CANADIAN BANKERS ASSOCIATION

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Mr. Thomas I. A. Allen, Q.C.
Chairman, IDA Task Force to Modernize Securities Legislation in Canada
Suite 1600
121 King Street West
Toronto, Ontario
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Dear Mr. Allen:

Re: Task Force to Modernize Securities Legislation in Canada

The Canadian Bankers Association (CBA) appreciates the opportunity to share our views with the Task Force on how securities legislation and regulation in Canada might be modernized.

Opening Comments: Structural Reform Also Needed To Achieve A "Dynamic, Fair, Efficient And Competitive Capital Market" In Canada

In this letter we are suggesting a number of approaches that are aimed at enhancing the securities legislative and regulatory framework. At the outset, though, we cannot help but wonder how effective these approaches can be without changes to the securities regulatory structure itself. The Task Force's objective is to consider how securities legislation and regulation might be changed to achieve the objective of a "dynamic, fair, efficient and competitive capital market" in Canada. In our minds, a key impediment to achieving this objective is the fact that there are 13 separate securities regulators in Canada overseeing a very small piece of the global capital market. As a result, we express the view that while the Task Force's focus on Canada's securities laws and regulations is timely and important, there is also a continuing critical need for the reform of the securities regulatory structure.

At the root of our concern is the need for efficiency in the regulation of the capital market in Canada, regardless of how this might be achieved. Last year David Dodge, Governor of the Bank of Canada noted that:

> [e]fficiency dictates that Canada should have uniform securities laws and regulations, based on principles that apply to everyone. Some have taken this idea further and advocated for a single, pan-Canadian securities regulator. I'm not here today to weigh in on that debate. But I do want to stress that, whatever the structure of the regulator, we must strive for

efficiency in regulation - the best regulation, at the lowest cost.'

Do we have an efficient securities regulatory structure? Clearly, we do not.

Consider, for example, the confusion and compliance challenges that have been created by the lack of harmonized securities rules is in the area of financial planning. Existing rules in Quebec require that in each case, all financial planning activities are to be conducted through a separate financial services firm licensed with the provincial Financial Markets Authority, but in all the other provinces, it is permissible to conduct these activities through an IDA Member firm. The unfortunate result of this regulatory structure is to require firms which operate on a national basis to provide financial planning services through separate legal entities (one for Quebec and one for the rest of Canada) in order to comply with two sets of rules that essentially regulate the same activity. As this example shows, the current regime clearly is not efficient and does not give issuers or investors "the best regulation at the lowest cost".

With such a fragmented regulatory structure, could we ever expect to achieve the uniformity in securities laws and regulation that, according to Mr. Dodge, is needed for an efficient capital market? Recent experiences, we note with regret, do not give us much room for hope. The Uniform Securities Legislation initiative, commenced in March 2002, has so far not produced uniformity of legislation and under the CSA's approach to rule-making, while considerable strides have been taken in the right direction, it still typically takes one or more years to produce multi-jurisdictional and "national" instruments that often, in the end, do not apply uniformly to all provinces and territories.

In short, we commend the Task Force for giving consideration to how the objective of "a dynamic, fair, efficient and competitive capital market" in Canada can be achieved by improving our securities laws and regulation. Our only cautionary note is that in our collective efforts to achieve this objective, we must also not lose sight of the need to reduce the number of securities regulators and more generally, to continue to focus on regulatory structural reform.

Suggestions to Modernize the Legislative and Regulatory Framework

We believe that there are a number of approaches that can be taken to modernize the securities legislative and regulatory framework. These include the following:

Focus on the Big Picture

We express the view, as a way of framing our suggestions at the outset, that securities regulators need to take a more holistic approach, generally, to developing and introducing new regulatory requirements.

Let us explain how we have come to this view and what it means.

