Direct Dial: (416) 216-3935
tdobbin@ogilvyrenault.com

BY COURIER

August 28, 2002

Five Year Review Committee
c/o Purdy Crawford, Chair
Osler, Hoskin & Harcourt LLP
Barristers & Solicitors
Suite 6600
Box 50, 1 First Canadian Place
Toronto, Ontario M5X 1B8

Dear Sirs/Mesdames:

RE: Five Year Review Committee Draft Report

This letter is submitted in response to the request for comments made by the Five Year Review Committee (the "Committee") in its draft report (the "Draft Report") dated May 29, 2002. We understand that the Committee is accepting comments until August 30. We have comments on the following chapters and sections of the Draft Report:

Chapter 1: The Need for a Single Regulator

As outlined in the Draft Report, the fragmented system of securities regulation in Canada is unnecessarily costly and complex. In the face of increasing globalization and the dismantling of impediments to capital flows, we believe that Canadian capital markets will be increasingly by-passed. There can be little doubt that the best way to ensure that Canadian capital markets remain attractive is through the creation of a national securities regulator; unfortunately, we do not believe there is any realistic prospect of this occurring.

As the Committee indicates, there have been several failed attempts to move to a national system of securities regulation. The Draft Report has laudably pushed the concept of a national securities regulator into the public consciousness to a degree not experienced in previous memory: letters were written and statements made supporting the creation of a national securities commission which received a surprising amount of media attention. Yet, it appears to us that governments remain unmoved. National securities regulation could not be placed on the

agenda of the provincial premiers at their recent conference, despite the concerted efforts of its supporters. We must reluctantly conclude that the political will necessary for the creation of a national securities regulator does not exist: a situation that we believe is unlikely to change. We think this is the political reality the Minister must deal with when considering changes to Ontario securities regulation.

We are not arguing that no attempt to create a national regulator can be made simply because it is almost certain to fail. The case for a national securities commission is so compelling that another tilt at the windmill may well be warranted, but only if it is clear that no injury will result from the fall. We are concerned that trying to address the troubling issues raised in the Draft Report in the context of a "final push" to a national securities regulator may impede or delay implementation of other, more achievable, solutions to these issues. Although a unilateral push may not necessarily create an equal and opposite reaction from those being pushed, it is unlikely to produce the environment necessary to achieve the consensus that will be required to effectively address these issues. Furthermore, a focus on the creation of a national securities regulator would divert focus from what we believe is urgently required: increased harmonization of Canadian securities laws and co-operation amongst Canadian securities regulators. Although the Draft Report also supports increased harmonization and co-operation, we respectfully suggest that categorizing these goals as interim steps may unnecessarily prejudice their achievement.

We believe that Ontario must take the lead in promoting harmonization and co-operation. This will require that Ontario balance its role as the regulator of Canada's largest capital market (which will often require it to be at the forefront of regulatory initiative) with the urgent need to improve harmonization and co-operation (which will often require regulatory restraint). The area where this balance is most critical is the exercise by the Ontario Securities Commission (the "Commission") of its rule-making authority.

We believe the goals of increased harmonization and co-operation should be given greater weight in the development of rules and policies by the Commission. We recognize that the Commission must retain the ability to act in the public interest even if the result is to further fragment the Canadian securities regulatory regime, but we would suggest that this should be the exceptional case. The Draft Report suggests the "most pressing securities regulation issue" across Canada is the need for a single securities regulator. In the absence of such a regulator, the Commission should recognize the need for coherent, harmonized Canadian regulation when exercising its rule-making authority.

We would propose that when exercising its rule-making authority the Commission should:

(i) adopt rules that have the effect of increasing the degree of harmonization and co-operation;

(ii) make every effort to have the same rule adopted by the other Canadian securities regulatory authorities (to the extent necessary); and

(iii) not adopt any rule that has the effect of lessening the degree of harmonization or co-operation, unless such rule is required in the public interest notwithstanding such effect.

We recognize that the Commission currently bears the foregoing principles in mind to some degree when exercising its rule-making authority; however, given the critical need to increase harmonization and co-operation, we would suggest that these principles should be formally entrenched and specifically addressed in the rule-making process. Moreover, we believe harmonization efforts among Canadian securities regulatory authorities should become more transparent. We would hope that increased transparency would encourage co-operation.

We would suggest that the notice accompanying a proposed rule or policy should:

(i) discuss the expected effect of the new rule or policy on harmonization and co-operation;

(ii) describe the efforts the Commission has made to have the new rule or policy adopted by the other Canadian securities regulatory authorities (to the extent necessary) and the positions of each of the authorities as understood by the Commission; and

(iii) if adoption of the proposed rule or policy is expected to lessen harmonization or co-operation, describe the reason the Commission believes it is in the public interest to adopt the new rule or policy notwithstanding this effect. The Commission should be required to explain why the benefits of the new rule or policy outweigh the costs associated with further regulatory fragmentation.

