FAIR | Canadian Foundation *for* Advancement *of* Investor Rights
Fondation canadienne *pour* l'avancement *des* droits *des* investisseurs

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Capital Markets Act Consultation
Capital Markets and Agency Transformation Branch
Ministry of Finance, Frost Building North
95 Grosvenor Street, 4th Floor
Toronto, ON M7A 1Z1

Delivered online and by email: CMA.Consultation@ontario.ca.

Re: Consultation Draft – Capital Markets Act

FAIR Canada is pleased to provide comments on Ontario's draft Capital Markets Act ("draft CMA").

FAIR Canada is a national, independent charitable organization dedicated to being a catalyst for advancing investors' rights in Canada. As a voice of the Canadian investor and financial consumer, FAIR Canada promotes its mission through outreach and education on public policy issues, policy submissions to government and regulators, and proactive identification of emerging issues.[1]

1. Introduction

FAIR Canada is generally supportive of the draft CMA because it will introduce several improvements over the current Securities Act (Ontario) (OSA). These include enhanced enforcement powers, comprehensive provisions addressing trading in derivatives, broader rule-making powers based on a platform approach, and market conduct related requirements organized in a single part of the draft CMA.

However, we have several specific concerns with some of the proposed changes to the existing regime. These are explained in detail below along with specific recommendations that would help improve the draft CMA for Ontarians. For convenience, our recommendations are consolidated in Appendix A of this submission.

In general, we urge the Government to bolster investor protections in several areas and bring greater focus to ensuring investors are treated fairly. For example, one significant concern is the lack of any provisions in the draft CMA authorizing the OSC to designate a dispute resolution service with binding decision-making powers. This was a key investor focused recommendation

[1] Visit www.faircanada.ca for more information.

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from the Capital Markets Modernization Taskforce that should be addressed in the legislation.

As outlined further below, we also have broader concerns around the Commission's continued role in important policy decisions under the draft CMA.

2. Achieving balance in the legal and regulatory framework

Historically, the primary impetus of securities law was to protect investors. It appears that the primacy of this purpose has been diminished by legislative changes and policy priorities in recent years, which have put greater emphasis on burden reduction and fostering capital formation and financial innovation. These include, for example:

- Adding "to foster capital formation" to the purposes of the OSA.
- Adding a new fundamental principle that a key means for achieving the purposes of the OSA is by facilitating "innovation in Ontario's capital markets."
- A wide-ranging, multi-year regulatory burden reduction initiative undertaken by the OSC at the direction of the Government.
- A series of OSC and Canadian Securities Administrators (CSA) policy changes designed to reduce regulatory requirements for companies accessing capital from investors, including by providing companies with new and more liberal prospectus exemptions for preparing and delivering a prospectus, a cornerstone disclosure document designed to protect investors.

The first principle in section 2 of the draft CMA states "[b]alancing the importance to be given to each of the purposes of this Act may be required in specific cases." Stated differently, regulating capital markets involves trade-off between the competing purposes to achieve an optimal balance. In our view, the totality of the changes noted above give rise to concerns this balance is being tilted away from the purpose of protecting investors.

Moreover, despite a recognition that regulators should focus on achieving meaningful outcomes, the investor protection purpose is still drafted narrowly and focused on protecting investors, but only from "unfair, improper or fraudulent practices." Indeed, the OSA and draft CMA are both silent about the notion that one of the purposes of the regulator should be to promote fair outcomes for (or treatment of) investors.

Similarly, despite years of regulatory work (backed by empirical research) to rebalance the investor relationship and promote putting the client's interests first (i.e., intermediaries should act in the best interests of their clients), the draft CMA remains silent on this critical investor protection issue.[2]

[2] The OSC and CSA have made several important changes to improve investor protection and fair treatment of investors in recent years, including implementing the "client focused reforms" that require registrants to put the

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Accordingly, FAIR Canada believes that promoting fair treatment and putting the client's interest first are fundamental principles that should be enshrined in the purposes of the draft CMA. Doing so would be consistent with the duty to act fairly, honestly and in good faith with registrants' clients.[3] It would also help convey a better balance in the purposes of the Act and validate that the OSC should be proactive in pursuing these results.

Finally, it would align the draft CMA with the approach in leading jurisdictions such as the UK, where firms have long been required to consistently show that fair treatment of customers is at the heart of their business model.

It is worth noting that the UK's Financial Conduct Authority (FCA) is continuing to raise the bar by establishing a new "Consumer Duty" that will supersede the fair treatment of customers principle and set a higher standard of care. The new standard will require firms to go "beyond ensuring narrow compliance with specific rules" and act to deliver "good outcomes" for retail customers. The authority for the new duty is derived from the FCA's statutory responsibility to "[secure] an appropriate degree of protection for consumers" enshrined in s. 1C of the Financial Services and Markets Act 2000. We also note that these reforms were commenced at the specific direction of the British Parliament under the Financial Services Act 2021, s. 29.

In this regard, our recommended changes to the draft CMA would assist in closing the disparity between the UK and Ontario's approach when it comes to promoting fair outcomes for investors.

Recommendations:

- **Purposes of Act – Amend section 1 (a) to add the words**
  (a) to promote fair outcomes for investors *[or fair treatment of investors]* and to provide protection to investors from unfair, improper, or fraudulent practices
- **Fundamental principles – Amend section 2, paragraph 2 to add a new primary means for achieving this purpose of the Act:**
  iv. requirements for registrants to put the interests of their clients first.

interests of investors first – ahead of the firm's own interests – when recommending investments to clients and when addressing potential conflicts of interest between the firm and the client. See Annex B to the CSA's Notice of Amendments to NI 31-103 and Companion Policy 31-103CP where the CSA states:

> **In our view, to put the client's interest first and to address conflicts of interest in the best interest of the client mean that the interests of the client are paramount.** *(Emphasis added)* A registered firm and its registered individuals must put the interests of their clients first, ahead of their own interests and any other competing considerations.

[3] Section 88 of the draft CMA.

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3. Enhancing market conduct and registrant business conduct

FAIR Canada supports the inclusion of *Part IX – Market Conduct* in the draft CMA. It contains many requirements of what are generally viewed as core market conduct rules that apply to all market participants, and "business conduct" rules that should specifically govern registrants.

As detailed below, FAIR Canada proposes three important additions to Part IX to enhance investor protection and firms' standards of business conduct.

