Keynote Address by

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Good Morning. Thank you for the introduction.

Balanced Regulation

Acknowledging the obvious tension between regulators and the regulated, I would like to start by repeating the familiar regulators' message that we are all on the same side, endeavouring to reach the same fundamental goals. Securities regulators are responsible to protect investors and the integrity of the capital markets. Efficient capital markets permit investment on a level playing field and access to capital by business enterprises. Intermediaries between investors and securities issuers have a significant role to play in both protecting investors and protecting the integrity of the capital markets. It is important to securities regulators that intermediaries are as effective as possible and, in that regard, that they be as skilled and experienced as possible, and are motivated by incentives to do as good a job as possible. What is good in the long run for their business ought to be as well good for the capital markets.

The trick behind effective regulation is always balance. We, the regulators, are often criticized for being, by intention, too protective of investors, in which case the regulatory burden risks smothering the activities of issuers and intermediaries. Alternatively, we are accused of being too supportive of the issuer and intermediary industries, in which case investors are subjected to inappropriate risks and possibly dissuaded from participating in the capital markets altogether. There may well be imbalances in our regulation, but they are not by intention. There is little upside to issuers if investors are frightened away, and there is little benefit to investors if issuers leave the capital markets, or the intermediaries they rely on abandon their businesses, and there are as a result no investments or no advice to be had.

With an appreciation that all of investors, market participants and regulators have the same fundamental goals in mind and that the rules, compliance with the rules and rigorous enforcement of the rules are essential ingredients for the achievement of those common fundamental goals, how do we get the balance right?

I wish I had the simple answer. I wish I could say when I am invited to speak to a group such as this in Toronto that we in Alberta have it all figured out, you should do things this way or that and you will both find and maintain the desired regulatory balance. In considering this address this morning I did develop and articulate in my own mind some novel ideas to project by way of answers and directions that would be helpful to all of you and for which you would presumably be grateful. I had the good sense to test some of these ideas on our ASC staff who flattered me for my vision but pointed out inconvenient facts and realities that stand in the way of that vision. In the area of market conduct regulation there are not easily identified means to balanced regulation, at least not that is balanced for all issuers, all investors, all market facilities and all intermediaries. And furthermore, if the balance is reached one day it is likely lost the next as a result of changes to economies, businesses, market cycles, new products, new marketplaces, international influences and, in recent years very significantly, new technology.

We, the regulators, do hear one message, loud and clear, from many in the investment industry that the regulatory burden is becoming unbearable because of its cost, its resource demands, its complication and its volume. We hear that small and medium-sized dealers cannot continue to bear the regulatory burden and that as a consequence only the major institutions will remain. Those are not satisfying messages to hear and are certainly not consequences intended by securities regulators. Those are not consequences that I would judge best serve investors or the capital markets, never mind the investment community.

So are there ways to lessen the burden of securities regulation on the investment industry without sacrificing or diluting the undertaking of our regulatory mandate to protect investors and the integrity of the capital markets?

It is at this point that I must resort to the common regulator’s disclaimer: my comments are my own and not those of the CSA or the ASC. Some of my own thinking does reflect that of the ASC, but certainly not all of these matters have been thoroughly researched, analyzed and decided upon. Some of the positions of the ASC may influence policy selections by the CSA, but that has yet to be determined. So my comments inform you only as to one individual regulator’s personal and rather high level attitudes and inclinations that may possibly influence changes of approach to national policy making.

Enforcement over Compliance

One policy re-alignment that could shift some of the burden would be for securities regulators to focus less on rule making and compliance and more on enforcement. If we focused less on exact compliance with detailed rules and more on offensive breaches of important fundamental standards, might everyone be better served and less time devoted to detailed and voluminous analysis of both the rules and related conduct?

The investment industry in Canada has long advocated for a principles-based approach to regulation, and the concept I am discussing is closely related. One concern has been that participants in the industry may lack the experience and judgement to fully understand what the principles are and what conduct supports or contravenes them. Another concern is that our system of due process, adjudication and sanction is based on the clarity of rules and the clarity of evidence of their alleged breach. A number of relevant questions arise. Are regulators prepared to accept that judgements as to compliance with principles can be made fairly by firms and individuals? Are compliance officers prepared to take responsibility for making those judgments in the absence of detailed rules? And would it be acceptable to participants who contravene the principles that they be dealt with severely under regulatory enforcement proceedings?

