

**BC Securities Commission**  
**Service Plan, 2009 – 2012**

**Updated August 6, 2009**



## **BC Securities Commission Service Plan**

This Service Plan sets out our strategy for the next three years, beginning April 1, 2009. Copies are available on the BCSC website at [www.bcsc.bc.ca](http://www.bcsc.bc.ca) (*About the Commission*), or by phoning or emailing our public inquiries group.

Each BCSC division has an operating plan that describes how it will implement the strategies in the Service Plan to address identified risks. Copies of these operating plans are also available by phoning or emailing our public inquiries group:

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## Accountability statement – BCSC Chair to Minister

Honourable Colin Hansen  
Minister of Finance  
Parliament Buildings  
Victoria, BC V8V 1X4

Dear Minister:

The British Columbia Securities Commission (BCSC) is the independent provincial government agency responsible for administering the *Securities Act*. We protect and promote the public interest by fostering:

- A securities market that is fair and warrants public confidence
- A dynamic and competitive securities industry that provides investment opportunities and access to capital

As we have prepared this plan over the past several months, the market and regulatory environment has evolved rapidly and in unexpected ways. This has made planning more difficult than usual. We have had not only to constantly update our analysis to reflect the most current information but also to build in enough flexibility to adapt to the continuing changes that are likely during the planning period.

### **Responding to market events**

The global economic downturn, and its effect on both BC investors and Canada's capital markets, has created significant new challenges for securities regulators.

One of the first signs of the turmoil to come was the freezing of the non-bank, asset-backed commercial paper (ABCP) market in August 2007. Several hundred retail investors in British Columbia held these investments, although most were held by pension funds and other professional money managers. The failure in the ABCP market has triggered a variety of actions by the Canadian Securities Administrators (CSA) and the self-regulatory organizations (SROs) we oversee. These have included investigations and compliance reviews related to past and current activities as well as more forward looking policy analysis to protect against a recurrence.

More generally, the international market decline is revealing risks that were masked during the preceding strong market conditions and will place significant pressure on the BCSC and our regulatory colleagues to deal appropriately with past misconduct, maintain active vigilance on current activities of market participants, and consider future regulatory initiatives. Our challenge will be to manage all of this effectively and to take firm, sensible steps while avoiding the temptation to overreact.

## **Improving Canadian securities regulation**

Canada's long-standing debate about the jurisdictional arrangements for securities regulation entered a new phase in January 2009 when the federal government budgeted for the formation of the Canadian Securities Transition Office (CSTO). In June 2009, the federal government appointed the BCSC Chair, Doug Hyndman, as its Chair and CEO. Doug Hyndman assumed his new role with the CSTO effective July 13, 2009. Federal and provincial governments, not regulators, will collectively decide whether to create a national securities commission. The BCSC will provide support to government in their decision making process, to ensure any decision on regulatory structure will ultimately be of net benefit to the Canadian securities market.

As the structural debate continues, it will be important for the BCSC and our colleagues to maintain a focus on the important regulatory challenges we face, including the work we have been doing to improve regulation under the current structure. Since 2004, our commission has worked closely with government and our regulatory colleagues across Canada to harmonize regulatory requirements and develop a [passport system for securities regulation](#). The goal of the passport system is to give each market participant access to the capital markets in all participating jurisdictions by dealing solely with the regulator in its home province.

Last year, the passport jurisdictions implemented passport for issuers, which simplifies the regulatory approval process for public offerings of securities and for obtaining exemptions from many requirements in securities legislation. All CSA members, including the Ontario Securities Commission, implemented new national policies for the filing and review of prospectuses and exemptive relief applications that benefit businesses and investors across Canada. These policies provide guidance on the operation of the passport system as well as an interface process for accessing the Ontario market from the passport jurisdictions.

The BCSC will lead the work to implement passport for registrants during 2009. The registration passport, which is scheduled to come into force on September 28, 2009, will significantly streamline the registration process for dealer firms and will be implemented at the same time as the national rule harmonizing registration requirements.

### **About this plan**

This Service Plan identifies two strategic risks that threaten investor protection and market integrity. These risks are:

- Unsuitable investments
- Securities fraud

The plan fully describes our work on these strategic risks. We will also continue giving priority to work started in fiscal 2009 in response to the market crisis, most notably through our national and international policy work and connections.

This is a three-year plan, which takes effect April 1, 2009. We will focus on 11 strategies during the year. Five respond directly to the two risks; six others aim to strengthen our ability to achieve our mission and strategic goals. We will measure progress in achieving our goals using essentially the same measures from fiscal 2009.

The board directed the preparation of the plan in accordance with the *Budget Transparency and Accountability Act* and BC Reporting Principles. The chair is accountable for its contents, including the selection of performance measures and targets. The performance measures are consistent with the BCSC's mandate and goals, and focus on aspects critical to the BCSC's performance. The performance targets have been determined in view of the Commission's operating environment, forecast conditions, risk assessment, and past performance.

The plan is consistent with government's strategic priorities and Fiscal Plan. We have considered all significant assumptions, policy decisions, and identified risks as of August 6, 2009 in our planning activity.

I am accountable for ensuring the BCSC achieves the objectives identified in the plan and for measuring and reporting actual performance.

Yours truly,

A handwritten signature in black ink, appearing to read 'Brent Aitken', written in a cursive style.

Brent Aitken  
Acting Chair

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# Organizational overview

## ***BCSC vision***

To play a leading role in securities regulation that inspires investor confidence and supports fair, efficient, and innovative Canadian capital markets.

## ***Mission***

The BCSC is the independent provincial government agency responsible for regulating securities trading in British Columbia through the administration of the *Securities Act*. Our mission is to protect and promote the public interest by fostering:

- A securities market that is fair and warrants public confidence
- A dynamic and competitive securities industry that provides investment opportunities and access to capital

Our commitment to appropriate, effective, and flexible regulation is guided by our values of integrity, accountability, and service. This commitment allows us to keep pace with quickly evolving capital market changes.

## ***Enabling legislation***

The BCSC's enabling legislation is the *Securities Act*, RSBC 1996, c. 418.

We are accountable to the provincial legislature and the public through the Minister of Finance, to whom we submit our annual report and audited financial statements. We submit our three-year Service Plan to the provincial Treasury Board as required by the *Securities Act* and the *Budget Transparency and Accountability Act*.

## ***Shareholder's Letter of Expectations***

The provincial government sets out the following expectations of the BCSC in the Shareholder's Letter of Expectations:

- Propose legislation that streamlines, simplifies, and harmonizes current legislation with other jurisdictions to reduce regulatory burden on business while strengthening investor protection
- Develop and implement the interprovincial regulatory passport system
- Work with other provinces and the federal government to explore further opportunities to strengthen the Canadian securities regulatory framework and investor protection

## ***Governance***

The BCSC is governed by a board of up to 11 (currently 7) commissioners appointed under the *Securities Act*. The commissioners have three categories of responsibilities. They:

- Review and approve the development and implementation of securities legislation, regulations, rules, policies, and guidance, and oversee the self-regulatory organizations (SROs)

- Act as adjudicators on applications for review of SRO and exchange decisions and enforcement matters brought under the *Securities Act*
- Act as the BCSC's board of directors, overseeing the BCSC's management, operations, and financial affairs

Our governance policy is on the BCSC website. Except where noted in the policy, the board's governance practices meet the government's *Best Practice Guidelines—BC Governance and Disclosure Guidelines for Governing Boards of Public Sector Organizations* (2005, Board Resourcing and Development Office). More information about the BCSC governance policy, including biographies of each commissioner and members of the senior management team, are on our public website at [www.bsc.bc.ca](http://www.bsc.bc.ca) (*About the Commission: Governance Policy; Organizational Chart*).

### ***Key stakeholders***

- *The public*—which relies on us to foster capital markets that contribute to the well being of British Columbia
- *Investors*—who seek to invest in fair and efficient securities markets
- *Issuers*—companies that rely on the capital markets to fund growth
- *Securities firms*—which advise investors and companies and facilitate trades
- *Other regulators*—with which we enforce compliance and develop and implement policy initiatives through the Canadian Securities Administrators (CSA)
- *The provincial government*—to which we are accountable

### ***The securities regulation landscape***

Although our statutory mandate is to regulate BC capital markets, we are part of a national system of securities regulation that operates through the CSA, the umbrella organization for the 13 securities regulators of Canada's provinces and territories. This significantly affects how we do our work and influences how we think about, and implement, securities policy and practice in BC.