4. Duty to clients

Section 88 of the draft CMA includes the long-standing duty to "deal fairly, honestly and in good faith with the registrant's clients." FAIR Canada proposes that, in addition, Part IX include a registrant's obligation to put the interests of their clients first as may be prescribed.

In our view, putting the client's interests first is a fundamental concept which should be enshrined in the regulatory foundation created by the draft CMA. The details could be set out in the rules, as is currently done in National Instrument 31-103 (NI 31-103) under the "client focussed reforms."

5. Investor complaints

FAIR Canada has commented many times on the inadequacies of the current complaint handling system.[4] In our view, a registrant's fundamental duty to their client should include having to establish a fair, accessible, and effective means of addressing complaints about the services and advice purchased by the client.

Part IX of the draft CMA should capture this obligation to reflect its importance for promoting the fair treatment of investors. Specifically, the draft CMA should include a requirement that registered firms implement and provide clients with a fair, accessible and effective means of addressing complaints as may be prescribed.

We would also encourage the OSC to prescribe the detailed requirements by way of a rule, similar to the draft regulation proposed by Autorité des marchés financiers (the "AMF").[5] The draft regulation in Quebec is intended to ensure the fair processing of consumer complaints in Québec's financial industry. For example, it would require financial institutions under the AMF's jurisdiction to respond to a client complaint within 60 days and maintain complaint records and a registry of all complaints received. These records could also be reviewed by the AMF in

[4] Since 2010, FAIR Canada has made more than 25 submissions advocating for and supporting positive changes to the complaint handling system.
[5] The draft Regulation Respecting Complaint Processing and Dispute Resolution in the Financial Sector was published for comment by the AMF on September 16, 2021.

appropriate situations.

We see no reason why the Government would not want to establish a similar framework to promote the fair processing of complaints by Ontarians.

6. Safe harbour for actions to protect vulnerable investors

FAIR Canada has long advocated for better protection of vulnerable investors, in particular seniors. Refer to our *Report on Vulnerable Investors: Elder Abuse, Financial Exploitation, Undue Influence and Diminished Mental Capacity* issued in 2017 with the Canadian Centre for Elder Law.[6]

The North American Securities Administrators (NASAA), of which the OSC is an active member, also supported legislative measures designed to better protect vulnerable investors. In this regard, it developed a *Model Act to Protect Vulnerable Adults from Financial Exploitation* (Model Act).[7] As explained by NASAA:

> [T]he provisions of the Model Act are designed to be statutorily adopted by a jurisdiction as part of its existing securities laws. The Model Act has five core features that, when taken together, clarify and more closely align the interests and responsibilities of North American Securities Administrators Association financial professionals, regulators, and law enforcement agencies regarding the reporting and prevention of senior financial exploitation. These features are:
>
> > (1) A mandatory reporting requirement applicable to qualified individuals of broker-dealers and investment advisers;
> > (2) Notification to certain third-parties of potential financial exploitation with advance consent of the investor;
> > (3) The authority to temporarily delay disbursement of funds;
> > (4) Immunity from civil and administrative liability for reporting, notifications, and delays; and
> > (5) Mandatory record-sharing in cases of exploitation with law enforcement and state adult protective services agencies.[8]

Elements of the Model Act, as well as certain recommendations made by FAIR Canada in 2017, were recently introduced in Canada through amendments to NI 31-103. Specifically, the amendments related to the Trusted Contact Person and Temporary Holds (respectively, items 2 and 3 from the Model Act).

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[6] FAIR Canada and the Canadian Centre for Elder Law, Report on Vulnerable Investors: Elder Abuse, Financial Exploitation, Undue Influence and Diminished Capacity, November 2017. .

[7] NASAA Model Legislation or Regulation to Protect Vulnerable Adults from Financial Exploitation

[8] NASAA Model Act to Protection Vulnerable Adults from Financial Exploitation – Legislative Text and Commentary for the 2021-2022 Legislative Session, pages 2-3.

We support these amendments, which are designed to enhance investor protection, particularly for more vulnerable Canadians by introducing new tools to help registrants to do the right thing when they suspect their clients may be or have become more vulnerable.

However, we are concerned that firms and registered persons may avoid using them for fear of exposing themselves to legal liability. To address this concern, FAIR Canada proposes that a legal "safe harbour" provision be added to the draft CMA to shield both salespersons and firms from potential legal liability if they act in good faith under the rules to protect a vulnerable client.

We advocated for such a legal provision in our 2017 report, which stated:

> Regulators should implement a legal safe harbour that shields firms and their representatives from regulatory liability if they act in good faith and exercise reasonable care in making a disclosure about a client to his or her designated TCP or specified government agency or securities commission or other designated reporting body. In addition, a regulatory legal safe harbor should be extended to the firm and their representatives for placing a temporary hold on disbursements or trades from the account of a vulnerable client, provided the firm and its representatives act in accordance with the regulatory requirements… including the applicable provisions of a regulator-approved conduct protocol.

We also note the Model Act specifically includes a legal safe harbour that could be adopted by way of legislation in NASAA member jurisdictions. As stated by NASAA:

> The immunity provisions provide immunity from administrative and civil liability for qualified individuals, broker-dealers, or investment advisers who, in good faith and exercising reasonable care, comply with the provisions of the act.

We strongly recommend the draft CMA be amended to provide registrants with a legal safe harbour in appropriate circumstances.

7. Unfair practices and false statements

FAIR Canada supports the inclusion of section 105 in the draft CMA, which would prohibit unfair practices in respect of trading in securities.[9] These would include practices such as putting unreasonable pressure on a person (such as a client or investor), or taking advantage of a person's inability to protect their own interest. The Commission could also prescribe other practices that are unfairly detrimental to investors.

[9] Unfair or deceptive practices are prohibited in other financial services sectors. See, for example, regulation 7/100 made under the Insurance Act (Ontario), R.S.O. 1990, c. I.8.

This section provides an important means to address the significant asymmetry in knowledge and experience that exists between many retail investors and investment firms and their salespeople. It would be helpful for the Commission to develop guidance on what constitutes an unfair practice or a practice that is unfairly detrimental to investors, and steps that should be taken to avoid such outcomes.