I do not believe that a principles-based regime can work effectively unless there is the prospect of serious consequences for a breach of the principles. Could participants in the industry accept that a response of "I didn't know" and "you can't point to a specific rule and breach" would not be acceptable defences? And just as regulators would have to trust the judgements of firms and individuals to a greater degree in the absence of detailed rules, would firms and individuals be prepared to accept the greater judgement-making that will be required of regulators in selecting the conduct that is deserving of serious sanction and based on the breach of general principles instead of detailed rules? If small and mid-sized dealers struggle to keep up with the flood of changing rules and the related compliance obligations, would they actually be any better equipped to understand, apply and follow principles?

So would less of a focus on specific compliance and more of a focus on serious enforcement shift some of the cost and resource burden from compliance officers to regulatory enforcement officials?

Principles-based regulation was very fashionable during a period leading up to 2008, and was led by the U.K.'s Financial Services Authority. Senior officers of the FSA were touring various western countries explaining and promoting the advantages of principles-based regulation and, in respect of implementation in the U.K., its huge success. That all changed with the collapse of Northern Rock and all that came thereafter. Principles-based regulation fell immediately out of favour and the model of its successful implementation, the U.K. FSA, has been restructured. The British Columbia Securities Commission was a strong proponent of the approach, but has also fell silent on the subject since 2008.

It may be time to look again at the approach in the Canadian context and see if there are features that could help in a practical way better control the regulatory burden.

If the regulatory burden is in fact becoming overwhelming because of volume and complexity, could regulation be reduced and simplified through a more principles-based approach? Are both participants and regulators prepared to trust each other to make the judgements required for the successful implementation of this approach? And are participants prepared to accept the tougher enforcement consequences that would be necessary to support the maintenance of the principles?

United States Influence

There is a natural tendency in Canada to replicate the regulatory regimes of the United States. There are good reasons for this, including: the desire to harmonize our regulatory environments to the greatest degree possible with our closest trading and business partner, and the fear that a regulatory regime perceived to be less rigorous than that of the U.S. would be judged to be sub-standard, weak and lacking in integrity.

The downside of following the U.S. lead in regulation is that their habit is to be voluminous, detailed and prescriptive. Even though their economies of size can better accommodate the resources required to respond to their prescriptive regulation, they as well are endeavouring to reduce the negative influences of the U.S. regulatory burden. The *JOBS Act* presented a good example of efforts by the U.S. Congress to lighten the ever-growing burden of U.S. securities regulation and the negative impacts it may be having on capital raising, business growth and job creation.

<u>Irrelevant Problem Fixing</u>

As more time passes since the 2008 financial crisis, there is greater realization that legislators and regulators are spending great amounts of time and energy fixing the prior decade's problems and may be loading up the regulatory burden more for the purpose of optics than for impact. That challenge is compounded in Canada where we may not only be trying to fix yesterday's problems, but we may be trying to fix problems that existed elsewhere, and not in Canada.

Defaults, questionable conduct and other problems observed among the biggest financial institutions in the world have truly shaken the trust that governments, regulators and the public have in the financial system and financial institutions. The revelations of bad investment products being sold to clients, huge trading losses being recorded by relatively junior employees and the alleged manipulation of reference interest rates and foreign exchange conversions has devastated the fundamental sense of trust that is necessary for the efficient working of financial markets.

Nevertheless, we must fully understand the circumstance of that offensive conduct and determine its relevance to the Canadian capital markets before mimicking the regulatory regimes of others. One cannot assume that Canada is immune from the problems that arose in the U.S., the U.K. and Europe and we need to be vigilant; but do we need to replicate every change that is introduced in the U.S. when our financial institutions have not been confronted by the same damaging revelations the Canadian financial system demonstrated comparative integrity?

Should Canada be now prepared to be different for the reasons that we can be without undertaking undue risk and that we need to be in order to avoid the cost, delay and distraction that regimes developed in the U.S. would impose? Should we all, regulators and the regulated, be spending more time trying to apply an effective but less burdensome regime in order that we would all spend less time dealing with the long term costs of a more burdensome regime? To successfully undertake that approach, we need confidence to make our own choices and a preparedness to defend and explain those choices.

Fiduciary Standard

A debate is ongoing in Canada concerning the imposition of a fiduciary, or as the regulators have preferred to call it, a best-interest standard by which to manage and judge the relationship and conduct between a securities salesperson and a client. Being careful to emphasize that I am speaking personally and not on behalf of others, I will say that I am not certain that this debate would be ongoing in Canada but for the focus given the subject in the United States. This issue is an example, in my view, of what we inherit from our neighbours to the south when we might not have seen the necessity or even purpose to address it on our own.