There is a broad consensus among all stakeholders that a high degree of harmonization and cooperation among all jurisdictions in Canada will best serve the interests of both industry and investors. We have made significant strides over the last few years towards harmonization across Canada through the passport system.

Canadian regulators also participate actively in international organizations and arrangements through which securities regulators are increasing levels of harmonization and cooperation on a global level.

Through CSA and powers provided under the *Securities Act*, we rely on two self-regulatory organizations to perform key regulatory functions related to investment dealer and mutual fund dealer firms, and to trading activity in Canadian equity markets:

- *Investment Industry Regulatory Organization of Canada (IIROC)*, which regulates investment dealers and equities trading on Canadian marketplaces, including the Toronto Stock Exchange, the TSX Venture Exchange, and others
- *Mutual Fund Dealers Association of Canada (MFDA)*, which regulates mutual fund dealers

Each SRO has a regulator leading the oversight work, subject to monitoring by and input from the other jurisdictions. The BCSC is the lead regulator for the MFDA.

Under our statutory power to recognize stock exchanges, we recognize the TSX Venture Exchange Inc. (TSX-V). The BCSC and the Alberta Securities Commission share lead regulatory responsibilities for overseeing the TSX-V. We exempt the TSX Inc., the Canadian National Stock Exchange (CNSX), and the NASDAQ Stock Market Inc. from recognition, because we rely on oversight by their principal regulators in other CSA jurisdictions.

## ***BCSC core business areas***

### **Compliance**

Our goal is to foster a culture of compliance. Investors are better protected if issuers, securities firms, and sales representatives registered under the *Securities Act* understand and comply with their regulatory obligations. We can achieve this in part by encouraging these organizations to have effective compliance systems and controls in place, thereby reducing the instances when we need to intervene.

We rely on the SROs to oversee their member firms. Our Capital Markets Regulation division oversees non-SRO member firms and their employees, the SROs, and other market participants doing securities business in BC. Our Corporate Finance division oversees companies and insiders.

### **Enforcement**

Our goal is to act decisively against misconduct. Decisive action depends on open channels for receiving tips, timely complaint reviews, targeted surveillance to detect misconduct, thoroughly investigating suspected securities law breaches, and resolving cases through timely settlements and administrative hearings.

Our Enforcement division focuses on cases with a strong BC connection. When cases with national implications emerge involving a BC-based market participant, we usually take the enforcement lead. We also work with international regulators, SROs, and policing agencies to enforce our rules. Cases involving SRO member misconduct are most often dealt with directly by the respective SRO.

### **Investor Education**

Our goal is to educate investors so they can make informed investment decisions and protect their financial interests. We want investors to confidently research and critically assess potential investments *before* they invest. Research shows that many adults lack the knowledge and understanding they need to make sound investment decisions. For this reason, our Communications & Education division develops programs using a life-cycle approach, which recognizes that young people with a proper financial education become more confident and knowledgeable adult investors.

BC is one of only two Canadian provinces providing mandatory financial learning programs for youth. We support the Planning 10 curriculum for BC high school students with a comprehensive financial life skills teaching resource that covers essential topics including budgeting, saving, investing, and investment fraud.

Our adult education programs target seniors and pre-retirees, two groups we know to be particularly vulnerable to investment fraud. If they fall victim to a fraud, the financial impact can be serious since they have less time to recover their losses than younger investors. We offer tools and information to help investors avoid and report investment fraud and to understand the basics of making informed investment choices through our website resource, InvestRight.org.

## **Policy-making**

Our goal is to advance cost-effective regulation, primarily through our work with the CSA. Policy-making is a key regulatory tool we use to protect investors and foster fair and competitive markets. We have the authority under the *Securities Act* to make rules. We also issue guidance to help market participants understand our requirements. Our Corporate Finance and Capital Markets Regulation divisions work to harmonize rules and guidance among all CSA jurisdictions and minimize compliance costs for market participants.

## ***BCSC operating capacity***

Securities regulation is highly specialized and dynamic. To do it well, we need to recruit and retain qualified and motivated professionals. We offer challenging work, competitive salaries and benefits, and an excellent working environment.

We plan to hire up to five additional staff this year to strengthen our enforcement intelligence capacity and compliance programs.

We allocate resources and manage capacity in the following ways:

- Strategic planning and enterprise-wide risk management to prioritize risks and opportunities
- Succession planning, and recruiting for specific expertise, to safeguard key competencies
- Rigorous annual budgeting process, monthly budget variance reporting, and strong project initiation and purchasing controls
- Continually improving the efficiency of our processes and monitoring the quality of our services

## **Strategic context**

### ***BCSC action in response to market events***

Market events in the last year have challenged both investors, who have seen returns fall and savings erode, and other market participants, who have seen revenues weaken, assets fall in value, and financing become expensive or unavailable. During the previous period of strong global growth, low interest rates, and apparent financial stability, the roots of

the ongoing financial crisis developed. Some of the major factors that led to the crisis include:

- Market participants with unsound risk management and due diligence practices seeking higher yields from investment products
- Weak underwriting standards in the US sub-prime mortgage market
- Dramatic growth in complex and opaque financial products
- Increased use and extent of leverage

Since we operate within a national regulatory system, we are working with CSA to identify problems arising from or revealed by the crisis that warrant a national response, including changes to our regulations. The CSA's responses during the past year have included proposals to strengthen securities regulation relating to asset-backed commercial paper, credit rating agency regulatory oversight, and executive compensation disclosure. The CSA's policy teams are also reviewing regulatory requirements in the over-the-counter (OTC) derivatives market and in the exempt market (where institutional investors and high net worth individuals access complex or structured securities without prospectus disclosure).

We consider international standards when developing Canadian proposals to change securities laws. When global market issues surface, securities regulators collaborate through the International Organization of Securities Commissions (IOSCO) to develop recommended outcomes for all to meet. The securities commissions in Ontario, Québec, Alberta, and BC represent Canada on various IOSCO committees and working groups. IOSCO is working on projects related to credit rating agencies, fair-value accounting, short selling, hedge fund regulation, and commodity futures markets. Other international bodies that touch on securities-related issues include the International Accounting Standards Board and the Financial Stability Forum.

While we continue to work on issues of national importance, we are also continuing our work "on the ground" in BC to deliver effective securities regulation, coordinating our work with the SROs and CSA. Informed by the market crisis, we have prioritized our resources to deal with the most immediate risks. We have stepped up some routine oversight controls, such as monitoring dealer capital adequacy and reviewing disclosure by public issuers in the financial services sector.

We are also determining the need for new or amended regulations. If regulatory changes are warranted, we will advocate appropriate, effective, and flexible regulation to deal with the key risks that the market will not fix on its own. Before deciding to make policy changes, we want to understand the complex events and interrelationships that cause a market failure and assess what, if any, regulatory changes might reduce the chances of a recurrence. We should not overlook the market's own ability to correct past failures. We will need to assess very carefully the calls for increased regulation in areas that have traditionally supported the growth of our capital markets, such as the exempt market. In conditions of such severe uncertainty, securities regulators and government policy makers must take a longer-term view and avoid overreacting to current events.

## ***Securities regulation in Canada***

In 2008, the Federal government appointed an Expert Panel on Securities Regulation to provide advice and recommendations on the best way forward to improve securities regulation in Canada. The Panel published a report on January 12, 2009. Later in January, the federal government set aside funding for the formation of the Canadian Securities Transition Office (CSTO). In June 2009, the federal government appointed the BCSC Chair, Doug Hyndman, as its Chair and CEO. Doug Hyndman assumed his new role with the CSTO effective July 13, 2009. The BCSC will provide support to government in their decision making process, to ensure any decision on regulatory structure will ultimately be of net benefit to the Canadian securities market.

