

Chapter 6

Request for Comments

6.1.1 OSC Notice 11-753 (Revised) – Request for Comments Regarding Statement of Priorities for Fiscal Year Ending March 31, 2011

OSC NOTICE 11-753 (REVISED)

REQUEST FOR COMMENTS REGARDING STATEMENT OF PRIORITIES FOR FISCAL YEAR ENDING MARCH 31, 2011

The *Securities Act* requires the Commission to deliver to the Minister and publish in its Bulletin each year a statement of the Chairman setting out the proposed priorities of the Commission for its current fiscal year in connection with the administration of the Act, the regulations and rules, together with a summary of the reasons for the adoption of the priorities.

In an effort to obtain feedback and specific advice on our proposed objectives and initiatives, the Commission is publishing a draft Statement of Priorities which follows this Request for Comments.

The schedule for publishing its draft Statement of Priorities occurs much earlier this year. This will allow us to receive feedback earlier so that it can be better integrated into our planning and budgeting process. The Commission will consider the feedback, and make any necessary revisions prior to finalizing and publishing its 2010/2011 Statement of Priorities. The Statement of Priorities, once approved by the Minister, will serve as the guide for the Commission's ongoing operations. Shortly after the conclusion of our 2009/2010 fiscal year we will publish a report on our progress against our 2009/2010 priorities on our website.

Comments

Interested parties are invited to make written submissions by February 15, 2010 to:

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ONTARIO SECURITIES COMMISSION
2010-2011

STATEMENT OF PRIORITIES – REQUEST FOR COMMENTS

DECEMBER 2009

Introduction

The *Securities Act* (Ontario) requires the Ontario Securities Commission (OSC) to publish in its Bulletin and to deliver to the Minister by June 30 of each year a statement by the Chair setting out the proposed priorities for the Commission for the current financial year.

This Statement of Priorities sets out the OSC's strategic goals and specific initiatives for the 2010-11 fiscal year in support of each of its goals. It also discusses the environmental factors that we considered in setting these goals.

The OSC remains committed to delivering its regulatory services with effectiveness and accountability and to working closely with its colleagues within the Canadian Securities Administrators (CSA) and with market participants to ensure that the regulatory system remains relevant to the changing marketplace.

Our Vision

To be an effective and responsive securities regulator – fostering a culture of integrity and compliance and instilling investor confidence in the capital markets.

Our Mandate

The OSC's mandate is to provide protection to investors from unfair, improper or fraudulent practices and to foster fair and efficient capital markets and confidence in capital markets. The mandate is established by statute.

Our Environment

The OSC vision and mandate underlie our business plan, and the goals and priorities we set each year. We also take into account environmental factors that could affect our organization. We have set out below a discussion of the main environmental factors that currently affect our work and that we expect will affect new work we plan to undertake over the next few years. Specific initiatives are set out later in this document.

Pace of Change

Capital markets, in Ontario and in other jurisdictions, have experienced significant structural change in recent years, including shifts from single marketplaces to multiple and increasingly complex marketplaces. At the same time, there has been a proliferation of complex securities products and investment advice (including the use of leverage, derivatives and exposure to commodities) and an increasing technological sophistication in the operations of market participants. Investors may not sufficiently appreciate the risks associated with novel investment options or new technologies. This is a particular concern in the current low interest rate environment in which many investors are trying to rebuild their portfolios after the recent market downturn.

These new realities, their impacts, the speed with which they arise, and the increasingly subtle and intricate nature of their consequences demand an adaptive, balanced and informed regulatory response.

Innovations, whether in products, market structures or distribution channels can challenge established approaches to understanding them and developing appropriate regulatory responses. New information/data will be required along with analytical approaches to ensure informed appreciation of their impact.

