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Cooperative Capital Markets Markets Regulatory System

Dear Sirs:

Our comments on the Consultation Draft of the Provincial Capital Markets Act and the Capital Markets Stability Act are enclosed.

Yours truly,

Linda Fuerst

LLF/sv
Enclosure

COMMENTS ON CONSULTATION DRAFT *PROVINCIAL CAPITAL MARKETS ACT* AND *CAPITAL MARKETS STABILITY ACT*

PROVINCIAL CAPITAL MARKETS ACT

PART 3: Designated Entities and Other Market Places

The intent of this Part is unclear.

Section 17: Designation of Entities

If an order is made "designating" a dispute resolution services provider under s. 17(1)(d), or any other legal services provider under s. 17(1)(g), that entity's obligation to provide information under s. 18 must exclude privileged information, including information protected by settlement privilege or by a contractual confidentiality requirement.

PARTS 4, 5 and 6: Registration, Prospectus Requirements and Trading in Derivatives

Sections 25(2), 31(3), 35(1), 36(1), 38(3): No Opportunity to be Heard

These provisions permit the Chief Regulator to make important decisions having a serious impact upon registrants, issuers and others without the opportunity for a prior hearing.

The courts recognize the devastating consequences that orders such as those impacting licensing or registration can have on individuals. As reflected in *Henderson v. College of Physicians and Surgeons of Ontario* [2003] O.J. No. 2213 (Ont. C.A.), sanctions of this type are often characterized as the "professional death penalty".

With the exception of s. 35(1), which excludes even the right to make prior representations, the proposed legislation affords affected persons only an opportunity to make "representations" prior to such an order being made, not a right to a hearing. A right to a hearing and review is available only after the decision has been made. In practice, such a hearing and review can take months to schedule and complete.

Restricting the affected person to making representations rather than providing the right to a hearing at which the evidence can be tested prior to the making of such an order represents a significant and unwelcome change from current provisions of the Ontario *Securities Act*, including in s. 31and 61(3). It is also inconsistent with powers to affect licensing contained in other Ontario statutes affecting professionals. See, for example, s. 25(1) of the *Architects Act*, R.S.O. 1990, c. A. 26 and s. 14 of the *Real Estate and Business Brokers Act*, 2002, S.O. 2001, c. 30, Sch. A.

If these proposed provisions are not changed to permit the affected person an opportunity to be heard prior to the making of the decision, the Chief Regulator should be required, at a minimum, to provide the affected person with reasonable notice of the basis for the proposed action or decision, and at least 14 days within which to make submissions to the Chief Regulator. See, for example, s. 37(5) of the Health Professions Procedural Code, Schedule 2 of the *Regulated Health*

Professions Act, 1991, S.O. 1991, c. 18 dealing with the making of interim orders to suspend or restrict registration as a regulated health professional.

PART 7: Disclosure and Proxies

Section 45: Information from Directors, etc.

The Chief Regulator's ability to require a director or officer of an issuer to give the Authority any "information, record or thing" in the person's possession or control "at the time and in the form required by the Chief Regulator" is overly broad. This has the potential for abuse and could be used as a disguised power of investigation, without any protection for the person required to provide information "in whatever form is required" by the Chief Regulator.

At a minimum, the PCMA should provide (a) that the officer or director is relieved of the obligation to provide information that is protected by a privilege, (b) that oral information or written narratives that are compelled from an individual under this section are inadmissible in a civil or criminal proceeding under the laws of any jurisdiction, or in any prosecution under section 112 of the Act, and (c) that if an oral statement or written narrative is compelled from an individual under this section, disclosure of it shall be governed by s. 196 and the evidence shall be treated as if it was given pursuant to s. 104 for that purpose.

PART 9: Market Conduct

Section 60: Prohibited Representations

The word "assurance" in subsection (3) should be defined or changed to "guarantee". Investors frequently seek guidance with respect to an advisor's evaluations of a security's prospects. Advice that the price of a security is likely to increase should not constitute a prohibited representation.