While the debate on the structure of Canadian securities regulation continues, we will complete work with provincial ministries and CSA on the passport system to make the Canadian securities regulatory system more efficient and effective. To date, all provinces and territories except Ontario have worked together through passport for issuers and made significant progress streamlining and harmonizing our regulatory system. Under the passport system, public companies and securities firms in participating provinces deal solely with their home regulator and comply with a single set of harmonized laws. A broader group of market participants will soon realize the benefits of a passport system when CSA implements passport for registrants in 2009.

In addition, most jurisdictions have recently passed new legislation to strengthen regulatory enforcement in Canada by enabling securities regulators to issue reciprocal orders. Our commission may issue enforcement orders based on sanctions imposed by other regulators and findings of misconduct made by courts.

To better protect investors in BC, we stepped up our efforts to issue reciprocal orders and are working with CSA to streamline the reciprocal order process to quickly prevent misconduct in multiple jurisdictions.

## ***Strategic risks***

We will continue to prioritize the work started last year to respond to the market crisis, most notably through our national and international policy work and discussions. We will also focus our resources on other strategic risks that pose the most serious threats to our mission which we have identified using our risk management process. This year we will focus on these key risks:

1. Unsuitable investments
2. Securities fraud

In the following chapter, we describe mitigation strategies to deal with these risks, grouping each strategy under the goal to which it is most directly related.

### **Risk 1: Unsuitable investments**

Registered dealers and their salespersons play a key role in the market as intermediaries and providers of expert advice to investors. Half of BC adults hold stocks or mutual funds outside of pension funds, and 61.5% of financial wealth in BC is held in market-sensitive

assets<sup>1</sup>. Retail investors often rely on the advice of their brokers and other advisors to make suitable investment choices.

Optimizing the advice provided by advisors is dependent upon many factors. First, an advisor needs to fully understand the client's financial and life circumstances, as well as the client's risk tolerance. Then, the advisor needs to understand the investment products and the relative risks of those products to recommend suitable investments. Finally, the client needs to play an active role in understanding and managing the relationship with their advisor. If any part of this relationship breaks down, retail investors are at risk of their advisors dealing unfairly with them or selling them unsuitable investments.

Many securities regulations are designed to put client interests first in the investing relationship. We rely on education, guidance, compliance examinations, and enforcement action to promote compliance by dealers and their salespersons with these rules. We rely on four key principles in our rules to align the interests of dealers and their clients:

- *Know your client*—a registrant must know the essential facts about each client they deal with
- *Suitability*—a registrant must evaluate the suitability of each sale of a product given a client's investment goals, time horizon, and risk tolerance
- *Fair dealing*—a registrant must deal fairly, honestly, and in good faith with clients
- *Truth in establishing a dealer relationship*—a registrant must provide full and true information on issues that would affect an individual's decision on whether to enter or maintain an advising relationship with the registrant

Both the MFDA and IIROC support these rules with detailed policies and oversight of their member firms. Last year, the MFDA issued additional guidance to its members about how to establish a suitability framework to comply with the "know your client" (KYC) and suitability rules. It also provided guidance on assessing suitability where investors borrow to make investments.

At the same time, IIROC conducted a compliance sweep of asset-backed commercial paper (ABCP) distribution activity in member firms and issued recommendations for product due diligence, suitability, and supervisory obligations. IIROC is also reviewing ABCP-related complaints with regard to a number of issues including, but not limited to, determining if individual clients were provided with adequate and appropriate information about the risk or the suitability of the product which was sold to them and if the firm undertook appropriate due diligence in its product review.

Both the MFDA and IIROC published rules for comment to clarify the client advisor relationship and enhance suitability services offered by dealers to clients.

To complement the work by the SROs to strengthen suitability compliance, the BCSC launched a targeted investor education program, aimed at helping investors take greater responsibility for their investment decisions and understand what they can and should

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<sup>1</sup> Investor Economics, Household Balance Sheet Report, 2008 Statistical Update and Rebased Forecast, Table 6.9. Market-sensitive assets are defined as equities, investment funds, and fixed income securities.

expect in a relationship with their advisor, with its publication of an “e-book”, “*Guide to Investing: How to Work with Your Investment Advisor.*” We believe investors will be better served and protected if they understand the responsibilities of their advisor and they actively work with their advisors to achieve their financial goals.

We describe our plans for work in this area under the following headings:

- Goal 1: *Promote a culture of compliance*
  - Strategy 1.1: *Strengthen suitability risk management*
- Goal 3: *Educate Investors*
  - Strategy 3.1: *Expand investor education content and marketing to promote greater awareness about investing with an advisor*

## **Risk 2: Securities fraud**

Research we conducted last year into the challenges facing investors showed that many investors believe they can get annual returns of eight to ten percent for their investments, making their expectations higher than the historical average return. These expectations may be tempered by the market downturn. However, the search for higher returns will increase investor vulnerability to fraudulent investment schemes.

Investors who do not know the signs (see [InvestRight.org/redflag](http://InvestRight.org/redflag)) of investment fraud are more likely to fall victim to a fraudulent investment pitch. We know from a 2007 CSA Investor Study<sup>2</sup> that about one-in-twenty Canadians —more than a million people— have been victims of investment fraud. Many more (41%) have been approached to invest in a fraud in their lifetime.

For these reasons, enforcement action must be timely, effective, and responsive. Enforcement staff aim to achieve timely enforcement through early intervention and pursuing cases that will deter future misconduct. They work cooperatively with securities regulators in other jurisdictions to share information, conduct investigations, and issue reciprocal enforcement orders. They also aggressively pursue securities fraud cases through both administrative and criminal enforcement proceedings. Under administrative proceedings, the BCSC can impose monetary sanctions and order people out of the market. Criminal cases pursued through the courts by Crown counsel can result in prison sentences and complement our regulatory efforts.

We also help protect investors from fraudulent investments through education and warnings. We are encouraging them to report any suspicious investment activities so that we are able to intervene earlier to minimize investor losses. Staff from our enforcement, communications and education, and other divisions, collaborate to provide fraud education to police agencies and financial institution frontline employees, issue public warnings about fraudulent investment schemes, and communicate fraud prevention messages through the news media, internet, and face-to-face seminars province-wide.

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<sup>2</sup> 2007 Investor Study: Understanding the Social Impact of Investment Fraud, Canadian Securities Administrators, October 2007.

Our goal is to disrupt and deter securities fraud. We describe our plans for work in this area under the following headings:

- Goal 2: *Act decisively against misconduct*
  - Strategy 2.1: *Detect and deter fraud through industry outreach and intelligence gathering*
  - Strategy 2.2: *Build stronger criminal investigation capability in BC for financial crime*
- Goal 3: *Educate investors*
  - Strategy 3.2: *Educate the public about fraud and encourage reporting to the BCSC.*

## Strategies by goal

We have the following goals:

1. Promote a culture of compliance
2. Act decisively against misconduct
3. Educate investors
4. Advance cost-effective regulation

We align strategies with our goals: the graphic below shows how strategies described under each goal tie to risks discussed in the Strategic Context chapter.

### Summary of risks and related strategies

	Unsuitable investments	Securities fraud	Other goal-related strategies
Goal 1: Promote a culture of compliance	Strategy 1.1		Strategy 1.2
Goal 2: Act decisively against misconduct		Strategy 2.1 Strategy 2.2	Strategy 2.3
Goal 3: Educate investors	Strategy 3.1	Strategy 3.2	Strategy 3.3
Goal 4: Cost-effective regulation			Strategies 4.1 - 4.3

## ***Goal 1: Promote a culture of compliance***

Investors are better protected if securities firms and securities issuers understand and comply with their regulatory obligations. They must have effective systems and controls in place to ensure compliance with our rules. We intervene to correct non-compliance when warranted.

