and economic affairs will please come to order. Good afternoon, everyone.

I invite our first presentation of the afternoon, Advocis, to come forward, please. Welcome to the committee. You have 20 minutes for your presentation. You may allow time for questions within that 20 minutes, if you so wish. I would ask you each to identify yourself for the purpose of Hansard.

Mr Steve Howard: My name is Steve Howard. I'm the president and chief executive officer of Advocis.

Ms Sara Gelgor: Sara Gelgor, director of regulatory affairs, Advocis.

Mr Dennis Caponi: Dennis Caponi, practitioner, member of the board of directors of Advocis.

Mr Howard: Good afternoon, Mr Chairman and distinguished committee members. I will be using approximately two thirds of my time today for presentation remarks, after which we would be pleased to answer any questions you may have.

I am Steve Howard, president and CEO of Advocis, which is the Financial Advisors Association of Canada. As you know, I am joined today by Sara Gelgor, who is the director of regulatory affairs at Advocis, and by Dennis Caponi, who is the chair of its public affairs committee. Mr Caponi has over 30 years of experience as a financial adviser and will join me in addressing any questions you may have following my presentation. Mr Caponi holds an insurance licence, a mutual funds licence and a securities licence. Thank you again for the opportunity to appear before you today.

Before I proceed to the substance of my presentation, allow me to give you a brief overview of Advocis. Advocis is a voluntary professional membership association of financial advisers within Canada, with 16,000 members. Our members are financial advisers licensed to distribute life and health insurance, mutual funds and other securities products. Advocis members provide financial and product advice to over 12 million Canadians across a variety of distinct areas, including estate and retirement planning, wealth management, risk management, and tax planning.

Advocis continues its history of serving Canadian financial advisers, their clients and the nation for almost a century. Advocis is committed to professionalism among financial advisers.

I would like to congratulate the Crawford committee on its detailed and far-reaching report. We are here today to address one key recommendation made by the committee, and that is the establishment of a national regulator.

Advocis supports the establishment of a national regulator. We believe that national regulation can be a viable approach to the regulation of capital markets where a single regulator can truly achieve greater efficiencies over the current model. You've already heard from a number of presenters on this issue, many of whom have undertaken a great deal of work to consider appropriate models of capital market regulation. While we do not take issue with much of what has been said, we are here to suggest to you that the other presenters and commentators have overlooked one important point: Consumers are best served by independent-minded professional advice, and the models proposed thus far for a national regulator seem to us to only perpetuate conflicts of interest within the regulatory framework. Allow me to explain.

I have in my hands the Advocis best practices manual. This living document borrows heavily from the work of the Financial Planners Standards Council and includes input from many advisers and companies across Canada. It is a comprehensive guide for financial advisers and represents the highest standards of professionalism. Although less mature, it can be compared to the same practice standards advocated for accountants and lawyers by their professional governing bodies.

I also have the Ontario Securities Commission proposal for a fair dealing model, which would have the OSC move assumed regulation of advice, not by promoting independent-mindedness but by charging self-interested companies with responsibility for regulatory oversight.

We believe that the regulation of financial advice should be free of any inherent conflicts of interest and based on a model not unlike that which is currently in place for other professions, particularly the legal, medical and accounting professions.

Responsibility for financial advice rests with the individual giving it. The relationship of the consumer to advice is a relationship between the consumer and the adviser. Ensuring that the adviser is positioned with a professional mindset is the consumer's best protection. Products, by their very nature, carry an inherent bias. Advice should be free from such bias and unquestionably neutral.

We propose that securities regulators continue to regulate the distribution of financial products and that financial advice be regulated by an independent professional body. Under our model, all individuals who hold themselves out to consumers as financial advisers would have to meet the same standards. In particular, they would be required to hold a professional designation, adhere to an established code of professional conduct, subscribe to practice standards, acquire meaningful continuing education credits, and maintain appropriate errors and omissions insurance coverage.

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In essence, the professional body would set and police guidelines respecting the ability of anyone to hold himself or herself out as a financial adviser. This would establish an accountability to the consumer, and one that does not exist today, directly between the advice and the recipient of that advice.

I'd like to back up for a moment to paint a picture for you of the environment in which financial advice is offered today.

The financial affairs of Canadians have become increasingly complex over the past 20 years. More and more Canadians are realizing that they must take responsibility for their own affairs. Many are self-employed, and those who are employees are finding that they are not able to rely upon their employers and on governments to provide for their future financial security. Taxation is more complicated, and many Canadians find it impossible to even file tax returns without professional assistance.

In this environment, a new body of financial advice has grown that is not focused on the sale of products. Typically, this advice involves the application of complementary strategies to best meet individual goals. These strategies can include cash flow management, tax minimization, retirement preparation and wealth management.

There are two fundamental types of advice available in the Canadian financial services industry today: (1) product advice; and (2) financial management advice, or what we refer to as independent-minded financial advice.

Advisers involved in the sale of a product provide product advice. Typically, the advice extends to the benefits and applications of the financial product in the client's circumstances, but ultimately results in some form of product recommendations. Some product advisers only provide product advice, but many also provide financial management advice as a separate and distinct activity from product sales. Product advice can generally be categorized as: (1) insurance, which includes life and health, property and casualty insurance; or (2) investment, which includes securities and mutual funds.

Independent-minded financial advice may be provided by advisers licensed to sell financial products, or by advisers with no involvement in product advice. Whichever adviser provides the advice, this type of advice is not grounded in product sales. It can consider all aspects of an individual's financial affairs, commonly referred to as comprehensive financial planning, or it can focus on one or more elements of an individual's financial affairs.

The ability to provide this type of advice, and the foundation for consumer confidence in financial advisers, is the professionalism of the adviser. That professional should be identified by restricting the use of the term "financial adviser" to appropriately qualified and governed individuals.

As I noted above, there are two broad types of product advice and sales: insurance and investment. Each is regulated very differently today. For example, the regulation of advisers providing insurance advice and sales is results-focused. It regulates what must be done, but not how it must be done. It is grounded in the regulation of the adviser directly. It allows for advisers to be independent of product manufacturers and distributors. It provides for client protection through errors and omissions insurance and, most importantly, it has experienced acceptable levels of market abuse.

In contrast, the regulation of advisers providing investment advice and sales is transactions-focused and regulates not only what must be done, but how it must be done. It's grounded in the regulation of the adviser through a dealer. It provides for client protection through a complex regulatory framework, and yet it has still experienced significant levels of market abuse. This is not the foundation upon which to build a national regulatory structure in and of itself.

To succeed, the national regulatory structure must, in our opinion, advantage itself of the learnings within the current model for insurance advice, and introduce the proper positioning of independent-minded financial advice.

Currently, there is no direct regulation in place for non-product advice. The regulation of this type of advice has been attempted by existing product regulators, but with limited success. Their experience in the regulation of sales activities and products is not the type of experience required to govern financial management activities. These non-product activities require a form of governance that is more similar to other advisory professions like accounting and law than to sales and marketing activities.

As the objectives of regulation within the Securities Act are to (a) provide protection to investors and (b) foster fair and efficient capital markets and confi-

dence in capital markets, the Advocis approach to the regulation of financial advisers is a natural ally to national regulation. We are only concerned inasmuch as this important principle has been given secondary status in discussions to date when, in reference to the principles and objectives of regulation, it should be the primary focus. We submit that it is the interest in self-promotion of the current regulatory environment which is obscuring the opportunity that we have identified.

For me, it is very simple: The advisers I represent speak to 12 million consumers or more annually. Those advisers know that what consumers need is the trust in their professional advisers to give them sound advice and match them with appropriate products. To do so, advisers must be unfettered in their pursuit of professional independent-mindedness.

The Advocis approach builds on an existing framework, it is national in scope, it complements the establishment of a national regulatory system, it encourages the highest standards of proficiency and transparency and it furthers consumer protection.

Moreover, the Advocis approach rationalizes the fragmentation of competing interests currently in the marketplace and integrates the roles of all interested groups and organizations recognized to issue designations and accreditations to financial advisers.

The lives and needs of Canadians are changing rapidly as the population ages and historical employment and lifestyle patterns unravel. The traditional reliance on advisers for product information and advice is declining with the growth in availability of this information from abundantly available alternative sources such as the Internet. Coincident to this decline in the need for traditional advice is the increase in the need for non-product advice. Advisers are adapting to this changing role, while regulators continue to apply old definitions and regulatory strategies developed for sales and marketing activities to professionally based advisory work.

We urge this committee to consider our proposal and recommend that the government of Ontario recognize the professional and highly skilled nature of the independently minded financial adviser by: embedding in legislation the requirement of professional designations for financial advisers; recognizing the two distinct types of advice serving the marketplace today and understanding that effective governance will only result when the financial services market is identified and separated by the type of advice provided, and non-product advice is regulated in the same manner as other advisory professions.

Thank you for your time and your attention today. We would now be pleased to answer any questions you may have.

The Chair: Thank you for your presentation. We have about two minutes per party and we'll begin with the NDP.

Mr Prue: I didn't see anything in here about licensing. Would you want these people to be licensed?

Mr Howard: Yes, we expect them to be licensed. As product providers, they are still licensed under the current regime. What we are arguing is the separation of this separate body of advice and that it be separately regulated. We are not talking about a revisiting of the current regulatory system. We are talking about an additional governance system for a separate type of advice.

Mr Prue: I understand that, but licensing comes solely under the jurisdiction of provinces. I'm wondering how you would do a national licence. That's a bit of the problem I have with your proposal, at least until you explain it to me.

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Mr Howard: I'm not here to comment on the best model for national regulation. I am here to say that that element of the separate advice has been overlooked and should not be swept into whatever that model may be.

Mr Prue: Again, whatever the model is, you're being very specific in terms of having the people licensed and then recognizing their advice as a professional product. If we are to proceed to a national system, I don't know how that's going to work, with the province having the licensing authorities. Everyone would have a different licensing authority. In my view, it would compound the difficulty of getting the national government to have one system in the first place. Certainly I think the claws would come out from most of the provinces if you got into the licensing aspect. I just wondered if you could comment on that.

Mr Howard: I respectfully differ from your interpretation. It does not compound. What it does is it clarifies for the consumer—which is the important end concern here—what they're receiving, who they're receiving it from and what qualifications that individual has to provide that advice. So it is actually a clarification for the consumer that results at the end of the day. We absolutely support that the national regulatory system be rationalized and improved, but we do not support that this independent-minded financial advice be swept in under whatever that product advice regulatory structure may look like.

The Chair: We'll go to the government.

Mrs Linda Jeffrey (Brampton Centre): Thank you, Mr Howard. I appreciate the depth of the information you gave us today, but our role is to look at this book and its recommendations. Based on what your recommendations were, I was unclear as to your position. We are being asked to look at the regulation of the market participants, and the recommendation I believe that would most likely be closest to what you spoke about today speaks about the act continuing "to distinguish between the requirement to be registered to advise concerning securities and the requirement to be registered to trade in securities (or, as we proposed in our earlier recommendation, to be in the business of trading securities). However, we recommend that the commission and CSA carefully review the proficiency, experience and suitability requirements applicable to dealers and employees."

Is that something you would support? Is there anything in the recommendation that you feel wasn't sufficient, based on your experience?

Mr Howard: Our fundamental concern is that there's something not in the recommendations. In particular, that is that there are two types of advice. In the interest of the protection of the consumer, we urge you to recognize that fact and to distinguish between them.

The Chair: We'll move to the official opposition.

Mr O'Toole: Thank you very much for your presentation and an interesting perspective. I just read with interest where you say here, "Products, by their very nature, inherently carry a bias." Ultimately, that's probably the issue. Technically, it's a push or a pull system.

Mr Prue asked some questions that were interesting. I know there's an ongoing concern about the accreditation or designations for the CAFP and these certified financial whatever. There are a lot of different designations out there that aren't accredited today. People put these little sticks behind their name, and all of a sudden they're an expert in everything. But in many cases they actually can't manage their own affairs. So that is an important standard—an acid test, if you will.

You say your key recommendation here is this national regulatory issue—the independent-minded, as you categorize it. It's just another fee-for-service issue from the client's perspective. All of us need some advice, whether it's insurance, wealth management, estate planning—all of the various products that are out there for people. And I totally agree with the sentiment of your presentation. Is that available today? I find people who are licensed are almost like tied sellers. If they're licensed to sell various mutual funds and things like that and they're a financial adviser, they have to be two businesses. I'm told that today they have to act almost in two different parts of their house if they're operating from home and have two different businesses, to be able to do that. Is that right?

Mr Howard: You've asked me a very complex question. In fact, you've asked me a number of questions. I'll take it back to two points of reference.

As you started out, I think what is missing today is the confidence of the consumer that the advice they're receiving is independent-minded. I think we are here today to address some of these issues and to reconcile them within the country. The fact is, to put it in simple terms, we don't believe that the solution lies entirely within the box. In fact, if the consumer is going to receive the confidence that their advice is independent and truly valuable to them, then it must demonstrate itself as being independent from the outset. If you build it upon the current regulatory system, you miss that opportunity.

