Management's Discussion and Analysis

The financial statements present the results of the Ontario Securities Commission for the year ended March 31, 2003 with March 31, 2002 comparatives and accompanying notes. The following comments provide an analysis of the factors which affected the Commission's operations during 2003 as well as the factors that reasonably may be expected to impact on future operations and results. The document should be read in conjunction with the financial statements.

Analysis of Operating Results

Excess of Revenue over Expenditures

Excess of revenue over expenditures for the twelve months ended March 31, 2003 was $14.6 million (2002 - $30.1 million). The general operating surplus as at March 31, 2003 was $7.0 million (2002 - $9.4 million).

In accordance with the provisions of the *Securities Act*, the Minister of Finance has requested the Commission to remit funds that are surplus to its operating requirements to the Province. During the twelve month period, the amount distributable from the Commission to the Province was $16.9 million (2002 - $20.0 million).

Actual Results Compared to Budget

Revenue is over budget because a planned 10% fee decrease was not implemented. Expense overspending occurred due to a one time, unbudgeted payment of $2.0 million to CDS Inc. which related to cost overruns on implementation of the National Registration Database system. Capital expenditures are over budget because renovation related costs were $665k higher than expected and were only partially offset by underspending on information technology capital which was $204K under plan.

2003 ACTUAL versus BUDGET

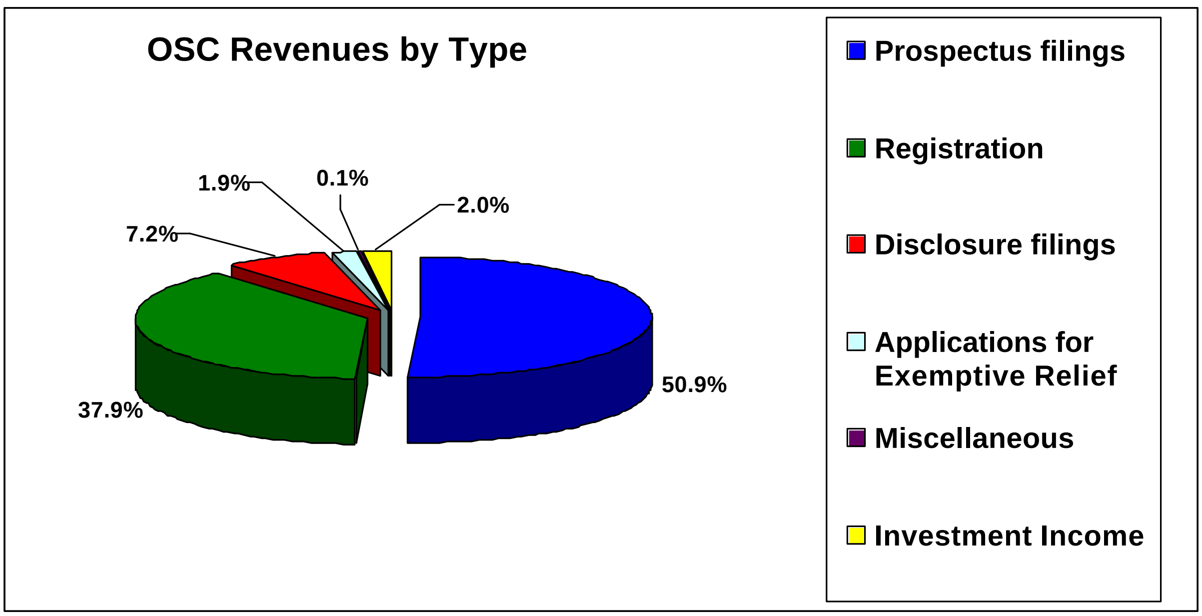
	ACTUAL ($000'S)	BUDGET ($000'S)	VARIANCE ($000'S)	VARIANCE %
Revenues	70,473	63,296	7,177	11.3
Expenses	55,874	53,807	(2,067)	(3.8)
Capital	2,232	1,755	(477)	(27.2)

Revenue

In 2003, $70.5 million was collected under the *Securities Act* and the *Commodity Futures Act*. Total revenue for 2002 was $79.9 million. This represents a decrease of $9.4 million or 11.8%.