### **Strategies supporting Goal 1**

Two strategies support this goal:

- Strategy 1.1: Strengthen suitability risk management
- Strategy 1.2: Maintain global leadership in mining disclosure standards

#### **Strategy 1.1: Strengthen suitability risk management**

*Lead: Capital Markets Regulation*

This strategy responds to Risk 1: *Unsuitable investments*, with the goal of continuing the work from previous years to deal with the risk of unsuitable investments. This year we will take a focused look at product due diligence for dealers. We will:

- Get regular reporting from and provide feedback to IIROC on their product due diligence compliance testing, compliance action, and enforcement activities
- Raise product due-diligence concerns about security types identified by our emerging retail investment trends team with IIROC for compliance against their standards
- Examine MFDA members' product due diligence practices related to sales of exempt products

We will also continue to monitor suitability risks and registrant compliance by:

- Leading the MFDA oversight audit and participating in the IIROC oversight audit, including review of how they test the KYC, suitability, and fair dealing principles
- Monitoring the MFDA's sales compliance examination results on suitability, and resulting compliance actions it has taken
- Monitoring IIROC's progress on its commitment to issue suitability guidance, educate members, and take appropriate compliance action
- Monitoring complaints and compliance/enforcement action related to suitability

#### **Strategy 1.2: Maintain global leadership in mining disclosure standards**

*Lead: Corporate Finance*

Mining and mineral resource exploration are vital and strategic industries, both economically and socially. About 1,000 BC-based issuers (more than 60%) are mining and exploration issuers. The BC mining industry directly employed about 7,500 people and generated gross revenues of \$6.9 billion and net income of \$1.2 billion in 2007.<sup>3</sup> TSX market monitoring shows that the TSX and TSX-V play leading roles globally in mining

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<sup>3</sup> PricewaterhouseCoopers 2007 Mining Report

funding, with 57% of public mining issuers worldwide listed on those Canadian marketplaces.<sup>4</sup>

A key regulation specific to raising capital in the mining sector, NI 43-101 *Standards of Disclosure for Mineral Projects*, came into force eight years ago. Our mining advisory committee has raised cost and efficiency issues with NI 43-101, so we will lead a CSA project and consult with market participants to examine these issues and develop NI 43-101 amendments. Our objectives are to reflect best practices in mining disclosure, improve cost efficiency, and foster dynamic and competitive capital raising in the mining industry.

### ***Goal 2: Act decisively against misconduct***

Decisive action depends on a variety of factors: open channels for receiving tips; timely processing of complaints; targeted surveillance to detect misconduct; thorough investigation of suspected securities laws breaches; and case resolution through timely settlements and administrative hearings.

Four core areas are critical to strong and effective enforcement:

- *Generate leads.* We raise public awareness about fraudulent investments, encourage investors to report suspicious activity, and share intelligence with other regulatory and enforcement agencies.
- *Select cases.* We use risk-based criteria to select and prioritize cases, and continuously evaluate the viability of active cases.
- *Complete cases.* We complete investigations, settlements, and hearings in a timely manner.
- *Maintain strong ties to Crown.* We work with Crown prosecutors and federal and provincial law enforcement agencies, and we investigate and refer appropriate cases for prosecution.

### **Strategies supporting Goal 2**

Three strategies support this goal:

- Strategy 2.1: Detect and deter fraud through industry outreach and intelligence gathering
- Strategy 2.2: Build stronger criminal investigation capability in BC for financial crime
- Strategy 2.3: Disrupt abusive junior market practices in British Columbia

#### **Strategy 2.1: Detect and deter fraud through industry outreach and intelligence gathering**

*Lead: Enforcement*

This strategy responds to Risk 2: *Securities fraud*, with the goal of strengthening our ability to detect fraud through gathering industry intelligence from RCMP, other policing agencies, and industry participants.

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<sup>4</sup> [http://www.tsx.com/en/pdf/Mining\\_Sector\\_Sheet.pdf](http://www.tsx.com/en/pdf/Mining_Sector_Sheet.pdf)

We will build on two current initiatives that extend our industry outreach and intelligence gathering capability. The first initiative is to continue RCMP outreach and launch a new Vancouver Police Department outreach program to strengthen early detection of investment fraud. Police turnover is high and investment fraud is a small component of their work, making ongoing training of securities fraud issues essential to the success of our outreach programs. The second initiative is to encourage Canadian banks to consider a frontline fraud detection training program similar to the program we developed last year with the credit unions.

We will build on our existing intelligence function to strengthen our ability to obtain leads on investment fraud. We will regularly probe for fraud leads from police and industry compliance contacts. Our research shows that the public most often turns to police to report suspicious activity including investment fraud, so capturing those leads is important. We plan to focus on special projects to sweep for frauds in specific areas, such as fraudulent offshore trading or exempt real estate investing.

### **Strategy 2.2: Build stronger criminal investigation capability in BC for financial crime**

*Lead: Enforcement*

This strategy responds to Risk 2: *Securities fraud*, with the goal of working closely with Crown counsel to pursue criminal charges where warranted.

Criminal convictions bring penalties that help deter serious misconduct. Last year:

- We opened four additional investigations targeted for prosecution
- We referred two more cases to the Crown for charge approval
- One of our previously charged cases resulted in the accused receiving a jail sentence of 12 months for breaching a BCSC decision and selling securities to the public

Successful prosecutions strengthen compliance with BCSC orders. In the coming year we expect to build and refer further criminal cases to the Crown.

### **Strategy 2.3: Disrupt abusive junior market practices in British Columbia**

*Lead: Corporate Finance*

This strategy continues our efforts to discourage abusive junior market activity in BC, such as illegal stock promotions, spam, and the creation of shell companies as vehicles for market manipulation. Some market participants with connections to BC engage in abusive market activities through the over-the-counter markets in the United States. These US OTC markets are the OTC Bulletin Board (OTCBB) and Pink Sheet quotation system.

Last year we imposed new regulatory requirements on both issuers and dealers dealing in OTCBB transactions to curb this abusive activity. We adopted a new rule, BCI 51-509

*Issuers Quoted in the U.S. Over-the-Counter Markets*, which makes issuers that have a connection to B.C., and are quoted on the OTCBB or Pink Sheets, reporting issuers. As reporting issuers, these new issuers must now comply with a range of disclosure requirements, which gives the BCSC a wider variety of tools to deal with suspicious activity. We also imposed reporting and other heightened know-your-client obligations on investment dealers with offices in BC selling OTC issuers' securities. Last year we put in place new programs to monitor compliance with these requirements.

This year we will:

- Monitor compliance by issuers and dealers
- Hold dealers accountable for their trading of OTCBB stocks, in coordination with IIROC
- Take compliance and enforcement action, when necessary, against issuers and dealers that have breached the requirements
- Measure and report on whether we are fixing the problem

### ***Goal 3: Educate investors***

Our goal is to help investors protect their financial interests. We want investors to have the confidence to research and assess potential investments before they invest.

We focus on these core areas to support a successful investor education program:

- *Increase public awareness.* We increase awareness of our education programs so that investors learn the appropriate skills to help them protect their finances.
- *Reach investors early.* We expand financial life skills programs to help investors spot fraudulent investments before they suffer investment losses.
- *Strengthen investor education.* We provide investors with tools and information to help investors get better service and advice.
- *Develop partner relationships.* We build partnerships to reach ethnic and religious communities throughout the province.

### **Strategies supporting Goal 3**

Three strategies support this goal:

- Strategy 3.1: Expand investor education content and marketing to promote greater awareness about investing with an advisor
- Strategy 3.2: Educate the public about fraud and encourage reporting to the BCSC
- Strategy 3.2: Expand financial life skills education programs for youth

#### **Strategy 3.1: Expand investor education content and marketing to promote greater awareness about investing with an advisor**

*Lead: Communications & Education*

This strategy responds to Risk 1: *Unsuitable investments*, with the goal of giving retail investors adequate skills and knowledge to understand the basics of making informed investment choices that are consistent with their investment goals.

Getting sound and objective financial advice is key to achieving financial goals. Investors play an important role in making sure they receive the advice they need. Investors need to learn how to decide if an advisor is a good match for them, choose suitable investments, and work with their advisors to monitor their portfolios on a regular basis.

We will step up our public awareness advertising to market the BCSC InvestRight investor education brand more aggressively, with emphasis on the following tools and programs:

- The “e-book”, “*Guide to Investing: How to Work with Your Investment Advisor*”. This online investor guide includes guidance, questions, and worksheets for investors working with advisors.
- Social marketing tools, including podcasts and the InvestRight blog, “Let’s talk about investing”.
- Fund Facts, the mutual fund point-of-sale disclosure document (when available). This easy-to-read document will provide investors with a basic understanding of the benefits, risks, and costs of investing in a particular mutual fund. It will also allow investors to compare one fund with another.

