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VIA E-MAIL

December 8, 2014

Cooperative Capital Markets Regulatory System

Dear Sir/Madam:

Re: Comments on the Consultation Draft of the Capital Markets Stability Act ("CMSA")

The Walton Group of Companies ("**Walton**") welcomes the opportunity to comment on the consultation draft of CMSA. Walton is an issuer/promoter of exempt market investment products and Walton Capital Management Inc. ("**WCMI**"), an affiliate of Walton, is an exempt market dealer ("**EMD**") that is registered in all Canadian provinces. The Walton Group is headquartered in Alberta, but because it operates across Canada, the implementation of the CMSA and the Provincial Capital Markets Act ("**PCMA**") will have a significant impact on the Walton Group's business.

We have organized our comments in two letters. This letter provides comments on the CMSA. A separate letter will provide comments on the PMCA. Given that the CMSA and PCMA will operate together to create a new capital markets/securities regulatory system in Canada, we ask that you please review both letters together to reflect to our comments.

The Walton Group is not opposed to the concept of a "national regulator" for capital markets in Canada. The proposed Cooperative Capital Markets Regulatory System ("**CCMR**") could potentially have a positive benefit to Canada and its economy as a whole if it were to be handled and operated properly and fairly in acknowledging regional differences and protecting the fundamental legal rights of market participants. The proposed CCMR creates an opportunity to organize the capital markets in a manner that could significantly boost the Canadian economy in a sustained manner and maintain appropriate protections for the participants in those markets, including investors. We do not see these two goals as inconsistent or difficult to achieve.

However, we are also not opposed to the current system of Canadian capital markets regulation. We believe the current system has done, and currently does, a very good job in regulating capital markets in Canada, in particular in recognizing and respecting the fundamental differences in the capital markets that are present in different areas of Canada. We believe that the current proponents of the CCMR have not given enough credit to the achievements of the provincial securities regulators, through the Canadian Securities Administrators ("**CSA**"), in facilitating cooperation among the various jurisdictions and creating a system that is substantially harmonized, yet recognizes and enhances regional capital market differences. In our view, the concerns that have been raised with the current system could be handled easily through other initiatives and systems of cooperation that do not require the historically significant, and potentially unsettling, changes that are currently being proposed by the CCMR.

Our concerns in this regard primarily relate to the potential that the CCMR has to materially and negatively impact and possibly eliminate the diversity of the Canadian capital markets across the country. Canada's strength arises from the diversity of its people, industry and culture. Similarly, Canadian capital markets are not uniform in that certain segments of capital markets in one region play a much more important part than they do in other regions. It is not by accident that there have arisen substantive differences in how those segments are regulated in different areas of the country. If the practical result of the implementation of the CCMR is to remove, in one or more regions, the benefits resulting from those differences, the Canadian economy as a whole could be substantially and negatively impacted. We fear that the legislation currently proposed by the CCMR could have this result.

<u>CMSA – Substantive Comments</u>

1. **Sufficient time has not been provided for capital market participants to review, fully understand and properly comment on the CMSA.**

We submit that the implementation of the CCMR is the most significant change to the Canadian capital markets regulatory system since the development of the "second generation" of provincial securities acts in Canada, and is likely more significant than that. The enactment of the CMSA and the PCMA are among the most crucial steps as they set out the framework under which the CCMR will operate, including the powers to be exercised by the Authority and the rights available (or not available, as the case may be) to capital markets participants. The CMSA itself introduces a new and significant layer to the capital markets system which, while initially simple to explain (regulation of national systemic risk), is not so easy to understand, including its potential reach, its interaction with the PCMA, its operation by the provinces signing on to the CCMR and its operation in the provinces that do not sign on to the CCMR.

Having read through the draft CMSA numerous times, we still struggle to adequately understand its full impact and reach. The CMSA adds a completely new layer to capital markets regulation. Additionally, the PCMA is not a simple re-creation of the current provincial legislation but contains many significant changes to the legislation currently in place and many more subtle changes in wording, the reasons for which, in a number of instances, are not readily apparent. However, many of those changes clearly have a broader reach, and place more limits on the rights of capital market participants than provisions in the current legislation.

In addition, while the CMSA and PCMA provide the framework for the proposed CCMR, a very significant portion of the substantive rules will be contained in the regulations to be issued under the CMSA and PCMA. Those regulations, which we expect to be more significant in size and at least as significant in practical impact than the CMSA and PCMA themselves, are not proposed to be published in draft form for comment until December 19, 2014.

