



Backgrounder

A New Canadian Securities Regulatory Authority

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Introduction

This Backgrounder provides an overview of the proposed Canadian *Securities Act* (Act) and the new securities regulatory regime. It also describes the next steps leading to the establishment of the Canadian Securities Regulatory Authority (CSRA) targeted to begin operations within the next three years. (Please see Annex A for the proposed timeline).

The Canadian Securities Transition Office is the principal organization leading and managing the transition to a Canadian securities regulator. As part of its mandate, the Transition Office has led the development of the proposed Act.

The Act represents one key step towards establishing a Canadian securities regulator, a long-standing priority for the Government, which would improve Canada's financial regulatory framework.

In Response to Evolving Capital Markets

Capital markets play an important role in and make a significant contribution to the Canadian economy. They affect the wellbeing and prosperity of Canadians. For example, they are a source of financing for Canadian companies and provide a vehicle through which individuals can invest for their retirement.

Strong and vibrant capital markets are essential for economic growth and prosperity in Canada.

The changing world economy and evolution of capital markets have implications for all Canadians. Investors and issuers of all sizes are located in every province and territory, and capital now flows across Canada and its borders as never before. The evolving capital markets also feature increasingly complex financial products and methods of distribution and trading that require oversight and a responsive regulatory regime.

A New Canadian Securities Regulatory Authority

In the wake of the global financial crisis, Canada's financial regulatory regime has been recognised as a sound model. However, Canada can build on its reputable financial regulatory regime by establishing a national securities regulator to oversee its capital markets. Market participants, institutional and retail investors, academics and international agencies have long supported the establishment of a national securities regulator. Canada is currently the only major industrialized country without a national securities regulator

The new regime would lead to capital markets that give enterprises of all sizes better access to capital, provide investors with increased investment choices and better protections, and create more highly skilled, well-paying jobs in a globally competitive financial services industry.

*“The current diversity of regulations – for example, each province has its own securities regulator – makes it difficult to maximise efficiency, and increases the risk that firms will choose to issue securities in other countries. A single regulator would eliminate the inefficiencies created by the limited enforcement authority of individual provincial agencies.” - **The Organisation for Economic Co-operation and Development (OECD), 2008 Survey of Canada***

*“A federal regulator could coordinate more readily with other regulators in monitoring risks and responding quickly to a crisis, and could also have an enhanced focus on the issues that securities markets may pose for national financial stability.” - **International Monetary Fund (IMF), 2009 Article IV report on Canada***

The proposed Act builds on provincial securities regulation by harmonizing existing legislation in the form of a single statute. The CSRA would have a structure that recognizes Canada's unique makeup as well as regional and local expertise. CSRA offices across Canada would initially consist mainly of staff from existing provincial securities regulators to ensure the continuity of regulatory expertise and to provide uninterrupted regional and local service. Empowered regional staff of the CSRA would deliver consistent and responsive services to all market segments and regions.

Having deep, consolidated expertise within a national securities regulator offers significant benefits. The CSRA would provide:

- Better and more consistent protection for investors across Canada;
- Improved regulatory and criminal enforcement to better fight securities-related crime;
- New tools to better support the stability of the Canadian financial system;
- Faster policy responses to emerging trends;
- Simpler processes for businesses, resulting in lower costs for investors; and
- More effective international representation and influence for Canada.

The proposed regime benefits from input from the Advisory Committee of Participating Provinces and Territories, comprising representatives of British Columbia, New Brunswick, Newfoundland and Labrador, Nova Scotia, Ontario, Prince Edward Island, Saskatchewan, Northwest Territories, Yukon and Nunavut. As well, securities regulators and government officials of participating provinces and territories are making important contributions.

The proposed regime also leverages the work of previous provincial and federal consultation and research activities on securities regulation. This includes the Expert Panel on Securities Regulation (the Expert Panel), the Crawford Panel on a Single Canadian Securities Regulator and the Wise Persons' Committee, which have all led public consultations and provided recommendations for establishing a national securities regulator. The regime also builds on domestic and international best practices, and the objectives and principles of securities regulation endorsed by the International Organization of Securities Commissions (IOSCO).

