



INVESTMENT INDUSTRY ASSOCIATION OF CANADA  
ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

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Dear Mesdames:

**Re: Proposed National Instrument 11-102 and Companion Policy 11-102CP**  
***Passport System***

**General Comments**

**1. Passport System Not a Final Solution**

The Investment Industry Association of Canada appreciates the opportunity to comment on this important CSA initiative. We believe that the Passport System is a significant step in the formidable but essential task of restructuring regulation of the Canadian securities marketplace.

The creation of a single point of access through the principal regulator concept will be an important improvement over the existing system that will likely result in increased efficiency and cost savings to the industry. It should not, however, be regarded as the final step in the evolution of the multi-jurisdictional Canadian market to a single regulator model. We believe that the cornerstone of the larger restructuring imperative is the harmonization and streamlining of the regulations underlying the Passport System.

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The ability of market participants to rely on one uniform set of more principles-based regulations is critical in creating an efficient system that can be easily navigated by domestic and foreign market participants.

Although the establishment of common regulations and a single point of access create the appearance of a relatively uniform and integrated market, the reality remains that there are 13 jurisdictions with different levels of participation in the Passport Model. Each jurisdiction continues to have the authority to enact local regulations, independent of the others. Although the proposed Passport Policy Statement states an intention not to do so, governments may nevertheless decide otherwise and regulators may choose to accomplish a common goal in different ways, undermining the harmonization objective.

In addition, the differences in the regions' abilities to act as principal regulator and the remaining local idiosyncrasies in legislation, not to mention multiple fees, result in a system that, despite its improvement over the current state of affairs, should only be considered to be transitional. This is especially so in view of the Ontario Government's decision not to participate in the Passport System.

We urge all members of the CSA (and the governments to which they report) to continue to work together to come to an agreement that would make this a truly national program and would allow for the further evolution of our regulatory structure pursuant to a timely and well executed plan.

## **2. Ontario as a Non-Participating Jurisdiction**

The Ontario Government has decided not to participate in the Passport System without a commitment from other jurisdictions to move toward a national regulator on a timely basis. The Ontario Securities Commission (the "OSC") will therefore not be able to participate fully in the Passport System, as it has no prospect of receiving statutory authority to delegate its decision-making authority to other regulators. Nevertheless, the second phase Passport Proposal is framed as a national instrument on the basis that the OSC will be participating and will be able to act as a principal regulator. As a result, the proposed instrument does not address Ontario's actual position or the issues that must be resolved in view of the fact that the regulator in the largest market in Canada cannot adopt the proposed instrument.

The Passport Proposal contemplates the repeal of the existing instruments under which the OSC and other regulators currently cooperate, for example, National Instrument 31-101 - *National Registration System* and National Policy 43-201 - *Mutual Reliance Review System for Prospectuses and Annual Information Forms*. But as the OSC cannot fully participate in the proposed Passport System, it may be necessary to utilize the mechanisms in these regulatory instruments, or devise other means to permit the OSC to continue to cooperate in the prospectus and registration processes.

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For example, another mechanism that would allow the OSC's participation in cooperative regulatory processes would be for other participating regulators to delegate authority to the OSC to enable it to act as a principal regulator under the Passport System for issuers and market participants whose principal jurisdiction (as defined in the instrument) is Ontario. Although the OSC will not be able to reciprocate, this could address potential transitional difficulties for registrants whose principal jurisdiction will be Ontario.

These and other possible ways of continuing the existing cooperative arrangements must be addressed in conjunction with, or as part of the Passport Proposal, if a comprehensive scheme is to be considered.

Without some indication of how the CSA intends to resolve these issues, any comments will necessarily be incomplete, as they will be based on a proposal that cannot be achieved in the form proposed.

The remainder of this letter contains comments on the Passport System as proposed. It does not comment further on the manner in which the OSC and other regulators may continue to cooperate under this System. Nor does it comment on other outstanding proposals that contemplate the Passport System and that must be taken into account when attempting to evaluate it, namely, proposed National Instrument 41-101 - *General Prospectus Requirements* and proposed National Instrument 31-103 - *Registration Requirements*. All of these matters must be viewed together when considering the Passport System and its implications for all market participants and regulation of the securities market in Canada. We recommend, therefore, that National Instrument 11-102 be re-proposed, along with these other national instruments, for a second round of comments so that the proposed Passport System can be considered on a comprehensive basis.

