

INSPIRING INVESTOR CONFIDENCE:

Building competitive and innovative capital markets in BC

Presentation to

Vancouver Board of Trade

British Columbia Securities Commission

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October 30, 2012

Thank you for the kind introduction. And thank you to the Board of Trade for hosting this event.

Good afternoon. I am pleased to be here at a particularly challenging time for all of us in the capital markets – as investors, advisers, businesses.

The fallout of the financial crisis has shaken investor confidence, especially in the equity markets, and regulators globally, are struggling to find ways to respond and bring back investor confidence.

I'd like to begin by sharing with you some thoughts around what often happens to regulators when dealing with a financial crisis.

Then I'll speak about the things regulators can do to help restore investor confidence and in particular, what the BCSC is doing.

I'll conclude by briefly describing some issues arising out of the financial crisis and others that have acquired greater profile since the crisis that warrant regulatory attention.

Regulation in the face of a crisis

While maintaining investor confidence is a core function for us, one thing is different in the wake of a crisis: the external environment. Most of the time, people don't pay attention to what regulators do. But that all changes when a crisis erupts.

Media coverage and pundit opinion strongly implies or even states outright, that whatever has happened is rooted in some fundamental failure of regulation. Calls emerge for new rules or even whole new forms of regulation.

If the issue is serious enough to attract the attention of politicians, pressure intensifies for new regulations to be implemented as quickly as possible.

You need only look to the south to know that this is exactly what has happened.

The Dodd-Frank Reform includes 95 separate rule-making requirements for the SEC, of which they have finalized 30 to date. Requirements relate to areas across the SEC's mandate and include securitization, derivatives, whistleblower channels, mineral disclosure, and corporate governance reform.

Dodd-Frank also includes 60 separate rule-making requirements for the CFTC, of which they have finalized 39 to date.

We believe that when facing a crisis, the regulatory response should be no different than it normally should be when we identify a threat to investors or markets.

We need to get data, analyze it to understand the problem. We need to decide if intervention will fix the problem. We must implement a solution that has minimal impact on market competitiveness.

We must measure the results.

Don't get me wrong. A sense of urgency is appropriate in the early stages of any crisis. And regulators must be open to the idea that at least part of the problem could be rooted in a regulatory failure.

But guessing wrong – intruding when not necessary, and imposing costly and burdensome requirements – can easily cause serious and lasting damage to markets.

A case in point was the introduction in the US of the Sarbanes-Oxley legislation to respond to major accounting scandals at Enron and Worldcom. In Canada, we did not immediately introduce its more draconian features because we were not convinced they were necessary.

We took the extra time to do the necessary analysis and ultimately implemented measures that addressed the same problem, but in a way that did not impose the exorbitant costs suffered by industry in the US.

Going forward, we must keep in mind that regulations designed to deal with the last crisis will do little to prevent the next one.

BCSC and investor confidence

So what is the BCSC doing to help restore investor confidence?

Well first, we think investors will have more confidence if they see healthy and vibrant capital markets – markets that have integrity and are competitive. These concepts are related.

Markets cannot be competitive if they have no integrity. If people don't trust your markets, they won't trade in them. However, you can have integrity without competitiveness.

This is how we think about regulation at the BCSC.

And why is this so important?

It is important because BC is often called the start-up capital of Canada. 98% of its businesses are small, generating one-third of the province's gross domestic product and responsible for 40% of our exports.

There are over 1100 BC based venture companies, representing about half of the companies listed on the TSX-Venture.

Many of these are junior mining companies looking for mining and exploration capital.

Our venture markets are vital to BC's economy. So it will not be a surprise to hear that we focus much of our efforts on ensuring we have a regulatory regime that supports a cost effective, innovative and reputable market for these early stage companies.

A recent article in Business in Vancouver said: "the province's "junior-friendly" securities laws have made the province a hub for mining sector financing.

BC is Canada's lead mining regulator. 43-101 (the mining rule) we introduced many years ago in the wake of the Bre-X debacle provides a transparent and

credible reporting regime; there is strong consensus that it has helped make Vancouver the junior mining capital of the world.

Greg Gosson, technical director at the Association of Mining and Exploration Companies says that institutional investors prefer the Canadian disclosure rules for easy access and reliable information.

For that reason, he says more money is flowing through BC and Canada than Australia for example.

But we are not resting on our laurels. Working with our Alberta colleagues, we are proposing more suitable and manageable disclosure requirements for early stage companies and that are more relevant and understandable for investors.

We think these changes will go some ways to reducing the compliance burden on publicly traded companies.

Over the years we have developed a good understanding of the public markets. What we realized a few years ago is that we did not know enough about the private markets. It is critical for effective regulation to understand well the markets you regulate.

What we learned is that capital raised in the private placement market now significantly exceeds the public markets, accounting for \$9.3 billion last year, down from \$13.2 billion the prior year.

The vast majority of those who use the private placement market to raise capital are investment funds and public companies. Mining and utilities head up the list.

A small percentage of this capital is raised to finance venture start-up businesses. These companies pose the highest risk for investors. They have limited disclosure obligations, investors cannot easily sell their securities and they are susceptible to failing.

With this growth in private placement financing, we have strengthened oversight of this market to provide more effective protection to those who choose to invest in these private start-ups.

In this post crisis environment, we are also mindful of increased investor vulnerability to what may appear to be attractive investment opportunities.

According to Jock Finlayson, executive vice president of the Business Council of BC, today's financial environment must rank among one of the least rewarding in half a century, if not longer.