Key features of the new proposed Canadian securities regulatory regime include:

- 1) A modern mandate and clear guiding principles;
- 2) A financial stability role with new powers and an effective scope of authority;
- 3) A strengthened enforcement regime that delivers better protection for investors;
- 4) A governance framework with clear accountability;
- 5) Streamlined regulatory requirements for market participants; and
- 6) Provisions allowing voluntary participation by provinces and territories.

Mandate and Guiding Principles

Securities regulation plays an important role in helping to ensure that capital markets function effectively. Securities regulation must protect investors and promote market integrity and stability, without imposing unnecessary compliance burdens.

To secure Canada's advantage in global capital markets, the CSRA's mandate would consist of three core objectives:

- i) Provide protection to investors from unfair, improper or fraudulent practices;
- ii) Foster fair, efficient and competitive capital markets in which the public has confidence; and
- iii) Contribute, as part of the Canadian financial regulatory framework, to the integrity and stability of the financial system.

The first two objectives are consistent with those of most provincial and territorial securities regulators today. The third objective reflects the need for the CSRA to support the stability of the financial system by being integrated into Canada's financial regulatory framework, which includes the Department of Finance, the Bank of Canada, the Office of the Superintendent of Financial Institutions (OSFI), the Canada Deposit Insurance Corporation (CDIC) and the Financial Consumer Agency of Canada (FCAC).

In pursuing its objectives, the CSRA would be guided by principles intended to achieve outcomes that are in the best interests of Canadians. Specifically, the administration of the regulatory regime should be open, efficient, flexible and responsive. As well, the cost of compliance should be commensurate with the significance of the regulatory outcomes sought to be achieved. Further, the interests of investors and businesses in all sectors and regions across Canada should be taken into account.

Having a uniform set of core objectives and guiding principles for Canada would foster a clear understanding of what securities regulation is intended to achieve.

The core objectives and guiding principles reflect the importance of capital markets in the Canadian economy. The objectives and principles would help build the foundation for a world-class Canadian securities regulator and ensure that outcomes are in the best interests of Canadians.

Financial Stability and Effective Scope of Authority

The evolution of capital markets and the experience of the recent credit market turmoil have demonstrated the need for securities regulation to contribute to the integrity and stability of the financial system. Drawing on the lessons of the global financial crisis, Canada has committed to ensuring that all financial regulatory authorities are able to identify significant risks across the financial system and that national regulatory authorities have the power to gather relevant information on financial institutions, markets and instruments in order to assess their potential for failure or likelihood to contribute to systemic risk.

The CSRA would have regulatory tools that contribute to the integrity and stability of Canada's financial system, including the power to gather information from market participants such as reporting issuers, dealers, investment-fund managers, exchanges, and self-regulatory organizations. As well, the CSRA would be able to share information

with other financial regulatory authorities in Canada, or elsewhere, for the purpose of contributing to the integrity and stability of the financial system. It could share that information so long as it would not be prejudicial to the public interest. Before disclosing information to foreign regulatory authorities, the CSRA would be required to enter into an agreement or have an arrangement in place with the authority.

The information gathering and sharing powers would allow the CSRA to monitor and evaluate developments affecting the integrity or stability of capital markets, and work effectively with its financial regulatory partners, such as the Department of Finance, OSFI, the Bank of Canada, CDIC, FCAC and other financial authorities outside of Canada.

The integrity and stability of Canada's financial system would be enhanced by the CSRA, as it would be integrated into the Canadian financial regulatory framework.

Effective Scope of Authority

The global financial crisis revealed that critical gaps exist in the regulation of financial instruments and market participants that have the potential to disrupt the financial system as whole.

The CSRA would have the capacity to regulate a broad range of instruments, including exchange-traded and over-the-counter (OTC) derivatives. It would also regulate market participants, including dealers, advisers, investment-fund managers, exchanges, clearing agencies, self-regulatory organizations, credit rating organizations, trade repositories and auditor oversight organizations. In addition, it would have the flexibility to designate and regulate new types of market participants.