FAIR Canada also supports the prohibition on persons engaged in promotional activity from making false and misleading statements about an issuer that would be considered important to an investor's decision to make a trade (section 94 of the draft CMA). This prohibition is necessary to protect investors (and market integrity) from the increased use of social media and online portals as a vehicle to spread false statements and rumours designed to encourage erroneous trading in public companies.

Recommendation:

Add these provisions to Part IX:

- **A registrant's' duty to put the interest of their clients first.**
- **A registrant's obligation to provide a fair, accessible, and effective means of addressing complaints from its clients.**
- **A legal safe harbour to protect a registrant from liability when acting in good faith to protect a vulnerable client under NI 31-103.**

8. Enabling OBSI to make binding decisions

FAIR Canada, together with many other groups, have long argued that the lack of binding decisions undermines fairness in the complaints process administered by the Ombudsman for Banking Services and Investments (OBSI). Stated succinctly, OBSI's inability to issue recommendations that are binding on firms means the process is weighted in favour of the firms, which remain free to ignore OBSI's recommendations or to offer a low-ball settlement to their clients.

As stated by the Capital Markets Modernization Taskforce established by the Government:

> […] because OBSI's recommendations are not binding, registered firms that have harmed retail investors sometimes refuse to follow OBSI's recommendations or offer settlements that fall below OBSI's recommendations. Furthermore, harmed investors could be induced to accept lesser settlements because of the likelihood they may receive nothing if OBSI's recommendations are ignored. In these circumstances, the harmed investors' only alternative is to resort to the courts, which may not be possible given the legal costs involved and the time it takes to pursue a civil action.

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> According to the OBSI Joint Regulators Committee Annual Report for 2019, clients received approximately $1.04 million less than what OBSI recommended in 2018 and 2019; out of 316 cases that ended with monetary compensation, there were 23 cases (approximately 7 per cent), involving 15 firms, that were settled below OBSI recommendations.[10]

Given this significant harm to investors, the Task Force specifically recommended that the Government give the OSC the power to designate a dispute resolution system such as OBSI with binding decision powers.[11] We also note that the federal government is prioritizing this issue and intends to address the lack of binding decisions involving complaints relating to federally regulated banks.[12]

Given OBSI's role as the ombudsperson for investors with complaints about the investment industry, the lack of any mention of this issue in the draft CMA and consultation notice is extremely disappointing. How much longer do investors have to wait for binding recommendations? Until then, the power imbalance and asymmetry in the existing complaint handling process will continue to lead to unfair outcomes for investors.

We call on the Government to amend the draft CMA to specifically address OBSI's role and ensure that OBSI decisions are binding on firms that are subject to OSC jurisdiction. This objective could be met by, for example, giving the OSC the authority to set requirements for financial ombudsman services or through the registration requirements in Part IV of the draft CMA.

Recommendation:
The draft CMA should require firms that are members of OBSI to follow recommendations made by OBSI, or permit the Commission to prescribe binding decisions for member firms.

9. Investor compensation: disgorgement, compensation, and restitution orders

FAIR Canada has repeatedly advocated in favour of expanding the power of regulators and SROs to order compensation for investors who suffer losses due to misconduct violations. See, for example, our submission to the Ontario Capital Markets Modernization Taskforce.[13]

[10] Capital Markets Modernization Taskforce, Final Report, January 2021, p. 104.
[11] Capital Markets Modernization Taskforce, Final Report, January 2021, p. 105.
[12] In December 2021, Prime Minister Trudeau issued a Mandate Letter to the Federal Minister of Finance to prioritize creating a single independent ombudsperson, with the power to impose binding arbitration, for consumer complaints involving banks.
[13] See our comments on Taskforce proposal 46, pages 2 – 5.

The reality of our system is that retail investors who suffer losses due to misconduct are rarely financially compensated. Occasionally, compensation is provided in OSC settlement agreements, but usually victims of misconduct are left to seek compensation on their own, which is often a costly, time consuming, and daunting experience, especially if commencing a lawsuit is their only option.

Consequently, we strongly support section 120 of the draft CMA. This provision gives the Capital Markets Tribunal (Tribunal) the authority to make disgorgement orders, and contemplates both a Commission or Court process to ensure the funds are administered and distributed to those who suffered financial losses due to contraventions.

We also support giving the Tribunal the authority, pursuant to subsection 121(5) of the draft CMA, to order payments to the Commission or other persons in settlement of a proceeding where the wrongdoer has consented to the settlement order.

Disgorgement orders, however, only require wrongdoers to return amounts of ill-gotten gains (or losses avoided) arising from their misconduct. This type of order may achieve salutary outcomes in situations where, for example, an insider was able to profit from trades using material non-public information. However, when investors lose money from a registrant's misconduct, the remedy is ineffective. This is because investor losses are largely irrelevant in assessing the amounts to be disgorged.

The fundamental limitation with the disgorgement power is that in many situations the losses suffered by investors are significantly larger than the ill-gotten gains derived from the misconduct. The difference between what the wrongdoer may be required to disgorge and what the investors lost means disgorgement orders often provide a poor remedy for addressing investor harm.

Apart from commencing a lawsuit, the only remedy available to investors under the draft CMA is for the Chief Regulator to apply to the court for a declaration the wrongdoer has not complied with the law, and request the court provide a compensation order. If successful, the Superior Court of Justice would have the power under section 133 of the draft CMA to order repayment, compensate or make restitution to the investors, as well as the power to order payment of damages. We also note that if a court finds that a person has committed an offence under section 171 of the draft CMA, the court may order the person to compensate or make restitution to others.

The powers under sections 133 and section 171 essentially exist today under sections 128 and 122 respectively of the OSA. While we endorse having these provisions in the draft CMA, the OSC has rarely used them in the past to seek compensation for harmed investors. When it comes to restitution, for example, we could only locate three cases where the Commission used section 122 of the OSC to seek restitution for harmed investors. With respect to section 128 of the OSA,

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there are only two cases.[14] The reality is that investors rarely, if ever, receive financial compensation in contested matters. To date, the main vehicle for providing some form of restitution is where the wrongdoer agrees to settle the matter on a voluntary basis. These scenarios, while welcome, are relatively rare as compared to the number of investors that suffer financial losses directly linked to misconduct.

To ensure that investors can be more frequently, and more fully compensated for their losses when harmed by misconduct, FAIR Canada urges the Ministry to empower the Tribunal under section 120 of the draft CMA to order compensation or make restitution to investors who suffer losses when a contravention of capital markets law is found.