### **Strategy 3.2: Educate the public about fraud and encourage reporting to the BCSC**

*Lead: Communications & Education*

We know from our research that almost one-in-twenty Canadians have been victims of investment fraud and that four-in-ten Canadians have been approached with a fraudulent investment. Yet despite this relatively common experience, few people report their investment fraud experience. Their reasons vary from just not bothering to report it to not knowing to whom to report it.

This strategy responds to Risk 2: *Securities fraud*, with the goal of strengthening fraud awareness and promoting the importance of reporting investment fraud and fraud attempts. In addition to supporting existing partnerships and intensifying our province-wide advertising campaign to bring these two messages to more BC investors, we will:

- Continue working with police agencies and financial institutions to create awareness of the importance of reporting and stopping investment fraud in its initial stages
- Continue to emphasize the need to raise awareness of investment fraud with InvestRight partners and in all InvestRight seminars
- Use InvestRight blog to educate investors about the Red Flags and reporting fraud leads
- Encourage more victims to come forward to do media and videos for podcast purposes
- Adapt fraud education videos from other securities commissions
- Issue Investor Alerts to encourage reporting

### **Strategy 3.3: Extend reach of financial life skills education for youth**

*Lead: Communications & Education*

Since 2004, we have focused our financial life skills education on youth, providing BC high school teachers with a comprehensive resource known as “The City: Financial Life

Skills for Planning 10”. This fall we launched a new online program, modelled on BCSC’s successful, award-winning resource. Called “The City”, this bilingual financial literacy program is a joint initiative of the Financial Consumer Agency of Canada (FCAC) and the BCSC. It is located on [themoneybelt.gc.ca](http://themoneybelt.gc.ca) – a new financial web site for teachers and students.

We will extend the reach of “The City” (both the Planning 10 Finances and FCAC partnership versions) through province-wide marketing, teacher conferences, free teacher-training webinars, and partnerships, such as the one with “Smart Cookies” that we piloted in 2008. The “Smart Cookies” are five young women who learned the hard way how to manage their money and to achieve their financial dreams and goals.

#### ***Goal 4: Advance cost-effective regulation***

Our goal is to advance cost-effective regulation through our CSA work. Regulation imposes costs through fees, compliance costs, and restrictions on innovation. Investors inevitably pay these costs. We aim to provide strong investor protection and market integrity for the least cost.

We advance cost-effective regulation by focusing on three core areas:

- *Emphasize practical solutions.* When the market cannot fix market problems, we emphasize practical solutions, looking at the full range of potential regulatory responses and advancing only those that will provide significant benefits that exceed the costs.
- *Use our resources efficiently.* We deploy our resources efficiently through risk management, teamwork, and relevant performance measures.
- *Deliver services reliably.* We deliver key regulatory services, on a timely basis, recognizing that delay adds to costs for market participants.

#### **Strategies supporting Goal 4**

Four strategies support this goal:

- Strategy 4.1: Work with government and other regulators to implement harmonized legislation and the passport system
- Strategy 4.2: Lead initiative to streamline delivery requirements in light of technological capabilities
- Strategy 4.3: Implement new CSA IT governance model

#### **Strategy 4.1: Work with government and other regulators to implement harmonized legislation and the passport system**

*Lead: Office of the Chair*

We continue to lead work with government and other Canadian securities regulators to make the Canadian securities regulatory system more efficient and effective through the passport system. The passport system is based on highly harmonized and streamlined securities regulation across Canada.

Last year, the passport jurisdictions implemented passport for issuers, which simplifies the regulatory approval process for public offerings of securities and for obtaining exemptions from many requirements in securities legislation. All CSA members, including the Ontario Securities Commission, implemented new national policies for the filing and review of prospectuses and exemptive relief applications that benefit businesses and investors across Canada.

This year we are leading the work to implement passport for registrants, with a target implementation date of September 28, 2009. The registration passport will significantly streamline the registration process for dealer firms and will be implemented at the same time as the national rule harmonizing registration requirements.

#### **Strategy 4.2: Lead initiative to streamline delivery requirements in light of technological capabilities**

*Lead: Corporate Finance, Capital Markets Regulation, and Information Management*

Our regulations mandate the delivery of many documents and forms from:

- Public companies to shareholders
- Dealers and advisors to clients
- Market participants to securities regulators

Our approach for collecting and disclosing information is still rooted in paper-style forms and documents. The current format of these forms and documents makes it difficult to access the important information they contain.

While we have amended our regulations to generally “allow” for electronic filing and delivery, a number of our regulations predate the internet. How these forms and documents are used and accessed has changed over the years. Today, there is a wider range of ways to make information available to investors and securities regulators.

The CSA is considering redeveloping its national filing systems. This presents an opportunity to step back and review a number of our disclosure and delivery requirements in light of current technologies to potentially:

- Reduce regulatory compliance costs by amending our disclosure requirements and enhancing the ability to file and deliver documents electronically
- Better inform investors and better meet their expectations
- Improve regulatory effectiveness by making the information within these forms and documents more accessible

We see this as a multi-year project that is strongly linked to our goal to advance cost-effective regulation.

### **Strategy 4.3: Implement new CSA IT governance model**

*Lead: Information Management*

In 2007, we led a CSA project that developed a strategic plan for future CSA information technology investments and produced a set of recommendations to improve its IT governance. Over the next three to five years, the CSA intend to redevelop the national systems to better support securities regulation in all jurisdictions. The CSA also intend to adopt a number of IT governance changes to manage IT-enabled projects and IT operations more cost-effectively.

The BCSC will support this significant initiative by:

- Dedicating resources to help develop requirements and an enterprise architecture for the CSA's core business functions relating to filings
- Providing technical and executive management support to implement the proposed governance recommendations and to execute the strategic plan
- Working with CSA to define a new infrastructure for the CSA's new systems
- Participating in IT governance oversight

## Ongoing performance measurements and targets by goal

This section describes the performance measurements by which we track our progress in achieving our goals through our operating activities. We track progress towards our goals using relevant, long-term measures so stakeholders can assess our performance over time. More information about our performance measurements, including performance management systems and how we set targets, can be found on our public website at [www.bcsc.bc.ca](http://www.bcsc.bc.ca) (*About the Commission*).

### Goal 1: Promote a culture of compliance

PERFORMANCE MEASURES	TARGETS				
	07/08 Actuals /Baseline	08/09 Actuals	09/10 Target	10/11 Target	11/12 Target
1.1 Percentage of reviewed issuers that reduce deficiencies in their continuous disclosure a) Improved disclosure subsequent to a continuous disclosure review b) Improved disclosure to minimum standards	a) 100% <sup>(1)</sup> b) 91%	a) 100% <sup>(2)</sup> b) 87%	a) ≥94% b) ≥90%	a) ≥95% b) Set new baseline to reflect IFRS transition <sup>(3)</sup>	a) ≥95% b) Improve on 10/11 baseline
	Our corporate finance division reviews issuer disclosure for non-compliance. At the end of each fiscal year, we retain an independent consultant to analyze the subsequent continuous disclosure of a statistically significant random sample of issuers that received comment letters from us during that year. The results of this review show the extent to which our detailed CD review work motivated non-compliant issuers to improve their disclosure voluntarily.				
1.2 Percentage of randomly sampled mining issuers that meet the minimum standards for technical disclosure in: a) Filed disclosure (News releases, Annual information forms, Management discussion and analysis) b) Issuer websites	a) 74% b) 57%	a) 73% b) 65%	a) ≥70% b) ≥70%	a) ≥75% b) ≥75%	a) ≥80% b) ≥75%
	BC is home to most Canadian mining issuers. We will randomly select from a list of BC-based mining issuers and analyze whether those issuers' most recent technical filings were compliant with NI 43-101 <i>Standards of Disclosure for Mineral Projects</i> . This review shows the extent to which a sample of BC-based mining issuers is compliant in specific areas of their technical disclosure.				