## **Specific Concerns**

### **1. Inconsistencies and Harmonization**

Aside from Ontario's decision not to participate in the Passport System, the nature of our concerns relate for the most part to outstanding inconsistencies in regional regulation that undermine the System's purpose and effectiveness.

We applaud the provinces' efforts to harmonize their regulation and defer to the principal regulator where certain differences remain. The remaining inconsistencies and restrictions, however, are significant and should be resolved in order to maximize the benefits of the system.

The treatment of non-harmonized local requirements raises concerns with respect to both prospectuses and registration. One unintended consequence of this treatment is that non-harmonized "additional" prospectus requirements will only apply to a prospectus that is

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filed in a single jurisdiction. The result is that small issuers raising capital in only one province may be subject to potentially more onerous requirements than those raising capital in two or more.

The fact that the Passport System does not apply to non-harmonized prospectus exemptions is problematic as it introduces complexity and reduces the potential benefits of the system. It is difficult to understand the rationale for many of the differences in these exemptions and, particularly, why investors in specific jurisdictions are deemed to be in need of different levels of investor protection than those in the rest of the country. The differences should be re-examined and harmonized, given the significance of the exempt market in Canada and the proposal to require registration of exempt market dealers under National Instrument 31-103.

The proposed Passport System would not exempt registrants from all non-harmonized requirements, but only the small number listed in Appendix D to the National Instrument. No explanation for this treatment is provided in the Policy Statement or Request for Comments. Again, it is difficult to understand why the local requirements cannot be harmonized for registrants that carry on business in more than one jurisdiction.

The retention of local requirements under the proposed Passport System highlights the fact that harmonization requires not only uniform legislation and rules, but also uniformity in their interpretation and application.

The proposed Policy Statement says that the CSA “has put in place administrative practices and procedures to ensure its members interpret and apply harmonized securities legislation in a uniform way.” These mechanisms should also be included in the National Instrument so that market participants may invoke them in appropriate circumstances.

## **2. Fees**

Under the Passport System market participants would deal only with their principal regulator. Nevertheless, issuers and registrants will be required to pay the applicable distribution, registration and filing fees in each jurisdiction. It is difficult to see a justification for continuing to require payment of fees in jurisdictions where the regulator does not do any work on an application or filing.

At a minimum, the fees paid to non-principal regulators under the Passport System should be substantially reduced.

## **3. Mobility Exemption**

The decision to retain the limits on the broker mobility exemption contained in the Passport System (subsequently to be moved into National Instrument 31-103 - *Registration Requirements*) is problematic and inconsistent with the principles of the

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Passport System. The exemption permits individual brokers to service only five inter-provincial clients and restricts an entire firm to ten such clients. These limits on the exemption are far too low to deal with the issue of client mobility and strip it of any real utility. The rationale for the limits is unclear, as the exemption does not diminish any of the protections currently afforded to clients regardless of the number of clients involved.

As long as the firm and the individual registrant meet the criteria required by their principal jurisdiction, there is no clear reason to establish such limits. In fact, the restriction is at odds with the purpose of the Passport System, which is to create a single point of contact by recognizing the regulations of other jurisdictions. From a practical point of view, the cost and time required for registrants to develop and monitor compliance with the exemption more than offset the benefits, due to the extremely limited number of clients that can be served. The result has been and will continue to be that dealers serving any number of inter-provincial clients will choose to register rather than use the exemption.

As a matter of principle, given that the provinces do not have materially different registration requirements, there is no reason to preclude a registrant from continuing to deal with existing clients who change their jurisdiction of residence. We question the rationale for the decision to effectively exclude broker mobility from the Passport System.

#### **4. Cost-Benefit Analysis**

The Request for Comments states that the CSA did not do a cost-benefit analysis of phase II of the Passport System because they “assumed that all jurisdictions would adopt it” and that it would therefore reduce, rather than impose, costs. In view of the position of the Ontario Government on the Passport System, the CSA’s assumption appears to be incorrect. Given that the cost-benefit equation underlying the Passport System will necessarily overstate the benefits and underestimate the costs, it is important to find ways to accommodate Ontario’s position in the Passport System and understand the real the cost-benefit of the Passport System, as compared to a single national regulator.

#### **Conclusion**

The Investment Industry Association of Canada applauds the CSA for the hard work and consensus building that has resulted in the Passport System and the harmonized regulations that underpin it. We look forward to continuing CSA efforts to ensure effective implementation of the Passport System with a view to the evolution to a single regulator solution.

Yours sincerely,



cc: Mr. John Stevenson, Secretary of the Commission, Ontario Securities Commission