We strongly support the recommendations contained in the Draft Report aimed at improving co-operation among securities regulators. As the Draft Report points out, increased harmonization is not itself enough. A system of true mutual reliance should be implemented. We believe a system of true reliance, together with a stepped-up effort to harmonize, can effectively address most (if not all) of the issues raised in the Draft Report. Moreover, we believe the likelihood of successfully implementing such a system is considerably greater than the creation of a national securities regulator.

We recognize that some jurisdictions may fear that a system of true reliance could effectively eliminate their role in securities regulation. Although moving to a system of true reliance should have the effect of reducing duplication, we believe it can be accomplished in a way that preserves and even strengthens the roles of each of the authorities. Under the new system we propose, each of the securities regulatory authorities would be primarily responsible for enforcement actions against issuers and registrants located in their jurisdiction. It should be most efficient to have enforcement actions lead by people "on the ground", with necessary support from other authorities if additional expertise or resources are required. We would also propose that those jurisdictions that wish to assume a broader role in the new system be assigned specific responsibilities. Under the existing MRRS system, regulatory responsibility is largely determined by the location of the issuer. We would suggest that division of responsibility should be functional. For prospectuses, this would likely be by sector or type of issuer (e.g. energy, financial services, etc.). For other matters, the division could be issue-based (e.g. shareholder rights plans, stock-based employee compensation matters, etc.). In this way, regulators responsible for a particular area can develop greater expertise in the area, which would be relied upon by others. This would ensure greater consistency of treatment, improve timeliness of response and allow securities regulatory authorities to allocate their resources more efficiently.

We believe a harmonized system of securities regulation, together with true reliance among regulators, can address virtually all of the issues raised in the Draft Report. Such a system, while admittedly falling short of the holy grail of a national regulator, has the advantage of being more politically palatable and, we believe, more achievable. We would respectfully suggest that the provinces and territories should be encouraged to rapidly develop and implement such a system.

Chapter 4: Objectives of the Act

Section 4.2 - Principles to Consider

As discussed above, we are concerned that the existing regulatory regime will lead to the increasing irrelevance of the Ontario capital markets. The Committee has recommended that the principle that "Capital markets are international in character and it is desirable to maintain the competitive position of Ontario's capital markets" be added to the Act. We agree that it is important to entrench this principle and, more importantly, to take the steps necessary to ensure competitiveness.

Chapter 5: Structure of the Act

Section 5.1 - Should the Act be Overhauled?

We agree that, given the existing regulatory regime, a complete overhaul of the Act while perhaps desirable is not realistic. Unless each of the provinces and territories were to engage in a

similar exercise in a co-ordinated fashion (an unrealistic prospect), a unilateral overhaul would likely have the effect of lessening harmonization.

Section 5.2 – Enriching Core Concepts

In addition to the core concepts referred to in section 5.2 of the Draft Report, we would also suggest that the following are of sufficient importance and in the nature of general principles such that they should be included in the Act:

(i) the "know your client" rule;

(ii) an anti-fraud on the marketplace concept (see recommendations 80 and 81 of the Draft Report and our comment on section 22.2(a) of the Draft Report); and

(iii) a recognition that safe harbours are appropriate in certain circumstances and may be provided for in the rules.

Chapter 6: Rulemaking

Section 6.2 - Scope of Rulemaking Authority

We agree with the recommendation that the Commission be given "basket" rulemaking authority as formulated, especially given the competition for legislative time and the fact that securities regulation rarely figures prominently on legislative agendas. It is our view that the Commission possesses the proper expertise to develop and propose new rules and there are sufficient safeguards in the system to ensure that such power is not abused, particularly if our recommendation with respect to the need for affirmative Ministerial approval is adopted (see our comment on section 6.3 below). We also think "basket" rulemaking authority will be particularly helpful in allowing the Commission to respond to and, where appropriate, duplicate regulatory initiatives in other Canadian jurisdictions.

Section 6.3 - The Need to Streamline the Rulemaking Process

We agree with the recommendation that the minimum initial comment period for rules be reduced from 90 to 60 days and that the minimum initial comment period for policies be reduced from 60 to 30 days. We would, however, discourage the Commission from applying this as a hard and fast rule and suggest that it continue to accept comments that may be received outside the period where appropriate and make appropriate allowances for the traditional summer and winter vacation periods.