Given the crucial interaction between the CMSA and PCMA and their respective regulations, we submit that complete and effective comments cannot be provided on the CMSA and PCMA until the draft regulations have been published and market participants have been given sufficient time to consider them. In this regard, we have more comments and questions with respect to the CMSA than are set out in this letter, but in order to provide meaningful comments, we need to assess how they are impacted by the regulations. We anticipate that we will provide further comments on the CMSA itself once we have reviewed the draft regulations.

Accordingly, it would be appropriate for the comment period for the CMSA and PMCA to be open until the end of the comment period for their respective regulations.

2. **As worded, the CMSA appears to delegate to the provinces that sign on to the CCMR the ability to administer the CMSA in those provinces that do not sign on to the CCMR.**

Under the terms of the CMSA, the Authority is responsible for the administration of the CMSA (Section 6(1)). In addition, the CMSA also provides that the Federal Minister of Finance may, after consultation with the Council of Ministers, make an order assigning to the Authority, the administration of any provision of the Bank Act.

The Authority will be administered by persons from the provinces that accept and sign on to the CCMR through the applicable Memorandum of Understanding (the "**MOU**") (the "**Participating Provinces**"). Those provinces in Canada that do not sign on to the CCMR (the "**Non-Participating Provinces**") will not be participating in the Authority or in the administration of the CCMR.

However, given the federal nature of the CMSA (national systemic risk, data collection in that regard and enforcement of certain criminal law matters), the CMSA will be law in the Non-Participating Provinces, and, based on the wording in the CMSA, will be administered and enforced by the Authority which will be run by Participating Jurisdictions. Also, any provisions of the Bank Act (being federal legislation) that are assigned to the Authority will be administered and enforced by the Authority.

We question the authority of the Participating Provinces to administer and enforce the CMSA (and potentially portions of the Bank Act) in the Non-Participating Provinces and do so against the citizens of the Non-Participating Provinces without their consent. A concern in this regard is how the Participating Provinces can properly enforce such law in any Non-Participating Province when the Participating Provinces may not understand the unique markets that exist in such province or how those markets add to the economy of such province. There is also a concern on how the policy makers of the Participating Provinces can enforce policy in such Non-Participating Province when the citizens of that province did not elect those policy makers.

We note that Section 6(2) of the CMSA states that "[i]n fulfilling its mandate, the Authority must coordinate, to the extent practicable, its regulatory activities with those of other federal, provincial and foreign financial authorities so as to promote efficient capital markets, to achieve effective regulation and to avoid imposing an undue regulatory burden." We agree with that subsection, however, we do not interpret Subsection 6(2) as addressing the concerns raised above.

3. The wording regarding the collection and use of information under Part 1 of the CMSA is too broad and is, in a number of spots, unclear.

(a) The wording in Part 1 regarding the type of information that may be collected by the Authority should be revised to make it clear that only information that will reasonably assist the fulfillment of the purposes set out in Subsections 9(a) and (b) and 10(a) and (b) may be collected (being the fulfillment of the federal powers intended to be fulfilled under the CMSA, not any provincial powers). The Authority should have no power to collect information that may have nothing to do with the purposes set out in those subsections and which may reach into provincial powers.

(b) Section 12 provides that certain third parties may provide personal information to the Authority if the disclosure is for the purpose of the administration of the CMSA or of assisting in the administration of the capital markets or financial legislation in Canada or elsewhere. The underlined portion of the previous sentence is not within the purposes of CMSA and we submit it should accordingly be removed. The inclusion of such phrase blurs the lines between the role of the Authority under the CMSA (federal power) and under the PMSA (provincial power). Presumably the PMSA provides such information gathering powers to the Authority and therefore the PMSA is the proper place for the provision of such powers, not the CMSA.

(c) We recommend that Section 13(2) which requires disclosure of information that "is not otherwise prohibited by law" also include wording that protects privacy of personal information. We suspect that the quoted wording above is intended to primarily relate to Canadian privacy laws and therefore we recommend that the reference should be made clear in the legislation.

(d) In some sections of Part 1, the Authority is given powers to disclose information (ie, Section 14) and, in other sections of Part 1, the Chief Regulator is given power to disclose certain information (ie, Section 15). It is unclear if there is a difference in practice between action by the Authority and action by the Chief Regulator. If there is a difference, it would be helpful to have an explanation of that. If there is no difference, it would be helpful to use the terms consistently.