There is a need, of course, to reconcile all the designations and so on. We have a plan for that but I don't have time today to go into that.

The Chair: Thank you very much for your presentation.

ERNEST WOTTON

The Chair: I would call on Ernest Wotton to come forward, please. Good afternoon. You have 10 minutes for your presentation. You may allow time within that 10 minutes for questions, if you wish. I would ask you to state your name for our recording Hansard.

Mr Ernest Wotton: Thank you, Mr Chairman. My name is Ernest Wotton. I know nothing about finance. I am by trade a lighting designer. I'm a fellow of four professional organizations. I have practised in Canada, in the United States and in the UK. I have taught my trade at leading schools of architecture across North America. I am 83.

In July 1999, I wrote to the Honourable Dalton McGuinty, then the Leader of the Opposition, saying:

"Not so long ago when you retired you received your '50 year' pin and a pension. Today you receive neither. Nobody expects to spend a working life with the same employer. Instead, one changes frequently.

"These frequent changes mean that you have to make your own arrangement for a pension. If, like most people, you know little about financial matters, you put the money you have set aside for a pension in the hands of a financial adviser.

"Suppose that your financial adviser does not invest in line with your instruction and you lose money. You may spend months in fruitless discussion with the adviser in an effort to obtain reimbursement."

My letter to Mr McGuinty, written over five years ago, did not end there. I will return to it in a moment. It begins when, in February 1995, my wife and I took a bundle of very solid securities and cash to a financial adviser employed by a leading investment firm. We asked him to manage an account for us.

As I said, I know nothing about managing money, but I can read a graph. The mid-1990s were a boom time for investment, yet a downward slope appeared in the graph of our portfolio. Every monthly statement from the investment firm directed its clients to make contact with their financial adviser if they had any questions. Accordingly, I wrote to our financial adviser and said that the downward trend in the value of our portfolio was a cause for concern. He stated that our portfolio was healthy. He also confirmed specifically that a particular security I named was healthy.

Then three things happened. Our adviser left the firm, the particular security became junk and the investment firm wrote that as we had written to our financial adviser, in line, you will have noticed, with the instructions on the monthly account, it "had no responsibility for" our financial adviser's statement "that the portfolio was healthy."

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I will not even try to outline my effort to obtain compensation. My correspondence occupies two binders, each three and a half inches thick. Some of the replies from the investment firm were marked "sub judice." I got no reply when I asked what this implied.

I drew to the attention of the president that his firm's newsletter referred to "the superb returns enjoyed over the past few years," and asked why I had not taken part in that bounty. The president wrote, "We remain committed to serving you with the best possible advice [and to] building strong relationships with our clients," but he omitted to send a cheque.

Meanwhile, I scouted for other ways to obtain restitution. I mentioned my letter to Mr McGuinty. He referred me to the Ontario Securities Commission, as did the Ministry of Finance. The OSC referred me to the Investment Dealers Association. From the time I wrote to the OSC, in line with the advice from Queen's Park, until the IDA hearing into what it referred to as "the matter," three years and seven months had passed. I learned that a number of other investors had also complained against our financial adviser. I was surprised, therefore, when IDA concluded that he had been correctly supervised.

At this point in my story my wife and I had been unable to get compensation for the enormous loss in our investment, and we were unable to take part in the arbitration process set up by IDA since our complaint fell outside its terms of reference. But the Ontario Ombudsman told me of the Ombudsman for Banking Services and Investments. Richard Bright of OBSI interviewed me and my wife and subsequently submitted his report to an arbitrator. We were awarded about 60% of our loss. Mr Bright's report identified a number of examples of investments obviously made without due diligence, yet they had eluded the investment firm.

May I summarize my conclusions arising from this sad recital of facts:

(1) An investment firm will not conduct a rigorous investigation into a complaint against its staff.

(2) An investment firm will use its enormous clout, including the use of legal terms in everyday correspondence, to wear down an investor, particularly the vulnerable.

(3) The provincial government has delegated to OSC its authority to protect investors from unfair or improper practices without ensuring that this authority is being exercised.

(4) OSC has delegated to IDA its authority to investigate complaints against financial advisers without ensuring that those investigations are swiftly and competently carried out.

(5) Neither OSC nor IDA has assumed the responsibility for ensuring that investors are compensated for their losses from investments carried out without due diligence. Instead, both OSC and IDA recommend that the investor take legal advice. OSC has stated that the average fee for legal advice is $37,500. This is far beyond anything many investors, particularly elderly investors, can afford.

(6) The March 21, 2003, review of the Securities Act of Ontario does not address the above issues.

(7) No investor, particularly the vulnerable, should have to go through the trouble and worry I had to go through, and that extended over eight years, in order to obtain relief.

In April 2002, the OSC mounted an investor education conference. About 100 delegates took part, representing 40 user groups. They broke into spontaneous applause only once: when a journalist member of a discussion panel stated, "The system is very wrong when one has to go to court for restitution. There must be another way. Companies must hold their employees accountable. Clients come first."

I was there. I noted this remark. I ask, Mr Chair, that you give it your urgent consideration. Thank you for your time.

The Chair: Thank you for your submission today. Regrettably, there is no time left for questions.

CANADIAN DEPOSITORY FOR SECURITIES

The Chair: I would ask the Canadian Depository for Securities to come forward, please. Good afternoon. You have 20 minutes for your presentation. You may allow time for questioning, if you so desire, within that 20 minutes. I would ask you to identify yourself for the purposes of Hansard.

Ms Barbara Amsden: Good afternoon. My name is Barbara Amsden and I'm the assistant vice-president at the Canadian Depository for Securities, or CDS. You have our letter and submission and a bit about CDS, which we like to consider one of Canada's best-kept secrets. We're the not-for-profit company standing between you and me as investors, making sure that wherever you are in the world and whoever your broker is in Canada, when I buy your shares, you get my money and I get your securities.

Our presentation will only cover highlights of our submission to you. Our focus is on recommendation 5 of the five-year review committee final report, the Uniform Securities Transfer Act, or USTA, and related legislative changes.

The USTA is distinct from the Securities Act. I think somebody yesterday mentioned that the reams of paper you're dealing with are enough to choke a horse. We hope to give you a small mouthful that you can digest. Not wishing to trivialize the other issues covered by the report, we can't emphasize enough the clear and present need for and the benefits that will arise from the USTA. We believe that the USTA can and should be separated from some of the thornier issues that you're going to be dealing with and that the USTA should be recommended by this committee for enactment on a priority basis, ideally by no later than the end of this year. We believe that this would be a signal achievement of this committee, one you could be proud of.

CDS's president and CEO, Al Cooper, extends his apologies for not being here today—he has to be in New York—and our general counsel, who waxes lyrical about this issue, has dared to go on vacation.

I am not a lawyer. I'm here to speak to you in business rather than legal terms. If you have technical legal issues, I'll follow up on them in writing after this presentation. While the legal matters and legal wording may seem complex, the business issues and the investor issues are not.

The best comparison I can come up with is the rotary phone. A few years ago, my mother asked my nephew, her seven-year-old grandson, to call his parents on her

rotary phone. He went to the phone and carefully started pushing the numbers through the finger holes that I used to dial without a second thought.

In some ways, I see the USTA as moving from rotary to Touch-Tone cell phones. It's not that the rotary phone doesn't work; it's that it's slow and there are risks in not moving on. Try getting through the maze of voicemail with a rotary phone in an emergency. You hang on the line, and even then, it's now only in rare cases that you'll get a live voice.

Our securities system is the same. It's not exactly that it doesn't work; it's that the risks in this particular area can be very high and are too high for us to accept any more.

The fact that you have such agreement on the USTA among lawyers, securities regulators and securities firms tells us something. With apologies to the legal profession present here, if you ask seven lawyers for an opinion, you'll ordinarily get 14 answers at least, and each will come with scores of caveats. Where I think you all recognize that agreement will be difficult to achieve with your colleagues not sitting on this committee is on the need to find a place for the USTA on the legislative agenda this year.

Some will consider the USTA legal mumbo-jumbo. Most will consider it mind-numbingly boring. Most will, in fact, believe that it ranks nowhere near as high as health care, education, the environment, consumer protection, taxes and others on the list of your priorities. But it does, both for Canada and certainly for us here in Ontario.

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Here in Ontario, a material percentage of the working population derives their jobs, their income and the taxes they pay into provincial coffers for things like health care and education from the financial services industry, directly or indirectly, from the many companies, small and large, that support that industry. These same individuals and companies also need the most efficient and safe capital markets possible in which to invest their savings and borrow to finance a variety of needs.

Canada's capital markets are part of our national competitive advantage. A huge part of this is our reputation for being economically stable, technologically sophisticated and reliable. With advances in technology, we are in a borderless world, not just within Canada, which I know is one of the issues you'll be discussing with other presenters, but also between Canada and the US and even globally. The Securities and Exchange Commission, in its recently published 2004-2009 Strategic Plan, notes that the "mix of technology, innovation" and worldwide competition "has helped to reduce costs borne by investors.... If trading costs had remained at their 1980 level, investors would have paid more than six times as much in transaction costs in 2003."

But for all the rewards that technology brings, it has brought some new challenges. Technology allows rumour and innuendo to travel like wildfire around the globe. A reputation built up over decades, and even centuries, can be damaged in seconds and can take years to restore. We don't want there to come a time when someone questions whether the Canadian capital markets are rock-solid because today, "If it don't seem broke, why fix it?" and because something looks "too technical."

We therefore need the USTA to provide a sound legal foundation for existing securities holding, transfer and pledging practices, particularly regarding the indirect system. That's the one we're most familiar with, where we never see our securities, everything is electronic and we just deal with our broker. The key principles regarding the USTA initiatives are the critical need for improved legal clarity and certainty; word-for-word consistency in the USTA and related amendments enacted in each relevant Canadian jurisdiction; greater harmonization with best practices globally; and implementation now.

While the USTA will contribute to fairness and transparency for investors and securities market integrity and efficiency, the USTA is not securities regulatory law, which regulates how securities are issued and traded and responds to inadequacies or abuses in securities markets, which are the issues of greatest concern to you. The USTA deals only with the transfer of property that occurs in the settlement of the trade, which is the exchange of securities for cash. And investors' only real interest is certainty; they want to be sure they get their money or their securities.

Implementing the USTA is a key part of broader efforts aimed at ensuring that Canadian capital markets do not fall further behind major industrialized securities marketplaces and remain as safe and strong as any in the world, and perhaps stronger than most. Current Canadian securities transfer rules are generally based on old versions of the uniform commercial code located in provincial business corporation statutes. Except in very limited circumstances, these rules were designed only for the direct holding system, where investors held their securities in certificated form.

The book entry settlement system is much more efficient than settlement by delivery of certificates and has enabled huge growth in securities trades. It would be virtually impossible to entertain a return to the physical environment in place when CDS was founded in 1970. Since then, shares traded have increased 106 times. Our securities legislation has not kept pace with the speed of technological change or with legislative change in other markets like the US.

While I have worked full-time for 25 years, I have never seen a certificate for any of the securities I have owned, other than a Canada savings bond. People not born 25 years ago probably have never seen a CSB certificate. They would be surprised to think there was any question at all regarding the certainty of settlement of their holdings, their ability to use electronic holdings as collateral for a loan or to have their broker lend securities on their behalf to earn a slightly higher return. We believe it is up to you and your counterparts in other

provinces and territories, and at the federal level, to make sure that the trust of these investors is not misplaced by ensuring that the protections are firmly entrenched in appropriate legislation. You can make sure that our marketplace remains competitive by bringing clarity regarding these protections. This is particularly important as global securities marketplaces increasingly have transactions involving multiple jurisdictions.

This is reflected in a number of reports that were referred to yesterday, including the G-30 or Group of Thirty report, the global efforts of CPSS-IOSCO—I won't give you the full words—the Canadian government's involvement in the PRIMA convention in The Hague, and Canada's participation in UNIDROIT, which was established under the League of Nations in 1926 to modernize and harmonize law between countries.

Our settlement is so invisible to millions of Canadians that many have never heard of CDS. Yet they place their faith in us to effect the transfer of their securities and payments, and the importance of uniformity in the implementation of the USTA therefore cannot be stressed enough.

CDS has recently sought legal opinions across Canada relating to the validity and enforceability of the security interests granted by our participants. Although we drafted our rules as being governed by the laws of Ontario, our participants, their clients and their issuers are located in all provinces and territories. While we take the position that Ontario laws apply uniformly to all transactions in our domestic systems, the result is not absolutely certain.

The opinion-seeking exercise was frustrating because of the subtle and technical differences between current legislation. The opinions were long and duplicative, not to say costly, dealing with many exceptions. By contrast, obtaining an opinion from New York legal counsel was straightforward.

In summary, there are three key parameters for effective enactment of the USTA. First, there's need for legal clarity and certainty. Not all federal and provincial laws reflect current commercial reality, and the laws of various provinces differ. The USTA will clearly establish the rights and duties of each player in the tiered holding system.