Section 7 and 66: Insider Trading

The definition of "special relationships" in s. 7 is unduly broad. The effect of s. 7(b), which provides that a person is in a special relationship with an issuer if the person is "*considering or evaluating* whether to engage…in any business or professional activity with or on behalf of the issuer" puts every lawyer or auditor in a special relationship with virtually any prospective client that is an issuer, even before communicating with or receiving information from that issuer. As well, by virtue of s. 7(c), every employee of that law firm or account or auditing firm would also become a person in a special relationship with that issuer in those circumstances.

Sections 83 and 114: Contravention Re: Acts of Employees and Agents

These provisions expose any corporation or partnership, including a firm of professionals, to sanctions including quasi-criminal penalties under s. 112 of the PCMA if, acting in the scope of his or her employment, an employee contravenes capital markets law, unless the firm can establish that it exercised due diligence to prevent the contravention and that the contravention was committed without the firm's knowledge or consent.

This is an unwarranted extension of the tort concept of vicarious liability to the regulatory sphere. It has no place in this legislation, particularly as a basis for imposing significant quasi-criminal penalties of up to $5 million per offence. As currently drafted, s. 114 exposes an organization to quasi-criminal liability not for conduct, but for mere systemic failure.

Section 114 should be redrafted to mirror section 22.2 of the *Criminal Code,* R.S.C. 1985, Chap. C-46, which makes an organization a party to an offence only if one of its senior officers (a) acting within the scope of his authority is a party to the offence, (b) has the *mens rea* for the offence and directs others within the organization to perform the *actus reus* of the offence, or (c) knows that another representative of the organization is or is about to become a party to the offence and does not take reasonable steps to stop the commission of the offence by the representative.

PART 10: Orders, Reviews and Appeals

Section 87(6): Cease Trade Order – Market Fluctuations

The Tribunal should not have the ability to order that all trading in a security cease on the basis that "*circumstances...are about to occur* that could result in other than orderly trading of the security".

The circumstances in which this extraordinary power can be exercised, which does not require the giving of prior notice or an opportunity to be heard, are not defined and as such are open to the potential for abuse.

The consequences of a cease trade order can be devastating for an issuer. An issuer that could be affected by such an order should be provided with reasonable advance notice and disclosure of the basis for the proposed order, and a right to a hearing to contest the proposal to make such an order, or this power should be removed from the legislation.

Section 89(1)(l): Orders of the Tribunal

Section 89(1)(l) should not be included in the PCMA. The power to prohibit a person from acting in a "consultative capacity in connection with activities in the securities or derivative market" is overly broad and could have the effect of allowing the tribunal to prohibit professionals regulated by other self-governing bodies from engaging in professional activities relating to the capital markets.

Section 95: Designation Orders

The Authority should be required to give a person which the Authority seeks to have designated as an insider or market participant notice of its intention to make the designation, disclosure of the basis for making such a designation and an opportunity to be heard, not simply an opportunity to make representations. The consequences of a finding or designation that a person is an insider or market participant are significant.

Section 100: Appeal of Tribunal's Decision

Pursuant to s. 100(6), the Tribunal should not be able to make a "further decision on new material or if there is a significant change in the circumstances" following an appeal unless the person affected has had an opportunity to be heard by the Tribunal. The person affected is denied natural justice if he is not given an opportunity to be heard in these circumstances.

Sections 102, 103 and 104: Powers to Order Reviews and Investigations

These sections should specifically provide that these orders cannot be made for the purpose of investigating the commission of an offence under sections 112 to 114 of the PCMA, a criminal offence under Part 5 of the CMSA, or a penal offence in any other jurisdiction.

The review power in s. 103(1) that may be exercised "for the purposes of the administration or enforcement of capital markets law or the regulation of the capital markets" is overly broad and at risk of being used arbitrarily. It should be restricted to permit a review of a market participant's business for the purpose of ensuring compliance with capital markets law.

A market participant's obligation to provide any information, record or thing pursuant to s. 103(3) should extend only to what is reasonably required for the purpose of the review to avoid resort to it as a fishing expedition.

As with s. 45, the authority to require individuals to provide oral information or written narratives pursuant to s. 103(3) or 103(6) should relieve the individual from having to provide information that is protected by a privilege. Oral information and written narratives compelled from an individual under these subsections should not be admissible in any civil or criminal proceeding under the laws of any jurisdiction, or in any prosecution under s. 112 of the PCMA. Disclosure of such oral information or written narratives should be governed by s. 196 and the evidence treated as if it was given pursuant to s. 104 for that purpose.