(e) It is unclear what the difference is between the powers to disclose information provided under Section 14 and under Section 15. Given that Section 14 is more general, it would be helpful to know if the requirements under Section 14 are required to be met when disclosure is contemplated under Section 15. If the Chief Regulator believes that the requirements for disclosure under Section 15 cannot be satisfied, is the Authority able to nevertheless make the disclosure to those persons under Section 14 if its requirements are satisfied? We believe the wording of Sections 14 and 15 is confusing. The powers of the Authority and the Chief Regulator to disclose to any other party information received by it under Sections 14 and 15 are very broad, especially because that information can be provided to those other parties for purposes that are beyond those for which the information was gathered by the Authority. We believe that the stipulated standard of "exceptional circumstances" as referenced in Section 15 fails to provide adequate protection, particularly given the very broad and discretionary nature of the terms "exceptional".

We recommend that (i) a more defined, restrictive and objective standard be used and that (ii) some independence be inserted into the process, for example, a process whereby the Tribunal must approve such release of information. Given that personal information can be released to other parties under Sections 14 and 15, we believe that it is appropriate to have the independent Tribunal approve the release before the information is disclosed. It would be of little comfort to any person to only have the Tribunal review a decision of the Authority or the Chief Regulator to release personal information after that personal information has already been released.

(f) The concept of "entering into an arrangement or agreement … regarding the terms of the disclosure" referred to in Section 16 is unclear as to what type of arrangement, or its parameters, is being referred to. The failure to define the scope of the arrangement creates ambiguity and reduces the protective effect of the section.

(g) In Section 17, the Chief Regulator must, before it discloses "compelled evidence", give notice to the person who gave the evidence and give that person an opportunity to make representations. While not specifically stated, it appears that the representations are to be made to the Chief Regulator. We find it troublesome that the Chief Regulator is the decision maker in a situation in which the Chief Regulator has already come to the conclusion that it wishes to make the disclosure. Since the person was compelled under oath (ie, involuntarily) to give such information, some independence ought to be inserted into the process, for example, a process whereby the Tribunal makes the decision as to the release of the information following representations made to it by both the Chief Regulator and the affected person.

(h) We believe that the protections set out in Section 188 of the PCMA that are proposed to be provided to persons required to provide information to the Authority under Section 187 of the PMCA should also be included in the CMSA.

4. The powers of the Authority under Part 2 of the CMSA do not impose sufficient objective standards or thresholds on the Authority and therefore could result in unnecessary and significant damage to Canadian businesses and intrude on provincial powers.

The definition of "systemic risk" in the CMSA and the operation of Sections 18 to 30 of the CMSA provide the Authority with significant and broad powers to designate individual businesses in certain Canadian industries as "systemically important", thereby allowing the Authority to regulate those businesses in a manner that, prior to such designation, would not otherwise have been applicable. These powers could be exercised in a way that could materially and negatively impact the profitable operations of those

businesses, make it impractical for those businesses to carry on operations or simply require that those businesses cease to operate, notwithstanding that, when formed or operated prior to such designation, they would not have contemplated being regulated in that manner. The exercise of such powers may be justified if doing so would prevent significant damage to the Canadian economy as a whole. The arbitrary or capricious exercise of such powers by the Authority in a circumstance where there is not a true, material and reasonably imminent risk could not only significantly damage Canadian businesses, it could be seen as an intrusion on provincial powers. We submit that stronger objective standards need to be inserted into the CMSA to ensure the proper and constitutional exercise by the Authority of its powers under Part 2 of the CMSA.

(a) In Section 3, systemic risk is defined as "a threat to the stability or integrity of Canada's financial system that originates in, is transmitted through or impairs capital markets and has the potential to have an adverse effect on the Canadian economy" (emphasis is ours). Our concerns with this definition and with the further wording in Section 4 include the fact that:

- a threat only has to have the "potential" to have an adverse effect in order for it to constitute a systemic risk, thereby giving the Authority jurisdiction to regulate. We suggest that a higher and objective standard be required for the triggering of the Authority's jurisdiction, such as "would reasonably likely" have an "imminent or proximate" adverse effect on the Canadian economy; and
- only a potential "adverse effect" would be required to trigger the Authority's jurisdiction. Again we suggest a higher standard be required, such as a "significant adverse effect" or "material adverse effect".