When current securities holding and transfer provisions were drafted, the situs of a security determined the applicable jurisdiction for the law governing the transfer or pledge of the security. Application of this in a world of bits and bytes representing uncertificated securities transferred electronically is much less clear. The USTA and conforming legislation will eliminate uncertainty and potential conflict.

We note as well that a major law firm in Canada has submitted that it has researched and debated with other major law firms legal issues associated with particularly securities transactions where legal uncertainty ultimately caused them to choose less than optimal forms of securities, move the location of the transaction to, for example, New York, or abandon it altogether. The USTA will reduce risk and cost, increasing the attractiveness of the Canadian jurisdiction.

The second parameter that I'll talk about is the need for absolute consistency in wording. As you can appreciate, subtle differences in wording can have significant impacts on the outcomes of legal rights and obligations. In this area, absolute conformity is critical. Wording variations will reintroduce risk and cost unnecessarily, and we're aware of no policy reasons why investors in one part of the country should be treated any differently or would want to be treated any differently from those in another part of the country.

Third, there's a need for harmonization of practice with the US and globally. One of the major benefits of the USTA and related changes is broad conformity with the US. This is clearly in line with commitments to UNIDROIT and the PRIMA convention, and by regulators to CPSS-IOSCO at the G-30.

You may still be asking yourself, "But why now? Why the rush?" Global market participants are increasingly aware of, and sensitive to, legal risk regarding attributes of national settlement systems, with the recent focus of these groups I've mentioned. We must reduce this risk by providing certainty.

We also believe there is extensive backing for the USTA by securities commissions, the Uniform Law Conference and many individuals and organizations. We are not aware of any opposition to the USTA and therefore do not consider it controversial.

Also, in view of the lengthy review and consultation that is already taking place on the USTA—without wanting to pre-empt your or the Ontario Legislative Assembly's responsibility to review legislation—we hope that you and your provincial and territorial counterparts will see no need for further changes. It's time to move to action.

In conclusion, the USTA and conforming amendments, similar to US provisions, are needed now. If the US could get agreement between 50 jurisdictions, we're sure that Canada's 13 jurisdictions can agree on this.

We're encouraging all relevant Canadian jurisdictions to move expeditiously to enact the USTA and related amendments word-for-word in their jurisdiction. The five-year review committee said in its report, "The need to update the legislation in Canada is clear and compelling. Canadian legislation in this area is currently out of step with legislation in the US and certain other countries. The legal foundation for the holding, transfer and pledging of securities is of fundamental importance to the clearing and settlement process, and to efficient and safe capital markets."

CDS agrees fully with these statements. And just because there are no widely known problems in our system doesn't mean they aren't there or that they can wait to be addressed.

We believe the USTA is a discrete issue that can be resolved easily and should not be delayed by debate of contentious items relating to provincial securities acts and regulations that will require more in-depth analysis and consideration. In the strongest possible terms, we request you to encourage your colleagues in the Legis-

lative Assembly to take the required measures on a priority basis, ideally by year-end 2004. This will lead the way for other provinces in keeping with Ontario's lead role in the securities industry.

Tell your colleagues that it's about time to move from the rotary phone to Touch-Tone cellphones and that, no, this can't wait, we can't stay on the line for the next available attendant. The USTA can't stay in line for a slow day on the legislative agenda. From what I can see, you will have no slow days in the next little while. The MPPs themselves should have an interest in this issue on behalf of their constituents as investors and as investors themselves.

I'd be pleased to answer any questions you may have.

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The Chair: Thank you for your presentation. We only have time for one question of about three minutes, a little bit more. In the rotation, this one question will go to the government.

Mr Berardinetti: Just very quickly, I want to thank you for your presentation. Just to understand, you support the concept of a single securities regulator, but you're saying that if we're going to do that, then the transfer legislation has to be uniform across Canada.

Ms Amsden: Actually, the two are distinct. I was told by the president that what CDS is is plumbing. I'm a plumber and I don't have any other opinions. What the USTA is and what has been developed is that there would be a word-for-word, identical USTA enacted in each province and territory across the country. So this can go ahead regardless of whether there is a national regulator, a federal regulator or a continuation with the current regulatory system. In fact, the individual regulators all support the USTA. That's one thing they did agree on.

Mr Berardinetti: I'll stop my questions there. I don't know if there's time for the opposition to ask any questions.

The Chair: Are there other questions? Thank you very much for your presentation.

Mr O'Toole: Chair, as a point of interest, that was recommended in Purdy Crawford's—it is fairly technical and it does take provincial legislation. I personally don't see a problem with it. It's administrative in nature, but you're going to have to drive it, because it's legislative time.

CIVIL LIABILITY COALITION

The Chair: The next presenter is the Civil Liability Coalition. Please come forward. Good afternoon. You have 20 minutes for your presentation.

Mr Robert Yalden: Thank you, Mr Chair. We've distributed paper copies of slides. If anybody would like to see them up electronically, we'd be happy to do that, but, in the interests of time, we're quite happy to move along and work with the paper versions.

Again, thank you, Mr Chair and members of the committee, for taking the time to meet with us today. I'm Robert Yalden, a partner in the law firm of Osler, Hoskin and Harcourt. We are Canadian counsel to the Civil Liability Coalition. With me on my right is my colleague François Janson.

I'm joined today on my left by Mr Ricciuto, who is assistant general counsel with BCE Inc. BCE Inc is a member of the coalition. It is, as you no doubt know, the largest telecommunications company in Canada. Mr Ricciuto is responsible for, among other matters, compliance with securities laws at BCE.

To Mr Ricciuto's left is Mr Epstein. Mr Epstein is a senior partner with the New York law firm of Shearman and Sterling. It's one of the leading Wall Street firms. Mr Epstein is a former federal prosecutor who, in the course of his distinguished career, has prosecuted violations of securities laws on behalf of the US government. He is now one of the US's leading class action securities litigators.

We've prepared written submissions for the committee, which I believe we've tabled with the clerk and will be distributed to you, if they haven't been already. We're going to do our best to limit our comments to less than 15 minutes in order to leave you with time for questions.

Let me start, then, with the first slide by explaining what the Civil Liability Coalition is. It's a group of Canadian companies. They include Alcan, BCE, Bell, EnCana Corp and Power Corp of Canada. These are companies, as you may know, that are listed on the Toronto Stock Exchange. They operate across Canada in a variety of economic sectors and play a key role in both this province's and the nation's economy. They are also very active participants in the United States' capital markets, an important point we want to come back to. They are therefore subject to regulation by the United States Securities and Exchange Commission.

The coalition supports the five-year review committee's report, in particular its conclusion that it's important that there be harmonization with respect to continuous disclosure requirements across Canada, and we support the report's call for civil liability for deficient corporate disclosure. We agree that this has a role to play in Ontario and other provinces in Canada. It's important that we be very clear about that up front.

However, the coalition does have some very serious concerns about certain aspects of the civil liability provisions that are contained in Bill 198, which was passed, as you know, by the Legislature, but has yet to be proclaimed.

Turning to the next slide, let me spend a second just reminding you what continuous disclosure is. There's actually a very good summary in the five-year review committee report. I understand that Mr Crawford, when he appeared before you this morning, walked through a description of it once again. Just to remind you, it's a process whereby companies release ongoing information into the market so that investors are always up to date on significant developments affecting that company.

The question is, what happens if that information is deficient? Historically, judge-made law, or what we

lawyers call common law, has not provided a strong foundation for claims against companies whose disclosure was deficient. Plaintiffs have had trouble proving that they actually relied on deficient disclosure when buying or selling. What Bill 198 is trying to do is remedy this by introducing a statutory remedy that removes the obligation to prove reliance.

But Bill 198 then goes on to reverse the onus of proof by requiring a defendant, the company, to prove that it took all necessary steps to ensure that its disclosure was not deficient and that the disclosure was not what caused the plaintiff's loss. Alcan, BCE, EnCana and Power are firmly of the view that these additional measures, the ones that reverse the onus of proof, go further than is necessary and will simply result in the promotion of unwarranted class action litigation.

I'd now ask Mr Ricciuto to provide you with more details on the coalition's position.

Mr Ildo Ricciuto: Thanks. Turning to slide 4, we now focus on the coalition's position. First, there's no question that the coalition believes that issuers must maintain the highest standards of disclosure in both their prospectuses and continuous disclosure, such as financial statements and annual reports. Second, I must emphasize that the coalition supports the concept of civil liability for misrepresentations and continuous disclosure. However, the coalition is very concerned with those aspects of Bill 198 that would result in Ontario having a regime that is not harmonized with the regime from the US.

Bill 41, which was introduced in May 2003 but not passed, was an attempt to bring some aspects of Bill 198 into line with practice in the US, but did not deal with the most serious issues of Bill 198.

Turning to slide 5, we must emphasize that one of the key premises underlying Bill 198 is really outdated. The source of Bill 198 is the 1997 Allen report, which recommended the introduction of statutory civil liability in Canada. However, one of the basic premises of the Allen report was that the plaintiffs' bar needed to be given exceptional tools to sue companies because securities regulators, in particular the OSC, did not have at that time sufficient resources to ensure compliance with continuous disclosure obligations.

Clearly, this premise is outdated. The OSC is now well-funded and, as the chair of the OSC mentioned yesterday, the OSC has administrative and criminal enforcement tools which can be and are being used to improve disclosure.

While the regime of secondary market civil liability also has a role to play in enhancing the quality of disclosure, there's no longer a case for the exceptional private right of action proposed in the Allen report and found in Bill 198, which unfairly reverses the onus of proof on defendants.

I will now ask our US counsel to deal with the US aspects of our submission on slides 6 and 7.

1400

Mr Jeremy Epstein: I want to thank the committee for hearing me. I've been asked to speak a little bit about the experience of US litigation with private securities litigation because we've had long experience with this. My understanding is that Bill 198 is intended to harmonize the Canadian regime of securities regulation with what exists in the United States and to afford Canadian investors with the same rights and remedies available to US investors. Unfortunately, it does not do that. As I read Bill 198, it affords Canadian investors much greater rights and remedies than what are available in the United States and it concurrently affords Canadian companies far less protection than what is available in the United States.

My remarks are going to cover pages 6 and 7, but I think it might be most instructive if the committee turns its attention to page 10, which is a chart that compares the proposed securities regulation regime under Bill 198 with what exists in the United States.

The simplest way I can address the differences is by pointing out that there are two salient distinctions between the elements required to prove a securities claim in the United States and what would be required under Bill 198. To prove a securities claim in the United States in private litigation, one must prove what's called scienter, which in lay terms means an intent to deceive or guilty knowledge that the statement one is making is false. One must also prove something called loss causation, which is to say that there is a clear connection between the alleged disclosure violation and any loss caused to the shareholders. Having laid out those two distinctions—both of those protections exist in the United States; they will not exist, as I understand it, under Bill 198—let me try to explain what this means in practical terms.

Over the last 40 years, the United States has seen a flood of private securities litigation, mostly in the form of securities class actions. There are several important safeguards built into the securities laws, however, that act as a deterrent to frivolous lawsuits, and one of the most important of those safeguards is the scienter requirement. What happens in the United States is that any adverse corporate event, be it a drop in sales, a drop in revenues, some industrial disaster that impedes production, is followed as day follows night by a securities class action. As long as there's a drop in the stock price, a plaintiff's lawyer will bring an action alleging not just that the stock price has dropped but that there has been fraud in prior public statements. The reasoning usually is, if something bad has happened to the company, the managers of the company must have known it or must have been able to see it coming and by not disclosing these dangers to the investing public they have committed fraud.

When these cases are filed, the first step that is typically taken by a defendant is to file what's called a motion to dismiss, which is a motion—and I'm told there are comparable procedures under Canadian law—that asks the court to dismiss the action at the threshold, before the company endures the cost of discovery and depositions and everything else that's attendant upon US litigation. A significant number of those motions to

dismiss succeed. In our longer, written submission, we estimate that 19% of all securities class actions are dismissed at the threshold. One of the principal reasons they are dismissed is because many of these cases cannot satisfy what's called the scienter requirement. The plaintiffs may be able to demonstrate the statement was made, and subsequent events perhaps have demonstrated the statement to be false, but that's a long way from pleading or proving that there was knowing falsity in the statement. That is a significant protection to American corporations, and it also provides a very effective way of weeding out frivolous actions at the threshold, before the significant expense of a securities class action is incurred.

I cannot estimate what the regime would be in the United States without the protection of a scienter requirement, but I can certainly venture an educated guess that, rather than 19% of securities actions being dismissed at the threshold, you wouldn't get more than 1% or 2% dismissed. That means that virtually every lawsuit filed that alleged fraud would go all the way through discovery and put a corporation through not months but years of document production depositions and would bring every single securities lawsuit to the brink of a trial or a settlement. This is a very expensive undertaking for any US corporation.

Very often, these cases turn out to be baseless. There's a well-developed body of law in the United States that says you cannot prove fraud through hindsight. In other words, if a company says in its public disclosures, "We've taken every safety precaution in our plans," and there's subsequently an explosion in an oil rig somewhere and production is stopped and the company's sales drop as a result, that does not make the statement in a public disclosure false. Nevertheless, those kinds of statements are routinely the source of lawsuits brought in the United States. Most of those lawsuits tend to be cut off at the very outset because of the scienter requirement, which is a valuable protection.