Regulatory Gaps and Coverage

Having an appropriate scope of regulatory authority is important to achieving the OSC's mandate. Recent market turmoil and the accompanying financial crisis have led some to observe that regulatory coverage has been uneven. For example, differing regulatory approaches to essentially similar products (such as investment funds and other managed investment products) or to similar activities conducted by different types of registrants can unintentionally reduce market competitiveness or undermine investor protection. At the same time, these inconsistencies may pose risks to investors who may be unaware of the differences. When combined with rapid product and market evolution, uneven regulatory coverage may also contribute to increased overall risk.

We remain committed to ensuring our regulatory regime applies to the full range of markets, market participants and products at play. Investor protection cannot be truly effective without assessing the extent to which derivatives, exempt markets, credit rating agencies and other areas are adequately supervised. We will need to consider whether the current level of regulation of these areas is appropriate and we will need to co-ordinate our efforts with those of other regulators and self-regulatory organizations.

The financial crisis also revealed weaknesses in the global financial regulatory system, highlighting the need for a co-ordinated global response to address systemic risk and develop a more effective system of oversight and regulation. Addressing regulatory gaps will require continued collaboration with the International Organization of Securities Commissions and other international standard setters and regulators to implement the G20 action plan.

In the Canadian capital markets, we will need to actively contribute to the discussions and work underway to redesign the regulatory framework to better address systemic risk. This will involve working with partners such as Office of the Superintendent of Financial Institutions, the Bank of Canada, insurance and other securities regulators.

Deepening Investor Focus

We recognize that new ways to effectively gauge and incorporate investor perspectives are necessary to achieve and enhance investor protection. This requires a flexible regulatory approach that can adapt to the diverse range of interests, demands and concerns. For example, investor demands and needs differ depending on whether an investor is researching potential investments, executing an investment transaction or protecting security holder rights once an investment has been made.

We will continue our work to ensure Ontario securities laws address the needs of investors throughout the investing cycle. To help prospective investors make informed investment decisions, we plan to better understand the information investors need, as well as how and when they need this information.

We will continue to monitor compliance with Ontario securities laws to ensure that market participants meet the regulatory standards for disclosure and advice that investors require.

Growing Public Expectations/Accountability

In light of recent market developments, market participants and industry watchers have called for regulators to move faster and more decisively in responding to potential problems. While the OSC seeks to be responsive to these demands, our response must be balanced and guided by our mandate, the scope of our authority and our operational capabilities.

Providing transparency and accountability in our operations requires going beyond demonstrating that our resources are effectively utilized. We are imposing greater fiscal discipline on all of our operations and we are prudent in our spending. While we will ensure that our spending is restrained, we remain focused on achieving our key priorities and fulfilling our mandate effectively. We will continue to use a disciplined risk assessment approach to focus resources on our highest priorities and clearly report on outcomes achieved.

Accountability to Ontario's investors and market participants is integral to the planning and implementation of the OSC's operational priorities. Effectively listening to and communicating with interested stakeholders is essential to meeting the challenges we face in fulfilling our mandate and addressing expectations about what we can accomplish. We will continue to outline our regulatory goals and outcomes, how we seek to achieve these goals and outcomes, and the challenges we face. OSC management and staff are accountable to fulfil the OSC's dual mandate. We will work with integrity, professionalism and efficiency.

Our Goals

Goal 1 – Identify the important issues and deal with them in a timely way.

Our goal is to deal with today's concerns, while anticipating tomorrow's challenges. We want to be a strategic leader in fulfilling our mandate to Ontario investors and Ontario capital markets.

Goal 2 – Deliver fair, vigorous and timely enforcement and compliance programs.

Timely and appropriate compliance and enforcement are integral to fostering confidence in capital markets and preventing harm to investors.

Goal 3 – Champion investor protection, especially for retail investors.

The interests and needs of investors, particularly retail investors, will continue to be strongly reflected in all the OSC's operations. In addition to our enforcement activities, investor education and awareness, and timely access to accurate information are important components of investor protection.

Goal 4 – Support and promote a more flexible, efficient and accountable organization.

The OSC's strength is its people. We will make the best use of all our resources, including people, technology, research and financial, to achieve timely and effective execution of all that we do.