(b) As indicated above, in Sections 18 to 30 of the CMSA, the Authority has the power to designate individual businesses in certain Canadian industries (trading facilities, clearing houses, credit rating organizations, benchmarks and capital market intermediaries – the "**Target Businesses**") as "systemically important", thereby allowing the Authority to thereafter regulate such Target Businesses. Generally, under those provisions, the Authority can declare those Target Businesses to be "systemically important" if, in the Authority's opinion, the activities of that business "could pose a systemic risk related to capital markets". Our concern is that the standard for triggering the jurisdiction of the Authority is only that such activity "could" pose a systemic risk. This technically means that all the Regulator has to do is come up with a scenario involving a Target Business that could result in a systemic risk and the Regulator could regulate that business, potentially from the moment such business commences operations, even though there is no imminent risk or actual risk. We suggest that a higher and objective standard be required for the triggering of the Authority's jurisdiction, such as the activities of the entity "would reasonably likely" pose an "imminent or proximate" systemic risk related to capital markets.

(c) In the sections that list the factors that the Authority is required to review in its determination of whether a business should be designated as "systemically important", we suggest that:

- there be included a specific requirement that the Regulator reasonably weigh the detriment to the business (and its industry in general) as a result of being declared as "systemically important" against the benefit to the Canadian economy as a whole from that declaration; and
- remove the last factor in each of those lists ("any other risk-related factors that the Authority considers appropriate") with "any other factor that should reasonably be considered". This creates a stronger objective standard to be followed by the Authority.

(d) Prior to declaring any entity "systematically important" under Part 2, the Authority is required to notify the Council of Ministers of its intention to make the order and to give the entity an opportunity to make representations. While not specifically stated, we assume that the representations are to be made to the Chief Regulator or someone else in the Authority. We find it troublesome that, if the Authority has come to the conclusion that it wishes to make an order, the entity that could be harmed by such declaration can only make representations to the Authority itself as the initial decision maker. We

believe that, given the potential for significant harm to the entity, some independence needs to be inserted into the process, ie, a process whereby the Tribunal makes the decision as to (i) the issuance of an order and (ii) the requirements, prohibitions and restrictions that will placed on that entity under the order, following representations made to the tribunal by both the Chief Regulator and the entity.

(e) We believe that a specific provision should be included in Part 2 that requires that any requirements, prohibitions and restrictions that may be placed against an entity declared to be "systemically important" under any regulations created for that purpose (see Sections 19, 21, 24, 26 and 28) must be proportionate to the systemic risks presented by the activities of such entity.

(f) Given the significant implications that a declaration that a Target Business is systemically important may have on the rest of the industry in which that business operates or to the capital markets industry as a whole, we suggest that a limited (but effective) right be included in Part 2 for other relevant parties to make representations along with the representations referred to in 7(d) above.

(g) Sections 30 to 33 provide the Authority with significant powers to prescribe classes of securities or derivatives or to prescribe "practices" as "systemically important" thereby allowing the Authority to regulate such securities, derivatives or practices in a manner that, prior to such designation, would not have been applicable to them. Our comments in 4(b), (c) and (d) above are also applicable to Sections 30 to 33.

5. The definition of "capital markets intermediaries" and its use in Sections 27 to 29 includes issuers that are not truly capital market intermediaries and does not include other issuers that could be systemically risky.

Clause (b) of the definition of "capital markets intermediary" includes "an issuer whose primary purpose is to invest money provided by its security holders, including an investment fund".

We find this portion of the definition puzzling because we believe that the use of the defined term "investment fund" would be more than adequate to catch the group of issuers that we believe the drafters are potentially contemplating. We do not know what other issuers the drafters are trying to capture beyond "investment funds". We believe there should be further explanation in this regard.

We also find it odd that other issuers are excluded from this definition. The only issuers that are caught by this definition are issuers the primary purpose of which is to invest money provided by its security holders. If these issuers could be seen as potentially systemically risky, surely other issuers could also be potentially systemically risky. As an example, at its height, the aggregate capitalization of Nortel Networks constituted more than one-third of the capitalization of all companies listed on the Toronto Stock Exchange. We speculate that Nortel might have been a candidate for being declared systemically risky. However, Nortel would not have been caught under the proposed definition of "capital markets intermediary" or any proposed provision in Part 2 that permits the Authority to declare entities as systemically risky.

This leads us to believe that the drafters of the legislation are intending something specific by not catching larger issuers that could be systemically risky in certain circumstances but catching other issuers that fall into (b) of the definition of "capital markets intermediary". It would be helpful for the drafters of the CMSA to explain why this is the case.

Without more, it is our view is that either all issuers should be potentially caught within, or the concept of an issuer should be removed altogether from, the definition of "capital markets intermediary".