From our vantage point, we note that when promoting regulatory initiatives that must be implemented downstream by SROs and by registrant firms, regulators can sometimes lose sight of the number of other regulatory initiatives that are underway and about the fact that registrant firms typically are devoting ever-increasing resources to regulatory compliance, possibly with diminishing returns. Our experience has also been that regulators tend sometimes to pay lip service to registrant concerns, raised at the time that a new regulatory initiative is being introduced, about the time and costs involved in building and implementing the processes and systems needed to comply with the new initiative.

Taking these observations into account, we believe that when developing and introducing

[1] Remarks by David Dodge, Governor of the Bank of Canada, to the Toronto CFA Society, Toronto, Ontario, September 22, 2005 ("Dodge Remarks")

new regulatory requirements, the regulators should consider the "big picture" and the impact of multiple regulatory initiatives on registrant firms.

In practice, what would this mean? We believe, for example, that regulators should establish a threshold test for regulatory intervention, and should only intervene in circumstances where the market has clearly failed to function appropriately and where the benefits that are expected to result would be greater than the costs to be imposed.

Consider the Regulatory Cost

We also believe that securities regulators should rigorously assess the costs and benefits of any new regulatory initiative. In this regard, we would again refer to remarks made earlier this year by David Dodge:

> Let me set out three principles that policy-makers should apply in deciding when regulation is appropriate. First, regulation is appropriate to correct a market failure or, to put it in economic jargon, to deal with "externalities." The second principle is that regulation must be effective. Even when a market failure is recognized, regulators should act only if there is a reasonable chance that they will actually address the failure in question. The third principle is that the benefits of a particular regulation must be greater than the costs it imposes. In trying to solve one problem, regulators must avoid causing even greater problems.'

Thus we believe that it is important for regulators to be prepared to undertake objective cost-benefit analyses of regulatory proposals, to consider the cost implications of individual initiatives and to reconsider initiatives where costs are likely to be large and benefits speculative.

In short, there needs to be a particular focus on the costs of regulation because the consequences of increasing the compliance burdens on registrant firms are significant not only for the firms involved but also for their clients. Based on experiences to date, for example, we note that the cost and complexity of regulation could very well threaten to put some financial services out of reach for small investors (e.g. mutual fund accounts) and it is precisely this constituency that regulation is meant to help.

We believe that the following approaches might address the concerns we have raised:

- Regulators, when they propose to direct the SROs to undertake regulatory initiatives, (or perhaps before they do so), should consult with the industry and other stakeholders, should commission independent cost studies, and should take into accounl the totality of regulatory initiatives that are concurrently underway and the overall compliance burdens on the industry.

- Regulators should pursue approaches that will lessen compliance burdens, such as the initiatives undertaken by the Financial Services Authority in the UK in its "Basic Advice" initiative. (The Basic Advice initiative seeks to simplify and reduce regulatory requirements and costs without sacrificing investor protection. Consumers receive limited, basic advice with regard to a specified range of suitable low-cost regulated saving and investment products such as investment funds. Salespeople conduct a basic assessment of product suitability to the customer's objectives, but are not required to hold formal financial planning qualifications.)

[2] Dodge Remarks.

Simplifying the Regulatory Burden

In an increasingly integrated and sophisticated global marketplace, Canadian regulators should work, we believe, to reduce the volume and complexity of the securities rules themselves. This would go a long way towards addressing the problems caused by the regulatory burdens facing registrant firms.

To this end, we generally support an approach to regulation that is both principles-based and risk-based. We observe that with the increasing sophistication of technology and market participants, it is difficult for regulators to develop and amend specific rules in a manner that is timely and does not slow the growth of the market or dramatically increase the costs of meeting the regulatory burden.

For example, we believe that electronic systems for information delivery or access should be developed to enable simplified compliance and better customer service without sacrificing any regulatory benefit. Existing requirements for cumbersome physical delivery of documents like prospectuses, quarterly reports and mutual fund documentation, we observe, can be expensive, wasteful and inefficient. Many of these documents, moreover, likely are not read and find their way very quickly into the recycling bins of the recipients. It follows that in our view, securities regulators in Canada should go much further in either permitting electronic delivery of these documents or, better yet, adopting the "access equals delivery" concept which is being implemented in the U.S.