The CSRA would ensure transparency and best practices in the Canadian derivative markets and adapt its regulation to evolving conditions and international developments in respect of derivatives.

Through registration, designation and recognition, market participants would be subject to governing frameworks established by the CSRA that reflect domestic and international best practices. For instance, the oversight framework for credit rating organizations would take into account the IOSCO Code of Conduct Fundamentals for Credit Rating Agencies.

The wide scope of authority supports the CSRA's mandate regarding financial stability. Having one set of regulations would ensure that financial instruments and market participants are regulated consistently across Canada.

Strengthening Enforcement to Better Protect Investors

Securities fraud and other forms of capital market abuse erode investor confidence and undermine the integrity of Canada's capital markets. They also impose a significant financial and emotional burden on their victims, affecting families and communities. Securing Canada's long-term prosperity requires a strong system of enforcement that protects Canada's capital markets and the investors that place their confidence in them.

The proposed Canadian securities regulatory regime would provide structural and legislative enhancements that support stronger enforcement in Canada's capital markets.

The establishment of the CSRA would lead to a strengthened, comprehensive and coordinated enforcement regime. This would concentrate expertise and resources, reduce unnecessary overlap and duplication and promote more consistent investor protection and coordinated enforcement actions across Canada.

To implement these structural enhancements, the Canadian securities regulatory regime would feature a comprehensive enforcement framework, building on the strengths of current provincial and territorial enforcement regimes (please see Annex B for an overview of the enforcement regime). The CSRA would have the power to undertake regulatory enforcement actions that could result in a range of sanctions. It would also play a role in the investigation of securities-related crime in a manner that would be set out in an agreement with each province. The current practice of securities regulators is to refer almost all securities-related criminal matters to police for investigation. Positioning the CSRA to assist with criminal enforcement would allow the CSRA to tailor enforcement responses to the seriousness of the suspected misconduct and would make available greater expertise and resources to combat securities-related crime.

The Act contains securities-related criminal offences that are equivalent to those that are currently prescribed in the *Criminal Code*. These include offences for securities fraud, market manipulation, prohibited insider trading and misrepresentation. These offences would apply nationally, in both participating and non-participating jurisdictions. The securities-related criminal offences in the Act have been modified (from those in the *Criminal Code*) to fit within the overall enforcement framework of the Canadian securities regulatory regime. The Act includes the aggravating circumstances, non-mitigating factors, and maximum sentences that currently apply to securities-related criminal offences in the *Criminal Code*. It also reflects the legislation recently tabled in Parliament that would amend the *Criminal Code* to strengthen sentencing measures for fraud and measures for victims of fraud.

The Attorney General of Canada and the Attorney General of a province or territory would continue to have concurrent jurisdiction over the prosecution of criminal offences. The provinces and territories would have the right of first refusal on these prosecutions, under an administrative arrangement that currently applies to the prosecution of securities-related criminal offences in the *Criminal Code*.

New evidence-gathering tools would enhance securities-related criminal investigations. These tools include:

- *Production Order (Written Statement)*: Criminal investigators would be able to obtain a court order to compel entities, such as publicly-traded companies or brokerage houses, to respond in writing to questions about certain aspects of alleged misconduct. The power would provide a new avenue for investigators to obtain evidence and could help to reduce the resources and time required to investigate securities crime.
- *Production Order (Names)*: Criminal investigators would be able to obtain a court order to compel a recognized entity to provide a list of registrants who purchased or traded a security during a specified period and to compel a registrant to produce a document that contains the names of all persons on whose behalf the registrant purchased or traded a specified security during a specified period as well as the time and date of the purchase or trade. This power would provide investigators with the information required to build cases involving trading misconduct, such as market manipulation and prohibited insider trading.
- *Civil Immunity*: The regime would provide immunity from civil action to persons who cooperate and disclose information to regulatory or criminal investigators that they reasonably believe is true. This measure is meant to protect people in order to promote greater rates of voluntary witness cooperation in securities-related investigations.