6. There should be a requirement that notice of a proposed "urgent order" under Section 34(5) be provided to the Council of Ministers prior to the issuance of the order.

The issuance of an "urgent order" by the Authority under Section 34 must, because of its nature, be viewed as an extraordinary action by the Authority. This issuance of such an order, if not handled properly by the Authority, could cause significant damage to the capital markets instead of alleviating a serious and immediate systemic risk.

As a result, we recommend that, before any "urgent order" is issued under Section 34, the notice to the Council of Ministers under Section 34(5) must be given at least 48 hours prior to the issuance of the order. This will allow the Council of Ministers, which sets the policy for the Authority, to consult with the Authority concerning the proposed order and be the "sober second thought" to the proposed action of the Authority. Section 35(1) recognizes this consultative role of the Council of Ministers in such a circumstance because it requires that the Federal Minister of Finance consult with the other members of the Council of Ministers before the Minister orders the Authority to make, amend or repeal an urgent order. Our view is that such consultative process should also apply to any urgent order proposed to be issued by the Authority of its own volition.

7. The CMSA does not contain adequate provisions to protect privileged information and communications.

The CMSA does not, but should, contain a specific provision that states that <u>any</u> records, communication or other information (collectively "**Information**") for which solicitor and client or other similar privilege can be claimed are not required to be delivered by any person to the Authority, the Chief Regulator, the Tribunal or other party under any terms of the CMSA requiring the delivery of any Information. Such a provision should also include a clear process by which Information over which privilege is claimed can be protected until such time as there is a judicial determination of whether the claims of privilege should be upheld.

8. The commencement of reviews and inquiries under Part 3 "Administration and Enforcement – Reviews and Inquiries" should be commenced only upon the approval of the Tribunal.

Part 3 "Administration and Enforcement – Reviews and Inquiries" provides that the Chief Regulator may issue orders launching reviews and inquiries and set out the parameters that the review is to follow. To ensure appropriate independence and oversight in the granting of such orders and setting out the powers exercisable thereunder, we are of the view that such order and powers should be granted not by the Chief Regulator, but by the Tribunal on application by the Chief Regulator (or his or her appropriate delegate). We note that the securities legislation of a number of the Participating Provinces specifically require that investigations can only be commenced by order of the applicable securities commission and not by the executive director of that commission.

9. The ability of the Chief Regulator under Part 3 "Administration and Enforcement – Administrative Monetary Penalties" to issue a notice of violation and administer significant penalties prior to an appropriate hearing on the matter could significantly prejudice capital market participants.

Under Section 44, the Chief Regulator may issue a notice of violation against a person if the Chief Regulator has reasonable grounds to believe that the person has committed a violation. Such Notice is required to set out every act or omission for which the notice is served and every provision at issue as well as the "administrative" monetary penalty that the person is liable to pay, which can be as high as $1 million in the case of an individual or $15 million for persons other than individuals. The person must either pay the fine or make representations to the Chief Regulator within 30 days. If the person pays the fine or does not pay and does not make representations within the required time period, the person is deemed to have committed the violation.

(a) The use of the words "notice of violation", as opposed to "notice of alleged violation" or "notice of alleged charge", creates the impression that the subject person is guilty prior to any representation

being made by it or its counsel. We assume that any such notice will be made public at the time that it is issued, which also means that the public will be told that the person is guilty, even though the person may not be. The practical impact of the above is that a person's reputation could be ruined even though they may not be guilty or may have not yet been able to present an appropriate defense. This could result in the loss of the ability for a person to earn a living or could result in significant losses to a business or the shut-down of a business, notwithstanding that the person may not be guilty. We see this as highly inappropriate and potentially unconstitutional.

(b) The burden of proof on the Chief Regulator for the issuance of a notice of violation is that he/she has "reasonable grounds to believe that the person has committed a violation". We submit that the standard should be on a balance of probabilities after the subject person has been given the reasonable ability to provide a defense. Our view is that this low burden of proof could be a violation of the common law principles of natural justice and/or procedural fairness and could be unconstitutional.

(c) As the Chief Regulator is the one who will initially make the determination that a violation has occurred, it is inappropriate to require the subject person to make its representation (ie, its defense) to the Chief Regulator. There is a significant issue of bias in this context which could be a violation of the common law principles of natural justice and/or procedural fairness and could be unconstitutional. Justice in this context cannot be done or be seen to be done when the subject person is required to make their defense in front of the person who declared them guilty in the first instance.