Notes: (1) Based on a sample of 23 issuers; (2) Based on a sample of 15 issuers; (3) Canada will adopt international financial reporting standards (IFRS), effective January 1, 2011, which changes the minimum standards

PERFORMANCE MEASURES			TARGETS		
	07/08 Actuals /Baseline	08/09 Actuals	09/10 Target	10/11 Target	11/12 Target
1.3 Total percentage of BC-prime reporting issuers on defaulting issuer list	14%	New system in place <sup>(1)</sup>	Set new baseline to reflect new system	Set new baseline to reflect IFRS transition <sup>(2)</sup>	25% improvement over 10/11
	The <i>Securities Act</i> requires reporting issuers to file certain information on time, in the required form, and with the appropriate fee. We put issuers on a list of defaulting issuers if they do not file, fail to pay fees, or file materials clearly not in the required form. We track the total percentage of BC-prime reporting issuers on this list during each year.				
1.4 Average number of deficiencies per examination in Capital Markets Regulation	6.68 out of 57 categories <sup>(3)</sup>	6.9 out of 57 categories <sup>(4)</sup>	Decrease deficiency average by 5% over 08/09	Set new baseline to reflect two new categories of registered dealer	Decrease deficiency average by 5% over 10/11
	Our Capital Markets Regulation division reviews securities firms that are not SRO members for compliance with their regulatory obligations. Using various indicators of risk, we assess ratings to our firms so that we can determine how frequently and how closely to examine their compliance.				

Notes: (1) Prior to December 2008, firms had a few days to resolve issues before they are placed on the list of issuers in default. The new system implemented in December 2008 eliminates the grace period, resulting in a higher default incidence in the coming year. (2) Canada will adopt international financial reporting standards (IFRS) effective January 1, 2011. Transitional non-compliance may lead to more issuers going on the defaulting issuers list. For this reason, we are unable to set a reasonable level of issuer compliance in this year. (3) Based on 19 examinations. (4) Based on 20 examinations.

**Goal 2: Act decisively against misconduct**

PERFORMANCE MEASURES			TARGETS		
	07/08 Actuals /Baseline	08/09 Actuals	09/10 Target	10/11 Target	11/12 Target
2.1 Percentage of new cases with active misconduct where we intervened	56%	88%	≥60%	≥65%	≥65%
	<p>Early detection and intervention helps to protect investors, particularly in illegal distribution cases where investor losses tend to increase exponentially over the life of the distribution. We track the cases (we accept for enforcement action) where there is active misconduct, when we learn of it. We calculate the percentage of those cases in which we take disruptive action – freeze assets, issue a cease trade order, or take other steps to disrupt the misconduct. Although we assess the potential for early intervention in all cases, we are not able to take action on all of them. For example, while we may suspect misconduct, we may lack sufficient evidence to intervene.</p> <p>This measure focuses our efforts on early detection and shows how often we take early action to stop the misconduct.</p>				
2.2 Average life, in months, of cases resolved via settlement or enforcement decision	39.5	47	<34	Set according to formula <sup>(1)</sup>	Set according to formula <sup>(1)</sup>
	<p>We want to be transparent about the average time our administrative enforcement process takes. For the cases we close by settlement or a decision in the fiscal year, we measure the average number of months a case is open from when we first learn of the conduct to the case’s completion by settlement or decision. Reciprocal orders are not included.</p>				

Note: (1) We calculate the target based on a case average of actual case age and service target timeframes for the enforcement steps outstanding on each case.

**Goal 3: Educate investors**

PERFORMANCE MEASURES			TARGETS		
	07/08 Actuals /Baseline	08/09 Actuals	09/10 Target	10/11 Target	11/12 Target
3.1 Number of complaints and tips received as a result of InvestRight investor education and industry outreach programs	92	87	Increase 5% over 08/09	Increase 5% over 09/10	Increase 5% over 10/11
	<p>Through our public awareness and outreach programs, we aim to increase the flow of complaints and information we receive about possible investment frauds or illegal activities. This network of information helps us prevent, stop, or disrupt these activities. We track the number of enquiries, referrals, and complaints we receive from the public, media, and policing agencies such as the RCMP, IMET, and local police.</p>				

PERFORMANCE MEASURES			TARGETS		
	07/08 Actuals /Baseline	08/09 Actuals	09/10 Target	10/11 Target	11/12 Target
3.2 Percentage of workshop participants who recall investor education messages of red flags	17%	11%	Increase 3% over 08/09	Increase 3% over 09/10	Increase 3% over 10/11
	We deliver investor education workshops to BC residents, primarily seniors. We hire a firm to survey seminar participants after each presentation, and a second time six months later, to measure the percentage of workshop participants who recall our investor education messages.				
3.3 Percentage of BC public aware of BCSC	30% <sup>(1)</sup>	43% <sup>(2)</sup>	≥45%	≥45%	≥45%
	BCSC investor education resources provide BC retail investors with valuable information to help them protect themselves from fraud and unsuitable investments. One in five BC adults are active investors. We aim to build awareness of the BCSC and our many investor education resources so that British Columbians will know where to turn and what to do when faced with a possible fraud or unsuitable investment opportunity. We collect data by asking awareness questions in each year's investor survey.				

Notes: (1) From our October 2007 investor survey. (2) From our July 2008 investor survey.

#### ***Goal 4: Advance cost-effective regulation***

PERFORMANCE MEASURES			TARGETS		
	07/08 Actuals /Baseline	08/09 Actuals	09/10 Target	10/11 Target	11/12 Target
4.1 Average score on cost-effective regulation scorecard	88%	89%	≥90%	≥90%	≥90%
	To measure cost-effective regulation, we use a scorecard that tracks the important steps and outcomes in responding to market problems. We apply the scorecard to all CSA and local projects. For CSA projects, the scorecard reports on the extent to which we took steps to advocate our cost-effective regulation principles. For all projects, the scorecard gives credit for outcomes-focused results. We report the average score of all the projects completed each year.				
4.2 Average approved project post-implementation score	100% on two projects	95%	≥80%	≥80%	≥80%
	We assess each local IT-enabled project at a predetermined time after the project's completion (as documented in the project proposal) and score the project's success relative to its proposed benefits.				

## Summary financial outlook

### *Financial overview*

We aim to break even over the business cycle. Our revenues fluctuate in proportion to market activity, while most of our costs are fixed.

### **Operations**

More than 95% of our operational funding comes from filing, registration, and application fees paid by market participants under the *Securities Act*. The remainder of our operational funding comes from investment income and enforcement cost recoveries, if any.

Salaries, benefits, and occupancy costs account for over 80% of our expenses: we currently employ 192 full-time equivalent staff (March 31, 2009 – 189).

As a government agency, we are exempt from income taxes and the GST.

### **Education reserve**

We order administrative penalties and disgorgements<sup>5</sup> under the *Securities Act*. We also negotiate settlements, which sometimes include monetary sanctions. We appropriate these revenues to our education reserve.

We mix education reserve funds with other funds for investment purposes, so we allocate a portion of investment income to the education reserve.

We spend education reserve funds only to educate securities market participants and members of the public about investing, financial matters, or the operation or regulation of securities markets.

### **Financial outlook**

We generated an operating surplus of \$1.9 million in fiscal 2009 (2008 – \$5.4 million). This is lower than fiscal 2008 due primarily to the following:

- \$2.2 million (12%) lower distribution filing revenue, due to weaker capital market conditions
- \$0.3 million (56%) lower exemption application revenue, due to regulatory streamlining initiatives and fewer financings
- \$0.4 million (4%) higher registration revenue, due to registrant population growth
- \$0.9 million (4%) higher salary and benefit expense, due to salary increases and staff additions
- \$0.3 million (20%) higher professional services expense, due to legal fees related to collection actions

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<sup>5</sup> Disgorgement is designed to return ill-gotten gains to victims. We allocate to the education reserve disgorgements collected and not claimed within three years of collection.

We expect market activity to remain relatively weak through fiscal 2010 and to strengthen in subsequent years. Since our revenues fluctuate with market activity while our costs are mostly fixed, we expect to generate deficits in fiscals 2010 and 2011.