Similarly, the requirement of loss causation is also a valuable protection because it requires that there be some causal connection between the false statement and the drop in the stock price. Otherwise, a stock can drop for a whole variety of reasons, including overall economic conditions, but without the protection of a loss causation requirement, it would be presumptively proven that a drop in the stock price was due to the false statement. That, again, is a significant protection that seems to be lacking under Bill 198.

I'd like to close simply with the observation that the trend in the United States is very much away from private enforcement of the securities laws and toward more vigorous public enforcement of the securities laws. There was a piece of legislation enacted in the mid-1990s called the Private Securities Litigation Reform Act, which materially toughened the standards applicable to bringing private actions. At the same time, we've seen legislative developments like Sarbanes-Oxley and increasing use by the SEC of both civil and criminal lawsuits to coerce enforcement. It is my view, as someone who has practised in this area for a long time, that the threat of government enforcement is a far more significant deterrent to corporate wrongdoing than the prospect of private litigation.

Mr Ricciuto: Turning to slide 8, we deal with the reasons why the lack of harmonization of Bill 198 with the US is a significant problem.

First, it should be noted that Bill 198 represents a very important and unnecessary departure from law as it exists in the US for almost 40 years. Canadian issuers, like BCE, also listed in the US on the New York Stock Exchange are already subject to the US secondary market civil liability. So unless Bill 198 is harmonized with the US regime, it will put Canadian issuers at a competitive disadvantage by requiring they also deal with a distinct and even more plaintiff-friendly regime that will promote unwarranted class actions with all the waste of corporate funds and management time that they will entail. We believe this will push companies to settle claims having little or no merit.

Adopting a more plaintiff-friendly regime would also be out of step with other recent and important policy choices in the US that, as US counsel has just mentioned, have seen efforts to place limitations on its class action regime and to rely instead on enhanced SEC enforcement.

The coalition greatly appreciates and recognizes the efforts made by Canadian regulators to harmonize new Canadian corporate governance and disclosure requirements with the US Sarbanes-Oxley Act. However, it is critical, from a competitive point of view, for both Canadian companies and financial markets, that the same approach be taken when dealing with civil liability in Canada.

I'll turn it over to Robert Yalden.

Mr Yalden: In summary, the coalition thinks it's extremely important not to lose sight of the role that Chairman Brown described yesterday: the role that securities regulators and prosecutors can play and are playing in dealing with deficient disclosure. We think emphasis should be placed on those tools.

We agree with Mr Brown and Mr Crawford that it's time to get on with civil liability. We agree it has a role to play in Canada, that there are problems with Bill 198. Some of those problems would have been addressed through Bill 41. We've identified other problems in our written submissions that result from a lack of harmonization with the US regime and, in our view, will need to be addressed at the same time that the issues identified in Bill 41 are addressed.

We therefore recommend the government adopt amendments to Bill 198 to bring it in line with the regime in place in the United States. We've prepared quite detailed amendments, which are contained in one of the appendices to our written submissions, and in particular we'd urge the government to look at those seriously and enact them.

Thank you very much. We'd be pleased to take questions if there's any remaining time.

1410

The Chair: Thank you. We have time for only one round of questions, about three minutes, and in this rotation it will go to the official opposition.

Mr O'Toole: Thank you very much. I appreciate, on a technical area where heavy-duty legal advice—obviously, Bill 198 was not proclaimed through the regulations. The bill passed but the regulations didn't, so they introduced Bill 41, as you probably know, and it was addressed this morning by the author, Purdy Crawford, as well. In his initial report he had agreed with the intent of Bill 198. It might have been poorly drafted. The regulations were bogged down in consultation. So I guess Bill 41 is the current government's attempt to modify Bill 198. That's my understanding.

Mr Yalden: With respect, Mr O'Toole, I think in fact it was the previous government that had tabled Bill 41.

Mr O'Toole: Did it come in in the last session?

Mr Yalden: Yes, and it died on the order paper.

Mr O'Toole: Was I correct in the assumption that it was an attempt to modify this liability?

Mr Yalden: Yes, you are correct. It was an attempt to deal with one area in which Bill 198 was out of step with the United States.

Mr O'Toole: Were they trying to get with the Sarbanes-Oxley sort of version of this corporate liability—

Mr Yalden: The issue was actually quite a technical one in Bill 41.

Mr O'Toole: It's hard for us to understand, because even if you read the legislation you have to be familiar with the Securities Act, which it is amending.

Mr Yalden: The submission actually deals with Bill 41 in part. Bill 41, as I say, was designed to deal with one more limited problem, in our view, which was what was in Bill 198, and that was a requirement that before issuing either in writing or orally what we call forward-looking statements—so predictions, if you will—various disclaimers had to be recited. The concern that was raised was the notion that the chief executive officer, before giving, say, a call to an investment analyst, would have to go through a long laundry list of these things instead of simply referring to a written list of these disclaimers. That's the practice in the United States. Bill 41 was designed to enable the Canadian practice to be consistent with the US practice. So it was very limited in its objectives.

Mr O'Toole: Mr Barrett has a question.

Mr Barrett: You described the US experience, and given the globalization of so much of those trades, is there anything we can learn from British law or other countries?

Mr Epstein: I didn't hear the entire question; I'm sorry.

Mr Barrett: You described the US experience. Is there anything we need to know concerning other countries, given the global nature of this business?

Mr Epstein: I cannot pretend to be an expert in the securities regulation of other countries. I do know that there is increasing co-operation between the Securities and Exchange Commission and regulators in Europe because many securities offerings now are global. There's a piece done in the United States, but there are also pieces done in various other jurisdictions. More and more government enforcement is coordinated, as you are saying, certainly in the anti-trust area as well. I think there are coordinated efforts, but every regulator is limited by the remedies available to him in the particular country, and the remedies now in the United States are quite extensive. I do not know if they are as extensive in other regimes.

Mr Yalden: If I can just jump in there, Mr Barrett: Again, in our written submissions we point to the experience in Europe where currently people are looking at the question of the balance between civil liability and public instruments such as securities regulators and prosecutorial mechanisms. We think you'll find in those submissions that the trend in Europe is the same as in the United States, which is away from relying on civil liability class actions. It's toward beefing up the enforcement power of regulators and prosecutors.

The Chair: Thank you for your submission this afternoon.

LARRY ELFORD

The Chair: Now, for the committee, we have a teleconference with Mr Larry Elford. Good afternoon, Mr Elford. Are you on the line?

Mr Larry Elford: Yes, I am. Am I coming through clearly?

The Chair: Yes, the committee can hear you. You have 10 minutes for your submission. You may allow time for questions within those 10 minutes. I would just ask you to state your name for the purposes of Hansard. You may begin.

Mr Elford: Thank you very much. My name is Larry Elford. I'm going to get right to the point because I understand your time is limited.

I worked for about 20 years in the investment industry, dealing with the average clients on the street, retail investors. I rose to the top of my profession in educational and ethical awards and things like that. I managed approximately $100 million or close to it. I'm now retired. So I feel able to speak on the industry from an inside point of view.

I had the luxury of being rather successful in my industry and I was able to spend the last five or 10 years questioning and probing for higher ethical standards, seeing things from the inside that I didn't particularly like and trying to improve them. I thought they gave the industry a black eye. My questions and attempts at improvement were not extremely welcomed, so I've come to the conclusion that the industry is largely out of step with those it promises to serves. It's interested at times in serving itself—or certainly some advisers are—at the expense of often trusting clients, often very vulnerable clients, uninformed clients for sure, and the majority of the time I find it's elderly clients.

If I were to stick my neck out, I would say it's a unique form of elder abuse that certain investment advisers are able to practise. They're able to identify that some elderly members of the Canadian investment community have the most money they've ever had to deal with in their entire lives and they are uniquely uninformed and in a position of trust. When I find that trust abused I'm really quite offended.

The title of my presentation is "The Industry is Serving Itself; Who is Serving the Canadian Investor?" I'm going to jump to page 11 of my submission. Just to make sure I don't run out of time, I'm going to give you my conclusions. There are four of them. Then I'll go through some examples or issues. The four conclusions to my presentation are:

(1) I believe that the Investment Dealers Association should be eliminated from any role whatsoever of a self-regulatory nature. They are an industry trade association and, as such, they are interested in the benefits and the protection of their members. They are, in my opinion, equivalent to allowing the foxes to watch the henhouse and they're not doing the job of protecting or compensating the public—to see the mandate of the IDA, written, is to protect investors—and based on my 20 years in the industry, I find that sad.

(2) Enact the Ontario Securities Commission fair dealing model, which I find to be a very well-thought-out, comprehensive set of proposals that would help clearly define the role between adviser and clients, leaving less room for ambiguity or wiggle room for unethical advisers or firms.

(3) I'd like to see a client advocate in this country. I'd go so far as to say, where is the investment clients' association? I see investment dealers' associations, I see the mutual fund dealers' associations; I see nothing in the form of a clients' association. It's people in the industry writing the rules for the industry, and I would like to see something at arm's length from the industry to protect clients.

(4) Last but not least I'd like to see, or I'd advise, a move toward a single regulator in Canada. Any claims to the contrary I think is self-interest, job preservation and is not in the public interest. I don't think we need 13 regulatory agencies in what I have heard is an economy the size of that of Texas.

On to the presentation: This industry was set up decades ago in, I imagine, private men's clubs on Bay Street, with people writing their own rules for the business way back when it was loosely forming.

I find the set-up is perfect for unethical members of the industry, of whom there are a few. They are very well rewarded for taking advantage of trusting clients. Punishment is slim to none. In fact, in some very good attempts at elder abuse or financial abuse of some clients, I see people being awarded vice-presidential designations and titles like that at some of the major investment firms.

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There is an entry requirement of a three-month correspondence course, the Canadian securities course, to enter this business, and investment people can be making a quarter to a half million dollars in a number of years in the business. I find that the money is simply too great and the entrance requirements too low for many to even understand what the meaning of duty of care to clients is from a professional to a client.

I'm giving some examples in the form of short stories, submissions or articles which are in my table of contents at the front of my presentation. The first one, on page 2, is a discussion of, is the investment relationship that of buyer beware? The industry, in my two decades within it, promised a high duty of trust and care and integrity, and the advertising certainly promises that the client will come first. I found numerous cases where, when push comes to shove, major high-quality investment firms have said, "I'm sorry, but we do not owe you a duty of care." I find that saddening, to say the least, and shocking, to say the most. There is an article or a submission about that.

The second one, page 5, is a discussion of double-dipping. It shows how investment people can apply two or three commissions or earning streams from one single mutual fund purchase. This is done without disclosure to the client. There is nothing in writing that clients have potentially three forms of commission. They could dig up two of them if they're willing to read a 200- or 300-page prospectus, which not many do. I've had one client uncover this situation and bring it to question to their investment adviser and as far as the IDA. They were told in writing that because they received a discount on the third fee, they should be quite happy to have paid three different fees to their adviser, unknowingly. I find that unacceptable.

Page 7, on rules to protect clients: Since we in this industry write our own rules and interpret and judge our own rules, we're certainly able to ignore any ones we see fit or enforce those we'd like to. I've seen many rules that were intended to protect clients ignored and rules that are there to the benefit of the industry enforced. I find it very haphazard, arbitrary and self-serving, and there is an article or a submission about that.

The industry now has a self-reporting system, so claims of wrongdoing sometimes have to be reported to the very people who may be benefiting from the wrongdoing. This is unacceptable. If the complaint is serious and raised to a higher level, it can sometimes be passed along to an industry trade association, which is by the industry and for the industry, and in the end the client or the complaint gets not much satisfaction, in my experience.

I again want to know where the investment clients' association is. We have a system that is perfect from the standpoint of someone who wishes to get away with things. It is, in my opinion, useless for an employee or a client who wishes to speak out to improve the system or to complain.

I'll move along to page 8 of my submission, that advisers may actually be salespersons in advisers' clothing, and a discussion of how advisers are using the guise of advice to place clients in the highest compen-

sating investment choices to themselves, again without disclosure, without transparency.

Last in that table of contents, page 9 discusses a code of silence, which in the industry is written as well as unwritten at some of the major firms and gags employees from open and transparent discussion of any kind on any issue with risk of losing their job. Several times I've seen the industry code of silence take precedence over our industry code of ethics. I've seen it used to cover up mutual fund incentive trips. I've seen it used to cover up double-dipping and competitive investment pricing, in opposition to the Competition Act. It simply means that thou shalt not speak out or you will be labelled a non-team player and things will get kind of tough for you.

Our industry has a long way to go. The Investment Executive magazine from August 2004, this month's edition, says the problem is that there is not enough transparency and accountability among regulators; it's time legislators let in the sun. This is our own industry writing on how embarrassed we are at times with the state of self-dealing and self-interest.

That may be my time. I'm certainly prepared to answer questions. Thank you very much for spending your afternoon indoors listening to this kind of thing.

The Chair: Sir, you've landed right on the 10-minute mark. There is no time for questions, but the committee thanks you for your presentation.