We believe that Ministerial approval or disapproval should be required as an active step in the rulemaking process as opposed to the current regime which provides for the lapse of time to

constitute non-disapproval. In our view, such an approach would ensure that the Minister has actively considered and supports any new rule.

Chapter 10: Continuous Disclosure

Section 10.1 – The Importance of Continuous Disclosure

We agree that in order to foster investor confidence continuous disclosure must be timely and reliable. We would add, however, that it is equally important that information be accessible to, and comprehensible by, the average investor. The method, style and nature of disclosure should assist in promoting an understanding of the issuer, its securities and the market. Market participants and regulators should be encouraged to implement a disclosure regime that provides comprehensible information to investors, including the increasing number of retail investors who make investment decisions without the benefit of advice from any registrant. Fulsome disclosure is not useful if investors do not understand it or are so intimidated by its volume and complexity that they ignore it. The Committee's recommendations should include a mandate to formulate a disclosure system that promotes concise and clear, as well as fulsome, disclosure. Use of "plain English" should be encouraged.

As a complement to the focus on improving the quality of continuous disclosure, and consistent with the Committee's recommendations 22 and 23, consideration should also to be given to improving public access to such information by, for example, requiring issuers to maintain a web-site with a link to SEDAR that provides a description of what can be found on the SEDAR site (or encouraging issuers to post all SEDAR-filings on their corporate web-sites, as recommended by National Policy 51-201 Disclosure Standards) and improving SEDAR to make it more user-friendly (e.g. improved search and sorting capabilities; and improved filing categories and document descriptions).

Chapter 16: Take-Over Bid Regulation

Section 16.3(b) – Defensive Tactics

To the extent that a proposed policy statement on the proper use of shareholder rights plans will merely summarize the body of decisions that have been issued by the Commission, we question the value added by this approach. Furthermore, it is questionable whether the existence of a non-binding policy statement will actually result in fewer hearings. Parties will be in the same position of referring to the guidance culled from Commission decisions as that contained in a policy statement when trying to decide whether a rights plan should be terminated.

If, on the other hand, the Commission is inclined to provide additional guidance on the appropriate circumstances under which rights plans should be terminated beyond that which is currently reflected in Commission decisions, we would support the formulation of such a policy

statement as a useful decision-making tool that may assist boards of directors in formulating an appropriate response to hostile bid situations.

Chapter 17: Mutual Fund Governance

Section 17.4 – How the Independent Governance Body Will Look

We agree that an independent mutual fund governance body established to oversee funds and fund managers would be the most appropriate entity to determine the number (and nature) of funds for which it will be responsible. The ability of a governance body to fulfil its mandate will depend, at least to a certain extent, upon co-ordinating the expertise of the individual members of the body with the range of funds under review and the types of investments made thereunder.

Section 17.6 – Should There Be Registration of Mutual Fund Managers?

While we agree that mutual fund managers should be subject to independent oversight of their capital adequacy, personnel proficiency and standards of business practice and that the independent governance body may be best situated to perform this oversight, our concern is that the governance body may not, at least initially, be the appropriate entity to establish the minimum standards to be met. Members of a governance body, particularly those recruited from non-traditional sources, will be faced with a steep learning curve. Issues such as capital adequacy and proficiency are complex and formulating appropriate guidelines will require expertise which, in our view, is most often found in regulatory authorities. We believe that a governance body will have (or will develop) sufficient expertise to effectively monitor compliance, but believe that, at least initially, minimum standards for mutual fund managers should be established by regulators. Leaving the establishment of such standards to the independent bodies, aside from creating a growth industry for costly consultants, may leave both investors and members of the independent bodies unfairly exposed.

Chapter 22 – Other Enforcement Matters

Section 22.1 - Confidentiality under Section 16

While we recognize that the purpose of section 16 of the Act is to protect the integrity of the investigation process, we remain concerned that the scope of subsection 16(1)(a) is too broad. Section 16 prohibits a corporation from disclosing a formal investigation not only to the public, but to its auditors, insurers, affiliates, underwriters, and possibly to its directors and officers (except in the latter case presumably to the extent necessary to discharge their supervisory or management responsibilities, instruct counsel and make decisions relating to the investigation), and even to other securities regulators (in both Canada, the U.S. and elsewhere). Consequently, the effect of the confidentiality provisions can be to severely restrict the ability of a corporation to report on the existence and status of an investigation to constituents who, in the circumstances, may have legitimate interests in such disclosure.