We expect OSC Commissioners and employees to maintain the highest standards of conduct and personal integrity, and to deal openly and fairly with all of our stakeholders. We will continue to constantly improve our business competence and effectiveness.

In delivering on our goals we will:

- Be responsive and flexible as an organization, and treat all stakeholders with respect and fairness;
- Consult and collaborate with investors, issuers, intermediaries, other industry participants and professionals to identify important issues;
- Continue to reflect investor interests in all that we do;
- Continue to support investor education initiatives;
- Continue to examine approaches to securities regulation used by other Canadian and international jurisdictions to assist us in providing a balanced regulatory approach and adopting best regulatory practices;
- Seek to render fair, clear, cogent and consistent adjudicative decisions quickly and cost effectively;
- Use the full range of tools available to achieve our mandate, and assign priorities to all our work based on our strategic goals;
- Continuously monitor and improve the efficiency and effectiveness of our operations; and
- Identify skills requirements and ensure that we attract, retain and motivate staff who possess the required skills.

Key Regulatory Priorities for 2010-11

In light of the environmental factors outlined above, we have identified five broad priorities for 2010-11. These priorities are set out below. In addition, we will carry out a number of smaller initiatives as well as ongoing operational programs in order to achieve our mandate.

We are also committed to supporting the Canadian Securities Transition Office, other provincial securities regulators and the Ontario Ministry of Finance, with the development of a national securities regulator. We believe the OSC has much to offer in terms of experience and expertise.

1. Deepen our Focus on Investor Protection

Build on the work undertaken in response to the Standing Committee on Government Agencies by focusing on issues relevant to investors at specific stages of the investment process as follows:

At the investment decision-making stage:

- promote clear and informative disclosure that allows investors to make informed investment decisions; and
- leverage the work of the OSC Investor Steering Committee through the OSC website.

Related to transaction or trade execution:

- implement the order protection rule; and
- implement new complaint handling, conflicts and referrals regime for registration.

For investors who own securities:

- review protections for shareholders rights and corporate governance;
- define guidelines or standards for performance and cost reporting information, including electronic delivery; and
- updating the early warning disclosure regime for takeover bids and proposing revised Commission policy on defensive tactics.

2. *Respond to Market Developments*

Review and analyze market developments to develop or modernize regulatory responses related to:

- the implementation of International Financial Reporting Standards in 2011;
- methods of trading (such as direct market access) and new structures (new order types and facilities such as dark pools) that may impact transparency, access and fairness; and
- regulation of alternative trading systems (ATs) and exchanges and update rules as necessary.

3. *Address Adequacy of Regulatory Coverage*

The recent financial crisis has shown that issues arising in areas of the market that are, relative to others, less regulated can have adverse impacts on both investor protection and market efficiency. In extreme conditions this can be an indication of systemic risk. Recognizing this, we plan to review and assess the regulation of both products and distribution practices with an emphasis on areas where jurisdiction is shared or needs to be confirmed. As necessary, we will pursue appropriate regulatory authority to allow us to effectively discharge our mandate. Specific areas to be addressed include:

- Risks related to products and distribution of securities in the exempt market;
- The regulatory framework for trading over-the-counter derivatives;
- Regulatory requirements applicable to non-conventional investment funds;
- Disclosure and operational rules applicable to scholarship plans; and
- The appropriate regulation of credit rating agencies.

4. *Maintain a Strong and Visible Enforcement Presence*

Our focus on enforcement activities is designed to protect investors and markets from abuse. Effective enforcement involves identifying the most serious risks associated with breaches of the *Securities Act* (Ontario) and taking actions to deter undesirable behaviours. It includes removing participants who do not comply with securities laws from our capital markets.