I cannot argue that the implementation of the fiduciary or best-interest standard does not, on its face, provide for an elevated standard for the benefit of an investor client. I also acknowledge that many investor clients have been under the impression that they were already the beneficiaries of this elevated standard. I further acknowledge that many salespersons already behave in a manner that would demonstrate compliance with this elevated standard. The question for me is whether we really need to create, define, implement and enforce an entirely new standard of conduct for the investment industry. I believe that the existing standards of suitability and know-your-client are very good standards. From my post as Chair of the ASC I do not observe that we have problems arising between salesperson and client because of our current standards, but we have problems because in too many cases the existing standards, on the part of the investor, are often not understood and, on the part of the salesperson, are often not abided by.

If we as regulators could be comforted that the suitability and know-your-client standards were being universally and rigorously applied, I do not believe we would need to be canvassing the application of a wholly new standard. The issue cannot only be whether or not a new policy could better protect investors. We must also consider the practical implications of a new policy and its impact on the balance we are attempting to achieve. Might we be saving a lot of time, energy and grief by bettering the compliance with our existing standards rather than trying to adopt an entirely new one. Is it necessary? Will it distort the balance we strive for?

If I were personally to be thoroughly persuaded by industry that a new standard was not required, it would not be through some exhaustive comparison and argument concerning the merits, but rather through evidence that the industry was working hard and effectively to instruct and police the unwavering application of the suitability and know-your-client standards. This evidence must come from an understanding of the communication between the salesperson and the client and the level of appreciation had by the client for the communication. It cannot be based on the form, content and execution of forms.

Form over Content

Lengthy, complex, unread forms provide a paper trail of evidence that can be used for the purposes of litigation defence, but it is not likely they serve the purpose of informing the client of the relationship had with the dealer, or of ensuring that the standards of suitability and know-your-client are being satisfied in substance and not simply in form. I think it is encumbant on regulators, compliance officers, dealers and their respective legal counsel to lessen the reliance on forms and find ways to ensure application of the substance of the standards. If the means cannot be found to break out of our collective attachment to the comfort provided by drawers full of executed forms, I do not know that we have any chance at providing for a made in Canada principles-based regulatory regime for the investment industry.

Disclosure

I have suggested that if the standards of suitability and know-your-client would be fully and meticulously followed we would not need to be considering the establishment of an entirely new standard and trying to address all of the complications that would entail. I would make a similar comment, again personally, around the subject of disclosure. Our securities regulatory regime in Canada is fundamentally built around the concepts of full, true and plain disclosure and the consequential ability of an investor to make an informed decision. These informed decisions by investors do not relate only to the securities they purchase and sell but also to the roles, expertise, duties and costs of the intermediaries they engage.

I can accept the position that an investor must take significant responsibility for his or her investment decisions, but I cannot accept that there be any lack of understanding on the part of an investor when making those decisions as to the role, expertise, duties and costs of those they are paying to serve as intermediaries in their purchase and sale transactions.

From the standpoint of a regulator, I can say that as confidence in the level of disclosure lessens, the inclination to intervene in the substantive features of the relationship increases. Simply put, if we cannot be comfortable that investors know what they are paying, and what they are paying for, we regulators will be tempted to intervene not only in respect of the disclosure deficiency, but also in respect of the costs themselves. One can be persuaded from a regulatory policy standpoint that investors should be responsible for making their own choices as influenced by the subject of cost, but it is very difficult to take that position when it appears they are not being fully or effectively informed as to what those costs are.

Technology Impact

We as regulators are receiving much comment from the small and medium sized dealer community, in particular, about the negative impact of technological changes in trading mechanics. Removed from the day-to-day and transaction-by-transaction experience, regulators around the globe are struggling to understand the features, mechanics, impact and consequences of matters such as, among other things, high frequency trading and dark pools. Regulators around the world are challenged by the same questions as we here in Canada. Is liquidity increased, decreased or affected at all? Are technological changes the result of ever-evolving marketplace mechanics that cannot be stopped, or do they represent an abuse of position and strength by those who can afford to take advantage of that evolution at the expense of those who are necessary players in the market but cannot afford to keep up? Are some of these practices designed to gain informational advantage or do they cross the line into market manipulation.

Regulators are working hard to understand these issues and the facts relevant to them. I believe it will take time to achieve that understanding and more time to react to it, if at all. We all wish there were quick and ready answers, but I am afraid both knowledge accumulation and appropriate responses will take more time than many would like. As in most areas of our regulatory responsibilities, your contribution to better and more quickly informing us will be helpful for all concerned.