Mindful of recent initiatives to encourage more meaningful corporate disclosure, and putting aside the issue of witness collusion (which is always a possibility in any type of investigation (including criminal investigations undertaken by law enforcement) and, in our view, does not justify complete secrecy), we question whether a corporation that is itself (or whose officers or employees are) the subject of investigation should not have the ability to disclose the nature or content (or even existence) of an investigation order in circumstances where such disclosure is believed to be warranted. Arguably, the corporation is better situated than the Commission to determine, in the circumstances, whether disclosure of an investigation pertaining to it is necessary and to consider the impact that such disclosure may have on the corporation's reputation and the capital markets. While the existence and details of an investigation should certainly be kept confidential by the Commission, a corporation that is the subject of an investigation may have a legitimate interest in disclosing its existence and nature to the public generally or to third parties specifically (e.g., auditors, underwriters and insurers) who themselves may have a legitimate interest and a need to know.

Certainly there are examples of other administrative (and quasi-judicial) tribunals endowed with investigative powers (e.g. the Canadian Competition Bureau and the Ontario Human Rights Commission) where similar concerns arise and interests are in need of protection, yet investigations undertaken by these bodies are not the subject of such a tight seal of confidentiality. Furthermore, in the normal course of business, a corporation must always decide whether any other form of investigation, proceeding or legal matter is material and necessary disclosure. Section 11 investigations should not be treated differently.

The provisions of section 16 are too restrictive to accomplish the goal of protecting the integrity of the process. Their consequences can be to severely hinder a corporation from effectively dealing with the investigation and from properly evaluating the case being made against it. We encourage the Committee to consider recommending that section 16 be amended to address the issues raised above.

Additionally, we would recommend that section 17 be amended to address issues such as standing to bring an application for disclosure of an order and to provide applicants with an opportunity to be heard in the event that an application has been denied. As it currently stands, the decision ultimately rests with staff, with no specific recourse provided to the parties.

Section 22.2(a) - Fraud and Market Manipulation

We support the Committee's recommendation that the Act should be amended to include a prohibition on market manipulation and fraudulent activity, but caution against extending the offence to mirror Rule 10(b)5 under the Securities Exchange Act of 1934, to the extent that it would provide parties with private rights of action. We are of the view that any actions brought under these provisions should be restricted to those initiated by the Commission.

Section 22.2(b) - Misrepresentations

We agree with the Committee's recommendation to amend the Act to prohibit a person or company from making a statement, whether written or oral, that it knows or ought to know is a misrepresentation. We point out, however, that, in light of the Committee's recommendation to impose civil liability for secondary market disclosure (section 10.6), it may not be appropriate to limit such prohibition to statements made with the intent of effecting a trade.

Section 22.3 - Insider Trading

We do not believe that the insider trading civil liability provisions should be broadened by eliminating the privity requirement. While dispensing with the need for investors to demonstrate reliance in the context of secondary market liability for misrepresentations may make sense (on the basis that investors may suffer damage indirectly due to the effect that the misrepresentation has on the market price of a security), the same reasoning should not be applied to instances of insider trading. The actions of an insider are not themselves the cause of any price fluctuations -- it is the undisclosed information, when made public, that may effect the price – and, accordingly, the notion that investors who, by mere coincidence, buy or sell securities at the price received or paid by the insider have suffered "damage", even indirectly as a result of the insider's actions, is insupportable.

Additionally, we question how the quantum of damages would even be assessed where privity is not required. Unlike subsection 122(4) where the fine payable to the Commission is tied to the monetary benefits incurred by the offender, in determining financial penalties whose purpose is compensatory, would the insider be liable to compensate all investors who have purchased securities at the relevant time or price for their losses, which could far exceed the profit made or losses averted by the insider?

Section 22.4 - Insider Reporting

In light of the increased scrutiny that insider reporting has been subject to recently, it is imperative that, in order to avert erroneous reporting (or under-reporting) of trades, the insider reporting regime be user-friendly so that individuals can easily determine when disclosure of trades is required and the nature of that disclosure. Although SEDI was created to facilitate disclosure by insiders and provide for easier public access, its establishment (and operational difficulties), together with the new prescribed paper form, have resulted in confusion and uncertainty for issuers and their insiders, particularly in the context of derivatives. We believe that the Commission should formulate clear guidelines to assist insiders in fulfilling their reporting obligations in respect of derivatives. If legislative changes are required in order to provide regulators with the requisite jurisdiction, they should be pursued.

This letter has been prepared by the Securities Law Group of our Toronto office. If you have any questions concerning our comments, please contact Terry Dobbin (Direct: (416) 216-3935, E-mail address: tdobbin@ogilvyrenault.com or Ava Yaskiel (Direct: (416) 216-3902, E-mail address: ayaskiel@ogilvyrenault.com), each of whom can be reached by fax at (416) 216-3930.

Yours very truly,