(d) The notice of violation issued against a person is required to "set out every act or omission for which the notice is served and every provision at issue"; however, there is no requirement for the production of the evidence that the Chief Regulator relied upon or the actual reasons for the decision. Without such disclosure to the subject person, that person will not be able to mount a reasonable or effective defense against the violations. Our view is that this could be a violation of the common law principles of natural justice and/or procedural fairness and could be unconstitutional.

(e) A deadline of 30 days to make representation in the context of potentially such a significant fine is in our view far too short to enable an appropriate defense to be mounted. We submit that a period of at least 90 days would be appropriate.

(f) We suspect that, procedurally, what may actually occur in these situations is that, prior to issuing a "notice of violation" under Section 44, the Authority will undertake an investigation of the person and contact that person in the context of the investigation. What has happened in the past in the context of investigations by securities commissions is that persons under investigation have been given a choice of either (i) entering into a settlement agreement, which imposes fines or cease trades or other penalties, or (ii) facing the issuance of a "notice of hearing" by the securities commission. Unfortunately, because (i) of the significant negative impact that a notice of hearing (which <u>only alleges</u> violations) can have on the reputation and business operations of a person, and (ii) the significant costs that a person may incur to properly defend itself against a securities commission which has significant resources at its disposal, many persons in such a situation fell compelled to accept a settlement even though they may not be guilty or their conduct may not have been as serious as alleged by the securities commission. The above scenario is in the context of the potential issuance of a notice of hearing under current provincial securities legislation which only "alleges" violations. In the context of Section 44, the notice issued by the Chief Regulator will be a notice of <u>actual</u> violation. We suspect that persons facing a Section 44 notice will feel even more significant pressure in those circumstances to settle even though they may not actually be guilty or their conduct may not have been as serious as alleged. We submit that this would be an unfortunate and unreasonable result of the implementation of Section 44.

Our view is that the procedure that should be followed in Part 3 "Administration and Enforcement – Administrative Monetary Penalties" is the same procedure that is generally followed under current provincial securities legislation. That is, if, after an investigation, the Chief Regulator is of the view that there has been a violation, a "notice of hearing" should be issued that "alleges" violations. After the

issuance of the “notice of hearing”, the subject person would then have the right to a hearing in front of the Tribunal, where both the Chief Regulator and the subject person may make representations. The procedure to be followed in that regard must be such that the person has adequate time and information to prepare a defense. For the CMSA to provide otherwise could result in conduct by the Chief Regulator that are violations of the principles of natural justice and procedural fairness and could be unconstitutional.

10. **The powers of the Tribunal under Section 49 to grant cease trade orders or to order certain entities to change their practices and procedures does not contain sufficient standards of proof before the jurisdiction of the Tribunal is triggered. The result could be an unconstitutional intrusion into provincial powers.**

Section 49 provides that the Tribunal may, if, after a hearing, it considers it necessary to protect the stability or integrity of Canada’s capital markets, make certain cease trade orders and orders requiring certain entities to change their practices or procedures. The statement “stability or integrity of Canada’s capital markets” is not defined anywhere in the CMSA and is capable of a broad interpretation that may negate meaningful direction to the Tribunal in its deliberations under this section. We believe this would also be the case if the wording in Section 49 were changed to “integrity of Canada’s financial system”, for which some guidance is provided in Section 3.

We believe that any standard of proof that is set out in Section 49 needs to include an element of reasonable likelihood of imminent or proximate danger to the stability or integrity of Canada’s capital markets. Otherwise, orders could technically be issued by the Tribunal where they are not truly justified. The exercise of such powers by the Authority in a circumstance where there is not a true, material and reasonably imminent or proximate risk could not only significantly cause damage to certain Canadian businesses, it could be seen as an intrusion on provincial powers.

11. **The powers of the Tribunal under Section 50 to order persons to retain the property of another person or to refrain from withdrawing its property from another person, if the Tribunal considers that it is “<u>expedient</u>” for the administration of the Act or to assist in the administration of a foreign jurisdiction’s capital markets, does not contain sufficient standards of proof before the jurisdiction of the Tribunal is triggered.**

Under Section 50, the Tribunal may, if it considers it expedient for the administration of the Act or to assist in the administration of a foreign jurisdiction’s capital markets, order that a person (i) retain the funds, securities or other property of another person that the first person has under its control, or (ii) refrain from withdrawing funds, securities or other property from another person that has this under its control.