Self Regulation

When I interviewed for the position as Chair and CEO of the Alberta Securities Commission now close to nine years ago, I was asked about my views on self-regulation. Being a lawyer and having enjoyed the privilege of the self-regulation of the legal profession for some 32 years, I did not have much difficulty in quickly expressing my support. Not long after taking the job and in speaking publicly in Alberta about the effective enforcement of securities laws, I made a plea to Alberta market participants to do much more of the job themselves. I was being surprised by comments from people who had read of our ASC enforcement efforts that it was about time we had cracked down on so-and-so or that they were certainly not surprised to see that so-and-so was now the subject of an allegation, a hearing or a sanction. I took to wondering out loud why these so-and-so's had not been brought to our attention at the ASC long before or had not been effectively discarded by other legitimate players in our capital market.

I am still a believer in the self-regulatory system, but do worry about some lack of alignment between the "self" in the industry and the "self" in the regulators. I am also of the view that more could be done by peers to clear out bad actors and bad behaviours.

It has been something of an eye opener for me that some of the strongest critics of the investment industry, its practices and its people, come from those who have spent a career in the industry and have moved on or retired. Some of those critics have from time to time, joined the ASC as members of our Commission. Their views come with credibility and can be persuasive.

Another observation is that the vast majority of complaints that come into our organization about market conduct comes from unhappy investors. Very rarely do these complaints or reports originate with industry members. That experience may be different for IIROC or the MFDA, who are more directly engaged with the industry, and it may be that I am overstating the concern, but it occurs to me that a much greater degree of self-policing would go a long way to reducing regulator burden. It is not just that the regulators might have less work to do in the enforcement area if industry was doing more of its own culling, but there might be far less need for prescriptive rule making and standard setting if it was observed that problem areas were being dealt with by the peers of those who do not meet standards.

Related to that issue is a sense that there is a "we" and a "them" comprised of the self-regulator and the self-regulated. I would personally prefer to believe that within these groups of "selves" everyone is on the same page, in that everyone will benefit from improved regulations for good service and integrity and from less intrusion by those outside of industry. This is another personal opinion that will not be shared by all of us within the regulatory community, but I am of the view that self-regulation ought to be truly self-regulation and not some hybrid or diluted version. To the degree there is less and less "self" in the model, the argument strengthens for someone wholly independent of industry to do the job, like provincial securities regulators.

In case my comments have raised any questions about the nature of the relationship between IIROC and the provincial securities regulators, it is my own observation that the relationships are good, there is mutual reliance and respect and a sense we are all trying to do our jobs as well as possible for common goals.

Culture

I read the other day in our consolidation of media reports that a senior regulator in the U.S. had commented that recent problems, particularly in the banking industry, had raised serious concerns about the culture of behaviour within financial institutions and the general appreciation, or lack of it, for the value of ethical behaviour. This comment struck me as coming rather late in the day. I think these concerns arose pretty soon following the mess created in 2008 and have been repeated often since. It may be that some of the most recent attention to these questions of ethical leadership and tone at the top was spurred by the realization that the most recent episodes of questionable conduct in FX trading had been undertaken after all the alarms had already been sounded about sub-prime mortgages, credit default swaps and rate setting, among other things.

It is to be hoped that the job of compliance officers within financial institutions includes contributing to an atmosphere of compliance, an assumption that ethical behaviour is a fundamental expectation that permits no exceptions and an understanding that there is no place for people who would hold, profess or practice a contrary view. In the end, peer pressure and internal discipline will be more effective than increased regulatory demands. Evidence of significant levels of peer pressure and internal discipline may go some distance to fending off the inclinations of regulators to regulate. To repeat the old saw that "if you are a hammer, every problem is a nail", it should be acknowledged that regulators have only two basic choices: to regulate or not to regulate.

OBSI

A subject closely related to compliance is dispute resolution. Securities regulators do not want, and are not resourced, to get into the business of dispute resolution and compensation for the clients of registrants. OBSI, the Ombudsman for Banking Services and Investment, provides what has been intended as an inexpensive and prompt service for the resolution of disputes between an investment dealer and a client based on the alleged failure of the investment dealer to comply with appropriate standards or practices. It has been a frustration for many that what ought to be an ideal service for all concerned has encountered so many obstacles to full satisfaction. I hope that we can move past them. Investors have much to gain from the process, provided it works as intended; industry has much to gain from a reputational standpoint; and regulators have much to gain from a system that provides remedies we are not responsible for, but are nevertheless demanded of us.