In part, that means that Canadians who are saving for retirement or relying on fixed income to fund their retirement are receiving far less from their investments than pre 2008.

In short, retail investors are worried. In a national survey conducted this past May, only 50% believed that they would be able to maintain or increase their level of current income in the next 12 months.

The sheer numbers of Canadians approaching retirement, the current low interest rates and market returns, and the lack of understanding of the fundamental relationship between risk and return suggests that we have to be vigilant in helping to protect investors.

Protecting Investors

Two things I am particularly pleased about are our progress on enforcement and our leadership on investor education.

We believe that an effective enforcement regime helps build investor confidence. If investors see that those who break the rules are dealt with decisively, they gain confidence in our markets.

We have improved the efficiency of our administrative enforcement practices, which lead to settlements or hearings before the Commission. This has resulted in more cases being handled with the same resources. In addition, many cases are being dealt with significantly faster.

But administrative settlements and hearings are only part of the picture. As a result of a concentrated initiative beginning in 2007, we have dramatically increased criminal enforcement.

Since 2007, when we formed a criminal enforcement team, Crown Counsel has laid 346 charges in connection with 26 cases. 27 people have been formally charged, and 10 people convicted.

In the ensuing years, we have seen a substantial increase in the number of cases opened and individuals charged.

In the first two years of our Criminal enforcement team's operation, twelve cases were opened. Five resulted in persons being charged with 16 counts under the *Criminal Code* and the *Securities Act*. All but one of those individuals have since pleaded guilty or been convicted at trial and received jail terms of up to 12 months.

In 2009/2010 we opened 17 cases. Thirteen resulted in persons being charged with 306 counts under the *Criminal Code* and the *Securities Act* with sentences up to two years in jail.

And we are not letting up. Since the beginning of 2011, we have opened twenty-one more cases. Our goal is to bring more and more cases before the Commission and the Courts to send strong deterrence messages.

On the investor education front, we believe that an informed investor is a more confident investor.

One of our recent initiatives vividly illustrates our commitment to this important role for building and maintaining investor confidence.

Last fall we started a three-year campaign called Be Fraud Aware in English, Punjabi, Mandarin and Cantonese. Its goal is to fraud-proof British Columbians.

We are in year two and have just launched an aggressive English TV and social media campaign that includes a "Be Fraud Aware App", available, free, in the Apple App store today.

The campaign has been a success. Awareness of the warning signs of investment fraud is up considerably in all three communities – Chinese, South Asian and

English speaking. We are receiving more information and questions from the public.

Emerging Issues

I'd like to close by describing some of the work we are doing on issues arising as a direct result of the crisis and others that are gaining attention.

Derivatives regulation is near the top of the list. It's a \$615 trillion notional market.

Working with other securities and federal financial regulators, we are working together to fulfill Canada's commitment as a G20 nation, to manage the risks of OTC derivatives trading by bringing greater transparency to this area.

This will affect BC market participants – pension, investment and hedge funds; local and provincial governments; and crown corporations – who use derivatives to hedge financial risks.

We are developing a framework to oversee this complex market in Canada. Our goal is to meet the international objectives, and our challenge will be to do so effectively without imposing exorbitant costs on industry.

A few words about some emerging issues that we believe are worth looking at.

Recent proxy battles have highlighted issues and concerns with the integrity of the proxy-voting infrastructure in corporate transactions.

This is a complicated area raising issues that include: shares being double-voted, shareholders not receiving proxy materials, and the phenomenon of empty voting.

We have our work cut out for us - an initial pass tells us that not everything in this area can be done at once, so we are in the process of gathering the data and doing the analysis to determine what intervention, if any, makes sense, and if so, where to start.

Broad consultation with industry leaders will be needed in order to understand the problems issuers and investors are facing with the system.

As a start, I believe there needs to be greater accountability by market participants who have an interest in the integrity of our proxy voting system. This is important for investor confidence.

In the interim, very soon we will be proposing changes to the early warning reporting system that will require more timely and meaningful disclosure of significant securities holdings. These changes underscore the importance of transparency in the system.

Another issue we are currently examining is crowd-funding- a means of capital raising for small businesses to raise money over the internet. There is a fear that Canada will be left behind in the race for scarce capital for start-ups.

In my view those fears are unfounded.

We already have a competitive regulatory regime for raising money for small business. I referred to this earlier as the private placement market.

In BC, you can use an Offering Memorandum to raise an unlimited amount of money from an unlimited number of people – as long as you comply with the rules.

But we have heard concerns expressed about the overly burdensome financial statement requirements that businesses must deliver with an offering memorandum. These are concerns we are paying attention to.

Crowd-funding is one of the topics a panel will discuss at our annual Capital Ideas conference on November 14.

Conclusion

That brings me back to the title of my talk today – inspiring investor confidence. We think investors and markets should be able to look to a regulator that is

seasoned and keeps a steady hand on the tiller – a regulator that knows when to act quickly, and when to wait for better information.

They should be able look to a regulator that imposes requirements and rules based on sound data and analysis, and so finds effective and efficient solutions.

They should able to look to a regulator that makes investor protection one of its highest priorities, and that looks for ways to stop frauds in progress before any harm is done. A regulator that has the respect of investors and the regulated community for how it enforces the rules.

They should be able to look to a regulator that is clear about the relationship between integrity and competitiveness in the markets it regulates, and tests every decision against what is best for investors and markets.

At the British Columbia Securities Commission, we strive every day to be that regulator, because we believe a regulator like that can truly inspire investor confidence.

Thank you.