The following table summarizes our actual and expected results of operations and financial position, by year:

		<b>Summarized Statements of Operations</b>				
		<b>08/09</b>	<b>09/10</b>	<b>09/10</b>	<b>10/11</b>	<b>11/12</b>
(millions)		Actual	Budget	Forecast	Projection	Projection
<b>OPERATIONS</b>						
<b>Revenue</b>						
<i>Filing fees</i>						
Prospectus and other distributions		16.0	12.9	12.9	14.0	16.1
Registration		9.6	9.7	9.7	9.9	10.1
Financial filings		4.6	4.6	4.6	4.7	4.8
Other fees		0.2	0.2	0.2	0.2	0.2
		<u>30.5</u>	<u>27.4</u>	<u>27.4</u>	<u>28.8</u>	<u>31.2</u>
<i>Other revenue</i>						
Investment income		1.1	0.5	0.5	0.5	0.8
Enforcement cost recoveries		-	-	-	-	-
<b>Total revenue</b>		<u>31.8</u>	<u>27.9</u>	<u>27.9</u>	<u>29.4</u>	<u>32.1</u>
<b>Expenses</b>						
Salaries and benefits		22.6	22.5	22.5	23.5	24.1
Other operating expenses		7.2	7.0	7.0	7.1	7.3
<b>Total expenses</b>		<u>29.8</u>	<u>29.5</u>	<u>29.5</u>	<u>30.6</u>	<u>31.4</u>
<b>Operating surplus / (deficit) for the year</b>		<u>1.9</u>	<u>(1.7)</u>	<u>(1.7)</u>	<u>(1.2)</u>	<u>0.7</u>
<b>EDUCATION RESERVE</b>						
<b>Revenue</b>						
Investment income		0.2	-	-	0.1	0.1
Enforcement sanctions		0.3	0.2	0.2	0.3	0.3
		<u>0.5</u>	<u>0.2</u>	<u>0.2</u>	<u>0.4</u>	<u>0.4</u>
<b>Disbursements</b>		<u>0.7</u>	<u>1.2</u>	<u>1.2</u>	<u>0.8</u>	<u>0.8</u>
<b>Education reserve (deficit) / surplus for the year</b>		<u>(0.2)</u>	<u>(1.0)</u>	<u>(1.0)</u>	<u>(0.4)</u>	<u>(0.4)</u>
<b>CONSOLIDATED SURPLUS / (DEFICIT) FOR THE YEAR</b>		<u>1.6</u>	<u>(2.6)</u>	<u>(2.6)</u>	<u>(1.7)</u>	<u>0.2</u>
<b>SURPLUSES</b>						
General		9.1	7.4	7.4	6.2	6.8
Fee stabilization reserve		15.0	15.0	15.0	15.0	15.0
Education reserve		3.7	2.7	2.7	2.3	1.9
		<u>27.8</u>	<u>25.1</u>	<u>25.1</u>	<u>23.5</u>	<u>23.7</u>
<b>SUPPLEMENTARY INFORMATION</b>						
Cash and short-term investments		16.7	15.6	15.6	14.6	15.6
Capital expenditures		0.7	0.3	0.3	0.8	0.7

## Operating revenues

More than 95% of our operational funding comes from filing, registration, and application fees paid by market participants under the *Securities Act*. The remainder of our operational funding comes from investment income and enforcement cost recoveries, if any.

## Fee revenue

(millions)	08/09 Actual	09/10 Budget	09/10 Forecast	10/11 Projection	11/12 Projection
Revenue from fees	30.5	27.4	27.4	28.8	31.2
Fee revenue growth rate	-6.3%	-10.1%	-10.1%	5.0%	8.3%

Each 1% change in our overall fee assumptions alters forecast revenues by about \$1.5 million over the planning period. We maintain a Fee Stabilization Reserve to ensure that temporary reductions in revenue do not immediately impair our ability to operate, or require reactive fee changes.

We collect the following fees:

Category	Source	Proportion of fee revenue	
		Fiscal 2009	Forecast 2010
Distribution fees	Securities issuers, to file disclosure documents	53%	47%
Registration fees	Firms and individuals, to register with us to sell or advise on securities	32%	35%
Financial filing fees	Public issuers and mutual funds, to file financial statements	14%	17%
Other fees	Market participants, primarily to request Securities Act exemptions	1%	1%

## Distribution fees

Distribution fee revenue varies depending on the number and size of securities offerings. Revenues are lower during weaker markets. The largest share of distribution fee revenue comes from prospectuses<sup>6</sup>, exempt distribution reports<sup>7</sup>, and annual information forms<sup>8</sup>. Issuers pay fees to file these documents. Also:

- When gross sales under a prospectus exceed \$7.5 million, an additional fee, called a “percent of proceeds fee,” may be payable
- When gross sales under an exempt distribution exceeds \$0.3 million, an additional fee may be payable

Distribution fee revenue fell by \$2.2 million (12%) in fiscal 2009, due primarily to fewer exempt distribution offerings, and fewer non-mutual fund prospectus distributions.

<sup>6</sup> Companies and mutual fund issuers are normally required to prepare a prospectus before raising money from the public. A prospectus gives details of the operations, financial status, and management of the company.

<sup>7</sup> Prospectus exemptions allow companies to sell securities without a prospectus when other factors (like relationship or financial sophistication) permit investors to have access to all information about the proposed transaction that could affect their purchase decision.

<sup>8</sup> Annual information forms give current details of the operations, financial status, and management of the company.

We expect a further \$3.1 million (19%) distribution fee decline in fiscal 2010, due primarily to lower percent of proceeds fees, lower exempt distribution fees, and lower non-mutual fund base prospectus fees. We expect market conditions to begin to improve after fiscal 2010, and project 9%, 15%, and 14% increases in distribution fee revenue in fiscals 2011, 2012, and 2013 respectively.

#### *Registration fees*

We receive registration fees annually, in advance, and recognize the revenue over the following calendar year. Registration fee revenue has low volatility. Registration fees have grown steadily over the last decade. Registration revenue grew by 4% in fiscal 2009 due to continued registrant population growth. We expect modest registration revenue growth in fiscal 2010 based on annual registration fees received in advance, in January 2009. We project growth of 2% per year over the remainder of the planning period.

#### *Financial filing fees*

Financial filings revenue is not volatile, except for the effects of temporary fee reductions and filing cycle changes. Financial filings revenue increased 2% in fiscal 2009. We expect it to remain flat in fiscal 2010. We expect revenue related to rule changes that make BC-based over-the-counter and Pink Sheet issuers BC reporting issuers, to be offset by a modest reduction in other issuers due to economic conditions. We project growth of 2% per year over the remainder of the planning cycle.

#### *Other fees*

Other revenue, comprised primarily of fees related to exemption applications, fluctuates annually depending on market activity. We lost \$0.3 million (56%) of revenue from this source in fiscal 2009 because harmonization and streamlining initiatives reduced filing volumes. We expect no growth in this revenue stream over the planning period.

#### **Investment income**

We invest conservatively, in highly liquid, high-quality money market instruments and government securities, so our portfolio generates modest returns. We mix education reserve funds with other funds for investment purposes, so we allocate a portion of our investment income to the education reserve.

We expect investment income to fall \$0.6 million (55%) in fiscal 2010 due to lower interest rates. We assume investment yields of 2% to 3% over the rest of the planning period, based on our investment manager's estimates of our portfolio's yield to maturity.

#### **Enforcement cost recoveries**

Enforcement cost recoveries are comprised of hearing cost recoveries and amounts designated under settlements as cost recoveries. Effective fiscal 2008, we stopped designating portions of settlement amounts as cost recoveries. Commission staff also stopped applying for hearing cost recoveries.

Revenue from enforcement cost recoveries depends on our ability to collect assessed amounts. Collecting cost recoveries can be difficult because respondents often have

limited assets, have poor credit, or have left British Columbia. Since our incorporation on April 1, 1995, we have collected \$3.9 million (66%) of \$6.0 million assessed. We pursue outstanding amounts vigorously and indefinitely. However, we have not recognized as revenue any of the outstanding \$2.1 million because collectibility is unlikely.

### ***Operating expenses***

Salaries, benefits, and occupancy costs account for over 80% of our expenses: we currently employ 192 full-time equivalent staff (March 31, 2009 – 189).