Continue to Harmonize

There should be a focus on harmonization, with regard not only to pursuing regulatory structural reform but also to modernizing the securities legislative and regulatory framework itself. Simply put, we need uniform rules are needed to foster efficient capital markets and we also need harmonized regulatory processes across Canada. To this end, we believe that efforts should be made to harmonize the registration process (e.g. the categories of registration, proficiency requirements, and the process for exemptive relief). We also believe that to the greatest extent possible, the regulation of the same activity by different regulatory bodies should be harmonized so that, for example, the investment products sold by insurance professionals and mutual fund salespersons are subject to the same rules.

Re-think Disclosure

We believe that there is a disconnect between disclosure requirements and the way that information actually is communicated to investors. In theory, the preparation of a complete and correct disclosure record and the delivery of disclosure to investors are both necessary to ensure that investors know what they are buying and getting into. In reality, however, we make the observation that as matters now stand, a great deal of the required disclosure is typically ignored by individual investors. Prospectuses and annual reports are, more often than not, regarded as nuisance mailings.

How to bridge this gap? Certainly, a more fulsome exploitation of the Internet could provide the nexus, making disclosure more accessible to investors than ever before.

More fundamentally, we believe that a concerted effort is needed to re-think disclosure requirements. The danger is not just that disclosure requirements, in our opinion, are reaching the point of diminishing returns. There is a real possibility that in some cases, additional disclosure might have negative consequences, with investors being even less likely to read and understand that which is disclosed to them.

The CBA fully supports the principle of robust disclosure for the benefit of regulators and investors alike. However, we are also fully supportive of sensible and reasonable disclosure. In a competitive marketplace, there are strong incentives for businesses to ensure that consumers

understand their rights and obligations in a commercial transaction. Beyond these commercial pressures, there are also a range of private and public sector initiatives designed to provide education to consumers to increase financial literacy. Taken together, these initiatives ensure that consumers interested in learning about the current range of financial and investment products and services available to them have more than enough information at their disposal. It follows, in our mind, that an assessment should be made on whether the existing range of regulatory disclosure requirements have gone too far in overburdening consumers with information that they do not want or need. Efforts to reduce or, more specifically, to target disclosure rules should be vigorously explored.

For example, a number of measures (e.g. improvements in continuous disclosure requirements, commission staff review, civil liability for continuous disclosure documents, and the increasing use of shelf offering procedures) have de-emphasized the role of the prospectus in capital formation. The CBA also believes that consideration should be given to extending the universal shelf concept to all reporting issuers. Combined with "access equals delivery" for the final prospectus or shelf supplement, this development would allow issuers to access the public markets more quickly and easily. Similarly, we believe that mutual fund prospectuses should be permitted to be streamlined and tailored more closely to a retail audience. Canadian securities regulators should, at the least. also develop and adopt offering reforms similar to those coming in the U.S. on December 1,2005 for "Well Known Seasoned Issuers".

Finally, we observe that the prospectus has traditionally been required as the only written offering document used to solicit expressions of interest in a security. We suggest that securities regulators in Canada should permit issuers, especially issuers of highly liquid securities, to use other summary offering documentation or summaries (which, we note, are increasingly subject to statutory civil liability).

In Closing

Achieving a "dynamic, fair, efficient and competitive capital market" in Canada can be accomplished in a number of ways. While there is a critical need to do this by embarking on a process of robust regulatory structural reform, we also agree that modernizing the legislative and regulatory framework could play a key role in realizing this objective. We thank the Task Force for this opportunity to provide suggestions on how this framework can be enhanced. Going forward, we would be pleased to answer any questions that you might have about our suggestions.

Yours truly,