Please see Annex C for examples of how the new evidence-gathering tools may support criminal investigations.

The CSRA would provide concentrated expertise and resources, reduce unnecessary overlap and duplication, and promote more consistent investor protection and coordinated enforcement actions across Canada. It would have a comprehensive set of enforcement powers and make available new expertise and resources to combat securities-related crime.

Governance Framework with Clear Accountability

Canadians would be better served by the CSRA, as it would lead to greater efficiencies, better coordination and more effective allocation of resources. Decisions by a single national entity with effective regional representation would complement the character of Canada's capital markets. As well, consolidation of regulation-making activities into a single entity would provide for more cohesive and responsive securities regulation. In turn, the single, streamlined regulatory approach would make Canada's capital markets more attractive to foreign issuers and investors, creating high-skilled employment opportunities across Canada. The Canadian securities regulatory regime would incorporate the most effective aspects of the current system of securities regulation in Canada as well as the best practices for corporate governance.

The regulatory structure provides for clear lines of accountability and effective regional representation. It builds on the strength of the current regulatory system and ensures a strong on-the-ground presence in all regions with expertise that would respond to regional needs.

The CSRA would be established as a Crown corporation, funded from fees levied on market participants. A Crown corporation structure would provide the CSRA with autonomy in managing its day-to-day operations, while ensuring a clear accountability framework and effective oversight by the federal Government. The CSRA would be headed by a board of directors, appointed by the Governor in Council, that would be accountable to Parliament through the Minister of Finance (Please see Annex D for an organizational chart).

The board would oversee the management of the CSRA, provide policy direction and approve new regulations subject to the consent of the Minister of Finance. The board would be composed of directors who have significant expertise and who would be representative of the various regions of Canada, enabling them to develop regulation in the best interest of investors, issuers, market intermediaries and the public.

The CSRA would submit an annual report to the Minister of Finance with respect to its operations and activities for that year. The report would contain financial statements, a list of regulations and policy statements made during the year, and an assessment of the extent to which the purposes of the Act have been fulfilled by the CSRA. The CSRA would also be required to submit to the Minister of Finance an annual statement of priorities in connection with the administration and enforcement of the Act.

The CSRA would have two distinct divisions: the Regulatory Division and the Canadian Securities Tribunal. The Regulatory Division would be responsible for the regulation of capital markets in Canada, while the Tribunal would be responsible for the adjudication of securities regulatory matters.

The executive management team of the Regulatory Division would be led by a Chief Regulator and regional Deputy Chief Regulators. The Act does not prescribe the regions nor where the offices would be located. It is expected that each participating province and territory would have an office with the expertise to meet the needs of the area it serves.

Collectively, the offices would give the CSRA the capacity to meet local, regional, and national priorities.

The Tribunal's primary function would be to adjudicate matters arising from the CSRA, including administrative enforcement actions and reviews of regulatory decisions. The Tribunal would be headed by a Chief Adjudicator who would oversee the Tribunal and assign members of the Tribunal to hearing panels located in participating jurisdictions across the country.

To ensure policy coordination and regular engagement between the two divisions, a Regulatory Policy Forum (Forum) would convene the senior management of the two divisions and representatives from the board, to discuss, consider and comment on policy initiatives and activities.

The Forum would help to ensure that the policies, practices and activities of the CSRA are developed by the complete leadership of the CSRA. The Forum would ensure that the Tribunal is connected to the policy environment of the CSRA, which would support more informed adjudication.

In order for meaningful input from and exchange of information with provinces and territories, there would be a Federal/Provincial/Territorial Council of Ministers (Council) comprising the federal Minister of Finance and a minister appointed by each participating province and territory. The Council would make recommendations to the Minister of Finance on appointments to the board and to the Tribunal as well as on the appointment of the Chief Regulator. The Council would be consulted on the CSRA's annual report and statement of priorities.