Mr Elford: Thank you very much.

The Chair: The committee should know that the 2:20 presentation has cancelled.

ONTARIO BAR ASSOCIATION

The Chair: I would ask the Ontario Bar Association to come forward. Good afternoon. You have 20 minutes for your presentation, and you may allow time for questions within that if you wish. I would ask you to identify yourself for the purpose of our recording Hansard.

Mr John Cameron: Mr Chair, honourable members of this committee, my name is John Cameron. I am a corporate lawyer practising at a Bay Street law firm. I'm here speaking on behalf of the Ontario Bar Association, my law firm and as a concerned citizen.

I'm speaking about only one issue, and that is the recommendation made on page 50 of the report, which urges all provincial governments in Canada to adopt a Uniform Securities Transfer Act. Canadian securities administrators published on their Web site in June of this year, subsequent to the preparation of the report, a draft Uniform Securities Transfer Act. The Ontario Bar Association and my firm strongly urge the Ontario government and each government in Canada to adopt that legislation in that form.

That legislation deals with several problems, the most important of which is that Canada's laws governing the transfer of securities are badly out of date. Our laws are based on the 19th-century concept that, to transfer shares, you deliver possession of a share certificate, and if you want to borrow money on the security of shares, you give the lender a share certificate. That's a very simple process. A share certificate looks like this. If I want to borrow money on it, I take it and just sign my name on the back and give it to my lender in exchange for some money. The lender takes that share certificate and knows that it's got a better right to that share than anybody else in the world.

A long time ago, the laws worked beautifully to do that. You can still do that today, if you can get your hands on a share certificate. The problem is, the system is set up so that you can't get your hands on a share certificate. The system makes it difficult for you to actually get a share certificate. Instead, it all happens now by computer, by the push of a button.

While our systems for physically transferring shares have been modernized, our laws haven't. The problem this creates is one for lenders, and therefore it's one for borrowers. From the lenders' point of view, they don't want to lend money on the security of a share certificate unless they know they're going to rank ahead of everybody else in the world. The current laws don't give them that comfort. The borrowers care about it because either the lenders won't lend them the money on the security of that share certificate or they're charged more money for doing so. I've seen lots of deals where lenders just won't do the transaction because the laws are too unclear.

I've been practising law now for over 20 years. I've seen it in my practice year after year, and I've canvassed people in preparation for coming to speak to you today. I've got numerous examples where people have told me this.

1430

The solution to this problem is easy, and it's not politically costly: You adopt the Uniform Securities Transfer Act. This act makes sure that the lender has the same priority as if it had physical possession of the share certificate. This act also has rules to say whose laws apply where you have connections to different jurisdictions.

That's pretty common in today's world. If you have a borrower in Ontario and a lender in New York, the new act is going to make clear whose laws apply. It's the same thing if the borrower is in Alberta and the lender is in Ontario.

In short, this new act is going to let people deal with their banks and other lenders a lot more easily than they can under current laws. This is going to have two effects. First, it's going to reduce the legal fees on these kinds of transactions. The laws now are so unclear that you get lawyers from firms like mine sitting around jabbering all day long about what it all means. The longer lawyers talk—and today is an exception because nobody's paying for me to talk—you all know that costs money. At the end of the day, one of two things happens: Either the lawyers can't agree, or there's too much risk for the lender and the lender doesn't want to do the deal or the lender is going to charge more money. No matter how

you slice it, the borrowers are paying. The borrowers pay for the lawyers to sit there talking about it or they also pay because their lender charges a greater interest rate or more legal fees.

When you adopt this act—and I say "when" because it is surely just a matter of time. The United States fixed this problem 10 years ago in something called revised article 8 of the Uniform Commercial Code. The proposed Uniform Securities Transfer Act is based largely on that drafting. It therefore gets the benefit of the experience that the United States has had with these laws over the last 10 years.

So I say "when this kind of legislation is adopted," because it needs to be adopted. There's a problem that needs to be fixed, and it's so easy to fix it.

When it's adopted, please adopt it in a way so that it's uniform across the country. In other words, adopt the version of the USTA that's on the Web site of the Canadian Securities Administrators, because there are no policy choices to make here. This isn't sexy stuff. It's just a bunch of backroom law to govern stuff that's really basic. There aren't real choices to make with this, and the language should be the same across every province. It's not controversial; this is motherhood and apple pie.

This is like fixing the potholes in our roads which cause people's cars and trucks to break down and have to be fixed, or which cause people to choose different routes or to go to different cities because they don't like the potholes in our roads. Unlike the potholes in our roads, this is a lot easier to fix. It doesn't cost money to fix it. You just have to pass this set of laws, and it will go a long way toward fixing it.

There also need to be amendments to the Personal Property Security Act. The Canadian Securities Administrators know this. They've published those amendments too on their Web site. A committee of some of Canada's leading experts in that area of the law have studied those amendments and commented on them. Their comments have been incorporated in a process that's happened over the past couple of years.

So you can take a high level of comfort from two aspects of this: one, the laws are based on the US solution, which has worked there; two, some of Canada's leading experts have looked at the changes that need to be made to the Personal Property Security Act.

In summary then, our laws are badly out of date. This is costing Canadian businesses money. The solution is easy—it doesn't cost anything—and that is to adopt the USTA now.

The Chair: Thank you very much for your presentation. We have about four minutes per caucus left. We begin this rotation with the NDP and Mr Prue.

Mr Prue: Thank you for your presentation. It's very narrow. It's just on the USTA. That's all. Does your firm or you or anyone else you're speaking for have any aspect you want to discuss other than the USTA?

Mr Cameron: No. I'm commenting on what I know best. I've done this kind of law for over 20 years. This is a problem that just needs to be fixed. It's so frustrating to see bills going out to clients. I think it gives lawyers a bad name when they let stuff like this sit around, where the clients have to pay—it's just that the laws are out of date; they just need to be updated. That's why I'm here to speak about this issue today, because this is the one I know about.

Mr Prue: OK. There are some 75 recommendations before us. You're confining it to just the one.

Mr Cameron: That's right.

Mr Prue: I have no further questions.

The Chair: We'll move to the government and Ms Matthews.

Ms Matthews: I must say that I appreciate the way you made your presentation so very clear and your arguments so concise and confined to something we're reviewing. We've heard from several people the same persuasive arguments that we should move forward on this. Maybe it's not fair to ask you this question, but other than simply time on the legislative agenda, are there any other reasons we should be cautious about this? Who will be unhappy if we proceed with this?

Mr Cameron: I don't think there will be any stakeholders who are unhappy. I think those people who don't understand the new law, who are trying to understand it, will want time to try to get familiar with it. But there's been a lot written in the United States about how to interpret these new laws and how they work. So there's a large body of commentary that people can look to.

I haven't heard anybody object to the new act. I don't think there's any valid basis to object to it. I think it's a new set of laws, and if there are people who say, "Let's move slowly," it will be people wanting to try to understand it.

This is a process that's gone on for 10 years already. Eric Spink, who's been mandated by the Canadian securities commissioners to work on this, has been working on this project for over 10 years, consulting with all kinds of experts both in Canada and in the United States, so there's been a lot of thought that's gone into it. I don't think this has been on the radar screen of most people in Canada, for obvious reasons.

Ms Matthews: I can tell you, I have not had one constituent call me on this.

Mr Cameron: And I don't think you ever will. That's what's frustrating about this issue and why I wanted to come today. I don't think people are going to speak up and say, "Let's do something about this," but something needs to be done about it, because our laws are broken and can be fixed, and it will save people money.

The Chair: We'll move to the official opposition and Mr Barrett.

Mr Barrett: You're focusing strictly on this issue of transfer of property during trades, and I recognize how important that is, because we're talking about billions of dollars of property moving back and forth.

About an hour ago, we had a presentation from the Canadian Depository for Securities. The Canadian Bar Association—would you have the identical position to their position?

Mr Cameron: I didn't hear what they said an hour ago, but I have met with representatives of CDS in weeks gone by. I've been following this issue over a period of months and a couple of years, and I'm generally familiar with their position. As I understand it, they are completely in favour of this legislation, and if that's what they told you an hour ago, then I agree with them.

Mr Barrett: This would impact solely on Ontario and provincial legislation, and not federal?

Mr Cameron: There's an interesting constitutional debate that has been going on a little bit. A couple of law professors have expressed different views about whether the federal government could or could not do it. It's clearly within the provincial government's jurisdiction. It's something I don't think the provinces would willingly give up to the feds, and so I think they should go ahead and do it. There is an argument to be made that the feds could do this by themselves.

The Chair: Mr O'Toole.

Mr O'Toole: The Wise Persons' Committee said they could do it, but you're right: There's a sense of revenue loss here provincially. They have to work out who gets the money: the fees, the licensing and all that. The money part of it is where the big issue is, and I don't think that's really been made clear to us as committee members. What is the revenue? That's a question for research that I'd like to get. What was the annualized revenue to the OSC or the organization that's delegated authority by the province? What's the revenue loss to the province, annualized?

Mr Cameron: The issue I'm addressing is the Uniform Securities Transfer Act, which does not raise any revenue. It's completely neutral. I don't know the answer in that other sphere.

The Chair: Thank you for your submission.

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DOUCET McBRIDE LLP

The Chair: Now we have Doucet McBride.

Good afternoon. I would ask you to state your name for the purposes of Hansard.

Mr John Hollander: Good afternoon, Mr Chairman. My name is John Hollander. I am a trial lawyer working with the law firm of Doucet McBride in Ottawa.

The purpose of my presentation is to address what I see to be a major failing in the regulatory scheme as it affects relations between the securities industry and the public, and to propose solutions to that problem.

The interface between capital markets and the private investor is the financial adviser. Financial advisers are not required to obtain much in the way of formal training, and nothing with respect to portfolio management. If the industry decides that poorly trained sales staff are to be allowed the freedom of advising private investors, then, in my view, the industry should pay the losses when the advice provided is not suitable for those investors. This should be a cost of doing business, by reason of their failure to invest in proper training and supervision. In other words, it appears to me that loss prevention and compensation are alternative strategies and the industry has chosen compensation as opposed to loss prevention.

Unlike the royal medical colleges and my own law society, the IDA and the MFDA are not statutory authorities. Rather, they are industry groups that deal with their members. When a private investor contacts either the IDA or the MFDA to complain about losses arising from what they see to be unsuitable trading advice, the investors assume both impartiality and expertise on the part of the organization. Unfortunately, in my experience, both of these assumptions are unfounded and lead to the abandonment of otherwise valid claims.

To establish my own credentials and my apparent bias, let me introduce myself. I have worked for 26 years in the practice of civil litigation and currently practise with a mid-sized litigation boutique—it has 12 lawyers—in Ottawa. I represent several clients with claims against investment and mutual fund dealers for allegedly unsuitable portfolio advice. I maintain a Web site devoted to this area of my practice, which is called Stockloss.ca, and I've been the subject of several articles in various national and Ottawa press. I've flown from Ottawa to make this presentation.

As an aside, I can say I represent the database to support the submissions the representatives of the consumers council were making. The consumers' council was making broad-stroke statements about what private investors are confronting. What she was talking about are my clients, and I'm going to be talking about their experience today.

As another aside, the committee, by and large, has been hearing witnesses who talk about the broad picture. What I will be talking about affects each and every one of you to the extent you are investors. What I will be saying will resonate with each one of you to the extent you have lost money in the markets in the last few years or in one of the previous bear markets. All of you have aunts, uncles, sisters, brothers, parents who have been involved in similar situations, and what I am going to say is going to strike home very closely to most of you.

I either currently represent or have already settled claims for 33 distinct clients. I count the claims of a family as being a single client. I have ongoing investigations concerning several others. I accept as clients approximately one third of the people who approach me for an opinion. Most of my clients have retainer agreements by which I am compensated only in the event of success of the claim; in other words, contingency fees. I can confirm that very few of my brokerage negligence clients would have hired me otherwise. I instituted a practice of trying to get a small amount of money to cover my disbursements—I have to pay for an expert fee; I have to pay an accountant to prepare bookkeeping ledgers. Clients would not even pay the $3,000, $4,000 or $5,000 I pay out of pocket in order to reach an opinion. It is a very, very gun-shy public out there.

While it is difficult to provide a precise profile of my clients or of their claims—of course, there are 33 differ-

ent ones—I can provide some statistics. The average amount of capital lost by each distinct client—remember, families are one client—is approximately $175,000. I represent primarily Ottawa-area clients, but not only. I've got clients in British Columbia, the Maritimes and a few in Toronto. The numbers will differ based upon the regions, I expect, although I don't have enough data to support that. Overall, my clients' average loss in capital is $175,000, and the period in which they lost that money is a few years.

The average age of the clients is at or near retirement. We are not talking about 30-year-olds who are losing $30,000. We are talking about people who have retired or are looking straight in the face at an early retirement or a nearby retirement, and they've now lost their ability to retire as comfortably as if they had never met the broker in the first place.

Approximately half of the claims are directed against the brokerage arms of chartered banks. I have not looked at market share nationally. I don't know whether that is reflective of market share, and I have no opinion respecting that.

