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Will OSC kill regulatory overkill?

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Any day now, the Ontario Securities Commission, and sister organizations at the Canadian Securities Administrators, will release a revised version of a relatively obscure set of proposed new regulations. Known as National Instrument 31-103, the aim of the proposals --first unveiled almost a year ago--is to redefine who must register to do business under securities laws across Canada.

Hailed as a "reform" to protect investors and -- in the words of the securities commissions -- to "harmonize, streamline and modernize" the already cumbersome Canadian registration regime, the proposals went down in flames when first released last February. An astounding 270 responses were filed by major law firms and industry players, most laden with harsh, detailed criticisms. If the plan was to "create a flexible regime leading to administrative efficiencies and reduced regulatory burden for registrants," the securities commissions missed the mark.

A review of the submissions suggests the commissions were mounting another round of regulatory overkill. Whether that was deliberate or accidental, the registration proposals threaten to hinder reform and instead inflict damage on Canadian and Ontario economic objectives. In an era where regulators are supposedly subjecting their reforms to cost-benefit analysis, there's little evidence of it here.

A good case in point:Goldman Sachs, the major U.S. investment house, said the proposals "represent a significant reversal of recent regulatory developments." Just as Canadians and the federal government are looking to bolster free trade in securities, the provincial regulators seem to be operating on another economic planet. The market wants less, but the OSC-CSA plan calls for more-- "a significant increase in the regulatory burden placed on non-resident dealers and advisors participating in the Canadian market."

According to Goldman, the proposed registration changes will increase costs and effectively limit the kind of work Goldman investment professionals can do in Canada, including limiting their ability to advise Canadians, perform services and seek new clients. By imposing the reforms, adds Goldman, the OSC/CSA are raising the regulatory burden when "there have been no major compliance or regulatory failings associated with the participation of non-resident securities firms in the Canadian market."

Another substantial brief from the **Canadian Bankers Association** raised the spectre of banks becoming subject to "inappropriate and duplicative" provincial regulation on top of existing federal regulation. So much for "harmonization." As the CBA reads the reforms, bank employees would have to be registered to sell index-linked GICs, federal and provincial government bonds (including CSBs).

The securities law subcommittee of the Ontario Bar Association takes aim at the potential for the reforms to hinder "the ability of venture capital issuers to raise money in the private placement part of the capital markets." Currently considered "exempt," this market would be subject to a new raft of registration and regulatory requirements.

Osprey Capital Partners, which operates in the Limited Market Dealers segment of the industry, said the new regulation will raise costs and do nothing to protect investors. Many LMDs, said Osprey, "will consider abandoning registration and cease providing advice to small and mid-cap public and private companies."

Most of the submissions on National Instrument 31-103 follow similar lines of attack. New costs, complexity, disruption, limited or negligible impact on market efficiency, unmeasured benefits to investor protection.

Lawyers and industry representatives believe the revisions to National Instrument 31-103 will clear up many of the objections raised by critics. We shall see.

This is not just minor bureaucratic fiddling with fine points of Canada's securities regulatory system. The reforms represent a major change in principles. New securities laws will have to be passed in all provinces to embed new definitions and a new foundation for the regulatory system. People who follow the issue say the draft legislation has already been written for Ontario, and will be introduced soon after the revised proposals are issued and following a brief comment period.

Whether anybody within Ontario's Ministry of Finance or the finance ministries of the other provinces is paying any attention to this major expansion of regulation will determine the progress of the reform. Finance officials, especially in Ontario, are notoriously indifferent to the all-powerful rule-making juggernaut at the OSC. If this reform is all cost and no benefit, with possible losses, somebody should be bringing an economic, not just a regulatory, perspective to bear on the proposals.

The OSC-CSA also has other power expansion campaigns under study. A group called the National Securities Fraud Enforcement Working Group -- co-chaired by OSC chairman David Wilson--produced a paper last November and distributed it to justice ministers at all levels of government. The paper has never been released. Given the regulatory tendency to overkill, there might be a good reason to keep it under wraps. Have the same cost-benefit standards been applied to the enforcement plan as appear to have been applied to National Instrument 31-103?