There is a long-standing precedent for this approach in Canada. Under the Manitoba Securities Act, the Director may, after the Manitoba Commission holds a hearing, request a compensation order for financial losses up to an amount of $100,000 in the case of an individual, and up to $500,000 in the case of another person or company.[15] In Manitoba, an investor can also submit a claim to the Director. In such cases, the Manitoba Securities Act permits the Director to request the Commission to make an order that the investor be compensated for his or her financial loss, up to a maximum of $250,000.[16]

In the United Kingdom, the FCA also has the power, in addition to the power of a court, to order restitution.[17] It may order that one or more persons who suffered losses because of a regulatory contravention be paid such amounts the FCA considers to be just.

Alternatively, we request that clause 120(3)(a) of the draft CMA be amended by deleting "as a result of the contravention giving rise to the payment" and replacing it with "as a result of a contravention of capital markets law". This would enable any investors harmed by a contravention to apply for compensation from funds disgorged to the Commission.

We further recommend that consideration be given to amending section 133 of the draft CMA to permit investors, and not just the Chief Regulator, to apply to the court directly for an order for restitution or compensation.[18]

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[14] We understand that a third section 128 case is in progress, but no final decision has been rendered as of the date of this submission.
[15] Section 148.2(1) of the Manitoba Securities Act.
[16] Section 148.2(3) the Manitoba Securities Act.
[17] Section 384 of the Financial Services and Market Act 2000.
[18] This recommendation is based on one of the recommendations made in the Five-Year Review Committee Final Report (March 21, 2003), which, to our knowledge, has never been seriously considered by the OSC or the Government. Given the passage of time and how notions of regulatory powers have evolved since 2003, this recommendation should be reconsidered today.

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Recommendations:

- **The Tribunal should be empowered to order compensation or make restitution to investors to recover direct losses suffered due to a contravention of capital markets law.**

- **Alternatively, the draft CMA should be amended such that any investor harmed by a contraction of capital markets law be able to apply for compensation, or apply to the Court for an order for compensation or to make restitution.**

10. Investment fund governance

The draft CMA enshrines independent review committees (IRCs) in the governance structure of investment funds.[19] The draft CMA does not provide much detail, other than an investment fund must maintain an IRC in the circumstances as may be prescribed.

IRCs were created by the CSA about 15 years ago as a compromise approach to addressing conflicts of interest in the governance of investment funds. At the time, the industry convinced regulators that requiring independent directors on fund boards was not necessary. It should be noted, however, that IRCs are unique to Canadian investment funds. In the U.S., mutual funds have long been required to have independent directors.

Typically, IRCs are intended to be independent of the investment fund manager. Their basic purpose is to review potential conflicts of interest between the fund and unitholders. For some types of conflicts, an IRC must decide whether to approve a proposed action. For others, an IRC can only make recommendations to the manager on how it should manage those conflicts.

FAIR Canada believes the IRC system has inherent weaknesses that reduces its effectiveness in addressing conflicts and ensuring funds are operated in the interests of unitholders, rather than the interests of the fund manager or sponsor. The main weaknesses are:

- IRCs are not sufficiently independent of funds and fund managers. This is because IRC members rely on management for their retainers and payment of their fees. Consequently, even though they were created to protect the interests of unitholders, the structure creates built-in incentives for IRC members to avoid disputes with management.

- IRC members have limited knowledge of the investment funds within their purview because they are limited-purpose entities that only review a narrow range of issues. Although IRCs should receive an overview of the funds in question and regular updates **on**

[19] Section 70(2).

the business from the funds manager, they do not have the same level of access to information or authority as directors of the fund.

- IRCs cannot initiate reviews of conflicts of interest – actual or potential. Rather, they can only review a conflict of interest that is referred to them by management. Although National Instrument 81-102 - Investment Funds (NI 81-102) sets out certain types of conflicts that require IRC approval, other types of conflicts do not require approval. If management does not consider that a conflict arises or that a potential conflict exists, an IRC cannot review the issue.

- If a conflict of interest does not require IRC approval under NI 81-102, the IRC makes a recommendation to management on handling the conflict, but management is only required to consider the IRC's recommendation and is free to disregard it.

Given these inherent drawbacks to the IRC system, we recommend against including subsections 70(2) to (5) in the draft CMA. Instead, the draft CMA should simply require the Commission to make rules on the means of handling conflicts of interest in investment fund management that fosters the interests of unitholders over the interests of management.

This approach would enable the OSC to consider making more fundamental changes for how conflicts of interest in investment fund governance should be overseen and by whom. To the extent the OSC and CSA choose to retain the IRC system at this time, it would continue to be covered in OSC rules and CSA national instruments.

Recommendations:

IRCs should not be enshrined in the CMA. The CMA should only require the Commission to make rules prescribing the means of handling of conflicts of interest in investment fund management.

The system of managing conflicts of interest between investment fund managers and unitholders should be reconsidered and further studied by the OSC.

11. Extending civil liability for misrepresentations in exempt offers

FAIR Canada is increasingly concerned by the recent trend of increasing retail access to the exempt market through more expansive prospectus exemptions. See, for example, our comments on the CSA's recent proposal for a "listed issuer financing exemption"[20] and the proposal by regulators in Alberta and Saskatchewan to allow a prospectus exemption for self-certified

[20] FAIR Canada submission – Proposed Amendments to Nation Instrument 45-106 Prospectus Exemptions to introduce the Listed Issuer Financing Exemption.

investors.[21]

The trend appears primarily driven by the desire to increase access to capital that can be raised in private markets, especially for small issuers and provide them with alternatives to the higher costs that come with the full range of investor protections when raising capital in public markets. While facilitating access to capital, the changes have also increased the risks to many investors, including those who may not be able to afford to lose their investment, or who may not possess the requisite knowledge to invest in the exempt markets prudently.

Many investors who may be eligible to buy exempt market securities are not sophisticated investors and do not fully understand that securities sold in the exempt market are often high risk, speculative investments. Registrants are supposed to disclose and explain the risks involved in buying an exempt market security, but the system often does not work well to ensure investors understand the risks involved.