The other half of the claims of my clients is directed approximately equally against other stock brokerage firms, or investor dealers, as they're called, and mutual funds dealers.

I want to talk about the nature of the claims specifically. These are suitability claims. I want to stress, at this point, we are not talking about putting people in jail. We are not talking about unethical conduct, unscrupulous conduct, blatant elder abuse. I'm not talking about churning. I'm not talking about conflict of interest or putting money in your brother-in-law's pet project. I'm talking about bad advice—honest, bad advice. Every professional you ever meet is going to admit, in private, to having given bad advice. I am representing clients who have suffered from bad advice.

The first area I want to discuss is setting risk tolerance. That is the benchmark. Before an investment becomes appropriate, you have to know against what background the investment is to be judged. In almost all of my cases, clients have said that the adviser did not provide any advice with respect to the investment goals and risk tolerance that ought to apply.

In many cases, expert witnesses that I have had to retain have expressed the opinion that the clients' actual risk tolerance was far less than that indicated in the account application forms. The forms are called KYCs, for "know your client." That means that the broker, in order to give suitable advice, has to know who the broker is dealing with. Is the broker dealing with a 55-year-old woman who is going to need an income from her investments five years from now? Is the broker dealing with somebody who has a tremendous amount of money in five jurisdictions? The rules are different for each person. The client has to have that client's particulars known by the broker. The broker then amasses that and says to the client, "You have a tolerance for X risk and X as a goal of either growth or income."

Accurate KYC information is required by both the IDA and the MFDA in their charters and by Ontario Securities Commission regulation. It obliges registrants, which would be the brokers and the mutual fund dealers, to conduct reasonable investigations to ascertain the general investment needs and objectives of the client and therefore the suitability of each proposed transaction. The courts have ruled that financial advisers owe their clients the duty of care to give advice with respect to appropriate investment goals and risk tolerance. What I'm saying is obvious, but the courts have recited it as well.

Does it make sense for a patient to tell his or her doctor the diagnosis so the doctor can then prescribe appropriate treatment? Do I go to my doctor and say, "I've got polio. Treat me"? No. I go to my doctor and say, "I feel badly. Here are my symptoms." The doctor puts me through a battery of tests, asks me a bunch of questions about myself, my parents, my living style or whatever, and then, as a result of all of those facts, the doctor tells me, "I'm sorry, Mr Hollander, you've got polio. Here's what we're going to do about it."

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The exact same analogy ought to apply to brokers. My clients have gone to the brokers and said, "Here's what I have. Here's what I earn. Here's what I want to accomplish in three, five, 10 years. What do I do about it?" The broker then says, "What is your risk tolerance?" The clients have no clue. What's risk? It's never explained. My clients are saying that the broker is asking the client for risk tolerance: "Tell me how much risk you're prepared to take on." My clients are saying, "I signed where I was told to sign. I don't know any more." When I question the clients, they don't have a clue what "risk" means. If a client wants to retire rich, but cannot save enough to reach that goal, then the adviser should tell the client this fact: "I've reviewed your expressed goals; you can't make it. You should accomplish this instead," or, "Let's talk about what you should accomplish." That's not what the brokers are doing, according to my clients.

The next area I want to talk about is called solicited trades. "Solicited" means the broker goes to the client and says, "I think you should buy this." "Unsolicited" is the opposite; the client goes to the broker and says, "I heard about this. I want to buy it."

After setting the goals and the risk tolerance, the investment adviser moves to portfolio recommendations. The adviser is presented with a portfolio of securities, transferred in from another brokerage perhaps, or newly invested money. The adviser should recommend steps to align the portfolio with the goals and the risk tolerance so that, just by way of example, a working investor nearing retirement can draw the income likely required on retirement.

What I see routinely in my cases is that the adviser recommends that their clients buy individual stocks or groups of stocks in mutual funds dedicated to a specific sector—tech, health care—investments which the clients cannot understand and the adviser does not take the time to explain.

Are these recommendations suitable for the client? That's what the KYC requirements in the Ontario Securities Commission's regulation requires. The court also mandates that the adviser has to provide suitable advice and provide the client with both the negatives as well as the positives about each investment decision: "Well, maybe you shouldn't buy Nortel, because it's awfully volatile and you can't afford to take the loss." Brokers don't do this, according to my clients.

Risk of loss in individual stocks or individual sectors, high volatility, concentration of securities, high management fees, as have been identified in some cases: These are all factors that should be discussed. My clients are reporting that their advisers routinely do not fulfill this function.

My clients also report that their advisers hold themselves out not to be salespeople of securities but as portfolio managers, financial managers. Look at the advertising; that will say it all. You can look up any of the big brokerage houses and they say, "We're your financial adviser." "We're you one-stop solution." "We have all four corners" or all four pillars—you've seen the ads; you've seen the bells and whistles. You have not seen the underlying delivery you've heard other witnesses talk about. These people are salespeople. They're rewarded for sales. They're rewarded for the turnover of their book. They are not rewarded for their clients making the appropriate investments and making money the old-fashioned way.

So when I question the adviser in the court process, the adviser maintains that this adviser is, in fact, knowledgeable about portfolio management. "Yes, I know that Nortel is such and such, and I've done the research. I've looked at my firm's analysis, and Nortel was appropriate for this client." But they cannot point to any training that gives them any expertise in portfolio management other than having been in the market.

Some of the people I'm pursuing have less than six months in the market. They have not been through one, much less three, bear markets. Looking around the table, most of the people here have been through two bear markets.

Interjection.

Mr Hollander: I was polite. Most of the people I'm looking at have not seen the 1990 bear market.

Doctors, accountants, engineers, architects—I blush to say, lawyers—we all have many years of formal training in university. We then have an apprenticeship program. If you go to one of the big Toronto Bay Street firms, they won't even let you touch a file until you've been in the firm for several years. You cannot do damage to the public until you are trained.

I took the Canadian securities course. I studied for it in the time it took me to make my presentation to the jury and the time that the jury came back with a verdict. This many hours: two. That's what it took for me to get through the Canadian securities course. There is half of one chapter dealing with things that you would consider law. I have an advantage over people who are not lawyers and are preparing. There are 12 chapters. It took me two hours. This is three months of home study. You can do it in two hours.

Once you've completed that, you then do what's called the Conduct and Practices Handbook. I have not done that. I have the handbook and I've read it. It does not take very long to complete that. You can then cause damage to a seven-figure portfolio. You're relying upon the supervision of people above you who are incented not to make you have the right decisions, but they are incented to have you sell lots of product. They are incenting you now to sell managed product so that you get 2.5%, 3%, or 3.5% of the investment per year in fees. That's where the incentives are.

In my experience, people follow incentives. Professionals—lawyers, doctors, accountants, chiropractors, nurses—do not follow the money incentive so much, because they are trained in other methods of acting. They have a different ethical base.

I heard someone say that there's no Hippocratic oath with respect to financial dealers. That's not true; there is. All of the institutions, whether it's the IFIC or the MFDA, have ethical standards. They are just simply not followed.

In my submission, the lack of training on the part of brokers does not contravene any regulatory requirement. They only have to complete the Canadian securities course, the Conduct and Practices Handbook, and not be guilty of a felony over the previous five years, and they qualify. That's not the breach on the part of the financial institution; that's a breach on the part of whichever regulator is setting the bar. The bar is set too low.

In my submission, as long as the brokerage house, whether it be a bank or another brokerage firm, is big enough to sustain the loss, that is their risk. But the flip side is, if you're not going to spend time on loss prevention, then you have to make good the losses. They don't.

I next want to talk briefly about unsolicited trades. Frequently, a client already has a security or wants to procure another security outside of the apparent objectives and risk tolerance. We all know recent examples of Nortel and JDS. Ten years ago, it was Bre-X. Twenty years ago, it was Avon and other stocks. There's nothing new about irrational exuberance. If the client requests that the adviser buy a specific stock or fund, then the rule is that the adviser is obliged to provide "appropriate cautionary advice": "Don't buy the Nortel. It's wrong for you." It could be whatever. You explain what's wrong. My clients routinely deny that their advisers have done so.

What happens when there's a deviation from the KYC profile, the know-your-client profile? In some cases, the investments that are recommended by the broker have deviated from the risk profile as set out in the KYC. For example, the profile says "medium risk." Well, what is medium risk? Financial advisers receive no training in portfolio management. There are no guiding principles of what is medium, as opposed to high, as opposed to low

risk. I've seen portfolios which are 100% income identified as medium risk, and vice versa.

There is no applicable benchmark. Could it be that buying all Nortel stock in one portfolio is medium risk? Is it possible that Nortel at $120 a share is medium risk, but at $5 a share is high risk? I've heard that exact testimony. If the portfolio consists only of securities in technology or only of a mutual fund that does so, is that medium or high risk? I have heard competing testimony from brokers on that point.

My clients routinely report that the trades in their portfolios were offside the recorded KYC profile. They were really offside what the KYC ought to have been. So the broker records it as medium, and you're looking at it, and it cries out "high." Well, maybe it became high because the market changed. Everybody thought Nortel was a great, safe stock to own when it was $120. Suddenly, it drops by 50%. Brokers told their low-risk clients to buy more—average down. That is a safe method of dealing with things.

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The Chair: I want to remind you that you have about one minute left in your submission.

Mr Hollander: I have three concerns, and the three concerns are this. The IDA receives complaints routinely. Those complaints deal with, "I lost money. My investment advice was bad. What do I do about it?" Well, the IDA routinely gives them a legal opinion—"You have no claim because of"—and provides the reasons why. I've got a problem with that. First of all, they are the industry representative. They don't disclose that they're the industry representative. They're in conflict. Second, they're not lawyers. It's not a lawyer writing the letter, but it's a legal conclusion. Third, they are discouraging the client. These are clients who then come to me, and I've got the letter from the IDA saying that they have a bad claim, and I then settle it with the broker for large money because it was a good claim.

What about all the people who get the letter from the IDA and say, "Well, they told me I have no claim. I'm not going to go to a lawyer, who's going to be very expensive"? They don't know that contingency-fee lawyers are an option. They are therefore discouraging claims at the expense of clients who do not know better.

Last, the process of submitting claims for review by the IDA and by the Ombudsman takes such a long period of time that the new Limitations Act may prevent the claims from proceeding; they may become statute-barred.

So I have three recommendations. First, clarify the role of the industry organization. They are not regulators; they are trade organizations. Second, raise the standards for registration. There are chartered financial analysts; I've never had to pursue a claim against one. Third, where the IDA, the MFDA or the Ombudsman deals with claims from private investors, they should state in clear language that they represent the industry and not the public, that their opinion is not cloaked with legal authority and that the client should get expert independence from someone who is not beholden to the industry.

Thank you for your attention today.

The Chair: Thank you for your submission.

Mr O'Toole: Chair, just quickly for the researcher, I wonder if they could begin drafting a list of acronyms. We're getting pretty much buried in them. I'm thinking we can remember most of them, but we need to have a list of acronyms.

The Chair: Research has advised me that there are definitions in this report.

Interjection.

The Chair: But there's more?

The researcher wants to talk to us about some other points as well. So we are advised of the request for acronym help.

MARTHA COADY

The Chair: Martha Coady. I would ask you to identify yourself for the purposes of our recording Hansard. You may begin.

Ms Martha Coady: Thank you, Mr Chair. My name is Martha Coady. I live up in Arnprior, Ontario. Other than Ms Matthews, whom I met years ago, I've never met any of you. I was called to the bar in 1981, practised big-city litigation for several years and then moved back to my hometown. I haven't been in active practice for the past few years, but I have kept up with what's going on in the law, and I have followed this issue with some interest because I had a number of dealings with the IDA while I was still in practice and I have a bit of a background in administrative law generally.

I had been a chair of a provincial board in the mid-1980s, was the first counsel retained by the Ontario Human Rights Commission to prosecute a French hearing in the province and did a series of administrative hearings in terms of the military; immigration; disciplinary at the College of Nurses; and advising police officers on disciplinary matters.

Having seen the recommendations that Justice Osborne has made, I would urge the committee to consider adopting them. I think they made eminent good sense. There's a real problem when you have a body that is trying to enforce its legislation and adjudicate on it at the same time when the reputations of individual members of the public are at stake.

In that regard, there are two very recent decisions that I thought might be helpful for your committee to consider when you're looking at possible changes. One of them is a Federal Court of Canada decision, so it's not something that would automatically be followed in Ontario, but it's a very well-written judgment and I think it would be of considerable persuasive value. The decision is called Democracy Watch v Howard Wilson, the ethics commissioner, and they talk about the apparent conflict that arises there and the reasonable apprehension of bias that arises because of the lack of security in terms of the ethics counsellor's tenure. There was a finding by federal court that there was a reasonable apprehension of bias, that there was a lack of independence, and it's a very strongly written judgment in terms of what could constitute bias.