To ensure that investors are properly engaged, an Investor Advisory Panel (Panel) would be established. The Panel would be composed of individuals with experience in capital markets and related investor issues. It would provide a strong voice for investors to influence the policy and procedures of the CSRA. Engaging investors in this way would help to promote public confidence in the securities regulatory system and ultimately achieve better outcomes for investors.

A representative of the Panel and representatives of the Council would also have the opportunity to participate in the Forum.

To further enhance investor protection, the CSRA would be able to fund the Panel from administrative penalties.

The new regulatory structure would ensure faster policy responses to emerging trends through better coordination and integrated national service delivery.

The CSRA would have the power to make regulations following a detailed public consultation and publication process, and subject to the consent of the Minister of Finance, for carrying out the purposes and provisions of the Act. The Governor in Council would have directive powers to order the CSRA to make, amend or repeal a regulation on the recommendation of the Minister of Finance. Urgent regulation-making powers allow temporary adoption of a regulation without the prescribed public comment period.

Substantive Securities Regulatory Requirements for Market Participants

Central to any securities regulatory regime are the substantive regulatory requirements for market participants, including those related to registration, prospectuses, continuous disclosure and take-over bids. In the Act, the substantive regulatory requirements are modeled primarily on those in provincial and territorial legislation. While the Act would contain broad substantive requirements, the technical requirements and exemptions that relate to these substantive provisions would be set out in the regulations. It is expected that the initial regulations would be primarily derived from the harmonized national instruments that have been developed by provincial and territorial regulators.

Exemptions from certain substantive regulatory requirements, such as prospectus filing and registration, for certain market participants would be set out in the regulations, consistent with the approach taken in most provinces and territories today.

Making the Transition to a Canadian Securities Regulator

The Government supports a process under which the Canadian securities regulatory regime would apply throughout Canada as willing provinces and territories opt in, with the objective of having a single national securities regulator as soon as possible.

The criminal offences and powers in the Act would, however, apply in all jurisdictions, including non-participating provinces, once the Act is in force. The Government has exclusive jurisdiction over criminal law in Canada and as the relevant offences would be transferred from the *Criminal Code* to the *Securities Act*, they would also apply nationally.

The regime provides for a formal opt-in process. Specifically, after receiving the written consent of the Lieutenant Governor in Council of a province or the Commissioner of a territory, and on the recommendation of the Minister of Finance, the Governor in Council could designate a province or territory as a participating province or territory. Before making a recommendation to designate a participating jurisdiction, the Minister of Finance would have to be satisfied that the single securities regulatory regime that is established by the Act would apply in the province or territory to be designated.

Reflecting the Government's willingness to work collaboratively with provinces and territories, this is a voluntary regime, which applies as willing provinces and territories opt in.
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Ensuring a smooth transition and integration that minimises disruptions is important to all stakeholders. As a key next step, the Transition Office will deliver the organizational and administrative transition plan this July. The plan will further elaborate a vision for the Canadian securities regulator and a high level road map for establishing it by building

on the infrastructure and expertise of participating provincial and territorial securities regulators. The plan will ensure that the resources of securities regulators from willing provinces and territories are effectively integrated so that, for example, employees will be able to find employment opportunities with the CSRA.

The Transition Office intends to begin discussions shortly with each participating province and territory for the purposes of coordinating the establishment of the CSRA and the implementation of the proposed securities regulatory regime.

Budget 2009 set aside \$150 million to enter into financial arrangements with participating provinces and territories as Canada moves from provincial and territorial securities regulators to a Canadian securities regulator.

Regulations will be required to address some of the legal issues related to the transition. For instance, regulations will be developed to address existing registrations, exemptions and enforcement orders and proceedings (regulatory, civil or quasi-criminal). The Transition Office will lead the development of the regulations and Tribunal rules during the transition period.

The Transition Office will seek input from the Advisory Committee, securities regulators and ministries responsible for securities regulation in participating provinces and territories and other stakeholders, throughout the transition and as it continues to develop the regime.

Next Steps

The CSRA is targeted to be established within the next three years. There are a number of necessary interim steps.