Consequently, FAIR Canada supports the changes in the draft CMA aimed at improving the rights of investors in the exempt market by:

- Extending civil liability rights and rescission rights to investors in the exempt market for misrepresentations in a "prescribed offering document" like an offering memorandum.[22]
- Extending civil liability and rescission rights to investors in the exempt market during the period of distribution for misrepresentations in a "prescribed offering document."[23]
- Extending civil liability and rescission rights to all investors in convertible and similar securities who acquires such second security for misrepresentations in the original prospectus or "prescribed offering document."[24]

FAIR Canada supports the proposed changes in the CMA to extend civil liability and rescission rights to investors in the exempt market for misrepresentations in offering documents such as an information memorandum.

12. Extending civil liability for misrepresentations in sales of ETFs

FAIR Canada supports including a provision in the draft CMA to deem that all persons or companies who purchase ETF units on an exchange have secondary market civil liability rights supplemented by certain civil liability rights for prospectus disclosures. The rights of ETF purchasers should be aligned with the prospectus rights of investment fund purchasers to the

[21] FAIR Canada submission - Proposed Prospectus Exemption for Self-Certified Investors
[22] Section 183 of the draft CMA.
[23] Section 177 of the draft CMA.
[24] Section 179 of the draft CMA.

extent possible. When buying any type of fund an investor is mainly relying on the prospectus disclosures of the fund manager, including those in any summary disclosure document like Fund Facts and ETF Facts.

Consequently, of the two options identified in the consultation paper, we believe option (ii) is preferable because it would most effectively align the rights of ETF purchasers with the rights of purchasers of investment funds.

13. Consultation period on rules and regulatory proposals

The draft CMA proposes to reduce the minimum consultation period for submitting public comments on proposed rules from 90 days to 60 days. FAIR Canada strongly opposes this proposal for several reasons, including that it will disproportionately impact investor advocates, and will lead to poorer policy decisions that may come back to harm our Ontario markets.

Preparing informed submissions requires time and effort due to the complexity of the public policy issues that underlie proposed laws and rules. This is compounded by the inherent complexity of the regulatory system and the markets themselves. In addition, proposed rules (or related amendments) are often lengthy and typically raise important concerns about their impact on investors, the industry and the integrity and effectiveness of our markets.

It is challenging for many, if not most, interested persons and advocates to respond to rule proposals even under the current 90-day period. That is true for many groups, including not-for-profit organizations like FAIR Canada that seek to provide professional and informed submissions based on research and empiricism.

The securities industry, and the large firms, including legal and accounting firms that act as their proxies, already dominate much of the process because of their sheer size, organizational resources, and desire to protect their entrenched economic interests in the status quo. Any reduction in the time consultation period would advantage the industry over other stakeholder groups. We believe the public consultation process will be more useful to the OSC and support development of better regulation if it is less susceptible to excessive influence from industry interests.

Moreover, we do not think it necessary to align Ontario's public consultation period with those of other CSA jurisdictions. Given that policy development timelines are typically measured in years, reducing the comment process by 30 days will not impact those timelines. In this context, the OSC's interest in receiving a wider and more representative range of quality submissions clearly outweighs short circuiting the process for an inconsequential gain.

Finally, we note that even the industry has difficulty keeping up with and commenting on the continuing flow of new regulatory proposals issued by the OSC, other CSA regulators and the SROs. As Paul Bourque, President & CEO of the Investment Funds Institute of Canada, recently

wrote:

> Stakeholder input can improve the scope and effectiveness of a proposal. Allowing 90 days for investors and registrants to provide comments through advisory panels, associations and advocates is adequate and certainly not excessive when compared to the years of regulatory development that precede the call for comment.
>
> Ninety days becomes completely inadequate, however, if stakeholders are trying to respond to multiple requests for comment on a variety of rule proposals simultaneously. When ever-increasing regulatory data surveys are added to the total, the industry's ability to respond constructively and thoughtfully is compromised.[25]

Fundamentally, we believe that an accessible and inclusive consultation process leads to smarter and better regulations. Arbitrarily reducing the time for consultations by 30 days will narrow the input and may lead to a deterioration in the quality of the submissions provided to policy makers.

Question 10 in the consultation asks if there are circumstances that the OSC should consider in determining when a consultation period should be longer than 60 days. As stated, the 90-day period should be the minimum standard. A longer period, however, should be allowed for proposals that are complex and lengthy, especially if many technical details are involved or they would have a significant impact on investors and the markets.

Recommendations:

The consultation period for proposed rule changes should remain a minimum of 90 days.

A longer period should be allowed for proposals that are complex and lengthy or raise many issues on regulatory policy and impact on investors and markets.

14. OSC rulemaking powers and Ministry of Finance oversight of the OSC

FAIR Canada supports the "platform legislation" approach in the draft CMA for the reasons set out in the consultation paper. Given the system of harmonized securities regulation across Canada that exists today, platform legislation provides the flexibility needed to change rules and policies in response to the dynamic capital markets environment.

In addition, we believe the OSC is best positioned to set the detailed rules and requirements that

[25] *The Regulatory Treadmill: An Industry Perspective,* Investment Executive

govern our capital markets because the OSC has the personnel (Commissioners, management, and staff) with extensive experience and expertise in capital markets. This includes experience and expertise on the structure, operations, and regulatory framework of our capital markets.

The draft CMA continues to grant the OSC extensive rulemaking powers, including broad power to make rules with immediate effect in extraordinary circumstances. We are comfortable with the rulemaking authority granted to the Commission.

It is necessary and appropriate that the OSC be subject to oversight by the Government through the Ministry of Finance, especially given the scope of the OSC's rulemaking powers. Both the OSA and the draft CMA provide mechanisms for the exercise of such oversight, along with the MoU that is in place between the Ministry and the OSC.

However, investor advocates were deeply concerned by findings reported by the Auditor General for Ontario that excessive industry lobbying, and untimely political interference affected the OSC's ability to make evidence-based rules, and delayed the implementation of bans on harmful deferred sales charges (DSCs). All stakeholders need to be concerned about this finding and ensure that it does not happen again.

We are also concerned by changes in the Ministry's approach to oversight of the OSC, including imposing new obligations on the OSC to pre-clear proposed rules before they are published for comment, and potential interference in the established process for appointing members to the Commission (who ultimately make the rules).[26]

We are particularly concerned by the Ministry's requiring the OSC to "pre-clear" regulatory proposals before they are published for comment. This requirement was introduced through an amendment to the MoU between the Ministry and the OSC in 2018. While not publicized or widely understood, this change effectively amends the rule-making process set out in the OSA (and the draft CMA).