The second judgment, the one that I think is more important for this committee's purposes, is a very recent decision of the Supreme Court of Canada. The case is called Phinney c. le barreau du Québec. In the Phinney decision the Supreme Court of Canada upheld an award of damages against the Quebec bar which had been rendered in favour of Ms Phinney. Ms Phinney had sued the bar for having failed to properly supervise one of its members. That particular lawyer had a history of difficulties and yet the barreau was very lax in terms of their dealings with him. What they found was that the bar owed a duty of care generally, and that it was reasonably foreseeable that the damage that she suffered would result. In that judgment, I think it could be argued that the definition of "gross carelessness" that was used as the basis for liability there would deprive the OSC of its ability to properly be independent in terms of adjudicating and enforcing.

If you have a prosecutor who handles a file badly, and handles it with the degree of gross carelessness that in Phinney gave rise to liability, you can get an award of damages against a prosecutor who does behave with what's called flagrant prosecutorial misconduct. But that being the case, if you have someone who puts himself in that position, the employer then becomes vicariously liable. If there is a financial interest in the potential outcome of litigation, how can it be said that you have an independent body adjudicating if they have a potential financial liability at the end of the day, once a decision is given?

There has been a bit of a spitting match over the years between the OSC and the law society about who really can discipline lawyers when they misbehave. As everybody knows, that's something that happens fairly frequently. But in terms of the function that the OSC provides, let me say this: They are the only body in Ontario that thus far has shown the determination and the interest in going after the major financial institutions such as the Royal Bank of Canada and other bodies of that size. Other enforcement agencies that are supposed to enforce the legislation have not done so. I would echo Mr Hollander's remarks about the frustrations and difficulties of dealing with the IDA. They quite simply do not do their job. But the OSC, when it does take on a prosecution of a major body, does, generally speaking, a good job.

For that reason, Justice Osborne's recommendations that the enforcement against the bodies be left in the hands of the OSC makes excellent sense. But more importantly, when the reputations of individuals are at stake and there are going to be allegations made against them personally, it is crucial that you have an independent adjudicative body. For that reason, his recommendations should surely be adopted. I looked with some interest at the newspaper reports of yesterday's hearing and the questions that Ms Matthews put. I can't help but think that it's not hard to find a lawyer who will write down any recommendation you want to have, based on what I've seen over the years in court. If I were given the legal opinions in question, surely I'd look at them with some interest. But Justice Osborne is a dispassionate individual. He has no axe to grind, he has no client here, and I had never known him, as a judge, not to call matters as he saw them. I think his recommendations make tremendous sense. I hope that you will adopt them.

Thank you very much for letting me speak.

The Chair: Thank you. We do have time for questions. We have about three minutes left. In this rotation we'll only have time for one party, and that would be the NDP.

Mr Prue: I think Justice Osborne was absolutely right too. I asked questions on that as well yesterday. It's preposterous to me that you can have a system where you have a judge and jury and a prosecutor and everybody rolled into one person. It just doesn't work.

But having said that, there were some other issues that you haven't dealt with. You're quite refreshing here in your candour, so I'm going to ask you: We've had a number of people talking over the last couple of days about prosecutions, criminal wrongdoings, the overwhelming, huge numbers—at least I thought they were huge—of people who are called for illegal activities. OSC finds one a week—excuse me, one a day; once a day, somebody is called. I asked one of the deputants this morning about the enforcement provisions: If we did one thing, would he suggest that it be to beef up entirely the enforcement provisions and the money there to go after these wrongdoers, and he said yes. Would you put the same kind of emphasis on it, or do you think that removing the adjudication branch would be sufficient?

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Ms Coady: No. In all of these—at the law society, at the OSC, at many of the administrative tribunals I've seen, including the Canadian Judicial Council—you've got difficulties because (a) there's a lack of transparency, (b) there's a lack of screening mechanism, and (c) there's a lack of enforcement, the point you've just made, which is an excellent one. The enforcement that's done is selective. It's not necessarily done with respect to the more serious ones; it's done with respect to the ones they figure they might be able to push through without anyone being the wiser.

The OSC doesn't tend to pick favourites, as far as I'm aware, the way some other bodies do. But there are other bodies where they will get an allegation of wrongdoing and, based on who it is, the enforcement isn't done, the investigation isn't properly done and the matter is buried. I think beefing up enforcement is a good thing, but if you are going to be beef it up, concurrent with that you must also make sure your screening mechanism at the prosecutorial level is a totally separate layer, is discrete and has some built-in checks and balances. Because in a number of these bodies, they're merged and basically become an indivisible whole, and it's almost impossible to penetrate or see any distinction between them. That's one of the major difficulties they have in terms of administrative law.

I hope I didn't go over the three minutes.

The Chair: No. Thank you for your submission.

ROBERT SCAVONE

The Chair: Is Robert Scavone in the room? OK. Have a seat, please. Good afternoon. I would ask you to state your name for the purposes of Hansard. You may begin your presentation.

Mr Robert Scavone: Thank you, Mr Chairman and committee members. My name is Robert Scavone. I am a partner with the corporate financial services group of the Toronto law firm McMillan Binch LLP, and I've practised corporate commercial law for over 17 years.

Let me begin by thanking you for giving me the opportunity to appear before you this afternoon. I am here on my own behalf as a lawyer with a strong professional interest in law reform in this area, but my remarks have the support of the Toronto Opinion Group, which is a group of about 40 Toronto lawyers who meet regularly to establish common standards for giving legal opinions in commercial transactions.

I am speaking in support of recommendation 5 of the five-year review committee final report, which advocates uniform legislation governing the transfer and pledge of securities, in particular the draft legislation known as the Uniform Securities Transfer Act or USTA, which has been prepared by the Uniform Law Conference of Canada and the Canadian Securities Administrators. I believe my friend John Cameron from Torys has already addressed you on this topic earlier this afternoon. I have been a consultant to the USTA project on a pro bono basis for the last three years. My colleague Wayne Gray and I submitted a written submission to your committee on August 11.

In my view, the USTA initiative is at least as important as the higher profile recommendations that are contained in the final report. There are any number of reasons why this is so, but I think the most significant is this: Without this legislation, Ontario's capital markets are at risk of losing millions, even billions, of dollars of business to the US, especially New York. Why? Because New York and every other state has uniform legislation that recognizes modern commercial practices in the securities industry and provides a sound legal framework that allows parties to predict the legal results of their actions with confidence, and we do not. What we have is a cobbled-up patchwork of laws that is at least 40 years out of date. It is no exaggeration to say that without this legislation our competitive position in the North American capital markets will be progressively eroded as business flows south.

I see signs of this erosion almost every day in my practice. Recently, a large financial institution asked me for an opinion that the transfer of certain debt securities held through the Euroclear system in Brussels was effective under Ontario law. I could not give that opinion, because it was not clear that Ontario law applied and the only way we could make that so would be to have someone actually withdraw the bond certificate from a vault in Brussels, take it out of the clearing system, have it couriered to Toronto, hand over the certificate to the bank in Toronto and then send it back to Brussels for re-entry into the clearing system. This was simply impracticable, and the bank either had to accept an opinion full of unsatisfactory qualifications or not do the deal.

My colleagues and I frequently encounter cross-border transactions in which the secured parties are surprised and annoyed to learn that in Ontario a security interest in US treasury bonds can only be perfected by registration under the Personal Property Security Act in Ontario and not by possession or control, a superior method that would guarantee them priority against other creditors. To ensure priority, they then have to do searches and seek subordinations from everyone else who is registered ahead of them, which can be costly, impracticable or both. This often results in the debtor having to post a letter of credit, which can be expensive. I've spent many long and often fruitless hours doing and supervising research into abstruse legal issues involving where the law considers book-based securities to be situated, delaying transactions for days and even weeks and adding thousands of dollars to the legal bills, to the benefit of few people, except, of course the lawyers.

If the USTA becomes law, such sad stories will be a thing of the past. Without it, Canada may one day become a marginalized backwater in the capital markets as we continue to lose business to Wall Street.

A few words of background may be helpful to understand the context. The USTA and the companion amendments to the Personal Property Security Act and the Business Corporations Act are part of a separate branch of commercial law that governs the purchase, sale, pledge and holding of securities and other interests in investment property. Unlike the other proposals addressed in the report, the USTA is not securities regulatory law as such. Instead, it is facilitative or framework law that would promote legal certainty and reduce risk to capital market participants by putting securities transfers on a sound legal footing that reflects and responds to modern market practices.

Think of this body of law as the plumbing and wiring behind the walls of securities trading. It's largely invisible, and we only realize how important it is when a pipe bursts and floods the basement or a circuit overloads and burns down the house. Fortunately that has not yet happened. But today, Ontario has the equivalent of knob and tube wiring and lead pipes that were designed for an age when high tech was a radio and a bathtub, only now we're trying to run computers and HDTVs and Jacuzzis. Plumbers and electricians over the years have patched the system here and there to make it work a little better, but the time has come to rip out the walls and do a complete overhaul. That's what the USTA will do.

The existing law, which is in part VI of the OBCA and parts of the PPSA, dates from an age when securities trades were largely paper-based, when volumes were low and owning a share meant you held a share certificate with your name on it. This is known as the direct holding system, and it still works well enough for private companies. But as trading volumes increased dramatically in the 1960s and 1970s, it became apparent that moving

physical certificates around was no longer practicable. Gradually, an indirect or tiered holding system evolved whereby a clearing agency such as the Canadian Depository for Securities Limited, or CDS, as it's known, holds in its vault the physical share certificate for an issue, known as a global certificate, which is registered in the name of CDS, and transfers of positions in that issue between brokers are accomplished through electronic book entries—hence the term "book-based securities."

This tiered holding system has resulted in much greater efficiencies. However, the law in Canada has not kept pace with these developments. The OBCA and PPSA were amended in the 1980s to create the legal fiction that the computer entries in CDS are the legal equivalent of delivering an endorsed share certificate and that it is possible to somehow be in possession of electronic book entries.

But these stop-gap fixes were less than satisfactory. The legal fictions tend to break down between anyone but banks and brokers who are the direct participants in CDS. It applies only to securities held through CDS. The law does not provide a coherent legal theory of what you actually own when you own a book-based security.

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There are serious gaps in particular in the area known as conflicts of law. These are the rules that allow the court to determine what law applies in transactions that have connections outside the court's own jurisdiction. For example, a Toronto-based bank might take a pledge of securities issued by a French company through Clearstream, which is in Luxembourg, from a debtor domiciled in Pennsylvania, using documents governed by New York law. Under the confused state of the law as it now stands, no one really knows what laws govern this sort of transaction. There are about half a dozen possible answers, mostly drawn from old cases that long predate the tiered holding system, and none is really on point. This uncertainty means that the secured party does not know where or how to perfect its interest in the securities so as to obtain priority over competing creditors and the trustee in bankruptcy. So as a lawyer, I have to advise my client to perfect its security interest in every possible jurisdiction that may have a connection, and then hope for the best. This adds needless expense, delay and uncertainty to transactions where margins are often razor-thin, time is money and certainty is essential.

The US is 10 years ahead of us in this area. In 1994, article 8 of the Uniform Commercial Code was extensively revised to reflect the realities of the tiered holding system. Revised article 8 introduced the concept of a security entitlement to describe the legal reality of what the owner of a book-based security actually owns, which is a bundle of rights against the securities intermediary. It provides a clear and easily applied set of conflicts-of-law rules. It replaces the fiction of constructive possession with the concept of control as the means of perfecting a security interest in investment property. The result isn't simple, but it is clear and coherent and certain. Those leaky pipes and frayed wires are history.

The USTA is based largely on revised article 8 and adapts much of its language verbatim as far as possible, even down to the official commentary. That's not to say that Ontario legislative drafters could not improve on this language—almost any statute could benefit from drafting refinements—but such tinkering would defeat one of the main purposes of the USTA, which is to bring to Canada legislation whose language and concepts are familiar to US capital markets, who value the certainty that revised article 8 brings. Familiarity in this area does not breed contempt; it breeds confidence.

The Chair: I want to remind you that you have about a minute.

Mr Scavone: That's all I need.

Implementing the USTA in Ontario will be the first step toward adopting truly uniform commercial legislation in this area across Canada, which is a very desirable goal.

If Ontario moves first to adopt the USTA, the goal of word-for-word uniformity throughout the country will be greatly advanced. As the leader in the Canadian capital markets, Ontario has a duty to provide leadership to the other provinces and territories.

Enacting the USTA will bring many immediate benefits. It will provide the legal framework for the increased operational efficiencies of straight-through processing, which will save the Canadian securities industry an estimated $140 million a year. It will control systemic risk, it will reduce transaction costs and legal uncertainty, and it will keep Ontario competitive in the increasingly cutthroat capital markets of North America.

In conclusion, I would ask that you give your strongest support to the USTA initiative. It is an idea whose time has come and whose implementation is vital to Ontario's future.

The Chair: Thank you for your submission this afternoon.

PHILIP ANISMAN

The Chair: Philip Anisman, barrister and solicitor.

Dr Philip Anisman: I'm Philip Anisman. I'd like to thank you for this opportunity to appear before this committee on a subject that I have dealt with for the last 30 years or so in a variety of capacities, including as a practising lawyer but also as a legislative adviser, a policy adviser to securities commissions and a law professor.