This effectively may mean that the Tribunal, if it finds it expedient to do so, could issue orders preventing persons in Canada from having access to their property (be it cash, securities or otherwise):

(a) in the context of <u>merely</u> the <u>administration</u> (ie, not enforcement) of the CMSA, or

(b) because the Tribunal wishes to assist <u>merely in</u> the <u>administration</u> (ie, not enforcement) of a foreign jurisdiction’s capital markets legislation.

The decision-making standard of “expedient” for the triggering of the Tribunal’s jurisdiction under this section is shockingly low and is potentially significantly prejudicial to property rights of persons in Canada. Moreover, as a result, the provisions as drafted could be unconstitutional as an intrusion on provincial powers. This is even more troublesome when viewed in the context of (b) above, where “mere expediency” is required to permit the Tribunal to withhold property from Canadians to assist a foreign government.

Rather than “expediency”, we submit that the Tribunal should be held to the same standards referred to in 10 above, ie, there must be included in Section 50 an element of reasonable likelihood of imminent or

proximate danger to the stability or integrity of Canada's capital markets or, in the case of (b) above, to the foreign jurisdiction's capital markets.

12. The powers of a court under Section 52 to appoint a receiver, trustee or liquidator over all or a part of the property of a systemically important entity, if the court is satisfied that the appointment is necessary to "address" a systemic risk related to capital markets, does not contain sufficient standards of proof before the jurisdiction of the court is triggered.

Under Section 52, a court may, on application by the Chief Regulator, make an order appointing a receiver, trustee or liquidator over all or a part of the property of a systemically important entity if the court is satisfied that the appointment is necessary to "address" a systemic risk related to capital markets.

Our view is that the jurisdiction to appoint a receiver/trustee/liquidator over the property of a systemically important entity incorporates an unreasonably low standard in this regard, because (i) "address" could easily have a very broad interpretation, and (ii) as referred to in 4 above, all that is required for there to be a systemic risk under Section 3 is that there be a "threat to the stability or integrity of Canada's financial system that … has the potential to have an adverse effect on the Canadian economy." (emphasis is ours)

We believe that any standard of proof that is set out in Section 52 needs to include an element of reasonable likelihood of imminent or proximate danger to the stability or integrity of Canada's capital markets. Otherwise, such orders could technically be issued by the court where they are not truly justified. The ability of the court to exercise such powers in a circumstance where there is not a true, material and reasonably imminent or proximate risk could not only significantly cause damage to certain Canadian businesses, it could be unconstitutional and put the entire capital markets of the country at risk.

13. The due diligence defence provided in Section 60 may not be effective.

Section 60 provides that, if an employee or agent of a person, within the scope of their employment or authority, commits an offence under the CMSA, that person also can then be found to have committed the offence unless (i) the offence was committed without the person's knowledge, and (ii) the person exercised due diligence to prevent its commission.

We do not understand what is required in order for a person to be able to say (under (ii) above) that it has exercised due diligence to prevent its commission. Our concern is that there may be circumstances in which an offence is surreptitiously committed in a novel and unanticipated manner. The person is not aware that the offence is being committed, and was not in a position to exercise appropriate due diligence to prevent its commission. We believe this section requires revisions to properly address the requirements to establish the due diligence defence.

14. The term "publicly traded" as used in Part 5 Criminal Offenses should be defined.

Part 5 sets out a number of criminal offences that are triggered when conduct is undertaken by a person in connection with the securities of a "publicly traded" issuer. These offences include insider trading, tipping, recommending and misrepresentation. Typically, under current provincial securities legislation, the concept of a "reporting issuer", which has a specific and clear definition, is the trigger for such offences. Since it would have been easy to use the definition of "reporting issuer" in the CMSA, the drafters of the CMSA must have intended to encompass a wider group of issuers with their use of the words "publicly traded".

The problem is that the term "publicly traded" is somewhat uncertain. For example, that term was adopted into the Canadian Income Tax Act a number of years ago in relation to what is referred to as the "SIFT rules". There has been significant concern among tax practitioners as to the meaning of this term and it has led to a significant amount of uncertainty in the interpretation of the "SIFT rules".

Given that the offences in Part 5 are criminal offences potentially involving significant monetary penalties and jail terms, we believe it is crucial for there to be certainty around what is meant by "publicly traded". We recommend that a sufficiently certain definition for "publicly traded" be included in Part 5, or alternatively, the use of "reporting issuer" be maintained.

15. We have concerns that the "criminal offences" created under Part 5 are not true matters of criminal law. Our view is that they are likely better characterized as administrative matters and therefore treating them as criminal offences may constitute overreach by the CMSA.