We also note the pre-clearance requirement imposes significant additional delays to the rulemaking process well beyond any time that would be saved by abridging the public comment process. Furthermore, the delays are not limited to rules that the Commission is proposing – the process also covers guidance and staff notices issued by the OSC. As noted by the Auditor General of Ontario:

> According to OSC data, pre-clearance has required additional time, averaging 93 days for rules before public consultation, 91 days for rules after public consultation but before sending the rules to the Minister for final approval, and 54 days for staff notices.[27]

[26] See the Value-for-Money Audit: Ontario Securities Commission issued by the Office of the Auditor General of Ontario, December 2021.
[27] Value-for-Money Audit: Ontario Securities Commission, page 23.

In addition to delays, the pre-clearance process creates the potential for interference in the OSC's expert policy development processes that may be unhealthy for capital markets, especially if proposals are changed or derailed due to political considerations or lobbying by interest groups. These risks are exacerbated by the absence of public transparency into the pre-clearance process. No public notices are required, no opportunity for public input is given and no disclosure of Ministry decisions is provided.

In FAIR Canada's view, this approach undermines the sound and robust process for OSC rulemaking and Ministry oversight that is set out in both the OSA and the draft CMA. Both require the Minister to approve rules adopted by the Commission before they are introduced, which is a transparent process to the public. We also note the draft CMA is silent about any need for a pre-clearance process.

We acknowledge that ongoing discussions between the Minister, Ministry, management, and staff of the OSC are necessary and appropriate. They allow for discussion of new policy initiatives that is sufficient for the Ministry to exercise proper oversight of the OSC. However, a formal but opaque pre-clearance process represents a different degree of Ministry oversight that we think compromises a well-devised rulemaking and policy development process and is therefore inappropriate. It undermines the principle that regulatory policy and rules will only be set after public notice of, and receipt of public comments on, regulatory proposals.

Recommendations:

The MoU between the Ministry and the OSC should be amended to eliminate the pre-clearance process that the Government recently introduced for OSC rule and policy proposals.

Any changes to the rule-making process should be fully transparent, and the public should have the opportunity to comment on any proposed changes. This includes any proposed changes to the rule-making process after the CMA is enacted.

15. OSC governance and decision-making authority

The draft CMA proposes to transfer several significant decision-making powers from the Commission to the Chief Regulator. FAIR Canada believes the changes would weaken the OSC's governance and the effective administration of securities law and capital markets policy.

We have three major concerns about the changes that centralize more decision-making authority in the Chief Regulator, as opposed to leaving them with the Commission:

1) Significant policy decision-making powers are being transferred to the Chief Regulator

FAIR Canada supports the general division of responsibilities set out in section 9 of the Securities Commission Act, 2021. The board is responsible for managing or supervising the OSC's affairs (including rulemaking) and the Chief Regulator is responsible for management and administration. We agree the Chief Regulator and management should be responsible for administration of the OSC's operations under the draft CMA, including making normal course of business decisions such as approving applications for registration and receipting prospectuses where OSC policy and rule interpretations are clear. Those kinds of decisions are currently the responsibility of the executive director (and by delegation, OSC staff) under the OSA.

However, we are concerned the draft CMA transfers decision-making powers to the Chief Regulator on important regulatory policy issues that have a broad impact on the operation of capital markets, investors' interests and the interests of registrants and other market participants. Further, the draft CMA proposes to empower the Chief Regulator to make those decisions without consulting with the Commission in most cases. In our view, some of these powers should rest with the Commission.

The decision-making powers in question are not simply administrative decisions on application of the Act and the rules. They involve the development of regulatory and capital markets policy ranging from market structure to competition in the market and investment services, to managing major risks. Such decisions belong within the purview of the Commission. Furthermore, most of these Chief Regulator decisions are not appealable under the draft CMA, as discussed below.

We are specifically concerned with decisions in the following areas:

- Recognition of key institutions – section 12 of the draft CMA and related powers
- Designation of entities – section 19 of the draft CMA and related powers
- Power to issue a CTO for a major market disruption – section 123 of the draft CMA
- Power to issue blanket exemption orders – section 126 of the draft CMA

We believe granting the Chief Regulator authority to make these decisions impinges on the Commission's role as the body responsible for making policy. They also create a risk of decisions being made by the Chief Regulator that have a negative impact on, or unintended consequences for, market operations and market participants. Those risks would be reduced if the issues involved are considered by all Commission members.

Discussion and debate among Commission members is important to arrive at sound regulatory policy decisions on such matters. Commissioners bring a great deal of experience and specialized expertise in capital markets to their roles. It is imperative to ensure that their experience and expertise is brought to bear on important matters of policy.

The division of responsibilities between the board and management is not an absolute in any

organization. There is no clear red line between the responsibility to supervise an organization's business and affairs and to administer its operations. The line is drawn at different points on a continuum that reflect the circumstances and needs of a particular organization.

In the OSC's case, the Commission is granted wide-ranging powers to, in effect, make law under the platform legislation approach of the draft CMA. The Commission's members are carefully chosen with those powers and responsibilities in mind. When a regulatory decision involves deciding important regulatory and market policy issues, we believe it is vital for the Commission to debate those issues and be responsible for making the decision.

Below we explain the reasons for our concerns about the four decision-making powers listed above.

a) Recognition and designation of key institutions

These decisions include:

- Recognition of entities such as a SRO, securities exchange or clearing agency under section 12; setting prescribed requirements under section 13; granting exemptions, and the power to make decisions on recognized entities under section 18.

- Designation of entities such as a marketplace or information processor under section 19; setting prescribed requirements under sections 20 to 23; granting exemptions, and the power to make decisions on designated entities in sections 26 and 27.

These are important policy decisions that involve the exercise of wide discretion in the interpretation of the rules and policies. Institutions such as exchanges, clearing agencies or information processors provide critical market infrastructure that form the foundation of Ontario capital markets. In addition to playing central roles in our markets, they perform essential services that enable markets to operate.

Ensuring the uninterrupted operation of these key institutions is vital to controlling risks, including the risk of a breakdown of Ontario capital markets if key parts of the infrastructure were to fail. They also perform vital risk management functions that help to control systemic risks, especially in the clearing and settlement services provided by CDS.