The Government has referred the Act to the Supreme Court of Canada for an opinion as to whether the Act is within the legislative authority of the Parliament of Canada. The Government is confident that Parliament has the necessary constitutional authority to implement the Act. An opinion from the Supreme Court of Canada will provide legal certainty to all provinces and territories, and market participants.

Should a favourable opinion be received from the Supreme Court of Canada, the Government intends to introduce the proposed Act in Parliament as a bill, which will follow the normal legislative process. It is envisaged that consequential amendments to existing federal legislation and to participating provinces' and territories' securities statutes will be required.

In the interim, details of the transition plan will be refined in consultation with participating provinces and territories.

Contact Information

For further information on the proposed Canadian *Securities Act*, please contact:

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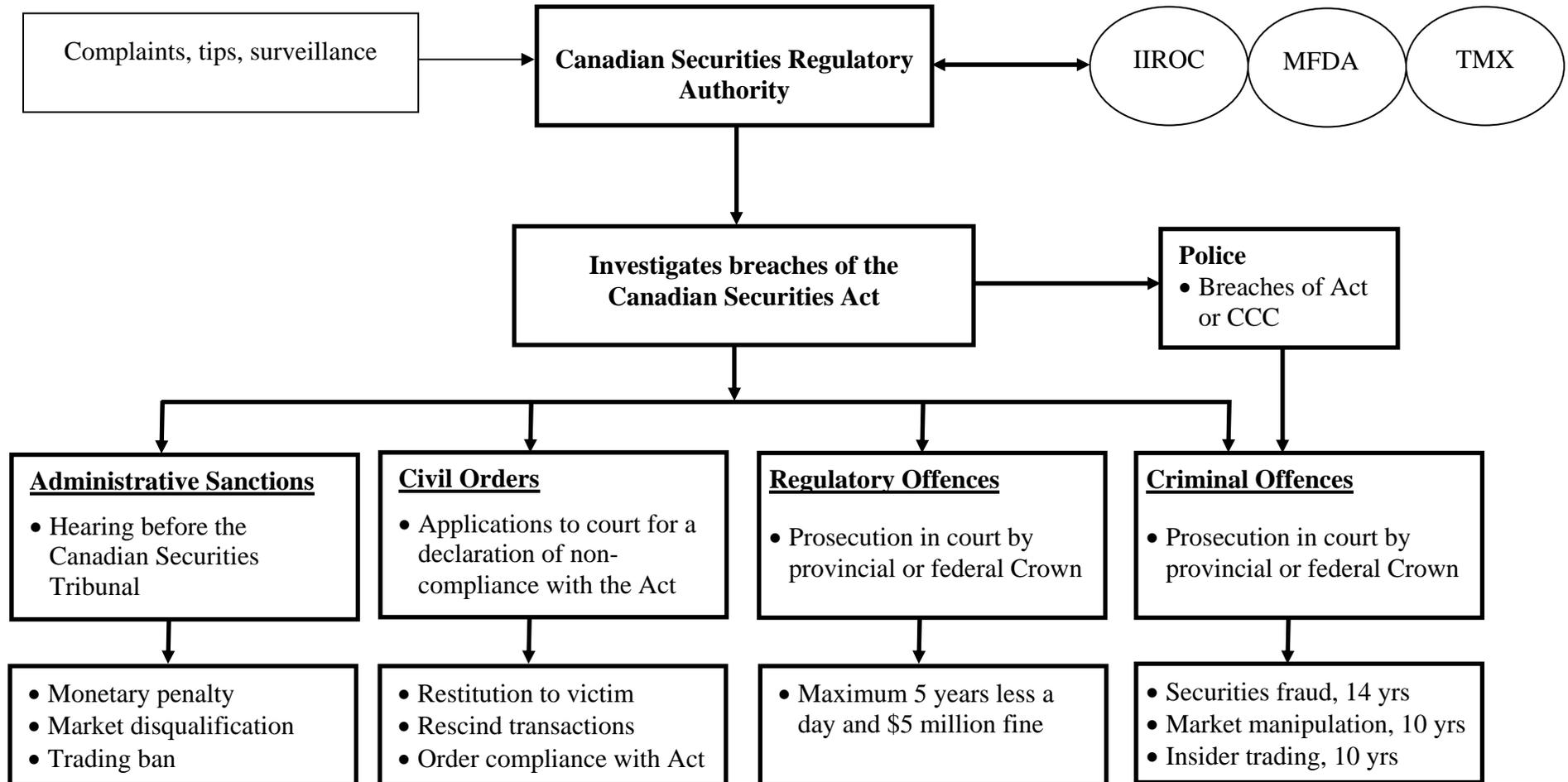
Annex A: Timeline