Part 5 sets out a number of offences that are called "criminal offences". These relate to matters such as insider trading, tipping, tipping based on action, recommending and misrepresentation. The Canadian Criminal Code does contain provisions relating to some (but not all) of these matters, particularly in the context of clear fraudulent conduct.

The December 2011 decision of the Supreme Court of Canada in *Reference Re Securities Act*, confirmed that it was appropriately in the sphere of the federal government to enact and administer legislation dealing with, among other things, national systemic risk in the Canadian capital markets and criminal law matters arising in connection with the Canadian capital markets. However, this does not mean that the federal government can, through federal legislation, declare anything to be a criminal law matter and then regulate it. The matter has to be truly a criminal law matter in order to do so. In other words, the concept of *mens rea*, ie, the "intending mind" or true and actual criminal intent, needs to be front and center in the matter be regulated. In addition, the enforcement of these matters needs to be handled through the police and criminal law courts with all the procedures and protections for the accused that apply in that context. We believe that, without appropriate changes to the provisions in Part 5, a number of the provisions therein may constitute inappropriate overreach by the CMSA.

We recommend that the provisions of Part 5 be revised to ensure that:

- *mens rea* is a clear element that must be present for each of the proposed offences;
- all investigations and enforcement under Part 5 be handled by the applicable police in the applicable jurisdiction and by the applicable criminal law courts; and
- all criminal law procedures and protections for the accused be applicable to the administration, investigation and enforcement of these matters, including the principle of innocence until proven guilty and the standard of proof being 'beyond a reasonable doubt'.

16. The decision of the Authority under Section 34 to issue an "urgent order" should be reviewable by the Tribunal. Also, all decisions of the Chief Regulator and the Authority should be reviewable by the courts, whether or not they have been first reviewed by the Tribunal, and all decisions of the Tribunal should be reviewable by the courts.

Section 103 provides that a person who is directly affected by a decision of the Chief Regulator, other than for a decision under Section 34 (urgent orders), may apply to the Tribunal to have the decision removed.

We do not understand why the issuance of an urgent order under Section 34 would not be reviewable by the Tribunal. Our view is that the urgent order concept under Section 34, given the rapid process, *ex parte* nature and the types of orders that can be issued thereunder, could lead to substantive damage to the rights and property of individuals and businesses. We do not dispute the need for the process under Section 34, but any decision thereunder should be reviewable by the Tribunal to ensure that there is an appropriate check and balance on this extraordinary power.

We recommend that provisions should be included in Part 6 that make it clear that all decisions of the Chief Regulator and the Authority under the CMSA are reviewable by the courts whether or not such

decisions have also been reviewed by the Tribunal and that all decisions of the Tribunal under the CMSA are reviewable by the courts. Ultimately Canadian courts have the necessary independence to ensure that appropriate oversight is maintained over the decisions of the Chief Regulator, the Authority and the Tribunal. Court review also ensures that a body of jurisprudence is created to provide certainty and consistency in the application of the PCMA. This provides important guidance to the Chief Regulator, the Tribunal and capital market participants. The ability to have decisions reviewed by the courts is crucial for the proper operation of capital markets in Canada.

17. Other Matters.

In addition to the points raised above, below are further comments with respect to some specific wording in the CMSA:

(a) We note the use of the word "mandatory" as a noun in the definitions of "dealer" and "underwriter" and in Sections 38, 48, 60 and in other sections in the CMSA. This word is not used in the definition of "dealer" or "underwriter" in the PCMA or in current securities legislation. We note that the dictionary defines this term as generally a person or other entity, ie, a government, that has a mandate. We are uncertain as to what is intended by this provision and we believe that a definition should be provided for the term "mandatory".

(b) We note that the definition of "security" in the CMSA is much narrower than in the PCMA, which contains the more standard definition under securities legislation. We are puzzled as to why this is the case. Having two significantly different definitions for the same term in the CMSA and the PCMA which are both intended to operate in the same "space", is hazardous and undesirable, particularly where the PCMA definition has a well developed meaning established through case law. We submit the definitions should be identical.

(c) We note that in Section 63, in addition to the requirement of "deceit, falsehood or other fraudulent means", the person must also have "intent to defraud". We do not understand why the requirement of "intent to defraud" would also not be required in Section 62, in addition to the requirement therein of "deceit, falsehood or other fraudulent means".

We would be happy to discuss this with you further if you wish.

Yours truly,

WALTON INTERNATIONAL GROUP INC.

(signed) "Kurtis T. Kulman"

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KTK\jvm