As personal observations, it is to be hoped that investors can accept that OBSI provides a dispute resolution process and is not intended to identify and either correct or report every deficiency observed in the practices of the subject financial institution. It is to be hoped that OBSI can accept the responsibility to address matters within as short a timeframe as possible and recognize that undue delays detract from the value of the process in its entirety. It is to be hoped that investment dealers can appreciate the relatively inexpensive nature of the process and its rewards, and can accept an outsider's evaluation of fault. I think that if investors want to squeeze every last nickel of potential compensation, they will have to resort to the courts. I do not believe it reasonable to expect an institution to accept an independent dispute resolver if that dispute resolver is also responsible to report on and address systemic issues observed in its process.

I would also advocate that internal compliance staff and fault evaluators should be a little better prepared to accept the opinion of an outside dispute resolution service, even when their opinion is at odds with the very good and well-intentioned opinion formed internally. Falling back on my experience as a lawyer, I would say that litigation lawyers would become suicidal if they viewed every contrary decision by a judge to be a questioning of their integrity, professional ability or entitlement to be paid by their client.

I am strongly of the belief that we must make OBSI work and that those concerned must be more understanding of the consequences of rigid positions. The recent reports of refusal of a number of investment dealers to comply with the decisions of OBSI are troublesome. I think it in the best interests of the industry to apply such pressure as is available to discourage these responses.

One should not consider it a viable alternative that there not be a dispute resolution process in place for which the investment industry pays the cost. The questions are only as to the degree of independence the investment industry retains in the management of the process and the degree to which securities regulators are forced to take responsibility for a legislated system and mandated awards. The further engagement of regulators and mandated decisions will only add to the cost and length of the process. I believe there are more simple and less costly solutions.

Industry Input

Closing back on the broad topic of regulatory burden, we regulators hear criticism of a lack of prioritization and of incessant changes. We have in our jurisdiction in Alberta asked industry for something more specific to deal with, such as: what are the regulatory demands that lack utility, and how can we reduce the volume without sacrificing the investor protection impact? I think it a fair question to ask: what specifically are the practical burdens of our regulatory demands and what can we get rid of? It is not helpful to receive an answer that suggests there is no point industry making the effort unless the regulators first agree that recommendations will be accepted. To bore you yet again with my lawyer analogies, would anyone think it a useful position to inform a court that you have a persuasive case but cannot take the time to deliver it unless first assured that it will be successful.

Finally, on the subject of feedback, regulators need the best information possible from those who have to conform to our regulation. In that regard, I would ask that it be as specific as possible. We all know that there are at least two sides to every position and that what benefits one side is likely to be seen as a cost or detriment to others. In picking the balance point, we must be informed of all the facts and all the consequences. I know that takes time and is a distraction from getting on with business, but I also know that it will save costs, time and distraction in the long term.

Conclusion

To summarize, acknowledging that (i) there are grave concerns about the harmful impact of the expanding regulatory burden, and (ii) there are no silver bullets, are there a number of incremental changes that can be pursued which, together, might produce positive results?

(1) Can we reduce the reliance on rule making and specific compliance and focus more on principles and their rigorous enforcement? In doing this are both the regulators and the regulated prepared to better accept each other's exercise of judgment?

(2) Do we have the confidence to develop "in-Canada" policies and be less fearful of being different from the Americans?

(3) Are we prepared to pass by last year's problems and those exposed in other jurisdictions and focus on what our circumstances are here in Canada?

(4) Do we need to devote time, effort and costs to new standards of conduct when a rigorous adherence to existing standards might get the job done?

(5) Can we dedicate less time to paper compliance, with the belief that some hard work reducing the volume now might save much more down the road?

(6) Might an acceptance and application of the paramouncy of disclosure ward off the regulators from more substantive intrusion into your business?

(7) Can we all work more closely to fully understand and appreciate the influence of technological changes – or as they are referred to, advancements?

(8) Might a greater degree of self policing lessen the inclination of regulators to control with rules?

(9) Can organizations and compliance officers comfort regulators that we have not lost a culture founded on an unwavering standard of ethical behaviour?

(10) Can we ensure that simple and available solutions are used and improved – like OBSI – instead of forcing the creation of new and more complicated ones?

The current and significant stress on many in the investment industry is attributable to a great degree to the events of 2008 and the state of business and investments cycles. Changes in those cycles will at some point relax much of the stress, but the timing of such changes is impossible to predict. We regulators run the risk of making unnecessary regulatory changes when those cycle changes may overtake us. We also run the risk that without trying new and better approaches soon, avoidable damage may be done. We are back to the balance issue.

I would invite the industry to tell us the severity of the stress, the influence of the regulatory burden and the efforts you, particularly in the compliance business, would like to see us make. And please take the time to give us the specifics.