REVENUE	Total Revenue	2003	2002	Change	Change
	%	$$$ Thousands			%
Prospectus filings	50.9	35,854	43,540	(7,686)	(17.7)
Registration	37.9	26,725	27,617	(892)	(3.2)
Disclosure filings	7.2	5,106	6,100	(994)	(16.3)
Applications for exemptive relief	1.9	1,311	971	340	35.0
Investment income	2.0	1,375	1,552	(177)	(11.4)
Miscellaneous	0.1	102	114	(12)	(10.5)
Total	100.0	70,473	79,894	(9,421)	(11.8)

The Commission has five primary sources of revenue:



Prospectus filings, comprising fees for preliminary and final filings and mutual fund renewals, were $35.9 million and accounted for 50.9% (2002 - 54.5%) of total revenues. Prospectus filings fees are strongly correlated to the overall level of capital market activity. Prospectus revenue fell by $7.7 million due to a decline in market financing activity by issuers as well as lower mutual fund fee revenues. These fees represent the most variable component of the Commission’s revenue base.

Registrations, comprising fees for registration of dealers, advisors and salespersons, were $26.7 million and accounted for 37.9% (2002 - 34.6%) of total revenues. Registration fees decreased by $0.9 million or 3.2% reflecting timing issues related to the introduction of a uniform registration date.

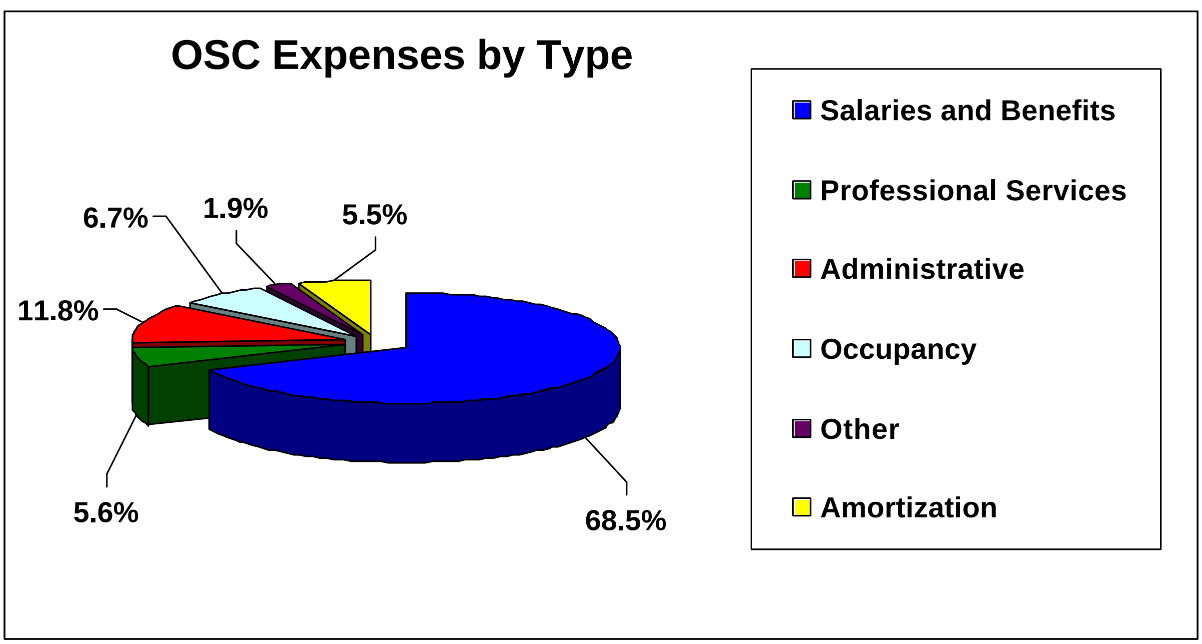
Disclosure filings, comprising fees related to filings by reporting issuers, were $5.1 million and accounted for 7.2% (2002 - 7.6%) of total revenues. Lower takeover bid activity was the cause of this 16.3% revenue decrease.

Applications for Exemptive Relief, comprising fees from issuers seeking exemptions or modifications to filing requirements, increased by 35.0% to $1.3 million and represented approximately 1.9% (2002 - 1.2%) of total revenues. This increase can be explained by one significant filing ($580K) received during the year.

Investment Income is comprised mainly of interest earned on cash balances at a rate of 1.75% below the prime rate or 0.25% below bankers' acceptance, as well as interest earned on the reserve which is invested in short and mid term instruments through the Ontario Financing Authority. Investment income generated by deposits and other investments was $1.4 million and accounted for 2.0% (2002 - 2.0%) of total revenues. The decrease in investment income can be traced to lower interest rates.

Expenses

Total expenses for 2003 increased 12.3% to $55.9 million (2002 - $49.7 million) against a budget of $53.9 million.