A person affected by an order under section 104(11), which allows the Chief Regulator to prohibit disclosure of information relating to an investigation, should have the ability to seek a variation of the order by the Chief Regulator. It may be desirable, for example, for an individual to advise his employer of the fact of the investigation, or for an issuer to notify an insurer. A provision like s. 38(12) of the CMSA should be included in the PCMA.

Section 105: Duty to Assist

The obligation upon a person under review or investigation is worded too broadly. As drafted, it could be interpreted to require that person to respond to questioning by the designated person without the benefit of legal counsel, or the ability to assert the protection against self-incrimination. The obligation should be limited to avoiding obstruction of the designated person.

Section 110: Administration and Enforcement

Although the s. 110 power to require a dealer to provide information to a peace officer pursuant to a court order permits the judge or justice to include terms to protect privileged communications between a lawyer and a client, none of the other powers to compel information

or documents in this Part contain similar protections. It is vitally important that all powers to compel information in the PCMA not entrench upon privilege, in particular, solicitor-client privilege.

PARTS 12 and 13: Civil Liability and Civil Liability for Secondary Market Disclosure

Section 143 and 166(5): Class Proceeding

These sections should be revised clarify that the obligation to send any material filed with the court to the Chief Regulator rests solely upon the plaintiff or applicant that has initiated the action.

Sections 145 and 169: Intervention by Chief Regulator

The Chief Regulator's ability to intervene in civil proceedings brought pursuant to Parts 12 and 13 should be restricted to issues of interpretation of capital markets law which may impact upon the administration of the Act. The Chief Regulator should not have the ability to intervene for the purpose of acting as a second plaintiff's counsel.

PART 14: General

Section 172: Power of Authority Re: Decisions

The power of the Authority to revoke or vary any of its decisions in s. 172(2) should require that the Authority give notice of its intention to do so to any person affected by the decision, and to provide a person affected with an opportunity to be heard by the Authority.

Section 174: Powers of Tribunal Re: Decisions

As with section 172, the power of the Tribunal to vary or revoke one of its decisions should be available only in circumstances where a person directly affected by the decision has been provided with an opportunity to be heard.

Sections 172 and 174 as currently drafted are unfair to persons which may be affected by such a variation and contrary to principles of natural justice.

Section 196: Disclosure of Compelled Evidence

Section 196 should require that, prior to the disclosure of evidence under paragraph 104(4)(b), the person who gave the evidence must be provided with the opportunity to be heard, not merely a chance to make representations.

The decision whether to disclose evidence given under paragraph 104(4)(b) should be made by the Tribunal or the court, not the Chief Regulator. It is vitally important that such decisions by made by a person acting in a judicial or quasi-judicial capacity, entirely independent of and disinterested in the investigation. See, for example, section 59 of the *Chartered Accountants Act, 2010*, S.O. 2010, c. 6, Sch. C, which requires the Institute of Chartered Accountants to apply to the Superior Court of Justice if it proposes to disclose information obtained by the Institute in the

administration of that statute and the by-laws to a public authority, and prohibits the disclosure of information that would defeat a person's protection against self-incrimination or violate solicitor-client privilege:

> **Disclosure to public authority**
>
> 59. (1) The Institute may apply to the Superior Court of Justice for an order authorizing the disclosure to a public authority of any information that a person to whom subsection 58 (1) applies would otherwise be prohibited from disclosing under that subsection. 2010, c. 6, Sched. C, s. 59 (1).
>
> **Restrictions**
>
> (2) The court shall not make an order under this section if the information sought to be disclosed came to the knowledge of the Institute as a result of,
>
> (a) the making of an oral or written statement by a person in the course of an investigation, inspection or proceeding that may tend to criminate the person or establish the person's liability to civil proceedings, unless the statement was made at a hearing held under this Act;
>
> (b) the making of an oral or written statement disclosing matters that the court determines to be subject to solicitor-client privilege; or
>
> (c) the examination of a document that the court determines to be subject to solicitor-client privilege. 2010, c. 6, Sched. C, s. 59 (2).

Similar protections should be incorporated into section 196 of the PCMA.