We are committed to managing our expenses so they do not exceed expected revenue over the business cycle. We do this by preparing an annual budget approved by the Board, monthly budget variance reporting to management, requiring Board approval of significant expenses, and continually improving our processes.

(millions)	<b>08/09</b> Actual	<b>09/10</b> Budget	<b>09/10</b> Forecast	<b>10/11</b> Projection	<b>11/12</b> Projection
Expenses, excluding education disbursements	29.8	29.5	29.5	30.6	31.4
Operating expense growth	4.9%	-0.8%	-0.8%	3.5%	2.6%

### **Salaries and benefits**

Staffing costs account for more than 75% of our operating expenses. We compete for professional staff with law and accounting firms, the securities industry, and other regulators. Like most of our competitors, we offer a compensation package that includes merit-based salary increases and performance-based incentives. To retain and recruit staff and remain market competitive, we conduct salary surveys annually and make adjustments as appropriate.

We spent our fiscal 2009 salaries in four areas (overhead allocated proportionately):

<b>Strategic Goal</b>	<b>Fiscal 2009</b>	<b>Fiscal 2008</b>
Promote a culture of compliance	36%	35%
Act decisively against misconduct	37%	39%
Educate investors	10%	11%
Advance cost effective regulation	17%	15%

Salary and benefit costs increased \$0.9 million (4%) in fiscal 2009. We expect salary and benefit costs to decrease \$0.1 million (1%) in 2010 because cost recoveries, largely from secondments, will more than offset salary and benefit cost increases. Over the remainder of the planning period, we forecast salaries and benefits expense to increase at an average rate of 2.5% per year due to merit and benefit cost increases.

### **Rent**

We have leased office space to November 2011 at an annual rent, net of sublease recoveries, of about \$0.9 million. Market rents have increased since we entered into our lease in fiscal 2000. We expect to pay higher rent after our lease expires in fiscal 2012.

We also pay a proportionate share of the building's operating and maintenance costs, which we do not expect to grow faster than inflation over the planning period.

### **Professional services**

We contract third-party professional services when it is not cost-effective, or when we do not have the skills, to perform the work ourselves. Professional service costs relate primarily to the following:

- Fees paid to IIROC for registration services delegated to them
- Our share of CSA project and management costs
- Legal services to defend our actions when appealed to higher courts
- Legal services to support policy development
- Interview and hearing transcription services
- Corporate services activities, including disaster recovery facility and internal audit costs

Professional fees increased \$0.3 million (20%) in fiscal 2009 due to higher legal fees for collection actions. We expect professional fees to decrease \$0.4 million (21%) in fiscal 2010 as a result of completing legal actions in fiscal 2009. We expect only inflationary growth in professional service costs over the remainder of the planning period.

### **Information management**

We spend significant amounts on information systems and management annually to improve public and market participants' access to our services and information, and to gain further efficiencies in our operations. Information management has three main components:

- Software licensing and maintenance fees
- Electronic information services and hardcopy materials
- Physical record scanning and storage costs

Information management expenses did not increase in fiscal 2009. We do not expect the composition of our information management activities to change significantly, and we expect only inflationary growth in their cost, over the planning period.

### **Depreciation and capital expenditures**

We depreciate our leasehold improvements, fixtures, and information technology over their useful lives using the straight-line method. We estimate the useful lives of our assets to be:

- Information technology – four years
- Intangible assets – four years
- Leasehold improvements – the remaining lease term to November, 2011
- Office furniture and equipment – 10 years

Depreciation increased \$0.2 million (19%) in fiscal 2009, due primarily to adjustments in economic lives. We expect depreciation to average \$0.9 million per year over the planning period.

Our capital spending relates primarily to computer systems and applications. We spent \$0.7 million in fiscal 2009. We plan a lower \$0.3 million of capital spending in fiscal

2010, primarily by deferring some capital improvements to future years. We project capital additions to average \$0.7 million per year over the remainder of the planning period.

### **Other operating expenses**

With the exception of activity-based expense changes, we expect all other expenses to increase at 2%, our estimate of the annual rate of inflation.

### ***Education reserve***

We appropriate sanctions to the Education reserve. We use reserve funds only to educate securities market participants and members of the public about investing, financial matters, or the operation and regulation of securities markets. We supplement education disbursements by absorbing indirect education costs—for example, staff salaries on education projects—in our operating budget.

### **Education revenue**

Education revenue is difficult to predict because it depends on the nature and timing of enforcement actions completed during the year, and on our ability to collect assessed amounts.

We reviewed previous years' receipts to estimate fiscal 2010 revenue, and have forecast no growth over the remainder of the planning period.

We recognize in revenue enforcement sanctions we determine are collectible. Collecting enforcement sanctions can be difficult because respondents often have limited assets, have poor credit, or have left British Columbia. Since our incorporation, we have collected \$9.3 million (25%) of \$37.5 million sanctioned. We pursue all outstanding amounts vigorously and indefinitely. However, of the \$28.2 million outstanding, only \$0.1 million is likely collectible and accrued in our financial statements. Approximately 60% of the \$28.2 million outstanding relates to two cases.

### **Education expenses**

We disbursed \$0.7 million in fiscal 2009 and had an Education reserve balance of \$3.7 million at the end of fiscal 2009. We project the Education reserve to decline to \$1.1 million over the planning period based on our revenue estimates and disbursement plans.

The most significant components of Education reserve expenses relate to investor education outreach programs, distributing and maintaining our financial planning course module (Planning 10) for grade 10 students, and maintaining our investor education website.

### ***Risks and opportunities***

#### **Fee revenue**

As previously mentioned, we fund operations primarily from filing fees paid by market participants. Fee revenue fluctuates with market activity, rising in strong market

conditions and falling in weak market conditions. We expect revenues to fall based upon economic events. We continuously monitor our fee structure and may propose changes to government to ensure we break even over the business cycle.

### **Securities regulatory reform**

While the debate on regulatory reform continues, we expect the BCSC to remain a going concern.

We have been supporting government's work to implement the regulatory reforms outlined in the September 2004 Provincial / Territorial Memorandum of Understanding Regarding Securities Regulation (Passport MOU) among all provinces and territories, except Ontario. The Passport MOU proposes single window access to capital markets in participating provinces and territories, and a review of the regulatory fees charged in the context of the passport system. Changes to date have not materially affected our operations even though exemption application fees have fallen as expected after Passport Phase II was implemented. We will implement the remaining phase of Passport during fiscal 2010. We do not expect the changes to affect our operations materially.

### **National electronic filing systems**

Under various agreements with the CSA that end on October 31, 2011, CDS Inc. operates three national electronic filing systems:

- The System for Electronic Document Analysis and Retrieval (SEDAR)
- The System for Electronic Disclosure by Insiders (SEDI)
- The National Registration Database (NRD)

We collect about 90% of our fee revenue through SEDAR and NRD. Should CDS become unable or unwilling to continue to operate them, the CSA would have to contract another party to host them.

### **National filing systems operating agreements**

CDS operates the SEDAR and SEDI national filing systems on behalf of the CSA under agreements with the Alberta Securities Commission, British Columbia Securities Commission, Ontario Securities Commission, and l' Autorité des marchés financiers, together called the CSA Principal Administrators. CDS operates the NRD national filing system under agreements with the CSA Principal Administrators and Investment Regulatory Organization of Canada Inc. Under the agreements:

- The CSA Principal Administrators must pay CDS if the SEDAR system budgeted operating costs exceed revenues (“shortfall”). Our portion of any SEDAR shortfall is limited to 15.4%.
- CDS must pay SEDAR revenues in excess of system budgeted operating costs (“surplus”) to the CSA Principal Administrators. Any surplus is not divisible; the CSA Principal Administrators own it as a group.
- CDS and the CSA Principal Administrators agree to share actual versus budgeted system operating cost (“expense”) variances equally.

The Ontario Securities Commission is holding \$35.2 million in trust, on behalf of the CSA Principal Administrators. The funds are the national filing systems’ accumulated surpluses and expense variances and interest earned on those amounts to June 30, 2009. The CSA Principal Administrators have agreed that we will use these funds only for the benefit of national filing system users through system enhancements or usage fee adjustments.