EXPENSES	Total Expenses	2003	2002	Change	Change
	%		$$$ Thousands		%
Salaries and benefits	68.5	38,278	34,032	4,246	12.5
Administrative	11.8	6,617	4,873	1,744	35.8
Occupancy	6.7	3,727	3,185	542	17.0
Professional services	5.6	3,123	3,345	(222)	(6.6)
Amortization	5.5	3,069	3,278	(209)	(6.4)
Other	1.9	1,060	1,036	24	2.4
Total	100.0	55,874	49,749	6,125	12.3

The key contributors to the expenditure increase were as follows:

Salaries and Benefits costs were $38.3 million (2002 - $34.0 million) and accounted for 68.5% of the Commission's total expenditures. Salaries and wages costs increased by 12.5% in 2003. A number of factors contributed to this increase including the full year cost impact of prior year hiring, an increase in staffing levels, higher benefit and pension costs and one-time severance costs. The OSC had 356 permanent employees on board (3.8% positions vacant) at the end of the year compared to 346 (4.7% positions vacant) at the end of the previous year.

Administrative costs accounted for approximately 11.9% (2002 - 9.8%) of the Commission's total expenditures. Expenditures on administrative costs increased by 35.8% to $6.6 million (2002 - $4.9 million). Significantly higher expenditures were incurred on Commission related expenses due to greater levels of hearing activity. Administrative costs also include a direct cash payment to CDS Inc. of $2.0 million. This amount represents the OSC's portion of the $4.25 million payment as agreed to between CDS, the OSC, the Alberta Securities Commission, the British Columbia Securities Commission and the Investment Dealers Association.

Professional Services costs were $3.1 million and accounted for approximately 5.6% (2002 - 6.7%) of the Commission's total expenditures. Expenditures in this area decreased by 7% over the previous year. This continues a trend toward reduced reliance on external resources as internal expertise has been hired.

Approximately 19.8% of the costs were incurred for enforcement-related matters. The Commission expects to continue to have an ongoing need to use specialized external legal and forensic accounting resources for enforcement activities. The OSC recovers a portion of its enforcement costs through settlements and orders of the Commission. During 2003 $855K was collected (2002 - $419K) which was applied to offset enforcement related expenditures.

The OSC is a member of the Canadian Securities Administrators (CSA), which is a forum composed of provincial securities regulators. All CSA projects, including the development of harmonized securities policies and rules and shared CSA information systems, are co-ordinated through a centralized project office. The operating costs of the project office are borne on a formula basis by CSA members. In 2003 the OSC contributed $171K toward the cost of the project office.

Total CSA spending on projects was $1.9 million in 2003 (2002 - $2.1 million) of which the OSC contributed $851K (2002 - $923K). The OSC contribution included $553K toward the professional services costs related to the establishment of the National Registration Database. Other significant CSA initiatives to which the OSC provided funding included Continuous Disclosure Harmonization ($41K), work related to various Joint Forum projects ($35K) and several Investor Education initiatives ($29K). The OSC contributed $10K in CSA cost sharing and a further $309K directly toward the completion of a national insider trade reporting system (SEDI).

Amortization costs account for approximately 5.5% (2002 - 6.6%) of the Commission's total expenditures. Amortization expenses decreased to $3.1 million (2002 - $3.3 million).

Occupancy costs accounted for approximately 6.7% (2002 - 6.4%) of the Commission's total expenditures. Expenditures on occupancy increased 17.0% to $3.7 million (2002 - $3.2 million) due to the acquisition and renovation of additional space.

Other costs, which represent travel and related expenses, were unchanged at $1.1 million (2002 - $1.0 million) and accounted for 1.9% (2002 - 2.1%) of the Commission's total expenditures.

Liquidity, Financial Position and Risks

Liquidity

The Commission requires liquidity to finance its operations and capital purchases. As at March 31, 2003 the Commission held cash in the amount of $22.7 million, current assets of $25.2 million and current liabilities of $24.3 million for a current ratio of 1.0:1 (2002 - 1.2:1).

Reserve

In 2003-2004 the OSC will be operating with a new OSC fee structure. The fee structure has been designed to reduce the potential for significant fluctuations in revenues arising from market volatility. Until the new fee structure has been in place for a period of time and the OSC has had an opportunity to verify the effectiveness of its design, revenue generation under the new fee regime will remain a source of risk for the OSC. The OSC is positioned to manage this uncertainty as the Commission has a reserve of $20 million which serves as an operating contingency for revenue shortfalls or unexpected expenditures. The OSC has an additional reserve of $12.0 million which may only be used to offset any costs incurred related to the proposed merger of the OSC with the Financial Services Commission of Ontario.
Income from the investments increased 5.5% to $1.0 million (2002 - 948K) reflecting the increased value of funds invested. The rate of return on investments is low as the funds are invested with the Province of Ontario and the prime investment consideration for the reserve is the protection of capital and the appropriate liquidity to meet unanticipated cash flow needs. Income generated by the reserve is taken into general operations.