Determining which entities should be recognized or designated to perform these roles is a critical policy decision that significantly impacts Ontario's capital markets, today and for decades to come. It is not simply an administrative question of having the Chief Regulator approve the application for recognition or designation based on rules established by the Commission. Rather, it involves a complex weighing and balancing of different issues and concerns, such as the applicant's ownership and governance structure, market services and scale. In our view, the Commission is best able to undertake this assessment.

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In making a recognition or designation decision, the OSC also makes policy by setting the specific terms and conditions that apply to the recognized or designated entity. Recognition orders for critical market infrastructures like the TSX, CDS and IIROC vary based on the roles played by the organization involved and the risks it poses.

We believe the Commission should exercise these powers because recognition and designation decisions have a major impact on the key elements of capital markets policy, including everything from investor protection, to promoting competition and regulating listing obligations.

This impact is illustrated well in the below example:

Example: Maple Group acquisition of TMX Group

In 2011 a consortium of major financial institutions named the Maple Group proposed to take control of TMX Group to prevent a takeover of the group by the London Stock Exchange. The proposal raised many major public policy issues about market structure, competition for market services and concentration of power in capital markets. The consortium aimed to take control of the TSX, TSX Venture Exchange, the Montreal Exchange, CDS and derivatives clearing agency CDCC – the key parts of Canada 's capital markets infrastructure. Many difficult policy issues had to be addressed in the OSC's (and CSA) review of the new applications for recognition that were involved.

In the end the OSC (and CSA) resolved the issues by obligating the Maple Group and the TMX Group to agree to extensive recognition orders on TMX Group and its subsidiaries, as conditions of approval of the transaction. The orders imposed strong ongoing regulatory oversight of their operations by the OSC and required the group to meet many stringent ongoing requirements. The OSC's review of this transaction was a highly complex policy decision that required balancing the interests of many stakeholders as well as trade-offs between different capital markets policy objectives.

b) Power to issue a CTO for a major market disruption

The power to issue a cease-trade order (CTO) without notice in extraordinary circumstances, including in response to major market disruptions and disturbances, is granted to the Chief Regulator under section 123. In this case the draft CMA provides checks and balances in the form of requiring notice to the Minister and prompt submission of the order to the Commission for confirmation. We do not believe those are sufficient qualifiers to the Chief Regulator's power to issue a CTO because such an order could require an exchange or all markets to shut down trading immediately. The consequences would obviously be major and wide-ranging.

In contrast, the OSA grants the power to issue a CTO in an emergency to the Commission. Given

the potential consequences, we believe it should remain with the Commission under the draft CMA.

c) Power to issue blanket exemption orders

The draft CMA gives the Chief Regulator the power to make blanket exemption orders -- an order exempting a class of persons, trades, intended trades, distributions, securities, or derivatives from any provision of Parts II to IX of the draft CMA or OSC rules. Such orders could be issued either on application of a person or on the Chief Regulator's own initiative if the Chief Regulator considers the order "would not be prejudicial to the public interest." The Chief Regulator may also impose conditions, restrictions, or requirements in an order.

FAIR Canada is opposed to giving the Chief Regulator such a wide-ranging power to issue blanket exemption orders from any securities law requirements. We are also concerned that such a power is based on a reverse public interest test with so few checks and balances around it.

Blanket orders are akin to rules because they have general application to classes of persons and transactions. If a power to issue blanket orders exists, it should be exercised only by the Commission because the Commission has the authority to make rules. Like rules, blanket orders raise broad policy issues because they enable the OSC to exempt classes of persons and transactions from any provision of Parts II to IX of the draft CMA or a rule.

However, even if the power to make blanket orders is vested in the Commission, FAIR Canada believes additional checks and balances are required in the draft CMA. Briefly put, it is vital to ensure that blanket orders do not become a shortcut for making rules or a substitute for the rulemaking process.

The draft CMA contains two limitations on blanket orders: 1) orders expire after 18 months, or an earlier date set by the OSC; and 2) the OSC must provide public notice of a blanket order, although advance notice is not required.

These limitations are not adequate in our view. Further safeguards should be in place to provide a process that is more transparent to the market and provides an opportunity for the public and interested persons to comment on the policy issues that arise. The goal of making the process more efficient by empowering the OSC to grant wide-ranging exemptions from the law or the rules should not outweigh the public interest in a transparent regulatory system and an effective consultation process. Regulators should not be able to make policy and issue what are effectively new rules at the stroke of a pen.

FAIR Canada recommends that before the Commission issues a blanket exemption order, the OSC be required to provide notice of the proposed exemption and invite comments from the public and affected persons for a reasonable period (for example, 30 days). Further, an additional notice and comment period should be required if the Commission proposes to extend an order after the

initial 18-month period.

d) Other Chief Regulator Powers

In our view the power to issue exemption orders under section 126 should also belong to the Commission because it allows the Chief Regulator to exempt any person or class of persons – as well as transactions and financial instruments -- from almost any requirements imposed by the draft CMA or the rules. This power is extremely broad and consequently a wide range of regulatory policy issues may arise in decisions to grant exemptions. Such broad powers to, in effect, make and waive requirements should not be exercised by the Chief Regulator without being considered by the Commission.

Many exemptions from recognition requirements are based on the fact the entity is recognized in another jurisdiction. However, exemptions issued on that basis raise policy questions about whether reliance on another regulator's policy is warranted. Ultimately, the Commission should decide whether granting an exemption from the recognition requirements is appropriate in the context of Ontario capital markets.

The power to make the wide range of designation orders under section 127 should also remain with the Commission for similar reasons.

2) Chief Regulator's decisions cannot be appealed or reviewed

Our second major concern is that the critical decisions assigned to the Chief Regulator discussed above cannot be appealed to or reviewed by the Tribunal. Subsection 137(2) of the draft CMA lists 9 exceptions to the right to appeal, including recognition of entities, designation of entities, cease trade orders for major market disruptions and exemption orders.

The list of decisions that are not subject to appeal or review exacerbates our concerns about transferring so much decision-making power over regulatory policy from the Commission to the Chief Regulator.

Furthermore, while the Chief Regulator's decisions may be subject to judicial review, these reviews tend to focus on whether the Chief Regulator had a reasonable basis for making the decision and did not make any error in law. They do not assess the merits of the decisions or any of the policy choices. This is not an adequate level of review for the purpose of ensuring major decisions of the Chief Regulator are subject to scrutiny or to protect the interests of persons directly affected by such decisions.