In general, the absence of these types of mechanisms and also of the express prohibition on disclosure of compelled testimony to persons responsible for the enforcement of the criminal law of any other country or jurisdiction contained in section 17(7)(b) of the Ontario *Securities Act* heightens the concern that compelled evidence may be disclosed to authorities including in other jurisdictions without sufficient limitations on use designed to protect the witness' privilege against self-incrimination.

In *Mr. A. v. Ontario Securities Commission*, [2006] O.J. No. 1768 Justice Colin Campbell denied an application by a witness for a declaration that he was not compellable to attend at an examination by the OSC in part because there was a risk that his testimony could end up in the hands of American authorities and be used against him in criminal proceedings in the United States without regard for his *Charter* protections against self-incrimination. In dismissing the application, Justice Campbell took comfort from the fact that the framework set out in the *Securities Act* was sufficient to protect Mr. A.'s *Charter* rights. In particular, Mr. A. would be entitled to prior notice and a hearing under section 17 if the OSC wanted to disclose his compelled testimony to the SEC or any other person. His Honour was "satisfied that with the supervisory role of the Commission itself and the protective mechanisms of ss 16 to 18 of the *Securities Act*, the Staff of the Commission [were] aware of their varying roles and duties".

To omit these important protections in the new statutory scheme risks a different result in circumstances similar to those in *Mr.A.* in future.

Section 200: Collection from Third Party

Subsection 200(4) should permit the third party who has failed to pay money to the Authority as required under subsection (2) to make representations concerning his or her liability to pay the amount demanded, and the amount of the alleged indebtedness, and to appeal the decision of the Authority.

CAPITAL MARKETS STABILITY ACT

PART 1: Information Collection and Disclosure

In general, see comments relating to section 45 and 196 of the PCMA.

Section 10 of the CMSA should prohibit the Chief Regulator from compelling the production of information protected by privilege.

If the information being compelled consists of oral information or written narratives from an individual, the CSMA should preclude that evidence from being admitted into evidence in any civil or criminal proceeding under the laws of any jurisdiction, including in any prosecution under Part V of the CSMA.

Decisions about the disclosure of any information or records compelled by the Chief Regulator should be determined by the Tribunal or the court, not the Chief Regulator, for reasons discussed in relation to s. 196 of the PCMA.

Section 17 should provide the person who gave the evidence sought to be disclosed an opportunity to be heard by the Tribunal or the court before a decision is made to disclose it, not just an opportunity to make representations.

PART 2: Systemic Risk

Section 27: Capital Markets Intermediaries

Given the consequences of being designated as a "systemically important" capital markets intermediary, the capital markets intermediary should be given a right to be heard and call evidence prior to that determination being made, not just the ability to make "representations". The factors to be considered in s. 27(2) are all factual in nature and require a proper evidentiary foundation to be laid.

Section 34: Urgent Orders

Section 34(5) should provide that notice to and an opportunity to be heard or to make representations by an affected person is required prior to the making of an "urgent order" unless, in the Authority's opinion, to do so would undermine the effect of the order or it is not practicable to or appropriate to do so. Providing notice and an opportunity to be heard should be the rule, not the exception, to inspire confidence in the administration of the legislation.

PART 3: Administration and Enforcement

The power to enter premises without a search warrant under section 37(3) should be limited to business premises.

Section 38 should expressly provide that the Chief Regulator cannot order an investigation under this section for the purpose of inquiring into the commission of any criminal offence under Part 5 of the CMSA, or of any penal offence in any other jurisdiction.

Section 39 should be redrafted to remove the duty to provide "all assistance that is reasonably required". See comments relating to section 105 of the PCMA.

Sections 43 and 44 must require that a person believed to have violated the CMSA be provided with notice of the suspected infraction and an opportunity to be heard by the Tribunal prior to a finding being made that the person is liable to a fine. The proposal to treat suspected violations of the legislation, which carry significant financial penalties, like traffic tickets is an affront to the principles of procedural fairness, which require, as a general proposition, that before a decision adverse to a person's interests is made, the person affected be notified of the case to be met and given an opportunity to respond. Findings of this nature should be made by a quasi-judicial body, not the Chief Regulator. Factors to be taken into account in s. 43(2) should include the person's cooperation and any other mitigating factors.

PART 4: General Offences

Comments relating to section 114 of the PCMA apply equally to section 60 of the CMSA.