Capital Transactions

Capital expenditures of $2.2 million (2002 - $1.4 million) were made during 2003. The majority of these expenditures (60.8%) were made in information technology ($1.3 million) and included the purchase of equipment for increased staff complement and an upgrade our computer network. The balance was spent on new space acquired to accommodate additional staff.

Liabilities

Included in the accounts payables and accrued liabilities is $1.7 million (2002 - $1.1 million) relating to a provision for refunds of prospectus revenues. The amount of revenue to be realized from prospectus filing fees is uncertain. Fees are paid based on estimated prospectus proceeds and refunds are issued as required based on actual proceeds. As a result, this revenue is recognized net of a provision for expected refunds. At the beginning of each fiscal year the Commission establishes a percentage for the provision for expected refunds based on the experience of the previous three years. In 2003 the Commission refunded $9.1 million of which $1.8 million related to prior year fees and $7.3 million related to 2003 fees.

The accrued benefit liability represents future obligations relating to supplementary pension plans established for certain full time members. The unfunded supplemental pension plans had an accrued benefit obligation of $545K (2002 - $606K) at March 31, 2003. The OSC's related expense for the year was $282 K (2002 - $295K) and is included in salaries and benefits.

In support of the development of the Mutual Funds Dealers Association (MFDA), the Commission has guaranteed 61% of a total $12 million line of credit as assistance during start-up of MFDA operations. The Alberta Securities Commission and the British Columbia Securities Commission have also guaranteed a specific percentage of the total indebtedness. As at March 31, 2003 the MFDA had $3.0 million outstanding (2002 - $8.9 million) on this line of credit. Current OSC exposure to the loan is $1.8 million. As the MFDA has commenced operations and is generating revenues through the registration of mutual fund dealers, the OSC does not anticipate being called upon to meet its share of this guarantee.

The OSC, together with the Alberta Securities Commission and the British Columbia Securities Commission and the Investment Dealers Association is contingently liable for a $4.25 million assured payment in respect of the development of the National Registration Database (NRD). The OSC's share of this contingency is $1.96 million. It is expected that the assured payment will be funded by users of NRD and no provision has been made to the financial statements for any potential cost to the OSC.

Designated Settlements

In August 2000, the Commission established a not-for-profit corporation, the Investor Education Fund, to increase knowledge and awareness among investors and potential investors and to support research and develop programs and partnerships which promote investor education. The Investor Education Fund is governed by a Board of Directors which is responsible for developing criteria for and approving the disbursement of funds.

During 2003, a total of $150K (2002 - $4.1 million) in designated settlements arising from enforcement proceedings was collected. These funds are receivable by the Commission to be allocated to or for the benefit of third parties as the Commission may determine. The Commission directed that the $150K collected as designated settlements in 2003 be provided to the Investor Education Fund.

Reliance on CDS Inc.

CDS Inc. operates a number of major systems on behalf of the CSA and the OSC. Approximately 58% (58% 2002) of our fee revenue is collected through the SEDAR system. CDS recovers the costs to operate the systems by charging filers user fees in addition to the fees collected for the OSC and other members of the CSA. The CSA is in the process of renewing the operating agreement for SEDAR which expired in December 2002.

CDS developed a national insider reporting system (SEDI) for the CSA which was launched in January 2002. SEDI operations were suspended on February 1, 2002 because technical issues resulted in unacceptable system performance levels. CDS is completing repairs to the system at their cost. It is not expected that CDS's efforts to repair the system will expose the OSC to any liability. The SEDI system is expected to be re-launched in May 2003.

The NRD system was launched on March 31, 2003. The current operating agreement for the NRD will run until March 2009.

Should CDS become unwilling or unable to operate one or all of these systems, the OSC and the CSA would need to explore options to continue the operation of these systems.

Risk Management Initiatives

The OSC has substantially completed a Business Continuity Plan (BCP) which is designed to allow the continuation of critical regulatory services should the OSC face a significant disruption to its operations. Individual business continuity plans have been developed for each priority business function. Each plan includes documented recovery procedures including manual workarounds and mitigation strategies. Additional work on establishment of offsite recovery services and facilities is expected to be completed early in 2003/2004.

The OSC also completed a risk assessment process to identify the top risks which could impact the achievement of its business objectives. Following an analysis of these risks a three-year internal audit plan was developed. The first phase of the plan will be carried out during 2003/2004 by internal auditors contracted by the OSC.