I might say, when I jump right in, that my first comment won't surprise you, given that I led and was the principal author of the proposals for a securities market law for Canada, published in 1979 by the federal government.

So let me jump right in and start by saying that I support the recommendation that this committee do everything it can in furtherance of the development of a national securities commission. That would include, I'd suggest, approving the recommendations with respect to the harmonization amendments in the Crawford report.

Having said that, my major submissions will be on two other areas. The first deals with the structure authority and accountability of the Ontario Securities Commission. The second deals with investor remedies. What I'd like to do is deal first with the question of the adjudicative function, then with rule-making, and now I'm talking about accountability of the commission, and then with an accountability structure.

Let me say, and I don't know if I'm the only person appearing before you who'll say this, but I think that the Osborne committee simply got it wrong. I think that the commission's adjudicative functions should be retained. The reasons are expressed in my submission to the committee, and particularly in tab A, which contains a paper I wrote on the subject last fall. I must say in candour that a copy was provided to the Osborne committee. They even acknowledged it.

I have five reasons for saying that the commission's adjudicative structure should remain.

First, policy and adjudication are complementary. What the commissioners learn in developing policy and in administration enables them to apply their rules more thoughtfully and more accurately in adjudicative settings.

Second, the adjudication itself gives them information that feeds back into policy. There's a cross-fertilization process, and there are numerous examples of that happening with the Ontario commission as well as with other commissions. My second reason is that the commission's mandate in adjudicating involves the public interest. The public interest mandate was given to them so that they could deal with novel circumstances created by fraudsters that aren't anticipated in the clear rules when they deal with people in the industry and other people engaged in the marketplace.

In this respect, the commission does not just apply past rules when they adjudicate in disciplinary proceedings; their purpose is to protect the public interest, and in this respect they're not like a court. That's why I suggest in my paper that the commercial list wouldn't do, because courts are not used to applying a public interest standard. They apply legal rules.

The same applies to the sanctioning process that the commission engages in, and I mention this specifically because it's a focus of the Osborne report, which I have to say I read last night and this morning. I got it off the Web. There is policy involved in sanctioning, and the commission's expertise is very important. When they deal with a registrant—a broker or a salesperson—they frequently don't just throw them out of the industry or suspend them. They frequently impose conditions on registration that allow them to continue, but under supervision of various types. That involves expertise. Another one of their sanctioning powers is to review the practices of corporate issuers. Then they can order issuers to change their practices. That also involves expertise.

Those are the types of things that courts can't do and for which the policy-making and the multifunctional agency is important. In fact, that's why they were set up in the first place in the 20th century.

My third point is that you can't separate disciplinary hearings from regulatory hearings, as the Osborne committee suggested. Regulatory hearings, like hearings dealing with poison pills and takeover bids, frequently involve—in fact, usually involve—a request for a disciplinary sanction, like a cease-trading order. Indeed, when the commission issues cease-trading orders, which is a classic disciplinary function, in some senses it's also regulatory, because what they're dealing with is the disclosure adequacy of a corporation's file, and it's the same when they lift the cease-trading order.

My fourth point is that the perception the Osborne committee talks about relates really to the combination of investigative and prosecutorial functions with adjudication in the same agency. But I'd suggest to you that the same people don't do that. The commission has internal separation of prosecutorial and investigative functions from the adjudicative functions. Commissioners who adjudicate do not participate in the other functions. There's internal separation. The perception is because people think there may be some kind of psychological allegiance to the agency or something like that, and the Osborne committee refers to that. I'd suggest to you that that isn't very concrete.

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My final point is this: Wherever separation of functions has occurred in North America in agencies like the commission—it hasn't happened with securities commissions, but in agencies that have a policy-making function—where the policy-making part and the adjudicative part have been separated, it has resulted in undermining the whole regulatory scheme. Indeed, when you read my submission, if you haven't already, it quotes the leading text on administrative law in the United States—this is US experience—to the effect that one of the strongest ways of undermining a regulatory scheme is to separate adjudicative and policy functions in the manner that the Osborne committee suggests. That's bifurcation.

My next concern is rule-making. I'll be fairly brief on rule-making. There are two recommendations in the five-year report that I think are misguided. The first one is recommendation 13, which recommends that the commission be given a Henry VIII rule-making power, the so-called basket clause, that would give it, in effect, unconfined authority to make rules relating to the purposes of the act.

The conclusion of the Daniels task force was that the commission shouldn't have that power. They thought it shouldn't have that power because expanding the coverage of the act beyond its current context, in their view, required legislative authority. They didn't think the commission should be able to do it. Indeed, they recommended a more limited basket clause that wouldn't have given them that kind of authority. Some of that is described in the Crawford report, and it's also dealt with in my submission. They also recommended that the cabinet not have a Henry VIII clause.

What you have in the act now is this: When it was enacted, there was no basket clause for the commission,

but the cabinet has a Henry VIII clause of the type that the Crawford committee recommended the commission should have.

As I read what happened when the rule-making power was given, it's that there was a conclusion on the part of the government that if the commission thought it necessary to expand the authority under the act with respect to rules, it should generally have to go to the Legislature, as Daniels recommended, but it should at least have to go to cabinet to get a regulation that would expand it. So there was a clear conclusion at the time that the commission should not have unconfined power to make rules on any matter it thinks fit, even if it isn't already covered under the act. Indeed, they don't need it. The SEC doesn't have it and, as matter of principle, they shouldn't either.

The second rule-making concern is the recommendation—it's recommendation 21—in favour of giving the commission the power to make blanket rulings and orders. Mr Brown, in his remarks yesterday, at least the written ones, suggested that the purpose of that power would be to reduce the regulatory burden. The problem with it is, it would also allow the commission to make rules without the accountability process involved in the notice and comment procedure—the public participation part—or ministerial approval.

The difficulty with the recommendation, in my view, even though it's confined to exemptions, is that what exemptions do is allow people to engage in transactions without having to comply with provisions of the act that are frequently intended to protect investors. They can do that in individual cases, because then they can check the parameters and see what will happen. But I would suggest that they should not be entitled to do it generally, because that's equivalent to making a rule without going through notice and comment and ministerial approval.

Indeed, the current statutory regime permits them to make a rule granting an exemption without notice and comment, but sets a standard. The standard is that the rule is not likely to have a substantial effect on the interests of people other than the person exempted. The other people are usually going to be investors.

The Daniels task force in 1994 recognized that blanket rulings had been used by the commission as a regulatory tool. Indeed, they frequently set up regimes through conditions imposed on the exemption. Daniels was clearly of the view that the commission should have to follow the rule-making procedure when it granted general exemptions, subject to that one exemption, where it wouldn't substantially harm the interests of anybody other than the person exempted. Once again, I'd suggest to you that this is a recommendation of the Crawford committee that should not be adopted. It undermines commission accountability.

That brings me to the question of accountability itself. What you have with the commission now is an independent agency that is self-funding, that has very broad powers. It legislates through rule-making, it investigates, it enforces, it adjudicates. It, in effect, controls its own budget, subject to its dealings with the minister under an MOU, which wasn't enacted as required by statute until five years later than it was supposed to have been.

I would suggest to you, and I'd submit strongly, that a stronger accountability mechanism is required for a commission with this kind of independence and the breadth of powers it has. What I suggest in my submission is that you recommend a standing committee before which the commission would have to appear on an annual or biannual basis for a review of its priorities, its accomplishments and its budget. I recognize that what I'm suggesting is closer to congressional practice than Canadian practice, where the SEC has to appear before congressional committees and appropriations committees to justify its budget and its conduct, but I'd submit to you that it is necessary in this case in view of the breadth of commission power. I'd suggest, as well, that that's the real answer to what Osborne is concerned with. Interestingly, for the Ontario securities tribunal, the separate adjudicator that Mr Osborne recommended, they recommended this kind of accountability mechanism as well.

If I can, briefly, I'd like to address investor remedies. I have basically two submissions on that. One goes to the secondary market civil liability regime. The second goes to the question of restitution and compensation power by the commission. There are other submissions on remedies in my written submission which I won't address.

I should point out as well that I was a member of the Allen committee, on which the current legislation is based, and I do support the recommendation in the Crawford report to adopt and enact the provisions in Bill 198, along with the amendments to it that died on the order paper in Bill 41, but subject to two caveats.

Before the legislation was enacted, as the Crawford report states, the CSA made modifications to the regime in order to address opposition by corporate issuers. I think what they did in doing that is they threw the balance that the Allen committee intended out of kilter, and they did it in two ways.

First, there's a mandatory costs requirement: Loser pays no matter what. That would remove a discretion in the court to say a plaintiff doesn't pay. I'd suggest that has the potential to deter actions. What you have to remember is that the civil liability regime is based on class actions brought on behalf of investors. That could deter them. Our courts have not been sympathetic to unmeritorious class actions, and there are a few cases cited in my submission. The mandatory provision, which could be a deterrent, I'd suggest, is unnecessary, unwarranted and unbalanced. I'd recommend that this committee recommend that section 138.11 of the act be deleted when it's enacted.

The second element of the statutory liability regime is the screening mechanism the CSA imposed. What they would require in order to ensure an action has merit before it is brought is an application to a court to get leave to bring it, in which the plaintiff would have to demonstrate that the action is being brought in good faith and it has a reasonable possibility of success at trial. The problem with that leave application is that it requires, in

effect, two leave applications: one to bring the action and a section under the Class Proceedings Act to certify it. That could impose additional costs—an unnecessary deterrent.

My recommendation is that the legislation be amended to allow a court, on the leave application, to also certify the action, if it grants leave at the same time, and leave that matter to the court's discretion.

The second issue is that the CSA would require affidavits, but they would only require in the affidavits that all of the parties swear to the facts on which they rely, and they refer for that recommendation to a report of the Ontario Law Reform Commission in 1982. The Ontario Law Reform Commission would have also required the parties to swear that there are no material facts relevant to the application of which they're aware that are not disclosed in the affidavit.

I'd submit that the amendments to accomplish this are simple. They're on page 30 of my submission. The act has to be amended in any event before the statutory scheme can be enacted. Bill 41's provisions have to go in. If you accept this submission, it's quite easy to plug in my proposed amendments and tilt the balance back a bit in favour of investor actions and the balance the Allen committee intended. It doesn't undermine what the CSA wanted in terms of a requirement for a plaintiff to demonstrate merit; it's just that it's a little more balanced.

My final submission—and if you'll give me one more minute, I'll conclude—is that the commission should have authority to make restitution and compensation orders after a disciplinary hearing.

The Crawford committee took a wait-and-see approach and said, "Monitor Manitoba and the UK, where this power exists." But it did recommend disgorgement and administrative fines, both of which the commission can now impose as a result of amendments in 2002. It also recommended that a criminal court, when it convicts someone of violating the Securities Act, should be able to make a restitution or compensation order. It just held back with respect to the commission. There's no reason to do that.

The commission should also be empowered to grant restitution or compensation to public investors where it's appropriate after a disciplinary hearing. After all, when you're talking about investor protection, compensation for harm is the greatest protection. There are reasons for my submission on that and I think they address any concerns the commission might have. They're in my brief.

I'll stop here, and if there's time for questions I'd be happy to address them.

The Chair: I regret that there is not time for questions, but we appreciate your submission before the committee.

That concludes the presentations for this afternoon, and indeed the public hearings.

Mr O'Toole: Mr Chair, with your indulgence, I'd like to move that at the completion of business today the subcommittee be authorized to meet to give direction on the legislative research compiling a report.

The Chair: All in favour? Carried. Further business?

SUBCOMMITTEE REPORT

Mr Delaney: Mr Chair, I have a report of the subcommittee of the standing committee on finance and economic affairs to table, and it reads as follows:

Your subcommittee met on Wednesday, August 11, 2004, to consider the method of proceeding on Bill 97, An Act respecting the sharing of resource revenues for First Nations, and recommends the following:

(1) That the committee intends to travel to Sioux Lookout, Osnaburg, Attawapiskat and Moose Factory for the purpose of holding public hearings on dates agreed to by the whips: September 20, 21, 22 and 23, 2004.

(2) That the committee clerk, with the authorization of the Chair, post information regarding the hearings on the Ontario parliamentary channel, the committee's Web site and advertise in the weekly and regional newspapers.

(3) That interested parties who wish to be considered to make an oral presentation may contact the committee clerk up to the day of the scheduled hearings.

(4) That the scheduling of witnesses and the length of presentations be as flexible as possible depending on the number of requests received.

(5) That the deadline for written submissions be established at a future subcommittee meeting.

(6) That Mr Bisson and the clerk of the committee, in consultation with the Chair, be authorized to finalize the logistics for the meetings.

(7) That the research officer provide the committee with background information relating to this bill prior to travel.

(8) That the research officer also provide the committee with a summary of deputations by Friday, October 1, 2004.

(9) That the clerk of the committee, in consultation with the Chair, be authorized, prior to the adoption of the report of the subcommittee, to commence making any preliminary arrangements necessary to facilitate the committee's proceedings.

The Chair: All in favour? Opposed? Carried.

This meeting stands adjourned.

The committee adjourned at 1544.

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