We strive to treat all market participants fairly and with integrity, and to be consistent in our approach and the sanctions we impose. Our work to improve the effectiveness of our enforcement will focus on the following areas:

- Continuing to refine our processes to reduce timelines for completing investigations and bringing regulatory proceedings forward;
- Improving deterrence by pursuing increased collaboration with other regulators and law enforcement agencies, including the provincial Office of the Attorney General, to identify more cases for prosecution in criminal court and seek stronger sanctions;

- Addressing information leakage relating to trading events by focusing on market participants and their advisors holding positions of substantial influence or trust; and
- Improving our regulatory surveillance and analysis by making greater use of automated tools to identify data anomalies.

5. *Improve the Way we Work*

We remain committed to improving our business capability and our accountability to stakeholders. We plan to improve our operational performance through process improvements and greater use of technology, including:

- Making changes to OSC tribunal case management processes to accelerate the adjudication process;
- Making greater use of e-delivery of specific reporting documents, including enhanced web access to information; and
- Continuing to develop more comprehensive internal performance reporting and measurement.

2010-11 Financial Outlook

OSC Revenues and Surplus

Securities market participants fund our operations through fees they pay. The current fee structure under the *Securities Act* (Ontario) and the *Commodity Futures Act* was established in 2003. The fee model is intended to recover our costs of operation in fulfilling our mandate while allowing us to remain financially stable. When we implemented the fee model, we committed to re-evaluate our fee levels every three years.

Achieving the appropriate balance can be challenging because most of our costs are relatively fixed, while our revenues fluctuate with market activity. From 2003 to 2008, the OSC generated accumulated surpluses. These surpluses were largely due to higher than anticipated market growth in that period. We were able to defer a fee increase in 2009-10 by using a portion of these surpluses in 2009-10. As a result, our fees have not changed since April 2006.

On October 2, 2009, we published proposed revised fee rules for public comment. The comment period closes December 31, 2009. The fees proposed are forecast to allow us to achieve cost recovery by the end of fiscal 2013. In order to minimize the impact on market participants, we forecast fully using our accumulated surplus and a portion of our reserve over the next three fiscal years.

Activity Fees – Under the proposal, most of the activity fees would remain unchanged from the rates set in 2006. The proposed increases on the remaining fees are due to increased complexity of the activity. None of the proposed changes is expected to have a material impact on market participants.

Participation Fees - Total participation fees paid by market participants would rise by a weighted average of 12.2% per year. This would result in increases of approximately 9% per year for registrants and 17% per year for issuers from the participation fees set in 2006. However, the issuers' participation fees for comparable fee tiers would be less in each of the years covered by the proposed amendments (2011 to 2013) than in 2003, when these fees were first set. The difference in fee increases proposed for issuers and registrants is to better align revenues generated from each group with its level of participation in the Ontario capital markets.

Even with these fee increases, we expect to operate at a deficit for each of the next three years. For the three years ending March 2013, we project operating costs will exceed revenues by \$25.4 million. This deficit will be offset by applying the expected March 2010 surplus of \$24.8 million and \$600,000 of our operating reserve.

OSC 2010-2011 Budget Approach

In developing our 2010-11 budget, we will carefully balance the need for restraint with our duty to achieve our mandate of providing protection to investors and fostering fair and efficient capital markets. Our Board of Directors and management are committed to prudently managing our budget and expenditures. We strive to provide value-for-money to our stakeholders and ensure that we deliver efficient and quality services.

Request for Comments

Challenging economic conditions continue to put significant pressure on market participants and our own operations. Our preliminary budget estimate for 2010-11 reflects a projected increase of \$2.5 million or 3.0% over forecast 2009-10 spending.

2011 Budget versus 2010 Forecast

<i>(Thousands)</i>	2011 Budget	2010 Forecast	Change	% Change
Revenues	\$ 70,200	\$ 61,900	\$ 8,300	13.4
Expenses	<u>86,400</u>	<u>83,900</u>	<u>2,500</u>	3.0
Deficiency of Revenue compared with Expenses	(16,200)	(22,000)	5,800	

Decisions on OSC key initiatives and budget allocations for 2010-11 will be completed following the comment period for this Statement of Priorities document. Additional details on the specific areas of spending will be included in our final Statement of Priorities.