Long standing priority and commitment – Budgets 2006, 2007, 2008, 2009, and 2010

January 2009	Expert Panel report
July 2009	Transition Office launched
October 2009	Advisory Committee of Participating Provinces and Territories created Intention and timing of constitutional reference announced
May 26	Proposed Canadian <i>Securities Act</i> tabled for information and submitted to Supreme Court of Canada for reference
July 2010	Transition Plan released by the Transition Office
Fall 2010	Development of agreements and financial arrangements Infrastructure and administrative plan refined Drafting of regulations initiated
2011	Opinion from the Supreme Court of Canada (expected) Introduction of bill Recruitment of initial board and executives
2012-13	CSRA is launched

Annex B:

Overview of the CSRA's Enforcement Regime



Annex C:

Examples of How New Evidence-Gathering Tools May Support Criminal Investigations

Production Order—Names

To support a criminal investigation related to unusual trading activity in a stock of a public company just days before the release of important regulatory filings (e.g., quarterly financial results), it would be helpful to know the names of people who traded in the stock just prior to the announcement. The Act establishes a new production order that would allow criminal investigators to more easily obtain the names of individuals (apart from insiders required to report such information) that traded a particular stock over a specified period of time (e.g., in advance of an important announcement). Criminal investigators would be able to get a court order for the production of the names of the broker-dealers who placed the trades from stock exchanges if there are reasonable grounds to suspect that an offence has been committed. In addition, a court order requiring the brokerage houses to provide a list of the names of individuals on whose behalf trades were placed and the dates and times of the trades could also be obtained. Without this tool, criminal investigators would need to show that they reasonably believed (not just suspected) that an offence has been committed in order to obtain a warrant under the *Criminal Code*. Obtaining a warrant is very difficult in the absence of a means of discovering the names of the people who traded in the securities. The information obtained using this new tool would give criminal investigators information necessary to build cases involving trading-based offences, including insider trading, tipping, and market manipulation.

Production Order—Written Statement

Investigating capital markets crime is complex, often involving making sense of vast amounts of financial and accounting information. The ability to obtain additional information from companies that have some connection to the alleged misconduct would help to make investigations more thorough and timely. The Act establishes a new production order that would require certain companies to respond to questions which are set out in writing. This additional tool would allow criminal investigators to get a court order when they have reasonable grounds to believe that an offence has been committed, requiring companies to produce answers to their questions, they would not otherwise be able to obtain. Questions may be related to how information flows between employees and senior management, discussions that took place in certain meetings, and who had access to certain sensitive information.

Civil Immunity Provision

Anyone can become aware of a situation where authorities should be notified to safeguard the integrity of capital markets. For example, an employee may believe that there is some form of wrongdoing going on in their workplace. The employee may be

reluctant to report it to the authorities for fear of breaching a confidentiality agreement, or otherwise being exposed to civil liability. For the same reasons, the employee may have concerns about cooperating if approached directly by authorities with questions. The Act would protect individuals in these types of situations. Under the Act, individuals receive immunity from being sued for cooperating and disclosing information to the CSRA or police that they reasonably believe is true. The protection this new measure affords would encourage more individuals to come forward to disclose wrongdoings or share information with investigators.

Annex D:

Proposed Structure for the Canadian Securities Regulatory Authority