Given the importance of the types of decisions listed in subsection 137(2), we believe it is essential that such decisions be appealable and reviewed based on their merits and substance. Accordingly, to the extent that the draft CMA devolves responsibility for making the critical policy decisions listed above to the Chief Regulator, at minimum the Chief Regulator's decisions should

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be subject to appeal or review on the merits. For the reasons set out below, such appeals or reviews should be heard by the Commission.

3) Appeals or Reviews of Chief Regulator's decisions should be to the Commission

Our third concern relates to the draft CMA permitting a person directly affected by a decision of the Chief Regulator to apply for a hearing and review of the decision by the Tribunal, except for the decisions listed in subsection 137(2).

We do not think the Tribunal is the appropriate body to hear appeals or reviews of decisions of the Chief Regulator that involve application of regulatory policy and capital markets policy. To the extent that the decision-making power continues to rest with the Chief Regulator, the Commission should hear appeals or reviews of the Chief Regulator's decisions because it is the policymaking body under the draft CMA.

Commissioners have the experience and expertise in capital markets that are needed to apply policy and interpret the rules. The rules are set by the Commission, so the rules are best interpreted and applied by the Commission if an appeal arises. This will produce better regulatory decision-making in cases where the Chief Regulator's decision is appealed or reviewed. That will reduce the risk of decisions being made on appeal or review that are not well aligned with the policy rationale behind the rules, with precedents and with practices in the markets.

Furthermore, if the Commission hears appeals from regulatory decisions of the Chief Regulator and recognized entities, its involvement in the practical application of the rules in specific cases will bolster the Commission's expertise on capital markets issues and enhance its ability to develop policy going forward.

The Commission should also hear any appeals of decisions made by an SRO or other recognized organization for the same reasons.

The appropriate role of the Tribunal is to hear cases and appeals on issues that involve the enforcement of and compliance with the draft CMA. The Tribunal will be best positioned to hear disciplinary matters and contested orders relating to non-compliance with the draft CMA and rules.

Recommendations:

The Commission should retain the authority to make decisions on:

1) **Recognition of key institutions and related powers – s. 12 and related powers**
2) **Designation of entities and related powers – s. 19 and related powers**
3) **Issuing a CTO for major market disruption - s. 123**
4) **Issuing blanket exemption orders – s. 126**

The Commission should provide notice of issuing or proposed issuance or extensions of blanket exemption orders and invite comments from the public and affected persons for a reasonable period (e.g., 30 days)

If the power to make decisions on the key matters in 1) is given to the Chief Regulator, such decisions should be subject to appeal or review by the Commission.
The Commission, rather than the Tribunal, should hear appeals or reviews of decisions by the Chief Regulator that involve the application of the rules and regulatory policy (other than enforcement matters).

16. Conclusion

We welcome many of the changes that will be introduced by the draft CMA for investors in Ontario. We believe, however, that there are several issues that need to be addressed before the CMA is tabled in the Legislative Assembly. We believe our recommendations, if adopted, will strengthen the CMA, and help promote better outcomes for all market participants.

We thank you for the opportunity to provide our comments and views in this submission. We welcome its public posting. Please be advised that we intend to make our submission public by posting it to the FAIR Canada website. We would be pleased to discuss our submission with the Ministry if you have questions or require further explanation of our views. Please contact me at jp.bureaud@faircanada.ca.

Sincerely,

Jean-Paul Bureaud,
Executive Director
Canadian Foundation for Advancement of Investor Rights

Appendix – FAIR Canada's Recommendations

1. Purposes of the Act – Amend section 1 (a) to add the words:
   to promote fair outcomes for investors [or fair treatment of investors] and to provide protection to investors from unfair, improper, or fraudulent practices

2. Fundamental principles – Amend section 2, paragraph 2 to add a new primary means for achieving this purpose of the Act:
   iv. requirements for registrants to put the interests of their clients first.

3. Add the following provisions to Part IX of the draft CMA:
   - A registrants' duty to put the interest of their clients first.
   - A registrant's obligation to provide a fair, accessible, and effective means of addressing complaints from its clients.
   - A legal safe harbour to protect a registrant from liability when acting in good faith to protect a vulnerable client under NI 31-103.

4. The draft CMA should require firms that are members of OBSI to follow recommendations made by OBSI, or permit the Commission to prescribe binding decisions for member firms.

5. The Tribunal should be empowered to order compensation or make restitution to investors to recover direct losses suffered due to a contravention of capital markets law.

6. Alternatively, the draft CMA should be amended such that any investor harmed by a contraction of capital markets law be able to apply for compensation, or apply to the Court for an order for compensation or to make restitution.

7. Remove the reference to IRCs from the draft CMA. The CMA should only require the Commission to make rules prescribing the means of handling of conflicts of interest in investment fund management.

8. The system of managing conflicts of interest between investment fund managers and unitholders should be reconsidered and further studied by the OSC.

9. Extend civil liability and rescission rights to investors in the exempt market for misrepresentations in offering documents such as an information memorandum.

10. The consultation period for proposed rules (or amendments to existing rules) should remain a minimum of 90 days.

11. A longer period should be allowed for proposals that are complex and lengthy or raise many issues on regulatory policy and impact on investors and markets.

12. Amend the MoU between the Ministry and the OSC to eliminate the pre-clearance process for OSC rules and policy proposals.

13. Ensure that any changes to the rule-making process are fully transparent, and the public be given the opportunity to comment on any proposed changes. This includes any proposed changes to the rule-making process after the CMA is enacted.

14. Retain the Commission's authority to make decisions on:
    - Recognition of key institutions and related powers
    - Designation of entities and related powers
    - Issuing a CTO for major market disruption
    - Issuing blanket exemption orders

15. The Commission should provide notice of issuing or proposed issuance or extensions of blanket exemption orders and invite comments from the public and affected persons for a reasonable period (e.g., 30 days)

16. If the power to make decisions on the key matters is given to the Chief Regulator, such decisions should be subject to appeal or review by the Commission.

17. The Commission, rather than the Tribunal, should hear appeals or reviews of decisions by the Chief Regulator that involve the application of the rules and regulatory policy (other than enforcement matters).