Memorandum of Understanding

In accordance with the provisions of the *Securities Act*, the Commission is required to complete a Memorandum of Understanding with the Minister of Finance to outline the ongoing roles, responsibilities and accountability relationships between the two parties. A Memorandum of Understanding between the OSC and the Minister of Finance was signed in May 2003.

2003/2004 Outlook

In order to streamline and simplify the fee structure and meet its commitment to align total fees with the cost of regulation, the OSC finalized a rule which established a new fee structure effective March 31, 2003. The fee rule is designed to accomplish three primary purposes: to reduce the overall fees charged to market participants; to create a clear and streamlined fee structure; and to adopt fees that accurately reflect the Commission's costs of operations. The new fee schedule is comprised primarily of two types of fees. Participation fees, which are estimated to generate about 70% of total revenues, are intended to represent the benefit derived by market participants from participating in Ontario's capital markets. Activity fees, which are estimated to generate less than 25% of total revenues, are intended to recover the direct cost of OSC staff resources to take a specific action or provide a specific service at the request of a market participant. The remaining sources of revenue are late filing fees and investment income which are expected to generate about 5% of total revenues.

The fee rule is expected to generate net positive benefits in two areas, fairness and efficiency, both for the industry and the OSC. The changing nature of the securities industry, from a business based on primary offerings to one where 95% of the activity takes place in the secondary markets, had not been reflected in the fee structure. With the shift to monitoring continuous disclosure and trading, fees based primarily on filings no longer mirror the cost of regulation. The fee rule ties the OSC's cost of regulation to the revenues from fees. The shift to fees based primarily on participation in the capital markets represents a considerable improvement in fairness.

Administration costs associated with paying fees should drop significantly for most stakeholders due to an expected reduction in the total number of fee transactions. With the fee calculation based on standard disclosure items, the set-up and ongoing costs of calculation should be minor. With improvements in both fairness and efficiency, only marginally offset by very modest set-up costs, the fee rule is expected to deliver substantial net benefits to the capital market's intermediaries and to the OSC.

The Commission revenue forecast for 2004 is $65.0 million, which is 7.8% lower than the $70.5 million collected in 2003. The forecast does not anticipate a material change in the level of market activity. The OSC revenue forecast for 2004 is made less predictable by uncertainties arising from the newness of the fee structure. The potential for material market fluctuations due to world events could have a negative impact on OSC revenues. The new OSC fee structure has been designed to reduce the potential for significant fluctuations in revenues arising from market volatility. Until the new fee structure has been in place for a period of time and the OSC has had an opportunity to verify the effectiveness its design, revenue generation under the new fee regime will remain a source of risk for the OSC.

Fee revenues collected on behalf of the OSC through systems operated by CDS Inc., are expected to increase substantially to more than 90% of total OSC revenues (58% 2003) due to the full year operation of the NRD.

The Commission has budgeted operating expenditures of $57.8 million for 2004 (2003 - $53.8 million). The budget increase relates primarily to salaries and benefits which are projected to rise by 8.6% to $40.6 million (2003 - $37.4 million). Key contributors to this expenditure increase include the annualized cost impact of hiring which occurred in 2003 as well as higher projected benefit rates. The budget includes a 1.7% increase in approved staffing to 379. The OSC benefited in 2003 from a temporary reduction in required pension contributions. The contribution rate was restored to regular levels December 2002. This change resulted in an additional 4% salaries and benefits cost.

The Commission has budgeted $3.2 million (2003 - $3.4 million) for professional services costs for 2004. The budget reflects no change from 2003 expenditures. Significant professional services costs are budgeted for litigation and investigation services ($420K), development of a continuous disclosure risk assessment database ($160K) and work related to the Uniform Securities Law project.

Occupancy expenses are projected to increase by 9.1% to $4.1 million in 2004. These increases reflect the costs for the additional space which the Commission has leased to accommodate its increased staff complement as well as higher lease-related operating costs. Amortization costs are projected to increase to $3.3 million in 2004.

The 2004 capital budget is $1.5 million, 31.5% lower than the $2.2 million spent in 2003. Approximately 88.8% of the planned capital expenditures are information technology-related reflecting the Commission's commitment to maintaining state of the art information technology capabilities.

The 2004 OSC budget does not include costs for the work that will be required if legislation is passed enabling a merger of the OSC and the Financial Services Commission of Ontario. Legislation is required in order to create the proposed new organization and specify its regulatory responsibilities and powers. The goal of the proposed merger will be to provide more integrated regulation of capital markets and financial services sectors.